**OJSC SEVERNEFTEGAZPROM**

**INTERNATIONAL FINANCIAL REPORTING STANDARDS**

**FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT**

**31 DECEMBER 2011**

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# *Independent Auditor's Report*

To the Shareholders and Board of Directors of OAO Severneftegazprom

We have audited the accompanying financial statements of OAO Severneftegazprom (the "Company"), which comprise the statement of financial position as of 31 December 2011 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2011, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

23 March 2012

Moscow, Russian Federation

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**OJSC SEVERNEFTEGAZPROM**
**IFRS STATEMENT OF FINANCIAL POSITION AS OF 31 DECEMBER 2011**
**(In thousands of Russian Roubles)**

| | Notes | 31 December 2011 | 31 December 2010 |
|---|---|---|---|
| **Assets** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 7 | 10,310,569 | 17,327,805 |
| Accounts receivable | 8 | 3,009,921 | 6,004,593 |
| Prepaid profit tax | | 1,397,586 | 704,602 |
| Inventories | 9 | 491,355 | 459,286 |
| **Total current assets** | | **15,209,431** | **24,496,286** |
| **Non-current assets** | | | |
| Property, plant and equipment | 11 | 67,320,110 | 70,113,416 |
| Long-term accounts receivables | 10 | 321,669 | 394,009 |
| Other non-current assets | 12 | 7,265,111 | - |
| **Total non-current assets** | | **74,906,890** | **70,507,425** |
| **Total assets** | | **90,116,321** | **95,003,711** |
| **Liabilities and equity** | | | |
| **Current liabilities** | | | |
| Accounts payable | 13 | 698,767 | 653,752 |
| Taxes payable | 14 | 1,959,010 | 2,292,654 |
| Short-term loans and current portion of long-term debt | 15 | 6,700,896 | 40,672,914 |
| **Total current liabilities** | | **9,358,673** | **43,619,320** |
| **Non-current liabilities** | | | |
| Long-term loans | 16 | 32,625,637 | - |
| Provisions for liabilities and charges | 17 | 3,045,978 | 3,315,300 |
| Deferred tax liabilities | 14 | 5,539,667 | 3,933,780 |
| **Total non-current liabilities** | | **41,211,282** | **7,249,080** |
| **Total liabilities** | | **50,569,955** | **50,868,400** |
| **Equity** | | | |
| Share capital | 18 | 40,000 | 667 |
| Share premium | 18 | 25,099,045 | 25,138,378 |
| Other reserves | 18 | 873,253 | 873,253 |
| Accumulated profit | | 13,534,068 | 18,123,013 |
| **Total equity** | | **39,546,366** | **44,135,311** |
| **Total liabilities and equity** | | **90,116,321** | **95,003,711** |

S. E. Tsygankov
General Director
23 March 2012

Y. V. Sukhanova
Deputy Director on economics and finance
23 March 2012

**OJSC SEVERNEFTEGAZPROM**
**IFRS STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2011**
**(In thousands of Russian Roubles)**

| | Notes | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|---|
| Sales | 19 | **26,038,396** | **36,901,899** |
| Cost of sales | 20 | (12,232,974) | (9,275,190) |
| **Gross profit** | | **13,805,422** | **27,626,709** |
| General and administrative expenses | 21 | (1,308,116) | (1,480,673) |
| Research and development costs | | (102,038) | (381,248) |
| Other operating income | 22 | 7,245 | 328,528 |
| Other operating expenses | 23 | (841,350) | (1,212,651) |
| **Operating profit** | | **11,561,163** | **24,880,665** |
| Finance income | 24 | 9,084,306 | 8,447,667 |
| Finance expenses | 25 | (9,862,912) | (7,949,357) |
| **Profit before Income tax** | | **10,782,557** | **25,408,975** |
| Income tax expense | 14 | (2,171,502) | (5,521,575) |
| **Profit for the period** | | **8,611,055** | **19,887,400** |
| Other comprehensive income | | - | - |
| Income tax expense/(benefit) related to other comprehensive income | | - | - |
| **Other comprehensive income for the period, net of tax** | | - | - |
| **Total comprehensive income for the period** | | **8,611,055** | **19,887,400** |

S. E. Tsygankov
General Director
23 March 2012

Y. V. Sukhanova
Deputy Director on economics and finance
23 March 2012

**OJSC SEVERNEFTEGAZPROM**
**IFRS STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2011**
**(In thousands of Russian Roubles)**

| | Notes | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|---|
| **Profit before income tax** | | **10,782,557** | **25,408,975** |
| **Adjustments for:** | | | |
| Interest income | 24 | (693,860) | (726,089) |
| Finance expense | 25 | 2,194,370 | 2,620,855 |
| Depreciation | 20 | 2,907,898 | 2,604,941 |
| Loss on disposal of property, plant and equipment | 23 | 19,252 | 948,047 |
| Provision for revegetation | 23 | 54,738 | 86,278 |
| Net unrealised foreign exchange (gain)/loss | 24, 25 | (721,904) | (2,423,076) |
| **Operating cash flows before changes in working capital** | | **14,543,051** | **28,519,931** |
| Increase in inventories | 9 | (32,069) | (120,173) |
| Decrease (increase)in accounts receivable, excluding interest receivable | | 3,442,308 | (2,268,356) |
| (Decrease) increase in provisions, accounts payable, taxes payable, excluding interest payable and payable for acquired property, plant and equipment and exploration and evaluation service | | (1,629,006) | 1,097,561 |
| Cash paid for exploration and evaluation service | | (108,250) | (393,871) |
| Profit tax paid | | (1,258,600) | (2,756,146) |
| **Net cash provided by operating activities** | | **14,957,434** | **24,078,944** |
| **Cash flows from investing activities** | | | |
| Purchase of property, plant and equipment | | (1,012,264) | (3,203,669) |
| Proceeds from sales of property, plant and equipment | | 651 | 1,213 |
| Interest received | | 354,756 | 810,664 |
| Restricted cash | | (7,265,111) | - |
| Repayment of deposits | | - | 3,000,000 |
| **Net cash used in investing activities** | | **(7,921,968)** | **608,208** |
| **Cash flows from financing activities** | | | |
| Loans received | | 76,149,415 | 10,102,647 |
| Repayment of loans | | (77,871,039) | (26,292,532) |
| Interest paid | | (1,375,936) | (1,657,939) |
| Payment of dividends | | (12,328,795) | - |
| **Net cash used in financing activities** | | **(15,426,355)** | **(17,847,824)** |
| **(Decrease) increase in cash and cash equivalents** | | **(8,390,889)** | **6,839,328** |
| Effect of exchange rate changes on cash and cash equivalents | | 1,373,653 | (97,654) |
| **Cash and cash equivalents at the beginning of the year** | | **17,327,805** | **10,586,131** |
| **Cash and cash equivalents at the end of the year** | 7 | **10,310,569** | **17,327,805** |

S. E. Tsygankov
General Director
23 March 2012

Y. V. Sukhanova
Deputy Director on economics and finance
23 March 2012

**OJSC SEVERNEFTEGAZPROM**
**IFRS STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2011**
**(In thousands of Russian Roubles)**

| | Number of shares outstanding | Share capital | Share premium | Other reserves | Retained profit/ (Accumulated deficit) | Total equity |
|---|---|---|---|---|---|---|
| **Balance at 1 January 2010** | **533,330** | **667** | **25,138,378** | **873,253** | **(1,764,387)** | **24,247,911** |
| Profit for the period | | - | - | - | 19,887,400 | 19,887,400 |
| Other comprehensive income | | - | - | - | - | - |
| **Total comprehensive income** | | - | - | - | - | - |
| **Balance at 31 December 2010** | **533,330** | **667** | **25,138,378** | **873,253** | **18,123,013** | **44,135,311** |
| **Profit for the period** | | | | | 8,611,055 | 8,611,055 |
| Conversion of shares: | | | | | | |
| ordinary shares | - | 31,466 | (31,466) | - | - | - |
| preference shares | - | 7,867 | (7,867) | - | - | - |
| Dividends declared | - | - | - | - | (13,200,000) | (13,200,000) |
| Other comprehensive income | | - | - | - | - | - |
| **Total comprehensive income** | | - | - | - | **(4,588,945)** | **(4,588,945)** |
| **Balance at 31 December 2011** | **533,330** | **40,000** | **25,099,045** | **873,253** | **13,534,068** | **39,546,366** |

S. E. Tsygankov
General Director
23 March 2012

Y. V. Sukhanova
Deputy Director on economics and finance
23 March 2012

## 1. ACTIVITIES

The core activities of Open Joint Stock Company Severneftegazprom ("the Company") are exploration and development of the Yuzhno-Russkoye oil and gas field, production and sales of gas.

