

Internal audit and control system

Audit Commission

The Audit Commission oversees the Company's business operations and acts on the basis of the laws of the Russian Federation, the Charter of Russian Railways and the Regulation on the Audit Commission of Russian Railways approved by Order No. 265-r of the Russian Government dated 25 February 2004.

The Audit Commission is responsible for:

- auditing the Company's business operations for any given year and at any time as it thinks fit or as resolved by the Company's Board of Directors or requested by the shareholder;
- auditing and reviewing the Company's financial and solvency position, systems for internal control and management of financial and operational risks, asset liquidity and debt to equity ratio;
- verifying the accuracy of the Company's annual report, annual financial statements and other disclosures or financial documents;
- checking any business-related resolutions adopted by the Chief Executive Officer – Chairman of the Management Board, the Board of Directors and the Management Board of the Company for compliance with the Company's Charter and resolutions of the General Meeting of Shareholders.

The Company's Audit Commission appointed in accordance with Order No. 1395-r of the Russian Government dated 30 June 2017 consists of seven people.

The remuneration of the Audit Commission in accordance with Order No. 1395-r of the Russian Government dated 30 June 2017 was approved in the amount of RUB 2.88 m.

Members of the Audit Commission

No.	Full name	Position
1.	Natalia Annikova	Chair
2.	Alexander Varvarin	
3.	Svetlana Gorbatykh	
4.	Maxim Eronin	
5.	Boris Luboshiz	
6.	Ekaterina Suvorova	
7.	Vasily Shipilov	

Internal control and audit

Russian Railways has an internal control system in place.

Russian Railways' internal control system leverages the most up-to-date organisational and methodological framework and best international and national professional practices, operating in full compliance with the ethical standards applied by the internal audit and control functions in the Russian and global business communities.

The main objectives of the internal control system are:

- to ensure the efficiency and robustness of business operations;
- to safeguard assets and use resources in a cost effective manner;
- to identify and manage risks;
- to ensure the accuracy and completeness of financial (accounting) and other types of statements;
- to ensure compliance with the laws and regulations of the Russian Federation and by-laws of Russian Railways.

The internal control system focuses on the business operations of Russian Railways' units and the Company's business processes.

The main structures in charge of the internal control function and their responsibilities are as follows:

- governance bodies such as the Board of Directors and its Audit and Risk Committee, the Chief Executive Officer – Chairman of the Management Board of Russian Railways, relevant deputies of the Chief Executive Officer, and the Director for Internal Control and Audit are responsible for putting internal controls in place at the corporate level;
- heads of branches, departments, divisions and units are responsible for putting internal controls in place and ensuring their smooth running at the operational level;
- employees are responsible for the timely and efficient execution of the existing internal control procedures;
- in addition to implementing internal controls and ensuring their smooth running in relevant business units, certain departments and divisions are also responsible for exercising functional internal control within the given terms of reference in relation to end-to-end processes;
- special internal control structures responsible for select functions.

Russian Railways' Board of Directors and its Audit and Risk Committee determine the overall concept of the internal control system, review its performance assessment results, and analyse its actual state subject to the nature, scale and conditions of Russian Railways' operations.

Deputy Chief Executive Officer – Director for Internal Control and Audit of Russian Railways supervises the internal control and internal audit operations, with the Zheldorkontrol Internal Control Centre and the Zheldoraudit Internal Audit Centre reporting directly to the Director. These centres play a special role in the internal audit and control system of Russian Railways as they conduct independent appraisals of the business units' operations and report appraisal results to the Company's management.

The Zheldorkontrol Internal Control Centre is responsible for auditing the business operations of Russian Railways' units, performing follow-up controls and providing Russian Railways' management with reliable information about the business operations of the Company's units.

The Zheldoraudit Internal Audit Centre, a structural unit of Russian Railways, is in charge of internal audit. The objective of the internal audit function is to provide the Board of Directors and executive governance bodies with independent and objective information about the business operations, reliability and effectiveness of the risk management and internal control systems and corporate governance practices adopted by the Company and its subsidiaries.

Auditor of IFRS financial statements

The auditor of the Company's IFRS consolidated financial statements is Ernst & Young LLC.

