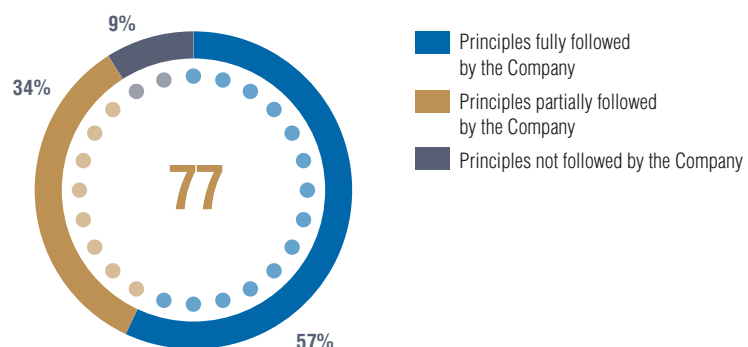


5.1.6. Corporate Governance Compliance

COMPLIANCE WITH THE CORPORATE GOVERNANCE CODE

Section	Principles recommended by the Code	Principles fully followed by the Company	Principles partially followed by the Company	Principles not followed by the Company
Rights of shareholders and equal conditions for shareholders to exercise their rights	13	11	1	1
Company's Board of Directors	34	11	18	5
Company's Corporate Secretary	2	2	–	–
Remuneration to the members of the Board of Directors, executive bodies, and other key managers of the Company	10	6	4	–
Risk management and internal control system	6	6	–	–
Disclosure of information on the Company and corporate information policy	7	5	2	–
Material corporate actions	5	2	2	1
Total	77	43	27	7

COMPLIANCE WITH THE CORPORATE GOVERNANCE CODE



5.2. RISK MANAGEMENT

The Company has a Risk Management System (hereinafter, RMS) aimed at ensuring sustainable continuous functioning and development of the Company by timely identification, assessment, and efficient management of risks that threaten the Company's efficient business and reputation, employee health, environment, and property interests of its shareholders and investors.

For the purpose of RMS development in the Company, the Board of Directors approved the new version of the Risk Management Policy (Minutes of the Board of Directors No. 164/6 dated September 01, 2014).

5.2.1. Participants of the risk management system

Main parties to the risk management process are:

- Board of Directors of the Company;
- Board of Directors' Audit Committee;
- General Director of the Company (Company's Management Board);
- Risk owners;
- employees responsible for control procedures and risk management;
- unit responsible for coordination and methodology support of risk management;
- unit responsible for internal audit.

5.2.2. Risk Management Goals

- Reduce the probability and/or consequences of events affecting achievement of the Company's goals;
- Set priorities for the Company's activities based on the concept of the existing risks, including financial ones;
- Security of assets and efficient use of available resources;
- Achievement of target indicators;
- Continuous operating efficiency improvement in all areas of the Company's activity by analyzing and assessing the existing risks;
- Ensuring a reliable functioning of electricity grids in the Russian Federation;
- Achievement of the highest performance for the risk management system at the Company and its subsidiaries;
- Timely and complete information and analytical support for managerial decisions and planning of the Company's and its subsidiaries' activities.

A system approach is used for risk identification and management. Activities aimed at prevention and minimization of risks are developed and analyzed on a quarterly basis.

5.2.3. Key Risks and Controls

Industry risks

1. The risk of a significant increase in receivables for electricity transmission, related to low payment discipline of end consumers, and a risk of growing bad debts for electricity transmission due to disputes with consumers over the application of industry legislation pertaining to payment for electricity transmission services.



The risk is related to non-payment for transmitted electricity (disputable or indisputable overdue receivables) by consumers. The main debtors are suppliers of last resort, electricity supply companies, and local grid operators. The risk is caused by both the imperfection of the retail energy market mechanisms and lack of effective mechanisms to encourage timely payments for electricity transmission as well as by the impact of macroeconomic factors.

Imperfect retail energy market entails disputes between electricity grid and supply companies with regard to consumed electricity and power. The result is disputable and overdue debts for electricity transmission which causes lower liquidity and financial stability of the Company.

- More active cooperation with court bailiffs service at the execution stage and signing of cooperation agreements.
- Initiation of the review of issues regarding unsatisfactory payment discipline at the meetings of the regional inter-departmental commissions for monitoring electricity and transmission payments.
- Implementation of measures against debtors subject to bankruptcy, including sale of receivables due from bankrupts.
- Activities to fully or partially limit electricity consumption by 'direct' consumers.
- Counter-injunction for immediate enforcement of the first instance court's

decision to reduce the period until receipt of enforcement orders.

