

**Consolidated Financial Statements of
PJSC Kubanenergo and its subsidiaries**

**prepared in accordance with International Financial Reporting Standards
for the year ended 31 December 2017**

with Auditor's Report

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15.03.2018
~ Pelli-1939

INDEPENDENT AUDITOR'S REPORT

To: the Shareholders of Kuban Power and Electrification, Public Joint Stock Company (PJSC "Kubanenergo")

Opinion

We have audited the consolidated financial statements of PJSC "Kubanenergo" and its subsidiaries (the Group), which comprise the Consolidated Statement of Financial Position as of 31 December 2017, and the Consolidated Statement of Profit or Loss and Other Comprehensive Income, Consolidated Statement of Changes in Equity and Consolidated Statement of Cash Flows for the year then ended and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for Opinion

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

Key Audit Matters

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

Impairment of non-current assets

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

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

Therefore, the value in use for property, plant and equipment as at 31 December 2017 was determined using projected cash flows method. This method considers the future net cash flows expected to be generated through the usage of property, plant and equipment during the operating activities and upon disposal, to determine the recoverable amount of these assets.

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

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

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

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

Non-current assets are disclosed in Note 2,13 and 14 to the consolidated financial statements.

Impairment of accounts receivable

In our opinion, this matter was one of most significance in our audit due to significant balances of the Group's accounts receivable as at 31 December 2017, and because the management estimate of collectability of the receivables is based on the assumptions, in particular, forecasting financial solvency of the Group's customers.

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

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

Accrued accounts receivables impairment allowance is disclosed by the Group in Notes 2, 9, 18 and 27 to the consolidated financial statements.

Recognition and measurement of revenue

Recognition and measurement of revenue were matters of most significance in our audit due to certain imperfection of mechanisms of operation of retail electricity market and it leads to disagreements between

electric grid companies and energy supply companies in respect of volume of electricity consumption and capacity. The assessment by the Group's management of favorable outcome of the dispute resolution is, to a large extent, subjective and is based on the assumptions of dispute resolution.

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

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

Recognition, measurement and disclosure of provisions and contingent liabilities

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

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

Provisions and contingent liabilities of the Group are disclosed in Notes 26, 30 to the consolidated financial statements.

Other Information

Management is responsible for the other information. The other information comprises the information included in the annual report of PJSC IDGC of Kubanenergo for 2017 and the quarterly report of the issuer

PJSC IDGC of Kubanenergo for the 1st quarter of 2018, but does not include the consolidated financial statements and our auditor's report thereon. The annual report of PJSC IDGC of Kubanenergo for 2017 and the quarterly report of the issuer for the 1st quarter of 2018 are expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

When we are acquainted with the annual report of PJSC IDGC of Kubanenergo for 2017 or the quarterly report of the issuer PJSC IDGC of Kubanenergo for the 1st quarter of 2018, if we conclude that there are material misstatements therein, we are required to communicate the matter to those charged with governance.

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

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

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

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

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

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

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

Management Board Chairperson

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

ORNZ in the Register of auditors and audit organizations – 21706004215

Engagement Leader on the audit resulting in this independent auditor's report

Audit Certificate No. 03-000591. Issued following Resolution of self-regulatory organization Not-for-Profit Partnership "Moscow Chamber of Auditors" dated 13 February 2013 No.188. Permanent award.

ORNZ in the Register of auditors and audit organizations – 20103037931



N.A. Dantser

R.F. Mykhailyk

Audited entity:

Kuban Power and Electrification, Public Joint Stock Company (abbreviated name - PJSC "Kubanenergo");

Location: 2A, Stavropolskaya street, Krasnodar, Krasnodar Region, 350033, the Russian Federation;
Primary state registration number – 1022301427268.

Auditor:

RSM RUS Ltd.

Location: 4, Pudovkina Str., Moscow, 119285;

Tel.: (495) 363-28-48; Fax: (495) 981-41-21;

Primary state registration number – 1027700257540;

RSM RUS Ltd. is a member of Self-regulatory organization of auditors Association "Sodruzhestvo" (membership certificate # 6938, ORNZ 11306030308), location: 21, Michurinsky Ave., bldg. 4, Moscow, 119192.

PJSC Kubanenergo
Consolidated statement of profit or loss and other comprehensive income
for the year ended 31 December 2017
(in thousands of Russian Roubles, unless otherwise stated)

	Note	Year ended 31 December 2017	Year ended 31 December 2016
Revenue	7	42,305,075	41,802,139
Operating expenses	9	(39,093,953)	(36,120,126)
Other income, net	8	653,502	288,526
Results from operating activities		3,864,624	5,970,539
Finance income	11	72,649	104,998
Finance costs	11	(2,022,610)	(1,924,456)
Net finance costs		(1,949,961)	(1,819,458)
Profit before income tax		1,914,663	4,151,081
Income tax expense	12	(1,197,526)	(1,295,592)
Profit for the year		717,137	2,855,489
Other comprehensive income			
<i>Items that will never be reclassified subsequently to profit or loss:</i>			
Remeasurements of defined benefit liability	24	(14,380)	(75,142)
Income tax related to items that will never be reclassified subsequently to profit or loss	16	2,876	15,028
Total items that will never be reclassified subsequently to profit or loss:		(11,504)	(60,114)
Other comprehensive income for the year, net of income tax		(11,504)	(60,114)
Total comprehensive income for the year		705,633	2,795,375
Earnings per share			
Basic and diluted earnings per share (in Russian Roubles)	21	2.36	10.09

These consolidated financial statements were approved by management on 14 March 2018 and were signed on its behalf by:

Director General
 (by the power of attorney of 20 December 2017 No. 1790/17)

O.V. Ocheredko

Chief Accountant

I.V. Skiba



PJSC Kubanenergo
Consolidated statement of financial position
as at 31 December 2017
(in thousands of Russian Roubles, unless otherwise stated)

	Note	31 December 2017	31 December 2016
ASSETS			
Non-current assets			
Property, plant and equipment	13	52,588,454	48,228,069
Intangible assets	14	150,435	108,227
Trade and other receivables	18	25,760	15,192
Assets related to employee benefit plans	24	318,910	290,092
Financial investments	15	1	1
Deferred tax assets	16	1,203,443	1,762,358
Total non-current assets		54,287,003	50,403,939
Current assets			
Inventories	17	1,584,669	1,408,336
Income tax prepayment		317,458	366,089
Trade and other receivables	18	6,694,054	6,749,803
Cash and cash equivalents	19	1,681,043	1,254,098
Total current assets		10,277,224	9,778,326
Assets classified as held for sale		8,492	8,492
Total assets		64,572,719	60,190,757
EQUITY AND LIABILITIES			
Equity			
Share capital	20	28,286,813	28,286,813
Share issue reserve		2,092,522	2,072,164
Share premium		6,481,916	6,481,916
Other reserves		(236,851)	(225,347)
Retained earnings		(8,218,225)	(8,400,237)
Total equity		28,406,175	28,215,309
Non-current liabilities			
Loans and borrowings	22	22,617,796	18,912,239
Trade and other payables	25	987,357	1,428,181
Employee benefit liabilities	24	611,115	575,813
Government grants	16	37,256	52,569
Total non-current liabilities		24,253,524	20,968,802
Current liabilities			
Loans and borrowings	22	91,686	80,100
Trade and other payables	25	10,900,665	8,469,015
Provisions	26	905,937	2,446,329
Government grants		12,355	11,202
Current income tax payable		2,377	-
Total current liabilities		11,913,020	11,006,646
Total liabilities		36,166,544	31,975,448
Total equity and liabilities		64,572,719	60,190,757

The accompanying notes are an integral part of these Consolidated Financial Statements

PJSC Kubanenergo
Consolidated statement of cash flows
for the year ended 31 December 2017
(in thousands of Russian Roubles, unless otherwise stated)

	Note	Year ended 31 December 2017	Year ended 31 December 2016
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit/(loss) for the year		717,137	2,855,489
<i>Adjustments for:</i>			
Depreciation of property, plant and equipment and amortization of intangible assets	9	3,174,946	2,890,714
Finance costs	11	2,022,610	1,924,456
Finance income	11	(72,649)	(104,998)
Loss/(gain) on disposal of property, plant and equipment		42,526	50,888
Loss/(gain) on disposal of intangible assets		11,908	763
Impairment of accounts receivable	9	(73,160)	(679,837)
Provision for legal processes		1,192,119	2,099,169
Other non-cash transactions		(99,386)	(11,261)
Income tax (income)/expense		1,197,526	1,295,592
Cash flows from operating activities before changes in working capital and provisions		8,113,577	10,320,975
<i>Changes in working capital:</i>			
Change in trade and other receivables (less provision for impairment)		111,822	(1,039,053)
Changes in financial assets related to employee benefits plan		(8,094)	22,090
Change in inventories (less provision for impairment of inventories)		(115,496)	(106,934)
Change in trade and other payables		2,006,365	(2,552,289)
Change in government grants		(14,161)	(17,024)
Change in employee benefit obligations		(22,868)	(35,378)
Change in provisions		(2,732,511)	(1,560,615)
Cash flows from operations before income tax and interest paid		7,338,634	5,031,772
Income tax paid		(584,725)	(2,136,495)
Interest paid		(2,079,716)	(1,893,149)
Net cash from/(used in) operating activities		4,674,193	1,002,127

The accompanying notes are an integral part of these Consolidated Financial Statements

PJSC Kubanenergo
Consolidated statement of cash flows
for the year ended 31 December 2017
(in thousands of Russian Roubles, unless otherwise stated)

CASH FLOWS FROM INVESTING ACTIVITIES:

Acquisition of property, plant and equipment and intangible assets	(7,487,957)	(5,259,237)
Proceeds from sale of property, plant and equipment and intangible assets	1,300	1,687
Interest received	48,556	92,177
Net cash from/(used in) investing activities	<u>(7,438,101)</u>	<u>(5,165,373)</u>

CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds from loans and borrowings	41,498,408	13,222,099
Repayment of loans and borrowings	(37,793,251)	(11,309,910)
Proceeds from share issue	20,358	2,072,164
Dividends paid	(534,662)	(1,144,760)
Net cash from/(used in) financing activities	<u>3,190,853</u>	<u>2,839,593</u>
Net increase/(decrease) in cash and cash equivalents	426,945	(1,323,653)
Cash and cash equivalents at the beginning of the year	<u>1,254,098</u>	<u>2,577,751</u>
Cash and cash equivalents at the end of the year	<u>1,681,043</u>	<u>1,254,098</u>

