

AK “ALROSA”

IFRS CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2005



AK “ALROSA”

IFRS consolidated financial statements for the year ended 31 December 2005

(in millions of Russian roubles, unless otherwise stated)

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AUDITORS' REPORT

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

1. We have audited the accompanying consolidated balance sheet of Closed Joint Stock Company AK "ALROSA" (the "Company") and its subsidiaries (the "Group") as of 31 December 2005, and the related consolidated statements of income, of cash flows and of changes in equity for the year then ended. These financial statements as set out on pages 4 to 37 are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audit.
2. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
3. In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2005 and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation
31 July 2006



Consolidated Balance Sheet

| | Notes | 31 December 2005 | 31 December 2004 |
|---|-------|------------------|------------------|
| Assets | | | |
| Non-current Assets | | | |
| Restricted cash | 4 | 92 | 252 |
| Investments in associates | 3 | 1,464 | 1,083 |
| Available-for-sale investments | 3 | 449 | 518 |
| Long-term accounts receivable | 7 | 6,010 | 3,973 |
| Property, plant and equipment | 5 | 126,931 | 113,898 |
| Total Non-current Assets | | 134,946 | 119,724 |
| Current Assets | | | |
| Restricted cash | 4 | 286 | 184 |
| Inventories | 6 | 21,153 | 19,537 |
| Trade and other receivables | 7 | 10,817 | 8,755 |
| Prepaid income tax | | 701 | 9 |
| Available-for-sale investments | | 20 | 269 |
| Cash and cash equivalents | 4 | 6,172 | 1,877 |
| Total Current Assets | | 39,149 | 30,631 |
| Total Assets | | 174,095 | 150,355 |
| Equity | | | |
| Share capital | 8 | 11,491 | 11,491 |
| Treasury shares | 8 | (192) | (72) |
| Retained earnings | | 72,432 | 60,652 |
| Equity attributable to shareholders of AK "ALROSA" | | 83,731 | 72,071 |
| Minority Interest | 8 | 4,027 | 2,958 |
| Total Equity | | 87,758 | 75,029 |
| Liabilities | | | |
| Non-current Liabilities | | | |
| Long-term debt | 10 | 33,593 | 31,410 |
| Grant | 9 | 8,664 | 9,363 |
| Provision for restoration liability | 12 | 8,517 | 6,492 |
| Provision for pension obligations | 13 | 1,089 | 1,462 |
| Other provisions | 15 | 229 | 1,095 |
| Deferred tax liabilities | 16 | 4,493 | 3,866 |
| Total Non-current Liabilities | | 56,585 | 53,688 |
| Current Liabilities | | | |
| Short-term loans and current portion of long-term debt | 11 | 17,128 | 10,032 |
| Trade and other payables | 14 | 9,210 | 8,568 |
| Income tax payable | | 337 | 341 |
| Other taxes payable | 16 | 3,012 | 2,641 |
| Dividends payable | | 65 | 56 |
| Total Current Liabilities | | 29,752 | 21,638 |
| Total Liabilities | | 86,337 | 75,326 |
| Total Equity and Liabilities | | 174,095 | 150,355 |

Signed by the following members of management:

Alexander O. Nichiporuk
President, Chairman of the Management Board
31 July 2006

Olga A. Lyashenko
Chief accountant



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(in millions of Russian roubles, unless otherwise stated)

Consolidated Statement of Income

| | Notes | Year ended 31 December 2005 | Year ended 31 December 2004 |
|-------------------------------------|-------|--------------------------------|--------------------------------|
| Sales | 17 | 96,833 | 77,949 |
| Cost of sales | 18 | (50,556) | (36,163) |
| Royalty | 9 | (8,650) | (8,665) |
| Gross profit | | 37,627 | 33,121 |
| General and administrative expenses | 19 | (3,397) | (3,447) |
| Selling and marketing expenses | | (1,214) | (1,164) |
| Other operating income | 20 | 4,048 | 2,852 |
| Other operating expenses | 21 | (11,524) | (9,233) |
| Operating profit | | 25,540 | 22,129 |
| Finance income | 22 | 781 | 2,072 |
| Finance costs | 23 | (6,446) | (4,804) |
| Gain on disposal of subsidiaries | 3 | 1,507 | - |
| Share of net profit of associates | 3 | 749 | 499 |
| Profit before Income Tax | | 22,131 | 19,896 |
| Income tax | 16 | (6,231) | (6,933) |
| Profit for the year | | 15,900 | 12,963 |
| Attributable to: | | | |
| Shareholders of AK “ALROSA” | | 13,790 | 12,118 |
| Minority interest | | 2,110 | 845 |
| Profit for the year | | 15,900 | 12,963 |



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Consolidated Statement of Cash Flows

| | Notes | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|-------|--------------------------------|--------------------------------|
| Net cash Inflow from Operating Activities | 24 | 19,083 | 14,870 |
| Cash Flows from Investing Activities | | | |
| Purchase of property, plant and equipment | | (15,250) | (15,270) |
| Proceeds from sales of fixed assets | | 340 | 292 |
| Purchase of available-for-sale investments | | (51) | (127) |
| Proceeds from sale of available-for-sale investments | | 151 | 34 |
| Advances paid for acquisition of subsidiaries | 7 | (960) | - |
| Acquisition of interest in "Escom-ALROSA Ltd." | 3 | (125) | - |
| Cash acquired on acquisition of subsidiary | 3 | 167 | - |
| Net proceeds from sale of subsidiaries | 3 | 3,251 | - |
| Interest received | | 759 | 289 |
| Dividends received from associates | | 207 | 202 |
| Net Cash Outflow from Investing Activities | | (11,511) | (14,580) |
| Cash Flows from Financing Activities | | | |
| Repayments of loans | | (56,779) | (75,766) |
| Loans received | | 60,150 | 79,605 |
| Interest paid | | (4,585) | (4,161) |
| Receipts from (payment to) restricted cash account | | 58 | (96) |
| Purchase of treasury shares | | (330) | (151) |
| Dividends paid | | (1,791) | (1,191) |
| Net Cash Outflow from Financing Activities | | (3,277) | (1,760) |
| Net Increase (Decrease) in Cash and Cash Equivalents | | 4,295 | (1,470) |
| Cash and cash equivalents at the beginning of the year | | 1,877 | 3,347 |
| Cash and Cash Equivalents at the End of The Year | | 6,172 | 1,877 |

Significant non-cash transactions are discussed in note 28.



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Consolidated Statement of Changes in Equity

| | Number of shares outstanding | Attributable to shareholders of AK “ALROSA” | | | | Minority interest | Total equity |
|---|------------------------------------|--|--------------------|----------------------|---------------|----------------------|-----------------|
| | | Share capital | Treasury shares | Retained Earnings | Total | | |
| Balance at 31 December 2003 | 200,000 | 11,491 | - | 49,813 | 61,304 | 3,035 | 64,339 |
| Profit for the year | | - | - | 12,118 | 12,118 | 845 | 12,963 |
| Dividends (note 8) | | - | - | (1,200) | (1,200) | - | (1,200) |
| Net treasury shares transactions (note 8) | (1,261) | - | (72) | (79) | (151) | - | (151) |
| Changes in minority interest (note 8) | | - | - | - | - | (922) | (922) |
| Balance at 31 December 2004 | 198,739 | 11,491 | (72) | 60,652 | 72,071 | 2,958 | 75,029 |
| Profit for the year | | - | - | 13,790 | 13,790 | 2,110 | 15,900 |
| Dividends (note 8) | | - | - | (1,800) | (1,800) | - | (1,800) |
| Net treasury shares transactions (note 8) | (2,087) | - | (120) | (210) | (330) | - | (330) |
| Changes in minority interest (note 8) | | - | - | - | - | (1,041) | (1,041) |
| Balance at 31 December 2005 | 196,652 | 11,491 | (192) | 72,432 | 83,731 | 4,027 | 87,758 |



AK “ALROSA”

Notes to the IFRS consolidated financial statements for the year ended 31 December 2005

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1. ACTIVITIES

The core activities of Closed Joint Stock Company AK “ALROSA” (“the Company”) and its subsidiaries (“the Group”) are the exploration and extraction of diamond reserves and the marketing and distribution of raw and cut diamonds. The Company was registered on 13 August 1992 as a closed joint stock company in the Republic of Sakha (Yakutia), which is located within the Russian Federation. The Group operates mining facilities in Mirny, Udachny, Aikhal, Nyurba and Anabar (located in Eastern Siberia). The Company is subject to special legislation issued by the Russian Federation and the Republic of Sakha (Yakutia), which significantly influences the Company’s core operating activities. This legislation includes, but is not limited to, requirements to obtain quotas for export of diamonds from the Government of the Russian Federation (see note 17). The licenses for the Group’s major diamond deposits expire between 2015 and 2022. Management believes the Group will be able to extend the licenses’ terms after they expire.

As at 31 December 2005 the Company’s principal shareholders are the Russian Federation (37 percent of shares) and the Republic of Sakha (Yakutia) (32 percent of shares). As at 31 December 2005, 2 percent of the Company’s shares are accounted for as treasury shares as they are held by the Group controlled entities (see note 8). The remaining shares of the Company are held by administrations of districts of the Republic of Sakha (Yakutia) (8 percent of shares) and individuals (21 percent of shares).

2. ACCOUNTING POLICIES

(a) Basis of presentation

The bulk of the Group’s activities are undertaken by the companies incorporated in Russia; these companies maintain their statutory accounting records and prepare statutory financial reports in accordance with the Regulations on Accounting and Reporting of the Russian Federation (“RAR”) and their functional currency is the Russian rouble (“RR”). Group companies incorporated in other countries maintain their statutory accounting records in accordance with relevant legislation and in an appropriate functional currency. The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of available-for-sale investments and financial assets held-for-trading. The consolidated financial statements are based on the statutory accounting records, with adjustments and reclassifications for the purpose of fair presentation in accordance with International Financial Reporting Standards (“IFRS”).

The Russian Federation has previously experienced relatively high levels of inflation and was considered to be hyperinflationary as defined by IAS 29 “Financial Reporting in Hyperinflationary Economies” (“IAS 29”). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicate that hyperinflation has ceased, effective from 1 January 2003 the Group no longer applies the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current at 31 December 2002 are treated as the basis for the carrying amounts in these financial statements.

The official US dollar to RR exchange rates as determined by the Central Bank of the Russian Federation were 28.78 and 27.75 as of 31 December 2005 and 31 December 2004, respectively.

The balance due in respect of the Grant (see note 2 (d)) was previously disclosed as a separate category in the balance sheet. It is now reclassified to non-current liabilities. Management believes that this presentation gives a fairer presentation of the Group’s non-current liabilities.

