AB Lietuvos dujos

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2005

INDEPENDENT AUDITOR'S REPORT
TO THE SHAREHOLDERS OF AB LIETUVOS DUJOS

1. We have audited the accompanying balance sheet of AB Lietuvos dujos (a joint stock company registered in the Republic of Lithuania, hereinafter - "the Company") as of 31 December 2005 and the related statements of income, changes in equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

2. Except as discussed in paragraph 3 below, we conducted our audit in accordance with International Standards on Auditing as set forth by the International Federation of Accountants. 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 the management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

3. In accordance with resolutions of the Government of the Republic of Lithuania, the Company's non-current tangible assets have been revalued four times (applying indexation rates) prior to 1 January 1996 (Notes 2.1 and 6), and consequently in the prior years' financial statements have not been stated at either historical cost or fair value (deemed cost), as required by IFRS. As further discussed in Note 2.1 to the accompanying financial statements, the 2005 financial statements have been prepared referring to IFRS 1 "First-time Adoption of International Financial Reporting Standards", except that the date of transition has been established as the beginning of this financial year – 1 January 2005, and not 1 January 2004 as required by IFRS 1. We are unable to determine the carrying values of non-current assets on 1 January 2004 and what effect this would have on the Company's equity as of 1 January 2004 and the income statement for the year ended 31 December 2004.

4. In our opinion, except for the effect of such adjustments, if any, as might have been disclosed had we been able to perform the procedures described in paragraph 3 above, the financial statements referred to above present fairly, in all material respects, the financial position of the Company 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, as adopted by the EU.

UAB ERNST & YOUNG BALTIC
Audit company's licence No. 000514

Jonas Akelis
Auditor's licence
No. 000003

The audit was completed on 8 March 2006.

Balance sheet

		Note	As of 31 December 2005	As of 31 December 2004 (restated)
	ASSETS			
A.	**Non-current assets**		**2 179 229**	**628 074**
I.	Intangible assets	5	3 009	2 824
II.	Non-current tangible assets	6	2 165 045	617 957
II.1.	Land		103	23
II.2.	Buildings and structures		2 020 008	465 326
II.2.1	Buildings		78 893	47 196
II.2.2.	Transmission networks and related installations		1 339 632	163 925
II.2.3.	Distribution networks and related installations		592 834	246 037
II.2.4.	Other buildings and structures		8 649	8 168
II.3.	Machinery and equipment		75 569	63 560
II.4.	Vehicles		8 593	7 801
II.5.	Other equipment, tools and devices		32 248	29 517
II.6.	Construction in progress		25 396	48 960
II.7.	Other non-current tangible assets		3 128	2 770
III.	Non-current financial assets		11 175	7 293
III.1.	Investments	1	10 737	6 410
III.2.	Non-current accounts receivable		427	873
III.3.	Other financial assets		11	10
B.	**Current assets**		**64 828**	**131 107**
I.	Inventories, prepayments and contracts in progress		10 511	5 633
I.1.	Inventories	7	10 310	5 098
I.1.1.	Raw materials, spare parts and other inventories		3 189	3 156
I.1.2.	Natural gas		7 121	1 942
I.2.	Prepayments		201	535
II.	Accounts receivable	8	48 265	43 123
II.1	Trade receivables		47 688	41 792
II.2.	Other receivables		577	1 331
III.	Other current assets	9	-	44 000
IV.	Cash and cash equivalents	10	6 052	38 351
	Total assets		**2 244 057**	**759 181**

The accompanying notes are an integral part of these financial statements.

Balance sheet (cont'd)

		Note	As of 31 December 2005	As of 31 December 2004
	EQUITY AND LIABILITIES			
C.	**Equity**		**1 848 998**	**603 181**
I.	Share capital	11	469 068	469 068
II.	Reserves	12	101 113	66 438
II.1.	Legal reserve		12 528	9 144
II.2.	Other reserves		88 585	57 294
III.	Retained earnings		1 278 817	67 675
D.	**Liabilities**		**395 059**	**156 000**
I.	Non-current liabilities		297 194	82 999
I.1.	Non-current borrowings	14	22 767	53 948
I.2.	Grants (deferred revenue)	13	60 803	29 051
I.3.	Deferred taxes		213 624	-
II.	Current liabilities		97 865	73 001
II.1.	Current portion of non-current borrowings	14	6 859	10 845
II.2.	Current borrowings	14	15 000	-
II.3.	Trade payables	15	44 419	43 864
II.4.	Prepayments received		12 816	8 450
II.5.	Income tax payable		2 608	-
II.6.	Payroll related liabilities		3 711	3 628
II.7.	Other current liabilities		12 452	6 214
	Total equity and liabilities		**2 244 057**	**759 181**

The accompanying notes are an integral part of these financial statements.

General Manager	V. Valentukevičius		8 March 2006
Chief Accountant	Ž. Augutis		8 March 2006

Income statement

		Note	2005	2004
I.	Sales	4	607 782	495 909
II.	Cost of sales	16	(340 262)	(251 390)
III.	**Gross profit (loss)**		**267 520**	**244 519**
IV.	Operating expenses	17	(211 840)	(165 814)
V.	**Profit (loss) from operations**		**55 680**	**78 705**
VI.	**Other operating activities**	18	**3 118**	**2 265**
VI.1.	Income		3 524	2 670
VI.2.	Expenses		(406)	(405)
VII.	**Financial and investing activities**	19	**(7 081)**	**(915)**
VII.1.	Income		1 175	5 597
VII.2.	Expenses		(8 256)	(6 512)
VIII.	**Profit (loss) before tax**		**51 717**	**80 055**
IX.	Income tax	20	(5 514)	(12 380)
X.	**Net profit (loss)**		**46 203**	**67 675**
	Basic and diluted earnings per share (LTL)	21	0.10	0.19

The accompanying notes are an integral part of these financial statements.

General Manager	V. Valentukevičius		8 March 2006
Chief Accountant	Ž. Augutis		8 March 2006

Statement of changes in equity

	Note	Share capital	Legal reserve	Corporate business development reserve	Reserve for securing social guarantees provided for in the Collective agreement, for support and for other purposes	Retained earnings (deficit)	Total
Balance as of 31 December 2003		**340 878**	**9 144**	**18 069**	**2 500**	**58 725**	**429 316**
Increase in share capital	11	128 190	-	-	-	-	128 190
Transfer from corporate business development reserve	12	-	-	(17 552)	-	17 552	-
Transfer from reserve for securing social guarantees provided for in the Collective agreement, for support and for other purpose	12	-		-	(2 500)	2 500	-
Transfers to corporate business development reserve	12	-	-	53 777	-	(53 777)	-
Dividends declared	22	-	-	-	-	(22 000)	(22 000)
Transfer from reserve for securing social guarantees provided for in the Collective agreement, for support and for other purpose	12	-	-	-	3 000	(3 000)	-
Net profit for the year		-	-	-	-	67 675	67 675
Balance as of 31 December 2004		**469 068**	**9 144**	**54 294**	**3 000**	**67 675**	**603 181**
Impact of IFRS 1 adoption:							
Revaluation of non-current tangible assets, net off deferred tax	3	-	-	-	-	1 232 614	1 232 614
Balance as of 1 January 2005		**469 068**	**9 144**	**54 294**	**3 000**	**1 300 289**	**1 835 795**
Transfer to legal reserve	12	-	3 384	-	-	(3 384)	-
Transfer from reserve for securing social guarantees provided for in the Collective agreement, for support and for other purpose	12	-	-	-	(3 000)	3 000	-
Transfers to corporate business development reserve	12	-	-	30 791	-	(30 791)	-
Dividends declared	22	-	-	-	-	(33 000)	(33 000)
Transfer from reserve for securing social guarantees provided for in the Collective agreement, for support and for other purpose	12	-	-	-	3 500	(3 500)	-
Net profit for the year		-	-	-	-	46 203	46 203
Balance as of 31 December 2005		**469 068**	**12 528**	**85 085**	**3 500**	**1 278 817**	**1 848 998**

The accompanying notes are an integral part of these financial statements.