The Company was established in 2001 as a result of reorganization of limited liability company Severneftegazprom. The Company is its successor, including the rights and obligations contained in the licenses received, certificates and other constitutive documents issued by governmental and controlling bodies.

Production at the Yuzhno-Russkoye oil and gas field began in October 2007.

As at 31 December 2011 shareholders of the Company were represented by OJSC Gazprom which holds 50 percent of ordinary shares plus 6 ordinary shares, Wintershall Holding GmbH which holds 25 percent of ordinary shares minus 3 ordinary shares plus 2 class A and 1 class C preference shares and E.ON Ruhrgas E&P GmbH which holds 25 percent of ordinary shares minus 3 ordinary shares plus 3 class B preference shares. E.ON Ruhrgas E&P GmbH received ownership of shares of the Company as a result of swap transaction with the Gazprom group in 2009.

The Company holds the license for the development of Yuzhno-Russkoye oil and gas field located in the Yamalo-Nenets Autonomous District of the Russian Federation. The license expires in 2043, however it may be extended in case of increase of the period of production.

***Registered address and place of business.*** 22, Lenin street, Krasnoselkup village, Krasnoselkupskiy district, the Yamalo-Nenets Autonomous District, Tyumen region, Russian Federation, 629380.

## 2. OPERATING ENVIRONMENT OF THE COMPANY

The Russian Federation displays certain characteristics of an emerging market. Tax, currency legislation is subject to varying interpretations and contributes to the challenges faced by companies operating in the Russian Federation (Note 26).

The international sovereign debt crisis, stock market volatility and other risks could have a negative effect on the Russian financial and corporate sectors.

The future economic development of the Russian Federation is dependent upon external factors and internal measures undertaken by the government to sustain growth, and to change the tax, legal and regulatory environment. Management believes it is taking all necessary measures to support the sustainability and development of the Company's business in the current business and economic environment.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### (a) Basis of presentation

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention. The principal accounting policies applied in the preparation of the financial statements are set out below. These policies have been consistently applied to all the periods presented.

The Company is incorporated in Russia and maintains its statutory accounting records and prepares statutory financial reports in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR"); its functional and presentation currency is the Russian Rouble ("RR").

The official US dollar to RR exchange rates as determined by the Central Bank of the Russian Federation were 32.20 and 30.48 as at 31 December 2011 and 31 December 2010, respectively. The official Euro to RR exchange rates, as determined by the Central bank of the Russian Federation, were 41.67 and 40.33 as at 31 December 2011 and 31 December 2010, respectively.

**(b) Property, plant and equipment**

Property, plant and equipment comprise costs incurred in developing areas of oil and gas as well as the costs related to the construction and acquisition of oil and gas assets.

Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation and impairment where required. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the company and the cost of the item can be measured reliably.
Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components of property, plant and equipment items are capitalised and the replaced part is retired.

Property, plant and equipment include the cost of dismantling and removing the item and restoring the site on which it is located.

Borrowing costs are capitalized as part of the cost of qualifying assets during the period of time that is required to construct and prepare the asset for its intended use.

Gains and losses arising from the disposal of property, plant and equipment are included in the profit or loss as incurred. They are measured as the difference between carrying amount and disposal proceeds.

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

***Oil and gas exploration assets***

Oil and natural gas exploration and evaluation expenditures are accounted for using the "successful efforts" method of accounting. Costs are accumulated on a field-by-field basis. Geological and geophysical costs are expensed as incurred. Exploration costs are classified as research and development expenses within operating expenses. Costs directly associated with exploration wells are capitalized until the determination of reserves is evaluated. If it is determined that commercial discovery has not been achieved, these costs are charged to expense.

Capitalization is made within property, plant and equipment. Once commercial reserves are found, exploration and evaluation assets are tested for impairment and transferred to development tangible assets. No depreciation is charged during the exploration and evaluation phase.

***Depreciation***

Property, plant and equipment are depreciated from the moment when they are placed in use.

Depreciation of pipelines, wells, buildings, plant and equipment related to extraction of gas is calculated using the units-of-production method based upon proved reserves. Gas reserves for this purpose are determined mainly in accordance with the guidelines of the Society of Petroleum Engineers and the World Petroleum Congress, and were estimated by independent reservoir engineers.

Depreciation of assets not directly associated with production is calculated on a straight-line basis over their estimated useful life.
Assets under construction are not depreciated until they are placed in service.

Summary of useful lives and alternative basis for depreciation:

| | |
|---|---|
| Buildings associated with production | Units of production |
| Buildings not associated with production | 15- 31 years |
| Pipeline | Units of production |
| Plant and equipment | Units of production /1-20 years |
| Wells | Units of production |
| Roads | Units of production |
| Other | 1-20 years |

**(c) Provisions for liabilities and charges (including dismantlement provision)**

Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Provisions are reassessed at each reporting period and are included in the financial statements at their expected net present values using discount rates appropriate to the Company that reflect current market assessments of the time value of money and those risks specific to the liability that have not been reflected in the best estimate of the expenditure.

After the end of exploitation of the deposit the Company is obliged to bear costs for decommissioning of the deposit. The initial provision for decommissioning and site restoration together with any changes in estimation of the ultimate restoration liability is recorded in the statement of financial position, with a corresponding amount recorded as part of property, plant and equipment in accordance with IAS 16 “Property, Plant and Equipment”. This amount is amortised over the term of the field development.

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

**(d) Uncertain tax positions**

The Company’s uncertain tax positions (potential tax expenses and tax assets) are reassessed by management at every reporting date. Liabilities are recorded for income tax positions that are determined by management as less likely than not to be sustained if challenged by tax authorities, based on the interpretation of tax laws that have been enacted or substantively enacted by the reporting date. Liabilities for penalties, interest and taxes other than on income are recognised based on management’s best estimate of the expenditure required to settle the obligations at the reporting date.

**(e) Inventories**

Inventories are valued at the lower of the weighted average cost and net realisable value.

Cost of inventories is determined by the weighted average cost method. Cost of finished goods and work in progress includes the costs of raw materials and supplies, direct labor costs and other direct costs and related normal production overhead. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated cost of completion and selling expenses.

**(f) Components of cash and cash equivalents**

Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less.

**(g) Restricted cash**

Restricted cash balances comprise balances of cash and cash equivalents which are restricted as to withdrawal under the terms of certain borrowings or under banking regulations. Restricted cash balances are excluded from cash and cash equivalents in the statement of cash flows.

Balances restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period are included in other non-current assets.

**(h) Income taxes**

Income taxes have been provided for in the financial statements in accordance with legislation enacted or substantively enacted by the end of the reporting period. The income tax charge comprises current tax and deferred tax and is recognised in profit or loss for the year, except if it is recognised in other comprehensive income or directly in equity because it relates to transactions that are also recognised, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to, or recovered from, the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxable profits or losses are based on estimates if financial statements are authorised prior to filing relevant tax returns. Taxes other than on income are recorded within operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

**(i) Foreign currencies**

The functional and presentation currency of the Company is the national currency of the Russian Federation, Russian Roubles (“RR”).

Monetary assets and liabilities are translated into Russian Roubles at the official exchange rate of the Central Bank of the Russian Federation (“CBRF”) at the respective end of the reporting period. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into Russian Roubles at year-end official exchange rates of the CBRF are recognised in profit or loss as finance income or costs. Translation at year-end rates does not apply to non-monetary items that are measured at historical cost.

**(j) Value added tax (VAT)**

Output value added tax related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is recognized in the statement of financial position on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

**(k) Revenue recognition**

Revenues from sale of gas are recognised for financial reporting purposes when gas is delivered to customers and title passes at transfer points in accordance with the agreements on the basis of technical acceptance-handover reports. Revenues are stated net of VAT.

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, the revenue is measured at the fair value of the goods or services given up.

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

**(l) Financial assets**

The Company does not enter into derivatives contracts. Financial assets essentially consist of trade receivables, other receivables and cash and cash equivalents. These assets are carried at amortized costs.