The accompanying notes are an integral part of these Consolidated Financial Statements

PJSC Kubanenergo
*Consolidated statement of changes in equity
for the year ended 31 December 2017*
(in thousands of Russian Roubles, unless otherwise stated)

	Share capital	Share issue reserve	Share premium	Reserves	Retained earnings	Total
Balance at 1 January 2017	28,286,813	2,072,164	6,481,916	(225,347)	(8,400,237)	28,215,309
Profit for the year	-	-	-	-	717,137	717,137
Other comprehensive income						
Re-measurement of the benefit plan liability	-	-	-	(14,380)	-	(14,380)
Income tax on other comprehensive income	-	-	-	2,876	-	2,876
Total comprehensive income for the year	-	-	-	(11,504)	717,137	705,633
Transactions with owners of the Company						
Contributions and payments						
Share issue (note 20)	-	20,358	-	-	-	20,358
Dividends to shareholders (note 20)	-	-	-	-	(535,125)	(535,125)
Total contributions and payments	-	20,358	-	-	(535,125)	(514,767)
Balance at 31 December 2017	28,286,813	2,092,522	6,481,916	(236,851)	(8,218,225)	28,406,175

The accompanying notes are an integral part of these Consolidated Financial Statements

PJSC Kubanenergo
*Consolidated statement of changes in equity
for the year ended 31 December 2017
(in thousands of Russian Roubles, unless otherwise stated)*

	Share capital	Share issue reserve	Share premium	Reserves	Retained earnings	Total
Balance at 1 January 2016	28,286,813	–	6,481,916	(165,233)	(10,110,930)	24,492,566
Profit for the year	–	–	–	–	2,855,489	2,855,489
Other comprehensive income						
Re-measurement of the benefit plan liability	–	–	–	(75,142)	–	(75,142)
Income tax on other comprehensive income	–	–	–	15,028	–	15,028
Total comprehensive income for the year	–	–	–	(60,114)	2,855,489	2,795,375
Transactions with owners of the Company						
Contributions and payments						
Share issue	–	2,072,164	–	–	–	2,072,164
Dividends to shareholders	–	–	–	–	(1,144,797)	(1,144,797)
Total contributions and payments	–	2,072,164	–	–	(1,144,797)	927,367
Balance at 31 December 2016	28,286,813	2,072,164	6,481,916	(225,347)	(8,400,237)	28,215,309

The accompanying notes are an integral part of these Consolidated Financial Statements

1 Background

The Group and its operations

In 1993 the Krasnodar Production Association of Power and Electrification “Krasnodarenergo” was reorganized into Kuban Power and Electrification Open Joint Stock Company (hereinafter referred to as OJSC “Kubanenergo” or “the Company”) in accordance with Decree No. 922 of the President of the Russian Federation “On Particular Features of Transformation of Public Enterprises, Associations, Organizations of Fuel and Energy Complex into Joint Stock Companies” dated 14 August 1992, with Decree No. 923 of the President of the Russian Federation “On Organization of Management of the Electric-Power Complex of the Russian Federation under Privatization Conditions” dated 15 August 1992, with Decree No. 1334 of the President of the Russian Federation dated 5 November 1992 “On Implementation in the Electric-Power Industry of Decree No. 922 of the President of the Russian Federation “On Particular Features of Transformation of Public Enterprises, Associations, Organizations of Fuel and Energy Complex into Joint Stock Companies” dated 14 August 1992”.

Due to amendments in the Civil Code of Russian Federation, the new brand title of the company’s organizational and legal form was approved by the Annual General Meeting of Shareholders held on 22 June 2015. Open Joint Stock Company Kuban Power and Electrification (OJSC “Kubanenergo”) was changed to Public Joint Stock Company Kuban Power and Electrification (PJSC “Kubanenergo”).

The Company’s registered office is located at 2A, Stavropolskaya Str., Krasnodar, Krasnodar Territory, Russia, 350033.

The Company’s principal activities are electricity transmission and technological connection services.

The Kubanenergo Group (hereinafter referred to as “the Group”) comprises PJSC “Kubanenergo” and its subsidiaries presented below:

Subsidiaries	Principal activity	Ownership, %	
		30 September 2017	31 December 2016
OJSC “Pansionat otdyha “Energetik”	Recreation	100	100
OJSC “Energoservis Kubani”	Repair services	100	100

According to the decision of the Court dated 2 September 2015 the insolvency (bankruptcy) procedure of OJSC “Ozdorovitelnyi kompleks “Plamya” was started. As a result, the Company lost control over the subsidiary and disclosed the disposal of the subsidiary in the 2015 consolidated financial statements. According to the decision of the Court dated 23 January 2017, the insolvency (bankruptcy) procedure was extended till 23 March 2017.

According to the decision of the Arbitration Court of Krasnodar territory dated 11 December 2017 on case A-32-31443/2014 37/71-Б. the insolvency (bankruptcy) procedure of OJSC “Ozdorovitelnyi kompleks “Plamya” was completed. A liquidation entry was made in the unified state register of legal entities on 31 January 2018.

The Group’s business environment

The Group operates in the Russian Federation.

Consequently, the Group’s business is influenced by the economics and financial markets of the Russian Federation which display the characteristics of an emerging market. The legal, tax and regulatory frameworks continue to develop, but are subject to varying interpretations and frequent changes which, together with other legal and fiscal impediments, contribute to the challenges faced by entities operating in the Russian Federation.

The ongoing conflict in Ukraine and related events has increased the perceived risks of doing business in the Russian Federation. The imposition of economic sanctions on Russian individuals and legal entities by the European Union, the United States of America, Japan, Canada, Australia and other countries, as well as retaliatory sanctions imposed by the Russian government, has resulted in increased economic uncertainty including more volatile equity markets, a depreciation of the Russian rouble, a reduction in both

local and foreign direct investment inflows and a significant tightening in the availability of credit. In particular, some Russian entities may be experiencing difficulties in accessing international equity and debt markets and may become increasingly dependent on Russian state banks to finance their operations. The longer term effects of recently implemented sanctions, as well as the threat of additional future sanctions, are difficult to determine.

The future economic development 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.

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

Relations with the state

The Russian Government, through the Federal Agency for the Management of State Property, is the ultimate controlling party of the Company.

As at 31 December 2017, the Government of the Russian Federation owned 88.89% of the voting ordinary shares and 7.01% of preference shares of PJSC ROSSETI, which in its turn owned 92.78% of the voting ordinary shares of the Group.

As at 31 December 2016, the Government of the Russian Federation owned 88.75% of the voting ordinary shares and 7.01% of preference shares of PJSC ROSSETI, which in its turn owned 92.24% of the voting ordinary shares of the Group.

The Russian Government directly affects the Group's operations through tariff regulation. In accordance with the Russian legislation, the Group's tariffs are regulated by executive authorities of the constituent entities of the Russian Federation in the field of state regulation of tariffs. Many consumers of the Group's services are entities under control of the state.

2 Basis of Preparation of Consolidated Financial Statements

Statement of compliance

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

Each subsidiary of the Group maintains accounting records and prepares its financial statements in accordance with the Russian Accounting Standards (hereinafter referred to as "RAS") individually. The consolidated financial statements of the Group have been prepared on the basis of the RAS accounting records adjusted and reclassified for the purposes of fair presentation in accordance with IFRS.

Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except for property, plant and equipment at 1 January 2011 that were measured at carrying amounts included in the consolidated IFRS financial statements of OJSC ROSSETI as part of the Group's first time adoption of IFRSs as at January 1, 2011 (Note 13).

Functional and presentation currency

The national currency of the Russian Federation is the Russian Rouble ("RUB"), which is the Group's functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in Russian roubles has been rounded to the nearest thousand.

Use of estimates and professional judgments

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

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

Professional judgements that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates and assumptions that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Impairment of property, plant and equipment

At each reporting date, the Group management assesses whether there are any indicators that property, plant and equipment may be impaired. Such indicators include changes in business plans, tariffs and other factors that may lead to unfavourable conditions for the Group's activities. When measuring the value in use the management assesses estimated cash flows from a cash-generating asset or a group of assets and chooses a justified discount rate to calculate the present value of cash flows. For more detail refer to note *Property, Plant and Equipment*.

Impairment of accounts receivable

Provision for impairment of accounts receivable is based on management assumptions of debt recovery made for each debtor individually. Objective indicators of impairment are default or debtor failure to meet contractual obligations, debt restructuring to the Group under such terms that would have never been taken in regular conditions, signs of possible bankruptcy, unfavourable change in debtors paying capacity. When cash inflow is not expected in regard with an account receivable, such account receivable is written off against the previously created provision.

Future cash flows with regard to accounts receivable to be assessed for impairment are estimated on the basis of the contractual cash flows and on the basis of the historical loss experience and on the possibility to recover the past-due debts. Historical information on losses is adjusted on the basis of current available information to record existent conditions that were not effective during the past periods of losses and excluding those conditions that are not active at the current moment.

Pension obligations

Defined benefit pension plans are based on actuarial estimates. Actuarial estimates are made with help of assumptions on demographic and financial data. The estimates are subject to uncertainty due to the long-term nature of the programme.

Deferred tax assets recognition

At each reporting date management assesses the deferred tax assets and determines the amount to be recognized to the extent in which it is likely to be used as tax allowances. When determining future taxable profit and related tax allowances management uses estimates and assumptions based on prior periods taxable profit and expectations related to the future profit that are reasonable under the circumstances.

Adoption of New or Revised Standards or Interpretations

In 2017, the Group applied all IFRS and amendments to IFRS which are effective from 1 January 2017 and relevant to its operations. None of them had material impact on the Group's consolidated financial statements.

The following new standards and interpretations have been issued and are effective for annual periods beginning on or after 1 January 2018, and which the Group has not early adopted:

IFRS 9 Financial Instruments. In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments that replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early application permitted. This standard will not have any material effect on the consolidated financial statements.

IFRS 15 Revenue from Contracts with Customers. This Standard was issued in May 2014. The new revenue standard will supersede all current revenue recognition requirements under IFRS. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. Either a full retrospective application or a modified retrospective application is required for annual periods beginning on or after 1 January 2018. Early application is permitted. This standard will not have any material effect on the consolidated financial statements.