(b) Recent accounting pronouncements

During the period December 2003 to June 2006, the International Accounting Standards Board (“IASB”) revised 17 of its standards and issued 7 new standards. In addition, during the same period, the International Financial Reporting Interpretations Committee (“IFRIC”) issued nine new interpretations, one of which was subsequently withdrawn. These standards and interpretations are effective for accounting periods commencing on or after 1 January 2005, except for IFRS 6 “Exploration and Evaluation of Mineral Resources” (“IFRS 6”) and IFRS 7 “Financial instruments: disclosures” (“IFRS 7”), which are effective for periods commencing on or after 1 January 2006 and 1 January 2007 respectively, but may be adopted early.



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The revisions to IAS 1, Presentation of Financial Statements, clarify certain presentation requirements. Most significantly, the revised standard requires that minority interest be presented within equity. The Company has retrospectively reflected the revised presentation standard for equity in the consolidated financial statements.

IAS 24, Related Party Disclosures, as revised, has affected the identification of related parties and some other related-party disclosures. Under IAS 24 (revised) the Group is no longer exempt from disclosing transactions with other entities under Governmental control.

Other revised and amended standards effective on 1 January 2005 are as follows: IAS 2, Inventories; IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors; IAS 10, Events after the Balance Sheet Date; IAS 16, Property, Plant and Equipment; IAS 17, Leases; IAS 21, The Effects of Changes in Foreign Exchange Rates; IAS 27, Consolidated and Separate Financial Statements; IAS 28, Investments in Associates; IAS 31, Investments in Joint Ventures; IAS 32, Financial Instruments: Disclosure and Presentation; IAS 33, Earnings per Share; IAS 36, Impairment of Assets; IAS 38, Intangible Assets; IAS 39, Financial Instruments: Recognition and Measurement; IAS 40, Investment Properties; IFRS 2, Share-based payments; IFRS 3, Business Combinations; IFRS 4, Insurance contracts and IFRS 5, Non-current Assets Held for Sale and Discontinued Operations. The adoption of these revised and amended standards has not had a material effect on the Group's financial position, statements of income or of cash flows.

In addition to the new standards summarised above, interpretations early adopted by the Group on 1 January 2005 are as follows: IFRIC 4, Determining whether an Arrangement contains a Lease; IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds. The adoption of these interpretations did not have a material impact on the Group's financial position, statements of income or of cash flows.

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

- IFRS 6, Exploration and Evaluation of Mineral Resources, which is effective for annual periods beginning on or after 1 January 2006. This standard provides guidance for accounting of costs incurred in the exploration for and evaluation of mineral resources.
- IFRS 7, Financial instruments: Disclosures, which is effective for annual periods beginning on or after 1 January 2007. The standard will require increased disclosure in respect of the Group's financial instruments.
- Amendment to IAS 1, Presentation of Financial Statements—Capital Disclosures, which is effective for annual periods beginning on or after 1 January 2007. The Standard will require increased disclosure in respect of the Group's capital.
- The Group has also not early adopted amendments to IAS 19 (Actuarial Gains and Losses, Group Plans and Disclosures), IAS 21 (Net Investment in a Foreign Operation), IAS 39 (Cash Flow Hedge Accounting of Forecast Intragroup Transactions; The Fair Value Option; Financial Guarantee Contracts), the new IFRIC interpretations 6 to 9 and the corrections to IFRS 6 and to IFRS 1.

(c) Principles of consolidation

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

A subsidiary is an entity in which the Group has control through holding of more than half of the voting rights or otherwise has the power to exercise control over the operations. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases.

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

Any excess of the cost of acquisition over the fair value of the net assets of the acquiree at each exchange transaction represents goodwill and is capitalised. Any excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost ("negative goodwill") is recognised immediately in profit or loss.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any minority interest.



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

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

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

The Group’s share of the post-acquisition profits or losses of associates is recorded in the consolidated income statement, and its share of post-acquisition movements in reserves is recognised in reserves. When the Group’s share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

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

(d) Grant

Production assets received from the Republic of Sakha (Yakutia) on 19 January 1993 under the terms of a mineral lease agreement (the “Lease Agreement”) to “transfer of rights to use and exploit land, diamond deposits, main production and non-production facilities”, are recorded in accordance with IAS 20, “Accounting for Government Grants and Disclosure of Government Assistance”, at historical cost adjusted for the effects of inflation, with a corresponding credit reflected as a Grant in the Group’s balance sheet. The Grant is amortised in line with the reduction in the carrying value of the underlying assets, with the amortised portion recorded as an increase in other operating income (see note 9).

Social assets received under the aforementioned Lease Agreement have not been included in the accompanying consolidated financial statements, since the majority of these assets have been or will be transferred free of charge to local administrations.

(e) Property, plant and equipment

Property, plant and equipment comprises costs incurred in developing areas of interest as well as the costs related to the construction and acquisition of production assets. Property, plant and equipment are carried at historic cost of acquisition or construction after deduction of accumulated depreciation and accumulated impairment. Expenditure related to geophysical analysis is expensed until it is determined to be probable that economically recoverable reserves exist.

Major renewals and improvements are capitalised. Maintenance, repairs and minor renewals are expensed as incurred. Minor renewals include all expenditures that do not result in a technical enhancement of the asset beyond its original capacity. Gains and losses arising from the disposal of property, plant and equipment are included in the consolidated statement of income as incurred.

At each reporting date, management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset’s fair value less costs to sell and its value in use, the carrying amount is reduced to the recoverable amount and the difference is recognised as an expense (impairment loss) in the statement of income. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset’s recoverable amount.



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Depreciation and amortisation

Property, plant and equipment are depreciated upon commencement of commercial mining activities at a specific area of interest.

Depreciation and amortisation of buildings, land and improvements related to extraction of minerals is calculated on a units of production basis for each area of interest. Depreciation of assets not directly associated with extraction of minerals is calculated on a straight-line basis over their estimated useful life.

Summary of useful lives and alternative basis for depreciation:

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

Local infrastructure assets

Local infrastructure assets constructed or purchased by the Group subsequent to 1 January 1993 (the date of privatisation) are included in the financial statements at historical cost adjusted for the effects of inflation and depreciated during their useful lives as set out above. These assets are integral part of the Group's production activities.

(f) Provisions

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

Provisions are reassessed at each reporting period, and are included in the consolidated financial statements at their expected net present values using discount rates appropriate to the Group in the economic environment in the Russian Federation at each balance sheet date.

The provision for restoration liability is determined based on the terms of the Lease Agreement (see note 9). Under this agreement, in the year 2017 the Company is obliged to transfer property, plant and equipment subject to the Lease Agreement to the Republic of Sakha (Yakutia) or settle its liability by means of a cash payment. The initial provision for restoration liability together with any changes in estimation of the ultimate restoration liability is recorded on the balance sheet, with a corresponding amount recorded as part of property, plant and equipment in accordance with IAS 16, “Property, Plant and Equipment”. This amount is amortised over the term of the Lease Agreement.

Changes in the provision for restoration liability resulting from the passage of time are reflected in the consolidated statement of income each period under finance costs. Other changes in the provision, relating to a change in the discount rate applied, in the expected pattern of settlement of the obligation or in the estimated amount of the obligation, are treated as a change in accounting estimate in the period of the change. The effects of such changes are added to, or deducted from, the cost of the related asset.

(g) Inventories

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

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



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(h) Investments

The Group classifies its investments into the following categories: trading, held-to-maturity or available-for-sale. Investments that are acquired principally for the purpose of generating a profit from short-term fluctuations in price are classified as trading investments and included in current assets. Investments with a fixed maturity that the management has the intent and ability to hold to maturity are classified as held-to-maturity and are included in non-current assets. During the years ended 31 December 2005 and 2004, the Group did not hold any investments classified as trading or held-to-maturity. Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; these are included in non-current assets unless management has expressed the intention of holding the investment for less than 12 months from the balance sheet date or unless they will need to be sold to raise operating capital, in which case they are included in current assets. Management determines the appropriate classification of its investments at the time of the purchase and reviews such designation on a regular basis.

Purchases and sales of available-for-sale investments are initially measured at fair value and recognised on the settlement date, which is the date that the investment is delivered to or by the Group. Cost of purchase includes transaction costs. Available-for-sale investments are subsequently carried at fair value. Unrealised gains and losses arising from changes in the fair value of these investments are included in the fair value reserve in equity in the period in which they arise. Realised gains and losses from the disposal of available-for-sale investments are included in the consolidated statement of income in the period in which they arise.

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

Sale and repurchase agreements

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

(i) Components of cash and cash equivalents

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

(j) Deferred income taxes

Deferred tax assets and liabilities are calculated in respect of temporary differences using the balance sheet liability method. Deferred income taxes are provided for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deferred tax asset will be realised or if it can be offset against existing deferred tax liabilities. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

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



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(k) Foreign currencies

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

(l) Revenue recognition

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

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

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

Dividend income is recognised when the shareholder's right to receive payment is established.

(m) Measurement of trade and other receivables

Trade and other receivables are initially recognised at the fair value of the consideration given, which is normally the original invoice amount including value added tax less any provision made for impairment of these receivables. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected future cash flows, discounted at the market rate of interest for similar borrowers at the inception date.

(n) Value added tax

Value added taxes related to sales of goods and services are payable to tax authorities upon collection of receivables from customers. Input VAT is generally reclaimable against sales VAT upon payment for purchases. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases, which have not been settled at the balance sheet date (VAT deferred), is recognised in the balance sheet on a gross basis and disclosed separately as an asset and liability. Where provision has been made for the impairment of receivables, an impairment loss is recorded for the gross amount of the debtor, including VAT; the related VAT deferred liability is maintained until the debtor is written off for tax purposes.

(o) Borrowings

Borrowings are recognised initially at cost, which is the fair value of the proceeds received (which is determined using the prevailing market rate of interest for a similar instrument, if significantly different from the transaction price), net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective yield method; any difference between fair value of the proceeds (net of transaction costs) and the redemption amount is recognised as interest expense over the period of the borrowings. Borrowing costs are expensed as incurred.

(p) Pension and other post-retirement benefits

In the normal course of business the Group contributes to the Russian Federation State pension plan on behalf of its employees. Mandatory contributions to the State pension plan, which is a defined contribution plan, are expensed when incurred and are included within wages, salaries and other staff costs in cost of sales.

The Group operates a defined benefit pension plan. Pension costs are recognised using the projected unit credit method. The cost of providing pensions is charged to the relevant category in the consolidated statement of income so as to spread the regular cost over the service lives of employees. The pension obligation is measured at the present value of the estimated future cash outflows using the interest rates on governmental securities, which have the terms to maturity approximating the terms of the related liability. Actuarial gains and losses are recognised over the average remaining service life of employees.