- In order to minimize the risk of non-payment, the Company developed and approved Rules for handling receivables for the Company's electricity transmission services and measures against non-paying parties.

2. Risk of reduction in the volume of electricity transmission services as a result of:

a) Overall reduction of electricity demand.

b) Optimization of external power supply systems, reduction of electricity consumption from the uniform energy system of Russia resulted from consumers' own generation development.



Industrial growth stopped in the North-West of Russia in 2015. The main causes included reduced investment activity in Russia and unfavorable changes in commodity markets.

Industrial development in 2015 was driven by: Stagnation of production volumes, low productivity growth, slowed down investment activity, weakened national currency, slowed domestic demand, external political pressure, and mutual sanctions.

In order to minimize this risk, the Company takes measures to improve the reliability of electricity transmission volume forecasting which is used for pricing and business planning based on macroeconomic statistics and the behavior of major consumers.

In accordance with the Resolutions of the Government of the Russian Federation and with active participation of PJSC ROSSETI and the Company, statutory measures are developed to reduce the number of grid companies and optimize consumers' costs of electricity transmission. In accordance with legislation amendments effective from 2014 the costs of 'monogrids' - grid companies which service mainly single consumer and were established with its assets - should be excluded from the 'uniform (boiler)' revenue.

In 2014, some industrial companies in the Republic of Karelia and Vologda Region initiated the removal of nearby power plants from the WEM and their conversion to isolated generating plant to support direct supplies of electricity for own needs without paying an electricity transmission tariff.

Another improvement to the legislation of the Russian Federation is a change of procedure for electricity transmission services volume and costs determination in order to determine the consumers' obligations based on the maximum power capacity and the electricity transmission price (tariff). The relevant proposals were submitted to the Government of the Russian Federation.

3. The risk of disallowance of some of the Company's costs by the regional tariff regulation entities in the context of electricity transmission tariff setting due to limits for the growth of maximum electricity tariff rates established at the federal level*.



This risk makes full recovery of feasible expenses incurred by the Company

impossible and limits investment in the development of electricity facilities.

- Interaction with regional tariff regulation authorities to establish more feasible tariffs to recover all costs of the Company and to ensure the implementation of the investment programme as needed.
- Well-reasoned approach to costs setting is implemented.

4. The risk of an increase in the number of 'privileged' consumers enjoying reduced rates and the volume of connected power capacity as compared to business plan targets.



The risk of an increase in the number of 'privileged' consumers enjoying reduced rates and the volume of connected power capacity as compared to business plan targets which in turn results in a growth

of 'privileged' consumers' facilities connection costs and attracting additional funds through borrowings or re-allocation of funds between sites.

- Interaction with regional administrations to developed integrated infrastructure development plans in line with the region development plans.
- Selection of the most cost-effective system for connecting 'privileged' consumers enjoying reduced rates.
- Works carried out using own resources.

5. Risks of violation of the timeframe for regulated purchasing procedures in the reporting period in the current year (violation of official timeframe for purchasing procedure announcement stipulated in the Purchasing Plan and resolutions of the Company's CTC (for unscheduled purchasing); timeframe for completion of purchasing procedures established by the Company's orders and purchasing documentation; and timeframe for goods delivery and execution of works.



The causes of this risk are late provision of terms of references and draft agreements, long approval period for the Purchasing

Plan and adjustments, and a long period of approval of unscheduled purchases.

- Control over the timeframe for provision of terms of references, data sheets, and draft agreements for timely drafting of a Purchasing Plan to survey the market value of necessary products.
- Control over conformance of the number of procedures implemented in different ways to the target values in the Purchasing Plan.
- Drafting statements of work for engineering and construction and installation, operations and repairs based on standard statements of work.
- Control over the timeframes for purchasing documentation development determined by the Company's orders.

6. Risk of exceeding the purchasing value above the Purchasing Plan.



Caused by inadequate verification of the substantiation of maximum (initial) costs of purchases when drafting a Purchasing Plan, preparation and

adjustment of a Purchasing Plan without a business plan approved by the Board of Directors (with scenario conditions for the forthcoming and current year).