IFRS 16 Leases. This Standard was issued in January 2016 and it replaces IAS 17 Leases, IFRIC 4 Determining whether an Arrangement Contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions in the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). The Group intends to apply both exemptions. At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). The Group will be required to recognize separately the interest expense on the lease liability and the depreciation expense on the right-of-use asset. IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. The Group can choose to apply the standard using either a retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs. The Group is considering the implication of this standard for its consolidated financial statements

The following amendments to standards and interpretations are not expected to have a significant impact on the Group's consolidated financial statements.

- Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28.
- Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2).
- Transfers of Investment Property (Amendments to IAS 40).
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28).
- IFRIC 22 Foreign Currency Transactions and Advance Consideration.
- IFRIC 23 Uncertainty over Income Tax Treatments.

Reclassification of comparatives

Certain comparative amounts for the previous period have been reclassified to conform to the current year's presentation. All reclassifications are insignificant.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by the Group entities.

a) Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to risks connected to variable returns from its involvement with the entity or has the rights to those returns and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group. Losses attributable to the non-controlling interests in a subsidiary are allocated to non-controlling interests, even if doing so causes the non-controlling interests to have a deficit balance.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

b) Financial instruments

Non-derivative financial instruments

Non-derivative financial instruments include cash and cash equivalents, investments in equity and debt securities, trade and other receivables, loans and borrowings, and trade and other payables.

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

Non-derivative financial assets

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

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

Non-derivative financial assets include: loans and receivables, cash and cash equivalents, available-for-sale financial assets and held for maturity financial assets.

Loans and receivables

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

Cash and cash equivalents

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

Financial assets held-to-maturity

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity financial assets. After initial measurement, held to maturity financial assets are measured at amortised cost using the effective interest rate, less impairment losses.

Non-derivative financial liabilities

The Group initially recognises debt securities issued on the date that they are originated. All other financial liabilities are recognised initially on the date at which the Group becomes a party to the contractual provisions of the instrument. The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group classifies non-derivative financial liabilities into the other financial liabilities category. Other financial liabilities comprise loans and borrowings, finance lease liabilities, trade and other payables. Such financial liabilities are recognised initially at fair value less any directly attributable transactions costs. Subsequent to initial recognition these financial liabilities are measured at amortised cost using the effective interest method.

Share capital

Ordinary shares are classified as equity. Additional expenditure directly attributable to issuance of ordinary shares are stated as deduction from equity with a tax effect.

Property, plant and equipment

Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses. The cost of property, plant and equipment at 1 January 2011, the date of transition to IFRSs, was determined by reference to its fair value at that date.

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

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

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and are recognised net in the item “Net other income/(expenses)”, within the profit or loss for the year.

Subsequent expenditure

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

Depreciation

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

The estimated useful lives of property, plant and equipment for the current and comparative periods are as follows:

- Buildings 1-83 years;
- Electricity transmission network 4-79 years;
- Equipment for electricity transmission 1-42 years;
- Other assets 1-50 years.

Estimated useful lives and residual values of property, plant and equipment are reviewed at each reporting date and adjusted if appropriate.

c) Intangible assets

Other intangible assets

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

Subsequent expenditure

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

Amortisation

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

- Licenses and certificates 1-10 years;
- Software 1-15 years.

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

d) Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum (discounted) lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognised in the consolidated statement of financial position of the Group.

e) Inventories

Inventories are measured at the lower of cost or net realisable value. The cost is determined on the weighted average cost method, and includes expenditure incurred in acquiring the inventories, production or processing costs and other costs incurred in bringing them to their existing location and condition.

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

f) Advances given

Advances given are classified as non-current if they are connected with the acquisition of an asset which will be classified as non-current upon initial recognition. Advances given for the acquisition of an asset are included in its carrying amount upon the acquisition of control over the asset, and when it is probable that the Group will obtain economic benefit from its usage.

g) Value-added tax

Output value-added tax (VAT) related to sales is payable to the tax authorities on the earlier of:

(a) collection of receivables from customers or (b) delivery of goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. Amounts of VAT related to advances received and given as well as VAT prepayment are recognised on a net basis within accounts receivable (VAT recoverable). Amounts of VAT to be paid to the tax authorities are presented separately within short-term liabilities.

Where a provision has been made for the impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

h) Impairment of assets

Financial assets

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

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

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance

account against receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss for the period.

Impairment losses on available-for-sale financial assets are recognized by transferring the cumulative loss that has been recognized in other comprehensive income, and presented in the fair value reserve in equity, to profit or loss. The cumulative loss that is reclassified from other comprehensive income and recognized in profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in profit or loss for the period.

Changes in impairment provisions attributable to time value are reflected as a component of interest income. If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognised in profit or loss for the period, then the impairment loss is reversed, with the amount of the reversal recognised in profit or loss for the period. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date. An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit (CGU) exceeds its recoverable amount.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use of the asset (this unit) and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The goodwill acquired in a business combination, for the purpose of impairment testing, is allocated to cash-generating units which it related to.

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

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

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

i) Employee Benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate (independent) entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans, including Russia's State pension fund, are recognised as an employee benefit expense in profit or loss in the periods during

which services are rendered by employees. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

Defined benefit plans

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

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

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

Short-term benefits

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

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably and it is highly probable that there will be an outflow of economic benefits.

j) Provisions

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

k) Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable taking into account contractually defined terms of payment and excluding taxes or duty.

Electricity transmission and sale services

Revenue from electricity transmission is recognised based on acts of services rendered. The act is prepared for each counterparty in accordance with the concluded contract on the provision of services based on the meter readings and the "boiler" tariffs. The tariffs for the distribution of electricity (in respect to all constituent entities of the Russian Federation) and sale of electricity on the regulated market (in respect to the Russian Federation constituent entities, not united in the price zones of the wholesale electricity market) are approved by the executive authorities of the constituent entities of the Russian Federation (hereinafter the "regional regulatory authority") in the sphere of the state energy tariff regulation within the range of cap (or) floor tariffs approved by the Federal Antimonopoly Service of the Russian Federation.

Revenue from the sale of electricity is recognised based on monthly acts of acceptance of electricity under the electricity supply agreements (electricity sale agreements) of legal entities, based on the meter readings under unregulated prices formed on the retails market in the settlement period; monthly documents (receipts) on the consumption of utilities services by individuals based on the meter readings and tariffs approved by the regional regulatory authority.

Revenue from resale of electricity and capacity which is sold under power supply contracts includes the part of revenue related to the transmission of electricity. The tariff for the sale of electricity under power supply contracts is calculated with the transmission fee taken into account.

Services for technological connection to electric grids

Regional regulatory authority approves payment for technological connection according to individual project, as well as standardized tariff rates per unit of maximum supplied power on the basis of which the territorial network organization calculates the fee for technological connection to electric networks.

Payment for technological connection to the unified national electric network is approved by the Federal Antimonopoly Service.

Revenue from technological connection to power grids is calculated on the basis of the size of payment for technological connection determined in accordance with the legislation of the Russian Federation in the electricity sector.

Revenue from technological connection to the power network is recognised on the basis of the acts of acceptance of technological connection. In cases where under the terms of the contracts technological connection to power grids is performed in stages, revenue is recognised upon completion of stages of service.

Other revenue

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

Other expenses

Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. The amount of lease incentives received reduces the total lease expenses over the term of the lease.

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

Determining whether an agreement contains a lease

At the inception of an arrangement, the Group determines whether such an arrangement is or contains indicators of a lease. A specific asset is the subject of a lease if fulfilment of the arrangement is dependent on the use of that specified asset. An arrangement conveys the right to use the asset if the arrangement conveys to the Group the right to control the use of the underlying asset.

At inception or upon reassessment of the arrangement, the Group separates payments and other considerations required by such an arrangement into those for the lease and those for other elements proportionately to their fair values. If the Group concludes for a finance lease that it is impracticable to separate the payments reliably, then an asset and a liability are recognised at an amount equal to the fair value of the underlying asset contract. Subsequently the liability is reduced as payments are made and an imputed finance expense is recognised.

Social expenditure

To the extent that the Group's contributions to social programs benefit the community at large and are not restricted to the Group's employees, they are recognised in profit or loss as incurred. The Group's costs related to the financing of social programs, without making a commitment with respect to such financing in the future date are recognised in the consolidated statement of profit or loss and other comprehensive income as they arise.

Finance income and costs

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets, discounts on financial instruments, and foreign currency gains. Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date that the Group's right to receive payment is established.

Finance costs are comprised of interest expense on borrowings, financial leasing, foreign currency losses, discounts on financial instruments and impairment losses recognised on financial assets other than trade receivables. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis as either finance income or finance costs, depending on whether foreign currency movements are in a net gain or net loss position.

Income tax expense

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

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

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

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

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

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

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

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

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

Earnings per share

The Group presents basic and diluted earnings per share (“EPS”) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Profit attributable to ordinary shareholders is calculated by adjusting profit attributable to owners of the Company by profit attributable to holders of preference shares.

Segment Reporting

The Group identifies and presents operating segments based on the information that internally is reported to the Management Board, which is the Group’s chief operating decision maker.

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

Financial results that are reported to the Management Board include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items are most represented by revenue, expenses, assets and liabilities of the Company.

Segment capital expenditure is represented by acquisition cost of property, plant and equipment and intangible assets (except for goodwill).

Inter-segment pricing is based on general commercial conditions.

4 Measurement of fair values

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

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

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

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

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

5 Significant subsidiaries

	Country of incorporation	31 December 2017	31 December 2016
		% ownership/voting shares	% ownership/voting shares
OJSC "Pansionat otдыхa "Energetik"	Russian Federation	100	100
OJSC "Energoservis Kubani"	Russian Federation	100	100

6 Information about segments

The Management Board of PJSC Kubanenergo has been determined as the Chief Operating Decision-Maker.

The internal management reporting system is based on segments (branches formed on a territorial basis) related to transmission and distribution of electricity, technological connection to electricity grids in a number of regions of the Russian Federation.

Performance of each reportable segment is measured based on earnings or loss before interest expense, income tax and depreciation and amortisation (EBITDA) since these are reported in statutory accounts and regularly assessed by the Management Board. EBITDA is calculated as profit or loss before interest expenses, taxation and depreciation and amortization. The Management Board believes, that these indicators are most relevant when assessing the performance of certain segments in relation to other segments and other companies that operate in these industries.