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Pension Fund “Almaznaya Osen”, in which the Group holds a 99 percent voting interest, administers the Group’s defined benefit plan. The Group contributes funds to the Pension Fund “Almaznaya Osen”, which invests them in governmental securities and other financial instruments. These investments, which represent the majority of assets of Pension Fund “Almaznaya Osen”, are considered the pension fund plan assets, as these assets are available to be used only to pay or fund employee benefits, are not available to the Group’s own creditors (even in bankruptcy), and cannot be returned to the Group, unless either the remaining assets of the Pension Fund are sufficient to meet all the related employee benefit obligations of the pension plan, or the assets are returned to the Group to reimburse it for employee benefits already paid. The defined benefit liability is recognised net of the fair value of plan assets at the balance sheet date.

(q) Social costs

Social costs relating to the maintenance of housing are determined in accordance with agreements with the local authorities and expensed or capitalised as appropriate.

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

(r) Non-cash transactions

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

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

(s) Equity

Share capital

Share capital consists of ordinary shares, which are classified as equity.

Treasury shares

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

Dividends

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

(t) Segment reporting

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



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

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

Impairment provision for property, plant and equipment. Management has used various assumptions in the calculation of the recoverable amount of property, plant and equipment. Variations in these assumptions may give rise to a significantly different amount for any impairment provision.

Impairment provision for receivables. Management has determined the allowance for doubtful debtors based on specific customer identification, customer payment trends and subsequent receipts and settlements. The management of the Group believes that Group entities will be able to realise the net receivable amount through direct collections and other non-cash settlements, and that, therefore, the recorded value approximates their fair value.

Impairment provision for investments. Management has determined the fair value of investments, using the analysis of expected future cash flows.

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

Provisions. The Group’s estimates for provisions for liabilities and charges are based on currently available facts and the Group’s estimates of the ultimate outcome or resolution of the liability in the future. Actual results may differ from the estimates, and the Group’s estimates can be revised in the future, either negatively or positively, depending upon the outcome or expectations based on the facts surrounding each exposure.

Pension benefits. The present value of the pension obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost (income) for pensions include the discount rate. Any changes in these assumptions will impact the carrying amount of pension obligations. The Group determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the pension obligations. In determining the appropriate discount rate, the Group considers the interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability. Other key assumptions for pension obligations are based in part on current market conditions (see note 13).

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***3. GROUP STRUCTURE AND INVESTMENTS**

The Company’s significant consolidated subsidiaries are as follows:

| Name | Country of Incorporation | Percentage of ownership interest held | |
|----------------------------------|--------------------------|---------------------------------------|------------------|
| | | 31 December 2005 | 31 December 2004 |
| “ALROSA Finance” S.A. | Luxembourg | 100 | 100 |
| “Arcos Belgium” N.V. | Belgium | 100 | 100 |
| “Sunland Trading” S.A. | (1) Switzerland | 100 | - |
| “New Technologies Holdings Ltd.” | (2) BVI | 100 | - |
| ZAO “Irelyakhneft” | Russia | 100 | 100 |
| OOO “Viluygesstroy” | Russia | 100 | 100 |
| OOO “GRK Aldanzoloto” | (3) Russia | - | 99 |
| OAD “Severalmaz” | Russia | 92 | 92 |
| OOO “MAK-Bank” | Russia | 88 | 88 |
| OAD “ALROSA-Nyurba” | Russia | 87 | 86 |
| OAD “Viluyskaya GES-3” | Russia | 79 | 76 |
| OAD “ALROSA-Gas” | Russia | 53 | 53 |
| OAD “Almazy Anabara” | Russia | 51 | 51 |
| OAD “Investment Group ALROSA” | (4) Russia | 50 | 50 |

As at 31 December 2005 and 2004 the percentage of ownership interest of the Group in subsidiaries is equal to the percentage of voting interest.

(1) In September 2005 the Group established “Sunland Trading” S.A., which is registered in Geneva, Switzerland, for the purpose of marketing and sale of diamonds produced in Angola.

(2) In December 2005 the Group purchased 100 percent of “New Technologies Holdings Ltd.” (“NTHL”), a company registered in the British Virgin Islands. “NTHL” holds a 90 percent interest in ZAO “Geotransgaz”, a Russian development stage company that holds a license for geological survey, exploration and production of gas and gas condensate from a deposit located in the Western Siberia. Subsequently the Group sold “NTHL” to an investment bank and simultaneously concluded a forward repurchase agreement with the bank providing for the repurchase by the Group of 100 percent of “NTHL” in December 2007 for an aggregate purchase price of US\$’mln 140 plus periodic payments in respect of this amount at a rate of six-months LIBOR plus 2.35 percent per annum payable semi-annually. The assets and liabilities of “NTHL” as at 31 December 2005 were consolidated in the Group’s consolidated financial statements. The corresponding liability totalling RR’mln 4,030 (US\$’mln 140), which represents a deferred purchase consideration payable to the investment bank, was recognised within long-term debt as at 31 December 2005 in the Group’s consolidated financial statements.

Details of the assets and liabilities acquired are as follows:

| | Carrying amount immediately before acquisition | Attributed fair value |
|--|--|-----------------------|
| Property, plant and equipment | 3,913 | 4,235 |
| Trade and other receivables | 626 | 626 |
| Cash | 167 | 167 |
| Deferred tax liability | (622) | (684) |
| Trade and other payables | (64) | (64) |
| Minority interest in net assets of ZAO “Geotransgaz” | (250) | (250) |
| Fair value of acquired net assets of “NTHL” | | 4,030 |
| Total purchase consideration | | 4,030 |

As “NTHL” was acquired at the end of the reporting year, the acquired company did not contribute any significant revenue or profit (loss) to the Group for the period from the date of acquisition to 31 December 2005. If the acquisition had occurred on 1 January 2005, the acquired company would have contributed revenue of RR’mln 223 and a loss of RR’mln 147 to the Group for the year ended 31 December 2005.


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Notes to the IFRS consolidated financial statements for the year ended 31 December 2005
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(3) In September 2005 OAO “Investment Group ALROSA”, a subsidiary of the Group, sold its gold mining operations (99 percent interest in OOO “GRK Aldanzoloto”, 100 percent interest in OAO “Yakutskaya Gornaya Company” and 50 percent interest in OAO “Yuzhno-Verkhoyanskaya Gornaya Company”) for an estimated consideration of US\$’mln 255. An initial part of consideration totalling RR’mln 3,259 (US\$’mln 115) was satisfied by cash. The remaining part of the contracted consideration is US\$’mln 140 and the final amount payable is contingent upon certain items still subject to negotiations. The negotiations with the buyer relating to the contingent element of sales proceeds are not completed as of the date of issuance of these consolidated financial statements. For the purposes of these consolidated financial statements, management is not able to estimate the final value of the uncertainties. Consequently, no value has been recorded in these consolidated financial statements relating to the remaining contracted contingent consideration of up to US\$’mln 140.

The net assets of gold mining operations at the date of disposal and at 31 December 2004 were as follows:

| | Disposal date | 31 December 2004 |
|---|----------------------|-------------------------|
| Property, plant and equipment | 1,270 | 1,224 |
| Trade and other receivables | 1,020 | 584 |
| Inventory | 163 | 155 |
| Cash | 8 | 1 |
| Trade and other payables | (412) | (192) |
| Borrowings and other liabilities | (297) | (611) |
| Net assets | 1,752 | 1,161 |
| Gain on disposal | 1,507 | |
| Total recognised consideration | 3,259 | |
| Net cash flow arising on disposal: | | |
| Cash consideration received | 3,259 | |
| Cash and cash equivalents disposed of | (8) | |
| | 3,251 | |

(4) The Group owned a 50.01 percent voting interest in OAO “Investment Group ALROSA” at 31 December 2005 and 31 December 2004.

Associates

| Name | Country of incorporation | Percentage of ownership interest held as at | | Carrying value of investment as at | | Group’s share of net profit (loss) for the year ended | |
|---|--------------------------|---|------|------------------------------------|-------|---|------|
| | | 31 December 2005 | 2004 | 31 December 2005 | 2004 | 2005 | 2004 |
| “Catoca Mining Company Ltd.” | (1) Angola | 33 | 33 | 1,205 | 904 | 833 | 515 |
| “Escom-ALROSA Ltd.” | (2) United Kingdom | 44 | 44 | 46 | 1 | (79) | - |
| OAO “Almazny Mir” | Russia | 47 | 47 | 169 | 168 | 1 | 4 |
| OAO “Yuzhno-Verkhoyanskaya Gornaya Company” | (3) Russia | - | 50 | - | - | - | (32) |
| Other | Russia | | | 44 | 10 | (6) | 12 |
| | | | | 1,464 | 1,083 | 749 | 499 |

As at 31 December 2005 and 2004 the percentage of ownership interest of the Group in associates is equal to the percentage of voting interest.

(1) “Catoca Mining Company Ltd.” is a diamond-mining venture located in Angola. In 2005 “Catoca Mining Company Ltd.” declared dividends for the year ended 31 December 2004; the Group’s share of these dividends amounted to RR’mln 532.

(2) “Escom-ALROSA Ltd.” was incorporated in 2003 in London, United Kingdom, and its share capital was fully paid in 2005. The contribution of the Group into the share capital of “Escom-ALROSA Ltd.” totalled RR’mln 125 (US\$’mln 4). “Escom-ALROSA Ltd.” owns a 45 percent voting interest in “Camatchia-Camagico”, a development stage diamond-mining venture located in Angola, which is in the pilot stage of mining of the Luo diamond deposit. In October 2005 the Group issued a loan totalling RR’mln 2,326 (US\$’mln 81) to “Escom-ALROSA Ltd.”; the repayment period of this loan is June 2006 – June 2014 and it bears interest at LIBOR plus 2.5 percent per annum. The purpose of the loan is to finance the construction of the main processing plant at the Luo deposit.

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

(3) OAO “Yuzhno-Verkhoyanskaya Gornaya Company” (OAO “YVGC”) is a development stage company, engaged in the extraction, refining and sale of gold in the Republic of Sakha (Yakutia). The Group’s share of the losses of OAO “YVGC” was accounted for under the equity method and recorded in the consolidated statement of income for the year ended 31 December 2004 until the investment in OAO “YVGC” was written down to a nil value. The Group’s interest in OAO “YVGC” was disposed along with the disposal of certain other gold mining operations in September 2005 (see above).