- Control over lots in the Purchasing Plan to prevent restriction of competition between bidders.
- Control over conformance of the number of procedures implemented in different ways to the target values in the Purchasing Plan.
- Control of conformance of the Purchasing Plan to the Company's production programs approved for the current calendar year.
- Control over drafting terms of references for works related to operation, repair and investment activities of the Company based on standard terms of references.
- Control over the timeframes for purchasing documentation preparation determined by the Company's orders.

7. Risk of decrease in transparency of purchasing operations.



A change in the ratio between the number and methods (open bidding, open request for proposal, purchasing from a single source,

etc.) of purchasing versus the approved Purchasing Plan.

- Control over unconditional implementation of the Regulations on Procurement of Goods, Works, and Services for the Company.
- Control over substantiation of purchasing from a single source.

8. Risk of absence of electric grid rebuild (development) activities in the Company's investment programme.



Higher risk of rebuild (development) of grid facilities of the Company being left out from the Company's investment programme results in untimely rebuild of the grids and

therefore, reduced reliability of power supply to consumers and untimely fulfillment of grid connection agreements.

- Interaction with regional administrations to approve investment programs, which include measures to maintain system reliability and ensure grid connection of new applicants as needed.
- Interaction with tariffs regulation authorities to include in the electricity transmission tariffs expenses that cannot be compensated through grid connection payments.

Country and regional risks

9. Risks related to political and economical situation in the country and regions



Country and regional risks of the Company are primarily attributable to macroeconomic factors at the global, national, and regional levels. Crises in global economy affect industrial production and electricity consumption which entails a reduction in the Company's revenue.

The impact of macroeconomic risks on the volume of the Company's electricity transmission services and actions aimed at the minimization of their effects are detailed in the Industry-Wide Risks section.

10. Risks related to potential military conflicts, emergency conditions, and strikes in the country (-ies) and regions.



The Northwestern Federal District includes regions with a similar social and economic development level but some regions border with other countries, including NATO countries, for this reason internal conflicts, including conflicts with military activities, cannot be fully ruled out. The Company cannot fully rule out the risks related to potential imposition of the state of emergency in the regions where the Company's facilities are located.

The probability of military conflicts and emergency conditions in the regions where the Company operates is insignificant. In case of potential military conflicts or acts of terrorism, the Company may bear risks of a breakdown of its fixed assets.

11. Risks related to the country and region geography: higher hazards of disasters, potential disruption of transport to remote and/or hard-to-access areas, etc.



The Company's geography is wide and the Company operates in two climatic belts (subarctic and moderate). There is a probability of emergencies due to disasters (hurricanes, storm rains, floods, ice rain, etc.) which may result in power and transport failures in regions.

Risks related to increased hazards of disasters are assumed by the Company to be minor.

Financial risks

12. Interest risks.

Interest risk implies unfavorable changes in the interest rate in financial markets. A growth of interest rates related to liquidity shortage in the banking system can have a significant impact on the Company's business as the company uses borrowings in its operations.

The average weighted rate under new loans in 2015 increased year-over-year.

The average weighted rate in the Company's loan portfolio since 2015 has increased due to a unilateral increase by lending banks of interest rates on the current loan debt in first and second quarters of 2015. In order to reduce the Company's cost of loans in the second quarter of 2015, the Company refinanced the loan debt by placing a bond issue.



13. Currency risks.

An increase in the FX rate of main global currencies does not affect the Company's financial state. The Company has payments with its contractors both during revenue-earning and expense-related activities in national currency only. The Company does not enter into direct contracts with its contractors with FX settlements. However, some projects as part of repair and investment programs provide for purchase of imported equipment.

An increase in the FX rate of the main global currencies results in the price increase for such equipment and increase of project costs as a whole. In order to reduce the exchange-rate risk, the Company considers replacement of the foreign equipment used under these projects with similar national equipment.



Legal risks

14. Risks of changes in tax laws.

Tax law application is sometimes unclear and contradictory resulting in significant tax risks. Changes in tax laws pertaining to an increase in the tax burden (changes in tax rates, procedure, and timeframe for tax payment, and introduction of new taxes) may result in a decrease in the Company's net profits which will in turn reduce

dividends to be paid out. Reduction of tax rates or cancellation by the Government of the Russian Federation of some taxes and duties benefit the Company's performance.