In accordance with the requirements of IFRS 8, based on the information on segment revenue, EBITDA and total assets reported to the Management Board, The Group has identified one reportable segment, as described below, which is the Group's strategic business unit. This strategic business unit offers electricity transmission services including technological connection services in different geographical regions of the Russian Federation (Krasnodar Territory and Republic of Adygeya) and is managed in common. The "other" segment includes several operating segments the primary activities of which are the provision of rent services and repair and maintenance services.

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

Capital expenditure represents total investments made during the year in acquisition of property, plant and equipment including advances given and acquisition of construction materials.

Key segment items presented to and analysed by the Management Board are presented in the tables below.

a) Information about reportable segments

PJSC Kubanenergo
Notes to the Consolidated Financial Statements
for the year ended 31 December 2017
(in thousands of Russian Roubles, unless otherwise stated)

As at and for the year ended 31 December 2017:

	Kubanenergo	Other segments	Total
Revenue from external customers	42,250,391	54,684	42,305,075
Inter-segment revenue	2,636	104,826	107,462
Segment revenue	42,253,027	159,510	42,412,537
including:			
<i>Electricity transmission</i>	41,485,670	–	41,485,670
<i>Services for technological connection to electric grids</i>	647,952	–	647,952
<i>Other revenue</i>	119,405	159,510	278,915
Finance income	47,525	181	47,706
Finance costs	(1,907,082)	(43)	(1,907,125)
Depreciation and amortization	3,782,780	3,808	3,786,588
Segment profit before tax	1,167,674	46,535	1,214,209
EBITDA	6,857,536	50,386	6,907,922
Segment assets	71,856,753	110,586	71,967,339
Including property, plant and equipment and construction in progress	59,659,050	28,864	59,687,914
Capital expenditure	7,298,165	64	7,298,229
Segment liabilities	36,447,835	53,173	36,501,008

As at and for the year ended 31 December 2016:

	Kubanenergo	Other segments	Total
Revenue from external customers	41,723,935	78,204	41,802,139
Inter-segment revenue	2,266	57,803	60,069
Segment revenue	41,726,201	136,007	41,862,208
including:			
<i>Electricity transmission</i>	39,262,365	–	39,262,365
<i>Services for technological connection to electric grids</i>	2,380,524	–	2,380,524
<i>Other revenue</i>	83,312	136,007	219,319
Finance income	89,719	408	90,127
Finance costs	(1,888,922)	(26)	(1,888,948)
Depreciation and amortization	3,623,869	4,610	3,628,479
Segment profit/(loss) before tax	3,506,235	(9,799)	3,496,436
EBITDA	9,019,026	(5,163)	9,013,863
Segment assets	67,288,201	54,048	67,342,249
Including property, plant and equipment and construction in progress	55,910,737	32,550	55,943,287
Capital expenditure	5,448,161	–	5,448,161
Segment liabilities	31,889,792	32,634	31,922,426

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b) Reconciliation of key segment items reportable to the Management Board of the Group with similar items in these consolidated financial statements

Reconciliation of segment revenues:

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Revenue of segments	42,412,537	41,862,208
Inter-segment revenue elimination	(107,462)	(60,069)
Revenue per consolidated statement of profit or loss and other comprehensive income	<u>42,305,075</u>	<u>41,802,139</u>

Reconciliation of reportable segment's profit before tax:

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
EBITDA of reportable segments	6,907,922	9,013,863
Adjustment for accrual of provision for unused vacations and bonuses	108,227	(125,593)
Recognition of pension and other long-term employee benefit liabilities	51,686	38,687
Adjustment for impairment of other financial assets	9,584	–
Adjustment for intangible assets	9,708	47,887
Adjustment for revenue from electricity transmission	49	29,587
Adjustment for property, plant and equipment	(149)	(12,511)
Adjustment for receivables' impairment provision	(140)	(35,675)
Write-off of receivables	(149)	–
Elimination of intercompany dividends	(277)	–
Other adjustments	16,361	10,007
EBITDA	<u>7,102,822</u>	<u>8,966,252</u>
Depreciation and amortisation	(3,165,549)	(2,890,714)
Interest expenses on financial liabilities	(2,022,610)	(1,924,457)
Income tax expense	(1,197,526)	(1,295,592)
Profit/loss for the year per consolidated statement of profit or loss and other comprehensive income	<u>717,137</u>	<u>2,855,489</u>

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Reconciliation of reportable segment total assets:

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Total segment assets	71,967,339	67,342,249
Adjustment for deferred tax	319,869	915,689
Recognition of assets related to employee benefit fund	318,910	290,092
Adjustment for provision for impairment of receivables	428	568
The decrease in receivables for advances by VAT on advances issued	(152)	(9,630)
Write-off of receivables	(958)	–
Adjustment for prepaid expenses	(21,464)	(26,476)
Intersegment financial assets	(45,687)	(45,687)
Intersegment balances	(59,031)	(1,137)
The decrease in the amount of VAT recoverable by the amount of VAT on advances received	(750,713)	(544,681)
Adjustment for property, plant and equipment	(7,090,966)	(7,706,725)
Other adjustments	(64,856)	(23,505)
Total assets per consolidated statement of financial position	<u>64,572,719</u>	<u>60,190,757</u>

Reconciliation of reportable segment total liabilities:

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Total segment liabilities	36,501,008	31,922,426
Recognition of pension and other long-term employee benefit liabilities	611,115	575,813
Adjustment for accrual of provision for unused vacations and bonuses	122,399	230,625
The decrease in other accounts payable by the amount of VAT on advances received	(152)	(9,630)
Intersegment balances	(59,031)	(1,137)
Write-off of deferred income	(77,007)	(66,459)
Adjustment for deferred tax	(179,076)	(128,943)
The decrease in accounts payable on advances received by the amount of VAT on advances received	(750,713)	(544,681)
Other adjustments	(2,000)	(2,566)
Total liabilities per consolidated statement of financial position	<u>36,166,543</u>	<u>31,975,448</u>

c) Major customer

The Group operates in the Russian Federation. The Group does not earn revenue from foreign customers and does not hold non-current assets abroad.

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For the years ended 31 December 2017 and 31 December 2016, the Group had two customers with individual turnover over 10% of total Group revenues. Revenues from these customers are reported by the operating segments in Kubanenergo.

Total amounts of revenues from Customer 1 for 2017 were RUB 19,375,047 thousand or 45.80 % of the Group total revenue (2016: RUB 18,539,390 thousand or 44.35%). Total amounts of revenues from Customer 2 for 2017 were RUB 15,112,964 thousand or 35.72 % of the Group total revenue (2016: RUB 14,757,407 thousand or 35.30%).

7 Revenue

	<u>Year ended</u> <u>31 December 2017</u>	<u>Year ended</u> <u>31 December 2016</u>
Electricity transmission	41,483,734	39,260,269
Services for technological connection to electric grids	647,952	2,380,524
Rental income	22,430	18,582
Repairs and maintenance	32,931	5,521
Other revenue	118,028	137,243
	<u>42,305,075</u>	<u>41,802,139</u>

Other revenue comprises generally revenue from rendering services related to restriction of electricity use conditions, assembly and dissembling of electrical meters, rendering services related to electricity metering.

8 Other income/(expense), net

	<u>Year ended</u> <u>31 December 2017</u>	<u>Year ended</u> <u>31 December 2016</u>
Income in the form of fines and penalties on commercial contracts	472,387	88,475
Insurance coverage, net	93,028	101,734
Gain on property, plant and equipment and inventories received for free	62,937	63,444
Accounts payable written-off	40,302	3,498
Income from identified non-contractual consumption of electricity	32,240	83,026
Income in the form of inventories received from liquidation of property, plant and equipment	7,042	6,111
Income from sale of property, plant and equipment	127	11,302
Expenses on write off of property, plant and equipment, including prepayments for property, plant and equipment	(42,653)	(68,301)
Loss on disposal of intangible assets (Note 14)	(11,908)	(763)
	<u>653,502</u>	<u>288,526</u>

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9 Operating expenses

	Year ended 31 December 2017	Year ended 31 December 2016
Personnel costs	5,602,477	5,526,659
Depreciation and amortisation	3,165,549	2,890,714
<i>Material expenses, including:</i>		
Electricity for compensation of technological losses	7,598,384	7,445,886
Purchased electricity and heat power for own needs	112,949	111,815
Other material expenses	1,005,380	896,651
<i>Production works and services, including:</i>		
Electricity transmission services	17,096,278	14,855,066
Taxes and charges other than income tax	669,274	620,853
Repair and maintenance services	390,415	408,400
Rent	243,658	225,781
Other production works and services	143,664	70,389
Insurance	76,172	75,858
<i>Other third-party services, including:</i>		
Security services	203,994	193,165
Consulting, legal and audit services	120,442	17,128
Software costs and servicing	70,748	63,950
Communication services	62,236	62,796
Transportation services	3,213	4,942
Other services	674,675	239,275
Provisions	1,192,119	2,099,169
Profit and loss of previous years	312,355	201,389
Business trip expenses	169,191	120,261
The costs associated with the maintenance of the property	129,556	139,721
Management services	76,485	76,485
Fines and penalties on commercial contracts	32,691	57,014
Impairment of accounts receivable	(73,160)	(679,837)
Other expenses	15,208	396,596
	39,093,953	36,120,126

10 Personnel costs

	Year ended 31 December 2017	Year ended 31 December 2016
Wages and salaries	4,090,100	4,036,506
Social security contributions	1,231,396	1,202,444
Expenses related to defined benefit plan	31,632	38,424
Other	249,349	249,284
	5,602,477	5,526,658

The amount of contributions to the defined contribution plan was RUB 54,500 thousand for the year ended 31 December 2017 (for the year ended 31 December 2016: RUB 86,433 thousand).

Remuneration to key management personnel is disclosed in Note *Related Parties*.