Summarised financial information on the Group’s associates is as follows:

| | Assets as at 31 December | | Liabilities as at 31 December | | Revenues for the year ended 31 December | | Profit (loss) for the year ended 31 December | |
|--|-----------------------------|-------|----------------------------------|-------|---|-------|--|-------|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| “Catoka Mining Company Ltd.” | 8,104 | 5,276 | 4,431 | 2,520 | 8,676 | 6,544 | 2,540 | 1,570 |
| “Escom-ALROSA Ltd.” | 5,435 | - | 5,330 | - | - | - | (180) | - |
| OAO “Almazny Mir” | 841 | 525 | 486 | 169 | 858 | 735 | 3 | 8 |
| OAO “Yuzhno-Verkhoyanskaya Gornaya Company” | - | 932 | - | 1,380 | 10 | 23 | (67) | (229) |
| Other | 259 | 210 | 282 | 232 | 105 | 582 | (18) | 28 |
| | 14,639 | 6,943 | 10,529 | 4,301 | 9,649 | 7,884 | 2,278 | 1,377 |

Revenues and loss for the year ended 31 December 2005 for OAO “Yuzhno-Verkhoyanskaya Gornaya Company” are disclosed for the period up to the date of disposal.

Non-current available-for-sale investments

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--------------------------------|--------------------------------|
| Available-for-sale investments at the beginning of the year | 518 | 1,187 |
| Additions | 53 | 128 |
| Disposals | (122) | (85) |
| Transfer to current available-for-sale investments | - | (248) |
| Change in provision for impairment of available-for-sale investments (see note 22) | - | (464) |
| Available-for-sale investments at the end of the year | 449 | 518 |

4. CASH AND CASH EQUIVALENTS AND RESTRICTED CASH**Cash and cash equivalents**

| | 31 December 2005 | 31 December 2004 |
|------------------|------------------|------------------|
| Current accounts | 3,329 | 1,489 |
| Special accounts | 2,768 | - |
| Deposit accounts | 75 | 388 |
| | 6,172 | 1,877 |

During the year ended 31 December 2005 the Group reserved on special accounts in banks cash totalling RR’mn 2,768. The Group intended to use this cash for the re-purchase of its own Eurobonds in the market.

At 31 December 2005 the weighted average interest rate on the cash balances of the Group is 1 percent (31 December 2004: 1 percent).

Restricted cash

Included within long-term restricted cash are balances of RR’mn 92 and RR’mn 78 as at 31 December 2005 and 2004, respectively, which represent mandatory reserve deposits held with the Central Bank of the Russian Federation by OOO “MAK-Bank”, a subsidiary of the Group; these balances are not available for use in the Group’s day to day operations.



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Notes to the IFRS consolidated financial statements for the year ended 31 December 2005

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The remaining RR'mln 174 as at 31 December 2004 was cash held in J.P. Morgan Chase Bank; the Group is required to maintain a balance equal to the amount of its next scheduled principal and interest payment in accordance with loan agreements with this bank. As these loan agreements mature in 2006, the respective balance held at deposit accounts with J.P. Morgan Chase Bank as at 31 December 2005 totalling RR'mln 173 was recognised as short-term restricted cash.

At 31 December 2005 and 2004 short-term restricted cash balances of RR'mln 113 and RR'mln 184, respectively, were held with authorised banks. According to Russian exchange regulation, these authorised banks reserved two percent (31 December 2004 – three percent) of loans proceeds received by the Group from foreign legal entities. These balances are not available for use in the Group's day-to-day operations for 365 days from the date of transfer of cash to the specified account.

At 31 December 2005 the weighted average interest rate on the restricted cash balances is approximately nil percent (31 December 2004: approximately nil percent).

5. PROPERTY, PLANT AND EQUIPMENT

| | Buildings | Land and Improvements | Plant and Equipment | Transport | Production licenses | Assets under Construction | Other | TOTAL |
|---|-----------------|-----------------------|---------------------|----------------|---------------------|---------------------------|--------------|-----------------|
| Cost at 31 December 2003 | 44,927 | 35,594 | 28,362 | 15,435 | 2,501 | 27,266 | 609 | 154,694 |
| Additions through acquisition of subsidiaries | 679 | 7 | 342 | 17 | - | 69 | 26 | 1,140 |
| Additions | 321 | 314 | 1,837 | 794 | 301 | 12,905 | 586 | 17,058 |
| Transfers | 2,644 | 3,479 | 2,170 | 41 | - | (8,605) | 271 | - |
| Disposals | (1,251) | (307) | (1,247) | (585) | - | (703) | (275) | (4,368) |
| Change in estimate of provision for restoration liability (see note 12) | 479 | 174 | 33 | 5 | - | - | 1 | 692 |
| Impairment of property, plant and equipment | (185) | (93) | - | - | - | (42) | - | (320) |
| Cost at 31 December 2004 | 47,614 | 39,168 | 31,497 | 15,707 | 2,802 | 30,890 | 1,218 | 168,896 |
| Additions through acquisition of subsidiary (see note 3) | 24 | 88 | 9 | 2 | 3,534 | 576 | 2 | 4,235 |
| Additions | 339 | 937 | 2,379 | 911 | - | 12,927 | 555 | 18,048 |
| Transfers | 3,883 | 7,085 | 1,918 | 111 | - | (13,093) | 96 | - |
| Disposal of gold mining operations (see note 3) | (698) | - | (570) | (4) | - | (167) | (34) | (1,473) |
| Other disposals | (494) | (3,210) | (1,322) | (1,443) | - | (357) | (524) | (7,350) |
| Change in estimate of provision for restoration liability (see note 12) | 1,134 | 412 | 77 | 12 | - | - | 1 | 1,636 |
| Impairment of property, plant and equipment | - | - | - | - | - | (165) | - | (165) |
| Cost at 31 December 2005 | 51,802 | 44,480 | 33,988 | 15,296 | 6,336 | 30,611 | 1,314 | 183,827 |
| Accumulated depreciation at 31 December 2003 | (13,185) | (14,146) | (13,808) | (8,830) | (60) | - | (222) | (50,251) |
| Charge for the year | (1,332) | (1,668) | (2,934) | (1,379) | (10) | - | (166) | (7,489) |
| Disposals | 853 | 222 | 1,071 | 517 | - | - | 79 | 2,742 |
| Accumulated depreciation at 31 December 2004 | (13,664) | (15,592) | (15,671) | (9,692) | (70) | - | (309) | (54,998) |
| Charge for the year | (1,509) | (1,731) | (3,464) | (1,309) | (16) | - | (137) | (8,166) |
| Disposal of gold mining operations (see note 3) | 88 | - | 109 | - | - | - | 6 | 203 |
| Other disposals | 371 | 3,076 | 1,194 | 1,364 | - | - | 60 | 6,065 |
| Accumulated depreciation at 31 December 2005 | (14,714) | (14,247) | (17,832) | (9,637) | (86) | - | (380) | (56,896) |
| Net book value at 31 December 2004 | 33,950 | 23,576 | 15,826 | 6,015 | 2,732 | 30,890 | 909 | 113,898 |
| Net book value at 31 December 2005 | 37,088 | 30,233 | 16,156 | 5,659 | 6,250 | 30,611 | 934 | 126,931 |

Refer to note 9 for property, plant and equipment included above which is subject to the Lease Agreement with the Republic of Sakha (Yakutia).


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Notes to the IFRS consolidated financial statements for the year ended 31 December 2005
(in millions of Russian roubles, unless otherwise stated)
6. INVENTORIES

| | 31 December 2005 | 31 December 2004 |
|-----------------------------------|-------------------------|-------------------------|
| Diamonds | 9,752 | 9,187 |
| Ores and concentrates | 2,419 | 2,146 |
| Mining and construction materials | 6,570 | 6,998 |
| Diamonds for resale | 1,695 | - |
| Consumable supplies | 717 | 1,206 |
| | 21,153 | 19,537 |

Diamonds for resale represent the diamonds purchased by the Group from “Sunland Mining Company Lda”, a third party Angolan diamond exporter, for the purpose of the subsequent resale on the open market.

7. TRADE AND OTHER RECEIVABLES

| Long-term accounts receivable | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| Receivables from associates (see note 27) | 2,271 | 283 |
| Loans issued | 1,526 | 948 |
| Long-term VAT recoverable | 1,385 | 1,967 |
| Notes receivable | 752 | - |
| Long-term advances to suppliers | - | 505 |
| Long-term prepaid royalty | - | 260 |
| Other long-term receivables | 76 | 10 |
| | 6,010 | 3,973 |

| Current accounts receivable | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| Taxes recoverable | 2,924 | 2,160 |
| Loans issued | 2,312 | 1,026 |
| Notes receivable | 1,372 | 2,297 |
| Advances for acquisition of subsidiaries | 960 | - |
| Receivables from associates (see note 27) | 677 | 582 |
| Advances to suppliers | 557 | 708 |
| Prepaid taxes, other than income tax | 497 | 686 |
| Trade receivables for supplied diamonds | 20 | 22 |
| Other receivables | 1,498 | 1,274 |
| | 10,817 | 8,755 |

Taxes recoverable relate to input Value Added Tax (VAT) incurred with respect to purchases. The amount is available for offset against future output VAT following the settlement of outstanding balances payable in relation to the inventories and services purchased.

Advances for acquisition of subsidiaries were paid in respect of the acquisition of controlling interests in OAO “NNGK Sakhaneftegaz”, OAO “Yakutskgeofisika” and ZAO “BRINT-M”. These acquisitions were completed in January – April 2006 (see note 30).

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

| Long-term accounts receivable | 31 December 2005 | Bad debt write-off | Interest on impaired receivables | Bad debt expense (reversal) | 31 December 2004 |
|---|-------------------------|---------------------------|---|------------------------------------|-------------------------|
| Loans issued | 45 | - | - | 45 | - |
| Long-term prepaid royalty | - | - | (6) | (50) | 56 |
| | 45 | - | (6) | (5) | 56 |
| Current accounts receivable | | | | | |
| Receivables from associates (see note 27) | 187 | (35) | - | (61) | 283 |
| Notes receivable | 226 | - | - | (25) | 251 |
| Loans issued | 78 | (41) | (2) | (55) | 176 |
| Prepaid taxes, other than income tax | - | - | - | (29) | 29 |
| Other receivables | 1,711 | (302) | - | 257 | 1,756 |
| | 2,202 | (378) | (2) | 87 | 2,495 |

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

| Long-term accounts receivable | 31 December 2004 | Bad debt write-off | Interest on impaired receivables | Bad debt expense (reversal) | 31 December 2003 |
|---|-------------------------|---------------------------|---|------------------------------------|-------------------------|
| Long-term prepaid royalty | 56 | - | (15) | - | 71 |
| | 56 | - | (15) | - | 71 |
| Current accounts receivable | | | | | |
| Receivables from associates (see note 27) | 283 | - | - | (24) | 307 |
| Notes receivable | 251 | - | - | - | 251 |
| Loans issued | 176 | - | - | 80 | 96 |
| Prepaid taxes, other than income tax | 29 | - | (16) | (1) | 46 |
| Other receivables | 1,756 | - | 4 | 271 | 1,481 |
| | 2,495 | - | (12) | 326 | 2,181 |

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

| Long-term accounts receivable | 31 December 2005 | 31 December 2004 |
|--------------------------------------|-------------------------|-------------------------|
| Receivables from associates | 7% | 12% |
| Loans issued | 16% | 19% |
| Notes receivable | 10% | - |
| Long-term prepaid royalty | - | 10% |

8. EQUITY***Share capital***

Share capital authorised, issued and paid in totals RR'mln 11,491 at 31 December 2005 and 31 December 2004 and consists of 200,000 ordinary shares at RR 57,455 per share.

