

APPROVED

By the Board of Directors of Mechel OAO
Minutes of December 18, 2006
Chairman of the Meeting:

APPROVED

By the Chairman of the Audit Committee
of the Board of Directors of OAO Mechel

BYLAW
On the Internal Audit Function
Of Mechel OAO

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1. Purpose

This Bylaw on the Internal Audit Function (hereinafter, the “Bylaw”) is the internal document of Mechel OAO (hereinafter, the “Company”) determining the status and competence of the Internal Audit Function and the rights and obligations of its staff.

2. Range of Application

This Bylaw shall be applicable to all staff of the IAF and to all staff of other units of the Company in interaction with the IAF.

3. Regulatory References

The staff of the Internal Audit Function shall guide themselves in their activities by the Russian Federation legislation, the Standards for the Professional Practice of Internal Auditing (hereinafter, the “Standards”) and the Code of Ethics established by the International Institute of Internal Auditors, and other regulatory documentation governing the issues in the field of internal audit and internal control (requirements of the US SEC, *etc.*), the Trading Rules of Not-for-profit Partnership “RTS Stock Exchange”, the Company's Code of Labor Conduct, Code of Business Conduct and Ethics, other internal documents of the Company, and this Bylaw and the staff's duty regulations.

4. Terms and Definitions

- “Internal Audit Function” shall mean a standalone organization unit, which is independent with respect to any other units of the Company.
- “The Company Management” shall mean General Director, Deputy General Directors, and Executive Director.

5. Abbreviations

The following abbreviations are used in this Bylaw:

- CAD – Control and Audit Division
- SEC – the US Securities and Exchange Commission
- IAF – the Internal Audit Function

6. Requirements for Ensuring Independence of the IAF

With the view of ensuring independence and objectiveness of internal auditing, the IAF shall be subordinated administratively to the sole executive body, General Director, and shall be subordinated functionally, with regard to fulfillment of assignments, work, and delivery of reports on results of works fulfilled, directly to the Audit Committee of the Board of Directors of the Company (hereinafter the “Audit Committee”).

The IAF is to be established and may be liquidated by the General Director of the Company with approval of the Audit Committee.

The Internal Audit Function shall be managed by the IAF Head. Appointment to the position, terms of employment agreement (contract), and decisions on incentives (penalties) and on termination of powers of the IAF Head shall be approved by order of the General Director of the Company with approval of the Audit Committee. To be

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appointed to the position of the IAF Head, a person must have tertiary education in economics, no less than 5-year previous experience in auditing, internal control, financial and/or economic practice or accountancy, and a recognized international certificate in one of the above fields. The IAF Head shall organize and directly manage all activities of the IAF and its units. The IAF Head shall be substituted for the period of his/her temporary absence by his/her Deputy or any other person to be appointed by the General Director's order with approval of the Audit Committee.

Staff of the IAF may be appointed to and relieved from their positions by order of the General Director based on a proposal of the IAF Head.

The IAF shall not be directly responsible for operational control of those kinds of activities, which are to be examined and evaluated by the IAF. Audits to be conducted by the IAF shall not release managers and employees of audited units from responsibilities entrusted to them.

Head of the IAF and its staff may not do the following:

Carry out any functional duties in the Company not related to the internal audit activities as defined in this Bylaw, *viz*:

- developing and implementing operational and control procedures;
- maintaining accounting of the Company's operations; and
- making any managerial decisions.

Initiate or approve any transactions not related directly to the IAF's activity;

Manage activities of employees of any other units/functions except any cases when such employees are appointed to take part in fulfillment of audit assignment;

Participate in any activities that could impair equity of their assessment or could be perceived as impairing it;

Use confidential information in their own interests or in any other manner contradicting to the legislation or capable to inflict damage to the Company; and

Accept as a gift anything that could impair their professional opinion or could be perceived as impairing it.