11 Finance income and costs

Recognised in profit or loss	Year ended 31 December 2017	Year ended 31 December 2016
Finance income		
Interest income on loans, bank deposits, promissory notes and balances in the bank accounts	47,429	90,127
Interest income on assets related to employee benefit liability	20,724	12,769
Effect of initial discounting of financial liabilities	1,618	96
Amortization of discount on financial assets	2,878	2,006
	<u>72,649</u>	<u>104,998</u>
Finance costs		
Interest expense on financial liabilities measured at amortized cost	(1,969,816)	(1,873,732)
Interest expense on long-term employee benefits liability	(43,790)	(40,104)
Effect of initial discounting of financial assets	(6,968)	(3,520)
Amortization of discount on financial liabilities	(2,036)	(7,100)
	<u>(2,022,610)</u>	<u>(1,924,456)</u>

12 Income tax

	Year ended 31 December 2017	Year ended 31 December 2016
Current income tax		
Accrual of current tax	(635,605)	(1,194,267)
Adjustment of tax for prior years	(130)	1,102
Total	<u>(635,735)</u>	<u>(1,193,165)</u>
Deferred income tax		
Origination and reversal of temporary differences	(561,791)	(102,427)
Total	<u>(561,791)</u>	<u>(102,427)</u>
Income tax expense	<u>(1,197,526)</u>	<u>(1,295,592)</u>

Income tax recognised in other comprehensive income:

	Year ended 31 December 2017			Year ended 31 December 2016		
	Before tax	Income tax	Net of tax	Before tax	Income tax	Net of tax
Remeasurments of the defined benefit liability	(14,380)	2,876	(11,504)	(75,142)	15,028	(60,114)
	<u>(14,380)</u>	<u>2,876</u>	<u>(11,504)</u>	<u>(75,142)</u>	<u>15,028</u>	<u>(60,114)</u>

The applicable tax rate of PJSC Kubanenergo and its subsidiaries in 2017 and 2016 is the standard income tax rate of 20% for Russian companies. This rate has been used in the calculation of deferred tax assets and liabilities.

Profit (loss) before tax is reconciled to income tax expenses as follows:

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	Year ended 31 December 2017	%	Year ended 31 December 2016	%
Profit/(loss) before tax	<u>1,914,662</u>	100	<u>4,151,081</u>	100
Income tax at applicable tax rate	(382,932)	(20)	(830,216)	(20)
Tax effect of items which are not deductible or taxable for taxation purposes	(819,423)	(43)	(464,582)	(11)
Adjustments of prior years	(130)	(0.01)	1,102	0.03
Change in unrecognised deferred tax assets	4,959	0.26	(1,896)	(0.05)
	<u>(1,197,526)</u>	<u>(63)</u>	<u>(1,295,592)</u>	<u>(31)</u>

13 Property, plant and equipment

	Land and buildings	Electricity transmission networks	Equipment for electricity transmission	Other PPE	Construction in progress	Total
Cost/Deemed cost						
As at 1 January 2016	7,150,299	34,640,288	13,336,956	6,496,358	3,158,744	64,782,645
Additions	48,691	31,537	59,763	297,733	5,468,742	5,906,466
Transfers	258,803	1,545,035	1,150,454	256,422	(3,210,714)	—
Disposals	(1,805)	(36,542)	(8,638)	(35,692)	(47,568)	(130,245)
Reclassifications between groups	(8,050)	(14,792)	(135,711)	158,553	—	—
As at 31 December 2016	7,447,938	36,165,526	14,402,824	7,173,374	5,369,204	70,558,866
As at 1 January 2017	7,447,938	36,165,526	14,402,824	7,173,374	5,369,204	70,558,866
Additions	2,271	8,123	126,899	152,614	7,280,233	7,570,140
Transfers	395,697	1,930,227	1,497,213	386,552	(4,209,689)	—
Disposals	(2,414)	(20,311)	(24,183)	(29,796)	(72,465)	(149,169)
Reclassification between groups	235	(106)	(383)	254	—	—
As at 31 December 2017	7,843,727	38,083,459	16,002,370	7,682,998	8,367,283	77,979,837

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	Land and buildings	Electricity transmission networks	Equipment for electricity transmission	Other PPE	Construction in progress	Total
Accumulated depreciation and impairment						
As at 1 January 2016	(2,123,229)	(8,067,995)	(5,421,686)	(3,785,005)	(145,519)	(19,543,434)
Transfer of impairment losses when entry into fixed assets	(11,748)	(9,463)	(6,843)	(4,876)	32,930	-
Accrual of impairment loss of property, plant and equipment	-	-	-	-	(29)	(29)
Depreciation charge	(244,095)	(1,256,184)	(770,005)	(567,873)	-	(2,838,157)
Disposals	1,728	12,368	5,658	27,994	3,075	50,823
Reclassification of depreciation and impairment losses	27,154	(1,731)	83,334	(108,757)	-	-
As at 31 December 2016	(2,350,190)	(9,323,005)	(6,109,542)	(4,438,517)	(109,543)	(22,330,797)
As at 1 January 2017	(2,350,190)	(9,323,005)	(6,109,542)	(4,438,517)	(109,543)	(22,330,797)
Transfer of impairment losses when entry into fixed assets	(107)	(9,196)	(7,271)	(368)	16,942	-
Depreciation charge	(260,735)	(1,390,024)	(859,938)	(597,393)	-	(3,108,090)
Disposals	1,425	4,857	14,045	26,903	274	47,504
Reclassification of depreciation and impairment losses	(132)	4	395	(267)	-	-
As at 31 December 2017	(2,609,739)	(10,717,364)	(6,962,311)	(5,009,642)	(92,327)	(25,391,383)
Net book value						
As at 31 December 2016	5,097,748	26,842,521	8,293,282	2,734,857	5,259,661	48,228,069
As at 31 December 2017	5,233,988	27,366,095	9,040,059	2,673,356	8,274,956	52,588,454

As at 31 December 2017 construction in progress includes prepayments for property, plant and equipment of RUB 1,071,716 thousand (as at 31 December 2016: RUB 95,124 thousand), and materials for construction of property, plant and equipment of RUB 655,135 thousand (as at 31 December 2016: RUB 936,021 thousand).

Capitalized interest for the year ended 31 December 2017 amounted to RUB 121,886 thousand (for the year ended 31 December 2016: RUB 27,150 thousand), with capitalization rate used to calculate borrowing costs to be capitalized during the period of 7,85% (for the year ended 31 December 2016: 6,16%).

The portion of depreciation has been capitalized to the cost of the capital construction objects for the year ended 31 December 2017 of RUB 8,281 thousand (for the year ended 31 December 2016: RUB 0 thousand).

As at 31 December 2017 and 31 December 2016 there are no fixed assets pledged as collateral for loans and borrowings.

Impairment of property, plant and equipment

As the indicators of impairment of non-current assets were revealed, the Group performed an impairment test as at 31 December 2017. For this, the Group analyzed cash flows and compared the estimated recoverable amount with the carrying amounts of non-current assets.

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

Therefore the value in use for property, plant and equipment as at 31 December 2017 was determined using projected cash flows method. This method considers the future net cash flows expected to be generated by the property, plant and equipment in the process of operating activities and upon disposal, to determine the recoverable amount of the assets.

Cash-generating units are determined by the Group based on the geographical location of the branches and subsidiaries which are the smallest identifiable groups of assets that generate cash inflows regardless of other assets of the Group.

The following key assumptions were used in assessing the recoverable amount of the cash-generating units:

The forecast cash flows have been determined for 2018-2022 based on the best estimate of the management in respect of the electricity transmission volumes, operating expenses and capital expenditure, and tariffs approved by regulatory authorities for 2017.

Source electricity transmission tariffs for the forecasted period were taken from business plans, which were based on tariff models prepared taking into account annual average growth of tariffs for electricity transmission services in accordance with the forecast for the social and economic development of the Russian Federation for 2017 and the planning period of 2018-2022. Growth rates of tariffs in 2018-2022 are limited by inflation rate as forecasted by the Ministry for Economic Development.

Forecasted electricity transmission volumes have been determined on the basis of annual business plans for 2018-2022.

Projected cash flows were discounted to their present value using the nominal weighted average cost of capital of 10.25%.

Growth rate of the net cash flows in the post-forecast period amounted to 3.3%.

As a result of testing as at 31 December 2017, no impairment of fixed assets was identified.

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Sensitivity of value in use of property, plant and equipment to changes in the underlying assumptions in calculation is disclosed in the table below:

	<u>Increase, %</u>	<u>Decrease, %</u>
Change in discount rate by 0.25%	-3,04	+3,26
Change in required gross proceeds to basis by 3% in every period	+1,75	-17,41
Change in growth rate of the net cash flows in the post-forecast period by 0.4%	+3,88	-3,46
Change in operating expenses by 5%	-14,05	+0,36
Change in (capital) investments by 10%	-1,42	+1,42

14 Intangible assets

	<u>Software</u>	<u>Research and development</u>	<u>Other intangible assets</u>	<u>Total intangible assets</u>
Cost				
As at 1 January 2016	212,826	15,741	16,836	245,403
Additions	56,263	11,166	–	67,429
Disposals	–	(763)	–	(763)
As at 31 December 2016	269,089	26,144	16,836	312,069
As at 1 January 2017	269,089	26,144	16,836	312,069
Reclassification between groups	11,633	(11,633)	–	–
Additions	96,905	12,559	11,508	120,972
Disposals	–	(11,908)	–	(11,908)
As at 31 December 2017	377,627	15,162	28,344	421,133
Accumulated amortisation and impairment				
As at 1 January 2016	(144,107)	–	(5,231)	(149,338)
Amortisation charge	(49,571)	–	(4,933)	(54,504)
As at 31 December 2016	(193,678)	–	(10,164)	(203,842)
As at 1 January 2017	(193,678)	–	(10,164)	(203,842)
Amortisation charge	(61,953)	–	(4,903)	(66,856)
As at 31 December 2017	(255,631)	–	(15,067)	(270,698)
Net book value				
As at 31 December 2016	75,411	26,144	6,672	108,227
As at 31 December 2017	121,996	15,162	13,277	150,435

The intangible assets amortisation charge included in operating expenses of the consolidated statement of profit or loss and other comprehensive income amounted to RUB 66,856 thousand (for the year ended 31 December 2016: RUB 52,557 thousand). The capitalized amortisation of intangible assets amounted to RUB 1,116 thousand (for the year ended 31 December 2016: RUB 1,947 thousand).

Intangible assets are amortised using the straight-line method.

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Research and development recognised in operating expenses for 2017 amounted to RUB 49,917 thousand (2016: RUB 0 thousand).