In case of changes in tax laws, the Company intends to plan its operations taking these changes into account.



15. The risk of lodging a dispute in relation to major or related-party transactions by the Company's shareholders (when such transactions are carried out without a legitimate approval of the Board of Directors or the General Shareholders' Meeting of the Company or approved with violation of the established procedure).



The risk of lodging a dispute in relation to major or related-party transactions by the Company's shareholders is not currently observed excepting transactions carried out without the approval of the Board of Directors or the General Shareholders' Meeting of the Company in accordance with the procedure stipulated by the applicable

legislation or approved with violation of the established procedure).

Mandatory legal analysis of the Company's transactions is carried out to check if corporate procedures stipulated by Russian legislation and/or the Articles of Association of the Company are needed.

16. Risks of changes in the Company's core operations licensing requirements or licensing requirements for the use of property with limited circulation (including natural resources).



Risks of changes in the Company's core operations licensing requirements or licensing requirements for the use of property with limited circulation (including natural resources) is not currently observed excepting cases where extension of a license or activities to be licensed stipulates requirements that cannot be met by the Company.

In case of a change in licensing requirements, the Company will take necessary measures to obtain relevant licenses and permits.

17. Risks of changes in the court practice on matters pertaining to the Company's activities which may affect the results of its activities or decisions in the current court cases where the Company participates.



Since a judicial precedent is not the source of law in the Russian Federation, the court practice will not have a significant effect on the Company's performance. A change in the court practice is mainly related to law changes. It is not possible to assess risks related to a change in law.

In case of a significant change in the court practice on matters pertaining to the Company's activities the Company intends to plan its operations taking these changes into account.

Risk of loss of goodwill (reputational risk)

18. Risk of loss of goodwill (reputational risk)

The Company's operations aim at complete fulfillment of its obligations to customers and contractors. The Company constantly works at ensuring reliable and uninterrupted power supply, improving quality of services and customer focus – achieving the goals determined by the Electricity Generation Sector Development Strategy.

The Company is a natural monopoly, therefore a significant customer or contractor attrition due to adverse reputational factors is hardly possible.



Strategic risk

19. Strategic risk.

Long-term development of the electricity sector in general as a key industry is determined by the government. The Government of the Russian Federation issued Decree No. 511-r dated April 03, 2013 which approved the Development Strategy of the Electric Grid Complex of the Russian Federation.

PJSC ROSSETI strategy is outlined in its Long-term Development Plan (approved by the Resolution of the Board of Directors of PJSC ROSSETI dated December 19, 2014, Minutes No. 174 dated December 22, 2014).



Risks related to the Company's operations

20. Risk of law suits due to failure to perform obligations to the Company by third parties in relation to the Company's core activities (electricity transmission and grid connections).

There are potential risks of law suits due to failure to perform contractual obligations to the Company by third parties in relation to the Company's core activities (electricity transmission and grid connections) among other reasons because of the current economic situation. However, the Company takes necessary efforts (pre-court settlement of disputes and negotiations) to minimize these risks and property damage to the Company.

If relevant lawsuits were lodged the legal position on significant cases is prepared for the Company as a whole and should get approval of core structural divisions of the Company's main office and branches. At the approval stage, a necessary evidence base is also developed. A legal position is developed with due regard to the relevant court practice.



21. Risk of fines to the Company due to non-compliance with anti-monopoly laws of the Russian Federation for grid connection of electricity consumers.



These fines do not relieve the Company from its obligations related to grid connection of applicants.

The Company may perform its obligations by reallocation of funds toward grid connection at the expense of reliability improvement actions in its investment programme or increase in borrowing for grid connection of applicants.

- monitoring of problematic agreements and complaints of consumers followed by pre-court settlement of disputes;
- follow-up of compliance with applicable laws governing grid connection, in particular:
 - a) development and submission of draft agreements to applicants;
 - b) follow-up of the Company's grid connection obligations;
- monitoring of applicable legislation and court practice of the Russian Federation;
- submission of proposals to amend grid connection legislation of the Russian Federation.

22. Risk of emergencies at electrical facilities



Risk of emergencies at electrical facilities as a result of adverse acts of nature (hurricanes, snowstorms, black frost, low air temperatures)

due to geographical and climate features of the Northwest of Russia.

- designing electrical facilities with due account of geographical and climate features of the region;
- electricity distributing facilities insurance that covers cases of disasters.