**(m) Prepayments**

Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Company has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Company. Other prepayments are written off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying value of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss for the year.

**(n) Impairment of financial assets carried at amortized cost.**

Impairment of the financial assets carried at amortized cost: impairment losses are recognized in profit and loss when incurred as a result of one or more events (loss events) that occurred after the initial recognition of the financial asset and which have an impact on amount or timing of the estimated future cash flows of the financial assets or group of the financial assets that can be reliable estimated.

The primary factors that the Company considers in determining whether a financial asset is impaired are its overdue status and realisability of related collateral, if any. The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any portion or instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the counterparty experiences a significant financial difficulty as evidenced by its financial information that the Company obtains;
- the counterparty considers bankruptcy or a financial reorganisation;
- there is adverse change in the payment status of the counterparty as a result of changes in the national or local economic conditions that impact the counterparty; or
- the value of collateral, if any, significantly decreases as a result of deteriorating market conditions.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

The accounts receivable impairment provision is created on the base of the management assessment of collectability of customers accounts according to contracts concluded. The indicators of accounts receivable impairment are financial difficulties of debtors, insolvency of customers, the presence of outstanding debts or delay in payment schedule (more than 12 months). Impairment losses are recognized in the profit or loss and recorded as "Other operating expenses".

**(o) Borrowings**

Borrowings are recognized initially at fair value, net of transaction costs incurred. In subsequent periods, borrowings are stated at amortized cost using the effective interest method; any difference between the amount at initial recognition and the redemption amount is recognized as interest expense over the period of the borrowings.

Borrowings received from shareholders are recognized initially at fair value, net of transaction costs incurred. The difference between the fair value of the loan and the amount of funds as at the receipt date is treated as an addition to equity and recorded in "Other reserves" (refer to 18).

**(p) Pension liabilities**

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

During 2009 the Company has started implementation of the non-State pension program. All the employees of the

Company have the right to receive pension benefits from the non-State pension fund by achieving the pension age. The contributions to the non-State pension plan, which is a defined contribution plan, are expensed when incurred. The Company has no legal or constructive obligation to make pension or similar benefit payments beyond the payments to the Russian Federation State pension fund and non-State pension program.

**(q) Social liabilities**

Social costs relating to the maintenance of housing are expensed when incurred.
Discretionary and voluntary payments made to support social programs and related operations are expensed as incurred.

**(r) Non-cash transactions**

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

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

**(s) Trade and other payables**

Trade payables are accrued when the counterparty performs its obligations under the contract and are carried at amortized cost using the effective interest method

**(t) Trade and other receivables**

Trade and other receivables are carried at amortized cost using the effective interest method.

**(u) Equity**

***Share capital***

Share capital consists of ordinary and non redeemable preference shares, which are classified as equity.

The excess of consideration received over the face-value of issued shares is recorded as a share premium in the statement of changes in equity.

**(v) Dividends**

Dividends are payable only with the respective decision of shareholders. Dividends are recorded as a liability and deducted from equity in the period in which they are declared and approved. Any dividends declared after the reporting period and before the financial statements are authorized for issue are disclosed in the subsequent events note.

**(w) New Accounting Developments**

***Adoption of new or Revised Standards and Interpretations***

Certain new standards and interpretations have been published that are mandatory for the Company's accounting periods beginning on or after 1 January 2011 or later periods and which are relevant to its operations.

(a) Standards effective for annual periods beginning on or after 1 January 2011

Amendment to IAS 24, Related Party Disclosures (issued in November 2009 and effective for annual periods beginning on or after 1 January 2011). IAS 24 was revised in 2009 by: (a) simplifying the definition of a related party, clarifying its intended meaning and eliminating inconsistencies; and by (b) providing a partial exemption from the disclosure requirements for government-related entities. The amendments did not have a material impact on Company's financial statements.

Improvements to International Financial Reporting Standards (issued in May 2010 and effective from 1 January 2011). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: IFRS 1 was amended (i) to allow previous GAAP carrying value to be used as deemed cost of an item of property, plant and equipment or an intangible asset if that item was used in operations subject to rate regulation, (ii) to allow an event driven revaluation to be used as deemed cost of property, plant and equipment even if the revaluation occurs during a period covered by the first IFRS financial statements and (iii) to require a first-time adopter to explain changes in accounting policies or in the IFRS 1 exemptions between its first IFRS interim report and its first IFRS financial statements; IFRS 3 was amended (i) to require measurement at fair value (unless another measurement basis is required by other IFRS standards) of non-controlling interests that are not present ownership interest or do not entitle the holder to a proportionate share of net assets in the event of liquidation, (ii) to provide guidance on the acquiree's share-based payment arrangements that were not replaced, or were voluntarily replaced as a result of a business combination and (iii) to clarify that the contingent considerations from business combinations that occurred before the effective date of revised IFRS 3 (issued in January 2008) will be accounted for in accordance with the guidance in the previous version of IFRS 3; IFRS 7 was amended to clarify certain disclosure requirements, in particular (i) by adding an explicit emphasis on the interaction between qualitative and quantitative disclosures about the nature and extent of financial risks, (ii) by removing the requirement to disclose carrying amount of renegotiated financial assets that would otherwise be past due or impaired, (iii) by replacing the requirement to disclose fair value of collateral by a more general requirement to disclose its financial effect, and (iv) by clarifying that an entity should disclose the amount of foreclosed collateral held at the reporting date, and not the amount obtained during the reporting period; IAS 1 was amended to clarify the requirements for the presentation and content of the statement of changes in equity; IAS 27 was amended by clarifying the transition rules for amendments to IAS 21, 28 and 31 made by the revised IAS 27 (as amended in January 2008); IAS 34 was amended to add additional examples of significant events and transactions requiring disclosure in a condensed interim financial report, including transfers between the levels of fair value hierarchy, changes in classification of financial assets or changes in business or economic environment that affect the fair values of the entity's financial instruments; and IFRIC 13 was amended to clarify measurement of fair value of award credits. The amendments did not have a material impact on Company's financial statements.

Other revised standards and interpretations effective for the current period. IFRIC 19 "Extinguishing financial liabilities with equity instruments", amendments to IAS 32 on classification of rights issues, clarifications in IFRIC 14 "IAS 19 - The limit on a defined benefit asset, minimum funding requirements and their interaction" relating to prepayments of minimum funding requirements and amendments to IFRS 1 "First-time adoption of IFRS", did not have any impact on these financial statements.

(b) Standards, amendments and interpretations to existing Standards that are not yet effective and are not relevant to the Company's operations:

- IFRS 10, Consolidated Financial Statements (issued in May 2011 and effective for annual periods beginning on or after 1 January 2013), replaces all of the guidance on control and consolidation in IAS 27 "Consolidated and separate financial statements" and SIC-12 "Consolidation - special purpose entities". IFRS 10 changes the definition of control so that the same criteria are applied to all entities to determine control. This definition is supported by extensive application guidance.
- IFRS 11, Joint Arrangements, (issued in May 2011 and effective for annual periods beginning on or after 1 January 2013), replaces IAS 31 "Interests in Joint Ventures" and SIC-13 "Jointly Controlled Entities—Non-Monetary Contributions by Ventures". Changes in the definitions have reduced the number of types of joint arrangements to two: joint operations and joint ventures. The existing policy choice of proportionate consolidation for jointly controlled entities has been eliminated.
- IFRS 12, Disclosure of Interest in Other Entities, (issued in May 2011 and effective for annual periods beginning on or after 1 January 2013), applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity.
- IAS 27, Separate Financial Statements, (revised in May 2011 and effective for annual periods beginning on or after 1 January 2013), was changed and its objective is now to prescribe the accounting and disclosure requirements for investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements.
- IAS 28, Investments in Associates and Joint Ventures, (revised in May 2011 and effective for annual periods beginning on or after 1 January 2013). The amendment of IAS 28 resulted from the Board's project on joint ventures. When discussing that project, the Board decided to incorporate the accounting for joint ventures using the equity method into IAS 28 because this method is applicable to both joint ventures and associates.
- Disclosures—Transfers of Financial Assets – Amendments to IFRS 7 (issued in October 2010 and effective for annual periods beginning on or after 1 July 2011). The amendment requires additional disclosures in respect of risk exposures arising from transferred financial assets.
- Other revised standards and interpretations: The amendments to IFRS 1 "First-time adoption of IFRS", relating to severe hyperinflation and eliminating references to fixed dates for certain exceptions and exemptions, the amendment to IAS 12 "Income taxes", which introduces a rebuttable presumption that an investment property carried at fair value is recovered entirely through sale, and IFRIC 20, "Stripping Costs in the Production Phase of a Surface Mine", which considers when and how to account for the benefits arising from the stripping activity in mining industry, will not have any impact on these financial statements.

c) Standards, amendments and interpretations to existing standards that are not effective and have not been early adopted by the Company.