Auditor of RAS financial statements

In accordance with Order No. 1395-r of the Russian Government dated 30 June 2017, Ernst & Young LLC was approved as the auditor of Russian Railways' financial (accounting) statements

for 2017 under the Russian Accounting Standards. The annual remuneration of Ernst & Young under the contract dated 8 August 2017 stands at RUB 25.96 m (including VAT of RUB 3.96 m).

Conflicts of interest

The conflict of interest procedures for the members of Russian Railways' Board of Directors are outlined in the Regulation on the Board of Directors of Russian Railways. Pursuant to this Regulation, the members of the Company's Board of Directors, acting reasonably and in good faith, are expected to make decisions considering all available information, in the absence of a conflict of interest. The members of the Company's Board of Directors may not use their official position and information about the Company's operations for their personal advantage or allow using the same for the personal advantage of other parties.

Besides, there is a procedure in place obliging the members of the Board of Directors to inform the Audit Commission and the Company's auditor about any legal entities, in which they independently or jointly with their affiliated person (persons) own

20 or more percent of voting shares (interests, stakes), as well as about their participation in the governance bodies of legal entities, any known or proposed transactions, in which they may be considered as interested parties, and about an intention to establish or hold interest in any entities competing with the Company.

The members of the Board of Directors must refrain from doing anything which triggers or may trigger a conflict between their interests and those of the Company.

These measures help to eliminate conflicts, enhance personal liability of the directors and mitigate legal and litigation risks of the Company, while also making it possible to duly resolve any conflicts of interest, including by way of resignation from the Board of Directors.

Anti-corruption

The Company has established a Conflict of Interest Commission (the "Commission") to facilitate coordination between the Executive Office, branches and business units of Russian Railways, improve the anti-corruption mechanisms, identify and eliminate causes of and conditions conducive to the emergence of conflicts of interest in the Company, and enhance personal liability of the Company's employees and officers for breaching the anti-corruption laws.

The Commission works in close collaboration with the Anti-Corruption Centre and other units responsible for resolving

conflicts of interest in Russian Railways, as well as with the relevant unit officers handling any such conflicts of interest.

Key functions of the Anti-Corruption Centre include organising and coordinating anti-corruption processes and procedures across Russian Railways Group, making arrangements for corruption risk assessment, developing relevant anti-corruption measures and monitoring compliance in the Company's business units.

Risk management system

Highlights

Risk monitoring and forecasting is an integral part of the strategic and operational management at Russian Railways. The Company has an effective risk management system to identify, handle and mitigate risks.

Russian Railways complies with the risk management principles of the Committee of Sponsoring Organisations of the Treadway Commission (COSO ERM: Enterprise Risk Management – Integrated Framework), ISO 31000 (Risk Management – Principles and Guidelines) and the relevant provisions of the Corporate Governance Code (Bank of Russia's Letter No. 06-52/2463 dated 10 April 2014).

The risk management system seeks to:

- ensure uninterrupted operations of Russian Railways by limiting its exposure to negative external and internal factors;
- provide a reasonable level of assurance about achieving the target benchmarks envisaged by the by-laws of Russian

Railways in the view of the Company's exposure to the external and internal factors;

- promote harmonisation based on a common methodology and unified principles taking into account the interconnectedness of risks, their mutual influences and possible implications;
- ensure integration of risk management practices as an essential part of all management processes, including strategic and operational planning;
- provide continuity by conducting regular monitoring and updating inputs for Russian Railways' risk management system;
- cover all business lines by integrating risk management procedures in all functional areas of the Company's operations, including as part of the Company's process approach to management;
- strike a reasonable balance between criteria determining the risk response, including the balance between potential losses and growth opportunities or the balance between risk management costs and potential damage caused by a risk.

Key risks of the Group

The following external risks may have the greatest impact on the Company's performance:

- weaker macroeconomic environment as compared to the outlook embedded in the Long-Term Development Programme of Russian Railways;
- insufficient indexation of tariffs against growing prices for products consumed by Russian Railways;
- no government resolutions on long-term financing of the railway transport development or a failure to implement such resolutions;
- liberalisation of the freight and passenger transportation markets.

To prevent these risks and timely respond to them, Russian Railways stays in regular contact with the Government and key customers keeping them informed about potential adverse effects of the adopted decisions. To mitigate potential risk impacts, Russian Railways enhances its customer focus and the quality of its services while also running an efficiency improvement programme.