General Manager	V. Valentukevičius		8 March 2006
Chief Accountant	Ž. Augutis		8 March 2006

Cash flows statement

		Note	2005	2004
I.	**Cash flows from (to) operating activities**			
I.1.	Net profit (loss)		46 203	67 675
	Adjustments of non-cash items:			
I.2.	Depreciation and amortisation		90 451	44 404
I.3.	(Gain) loss on non current tangible assets, doubtful accounts receivable and inventories write-off and disposal		(687)	553
I.4.	Impairment (reversal of) of non-current tangible assets, allowance (reversal of) for doubtful accounts receivable and inventories		(774)	4 860
I.5.	Impairment (reversal of) of non-current financial assets		(1 055)	1
I.6.	Income tax expenses		5 514	12 380
I.7.	Interest (income)		(894)	(823)
I.8.	Interest expenses		2 618	6 497
I.9.	Dividends (income)		-	(2)
I.10.	Loss (gain) on foreign currency exchange		6 693	(3 419)
I.11.	Corrections on other non-cash items		(897)	(142)
			147 172	**131 984**
	Changes in working capital:			
I.12.	(Increase) decrease in inventories		(5 397)	2 071
I.13.	(Increase) decrease in trade accounts receivable		(5 552)	(7 913)
I.14.	(Increase) decrease in other accounts receivable and prepayments		1 015	(13)
I.15.	Increase (decrease) in trade accounts payable		1 455	9 465
I.16.	Increase (decrease) in other current liabilities		11 069	1 212
I.17.	Income tax (paid)		(11 376)	(12 913)
	Net cash flows from operating activities		**138 386**	**123 893**
II.	**Cash flows from (to) investing activities**			
II.1.	(Acquisitions) of non-current tangible and intangible assets		(190 929)	(83 440)
II.2.	Proceeds from sales of non-current assets		2 483	-
II.3.	Recovery of non-current loans and accounts receivable		445	603
II.4.	Proceeds from sales of financial assets		2	6
II.5.	Dividends received		-	2
II.6.	Interest received		894	823
	Net cash flows (to) investing activities		**(187 105)**	**(82 006)**

The accompanying notes are an integral part of these financial statements.

Cash flow statement (cont'd)

		Note	2005	2004
III.	**Cash flow from (to) financing activities**			
III.1.	Issue of shares	11	-	128 190
III.2.	Dividends (paid)		(32 901)	(21 993)
III.3.	Loans received		15 000	-
III.4.	Loans (repaid)		(39 855)	(93 400)
III.5.	Acquisition of held-to-maturity investments		-	(44 000)
III.6.	Proceeds from redemption of held-to-maturity investments		44 000	-
III.7.	Issue of bonds		-	29 573
III.8.	(Retirement) of bonds		-	(29 573)
III.9.	Grants (received)		32 521	28 522
III.10.	Interest (paid)		(3 099)	(7 715)
	Net cash flows from (to) financing activities		**15 666**	**(10 396)**
IV.	**Impact of currency exchange on cash and cash equivalents balance**		**754**	**(319)**
V.	**Net (decrease) increase in cash and cash equivalents**		**(32 299)**	**31 172**
VI.	**Cash and cash equivalents at the beginning of the year**		**38 351**	**7 179**
VII.	**Cash and cash equivalents at the end of the year**		**6 052**	**38 351**

The accompanying notes are an integral part of these financial statements.

General Manager	V. Valentukevičius		8 March 2006
Chief Accountant	Ž. Augutis		8 March 2006

Notes to the financial statements

1 General information

AB Lietuvos dujos (hereinafter “the Company”) is a joint stock company registered in the Republic of Lithuania. The address of its registered office is as follows:

Aguonų st. 24,
LT-03212 Vilnius,
Lithuania

The Company is engaged in transmission, distribution and supply of natural gas. The Company was registered on 1 August 1995, after reorganisation of State company Lietuvos dujos. The Company ’s shares are traded on the Current List of the Vilnius Stock Exchange.

In 2001 the Government of the Republic of Lithuania decided to privatise the Company by offering a total of 68% of the State holding in the Company in two stages and to two different investors, one of which would be a strategic investor and the other would be a natural gas supplier. The sale of 34% of the State holding to a strategic investor, Ruhrgas AG and E.ON Energie AG consortium, was agreed by the parties on 17 May 2002. Following the approval of the Government received on 12 December 2003, E.ON Energie AG transferred its holding in the Company to Ruhrgas Energie Beteiligungs AG on 18 December 2003. Ruhrgas Energie Beteiligungs AG was renamed to E.ON Ruhrgas International AG on 1 July 2004. The remaining 34% of the shares on 23 January 2004 were sold to the other investor - OAO Gazprom, the supplier of natural gas.

As of 31 December 2005 and 2004 the shareholders of the Company were as follows:

	Number of shares held	Percentage
E.ON Ruhrgas International AG	182 534 384	38.9
OAO Gazprom	173 847 696	37.1
State Property Fund	83 030 367	17.7
Other shareholders	29 655 807	6.3
	469 068 254	100.0

All the shares of the Company are ordinary registered shares with a par value of LTL 1 each and were fully paid as of 31 December 2005 and 2004. The Company did not hold its own shares.

The Company consists of an administrative and gas transmission centre and 5 natural gas distribution and supply branches.

The Company controls 100% of the shares of UAB Palangos perlas established during the restructuring in 1997. The subsidiary is running a restaurant and accommodation facilities. In these financial statements the investment into the subsidiary is carried at acquisition cost less impairment. The subsidiary was not consolidated due to its immateriality:

	As of 31 December 2005	As of 31 December 2004
Total assets of the subsidiary	14 760	6 977
Shareholders’ equity of the subsidiary	13 409	6 960
Revenue (including other income)	4 662	1 092
Net profit of the subsidiary	2 891	(16)

On 10 August 2005 the Company has increased share capital of the subsidiary by an in-kind contribution – transfer of building with a net book value of LTL 3 167 thousand and fair value of LTL 3 294 thousand, as determined by independent valuators. The subsidiary has issued 3 294 thousand shares with a par value of LTL 1 each. All shares were acquired by the Company. Net profit of the subsidiary mainly consist of the gain on the non-current tangible assets disposal (the profit of non-current tangible assets disposal amounts to LTL 3 369 thousand).

1 General information (cont'd)

The average number of employees of the Company was 1 955 in 2005 (1 968 in 2004).

Activities of AB Lietuvos Dujos are subject to regulating by the Natural Gas Law No. VIII-1973 as of 10 October 2000 of the Republic of Lithuania. Article 10 requires unbundling the accounting among the above mentioned activities of the Company. The Company has unbundled the accounting by its segments as prescribed by the Law from 1 January 2002.

Based on the provisions of the Natural Gas Law, the Company's activities are subject to licensing and regulating by the National Control Commission for Prices and Energy (hereinafter "the Commission"). On 18 December 2001 the Commission granted the Company Natural Gas Transmission and Distribution licenses and on 16 May 2002 the Commission granted a Natural Gas Supply license. The licenses have no expiration date, but are subject to meeting certain requirements and may be revoked based on the respective decision of the Commission. The Commission also sets transmission and distribution price caps as well as price caps for the regulated customers.

The management of the Company approved these financial statements on 8 March 2006. The shareholders of the Company have a statutory right to either approve the financial statements after the management's approval or not approve them and require amended financial statements.

2 Accounting principles

The principal accounting policies adopted in preparing the Company's financial statements for 2005 are as follows:

2.1. Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, except that the date of transition to IFRS as defined in IFRS 1 "First-time Adoption of International Financial Reporting Standards" has been established as the beginning of this financial year – 1 January 2005, and not 1 January 2004 as required by IFRS 1. Due to this the shareholders' equity as of 1 January 2004 and the depreciation expenses in the 2004 income statement have not been adjusted to comply with IFRS, as disclosed in the accounting policies hereafter.

IASB has issued IFRS 1 which requires that an entity's first IFRS financial statements are the first annual financial statements in which the entity adopts all IFRS, by an explicit and unreserved statement in those financial statements of compliance with IFRS. IFRS 1 requires the Company to prepare its IFRS financial statements as if it is a first-time adopter as the Company's financial statements in prior years did not have an explicit and unreserved statement of compliance with IFRS, owning to non implementation of IAS 29 "Financial Reporting in Hyperinflationary Economies" and the inclusion of indexations of non-current tangible assets, which did not meet the requirements of IAS 16 "Property, Plant and Equipment" (see section 2.4 below).