The IAF may, with no detriment to its status as objective observer, make recommendations regarding standards of control systems, which are to be complied with in developing new systems and procedures, or conduct evaluation of existing or planned improvements, which pursue the objective of enhancing reliability of control systems and/or efficiency of operational and financial systems and respective procedures.

7. Requirements for Arranging the IAF's activities

The principal objective of the IAF's activities shall be assistance to achievement of the Company's objectives with the use of systematic, consistent, and independent from the Management approach to evaluation and enhancement of efficiency of the systems of risk management, internal control, and corporate government, and informational systems of the Company and its subsidiaries and affiliates.

To achieve the above objective, the IAF shall exercise the following functions:

Internal audit

Audit of the state of the Company's internal control system and development of

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proposals on enhancement of its reliability and efficiency in regard to the following:

- reliability and completeness of operational, accounting, tax, and managerial reporting, and the state of accounting and reporting;
- safety of the Company's assets;
- compliance by all the Company's employees and the management of its subsidiaries and affiliates with the legislative acts to which the Company's operations are subject, and the rules, standards, provisions, and other internal regulating documents of the Company;
- assessment of efficiency of conduct of financial and business operations and use of resources;
- business processes regulation;
- business processes planning and performing.

Assessment of risk management system efficiency and development of proposals for enhancing risk management system efficiency in regard to the following:

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- detection of existing risks and any possibility of appearance of any new kind of risks;
- correct assessment of risks;
- efficiency of actions undertaken to control risks;
- reporting on the state of the principal risks and actions undertaken to control them;
- compliance with the procedure of decision-making for conducting risk-related operations.

Audit of the corporate governance and informational systems existing in the Company and development of proposals for their improvement.

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Control of completeness, quality, and timeliness of elimination of any deficiencies detected earlier and realization of measures aimed to enhance efficiency of the Company's business processes.

Development, implementation, and continuous improvement of the internal audit methodology for the purpose of its correspondence to the Company's needs and requirements of the Standards of Internal Auditing, and organization of continuous work to raise professional level of the IAF staff.

Provision of consultations

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Consulting to the Company Management on the issues of risk management, control, and corporate governance.

Consulting to the Company Management on the issues of conducting financial and business operations, preparing managerial and accounting reporting, and audit of compliance with the requirements in this field.

Participation within its competence in working groups, commissions, committees, and any other consultative and advisory measures organized in the Company.

Assistance to the Company Management in developing measures (corrective steps) based on results of audits conducted and monitoring of progress in performance of such measures

Consulting to the Company employees on any issues within the competence of the IAF.

Interaction with the CAD:

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Development and realization of joint work plans for assessment of completeness and reliability of all kinds of reporting, state of accountancy and reporting, assets safety, and efficiency in use of resources.

Use of information on the level of internal control development, specificity of business processes, and employed methods of control of the Company's various units, as provided

by the CAD in the process of risk assessment, for the purpose of preparation of annual plans of the IAF's activities.

Methodological support of the CAD's activities and making recommendations to enhance efficiency of the CAD's activities.

Organization and mutual participation in round tables, seminars, training, and working projects on the issues within the area of their mutual interests.

Providing information to the CAD on any infractions in activities of the Company's units, as identified in the result of conducted audits, on their causes, and plans of corrective actions developed by the Management.

Interaction with external auditor of the Company

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Interaction with external auditor of the Company within its competence to ensure more full achievement of the objectives of the both parties in developing conclusions on the state of internal control systems in the Company so as to avoid duplicated efforts and to minimize costs of audit.

Interaction of the IAF and external auditor shall include the right of the IAF Head to address to external auditor (provided that provision of such services has been approved by the Audit Committee in advance):

- for explanations in regard to any issues reflected in opinion (report) of external auditor or any issues, which must be reflected in opinion (report) of external auditor in accordance with the legislation or terms of the contract;
- for consultations regarding assessment of the internal control systems and business risks of various business processes; and
- for consultations regarding development of organization and methods to conduct audits.

Other functions

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Assessment of efficiency of control in the area of assets safety and fraud prevention.