Distributable profits

The statutory accounting reports of the Company are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the current year net profit. For the years ended 31 December 2005 and 31 December 2004, the statutory profit of the Company as reported in the published statutory reporting forms was RR'mln 15,090 and RR'mln 13,917, respectively. However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation, and accordingly, management believes that at present it would not be appropriate to disclose an amount for the distributable reserves in these financial statements.

Treasury shares

At 31 December 2005 OOO “Management Companyalmaz”, OOO “MAK-Bank” and NPF “Almaznaya osen”, subsidiaries of the Group, held 3,348 ordinary shares of the Company (at 31 December 2004 – 1,261 shares). The Group management controls the voting right of these shares.

Dividends

On 19 June 2004, the Company’s shareholders approved dividends for the year ended 31 December 2003 totalling RR'mln 1,200. Dividends per share amounted to RR 6,000.

On 25 June 2005, the Company’s shareholders approved dividends for the year ended 31 December 2004 totalling RR'mln 1,800. Dividends per share amounted to RR 9,000.

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***Minority interest**

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--|--|--|
| Minority interest at the beginning of the year | 2,958 | 3,035 |
| Minority interest share of net profit of subsidiaries | 2,110 | 845 |
| Distribution of minority interest share in the statutory retained earnings of OAO “ALROSA-Nyurba” to AK “ALROSA” | (1,080) | (822) |
| <u>Business combinations and purchase of minority interest</u> | <u>39</u> | <u>(100)</u> |
| Minority interest at the end of the year | 4,027 | 2,958 |

During the year ended 31 December 2005 and 2004 OAO “ALROSA-Nyurba”, a subsidiary of the Group, distributed part of its statutory retained earnings to the Company as financial assistance without making a share of such distributions available to minority shareholders. These distributions were approved by the minority shareholders of OAO “ALROSA-Nyurba” and their share in the statutory retained earnings distributed to the Company totalling RR’mln 1,080 for the year ended 31 December 2005 (RR’mln 822 for the year ended 31 December 2004) was recognised by the Group within other operating income (see note 20).

As a result of the acquisition by the Group of “New Technologies Holdings Ltd.” in December 2005 (see note 3), minority interest increased by RR’mln 250. As a result of the acquisition of an additional 3 percent in OAO “Viluyskaya GES-3” (see note 27) and an additional 1 percent in OAO “ALROSA-Nyurba”, minority interest decreased by RR’mln 211.

9. GRANT AND ASSETS SUBJECT TO MINERAL LEASE AGREEMENT

On 19 January 1993, the Company entered into a Lease Agreement with the Republic of Sakha (Yakutia) for the “transfer of rights to use and exploit land, diamond deposits, main production and non-production facilities”. This agreement has a term of 25 years and provides the Company with the right to use certain production and non-production assets for exploring, mining and operating diamond deposits. The agreement requires the Company to return the assets in 2017 and reimburse the Government of Republic of Sakha (Yakutia) for depreciation of the assets. The Government in turn is required to reimburse the Company for qualifying repair and maintenance costs. The precise mechanism for determining the value and nature of the assets to be returned to the Republic of Sakha (Yakutia) under the terms of the Lease Agreement is being negotiated between the parties.

Management have estimated the restoration liability based upon their interpretation of the Lease Agreement and, in accordance with IAS 37, “Provisions, Contingent Liabilities and Contingent Assets”, have calculated and recorded the net present value of the restoration liability (see notes 2 (f) and 12).

The agreement stipulates that certain terms of the agreement should be renegotiated every five years. The agreement also stipulates that the Company is subject to royalties and other taxes on the right to use the land and logging areas, disposal and burial of waste and contaminated materials and the use of mineral resources and water for industrial purposes. The main subject of the renegotiations relates to the amount and timing of royalty and other payments.

Royalty payments expensed during the year ended 31 December 2005 totalled RR’mln 8,650 (year ended 31 December 2004: RR’mln 8,665). Ecology fund payments expensed during the year ended 31 December 2005 totalled RR’mln 864 (year ended 31 December 2004: RR’mln 906).

Pursuant to an addendum to the Lease Agreement dated 17 September 2003, the Company and the Republic of Sakha (Yakutia) agreed that the royalty payments, including ecology fund payments and value added tax, due in 2004 are fixed at RR’mln 10,500.

Pursuant to an addendum to the Lease Agreement dated 17 December 2004, the Company and the Republic of Sakha (Yakutia) agreed that the royalty payments, including ecology fund payments and value added tax, due in 2005 are fixed at RR’mln 10,500.

Recoverable value added tax related to royalty and ecology fund payments depends on the percentage of export diamond sales to the total diamond sales of the Company. The amount of such value added tax for the year ended 31 December 2005 was RR’mln 986 (for the year ended 31 December 2004 – RR’mln 929).

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

The carrying values of Company owned and granted assets subject to the Lease Agreement with the Republic of Sakha (Yakutia) and Grant are as follows:

| Assets subject to the agreement with the Republic of Sakha (Yakutia) | 31 December 2005 | 31 December 2004 |
|--|-------------------------|-------------------------|
| Net book value of granted assets received in 1993 | 8,664 | 9,363 |
| Net book value of Company owned assets subsequently transferred to the lease | 5,470 | 5,309 |
| Net book value at the end of the year | 14,134 | 14,672 |

10. LONG-TERM DEBT

| | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| Banks: | | |
| US\$ denominated floating rate | 10,249 | 6,870 |
| US\$ denominated fixed rate | 6,111 | 5,746 |
| RR denominated fixed rate | - | 400 |
| | 16,360 | 13,016 |
| Eurobonds | 25,441 | 19,594 |
| RR denominated non-convertible bonds | - | 3,921 |
| Commercial paper | 284 | 175 |
| Other US\$ denominated fixed rate loans | 462 | 511 |
| Other RR denominated fixed rate loans | 470 | 467 |
| | 43,017 | 37,684 |
| Less: current portion of long-term debt (see note 11) | (9,424) | (6,274) |
| | 33,593 | 31,410 |

Included within US\$ denominated floating rate bank loans are RR'mln 4,030 (US\$m 140) of deferred purchase consideration payable to the investment bank in December 2007 for acquisition of 100 percent in “New Technologies Holdings Ltd.” (see note 3). This amount is secured by shares of “New Technologies Holdings Ltd.” and bears interest at a rate of six-months LIBOR plus 2.35 percent per annum.

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

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

| | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| Banks: | | |
| US\$ denominated floating rate | 7.6% | 6.0% |
| US\$ denominated fixed rate | 9.8% | 9.6% |
| RR denominated fixed rate | - | 14.0% |
| Eurobonds | 8.8% | 8.9% |
| RR denominated non-convertible bonds | - | 13.8% |
| Commercial paper | 53.8% | 51.6% |
| Other US\$ denominated fixed rate loans | 9.0% | 11.0% |
| Other RR denominated fixed rate loans | 11.0% | 10.3% |

**AK "ALROSA"****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

At 31 December 2005 long-term loans had the following maturity profile:

| | Within 1 year | 1 to 2 years | 2 to 3 years | 3 to 4 years | 4 years and thereafter | Total |
|---|--------------------------|-------------------------|-------------------------|-------------------------|-----------------------------------|---------------|
| Banks: | | | | | | |
| US\$ denominated floating rate | 4,878 | 5,371 | - | - | - | 10,249 |
| US\$ denominated fixed rate | 4,418 | 1,324 | - | 21 | 348 | 6,111 |
| Eurobonds | - | - | 11,082 | - | 14,359 | 25,441 |
| Commercial paper | - | 131 | 67 | 32 | 54 | 284 |
| Other US\$ denominated fixed rate loans | - | 209 | 92 | 84 | 77 | 462 |
| Other RR denominated fixed rate loans | 128 | 202 | - | - | 140 | 470 |
| | 9,424 | 7,237 | 11,241 | 137 | 14,978 | 43,017 |

At 31 December 2004 long-term loans had the following maturity profile:

| | Within 1 year | 1 to 2 years | 2 to 3 years | 3 to 4 years | 4 years and thereafter | Total |
|---|--------------------------|-------------------------|-------------------------|-------------------------|-----------------------------------|---------------|
| Banks: | | | | | | |
| US\$ denominated floating rate | 982 | 2,688 | 2,888 | 312 | - | 6,870 |
| US\$ denominated fixed rate | 702 | 4,141 | 638 | - | 265 | 5,746 |
| RR denominated fixed rate | 400 | - | - | - | - | 400 |
| Eurobonds | - | - | - | 11,379 | 8,215 | 19,594 |
| RR denominated non-convertible bonds | 3,921 | - | - | - | - | 3,921 |
| Commercial paper | - | 8 | 75 | 40 | 52 | 175 |
| Other US\$ denominated fixed rate loans | 179 | 78 | 72 | 66 | 116 | 511 |
| Other RR denominated fixed rate loans | 90 | 217 | 20 | - | 140 | 467 |
| | 6,274 | 7,132 | 3,693 | 11,797 | 8,788 | 37,684 |

The Group has not entered into any derivative contracts in respect of its foreign currency obligations or interest rate exposure.

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

| | 31 December 2005 | | 31 December 2004 | |
|---|-------------------------|--------------------|-------------------------|--------------------|
| | Carrying amounts | Fair values | Carrying amounts | Fair values |
| Banks | 16,360 | 16,266 | 13,016 | 13,054 |
| Eurobonds | 25,441 | 28,441 | 19,594 | 20,623 |
| Non-convertible bonds | - | - | 3,921 | 3,972 |
| Commercial paper | 284 | 1,025 | 175 | 841 |
| Other US\$ denominated fixed rate loans | 462 | 463 | 511 | 511 |
| Other RR denominated fixed rate loans | 470 | 502 | 467 | 493 |

The fair value of long-term debt is estimated by discounting the future contractual cash outflows at the market interest rate available to the Group at the balance sheet date.

As at 31 December 2005, long-term debt totalling RR'mln 4,175 (31 December 2004: RR'mln 42) included above was secured with the assets of the Group. As separate loan agreements do not specify individual pledged assets, the carrying amount of pledged assets is not disclosed.