Other intangible assets comprise licenses and calculation models including graphical schemes and models of RUB 13 277 thousand as at 31 December 2017 (as at 31 December 2016: RUB 6 672 thousand).

15 Financial investments

	<u>31 December 2017</u>	<u>31 December 2016</u>
Non-current		
Financial assets held-to-maturity	1	1
	<u>1</u>	<u>1</u>

16 Deferred tax assets and liabilities

The differences between IFRS and Russian tax law result in temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes.

a) *Recognised deferred tax assets and liabilities*

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

	<u>Assets</u>		<u>Liabilities</u>		<u>Net</u>	
	<u>31 December 2017</u>	<u>31 December 2016</u>	<u>31 December 2017</u>	<u>31 December 2016</u>	<u>31 December 2017</u>	<u>31 December 2016</u>
Property, plant and equipment	535,043	590,561	–	–	535,043	590,561
Intangible assets	10,948	–	–	(149)	10,948	(149)
Available-for-sale financial investments	–	–	(1,937)	(20)	(1,937)	(20)
Inventories	–	–	–	(41)	–	(41)
Trade and other receivables and prepayments	408,262	491,270	–	–	408,262	491,270
Provisions	–	489,266	(1,398)	–	(1,398)	489,266
Employee benefit liabilities	29,420	29,181	–	–	29,420	29,181
Trade and other payables	132,400	154,863	–	–	132,400	154,863
The tax loss carry forward	84,428	7,091	–	–	84,428	7,091
Other	6,277	5,295	–	–	6,277	5,295
Tax assets/(liabilities)	<u>1,206,778</u>	<u>1,767,527</u>	<u>(3,335)</u>	<u>(210)</u>	<u>1,203,443</u>	<u>1,767,317</u>
Set off of tax	(3,335)	(210)	3,335	210	–	–
Unrecognized deferred tax assets	–	(4,959)	–	–	–	(4,959)
Net tax assets/(liabilities)	<u>1,203,443</u>	<u>1,762,358</u>	<u>–</u>	<u>–</u>	<u>1,203,443</u>	<u>1,762,358</u>

b) *Unrecognized deferred tax assets*

The deductible temporary differences and tax losses do not expire under current tax legislation. Deferred tax assets have not been recognised with respect to tax losses and temporary differences because it is not probable that future taxable profit will be available, against which the loss-making Group's companies can utilize the relevant temporary differences and tax losses.

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Deferred tax assets have not been recognised in respect of the following items:

	31 December 2017	31 December 2016
Tax losses	–	24,795
Total	–	24,795
Unrecognised deferred tax assets at the applicable tax rate	–	4,959

c) Movement in temporary differences during the year

	1 January 2017	Recognised in profit or loss	Recognised in other comprehensive income	31 December 2017
Property, plant and equipment	590,561	(55,518)	–	535,043
Intangible assets	(149)	11,097	–	10,948
Available-for-sale financial investments	(20)	(1,917)	–	(1,937)
Inventories	(41)	41	–	–
Trade and other receivables and prepayments	491,270	(83,008)	–	408,262
Provisions	489,266	(490,664)	–	(1,398)
Employee benefit liabilities	29,181	(2,637)	2,876	29,420
Trade and other payables	154,863	(22,463)	–	132,400
The tax loss carry forward	7,091	77,337	–	84,428
Other	5,295	982	–	6,277
Unrecognized deferred tax assets	(4,959)	4,959	–	–
	1,762,358	(561,791)	2,876	1,203,443

	1 January 2016	Recognised in profit or loss	Recognised in other comprehensive income	31 December 2016
Property, plant and equipment	657,342	(66,781)	–	590,561
Intangible assets	72	(221)	–	(149)
Available-for-sale financial investments	3,447	(3,467)	–	(20)
Inventories	(202)	161	–	(41)
Trade and other receivables and prepayments	651,052	(159,782)	–	491,270
Provisions	381,555	107,711	–	489,266
Employee benefit liabilities	12,865	1,288	15,028	29,181
Trade and other payables	135,299	19,564	–	154,863
The tax loss carry forward	3,981	3,110	–	7,091
Other	7,409	(2,114)	–	5,295
Unrecognized deferred tax assets	(3,063)	(1,896)	–	(4,959)
	1,849,757	(102,427)	15,028	1,762,358

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17 Inventories

	<u>31 December 2017</u>	<u>31 December 2016</u>
Raw materials and supplies	774,507	735,930
Provision for impairment of raw materials and supplies	(3,239)	(5,037)
Other inventories	817,157	681,765
Provision for impairment of other inventories	(3,756)	(4,322)
	<u>1,584,669</u>	<u>1,408,336</u>

As at 31 December 2017 and 31 December 2016, the Group did not pledge inventories as collateral under loan or other agreements.

During the year ended 31 December 2017, RUB 1,005,380 thousand were recognised as expenses (during the year ended 31 December 2016: RUB 896,651 thousand) within operating expenses as *Other material expenses*.

18 Trade and other receivables

	<u>31 December 2017</u>	<u>31 December 2016</u>
Non-current trade and other receivables		
Other receivables	14,207	5,655
Total financial assets	<u>14,207</u>	<u>5,655</u>
Advances given	5,890	4,337
VAT on advances of customers and clients	5,663	5,200
	<u>25,760</u>	<u>15,192</u>
Current trade and other receivables		
Trade receivables	7,463,513	7,847,756
Provision for impairment of trade receivables	(1,307,373)	(1,436,089)
Other receivables	1,007,802	1,196,363
Provision for impairment of other receivables	(701,532)	(889,801)
Total financial assets	<u>6,462,410</u>	<u>6,718,229</u>
Advances given	146,617	121,513
Provision for impairment of advances given	(112,813)	(111,666)
VAT recoverable	190,081	17,384
Prepaid taxes, other than income tax and VAT	7,759	4,343
	<u>6,694,054</u>	<u>6,749,803</u>

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 27.

Balances with related parties are disclosed in Note 31.

19 Cash and cash equivalents

	<u>31 December 2017</u>	<u>31 December 2016</u>
Cash in banks and in hand	1,678,788	1,249,959
Cash equivalents	2,255	4,139
	<u>1,681,043</u>	<u>1,254,098</u>

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	Rating	Rating agency	31 December 2017	31 December 2016
Sberbank*	Ba2	Moody's	39,799	37,238
Gazprombank*	Ba2	Moody's	910,745	183,587
Other			728,222	1,029,122
Petty cash			22	12
			<u>1,678,788</u>	<u>1,249,959</u>

*State related banks

Cash equivalents consist of short-term bank deposits:

	Interest rate	Rating	Rating agency	31 December 2017	31 December 2016
Sberbank*	4.83%-7.34%	Ba2	Moody's	2,000	4,000
				<u>2,000</u>	<u>4,000</u>

*State related banks

As at 31 December 2017 and 31 December 2016 all cash and cash equivalents balances are denominated in roubles.

20 Share capital

	Ordinary shares	
	31 December 2017	31 December 2016
Par value	100 RUB	100 RUB
On issue at 1 January	282,868,130	282,868,130
In issue at end of year, fully paid	282,868,130	282,868,130

a) Dividends

Distribution and other use of year-end profit is based on the annual official financial statements of the parent of the Group PJSC "Kubanenergo" prepared in accordance with the Russian Accounting Principles. Net profit of the current year is subject to distribution under the Russian legislation.

At the annual shareholders general meeting held on 20 June 2017, dividends for 2016 were declared in the amount of RUB 535,125 thousand (RUB 1.762658 per ordinary share). No dividends were declared for 2017.

b) Additional issue of shares

On 19 September 2016, the annual General Meeting of Shareholders of PJSC "Kubanenergo" approved the decision to increase the Company's authorized capital by issuing additional 57,457,846 ordinary shares with a nominal value of RUB 100 per share. The issue of shares was registered by the Central Bank of the Russian Federation on 15 December 2016. Within the framework of this right, the shareholders contributed to the authorized capital of the Company RUB 20,358 thousand in 2017 (2016: RUB 2,072,164 thousand), which were recognised as a reserve for the issue of shares directly in equity.

21 Earnings per share

The calculation of basic earnings per share for the year ended 31 December 2017 was based on the earnings attributable to ordinary shareholders for 2017 in the amount of RUB 718,835 thousand (for 2016: earnings of RUB 2,855,489 thousand) and the weighted average number of ordinary shares outstanding of 303,589,790 in 2017 (2016: 282,868 130 shares).

The Company has no dilutive financial instruments.

<i>In thousands of shares</i>	<u>2017</u>	<u>2016</u>
Ordinary shares at 1 January	282,868	282,868
The number of unregistered shares	20,722	—
Weighted average number of shares for the year ended 31 December	303,590	282,868
	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Weighted average number of ordinary shares outstanding, for the year ended 31 December (thousands of shares)	303,590	282,868
Earnings for the year attributable to holders of ordinary shares	717,136	2,855,489
Earnings per ordinary share - basic and diluted (in Russian Roubles)	2.36	10.09

22 Loans and borrowings

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Non-current liabilities		
Unsecured loans and borrowings	15,617,796	11,912,239
Bonds issued	7,000,000	7,000,000
	<u>22,617,796</u>	<u>18,912,239</u>
Current liabilities		
Unsecured loans and borrowings	91,686	80,100
	<u>91,686</u>	<u>80,100</u>
including:		
Interest payable on loans and borrowings	91,064	79,078
	<u>91,064</u>	<u>79,078</u>

	<u>Year of maturity</u>	<u>Effective interest rate</u>		<u>Carrying amount</u>	
		<u>31 December 2017</u>	<u>31 December 2016</u>	<u>31 December 2017</u>	<u>31 December 2016</u>
Unsecured loans and borrowings					
Sberbank*	2019-2020	8.25%-10.25%	9.9%	8,913,336	2,000,000
Gazprombank*	2019-2020	8.35%-10.80%	10.00-10.80%	5,904,459	9,912,239
Bonds issued (PJSC "ROSSETI"*)	2019-2025	10.44-12.63%	10.44-12.63%	7,000,000	7,000,000
Bank VBRR (JSC)	2019	0%-10.20%	—	800,000	—
Other	2018	Interest free	Interest free	622	1,022

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*Loans and borrowings from the state - related entities.

As at 31 December 2017 and 31 December 2016, all loans and borrowings balances are denominated in roubles.

The Group has not entered into any hedging agreements in respect of its interest rate exposure. The Group's exposure to interest rate risk is disclosed in Note 27.