- IFRS 9, Financial Instruments: Classification and Measurement. IFRS 9, issued in November 2009, replaces those parts of IAS 39 relating to the classification and measurement of financial assets. IFRS 9 was further amended in October 2010 to address the classification and measurement of financial liabilities and in December 2011 to (i) change its effective date to annual periods beginning on or after 1 January 2015 and (ii) add transition disclosures. The application of this standard is not expected to have material effect on the Company's financial statement.
- IFRS 13, Fair value measurement, (issued in May 2011 and effective for annual periods beginning on or after 1 January 2013), aims to improve consistency and reduce complexity by providing a revised definition of fair value, and a single source of fair value measurement and disclosure requirements for use across IFRSs. The application of this standard is not expected to have material effect on the Company's financial statement.
- Amendments to IAS 1, Presentation of Financial Statements (issued June 2011, effective for annual periods beginning on or after 1 July 2012), changes the disclosure of items presented in other comprehensive income. The amendments require entities to separate items presented in other comprehensive income into two groups, based on whether or not they may be reclassified to profit or loss in the future. The suggested title used by IAS 1 has changed to 'statement of profit or loss and other comprehensive income'. The Company expects the amended standard to change presentation of its financial statements, but have no impact on measurement of transactions and balances.
- Amended IAS 19, Employee Benefits (issued in June 2011, effective for periods beginning on or after 1 January 2013), makes significant changes to the recognition and measurement of defined benefit pension expense and termination benefits, and to the disclosures for all employee benefits. The standard requires recognition of all changes in the net defined benefit liability (asset) when they occur, as follows: (i) service cost and net interest in profit or loss; and (ii) remeasurements in other comprehensive income. The application of this standard is not expected to have material effect on the Company's financial statement.
- Disclosures—Offsetting Financial Assets and Financial Liabilities - Amendments to IFRS 7 (issued in December 2011 and effective for annual periods beginning on or after 1 January 2013). The amendment requires disclosures that will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off. The amendment will have an impact on disclosures but will have no effect on measurement and recognition of financial instruments.
  Offsetting Financial Assets and Financial Liabilities - Amendments to IAS 32 (issued in December 2011 and effective for annual periods beginning on or after 1 January 2014). The amendment added application guidance to IAS 32 to address inconsistencies identified in applying some of the offsetting criteria. This includes clarifying the meaning of 'currently has a legally enforceable right of set-off' and that some gross settlement systems may be considered equivalent to net settlement. The application of this standard is not expected to have material effect on the Company's financial statement.

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Company makes estimates and assumptions that affect the amounts recognised in the financial statements and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

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

***Useful lives of property, plant and equipment.*** Items of property, plant and equipment are stated at cost less accumulated depreciation. The estimation of the useful life of an item of property, plant and equipment is a matter of management judgment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any of these conditions or estimates may result in adjustments to future depreciation rates.

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***Classification of production licenses***. Management treats cost of production licenses as cost of acquisition of oil and gas properties, accordingly, production licenses are included in property, plant and equipment in these financial statements.

***Site restoration and environmental costs.*** Site restoration costs that may be incurred by the Company at the end of the operating life of certain of the Company facilities and properties are recognized when the Company has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. The cost is depreciated through the profit and loss on an units of production basis. Changes in the measurement of an existing site restoration obligation that result from changes in the estimated timing or amount of the outflows, or from changes in the discount rate adjust the cost of the related asset in the current period. IFRS prescribes the recording of liabilities for these costs. Estimating the amounts and timing of those obligations that should be recorded requires significant judgment. This judgment is based on cost and engineering studies using currently available technology and is based on current environmental regulations. Liabilities for site restoration are subject to change because of change in laws and regulations, and their interpretation.

***Reserves estimation.*** Unit-of-production depreciation charges are principally measured based on Company's estimates of proved reserves. Proved reserves are estimated by reference to available geological and engineering data and only include volumes for which access to market is assured with reasonable certainty. Estimates of gas reserves are inherently imprecise, require the application of judgment and are subject to regular revision, either upward or downward, based on new information such as from the drilling of additional wells, observation of long-term reservoir performance under producing conditions and changes in economic factors, including product prices, contract terms or development plans. Changes to Company's estimates of proved reserves affect prospectively the amounts of depreciation charged and, consequently, the carrying amounts of production assets. The outcome of, or assessment of plans for, exploration or appraisal activity may result in the related exploration drilling costs. Information about the carrying amounts of production assets and the amounts of depreciation charged to the profit or loss is presented in Note 11.

## 5. FINANCIAL RISK MANAGEMENT

The Company's activities expose it to a variety of financial risks, including market risk (currency risk, fair value interest rate risk and cash flow interest rate risk), credit risk and liquidity risk. The Company's overall risk management focuses on minimising potential adverse effects on the financial performance of the Company.

### *a) Market risk*

***(i) Foreign exchange risk.*** The Company has a substantial amount of foreign currency denominated borrowings and thus, is exposed to foreign exchange risk arising from various exposures with respect to the US dollar and to the Euro. Foreign currency denominated assets and liabilities give rise to foreign exchange risk exposure.

The table below summarized the Company's exposure to foreign currency exchange rate risk at the end of reporting period. Financial assets and liabilities in foreign currencies, denominated in thousand of RR:

| | **US$** | **Euro** |
|---|---:|---:|
| **31 December 2011** | | |
| Cash and cash equivalents | 404 | 9,049 |
| Advances to suppliers | - | - |
| Other receivables | 1,253 | 3,932 |
| Other non-current assets | 1,924,346 | 1,795,991 |
| **31 December 2011** | | |
| Borrowings | 17,940,182 | 16,743,561 |
| Interest payable | 43,011 | 53,398 |
| Payables to related parties | - | - |
| Trade and other payables | - | - |

| | US$ | Euro |
|---|---|---|
| **31 December 2010** | | |
| Cash and cash equivalents | 469 | 182,003 |
| Advances to suppliers | 17,872 | 7,523 |
| Other receivables | - | - |
| **31 December 2010** | | |
| Borrowings | 32,917,619 | 7,755,294 |
| Interest payable | 12,322 | 4,262 |
| Payables to related parties | 6,333 | 1,493 |
| Trade and other payables | 2,852 | 15,741 |

As at 31 December 2011, if the Russian Rouble had weakened by 5 percent against the US dollar with all other variables held constant, profit before tax would have been lower by RR 802,860 thousand (as at 31 December 2010 loss would be lower by RR 1,645,423 thousand), mainly as a result of foreign exchange losses on translation of US dollar denominated borrowings and foreign exchange gains on translation of US dollar denominated cash and cash equivalents. The effect of a corresponding strengthening of the Russian Rouble against the US dollar is approximately equal and opposite.

As at 31 December 2011, if the Russian Rouble had weakened by 10 percent against the Euro with all other variables held constant, profit before tax would have been lower by RR 1,498,799 thousand (as at 31 December 2010 loss would be lower by RR 758,300 thousand), mainly as a result of foreign exchange losses on translation of Euro denominated borrowings and foreign exchange gains on translation of Euro denominated cash and cash equivalents. The effect of a corresponding strengthening of the Russian Rouble against the Euro is approximately equal and opposite.

***(ii) Cash flow and fair value interest rate risk.*** The Company principal interest rate risk arises from long-term and short-term borrowings. Borrowings issued at variable rates expose the Company to cash flow interest rate risk. Borrowings issued at fixed rates expose the Company to fair value interest rate risk.

To mitigate this risk, the Company performs periodic analysis of the current interest rate environment. Financial decisions of management may include re-financing and prolongation of loan agreements as well as other methods of financing.

The Company does not hedge its cash flow and fair value interest rate risk.