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***Eurobonds**

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--------------------------------------|--|--|
| Balance at the beginning of the year | 19,594 | 14,463 |
| Issuance | 5,699 | 8,491 |
| Amortisation of discount | 57 | 61 |
| Repayment | (771) | (2,315) |
| Exchange loss (gain) | 862 | (1,106) |
| Balance at the end of the year | <u>25,441</u> | <u>19,594</u> |

In May 2003 “ALROSA Finance S.A.”, a wholly owned subsidiary of the Group, issued Eurobonds in the amount of RR’mln 15,280 (nominal value - US\$’mln 500) due for repayment on 6 May 2008 with an interest rate of 8.125 percent per annum. During the year ended 31 December 2004 part of these Eurobonds in the amount of RR’mln 2,315 (nominal value - US\$’mln 83) was repaid early and cancelled. During the year ended 31 December 2005 an additional part of these Eurobonds in the amount of RR’mln 771 (nominal value - US\$’mln 27) was repaid early and cancelled.

In November 2004 “ALROSA Finance S.A.” issued Eurobonds in the amount of RR’mln 8,491 (nominal value - US\$’mln 300) due for repayment on 17 November 2014 with an interest rate of 8.875 percent per annum.

In January 2005 “ALROSA Finance S.A.” issued Eurobonds in the amount of RR’mln 5,699 (nominal value - US\$’mln 200) due for repayment on 17 November 2014 with an interest rate of 8.53 percent per annum.

RR denominated non-convertible bonds

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--------------------------------------|--|--|
| Balance at the beginning of the year | 3,921 | 4,870 |
| Issuance | - | 104 |
| Amortisation of discount | 32 | 39 |
| Repayment | (3,953) | (1,092) |
| Balance at the end of the year | <u>-</u> | <u>3,921</u> |

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

| | 31 December 2005 | 31 December 2004 |
|--|-------------------------|-------------------------|
| Banks: | | |
| US\$ denominated floating rate | - | 277 |
| US\$ denominated fixed rate | 5,537 | 1,380 |
| RR denominated fixed rate | 92 | 217 |
| | <u>5,629</u> | <u>1,874</u> |
| Commercial paper | 427 | 482 |
| Other US\$ denominated fixed rate loans | 173 | 161 |
| Other RR denominated fixed rate loans | 1,475 | 1,241 |
| | <u>7,704</u> | <u>3,758</u> |
| Add: current portion of long-term debt (see note 10) | 9,424 | 6,274 |
| | <u>17,128</u> | <u>10,032</u> |

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

| | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| Banks: | | |
| US\$ denominated floating rate | - | 4.0% |
| US\$ denominated fixed rate | 7.9% | 10.5% |
| RR denominated fixed rate | 16.1% | 13.3% |
| Commercial paper | 13.0% | 18.6% |
| Other US\$ denominated fixed rate loans | 6.7% | 6.0% |
| Other RR denominated fixed rate loans | 2.0% | 3.5% |

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

As at 31 December 2005 there were no short-term loans secured with the assets of the Group. As at 31 December 2004, short-term loans totalling RR'mln 139 included above were secured with the assets of the Group. As separate loan agreements do not specify individual pledged assets, the carrying amount of pledged assets is not disclosed.

Commercial paper

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

European commercial paper

In March 2005 “ALROSA Finance S.A.” established a program for issuing European commercial paper (ECP). The program allows for the issue of short-term fixed rate commercial paper with maturity dates within 364 days. Within the framework of this program “ALROSA Finance S.A.” issued four series of European commercial paper in the total amount of RR'mln 5,729 (nominal value - US\$'mln 200) during the year ended 31 December 2005. By 31 December 2005 all series of European commercial paper were redeemed.

12. PROVISION FOR RESTORATION LIABILITY

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--|--|
| At the beginning of the year | 6,492 | 5,394 |
| Change in estimate of provision for restoration liability | 1,636 | 692 |
| Unwinding of the present value discount | 389 | 406 |
| At the end of the year | 8,517 | 6,492 |

The provision for restoration liability represents the net present value of the estimated future obligation, upon termination of the Lease Agreement, to return certain property, plant and equipment received from the Republic of Sakha (Yakutia) under the terms of the Lease Agreement (see notes 2(f) and 9). The discount rate used to calculate the net present value of the restoration liability at 31 December 2005 was 4.8 percent (31 December 2004: 6.7 percent), which is a pre-tax real rate and is considered appropriate to the Group in the economic environment in the Russian Federation at the balance sheet date.

Under the Lease Agreement the Company is obliged to reimburse to the Republic of Sakha (Yakutia) the amount of accumulated depreciation on property, plant and equipment subject to this agreement (leased property, plant and equipment) and the Republic of Sakha (Yakutia) is obliged to reimburse to the Company the amount of qualified repair and maintenance expense incurred by the Company in relation to the leased property, plant and equipment. The Company and the Republic of Sakha (Yakutia) determined the amount to be reimbursed by the Company on a net basis as the difference between the amount of depreciation on leased assets and the amount of repair and maintenance expense in relation to the leased property, plant and equipment. Reimbursement is effected by means of the transfer of title of certain of the Company's own items of property, plant and equipment to the Republic of Sakha (Yakutia) and these assets are, subsequent to their transfer, treated as leased property, plant and equipment (see note 9).

Prior to 1 January 2003 the Republic of Sakha (Yakutia) was obliged to reimburse to the Company the actual amount of qualified repair and maintenance expense incurred by the Company in relation to the leased property, plant and equipment. Pursuant to an addendum to the Lease Agreement dated 17 September 2003, starting from 1 January 2003 the Republic of Sakha (Yakutia) is obliged to reimburse qualified repair and maintenance expense incurred by the Company, subject to such expense being limited to 30 percent of the depreciation on leased property, plant and equipment.

In the year ended 31 December 2004 a decrease of the discount rate from 8.2 to 6.7 percent resulted in a change in the estimate of provision for restoration liability totalling RR'mln 692, which was added to the cost of the related assets (see note 5). In the year ended 31 December 2005 a further decrease of the discount rate from 6.7 to 4.8 percent resulted in a change in the estimate of the provision for restoration liability totalling RR'mln 1,636, which was added to the cost of the related assets (see note 5).

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***13. PROVISION FOR PENSION OBLIGATIONS**

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

| | 31 December 2005 | 31 December 2004 |
|-------------------------------|-------------------------|-------------------------|
| Present value of obligations | 8,590 | 7,513 |
| Fair value of plan assets | (2,648) | (1,544) |
| Unrecognised actuarial losses | (4,853) | (4,507) |
| Net liability | 1,089 | 1,462 |

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

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--|--|--|
| Current service cost | 270 | 293 |
| Interest cost | 692 | 789 |
| Expected return on plan assets | (147) | (65) |
| Net actuarial losses | 310 | 314 |
| Net expense recognised in the statement of income | 1,125 | 1,331 |

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

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

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--|--|
| Net liability at the beginning of the year | 1,462 | 1,963 |
| Net expense recognised in the statement of income during the year | 1,125 | 1,331 |
| Contributions made | (1,170) | (1,544) |
| Benefits paid | (328) | (288) |
| Net liability at the end of the year | 1,089 | 1,462 |

Principal actuarial assumptions used:

| | 31 December 2005 | 31 December 2004 |
|--|-------------------------|-------------------------|
| Discount rate (nominal) | 9% | 9% |
| Future pension increases (nominal) | 9% | 9% |
| Employees average remaining working life (years) | 13 | 13 |

14. TRADE AND OTHER PAYABLES

| | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| Accrual for employee flights and holidays | 3,312 | 3,133 |
| Trade payables | 2,942 | 2,435 |
| Wages and salaries | 1,321 | 1,411 |
| Current accounts of third parties in OOO “MAK-Bank” | 574 | 455 |
| Interest payable | 490 | 511 |
| Advances from customers | 120 | 210 |
| Payables to associates | 66 | 40 |
| Other payables and accruals | 385 | 373 |
| | 9,210 | 8,568 |

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

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***15. OTHER PROVISIONS**

| | 31 December 2005 | 31 December 2004 |
|-------------------------------|-------------------------|-------------------------|
| Provision for guarantee given | - | 866 |
| Provision for legal claim | 229 | 229 |
| | 229 | 1,095 |

Provision for guarantee given

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|------------------------------|--|--|
| At the beginning of the year | 866 | 972 |
| Interest accrued | 68 | 89 |
| Interest paid | (43) | (139) |
| Exchange loss (gain) | 25 | (56) |
| Reversal of provision | (916) | - |
| At the end of the year | - | 866 |

In April 2003 the Company guaranteed a US\$ denominated fixed rate loan issued by OAO “Investment Bank Trust” to ZAO “Nazymyskaya Oil and Gas Research Expedition”, which is due for repayment in 2006. The Company management expected the Group to incur a probable outflow of economic resources in connection with this guarantee and therefore the Group recognised a provision for the principal amount of the loan and accrued interest in the financial statements for the years ended 31 December 2003 and 2004. During the period December 2005 – March 2006 ZAO “Nazymyskaya Oil and Gas Research Expedition” repaid to OAO “Investment Bank Trust” the whole of the principal amount of the loan and the related interest. Consequently the Group was able to reverse provision for guarantee given in the year ended 31 December 2005.

16. INCOME AND OTHER TAX ASSETS AND LIABILITIES

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

| | 31 December 2005 | 31 December 2004 |
|---------------------------------|-------------------------|-------------------------|
| Value added tax | 834 | 566 |
| Unified social tax | 736 | 831 |
| Extraction tax | 478 | 472 |
| Property tax | 376 | 277 |
| Tax penalties | 290 | 160 |
| Personal income tax (employees) | 202 | 218 |
| Other taxes and accruals | 96 | 117 |
| | 3,012 | 2,641 |

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

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--------------------------|--|--|
| Property tax | 1,306 | 1,003 |
| Ecology fund | 864 | 906 |
| Tax penalties | 639 | 65 |
| Other taxes and accruals | 331 | 370 |
| | 3,140 | 2,344 |

In accordance with Resolution № 1364 of the Government of the Russian Federation dated 9 December 1999, in addition to the taxes noted above, the Group is obliged to pay 6.5 percent on the value of diamonds sold for export in the form of an export duty (see note 17).

As a result of a tax audit, the Group accrued tax penalties for the year ended 31 December 2005 totalling RR'mln 590, relating to 2002, 2003 and 2004 years.



AK “ALROSA”

Notes to the IFRS consolidated financial statements for the year ended 31 December 2005

(in millions of Russian roubles, unless otherwise stated)

According to legislation which became substantively enacted in the year ended 31 December 2001, income tax payable by companies in the Russian Federation with effect from 1 January 2002 ranges from 20 percent to 24 percent, depending on the decision each year of regional and local tax authorities, which can agree jointly on a supplementary amount of up to 4 percent above that set by the federal tax authorities. The rate used to compute the deferred income tax assets and liabilities of the Group at 31 December 2005 and 31 December 2004 was 24 percent, which reflects the fact that, based on their decisions in respect of tax rates, substantially all regional and local tax authorities in the regions in which the Group operates assessed the maximum supplementary amount in respect of the year ended 31 December 2005 and year ended 31 December 2004.