23 Changes in liabilities arising from financial activities

	Principal amount of financial liabilities payable net of finance lease and dividends payable		Interest on financial liabilities payable net of finance lease and dividends payable	Dividends payable	Total
	Non- current portion	Current portion			
At 1 January 2017	11,913	11,912	3	—	11,916
Cash flows from financing activities, net	3,706	3,706	—	(38)	3,668
Cash flows from interest paid (operating activities, for reference)	—	—	(1,277)	—	(1,277)
Interest and dividends payable accrued	—	—	1,165	39	1,204
Interest capitalized	—	—	122	—	122
At 31 December 2017	15,619	15,618	13	1	15,633

24 Employee Benefits

The Group has a defined benefit pension and other long-term defined benefit plans that cover most full-time and retired employees. Defined post-employment benefits consist of several unfunded plans providing for lump-sum payments upon retirement, financial support for current pensioners, death benefits and anniversary benefits.

Amounts of obligations recognised in the statement of financial position are presented below:

Net value of defined benefit plan liabilities:

	<u>31 December 2017</u>	<u>31 December 2016</u>
Net value of post-employment benefit plan obligations	611,115	575,813
Net value of other long-term employee benefit plan obligation	—	—
Total obligations, net	<u>611,115</u>	<u>575,813</u>

Changes in the value of assets related to employee benefits obligations:

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Value of assets at 1 January	290,092	299,413
Return on plan assets	20,724	12,769
Employer contributions	52,000	—
Other movements in the accounts	1,007	1,015
Payment of benefits	(44,913)	(23,105)
Value of assets at 31 December	<u>318,910</u>	<u>290,092</u>

Assets related to pension plans and defined benefit plans are administrated by non-state pension funds NPF Electroenergetiki and Professionalny.

These assets are not the defined benefit plans' assets because under the terms of agreements between the Group and the funds the Group has the right to use the contributions paid under defined benefit plans to fund its defined contribution pension plans or transfer to another fund on the Group's own initiative.

Movements in the present value of defined benefit liabilities:

	<u>Year ended 31 December 2017</u>		<u>Year ended 31 December 2016</u>	
	<u>Post employment benefits</u>	<u>Other long- term employee benefits</u>	<u>Post employment benefits</u>	<u>Other long- term employee benefits</u>
Defined benefit plan obligation as at 1 January	575,813	—	508,576	—
Current service cost	31,632	—	38,424	—
Past service cost and curtailments	—	—	—	—
Interest expense on liabilities	43,790	—	40,104	—
Remeasurement effect from:				
- loss/(gain) from change in demographic actuarial assumptions	29,067	—	7,558	—
- (gain)/loss from change in financial actuarial assumptions	45,843	—	(7,901)	—
- (gain)/loss from experience adjustment	(60,530)	—	75,485	—
Contributions to the plan	(54,500)	—	(86,433)	—
Defined benefit plan obligation as at 31 December	<u>611,115</u>	<u>—</u>	<u>575,813</u>	<u>—</u>

Expenses recognised in profit or loss for the period:

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	<u>Year ended</u> <u>31 December 2017</u>	<u>Year ended</u> <u>31 December 2016</u>
Employee service cost	31,632	38,424
Remeasurement of other long-term employee benefit obligation	–	–
Interest expense	43,790	40,104
Total expenses recognised in profit or loss	75,422	78,528

(Gains)/losses recognised in other comprehensive income for the period:

	<u>Year ended</u> <u>31 December 2017</u>	<u>Year ended</u> <u>31 December 2016</u>
Loss/(gain) from change in demographic actuarial assumptions	29,067	7,558
(Gain)/loss from change in financial actuarial assumptions	45,843	(7,901)
(Gain)/loss from experience adjustment	(60,530)	75,485
Total (gain)/loss recognised in other comprehensive income	14,380	75,142

Movements in provision for remeasurement of obligations in other comprehensive income during the period:

	<u>Year ended</u> <u>31 December 2017</u>	<u>Year ended</u> <u>31 December 2016</u>
Remeasurements at 1 January	281,683	206,541
Movement of remeasurements	14,380	75,142
Remeasurements at 31 December	296,063	281,683

The key actuarial assumptions are as follows:

	<u>31 December 2017</u>	<u>31 December 2016</u>
Financial assumptions		
Discount rate	7.5%	8.5%
Future salary increase	4.5%	4.7%
Inflation rate	4.0%	4.7%
Demographic assumptions		
Expected age of retirement		
• Men	60 years	60 years
• Women	55 years	55 years
Average level of staff movement	9.5%	11.2%

A sensitivity of total employee benefits obligations to changes in the key actuarial assumptions is as follows:

	<u>Changes in the</u> <u>assumption</u>	<u>Impact on obligation</u>
Discount rate	Increase/decrease by 0.5%	Decrease/increase by 5.5%
Future salary growth	Increase/decrease by 0.5%	Increase/decrease by 0.8%
Future growth of benefits (inflation)	Increase/decrease by 0.5%	Increase/decrease by 4.7%
Level of staff movement	Increase/decrease by 10%	Decrease/increase by 4.3%
Mortality level	Increase/decrease by 10%	Decrease/increase by 1.0%
	31 December 2017	31 December 2016

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Defined benefit plan liability	(611,115)	(575,813)
Value of assets	318,910	290,092
Net value	292,205	(285,721)

Expected payments under the long-term employee benefit plans in 2018 are RUB 65,756 thousand including RUB 65,756 thousand under the defined benefit plan including non-state pension schemes.

25 Trade and other payables

	<u>31 December 2017</u>	<u>31 December 2016</u>
Non-current payables		
Trade payables	3,013	2
Other payables	251	1,344
Total financial liabilities	3,264	1,346
Advances from customers	984,093	1,426,835
	987,357	1,428,181
Current payables		
Trade payables	6,230,622	4,863,063
Other payables and accrued expenses	1,325,818	550,148
Payables to employees	826,831	928,037
Dividends payable	500	37
Total financial liabilities	8,383,771	6,341,285
Advances from customers	2,138,408	1,378,158
	2,138,408	1,378,158
Taxes payable		
VAT	70,804	474,949
Property tax	152,509	133,872
Social security contributions	108,968	93,935
Other taxes payables	46,205	46,816
	378,486	749,572
	10,900,665	8,469,015

The Group's exposure to liquidity risk related to payables is disclosed in Note 27.

Long-term advances from customers include advances for technological connections services of RUB 984,093 thousand as at 31 December 2017 (as at 31 December 2016: RUB 1,426,835 thousand).

26 Provisions

	<u>For the year ended 31 December 2017</u>	<u>For the year ended 31 December 2016</u>
Balance at 1 January	2,446,329	1,907,775
Increase for the year	1,380,389	2,223,710
Decrease due to reversal of provisions	(188,270)	(124,541)
Provisions used	(2,757,800)	(1,560,615)
Capitalized	25,289	—
Balance at 31 December	905,937	2,446,329

Provisions relate mainly to legal proceedings and claims against the Group in the day-to-day terms of business.

27 Financial risk and capital management

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In the course of its ordinary business activities, the Group is exposed to various financial risks including but not limited to as follows: market risk (currency risk, interest risk and price risk), credit risk and liquidity risk.

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

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

a) Credit risk

Credit risk is the risk of financial losses to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

Trade and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. The Group monitors existing debt on a regular basis and takes steps to collect the debt and to mitigate losses.

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

The Group does not require collateral in respect of receivables.

The Group establishes a provision for impairment that represents its estimate of anticipated losses with respect to receivables that relate to individually significant exposures.

Exposure to credit risk

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

	Carrying amount	
	31 December 2017	31 December 2016
Trade and other receivables (less provision for impairment)	6,476,617	6,723,884
Cash and cash equivalents	1,681,043	1,254,098
	8,157,660	7,977,982

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

	Gross	Impairment loss	Gross	Impairment loss
	31 December 2017	31 December 2017	31 December 2016	31 December 2016
Customers of electricity transmission services	7,393,769	(1,289,116)	7,807,100	(1,425,230)
Customers of services for technological connection to electric grids	37,259	(11,681)	22,287	(7,404)
Other customers	1,054,494	(708,108)	1,220,387	(893,256)
	8,485,522	(2,008,905)	9,049,774	(2,325,890)

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The Group's ten most significant debtors account for RUB 5,968,871 thousand of the trade receivables carrying amount as at 31 December 2017 (as at 31 December 2016: RUB 6,176,459 thousand).

Impairment losses of trade and other receivables

The aging of trade and other receivables is provided below:

	<u>Gross</u> <u>31 December</u> <u>2017</u>	<u>Impairment loss</u> <u>31 December</u> <u>2017</u>	<u>Gross</u> <u>31 December</u> <u>2016</u>	<u>Impairment loss</u> <u>31 December</u> <u>2016</u>
Not past due	5,311,784	(197,200)	5,212,269	(173,489)
Past due less than 3 months	1,278,427	(288,779)	2,052,007	(552,034)
Past due more than 3 months and less than 6 months	209,733	(42,234)	156,098	(127,410)
Past due more than 6 months and less than 1 year	414,790	(349,987)	191,083	(150,465)
Past due more than 1 year	1,270,788	(1,130,705)	1,438,317	(1,322,492)
	<u>8,485,522</u>	<u>(2,008,905)</u>	<u>9,049,774</u>	<u>(2,325,890)</u>

The Group analyzed that not impaired past due accounts receivable are recoverable with high level of probability at the reporting date.

The movement in the provision for impairment of trade and other receivables was as follows:

	<u>2017</u>	<u>2016</u>
Balance at 1 January	2,325,890	3,059,013
Increase in provision for the period	572,995	636,990
Amounts of trade and other receivables written off using the provision accrued earlier	(651,352)	(56,835)
Provision reversal for the period	(238,628)	(1,313,278)
Balance at 31 December	<u>2,008,905</u>	<u>2,325,890</u>

The Group has no contractual basis for netting off of financial assets and financial liabilities and management of the Group does not expect future netting based on additional agreements as at 31 December 2017 and as at 31 December 2016.

b) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due.

Management of liquidity risk involves maintaining sufficient cash and the availability of financial resources by securing credit lines. The Group adheres to a balanced model of financing working capital by using both short-term and long-term sources. Basically temporarily free funds invested in the short-term financial instruments such as bank deposits.