As at 31 December 2011, if interest rates on US dollar denominated borrowings at these dates had been on 5 percent share higher than with all other variables held constant, profit before tax would have been lower by RR 25,565 thousand (as at 31 December 2010 loss would be higher by RR 22,096 thousand), mainly as a result of higher interest expense on floating rate borrowings. The effect of a corresponding decrease in interest rate is approximately equal and opposite.

As at 31 December 2011, if interest rates on Euro denominated borrowings at these dates had increased by 5 percent (for example: 10 percent would become 10.5 percent) with all other variables held constant, profit before tax would have been lower by RR 31,701 thousand (as at 31 December 2010 loss would be higher by RR 7,635 thousand), mainly as a result of higher interest expense on floating rate borrowings. The effect of a corresponding decrease in interest rate is approximately equal and opposite.

As at 31 December 2011, interest rate on RR-denominated borrowings is fixed. As at 31 December 2010 the Company does not have Roubles-denominated borrowings.

***b) Credit risk.*** Credit risk arises from cash and cash equivalents, deposits with banks and financial institutions as well as credit exposures to customers, including outstanding trade receivables. The banks with which the Company places funds have insignificant risk of default since the Company places its funds in highly rated leading foreign banks and Russian banks with state participation which minimizes the risk of default. As the main debtors of the Company are the Gazprom Group entities, management believes that the credit risk is low. Receivables from related parties relate to sales performed in 2011 and the Company has no past due nor impaired receivable as at 31 December 2011 and defaults are historically rare.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the statement of financial position (see notes 7, 8, 10, 12).

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***c) Credit risks concentration.*** The Company is exposed to concentrations of credit risk. As at 31 December 2011 the Company had three counterparties (2010: three counterparties) with the total aggregate amount of these balances RR 3,185,219 thousand (2010: RR 6,141,624 thousand) or 96 % of the gross amount of trade and other receivables (2010: 87 %).
In 2011 the Company's bank deposits are held in several bank accounts with different banks. In 2010 the Company's bank deposits are held only with two banks thus exposing the Company to a concentration of credit risk.

***d) Liquidity risk.*** The Company's liquidity management objective involves projecting cash flows in major currencies and considering the level of liquid assets necessary to meet these and maintaining debt financing plans.

The table below analyses the Company's liabilities into relevant maturity grouping based on the remaining period in the statement of financial position date to contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows which include future interest payments. These amounts will not reconcile to the amounts disclosed on statement of financial position for borrowings, as these amounts are measured at amortised cost.

| | **within 1 year** | **from 1 to 5 years** | **over 5 years** |
|---|---|---|---|
| **31 December 2011** | | | |
| Borrowings | 6,758,310 | 24,931,638 | 10,125,460 |
| Interest payable | 1,668,654 | 3,842,112 | 509,714 |
| Trade payables | 190,599 | - | - |
| Payables to related parties | 41,025 | - | - |
| Other payables and accruals | 528 | - | - |
| | **8,659,116** | **28,773,750** | **10,635,174** |

| | **within 1 year** |
|---|---|
| **31 December 2010** | |
| Borrowings | 40,672,914 |
| Interest payable | 754,538 |
| Trade payables | 231,260 |
| Payables to related parties | 138,846 |
| Other payables and accruals | 5,130 |
| | **41,802,688** |

***e) Capital management.*** The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The Company monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings, as shown in the statement of financial position, less cash and cash equivalents and restricted cash. Total capital is calculated as equity, as shown in the statement of financial position, plus net debt.

The gearing ratios as at 31 December 2011 and 31 December 2010 were as follows:

| | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Total borrowings | 39,326,533 | 40,672,914 |
| Less: cash and cash equivalents | (10,310,569) | (17,327,805) |
| Less: other long-term non-current assets | (7,265,111) | - |
| Net debt | **21,750,853** | **23,345,109** |
| Total equity | 39,546,366 | 44,135,311 |
| Total capital | **61,297,219** | **67,480,420** |
| **Gearing ratio** | **35 percent** | **35 percent** |

Company's current gearing ratio for 2011 is 35 percent. As at 31 December 2011 and as at 31 December 2010 this target was met by the Company.

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## 6. FINANCIAL INSTRUMENTS BY CATEGORY

| **Assets at amortized cost** | **31 December 2011** | **31 December 2010** |
|---|---|---|
| **Current assets** | | |
| Cash and cash equivalents | 10,310,569 | 17,327,805 |
| Receivables from related parties | 2,877,473 | 5,760,564 |
| Other short-term receivables | 82,720 | 155,220 |
| **Non-current assets** | | |
| Long-term receivables from related parties | 309,439 | 381,780 |
| Long-term other receivables | 12,230 | 12,230 |
| Other non-current assets | 7,265,111 | - |
| | **20,857,542** | **23,637,599** |

| **Liabilities at amortized cost** | **31 December 2011** | **31 December 2010** |
|---|---|---|
| **Current liabilities** | | |
| Short-term loans and current portion of long-term debt | 6,700,896 | 40,672,914 |
| Trade payables | 190,599 | 231,260 |
| Interest payable | 144,657 | 16,583 |
| Payables to related parties | 41,025 | 138,846 |
| Other payables and accruals | 7,914 | 5,131 |
| **Long-term liabilities** | | |
| Long-term loans | - | - |
| | **7,085,091** | **41,064,734** |

## 7. CASH AND CASH EQUIVALENTS

| | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Current accounts | 9,223,409 | 190,585 |
| Deposit accounts | 1,087,160 | 17,137,220 |
| | **10,310,569** | **17,327,805** |

As at 31 December 2011 cash in the amount of RR 1,078,090 thousand was placed on deposit accounts in Vneshprombank, RR 133 thousand was placed on deposit accounts in Rosbank, Euro 206 thousand was placed on deposit accounts in ING bank NV and US Dollar 12 thousand was placed on deposit accounts in ING bank NV.

As at 31 December 2010 cash in the amount of RR 4,683,980 thousand was placed on deposit accounts in Banque Societe Generale Vostok and the amount of RR 12,453,240 thousand was placed on deposit accounts in Gazprombank.

As at 31 December 2011 the weighted average interest rate on the cash balances of the Company was 5.50 percent for RR, 1.33 percent for Euro, 0.41 percent for US Dollar (31 December 2010 – 3.72 percent for RR).

The table below shows analysis of cash and cash equivalents and presents balance of major Company's counterparties at the reporting date.

| | | | | **31 December 2011** | **31 December 2010** |
|---|---|---|---|---|---|
| | **Rating** | **Rating agency** | **Credit limit for one bank** | **Balance** | **Balance** |
| Rosbank | Baa2 | Moody's | Not set | 133 | 4,684,486 |
| Credit Agricole | Aa3 | Moody's | Not set | 9,219,048 | - |
| ING bank NV | Aa3 | Moody's | Not set | 9,452 | - |
| Gazprombank | Baa3 | Moody's | Not set | 3,846 | 12,643,319 |
| Vneshprombank | B2 | Moody's | Not set | 1,078,090 | |
| | | | | **10,310,569** | **17,327,805** |

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The table below shows analysis of restricted cash (Note 12):

| | | | | 31 December 2011 | 31 December 2010 |
|---|---|---|---|---|---|
| | Rating | Rating agency | Credit limit for one bank | Balance | Balance |
| Credit Agricole | Aa3 | Moody's | Not set | 3,000,000 | - |
| ING bank NV | Aa3 | Moody's | Not set | 4,265,111 | - |
| | | | | **7,265,111** | **-** |

## 8. ACCOUNTS RECEIVABLE

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| **Financial assets** | | |
| Receivables from related parties (see note 27) | 2,877,473 | 5,760,564 |
| Other receivables | 132,071 | 204,813 |
| Impairment provision for other receivables | (49,351) | (49,593) |
| | **2,960,193** | **5,915,784** |
| **Non-financial assets** | | |
| Advances to suppliers | 9,372 | 45,241 |
| Impairment for advances to supplies | (1,309) | - |
| VAT recoverable | 36,249 | 36,755 |
| Prepaid taxes, other than income tax | 5,416 | 6,813 |
| | **49,728** | **88,809** |
| | **3,009,921** | **6,004,593** |

As at 31 December 2011 other receivables of RR 49,351 thousand and advances to suppliers of RR 1,309 thousand were impaired and provided for. As at 31 December 2010 other receivables of RR 49,593 thousand were impaired and provided for. The ageing analysis of these receivables and advances are as follows:

**Aging from the due date**

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| Up to 360 days overdue | - | 32,064 |
| From 1 to 3 years overdue | 33,465 | 17,105 |
| More than 3 years overdue | 17,195 | 424 |
| | **50,660** | **49,593** |

Movements of the provision for impairment of other accounts receivable and advances to supplies are as follows:

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| Impairment provision at the beginning of the year | (49,593) | - |
| Impairment provision accrued | (1,067) | (49,593) |
| **Impairment provision at the end of the year** | **(50,660)** | **(49,593)** |

All receivables that are past due are fully provided against as at 31 December 2011 and 31 December 2010.