Assistance in investigation of frauds and informing the Audit Committee and the General Director of results of such investigations.

Maintaining interaction with the units of the Company, its subsidiaries, and affiliates on the issues related to conducting of internal audit.

Coordination of activities and maintaining interaction with any other units of the Company exercising control functions on behalf of the Management.

Fulfillment of any other assignments and participation in other projects on request of the Audit Committee and General Director of the Company.

Participation of the IAF Head in meetings of the Audit Committee (on invitation of the Committee).

8. Requirements for Developing the IAF's Plans of Activities, Budgets, and Provision of Reporting

The IAF Head shall prepare, based on the risk analysis and subject to proposals of the Company top management, the activity plan agreed on with the Audit Committee, which determines priorities of internal audit and corresponds to the Company's objectives.

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With the view of proper providing of the IAF's activity, the IAF Head shall prepare draft budget for each subsequent financial year based on the IAF's activity plan for such a year. A budget shall include labor costs, travel expenses, fees for retaining any external consultants, training and raising qualification level of the IAF's staff, and any other needs required to provide the IAF's activity.

The IAF Head shall submit the IAF's budget agreed on with the Audit Committee to the General Director for approval.

The Audit Committee and the General Director of the Company may make proposals during a year, as necessary, on conducting any additional audits and changing or supplementing the IAF's work plan. A changed work plan of the IAF has to be prepared by the IAF Head and approved at the respective nearest meeting of the Audit Committee.

Audit assignment (order to conduct audit) has to be approved by the General Director based on presentation of the IAF Head. A copy of such audit assignment (order) shall be directed to a respective Head of a unit to be audited.

The IAF has to issue a Report on the audit results containing information on goals of the audit assignment, scope of the audit, as well as description of major deficiencies, conclusions, and recommendations, not later than two weeks following the audit completion. Such Report shall be directed to the Head of an audited unit. Concurrently with the Report, Information Memorandum shall be issued containing brief conclusions and proposals for elimination of deficiencies and improvement of efficiency of the control procedures, which shall be directed to the General Director of the Company.

The IAF Head shall report to the Audit Committee on the quarterly basis as follows:

- on fulfillment of the IAF's activity plan;
- on any major deficiencies in the systems of risk management, control, and corporative management, analysis of their causes, proposals for changing control procedures in order to eliminate deficiencies and minimize negative consequences, and on results and quality of such proposals. A copy of such quarterly report shall be directed to the General Director of the Company.

The IAF Head shall inform the Audit Committee and General Director on any existing restrictions that prevent the IAF from effective fulfillment of the objectives set, as necessary.

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9. Amendments

Amendments may be introduced in this Bylaw by the Company Board of Directors on presentation of the IAF Head and/or the General Director upon their approval by the Audit Committee.

10. Responsibility

- 10.1. The IAF Head shall be entirely responsible for quality and timely fulfillment of objectives and functions vested by this Bylaw. With the view to ensure fulfillment of obligations and duty regulations by the Head and all the staff of the IAF and its units, the IAF Head shall be obliged to inform timely the General Director and the Audit Committee on any circumstances impeding fulfillment of such obligations in order to eliminate such circumstances.
- 10.2. The IAF Head and staff shall be responsible in the order and scopes as stipulated in the respective duty regulations in accordance with the effective legislation of the Russian Federation and local internal regulating documents of the Company.

11. Final Provisions

Wherever the provisions of this Bylaw may contradict to the requirements of the Charter and the Bylaw on the Audit Committee of the Company Board of Directors, the provisions of the Charter and the Bylaw on the Audit Committee shall prevail.

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Wherever the provisions of this Bylaw may contradict to the requirements of the effective Russian Federation legislation, norms of the effective legislation shall apply.

Responsibility for bringing this Bylaw in accordance with the requirements of the effective legislation, the Company Charter, and the Bylaw on the Audit Committee shall rest on the IAF Head.

Declaring any specific clauses of this Bylaw invalid shall not result in declaring invalidity of any other clauses thereof.