IFRS 1 requires that the Company recognised all assets and liabilities that meet the recognition criteria of IFRS and measure these assets and liabilities in accordance with each IFRS, with the prior period financial information recognised based on the same criteria. As discussed above, the Company has chosen 1 January 2005 as the date of transition to IFRS. Consequently, in its 2005 financial statements the Company has not fully implemented IFRS 1 requirements, according to which the date of transition had to be 1 January 2004 and comparative information had to be restated accordingly (the Company has only adjusted the balance sheet as of 1 January 2005, as discussed in Note 3).

2 Accounting principles (cont'd)

2.1 Basis of preparation (cont'd)

IFRSs and IFRIC Interpretations not yet effective

The Company has not applied the following IFRSs and IFRIC Interpretations that have been issued but are not yet effective and which may be applicable to the Company in the future:

- IFRIC 4 Determining whether an Arrangement contains a Lease (effective from 1 January 2006);
- IFRIC 5 Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from 1 January 2006);
- IFRIC 7 Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflatory Economies (effective from 1 March 2006);
- IFRIC 9 Reassessment of Embedded Derivatives (effective from 1 June 2006);
- Amendments to IFRS 1 First-time Adoption of IFRS and the Basis for Conclusions of IFRS 7 - Financial instruments: Disclosures (effective from 27 January 2006);
- Amendment to IAS 1 Presentation of Financial Statements - Capital Disclosures (effective from 27 January 2006);
- Amendments to IAS 39 Financial Instruments: Recognition and Measurement and IFRS 4 Insurance Contracts - Financial Guarantee Contracts (effective from 27 January 2006);
- IFRS 7 Financial Instruments: Disclosures (effective from 27 January 2006).

The Company expects that adoption of the pronouncements listed above as they become effective will not have significant impact on the financial statements.

2.2. Measurement and presentation currency

The amounts shown in these financial statements are presented in the local currency of the Republic of Lithuania, Litas (LTL).

Starting from 2 February 2002, Lithuanian Litas is pegged to EUR at the rate of 3.4528 Litas for 1 EUR, and the exchange rates in relation to other currencies are set daily by the Bank of Lithuania.

2.3. Intangible assets

Intangible assets are measured initially at cost. Intangible assets are recognised if it is probable that future economic benefits that are attributable to the asset will flow to the company and the cost of asset can be measured reliably. After initial recognition, intangible assets are measured at cost less accumulated amortisation and any accumulated impairment losses. Intangible assets are amortised on a straight-line basis over the best estimate of their useful lives (4 years). The useful lives are reviewed annually to ensure that the period of depreciation is consistent with the expected pattern of economic benefits from items of non-current intangible assets.

2.4. Non-current tangible assets

According to IFRS 1, non-current tangible assets, acquired before 1 January 2005, were measured at fair values, determined as of 1 January 2005 by independent property valuator, and these values are used as deemed cost at that date (Note 3) (except for vehicles, other equipment, tools, devices and machinery and other non-current tangible assets, which are valued at acquisition cost).

Till 1 January 2005, non-current tangible assets were accounted as follows:

- The Company's non-current tangible assets, acquired before 1 January 1996, were stated at indexed cost less indexed accumulated depreciation and impairment losses evaluated.
- Non-current tangible assets, acquired after 1 January 1996, were stated at acquisition cost less accumulated depreciation and impairment losses evaluated.

The impact of indexation to financial statements is presented in Note 6.

2 Accounting principles (cont'd)

2.4 Non-current tangible assets (cont'd)

The initial cost of non-current tangible assets, acquired prior to 1 January 2005, comprises its purchase price, including non-refundable purchase taxes and any directly attributable costs of bringing the asset to its working condition and location for its intended use.

When assets are sold or retired, their cost, accumulated depreciation and impairment are eliminated from the accounting, and any gain or loss resulting from their disposal is included in the income statement.

Depreciation is computed on a straight-line basis over the following average estimated useful lives:

	Years
Buildings	25 – 60
Transmission networks and related installations	30 – 55
Distribution networks	30 - 55
Machinery and equipment	5 – 18
Other buildings and structures	18
Vehicles	6 - 9
Other equipment, tools and devices	4 – 9
Other non-current tangible assets	6 – 9

The useful lives are reviewed annually to ensure that the period of depreciation is consistent with the expected pattern of economic benefits from items of non-current tangible assets.

Construction in progress is stated at cost. This includes the cost of construction, plant and equipment and other directly attributable costs. Construction in progress is not depreciated until the relevant assets are completed and put into operation.

The Company estimates the fair value of an asset whenever there is an indication that the asset may be impaired. An impairment loss is recognised in the income statement, whenever estimated.

The amendments to IAS 16, effective from 1 January 2005, requiring component accounting for property, plant and equipment had no significant impact on the Company's accounting, as till the implementation of the above-mentioned amendments the property, plant and equipment of the Company was accounted in detail, which approximates component accounting, in the cases of capitalised repairs, replaced item was written-off and a new one depreciated over the new estimated useful life.

2.5 Financial assets

According to IAS 39 "Financial Instruments: Recognition and Measurement" financial assets are classified as either financial assets at fair value through profit or loss, held-to-maturity investments, loans and receivables, and available-for-sale financial assets, as appropriate. All purchases and sales of financial assets are recognised on the trade date. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

<u>Financial assets at fair value through profit or loss</u>

The category 'financial assets at fair value through profit or loss' includes financial assets classified as held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Gains or losses on investments held for trading are recognised in income statement.

<u>Held-to-maturity investments</u>

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Company has the positive intention and ability to hold to maturity. Investments that are intended to be held-to-maturity are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in income statement when the investments are derecognised or impaired, as well as through the amortisation process.

2 Accounting principles (cont'd)

2.5. Financial assets (cont'd)

Loans and receivables.

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

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for-sale financial assets are measured at fair value with gains or losses (except impairment and gain or losses from foreign currencies exchange) being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the income statement.

2.6 Non-current assets held for sale

Non-current assets item is classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. Depreciation of such assets is discontinued. Non-current asset held for sale is accounted at the lower of its carrying amount and fair value less costs to sell.

2.7 Inventories

Inventories, mainly consisting of natural gas for sale that remained in the Company at the year-end and spare parts, are valued at the lower of cost or net realisable value. Cost of natural gas is determined on the basis of weighted average cost, and the cost of the remaining inventories is determined on the basis of the first-in, first-out (FIFO) method. Inventories that cannot be realised are written off.

2.8 Receivables and loans granted

Receivables are initially recorded at the fair value of the consideration given. Current receivables are subsequently carried at cost less impairment, and non-current receivables and loans granted – at amortised cost, less impairment. Allowance for doubtful receivables is based on the aging of accounts receivable and individual evaluation of the accounts.

2.9 Cash and cash equivalents

Cash includes cash on hand, cash in transit and cash in banks. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash with original maturities of three months or less and that are subject to an insignificant risk of change in value.

For the purposes of the cash flow statement, cash and cash equivalents comprise cash on hand, in transit and in banks, deposits held at call with banks, and other short-term highly liquid investments.

2.10 Borrowings

Borrowing costs are expensed as incurred.

Borrowings are initially recognised at fair value of proceeds received, less the costs of transaction. They are subsequently carried at amortised cost, the difference between net proceeds and redemption value being recognised in the net profit or loss over the period of the borrowings.

2 Accounting principles (cont'd)

2.11 Financial and operating leases

Financial lease

The Company recognises financial leases as assets and liabilities in the balance sheet at amounts equal at the inception of the lease to the fair value of the leased property or, if lower, to the present value of the minimum lease payments. The rate of discount used when calculating the present value of minimum payments of financial lease is the interest rate of financial lease payment, when it is possible to determine it, in other cases, the Company's composite interest rate on borrowings applies. Directly attributable initial costs are included into the asset value. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability.

The depreciation is accounted for financial lease assets and it also gives rise to financial expenses in the Company's income statement for each accounting period. The depreciation policy for leased assets is consistent with that for depreciable assets that are owned. The leased assets can not be depreciated over the period longer than lease term, unless the Company, according by the lease contract, gets transferred their ownership after the lease term is over.

If the result of sales and lease back transactions is financial lease, any profit from sales exceeding the book value is not recognised as income immediately. It is postponed and amortised over the lease term.