As the principal debtors of the Company are related parties, the Company believes that the default risk is low and, therefore, does not establish provision for impairment of these receivables. No receivables from related parties were past due or impaired as at 31 December 2011.

The fair value of accounts receivable as at 31 December 2011 and 31 December 2010 approximates their carrying value.

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## 9. INVENTORIES

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| Materials and supplies | 485,182 | 454,198 |
| Other materials | 6,173 | 5,088 |
| | **491,355** | **459,286** |

## 10. LONG-TERM ACCOUNTS RECEIVABLE

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| **Financial assets** | | |
| Receivables from related parties (see note 27) | 309,439 | 381,779 |
| Other receivables | 12,230 | 12,230 |
| | **321,669** | **394,009** |

Long-term accounts receivable are initially recognized in the statement of financial position at fair value. The difference between the fair value of the long-term accounts receivable and the amount of cash received was recorded in the profit or loss. As at 31 December 2011 receivables from related parties in the amount of RR 309,439 (31 December 2010 – RR 381,779) represents receivables from OJSC “Gazprom” in relation to compensation of losses caused by default in its contractual obligation to purchase a set volume of gas in 2009, to be paid in equal amounts over 5 years starting from December 2011.

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## 11. PROPERTY, PLANT AND EQUIPMENT

| | Pipeline | Wells | Buildings and facilities | Machinery and equipment | Roads | Other | Assets under construction | Total |
|---|---|---|---|---|---|---|---|---|
| **Cost at 1 January 2010** | **9 712 365** | **10 188 620** | **25 416 957** | **3 910 014** | **12 941 466** | **47 491,000** | **10 141 665** | **72 358 578** |
| Additions | - | - | 549 | 81,470 | - | 1,557 | 3,290,005 | 3,373,581 |
| Net change in component for decommissioning and site restoration obligation (Note 17) | 147 | 406 | - | 64 063 | - | - | - | 617 |
| Disposals | - | (2,359) | (7) | (15,061) | - | - | (972,905) | (990,332) |
| Transfers | 4,268 | 492,078 | 3,516,112 | 5,378,271 | 743,459 | 2,619 | (10,136,807) | - |
| **Cost at 31 December 2010** | **9,863,369** | **11,084,236** | **28,933,611** | **9,418,757** | **13,684,925** | **51,667,000** | **2,321,958** | **75,358,523** |
| Additions | - | - | 414 | 103,028 | - | 44,303 | 886,525 | 1,034,270 |
| Net change in component for decommissioning and site restoration obligation (Note 17) | (197,283) | (1,259,347) | 1,057,089 | (92,498) | - | - | - | (492,039) |
| Impairment of PPE | - | - | - | - | - | - | (380,068) | (380,068) |
| Disposals | - | - | - | (18,191) | - | (1,899) | (6,376) | (26,466) |
| Transfers | - | - | 368,420 | 17,582 | - | 1,586 | (387,589) | - |
| **Cost at 31 December 2011** | **9,666,086** | **9,824,889** | **30,359,534** | **9,428,678** | **13,684,925** | **95,656** | **2,434,451** | **75,494,220** |
| **Accumulated depreciation at 1 January 2011** | **(418,384)** | **(379,880)** | **(1,110,381)** | **(358,890)** | **(278,384)** | **(17,033)** | **-** | **(2,562,952)** |
| Charged for the year (Note 20) | (353,998) | (369,389) | (1,042,744) | (418,650) | (502,477) | (10,064) | - | (2,697,322) |
| Disposals | - | 105 | 1 | 15,061 | - | - | - | 15,167 |
| **Accumulated depreciation at 31 December 2011** | **(772,382)** | **(749,164)** | **(2,153,124)** | **(762,479)** | **(780,861)** | **(27,097)** | **-** | **(5,245,107)** |
| Charged for the year | (358,012) | (416,326) | (1,065,466) | (588,492) | (508,173) | (11,439) | - | (2,947,907) |
| Disposals | - | 28 | - | 16,977 | - | 1,899 | - | 18,904 |
| **Accumulated depreciation at 31 December 2011** | **(1,130,394)** | **(1,165,463)** | **(3,218,589)** | **(1,333,993)** | **(1,289,034)** | **(36,636)** | **-** | **(8,174,109)** |
| **Net book value at 31 December 2010** | **9,090,987** | **10,335,072** | **26,780,487** | **8,656,278** | **12,904,064** | **24,57** | **2,321,958** | **70,113,416** |
| **Net book value at 31 December 2011** | **8,535,693** | **8,659,426** | **27,140,944** | **8,094,685** | **12,395,891** | **59,020** | **2,434,451** | **67,320,110** |

During the year ended 31 December 2011 no borrowing costs were capitalized.

As at December 2011 the Company provided RR 380,068 thousand (at December 2010: RR nil) relating to impairment of certain materials used in the construction of oil&gas properties. The amount provided has been included in other operating expense in profit or loss for the year (Note 23).

Movements in the decommissioning and site restoration asset are due to changes in the estimate of future costs to be incurred in setting the associated obligation.

As at 31 December 2011 the Company has properties transferred as a deposit (mortgage) under the long-term multicurrency project facility agreement with Unicredit Bank AG acting as Facility Agent, amounting to RR 26,666,303 thousand (Note 16). ING BANK N.V., LONDON BRANCH acts as the mortgagee.

31 DECEMBER 2011 (In thousands of Russian Roubles)

| | Pipeline | Wells | Buildings and facilities | Machinery and equipment | Roads | Total |
|---|---|---|---|---|---|---|
| **Initial cost at 31 December 2011** | **9,248,693** | **7,936,778** | **8,267,033** | **4,267,732** | **129,657** | **29,849,893** |
| **Accumulated depreciation at 31 December 2011** | **1,078,373** | **898,016** | **867,848** | **325,659** | **13,693** | **3,183,590** |
| **Net book value at 31 December 2011** | **8,170,320** | **7,038,762** | **7,399,184** | **3,942,073** | **115,964** | **26,666,303** |

## 12. OTHER NON-CURRENT ASSETS

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| Debt service reserve account | 4,265,111 | - |
| Expenditure reserve account | 3,000,000 | - |
| | **7,265,111** | **-** |

In accordance with the long term project financing agreement finalized in 2011, certain cash is required to be set aside and can only be used in restricted circumstances.

As at 31 December 2011 cash balances of the Company on debt service reserve accounts were RR 1,795,991 thousand (Euro 43,099 thousand), RR 1,924,345 thousand (US dollar 59,769 thousand) and RR 544,775 thousand. The cash in amount of RR 3,000,000 thousand was placed on expenditure reserve account. According to the project financing contract the Company may withdraw amounts from the expenditure reserve account to meet any budgeted capital or operating expenditure due and payable to the extent that it would not otherwise have sufficient funds in the proceeds or operation accounts available to pay such expenditures.

## 13. ACCOUNTS PAYABLE

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| **Financial liabilities** | | |
| Trade payables | 190,599 | 231,260 |
| Interest payable | 144,657 | 16,583 |
| Payables to related parties (see note 27) | 41,025 | 138,846 |
| Other payables and accruals | 7,914 | 5,131 |
| | **384,195** | **391,820** |
| **Non-financial liabilities** | | |
| Accrual for employee bonuses and unused holidays | 262,692 | 174,613 |
| Wages and salaries | - | 1,041 |
| Provision for revegetation | 51,880 | 86,278 |
| | **314,572** | **261,932** |
| | **698,767** | **653,752** |

The Company is obliged to perform revegetation works on the pit of mineral soil which was used for construction purposes. Provision was recognised in the financial statements in respects of revegetation works to be performed in 2011 and 2012 respectively.