Income tax expense comprises the following:

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--------------------------------|--------------------------------|--------------------------------|
| Current tax expense | 6,288 | 5,533 |
| Deferred tax (benefit) expense | (57) | 1,400 |
| | 6,231 | 6,933 |

Net profit before taxation for financial reporting purposes is reconciled to tax expense as follows:

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--|--------------------------------|--------------------------------|
| Profit before income tax | 22,131 | 19,896 |
| Theoretical tax charge at statutory rate of 24 percent thereon | 5,311 | 4,775 |
| Income not assessable for income tax purposes | (963) | (655) |
| Expenses and losses not deductible for income tax purposes | 1,883 | 2,813 |
| | 6,231 | 6,933 |

Differences between IFRS and Russian statutory tax accounting give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes. The tax effect of the movement on these temporary differences is recorded at the rate of 24 percent (2004: 24 percent).

| | 31 December 2005 | Tax effect of movement in temporary differences | | 31 December 2004 | Tax effect of movement in temporary differences | 31 December 2003 |
|--|---------------------|--|--------------------------------------|---------------------|--|---------------------|
| | | Resulting from acquisition of subsidiary (see note 3) | Charged to statement of income | | Charged to statement of income | |
| Deferred tax liabilities | | | | | | |
| Property, plant and equipment | 4,243 | 684 | (330) | 3,889 | 183 | 3,706 |
| Inventories | 2,402 | - | 165 | 2,237 | 1,253 | 984 |
| Long-term investments | 326 | - | 141 | 185 | 66 | 119 |
| Impairment of accounts receivable | 23 | - | 103 | (80) | 440 | (520) |
| Deferred tax assets | | | | | | |
| Accrual for employee benefits | (1,030) | - | (30) | (1,000) | (13) | (987) |
| Exploration costs written off | (303) | - | (38) | (265) | (91) | (174) |
| Provision for pension obligations | (115) | - | 131 | (246) | (91) | (155) |
| Write-down of inventories | (899) | - | (390) | (509) | (129) | (380) |
| Other deductible temporary differences | (154) | - | 191 | (345) | (218) | (127) |
| Net deferred tax liability | 4,493 | 684 | (57) | 3,866 | 1,400 | 2,466 |

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***17. SALES**

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|----------------------------------|--|--|
| Revenue from diamond sales: | | |
| Export | 46,315 | 34,923 |
| Domestic | 33,931 | 35,484 |
| Revenue from diamonds for resale | 7,602 | - |
| | 87,848 | 70,407 |
| Other revenue: | | |
| Transport | 2,659 | 1,954 |
| Social infrastructure | 1,049 | 929 |
| Construction | 1,021 | 602 |
| Gold | 808 | 1,272 |
| Trading | 597 | 832 |
| Other | 2,851 | 1,953 |
| | 96,833 | 77,949 |

Export duties totalling RR'mln 2,945 for the year ended 31 December 2005 (year ended 31 December 2004: RR'mln 2,311) were netted against revenues from export of diamonds.

In March 2005 the Group concluded an agreement with “Sunland Mining Company Lda”, a third party Angolan diamond exporter, in accordance with which it received the right to purchase diamonds produced in Angola from “Sunland Mining Company Lda” and subsequently resell these diamonds in the open market.

In December 2001 a trade agreement between the Company and De Beers was signed, covering the period from 1 January 2002 to 31 December 2006. Pursuant to this agreement, the Company agreed to sell and De Beers agreed to buy up to US\$'mln 800 in value of the Company's annual diamond production at the current market prices. To be legally enforceable, this agreement required the regulatory permission of the European Commission. In January 2003 the European Commission issued a Statement of Objections to the De Beers Trade Agreement. In February 2006 De Beers agreed with the European Commission to gradually reduce its purchases of rough diamonds from the Company to a maximum of US\$'mln 400 in 2008 and thereafter to cease any further purchases altogether.

In November 2002, the President of the Russian Federation signed a decree liberalising the Russian diamond market. The decree authorised the Government of the Russian Federation to grant multi-year quotas, not to exceed five years. In February 2003 the Company was granted a five-year quota to export up to US\$'mln 1,638 of diamonds each year, based on current market prices. In August 2005 OAO “ALROSA-Nyurba”, a subsidiary of the Group, was granted a quota for the year ended 31 December 2005 to export up to US\$'mln 277 of diamonds based on current market prices.

18. COST OF SALES

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---------------------------------------|--|--|
| Wages, salaries and other staff costs | 13,480 | 12,437 |
| Depreciation | 7,671 | 6,821 |
| Cost of diamonds for resale | 7,234 | - |
| Fuel and energy | 6,997 | 6,029 |
| Extraction tax | 6,613 | 5,907 |
| Materials | 5,643 | 5,396 |
| Services | 2,292 | 1,955 |
| Transport | 926 | 1,068 |
| Write down of inventory | 244 | 160 |
| Other | 294 | 345 |
| Movement in inventories | (838) | (3,955) |
| | 50,556 | 36,163 |

Depreciation totalling RR'mln 495 (year ended 31 December 2004: RR'mln 668) and staff costs totalling RR'mln 1,776 (year ended 31 December 2004: RR'mln 1,907) were incurred by the Group's construction divisions and were capitalised in the year.

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

Cost of diamonds for resale represents the cost of diamonds purchased by the Group from “Sunland Mining Company Lda” for the purpose of the subsequent resale on the open market (see note 17).

19. GENERAL AND ADMINISTRATIVE EXPENSES

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|-------------------------|--------------------------------|--------------------------------|
| Administrative expenses | 3,315 | 3,121 |
| Bad debt expense | 82 | 326 |
| | 3,397 | 3,447 |

Wages, salaries and other staff costs totalling RR'mln 850 (year ended 31 December 2004: RR'mln 711) were included into administrative expenses.

20. OTHER OPERATING INCOME

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--------------------------------|--------------------------------|
| Distribution of minority interest share in the statutory retained earnings of OAO “ALROSA-Nyurba” to AK “ALROSA” (see note 8) | 1,080 | 822 |
| Reversal of provision for guarantee given (see note 15) | 916 | - |
| Amortisation of Grant (see note 9) | 699 | 1,135 |
| Reversal of tax penalties | 391 | - |
| Other | 962 | 895 |
| | 4,048 | 2,852 |

In the year ended 31 December 2005 the Group reversed tax penalties in total amount of RR'mln 391 related to 1999-2001 tax audit after the final decision of a court in favour of the Group.

21. OTHER OPERATING EXPENSES

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--------------------------------|--------------------------------|
| Social costs | 3,362 | 2,491 |
| Taxes other than income tax and extraction tax (see note 16) | 3,140 | 2,344 |
| Exploration expenses | 2,463 | 1,858 |
| Loss on disposal and write-off of property, plant and equipment | 934 | 590 |
| Impairment of property, plant and equipment | 165 | 320 |
| Provision for guarantee given (see note 15) | 68 | 89 |
| Provision for impairment of available-for-sale investments | - | 464 |
| Other | 1,392 | 1,077 |
| | 11,524 | 9,233 |

Social costs consist of:

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|--|--------------------------------|--------------------------------|
| Maintenance of local infrastructure | 1,700 | 1,302 |
| Charity | 521 | 369 |
| Hospital expenses | 312 | 215 |
| Celebration of semi centenary of diamond-mining industry | 174 | - |
| Education | 153 | 185 |
| Other | 502 | 420 |
| | 3,362 | 2,491 |

**AK “ALROSA”**

Notes to the IFRS consolidated financial statements for the year ended 31 December 2005

*(in millions of Russian roubles, unless otherwise stated)***22. FINANCE INCOME**

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|-----------------|--------------------------------|--------------------------------|
| Interest income | 781 | 316 |
| Exchange gains | - | 1,756 |
| | 781 | 2,072 |

23. FINANCE COSTS

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--------------------------------|--------------------------------|
| Interest expense: | | |
| Eurobonds | 2,236 | 1,326 |
| Bank loans | 1,607 | 2,051 |
| Non-convertible bonds | 447 | 830 |
| European commercial paper | 149 | - |
| Commercial paper | 146 | 123 |
| Other | 123 | 68 |
| Exchange loss | 1,349 | - |
| Provision for restoration liability (see note 12) | 389 | 406 |
| | 6,446 | 4,804 |

24. CASH GENERATED FROM OPERATIONS

Reconciliation of profit before tax to cash generated from operations:

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---|--------------------------------|--------------------------------|
| Profit before income tax | 22,131 | 19,896 |
| Adjustments for: | | |
| Share of net profit of associates (note 3) | (749) | (499) |
| Gain on disposal of subsidiaries (note 3) | (1,507) | - |
| Interest income (note 22) | (781) | (316) |
| Interest expense (note 23) | 5,097 | 4,804 |
| Provision for impairment of available-for-sale investments (note 21) | - | 464 |
| Impairment of property, plant and equipment (note 21) | 165 | 320 |
| Provision for guarantee given (note 21) | 68 | 89 |
| Loss on disposal and write-off of property, plant and equipment (note 21) | 934 | 590 |
| Distribution of minority interest share in the statutory retained earnings of OAO “ALROSA-Nyurba” to AK “ALROSA” (note 20) | (1,080) | (822) |
| Reversal of provision for guarantee given (note 20) | (916) | - |
| Amortisation of Grant (note 20) | (699) | (1,135) |
| Depreciation (note 18) | 7,671 | 6,821 |
| Adjustments for non-cash investing activity (note 28) | (2,321) | (1,314) |
| Adjustments for non-cash financing activity (note 28) | 128 | 230 |
| Unrealised foreign exchange effect on non-operating items | 1,605 | (1,633) |
| Net operating cash flow before changes in working capital | 29,746 | 27,495 |
| Net increase in inventories | (1,779) | (3,741) |
| Net increase in trade and other receivables, excluding dividends receivable and advances for acquisition of subsidiaries | (3,172) | (2,963) |
| Net increase (decrease) in provisions, trade and other payables, excluding interest payable and payables for acquired property, plant and equipment | 901 | (880) |
| Net increase in taxes payable other than income tax | 371 | 85 |
| Cash generated from operations | 26,067 | 19,996 |
| Income tax paid | (6,984) | (5,126) |
| Net cash flows from operating activities | 19,083 | 14,870 |



25. FINANCIAL RISKS MANAGEMENT

(a) Credit risk

Financial assets, which potentially subject Group entities to credit risk, consist principally of trade and other receivables. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. The carrying amount of accounts receivable, net of impairment provision, represents the maximum amount exposed to credit risk. The Group has no other significant concentrations of credit risk. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision already recorded.

Cash is placed in financial institutions, which are considered at the time of deposit to have minimal risk of default.