Operating lease

Leases where the lessor retains all the risk and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

The gains from discounts provided by the lessor are recognised as a decrease in lease expenses over the period of the lease using the straight-line method.

If the result of sales and lease back transactions is operating lease and it is obvious that the transaction has been carried out at fair value, any profit or loss is recognised immediately. If the sales price is lower than the fair value, any profit or loss is recognised immediately, except for the cases when the loss is compensated by lower than market prices for lease payments in the future. The profit is then deferred and it is amortised in proportion to the lease payments over a period, during which the assets are expected to be operated. If the sales price exceeds the fair value, a deferral is made for the amount by which the fair value is exceeded and it is amortised over a period, during which the assets are expected to be operated.

2.12 Grants (deferred revenue)

Grants received in the form of non-current assets or intended for the purchase, construction or other acquisition of non-current assets are considered as asset-related grants. Assets received free of charge are also allocated to this group of grants. The amount of the grants related to assets is recognised as income in the financial statements over the period of depreciation of the assets associated with this grant. In the income statement, other income account is increased by the amount of grant amortisation.

Grants received as a compensation for the expenses or unearned income of the current or previous reporting period, also, all the grants, which are not grants related to assets, are considered as grants related to income. The income-related grants are recognised as used in parts to the extent of the expenses incurred during the reporting period or unearned income to be compensated by that grant.

The balance of unutilised grants is shown under caption of "Grants (deferred revenue)" in the balance sheet.

2 Accounting principles (cont'd)

2.13 Income tax

Income tax charge is based on profit for the year and considers deferred taxation. Income tax is calculated based on the Lithuanian tax legislation.

Standard income tax rate applied for the Company is 15%. On 1 January 2006 the Provisional Social Tax Law came into effect in the Republic of Lithuania, which stipulates that along with the corporate income tax, for one financial year beginning on 1 January 2006, companies will have to pay an additional 4% tax calculated based on the income tax principles, and for the following year a 3% tax starting from 1 January 2007. After the year 2007 the income tax applied to the companies in the Republic of Lithuania will be standard, i.e. 15 %. Tax losses can be carried forward for 5 consecutive years, except for the losses incurred as a result of disposal of securities and (or) derivative financial instruments that can be carried forward for 3 consecutive years. The losses from disposal of securities and (or) derivative financial instruments can only be used to reduce the taxable income earned from the transactions of the same nature.

Deferred taxes are calculated using the balance sheet liability method. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Deferred tax assets and liabilities are measured using the tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse based on tax rates enacted or substantially enacted at the balance sheet date.

Deferred tax assets have been recognised in the balance sheet to the extent the management believes it will be realised in the foreseeable future, based on taxable profit forecasts. If it is believed that part of the deferred tax asset is not going to be realised, this part of the deferred tax asset is not recognised in the financial statements.

2.14 Revenue recognition

Revenue is recognised when it is probable that the economic benefits associated with the transaction will flow to the Company and the amount of the revenue can be measured reliably. Sales are recognised net of VAT and discounts.

Revenues from transmission, distribution and supply for industrial and commercial customers are recognised monthly based on meter readings declared by the customer and checked by the Company (accrual basis). Revenues from household customers are recognised monthly based on meter readings declared by the customers or based on the volume of gas supplied to customers but not yet declared, which approximates an accrual basis.

Fees paid by customers for connection are recognised as revenue at the time of receipt. The related costs of installation, which include cost of building property, plant and equipment and other costs, are capitalised and depreciated over the estimated useful lives of the capitalised assets.

The worldwide practice for accounting for connection fees in the utilities industry is differing where some companies record these fees as income, yet others defer it and amortise to the income statement over a number of years. In the resent years the recognition principle has been moving towards recognising such fees over the period of the expected relationship with the customer or the useful life of the connection assets. It is possible that in the future years IASB or IFRIC will address this issue, too. Because of the above the Company in the future may have to change it's accounting policy for connection fees accordingly, including the restatement of comparative figures.

2.15 Expense recognition

Expenses are recognised on the basis of accrual and revenue and expense matching principles in the reporting period when the income related to these expenses was earned, irrespective of the time the money was spent. In those cases when the costs incurred cannot be directly attributed to the specific income and they will not bring income during the future periods, they are expensed as incurred.

The amount of expenses is usually accounted as the amount paid or due to be paid, excluding VAT. In those cases when long period of payment is established and the interest is not distinguished, the amount of expenses is estimated by discounting the amount of payment using the market interest rate.

2.16 Foreign currencies

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies on the balance sheet date are recognised in the income statement. Such balances are translated at period-end exchange rates.

2 Accounting principles (cont'd)

2.17 Segment information

Business segments

The Company has four principle operating segments and one auxiliary business segment. The data on segment activities is being collected by the internal Company structural divisions and form the basis upon which the Company reports its primary segment information.

Geographical segments

All of the Company's assets are located and revenues are generated in the Republic of Lithuania.

Financial information on business segments is presented in Note 4.

2.18 Impairment of assets

Financial assets

Financial assets are reviewed for impairment at each balance sheet date.

For financial assets carried at amortised cost, whenever it is probable that the Company will not collect all amounts due according to the contractual terms of loans or receivables, an impairment or bad debt loss is recognised in the income statement. The reversal of impairment losses previously recognised is recorded when the decrease in impairment loss can be justified by an event occurring after the write-down. Such reversal is recorded in the income statement in the same article, where the impairment losses have been recognised. However, the increased carrying amount is only recognised to the extent it does not exceed the amortised cost that would have been had the impairment not been recognised.

Other assets

Other assets are reviewed for impairment whenever events or changes in circumstances indicate that carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its recoverable amount, an impairment loss is recognised in the income statement. Reversal of impairment losses recognised in prior years is recorded when there is an indication that the impairment losses recognised for the asset no longer exist or have decreased. The reversal is accounted in the same caption of the income statement as the impairment loss. For the purpose of impairment testing all Company is considered to be one cash generating unit.

2.19 Financial derivatives

Financial derivatives including foreign exchange contracts, forward rate agreements and other financial derivatives are initially recognised in the balance sheet at cost (including transaction costs) and subsequently are re-measured to their fair value with changes in fair value included in net profit or loss. Fair values are obtained from quoted market prices. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

2.20 Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with International Financial Reporting Standards requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingencies. The significant areas of estimation used in the preparation of these financial statements relate to depreciation and impairment evaluation. Future events may occur which may cause the assumptions used in arriving at the estimates to change. The effect of any changes in estimates will be recorded in the financial statements, when determinable.

2 Accounting principles (cont'd)

2.21 Contingencies

Contingent liabilities are not recognised in the financial statements. They are disclosed in financial statements unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognised in the financial statements but disclosed when an inflow or economic benefits is probable.

2.22 Subsequent events

Post-balance sheet events that provide additional information about the Company's position at the balance sheet date (adjusting events) are reflected in the financial statements. Post-balance sheet events that are not adjusting events are disclosed in the notes when material.

2.23 Offsetting and comparative figures

When preparing the financial statements, assets and liabilities, as well as revenue and expenses are not set off, except the cases when certain International Accounting Standards specifically require such set-off.

Where necessary, comparative figures have been adjusted to correspond to the presentation of the current year.