NOTES TO THE IFRS FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (In thousands of Russian Roubles)

## 14. INCOME TAX AND OTHER TAXES

Taxes payable other than income tax comprise the following:

| | 31 December 2011 | 31 December 2010 |
|---|---|---|
| Value added tax (VAT) | 1,111,272 | 1,650,833 |
| Natural resources production tax | 563,807 | 355,313 |
| Property tax | 243,211 | 269,344 |
| Insurance contributions for employees | 40,192 | 15,474 |
| Other taxes and accruals | 528 | 1,690 |
| | **1,959,010** | **2,292,654** |

Income tax expense comprises the following:

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| Current tax expense | (565,615) | (2,051,544) |
| Deferred tax expense | (1,605,887) | (3,470,031) |
| | **(2,171,502)** | **(5,521,575)** |

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| **Profit before tax** | **10,782,557** | **25,408,975** |
| Theoretical tax expense at statutory rate 20 percent | (2,156,511) | (5,081,795) |
| Tax effect of items which are not deductible or assessable for taxation purposes: | | |
| Effects related to the change in provision for decommissioning and site restoration | 43,636 | (158,944) |
| Other non-deductible expenses | (58,627) | (280,836) |
| **Income tax expense for the year** | **(2,171,502)** | **(5,521,575)** |

| | 31 December 2011 | Tax effect of movement in temporary differences | 31 December 2010 | Tax effect of movement in temporary differences | 31 December 2009 |
|---|---|---|---|---|---|
| **Tax effect of taxable temporary differences:** | | | | | |
| Property, plant and equipment | (5,627,409) | (1,465,779) | (4,161,630) | (2,083,330) | (2,078,300) |
| Discounting of borrowings | (87,201) | (55,197) | (32,004) | 61,370 | (93,374) |
| | **(5,714,610)** | **(1,520,976)** | **(4,193,634)** | **(2,021,960)** | **(2,171,674)** |
| **Tax effect of deductible temporary differences:** | | | | | |
| Tax losses carry forward | - | - | - | (1,272,394) | 1,272,394 |
| Foreign currency denominated borrowings | - | - | - | (329,337) | 329,337 |
| Inventories | 53,318 | (76,739) | 130,058 | 153,154 | (23,096) |
| Other deductible temporary differences | 121,625 | (8,172) | 129,796 | 507 | 129,290 |
| **Total net deferred tax liability** | **(5,539,667)** | **(1,605,887)** | **(3,933,780)** | **(3,470,031)** | **(463,749)** |

Based on the amount of proved gas reserves and contracted sales management believes that the Company will generate sufficient taxable profits in the future periods against which the deductible temporary differences will be reversed.

31 DECEMBER 2011 (In thousands of Russian Roubles)

## 15. SHORT-TERM LOANS

| | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Banks: | | |
| Banque Societe Generale | | |
| US$ denominated floating rate: | - | 32,917,619 |
| Euro denominated floating rate: | - | 7,755,295 |
| | **-** | **40,672,914** |
| Plus: Long-term debt, current portion (Note 16) including: | | |
| US$ denominated floating rate: | 3,024,643 | - |
| Euro denominated floating rate: | 2,820,909 | - |
| RR denominated fixed rate: | 855,344 | - |
| **Total** | **6,700,896** | **40,672,914** |

For the purpose of refinancing of the loan received in 2009, in June 2010 the Company entered into a multicurrency loan agreement totaling Euro 193,183 thousand and US dollar 1,084,142 thousand. Societe Generale London Branch acted as Facility Agent for a group of international financial institutions. The loan was initially agreed with repayment due in 2011. This loan was guaranteed by OJSC Gazprom, BASF SE and E.ON AG.

Interest rate for the Euro-denominated part of loan guaranteed by OJSC Gazprom was Euro LIBOR+175 basis points; guaranteed by BASF SE – Euro LIBOR+60 basis points and guaranteed by E.ON AG – Euro LIBOR+60 basis points.

Interest rate for the US dollars-nominated part of loan guaranteed by OJSC Gazprom was LIBOR+175 basis points; guaranteed by BASF SE - LIBOR+60 basis points and guaranteed by E.ON AG – LIBOR+60 basis points.

In March 2011 the multicurrency loan was fully repaid.

In March 2011 the Company signed agreements to obtain short-term borrowings from its shareholders totaling RR 32,500,000 thousand with repayment due in September 2011. Interest rate was 5.2% per annum. In May 2011these short-term borrowings were fully repaid.

## 16. LONG-TERM LOANS

| | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Banks: | | |
| UniCredit Bank AG | | |
| US$ denominated floating rate: | 17,753,427 | - |
| Euro denominated floating rate: | 16,554,167 | - |
| RR denominated fixed rate: | 5,018,939 | - |
| | **39,326,533** | **-** |
| Less: Long-term debt, current portion (Note 15) | 6,700,896 | - |
| **Total** | **32,625,637** | **-** |

In order to repay outstanding borrowings in March 2011 the Company entered into the project facility agreement to obtain long-term multicurrency financing totaling Euro 474,088 thousand, US dollar 657,465 thousand and RUR 5,992,523 thousand. Unicredit Bank AG is acting as Facility Agent for a group of international financial institutions. Final repayment of this project financing is due in December 2018. In May 2011 the project financing was received.
This loan is collateralized by a mortgage in respect of the gas pipeline, certain immovable assets and certain gas wells, land lease rights and a pledge of rights under the gas sale agreements (Note 11).

Interest rates for the Euro- and US dollar-denominated parts of the loan are EURIBOR/LIBOR +235 basis points per annum from the date of the agreement to 31 March 2014, EURIBOR/LIBOR +250 basis points per annum from 1 April 2014 to 31 March 2017, EURIBOR/LIBOR +275 basis points per annum from 1 April 2017 to the final repayment date. A fixed interest rate for the RUR-denominated part of the loan is 11.4 % per annum.

31 DECEMBER 2011 (In thousands of Russian Roubles)

The average effective interest rates at the end of reporting period were as follows:

| | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Banks: | | |
| US$ denominated floating rate | 2.65 | 3.86 |
| Euro denominated floating rate | 3.79 | 4.05 |
| RR denominated fixed rate | 11.4 | - |

As at 31 December 2011 and 31 December 2010 the carrying amounts of long-term loans approximate their fair values.

## 17. PROVISIONS FOR LIABILITIES AND CHARGES

| | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Provision for decommissioning and site restoration | 2,966,254 | 3,184,432 |
| Provision for state wells decommissioning | 79,724 | 130,868 |
| | **3,045,978** | **3,315,300** |

***Provision for decommissioning and site restoration***

| | **Year ended 31 December 2011** | **Year ended 31 December 2010** |
|---|---|---|
| At the beginning of the year | 3,184,432 | 2,389,711 |
| Change in estimate of provision for decommissioning and site restoration | (492,039) | 616,695 |
| Unwinding of discount | 273,861 | 178,026 |
| **At the end of the year** | **2,966,254** | **3,184,432** |

The Company is obliged to bear expenses for decommissioning and site restoration of the Yuzhno-Russkoye deposit after its development and accordingly a provision for decommissioning and site restoration was recognized in the financial statements for the year ended 31 December 2011 and for the year ended 31 December 2010 with a corresponding asset recognised within property, plant and equipment (see Note 11). The discount rate used to calculate the net present value of the future cash outflows relating to decommissioning and site restoration as at 31 December 2011 was 9.03 percent (31 December 2010 - 8.6 percent), which represents the pre-tax rate which reflects market assessment of time value of money and the risk specific to the liability at the end of reporting period.

***Provision for state wells decommissioning***

| | **Year ended 31 December 2011** | **Year ended 31 December 2010** |
|---|---|---|
| At the beginning of the year | 130,868 | 222,966 |
| Change in estimate of provision for state wells decommissioning | 14,004 | - |
| Unwinding of discount | 8,271 | 13,784 |
| Utilization of provision | (73,418) | (105,882) |
| **At the end of the year** | **79,724** | **130,868** |

According to the license agreement between the Company and the Administration of the Yamalo-Nenets Autonomous District, the Company is obliged to bear expenses for liquidation of exploration wells located at Yuzhno-Russkoye oil and gas field owned by the state. The Company recognised a provision for these expenses in its financial statements for the year ended 31 December 2011 and for the year ended 31 December 2010. The discount rate used to calculate the net present value of the future cash outflows relating to state wells liquidation as at 31 December 2011 was 9.03 percent (31 December 2010: 9.85 percent).