(b) Foreign exchange risk

The Group exports production to European and other countries and attracts a substantial amount of foreign currency denominated long-term borrowings and is thus exposed to foreign exchange risk. Foreign currency denominated liabilities (see notes 10 and 11) give rise to foreign exchange exposure.

At 31 December 2005 the Group does not have arrangements to mitigate the foreign exchange risks of the Group's operations

(c) Interest rate risk

The Group's income and operating cash flows are substantially independent of changes in market interest rates. The Group is exposed to interest rate risk through market value fluctuations of interest bearing long-term borrowings. The majorities of interest rates on long-term borrowings are fixed, and are disclosed in note 10. The Group's principal interest bearing assets are current accounts opened with a number of banks (see note 4), loans issued and notes receivable.

At 31 December 2005 the Group does not have arrangements to mitigate the interest rate risk.

(d) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, and ensuring the availability of additional funding through an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, the Group aims to maintain flexibility in its funding requirements by keeping committed credit lines available.

(e) Fair value estimation

The fair value of publicly traded trading and available-for-sale securities is based on quoted market prices at the balance sheet date.

The estimated fair value of financial assets carried at amortised cost is determined by discounting estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates available to the Group for similar financial instruments. Fair value of these financial assets did not materially differ from their carrying amount at 31 December 2005 and 31 December 2004. At 31 December 2005 and 31 December 2004 the fair value of financial liabilities, which is estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments with the same remaining maturity, did not materially differ from the carrying amount of these financial liabilities (note 10).

The carrying amounts of financial assets and liabilities with maturity of less than one year are assumed to approximate their fair values.



26. CONTINGENCIES, COMMITMENTS AND OTHER RISKS

(a) Operating environment

Whilst there have been improvements in economic trends in the Russian Federation, the country continues to display certain characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in most countries outside of the Russian Federation and relatively high inflation. The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations, and changes, which can occur frequently.

The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

(b) Taxes

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

At 31 December 2005 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that the financial position cannot be sustained, an appropriate amount has been accrued for in these consolidated financial statements.

As at 31 December 2005 the Group had tax contingencies relating to transactions between the Company and its subsidiaries. Management of the Group believes that the exposure in respect of these tax risks is not probable, therefore as at 31 December 2005 no provision for tax liabilities had been recorded (as at 31 December 2004 – no provision).

(c) Legal proceedings

The Group is a party to certain legal proceedings arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material adverse effect on the results of operations or financial position of the Group as at 31 December 2005, other than amounts that have been accrued in the consolidated financial statements.

(d) Insurance

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

(e) Capital commitments

At 31 December 2005, the Group has contractual commitments for capital expenditures of approximately RR'mln 3,873 (31 December 2004: RR'mln 4,078).

(f) Restoration, rehabilitation and environmental costs

Under its license agreements, the Group is not responsible for any significant restoration, rehabilitation and environmental expenditures that may be incurred subsequent to the cessation of production at each mine, apart from the obligation to return assets received under the Lease agreement (see note 9). However, the Group is obliged to restore riverbeds and the surrounding areas. These expenses are not expected to be material to the Group and are expensed in the period incurred.



AK “ALROSA”

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(in millions of Russian roubles, unless otherwise stated)

27. RELATED PARTY TRANSACTIONS

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24, “Related Party Disclosures”. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

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

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

Governments of the Russian Federation and the Republic of Sakha (Yakutia) are the ultimate controlling parties of AK “ALROSA” and have a controlling interest of over 50 percent in AK “ALROSA”. As at 31 December 2005 69 percent of AK “ALROSA” issued shares were directly owned by the Governments of the Russian Federation and the Republic of Sakha (Yakutia). Following the General Meeting of Shareholders in June 2005, the 15 seats on the Supervisory Council include 11 representatives of the Russian Federation and the Republic of Sakha (Yakutia), three management representatives and one representative of districts of the Republic of Sakha (Yakutia). Governmental, federal and local, economic and social policies affect the Group’s financial position, results of operations and cash flows.

Tax balances are disclosed in notes 7 and 16. Tax transactions are disclosed in note 16. Information related to the Lease Agreement with the Republic of Sakha (Yakutia) is disclosed in notes 9 and 12.

During the year ended 31 December 2005 the Group acquired 16,361,256 common shares of OAO “Viluyskaya GES-3” from the Ministry of Property of Republic of Sakha (Yakutia) for a total consideration of RR’mn 250. As a result of this transaction the Group increased its shareholding in OAO “Viluyskaya GES-3” to 79 percent.

Parties under control of the Government

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

As at 31 December 2005 and 31 December 2004 there were no balances of accounts receivable and payable with the parties under control of the Government. During the years ended 31 December 2005 and 2004 the Group had the following significant transactions with parties under control of the Government:

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|-----------------------------------|--------------------------------|--------------------------------|
| Sales of diamonds | 13,342 | 14,232 |
| Other sales | 274 | 360 |
| Electricity and heating purchases | 4,069 | 3,371 |
| Other purchases | 591 | 732 |

As at 31 December 2005 the amount of loans received by the Group from entities under Governmental control totalled RR’mn 6,139 (31 December 2004 – RR’mn 2,882). As at 31 December 2005 the amount of loans issued by the Group to entities under Governmental control totalled RR’mn 920 (31 December 2004 – RR’mn 272).

Key management compensation

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

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)*

The Management Board consists of 24 members, three of whom are also members of the Supervisory Council. Management Board members are entitled to salary, bonuses, voluntary medical insurance, compensation for serving as members of the Board of directors for certain Group companies and other short term employee benefits. Salary and bonus compensation paid to members of the Management Board is determined by the terms of employment contracts.

Supervisory Council and Management Board members received benefits in the year ended 31 December 2005 totalling RR'mln 164 (year ended 31 December 2004: RR'mln 207).

Associates

Significant transactions and balances with associates are summarised as follows:

| Long-term accounts receivable | 31 December 2005 | 31 December 2004 |
|---|-------------------------|-------------------------|
| “Escom-ALROSA Ltd.”, loan issued and interest receivable (see note 3) | 2,271 | - |
| OAo “Yuzhno-Verkhoyanskaya Gornaya Company”, loans issued | - | 283 |
| | <u>2,271</u> | <u>283</u> |

Long-term loans issued to OAO “Yuzhno-Verkhoyanskaya Gornaya Company” are RR denominated, unsecured and bear a weighted average interest rate of 12 percent per annum.

| Current accounts receivable | 31 December 2005 | 31 December 2004 |
|--|-------------------------|-------------------------|
| Catoca Mining Company Ltd., dividends receivable | 554 | 193 |
| ZAO “PIC Orel Almaz”, receivables for supplied diamonds | 164 | 165 |
| “Escom-ALROSA Ltd.”, loan issued (see note 3) | 78 | - |
| OAo “Tuymaada Diamond”, receivables for supplied diamonds | - | 145 |
| OAo “Yuzhno-Verkhoyanskaya Gornaya Company”, loans issued | - | 206 |
| OAo “Yuzhno-Verkhoyanskaya Gornaya Company”, other receivables | - | 97 |
| Other | 68 | 59 |
| Less: provision for bad debt | (187) | (283) |
| | <u>677</u> | <u>582</u> |

Short-term loans issued to OAO “Yuzhno-Verkhoyanskaya Gornaya Company” are US\$ and RR denominated, unsecured and bear a weighted average interest rate of 12 percent per annum.

During the year ended 31 December 2005 the Group sold diamonds to ZAO “PIC Orel Almaz” for a total amount of RR'mln 50 (year ended 31 December 2004: RR'mln 548).

Management believes that in the years ended 31 December 2005 and 2004 transactions with associates were performed under market terms.

28. SIGNIFICANT NON-CASH TRANSACTIONS

| | Year ended 31 December 2005 | Year ended 31 December 2004 |
|---------------------------------------|--|--|
| Non-cash investing activities: | | |
| Inventory used in construction | (2,107) | (1,192) |
| Other | (214) | (122) |
| | <u>(2,321)</u> | <u>(1,314)</u> |
| Non-cash financing activities: | | |
| Commercial paper issuance | 358 | 230 |
| Commercial paper and loans redemption | (230) | - |
| | <u>128</u> | <u>230</u> |

**AK “ALROSA”****Notes to the IFRS consolidated financial statements for the year ended 31 December 2005***(in millions of Russian roubles, unless otherwise stated)***29. SEGMENT INFORMATION**

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

An analysis of revenue by type is disclosed in note 17. Revenue from sales by geographical location of the customer, and assets and capital expenditures by geographical location of the asset are as follows:

| | Sales | | Total assets | | Capital Expenditures | |
|--------------------|--------------------------------|--------------------------------|------------------|------------------|--------------------------------|--------------------------------|
| | Year ended 31 December 2005 | Year ended 31 December 2004 | 31 December 2005 | 31 December 2004 | Year ended 31 December 2005 | Year ended 31 December 2004 |
| Russian Federation | 42,431 | 43,026 | 167,396 | 148,405 | 17,337 | 16,595 |
| Western Europe | 28,358 | 21,925 | 1,966 | - | 37 | - |
| Other countries | 26,044 | 12,998 | 2,568 | 858 | 674 | 463 |
| | 96,833 | 77,949 | 171,930 | 149,263 | 18,048 | 17,058 |
| Associates | - | - | 1,464 | 1,083 | - | - |
| Unallocated assets | - | - | 701 | 9 | - | - |
| Total | 96,833 | 77,949 | 174,095 | 150,355 | 18,048 | 17,058 |

Sales to De Beers are included in the Western Europe geographical segment.

The Group has one individual customer, De Beers, that accounted for 19 percent of its sales during the year ended 31 December 2005 (year ended 31 December 2004: 23 percent).

30. POST BALANCE SHEET EVENTS*Acquisitions*

In January 2006 the Company acquired 75 percent of the voting shares of OAO “Yakutskgeofizika”, a company involved in geological survey and exploration of oil and gas deposits in the Republic of Sakha (Yakutia), for a total purchase consideration of RR’mln 160.

In February 2006 the Company acquired 50.4 percent of the voting shares of OAO “NNGK Sakhaneftgaz”, a company holding licenses and involved in the development of several oil and gas deposits located in the Republic of Sakha (Yakutia), for a total purchase consideration of RR’mln 493.

In April 2006 the Company acquired 100 percent of the voting shares of ZAO “BRINT-M”, a company holding licenses for geological survey of diamond deposits in the Arkhangelsk and Murmansk regions of Russia, for a total purchase consideration of RR’mln 313.

Management of the Group is in process of a formal assessment of fair value allocations for the above transactions. As a result of this assessment goodwill or negative goodwill may arise from these transactions.

Dividends

On 24 June 2005, the Company’s shareholders approved dividends for the year ended 31 December 2005 totalling RR’mln 1,962. Dividends per share amounted to RR 9,810.