The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. This approach is used to analyze payment dates associated with financial assets, and also to forecast cash flows from operating activities.

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The amount of free limit on open but unused credit lines of the Group was RUB 9,402,205 thousand as at 31 December 2017 (31 December 2016: RUB 4,938,033 thousand). The Group has opportunity to attract additional financing within the corresponding limits including for the purpose of execution of the short-term obligations.

The following are the contractual maturities of financial liabilities, including estimated interest payments and without the impact of netting agreements. It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

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31 December 2017	Carrying amount	Contractual cash flows	less than 12 months	1-2 years	2-3 years	3-4 years	4-5 years	more than 5 years
Non-derivative financial liabilities								
Loans and borrowings	22,709,482	29,523,503	2,199,893	11,181,362	10,668,088	374,832	374,832	4,724,496
Trade and other payables	8,386,535	8,388,684	8,383,272	4,339	705	368	-	-
	31,096,017	37,912,187	10,583,165	11,185,701	10,668,793	375,200	374,832	4,724,496
31 December 2016								
Non-derivative financial liabilities								
Loans and borrowings	18,992,339	26,486,947	2,105,966	6,044,671	12,488,542	408,708	339,804	5,099,256
Trade and other payables	6,342,594	6,345,087	6,342,557	705	752	705	368	-
	25,334,933	32,832,034	8,448,523	6,045,376	12,489,294	409,413	340,172	5,099,256

c) Market risk

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

Currency risk

The majority of the Group's revenues and expenditures, monetary assets and liabilities are denominated in RUB, and as such financial results are insignificantly impacted by changes in exchange rates.

Interest rate risk

Changes in interest rates primarily influence loans and borrowings since they change their fair values (loans and borrowings with fixed rates) or future cash flows (loans and borrowings with variable rate). The Group management does not have a formal policy for determining how much of the group's exposure should be to fixed or variable rates. However, when making a decision about new loans and borrowings, the Group management gives priority to loans and borrowings with fixed rates, and as a result, the Group is exposed to interest rate risk to a limited extent.

As a rule, loan agreements entered into by the Group do not contain any charges for the early repayment of loans on the borrower's initiative which facilitates additional flexibility for the Group in relation to optimizing interest rates in the current economic environment.

Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss for the period. Therefore, a change in interest rates at the reporting date would not affect profit or loss.

d) Fair values and carrying amounts

The Group Management believes that the fair value of other financial assets and financial liabilities is approximately equal to their carrying amount.

There were no transfers between the fair value hierarchy levels during 2017.

e) Capital management

The main goal of capital management for the Group is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business.

The Group monitors the capital structure (debt and own) including the debt-to-capital ratio determined in accordance with the Russian Accounting Principles. In accordance with the credit policy, the Group companies must maintain the debt-to-capital ratio less than 1.

The Company and its subsidiaries must comply with the capital requirements under which net assets in accordance with the Russian Accounting Principles must exceed its share capital.

As at 31 December 2017 and 2016, the Group complied with the requirements.

28 Operating leases

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

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Lease agreements were entered into in prior periods and consist of land plots on which power lines, equipment for electricity transmission and other assets are located. The land leases typically run for an initial period of 1 to 49 years with an option to renew the lease after that date. The Group is not entitled to purchase the leased asset upon expiration of the operating lease arrangement. Lease payments are reviewed regularly to reflect market rentals.

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

Non-cancellable operating lease rentals are payable as follows:

	<u>31 December 2017</u>	<u>31 December 2016</u>
Less than 1 year	40,480	83,700
Between 1 and 5 years	132,755	188,496
More than 5 years	1,109,210	1,561,524
	<u>1,282,445</u>	<u>1,833,720</u>

Operating lease expenses for the year ended 31 December 2017 included in the operating expenses amount to RUB 243,658 thousand (for the year ended 31 December 2016: RUB 225,781 thousand).

29 Capital commitments

As at 31 December 2017, the Group has outstanding commitments under contracts for the purchase and construction of property, plant and equipment items for RUB 6,856,338 thousand VAT inclusive (as at 31 December 2016: RUB 2,092,294 thousand VAT inclusive).

30 Contingencies

Insurance

The Group has unified requirements in respect of the volume of insurance coverage, reliability of insurance companies and about procedures of insurance protection organization. The Group maintains insurance of assets, civil liability and other insurance risks. The main business areas of the Group have insurance coverage including coverage in case of damage or loss of assets. However, there are risks of negative impact on the operations and the financial position of the Group in the case of damage caused to third parties, and also as a result of damage or loss of assets, insurance protection of which is non-existent or not fully implemented.

Taxation contingencies

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

Management of the Group believes that it has adequately provided for tax assets and liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and have an effect on these consolidated statements if the authorities were successful in enforcing their interpretations.

New transfer pricing regulations have become effective since 01 January 2012 which are converged with the OECD principles however adding uncertainty as to practical application of new pronouncements in certain cases.

The new transfer pricing regulations have no practice yet due to its recent establishment. However, transactions subject to transfer pricing regulations are expected to be thoroughly inspected that could have an effect on these consolidated financial statements.

Litigations

The Group is a party to certain legal proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the management's opinion, there are no actual litigations or other claims which could materially influence the performance or financial position of the Group and which wouldn't be recognized or disclosed in these consolidated financial statements.

Environmental matters

The Group has operated in the electric transmission industry in the Russian Federation for many years. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement posture of Government authorities is continually being reconsidered. Potential liabilities might arise as a result of changes in legislation and regulation or civil litigation. The impact of these potential changes cannot be estimated. In the current enforcement climate under existing legislation, management believes that there are no significant obligations which could have an adverse effect on the Group's financial position, its performance or its cash flows.

31 Related party transactions

a. Control relationship

Related parties include shareholders, affiliates and entities under common ownership and control of the Group and members of the Board of Directors and key management personnel of the Company. The Company's parent as at 31 December 2017 and 31 December 2016 was PJSC ROSSETI. The ultimate controlling party is the state represented by the Federal Agency for Property Management which held the majority of the voting rights of PJSC ROSSETI.

b. Transactions with the parent, its subsidiaries and associates

Transactions with the Parent, its subsidiaries and associates include transactions with PJSC ROSSETI, its subsidiaries and associates:

	Transaction amount for the year ended 31 December		Carrying amount	
	2017	2016	31 December 2017	31 December 2016
Revenue, net other income, finance income				
Parent				
Other revenue	1,185	1,185	–	–
Entities under common control of the parent				
Rent	49	49	5	9
Other revenue	30,793	22,232	205,223	255,909
Reversal of provisions	27,777	–	–	–
Provision for impairment of other receivables	561	–	(168,409)	(167,116)
Services for technological connection	9	–	–	–
	60,374	23,466	36,819	88,802

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	Transaction amount for the year ended 31 December		Carrying amount	
	2017	2016	31 December 2017	31 December 2016
Operating expenses, finance costs				
Parent				
Managing services	76,485	76,485	–	–
Other expenses	21,713	21,713	5,297	5,297
Entities under common control of the parent				
Electricity transmission services	6,438,622	4,904,590	2,254,015	371,979
Services for technological connection to electric grids	1,960	488	54	–
Rent	86	11,306	221	31,063
Other expenses	198,568	97,022	77,372	135,224
	6,737,434	5,111,604	2,336,959	543,563
Capitalized installation and construction activities	1,790	2,889	39,805	122,170
	6,739,224	5,114,493	2,376,764	665,733

	Carrying amount	
	31 December 2017	31 December 2016
Parent		
Advances given	–	–
Advances received	–	–
Entities under common control of the parent		
Advances given	5,890	10,400
Advances received	90	94
	5,980	10,494

	Transaction amount for the year ended 31 December		Carrying amount	
	2017	2016	31 December 2017	31 December 2016
Parent company				
Bonds issued	–	–	7,000,000	7,000,000
Interest on bonds issued	805,226	807,564	77,944	75,814
	805,226	807,564	7,077,944	7,075,814

Dividends attributable to the parent for the year ended 31 December 2017 amounted to RUB 496,441 thousand. Dividends payable to the parent as at 31 December 2017 were RUB 500 thousand.

c. Transactions with key management personnel

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In order to prepare these consolidated financial statements, the key management personnel are members of the Management Board, the Board of Directors.

The Group has no transactions or balances with key management personnel and their close family members except their remuneration in the form of salary and bonuses.

The amounts of key management personnel remuneration disclosed in the table are recognized as an expense related to key management personnel during the reporting period and included in personnel costs.

	<u>Year ended 31 December 2017</u>	<u>Year ended 31 December 2016</u>
Short-term remuneration to personnel	162,648	181,315
Post employment benefits and other long-term benefits	172	71
	<u>162,820</u>	<u>181,386</u>

As at 31 December 2017 the present value of defined benefit plans obligations recognised in the consolidated statement of financial position included obligations in respect of key management personnel in the amount of RUB 1,230 thousand (31 December 2016: RUB 1,140 thousand).

d. Transactions with government-related entities

In the course of its operating activities the Group is engaged in many transactions with government-related entities. The transactions are carried out in accordance with regulated tariffs or based on market prices.

Revenues from government-related entities for the year ended 31 December 2017 constitute 0.65% (2016: 5.79%) of total Group revenues, including 0.52% (2016: 0.80%) of electricity transmission revenues.

Electricity transmission costs (including compensation of technological losses) for government-related entities for the year ended 31 December 2017 constitute 3.78% (2016: 3.25%) of total electricity transmission costs.

Interest accrued on loans and borrowings from state-related banks for the year ended 31 December 2017 amounted to 64.13% (2016: 100%) of total interest accrued.

As at 31 December 2017, the cash and cash equivalents balances placed with state-related banks amounted to RUB 952,544 thousand (as at 31 December 2016: RUB 224,825 thousand.)

Loans and borrowings received from state-related banks are disclosed in Note 22.

32 Events after the reporting date

PJSC Kubanenergo received the following loans during the period from 1 January 2018 to 14 March 2018:

- RUB 15,518,617 thousand from PJSC Sberbank with the purpose to refinance the loans previously received;

- RUB 382,650 thousand from Gazprombank (AO) with the purpose to finance its investing activities;

- RUB 692,162 thousand from PJSC Sberbank with the purpose to finance its investing activities;

- RUB 330,538 thousand from PJSC Sberbank with the purpose to finance its operating activities.