3 First – time adoption of International Financial Reporting Standards

As it is mentioned in Note 2, these financial statements prepared in accordance with IFRS are the first financial statements in which all IFRS are adopted by the Company, except that the date of transition has been established as at the beginning of this financial year – 1 January 2005, and not 1 January 2004 as required by IFRS 1. The only change between the previously applied accounting principles and the principles applied from 1 January 2005 related to the change from the indexed cost to deemed cost for accounting of non-current tangible assets, as discussed in Note 2.4. Reconciliation of equity presented in the prior year financial statements with the equity presented in the current year financial statements prepared by adopting all requirements of IFRS except one as mentioned above, is presented below:

	Equity
As presented in the financial statements for the year ended 31 December 2004	603 181
Impact of IFRS 1 adoption:	
Revaluation of non-current tangible assets at deemed cost	1 454 794
Deferred tax liability related to deemed cost accounting for non-current tangible assets (Note 20)	(222 180)
According to IFRS as of 1 January 2005	1 835 795

4 Segment information

Segment information for the years ended 31 December 2005 and 2004 is presented below :

2005	Transmission	Distribution	Supply for regulated customers	Supply for eligible customers	Other	Total
Sales	87 290	118 806	159 088	226 184	16 414	607 782
Profit from operations	(7 459)	7 900	12 474	28 896	13 869	55 680
Assets	1 484 210	692 206	32 842	19 416	15 383	2 244 057
Liabilities	265 379	65 652	41 048	16 246	6 734	395 059
Other segment information						
Acquisition of assets	141 810	44 955	46	12	449	187 272
Depreciation and amortisation	58 217	30 796	786	229	423	90 451
Impairment (reversals) of non-current assets		5	-	-	-	5
Average number of employees	363	1 357	186	12	37	1 955

4 Segment information (cont'd)

2004	**Transmission**	**Distribution**	**Supply for regulated customers**	**Supply for eligible customers**	**Other**	**Total**
Sales	84 952	111 935	156 796	130 006	12 220	495 909
Profit from operations	21 622	20 556	10 872	15 519	10 136	78 705
Assets	308 096	320 994	70 573	35 649	23 869	759 181
Liabilities	81 223	23 557	35 207	12 313	3 700	156 000
Other segment information						
Acquisition of assets	48 831	36 393	332	-	305	85 861
Depreciation and amortisation	25 034	18 296	618	118	338	44 404
Impairment (reversals) of non-current assets	4 369	483	(27)	36	(1)	4 860
Average number of employees	368	1 366	187	10	37	1 968

5 Intangible assets

Movement of intangible assets for the current period :

	Development costs	**Patents, licenses**	**Software**	**Other intangible assets**	**Total**
Cost:					
Balance as of 31 December 2004	21	1 080	4 325	2 455	7 881
Additions	-	324	526	408	1 258
Disposals	-	(29)	(134)	(204)	(367)
Balance as of 31 December 2005	**21**	**1 375**	**4 717**	**2 659**	**8 772**
Amortisation:					
Balance as of 31 December 2004	11	744	2 576	1 726	5 057
Charge for the year	5	155	619	294	1 073
Disposals	-	(29)	(134)	(204)	(367)
Balance as of 31 December 2005	**16**	**870**	**3 061**	**1 816**	**5 763**
Net book value as of 31 December 2005	**5**	**505**	**1 656**	**843**	**3 009**
Net book value as of 31 December 2004 (restated)	**10**	**336**	**1 749**	**729**	**2 824**

5 Intangible assets (cont'd)

Movement of intangible assets for the previous period :

	Development costs	Patents, licenses	Software	Other intangible assets	Total
Cost:					
Balance as of 31 December 2003	863	3 837	2 860	-	7 560
Additions	-	264	1 239	28	1 531
Disposals	(8)	(854)	(355)	-	(1 217)
Reclassifications	(46)	41	5	-	-
Balance as of 31 December 2004	809	3 288	3 749	28	7 874
Amortisation:					
Balance as of 31 December 2003	469	2 587	2 224	-	5 280
Charge for the year	195	490	309	-	994
Disposals	(8)	(854)	(355)	-	(1 217)
Reclassifications	-	(4)	4	-	-
Balance as of 31 December 2004	656	2 219	2 182	-	5 057
Net book value as of 31 December 2004 (as reported in the financial statements for the year 2004)	**153**	**1 069**	**1 567**	**28**	**2 817**
Net book value as of 31 December 2003	**394**	**1 250**	**636**	**-**	**2 280**
Corrections according to IFRS requirements					
Cost reclassification*	(788)	(2 208)	576	2 427	7
Accumulated amortisation reclassification*	(645)	(1 475)	394	1 726	-
Net book value as of 31 December 2004 (restated)	**10**	**336**	**1 749**	**729**	**2 824**

*On 1 January 2005 the Company redefined the groups of non-current intangible assets, which resulted in reclassifications of cost and accumulated amortisation.

Amortisation expenses of intangible assets are included in operating expenses in the income statement.

Part of the non-current intangible assets of the Company with the acquisition value of LTL 3 522 thousand as of 31 December 2005 (LTL 3 307 thousand as of 31 December 2004) was fully amortised but still in use.

6 Non-current tangible assets

Movement of non-current tangible assets for the current period:

	Land	Buildings	Transmission networks and related installations	Distribution networks and related installations	Other structures	Machinery and equipment	Vehicles	Other equipment, tools and devices	Construction in progress	Other non-current tangible assets	Total
Cost:											
Balance as of 1 January 2005	23	79 089	1 249 790	581 461	7 679	66 101	24 549	71 145	48 520	6 957	2 135 314
Additions	80	72	7	2 032	29	597	2 735	3 240	176 194	1 028	186 014
Disposals and retirements	-	(2 297)	-	(86)	(363)	(107)	(875)	(1 809)	(1 501)	(882)	(7 920)
Reclassifications	-	4 697	133 048	31 178	1 949	19 910	-	7 058	(197 812)	(28)	-
Balance as of 31 December 2005	**103**	**81 561**	**1 382 845**	**614 585**	**9 294**	**86 501**	**26 409**	**79 634**	**25 401**	**7 075**	**2 313 408**
Accumulated depreciation:											
Balance as of 1 January 2005	-	-	-	-	-	-	16 748	41 628	-	4 187	62 563
Charge for the year	-	2 710	43 213	21 759	674	11 017	1 908	7 520	-	577	89 378
Disposals and retirements	-	(43)	-	(8)	(29)	(84)	(840)	(1 762)	-	(817)	(3 583)
Reclassifications	-	1	-	-	-	(1)	-	-	-	-	-
Balance as of 31 December 2005		**2 668**	**43 213**	**21 751**	**645**	**10 932**	**17 816**	**47 386**	**-**	**3 947**	**148 358**
Impairment losses:											
Balance as of 1 January 2005	-	-	-	-	-	-	-	-	-	2	2
Charge for the year	-	-	-	-	-	-	-	-	5	-	5
Disposals and retirements	-	-	-	-	-	-	-	-	-	(2)	(2)
Balance as of 31 December 2005	-	-	-	-	-	-	-	-	**5**	-	**5**
Net book value as of 31 December 2005	**103**	**78 893**	**1 339 632**	**592 834**	**8 649**	**75 569**	**8 593**	**32 248**	**25 396**	**3 128**	**2 165 045**
Net book value as of 1 January 2005	**23**	**79 089**	**1 249 790**	**581 461**	**7 679**	**66 101**	**7 801**	**29 517**	**48 520**	**2 770**	**2 072 751**

6 Non-current tangible assets (cont'd)

Movement of non-current tangible assets for the previous period:

	Land	Buildings	Transmission networks and related installations	Distribution networks and related installations	Other buildings and structures	Machinery and equipment	Vehicles	Other equipment, tools and devices	Construction in progress	Other non-current tangible assets	Total
Cost, original or indexed:											
Balance as of 31 December 2003	-	65 536	325 949	369 843	19 349	119 541	23 021	50 782	19 510	2 604	996 135
Additions	23	2 848	-	1 584	15	270	2 462	3 031	73 994	103	84 330
Disposals and retirements	-	(117)	-	(84)	(251)	(3 092)	(1 443)	(2 126)	-	(269)	(7 382)
Reclassifications	-	1 944	1 524	21 462	250	9 209	303	2 875	(37 638)	71	-
Balance as of 31 December 2004	**23**	**70 211**	**327 473**	**392 805**	**19 363**	**125 928**	**24 343**	**54 562**	**55 866**	**2 509**	**1 073 083**
Accumulated depreciation:											
Balance as of 31 December 2003	-	18 933	150 410	125 090	12 513	49 897	16 295	25 899	-	1 765	400 802
Charge for the year	-	1 139	12 975	11 670	578	9 850	1 752	5 265	-	181	43 410
Disposals and retirements	-	(39)	-	(57)	(180)	(2 047)	(1 397)	(1 859)	-	(267)	(5 846)
Reclassifications	-	-	-	-	-	-	-	-	-	-	-
Balance as of 31 December 2004		**20 033**	**163 385**	**136 703**	**12 911**	**57 700**	**16 650**	**29 305**	**-**	**1 679**	**438 366**
Impairment losses:											
Balance as of 31 December 2003	-	6 010	-	-	54	198	34	183	6 904	1	13 384
Charge for the year	-	-	-	-	808	3 888	-	2	2	-	4 700
Reversals	-	(127)	-	-	-	-	-	-	-	-	(127)
Disposals and retirements	-	(6)	-	-	(54)	(926)	(34)	(183)	-	(1)	(1 204)
Balance as of 31 December 2004		**5 877**	**-**	**-**	**808**	**3 160**	**-**	**2**	**6 906**	**-**	**16 753**
Net book value as of 31 December 2004 (as reported in the financial statements for the year 2004)	23	44 301	164 088	256 102	5 644	65 068	7 693	25 255	48 960	830	617 964
Net book value as of 31 December 2003	-	40 594	175 539	244 753	6 781	69 446	6 692	24 700	12 606	838	581 949
Cost reclassification*	-	6 134	(198)	(16 854)	4 966	(15 293)	204	16 584	-	4 450	(7)
Accumulated depreciation reclassification*	-	3 403	(35)	(6 789)	2 278	(13 785)	96	12 324	-	2 508	-
Impairment reclassification*	-	(164)	-	-	164	-	-	(2)	-	2	-
Net book value as of 31 December 2004 (restated)	23	47 196	163 925	246 037	8 168	63 560	7 801	29 517	48 960	2 770	617 957
Corrections according to IFRS requirements:											
Revaluation	-	31 893	1 085 865	335 424	(489)	2 541	-	-	(440)	-	1 454 794
Net book value as of 1 January 2005	**23**	**79 089**	**1 249 790**	**581 461**	**7 679**	**66 101**	**7 801**	**29 517**	**48 520**	**2 770**	**2 072 751**

6 Non-current tangible assets (cont'd)

* On 1 January 2005 the Company redefined the groups of non-current tangible assets, which resulted in reclassifications of cost, accumulated depreciation and impairment. Comparative numbers in the balance sheet were restated accordingly.

.The depreciation of the Company's non-current tangible assets for 2005 amounts to LTL 89 378 thousand (LTL 43 410 thousand for 2004). The amount of LTL 89 299 thousand is included into operating expenses, the remaining amount is included into other activities expenses in the Company's income statement (in 2004 full amount is included into operating expenses).

Non-current tangible assets of the Company with the acquisition cost of LTL 38 501 thousand were fully depreciated as of 31 December 2005 (LTL 44 587 thousand as of 31 December 2004) but were still in use.

As of 31 December 2005 the Company had no non-current tangible assets, purchased by financial lease.

As it is mentioned in Note 2, non-current tangible assets presented in comparative information do not comply with IFRS requirements, because of accounting for non-current tangible assets acquired before 31 December 2004.

In accordance with resolutions of the Government of the Republic of Lithuania, four revaluations of non-current tangible assets were performed during a period of hyperinflation prior to 1 January 1996. Revaluations of non-current tangible assets were performed by indexing the cost and accumulated depreciation of non-current tangible assets, applying indexation rates set by the Lithuanian Government for different asset categories.

Indexation rates used for the four revaluations were as follows (depending upon the date of acquisition and category of non-current tangible assets):

Revaluation	**The range of indexes for non-current tangible assets revaluation**
Revaluation effective 1 July 1991	2.2 times
Revaluation effective 1 January 1992	2 – 5 times
Revaluation effective 1 April 1994	1.4 – 14 times
Revaluation effective 31 December 1995	1.6 – 1.7 times

The effect of these revaluations on the net book value of non-current tangible assets at the time of indexation is specified below:

Revaluation	**Increase in carrying value**	**Increase in accumulated depreciation**	**Increase in net book value**
Revaluation effective 1 July 1991	1 141	226	915
Revaluation effective 1 January 1992	19 737	3 206	16 531
Revaluation effective 1 April 1994	210 388	92 434	117 954
Revaluation effective 31 December 1995	121 839	33 543	88 296
	353 105	129 409	223 696

Because of major movements and lack of separate registrations of the effect of indexations per asset, the Company cannot quantify the remaining effect of indexation on the balance of non-current tangible assets as of 31 December 2004 (before revaluation).

On 1 January 2005, independent valuators UAB Korporacija Matininkai (licence No 000001), evaluated non-current tangible assets (including construction in progress) of the Company at fair value, which in the Company's financial statements was recognised and presented as cost.

6 Non-current tangible assets (cont'd)

Major objects of construction in progress as of 31 December 2005 were as follows:

Object	**Net book value**	**The amount of funds needed for completion of the object**
Transmission pipeline from Panevėžys to Klaipėda - increase of capacity	7 806	35 194
Reconstruction of M/R-stations (6 units)	2 690	12 070
Other	14 900	23 960
Net book value as of 31 December 2005	**25 396**	**71 224**

7 Inventories

	As of 31 December 2005	**As of 31 December 2004**
Raw materials, spare parts and other inventories	3 883	3 714
Natural gas	7 121	1 942
Inventories, gross	11 004	5 656
Less: allowance for inventories	(694)	(558)
	10 310	5 098

As of 31 December 2005, part of natural gas inventories were stored in an underground gas storage facility in Incukalnis (Latvia), amounting to LTL 3.667 thousand (none in 2004).

The cost of slow moving and obsolete inventories accounted at net realisable value amounted to LTL 694 thousand as of 31 December 2005 (LTL 558 thousand as of 31 December 2004). Changes in the allowance for inventories in 2005 and 2004 were included into operating expenses.

8 Accounts receivable

	As of 31 December 2005	**As of 31 December 2004**
Receivables for natural gas from industrial and commercial entities	44 627	40 832
Receivables for natural gas from residents	9 437	7 946
Other trade receivables	580	867
	54 644	49 645
Other accounts receivable	725	1 491
	55 369	51 136
Less: allowance for accounts receivables	(7 104)	(8 013)
	48 265	43 123

Changes in allowance for doubtful receivables in 2005 and 2004 were included into operating expenses.

9 Other current assets

	As of 31 December 2005	As of 31 December 2004
Bonds of AB SEB Vilniaus Bankas	-	24,000
Investment units of money market fund of AB Bankas Nord/LB Lietuva	-	20,000
	-	44,000

Weighted average annual interest rate of these investments was 2.16% as of 31 December 2004.

10 Cash and cash equivalents

	As of 31 December 2005	As of 31 December 2004
Cash at bank, in transit and on hand	4 320	5 295
Frozen funds	6 807	6 807
Deposits with the term of less than three months	1 732	33 056
	12 859	45 158
Less: net realisable value allowance	(6 807)	(6 807)
	6 052	38 351

Frozen funds mostly consist of the Company's cash deposited at the bank AB Litimpeks Bankas. The bank went bankrupt in 1999 and it is now administrated by UAB Valeksa. A 100% impairment adjustment is recorded for this amount. See also Note 28.

All deposits with the term of less than three months were overnight deposits as of 31 December 2005 and 2004. The annual interest rate for these deposits as of 31 December 2005 was 1.78% (1.4% - 1.99% as of 31 December 2004).

11 Share capital

There were no changes in share capital during 2005, and as of 31 December 2005 the share capital of the Company amounted to LTL 469 068 thousand.

On 25 October 2004 the Company registered the increase of share capital in the amount of LTL 128 190 419. A new emission of ordinary registered shares was issued and distributed among the existing shareholders of the Company. As of 31 December 2004 the share capital of the Company amounted to LTL 469 068 thousand.

12 Reserves

Legal reserve

A legal reserve is a compulsory reserve under legislation of the Republic of Lithuania. Annual transfers of not less than 5% of net profit are compulsory until the reserve reaches 10% of the share capital. At least an amount of LTL 2 310 thousand of the net 2005 profit must be assigned for a transfer to the legal reserve for 2005. This amount may change depending on the final decision of the shareholders of the Company to be made after the issue of these financial statements.

Other reserves

Other reserves consist of corporate business development reserve and reserve for meeting the obligations under the Collective agreement, for support and for other purposes. These reserves can be used only for the purposes approved by the General Shareholders' Meeting.

Profit distribution

The Company did not have a draft proposal of profit distribution for 2005 on the date of issue of these financial statements.

13 Grants

	As of 31 December 2005	As of 31 December 2004
Balance at the beginning of the period	29 051	671
Additions per year	32 521	28 522
Amortisation per year	(769)	(142)
Balance at end of the period	60 803	29 051

In 2005, the Company received a grant amounting to LTL 32 521 thousand, LTL 31 511 thousand of which was designated for building a transmission pipeline to Visaginas and the Ignalina Nuclear Power Plant.

The 1st reactor of the Ignalina Nuclear Power Plant was closed on 31 December 2004. The closure of the 2nd reactor of the Ignalina Nuclear Power Plant is scheduled in 2009. The construction of a new natural gas transmission pipeline from Pabradė to Visaginas and a gas distribution pipeline from Visaginas to the new heat boiler station construction is related to discontinuing of Ignalina Nuclear Power Plant activities. Since the construction of the new pipeline connection is not economically feasible due to low forecasted natural gas consumption volumes, the project was mainly financed through grant funding. During 2004 - 2005 grants in the amount of LTL 41 209 thousand were provided by the Ignalina International Decommissioning Support Fund, which is administered by the European Bank for Reconstruction and Development, and the grant amounting to LTL 18 396 thousand was provided by the Ignalina Nuclear Power Plant Decommissioning Fund administrated by the Ministry of Economy of the Republic of Lithuania. The construction of a natural gas transmission pipeline from Pabradė to Visaginas was completed in August 2005. During the implementation of the above mentioned project, an amount of LTL 1 604 thousand, allocated by Ignalina Nuclear Power Plant Decommissioning Fund, and an amount of LTL 3 505 thousand, allocated by the Ignalina International Decommissioning Support Fund were saved due to effective organisation of purchases and project management.

Grants also include non-current tangible assets received free of charge and accounted in the income statement in portions on a straight-line basis over the assets' estimated useful life.

14 Borrowings

	As of 31 December 2005	As of 31 December 2004
Non-current borrowings		
Borrowings from Lithuanian credit institutions	22 046	27 679
Borrowings from foreign credit institutions	721	26 269
	22 767	53 948
Current borrowings		
Current portion of non-current borrowings	6 859	10 845
Overdraft used	15 000	-
	21 859	10 845
	44 626	64 793

Borrowings	**Current borrowings**	**Payable after one year but not later than in five years**	**Payable after five years**
Borrowings from Lithuanian credit institutions	21 138	14 150	7 896
Borrowings from foreign credit institutions	721	721	-
	21 859	14 871	7 896

14 Borrowings (cont'd)

Terms of repayment of non-current borrowings are as follows:

	As of 31 December 2005			As of 31 December 2004		
	Non-interest bearing loans	Fixed interest bearing loans	Variable interest bearing loans	Non-interest bearing loans	Fixed interest bearing loans	Variable interest bearing loans
2005	-	-	-	2 614	5 049	3 182
2006	2 707	2 632	1 520	2 614	5 049	1 520
2007	1 628	2 632	1 520	1 535	5 049	1 520
2008	-	2 632	1 195	-	5 049	1 195
2009	-	2 632	-	-	5 049	-
2010	-	2 632	-	-	5 049	-
2011	-	2 632	-	-	5 049	-
2012	-	2 632	-	-	5 049	-
2013	-	2 632	-	-	5 049	-
2014	-	-	-	-	2 483	-
2015	-	-	-	-	2 689	-
	4 335	21 056	4 235	6 763	50 613	7 417

As of 31 December 2005 weighted average effective annual interest rate of borrowings outstanding was 4% (5.16% as of 31 December 2004). In 2004 and 2005 the periods of repricing variable interest rates on borrowings varied from 3 to 6 months.

Borrowings at the end of the year in national and foreign currencies denominated in LTL were as follows:

Borrowings denominated in:	As of 31 December 2005	As of 31 December 2004
EUR	20 043	25 834
KWD	-	27 494
USD	5 347	5 710
LTL	19 236	5 755
	44 626	64 793

15 Trade payables

	As of 31 December 2005	As of 31 December 2004
Suppliers of natural gas	42 912	38 746
Other	1 507	5 118
	44 419	43 864

16 Cost of sales

The major part (99.9%) of the cost of sales consists of the cost of natural gas in 2005 and 2004.

17 Operating expenses

	2005	2004
Salaries and social security	62 720	56 545
Depreciation and amortisation	90 372	44 404
Repairs	15 733	13 174
Taxes other than income tax	12 760	13 307
Impairment of assets	(774)	4 860
Other	31 029	33 524
	211 840	165 814

18 Other operating activities

The major part of the income from other activities consist of the gain on non-current tangible assets disposal in 2005 and of the VAT relief, related to the employment of disabled persons in prior periods, in 2004.

19 Financial and investment activities

	2005	2004
Foreign currency exchange gain, net	-	3 497
Penalty interest and penalties received	274	1 222
Interest income	894	823
Other income from financial and investment activities	7	55
Total income from financial and investment activities	1 175	5 597
Foreign currency exchange loss, net	(6 693)	-
Reversal of investment impairment	1 055	-
Interest expenses	(2 618)	(6 497)
Paid overdue interests and penalties	-	(14)
Other expenses from financial and investment activities	-	(1)
Total expenses from financial and investment activities	(8 256)	(6 512)
(Loss) from financing and investment activities, net	(7 081)	(915)

20 Income tax

	2005	2004
Income tax:		
Income for the year before income tax according to IFRS	51 717	80 055
Changes in temporary differences*	42 559	5 444
Permanent differences*	11 462	3 026
Taxable income for the year	105 738	88 525
Current income tax	15 861	13 279
Prior periods' income tax adjustment	(1 791)	(899)
Change in deferred income tax	213 624	-
Deferred income tax related to non-current tangible assets revaluation, booked directly to equity (Note 3)	(222 180)	-
Income tax expense charged to the income statement	5 514	12 380
Deferred tax assets:		
Impairment losses on construction in progress, non-current tangible assets, accounts receivable and inventories	5 147	5 788
Financial activities loss carry forward	-	1 791
Other	809	390
Deferred tax asset before valuation allowance	5 956	7 969
Less: valuation allowance	(5 956)	(7 969)
Deferred tax asset, net	**-**	**-**
Deferred tax liability:		
Revaluation of non-current tangible assets	213 624	-
Deferred tax liability, net	**213 624**	**-**

*The amounts include tax difference related to loss from derivatives, incurred in prior periods and amounting to LTL 11 938 thousand. This amount was non-deductable for income tax purposes, however in 2005 the Company was allowed by the State Tax Inspectorate to reduce income tax payable by respective tax amount of LTL 1 791 thousand.

Valuation allowance was made for part of the deferred tax asset that, in the opinion of the management, is not likely to be realised in the foreseeable future. Deferred income tax asset and deferred income tax liability are netted off in the balance sheet of the Company, as they both are related to the same tax authority.

While assessing deferred income tax asset and liability components for the year ended 31 December 2005 the Company has used income tax rates of 19 % and 18 % for those items, which will be realised in 2006 and 2007, respectively, and 15 % rate was used for the items which will be realised in 2008 and later.

20 Income tax (cont'd)

The reported amount of income tax expenses for the year can be reconciled to the amount of income tax expenses that would result from applying the statutory income tax rate of 15% to pretax income:

	2005	2004
Profit before tax	51 717	80 055
Tax (expense) at the applicable standard tax rate	(7 758)	(12 008)
Permanent differences	(1 719)	(454)
Change in deferred tax asset realisation allowance	2 013	(817)
Impact of changes in income tax rates on change in deferred tax asset realisation allowance	159	-
Effect of prior periods income tax adjustments	1 791	899
Income tax (expense)	**(5 514)**	**(12 380)**

21 Earnings per share

Basic earnings per share reflect the Company's net income, divided by the weighted average number of shares. There are no diluting instruments, therefore basic and diluted earnings per share are equal. Calculations of the basic earnings per share are presented below:

	2005	2004
Net profit attributable to the shareholders (in LTL thousand)	46 203	67 675
Weighted average number of shares (thousand) *	469 068	362 243
Basic earnings per share (in LTL)	0.10	0.19

* Weighted average number of shares in 2004: 340 878*10/12+469 068*2/12=362 243.

As there were no changes in the share capital of the Company during 2005, therefore the weighted average number of shares equals to the total number of shares.

22 Dividends

	2005	2004
Approved dividends (in LTL thousand)*	33 000	22 000
Number of shares at the date when dividends were declared (in thousand)	469 068	340 878
Approved dividends per share (LTL)	0.07	0.06

* In the year when the dividends are approved.

23 Cash generated from operations

When calculating cash flows from investing activities, the difference of accounts payable for non-current assets amounting to LTL (2 421) thousand in 2004 and LTL 3 657 thousand in 2005 was eliminated.

When calculating cash flows from operating activities, in 2005 the acquisition of the subsidiary's shares by an in-kind contribution amounting to LTL 3 294 thousand was eliminated .

Revaluation of non current tangible assets as of 1 January 2005 was also excluded from the cash flow statement (see Note 6).

24 Capital commitments

In accordance with the Natural Gas Law of the Republic of Lithuania and pursuant to the procedure approved by the order No. 201 of the Ministry of Economy of the Republic of Lithuania dated 20 June 2001, in 2002 the Company started the process of buying-out natural gas supply systems of common use owned by other legal entities and natural persons. Before this process has been launched, there were 973 km of such pipelines in Lithuania and the estimated buy-out price was in the range of approximately LTL 15 000 thousand to LTL 20 000 thousand. During 2002 - 2005 the Company has bought out pipelines for the total value of LTL 3 795 thousand. In 2006 the Company is planning to buy out pipelines for an amount of LTL 1 000 thousand.

As of 31 December 2005, capital expenditure contracted for at the balance sheet date but not recognised in the financial statements amounts to LTL 22 842 thousand.

25 Financial assets and liabilities and risk management

Credit risk

As the Company has many partners and clients, it does not face a significant credit concentration risk.

The Company does not guarantee obligations of other parties. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, if any, in the balance sheet. Consequently, the Company considers that its maximum exposure is reflected by the amount of trade receivables, net of allowance for doubtful accounts recognised at the balance sheet date.

Interest rate risk

Part of the Company's borrowings are with variable interest rates, related to VILIBOR, which creates an interest rate risk. The borrowing with variable interest rate amounts LTL 4 235 thousand and is not material.

Liquidity risk

The Company's policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of committed overdraft to meet its commitments at a given date.

25 Financial assets and liabilities and risk management (cont'd)

Foreign currency risk

Major currency risks of the Company occur due to the fact that the Company borrows foreign currency denominated funds as well as is being involved in imports and transit of natural gas. The Company did not use any financial instruments to manage its exposure to foreign currency risk in 2005. Monetary assets and liabilities denominated in various currencies as of 31 December 2005 were as follows (stated in LTL):

	Assets	**Liabilities**
LTL	54 733	39 514
EUR	11	20 043
USD	-	48 259
Total	54 744	107 816

Fair value of financial instruments

The Company's principal financial instruments not carried at fair value are trade and other receivables, investment into subsidiary, trade and other payables, long-term and short-term borrowings.

Fair value is defined as the amount at which the instrument could be exchanged between knowledgeable willing parties in an arm's length transaction, other than in forced or liquidation sale. Fair values are obtained from quoted market prices, discounted cash flow models and option pricing models as appropriate.

The following methods and assumptions are used to estimate the fair value of each class of financial instruments:

(a) The carrying amount of current trade and other accounts receivable, investments into subsidiary, current accounts payable and short-term borrowings approximates fair value.

(b) The fair value of non-current borrowings is based on the quoted market price for the same or similar issues or on the current rates available for borrowings with the same maturity profile. The fair value of non-current borrowings with variable and fixed interest rates approximates their carrying amounts.

26 Commitments and contingencies

Litigation with AB Kauno Energija

The Company, as a plaintiff, has been engaged in legal proceedings with AB Kauno Energija (defendant) in respect of penalty interest charged by the Company to the defendant for late settlement of debts for delivered natural gas and gas transportation services during the period from 5 October 1999 to 7 March 2001. The total amount of late payment fines claimed is LTL 20,165 thousand. On 4 October 2004, Kaunas District Court rejected the claim. On 25 January 2005, a decision of the Lithuanian Court of Appeal was adopted, granting a partial satisfaction, i.e. confirming a penalty for late payment in the amount of LTL 6,314 thousand and court expenses in the amount of LTL 40 thousand to be paid to AB Lietuvos dujos, the plaintiff, by AB Kauno Energija, the defendant. On 19 October 2005, the enlarged judges board of Lithuanian Supreme Court civil cases department has issued a ruling to cancel the decision made by the Lithuanian Court of Appeal on 25 January 2005 and leave in force the ruling issued on 4 October 2004 by Kaunas District Court and adjudged AB Lietuvos dujos to pay the amount of LTL 40 thousand for the execution of economical forensics and the amount of LTL 30 thousand for stamp-duty. The mentioned above claimed amount has not been recognised in the Company's balance sheets as of 31 December 2005 and 2004.

26 Commitments and contingencies (cont'd)

Litigation with National Control Commission for Prices and Energy

AB Lietuvos dujos financial results from regulated activities have been negatively affected after the National Control Commission for Prices and Energy (hereinafter the "Commission") has ex-parte approved natural gas transmission and distribution prices and prices for regulated customers for the Company effective from 1 July 2005 by the decree No 03-30, dated 30 May 2005. Three administrative trials are now in process due to the reasons above. The Company has gone to administrative court by asking to annul the following decrees of the Commission:

- decree No 03-18, dated 29 April 2005, Re: Natural gas transmission and distribution price caps and natural gas price caps for the regulated customers for AB Lietuvos dujos;
- decree No 03-30, dated 30 May 2005, Re: Natural gas transmission and distribution prices and prices for regulated customers for AB Lietuvos dujos;
- decree No 03-36, dated 30 June 2005, Re: Natural gas transmission and distribution prices and prices for regulated customers for AB Lietuvos dujos.

These three cases were merged into one. For the moment the case is stopped, as the Court based on an application of AB Lietuvos dujos has enquired the Supreme Administrative Court of Lithuania by asking to investigate whether certain clauses of Natural gas price caps calculation methodology, approved by the Commission decree No O3-15, dated 12 April 2005, do not contradict the higher-level legislation.

27 Related party transactions

The parties are considered related when one party has the possibility to control the other one or have significant influence over the other party in making financial and operating decisions. The related parties of the Company and related party transactions in 2005 and 2004 were as follows:

- E.ON Ruhrgas International AG (one of the major shareholders of the Company since 2002);
- OAO Gazprom (one of the major shareholders of the Company since 2004);
- State Property Fund (one of the major shareholders of the Company);
- UAB Palangos perlas (subsidiary of the Company).

2005	Purchases	Sales	Accounts receivable	Accounts payable
OAO Gazprom	345 694	2 501	-	42 912
	345 694	2 501	-	42 912

2004	Purchases	Sales	Accounts receivable	Accounts payable
OAO Gazprom	214 828	2 190	-	38 746
	214 828	2 190	-	38 746

In 2004, transactions with other related parties, except for the subsidiary, consisted only of dividends for 2003 paid to the shareholders. Dividends to the shareholders have been paid in 2005 as well. In addition, in 2005 the Company has increased the share capital of UAB Palangos perlas by a contribution in kind (Note 1).

Outstanding balances at the year end are unsecured, interest free and settlement occurs in cash. There have been no guarantees provided or received for any related party receivable or payable and no allowance has been made for debts relating to amounts owned by related party.

Remuneration of the management and other payments

The Company's management and related individuals' remuneration amounted to LTL 1 234 thousand in 2005 (LTL 1 000 thousand in 2004). In 2005 and 2004, the management of the Company did not receive any loans, guarantees; no other payments or property transfers were made or accrued.

28 Subsequent events

In January 2006 the Company has obtained short-term loan in amount of EUR 40,000 thousand.

Increasing prices of gas in Europe market resulted in the increase of gas price to Lithuanian consumers in the beginning of 2006. On 22 December 2005 the National Control Commission for Prices and Energy increased the prices for the regulated customers by LTL 130 Lt/1000 m3 for the first half - year of 2006. The price for different groups of regulated customers increased from 14.1% to 35.8%.

On 24 February 2006 AB Litimpeks Bankas (being administered by UAB Valeksa) transferred to the Company LTL 670 thousand, comprising 10% of total Company's funds frozen in this bank (Note 10).