## 18. EQUITY

### *Share capital*

In July 2011, according to the decision of the general meeting of shareholders of 11 May 2011, the share capital of the Company was increased from its own funds (from the share premium). The Company converted its shares into shares of the same category with a higher nominal value. After this convertation share capital of the Company includes 533,324 ordinary shares with the nominal value of 60 rouble per share and 2 preference shares (type «A») with the nominal value of RR 2,462 thousand, 3 preference shares (type «B») with the nominal value of RR 667 thousand per share and 1 preference share (type «C») with the nominal value of RR 1,077 thousand. Total amount of share capital amounts to RR 39,999 thousand.

As at 31 December 2011 according to the project facility agreement all the shares (533,324 ordinary shares, 2 preference shares (type «A») , 3 preference shares (type «B») 1 preference share (type «C») are pledged to ING BANK N.V., London Branch until all the obligations, under the Project Facility Agreement are fulfilled.

As at 30 June 2011 share capital of the Company included 533,324 ordinary shares with the nominal value of 1 rouble per share and 2 preference shares (type «A») with the nominal value of RR 41 thousand, 3 preference shares (type «B») with the nominal value of RR 11 thousand per share and 1 preference share (type «C») with the nominal value of RR 18 thousand. Total amount of share capital was RR 667 thousand.

In fourth quarter 2009, according to the decision of the general meeting of shareholders of 18 August 2009, the Company additionally issued 4 ordinary shares with the nominal value of 1 rouble per share, 3 preference shares (type «B») with the nominal value of RR 11 thousand per share and 1 preference share (type «C») with the nominal value of RR 18 thousand.

The excess of the proceeds from additional share issuance over the nominal value totaling RR 1,639,449 thousand was recorded in equity as share premium.

As at 31 December 2008 share capital of the Company included 533,320 ordinary shares with the nominal value of 1 rouble per share and 2 preference shares (type «A») with the nominal value of RR 41 thousand. Total amount of share capital was RR 616 thousand.

The preference shares are not redeemable and rank ahead of the ordinary shares in the event of the Company's liquidation. The preference shares give the holders the right to participate in general shareholders' meetings without voting rights except in instances where decisions are made in relation to re-organization and liquidation of the Company, and where changes and amendments to the Company's charter which restrict the rights of preference shareholders are proposed. Upon a positive decision of the shareholders meeting to pay dividends, dividends on preference shares (type «A») are calculated as 12.308 percent of the portion of the profit of the Company which has been allocated for dividends payment in accordance with the resolution of the shareholders meeting; preference shares (type «B») are 5 percent of the allocated profit for dividends; preference shares (type «C») are 2.692 percent of the profit allocated for dividends. These preference dividends rank above ordinary dividends. If preference dividends are not declared by ordinary shareholders, the preference shareholders obtain the right to vote as ordinary shareholders until such time that the dividend is paid.

The basis of distribution is defined by legislation as the current year net profit as calculated in accordance with the Russian accounting rules. However, the legislation and other statutory laws and regulations dealing with profit distribution are open to legal interpretation and accordingly management believes at present it would not be appropriate to disclose an amount for the distributable profits and reserves in the financial statement.

### *Other reserves*

Before 1 January 2007 the Company received loans from its shareholders. Indebtedness under the loans was recognized in the financial statements at fair value calculated using average interest rates on similar loans. The difference between the fair value of the loan and the amount of received funds totaling RR 1,810,635 thousand, net of respective deferred tax effect of RR 571,799 thousand, was recorded in equity in Other reserves.
In the year ended 31 December 2007 the Company received loans from its shareholders. Indebtedness under the loans was recognized in the financial statements at fair value calculated using average interest rates on similar loans. The difference between the fair value of the loan and the amount of received funds totaling RR 4,585,301 thousand, net of respective deferred tax effect of RR 1,447,990 thousand, was recorded in equity in Other reserves.

In the year ended 31 December 2007 the Company early repaid part of the loans to its shareholder. The fair value effect from early redemption of these loans totaling RR 1,323,746 thousand, net of respective deferred tax effect of RR 418,025 thousand, was recognized as a reduction in Other reserves.

In the year ended 31 December 2008 the Company redeemed all the loans for which Other reserves were recognized. The fair value effect from early redemption in the amount of RR 4,198,937 thousand, net of respective deferred tax effect of RR 1,325,954 thousand, was recognized as a reduction in Other reserves.

***Dividends***

The Extraordinary General Shareholders' Meeting of OJSC Severneftegazprom held on December 21, 2011 decided to pay dividends RR 13,200,000 thousand for the nine months ended September 30, 2011.

The Annual General Shareholders' Meeting of OJSC Severneftegazprom held on June 29, 2010 decided not to pay dividends for the year ended December 31, 2009.

Dividends declared and paid during the year were as follows:

| | 2011 | | 2010 | |
|---|---|---|---|---|
| In thousands of Russian Roubles | Ordinary | Preference | Ordinary | Preference |
| **Dividends payable at 1 January** | - | - | - | - |
| Dividends declared during the year | 10,560,000 | 2,640,000 | - | - |
| Dividends paid during the year | (10,560,000) | (2,640,000) | - | - |
| **Dividends payable at 31 December** | - | - | - | - |
| **Dividends per share declared during the year** | 19.80 | 440,000.00 | - | - |

In 2011 Company accrued dividends in the amount of RR 13,200,000 thousand. Amount of dividends paid was RR 12,328,795 thousand net of withholding tax.

All dividends are declared and paid in Russian Roubles. In accordance with Russian legislation, the Company distributes profits as dividends on the basis of financial statements prepared in accordance with Russian Accounting Rules. The statutory accounting reports of the Company are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit.

## 19. SALES

| | **Year ended 31 December 2011** | **Year ended 31 December 2010** |
|---|---|---|
| Revenue from gas sales | 26,038,396 | 36,901,899 |
| | **26,038,396** | **36,901,899** |

All customers of the Company represent related parties. Please refer to Note 27.

## 20. COST OF SALES

| | **Year ended 31 December 2011** | **Year ended 31 December 2010** |
|---|---|---|
| Natural resources production tax | 6,079,798 | 3,728,373 |
| Depreciation | 2,907,898 | 2,604,941 |
| Property tax | 1,055,127 | 998,373 |
| Wages, salaries and other staff costs | 1,009,197 | 877,869 |
| Services | 533,702 | 611,625 |
| Materials | 251,799 | 147,347 |
| Insurance | 156,214 | 123,711 |
| Transportation services | 62,517 | 24,778 |
| Fuel and energy | 38,609 | 31,128 |
| Other | 138,113 | 127,045 |
| | **12,232,974** | **9,275,190** |

Depreciation in the amount of RR 40,009 thousand for the year ended 31 December 2011 was capitalized (for the year ended 31 December 2010 – RR 92,381 thousand).

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## 21. GENERAL AND ADMINISTRATIVE EXPENSES

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| Wages, salaries and other staff costs | 724,729 | 603,317 |
| Services and other administrative expenses | 583,387 | 877,356 |
| | **1,308,116** | **1,480,673** |

## 22. OTHER OPERATING INCOME

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| Penalties received | - | 266,414 |
| Other | 7,245 | 62,114 |
| | **7,245** | **328,528** |

## 23. OTHER OPERATING EXPENSES

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| Social costs | 55,849 | 82,455 |
| Nonrefundable VAT | 15,054 | 14,152 |
| Provision for impairment of receivables | 1,491 | 49,593 |
| Impairment of CIP | 380,068 | - |
| Loss on disposal of property, plant and equipment | 19,252 | 948,047 |
| Provision for revegetation | 54,738 | 86,278 |
| Losses from purchase and sale of foreign currencies | 235,560 | 12,286 |
| Other | 79,338 | 19,840 |
| | **841,350** | **1,212,651** |

## 24. FINANCE INCOME

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| Interest income | 693,860 | 726,089 |
| Foreign currency exchange gains | 8,390,446 | 7,751,578 |
| | **9,084,306** | **8,477,667** |

## 25. FINANCE EXPENSES

| | Year ended 31 December 2011 | Year ended 31 December 2010 |
|---|---|---|
| **Interest expense:** | | |
| Bank loans | 1,639,060 | 1,477,797 |
| Other | 273,178 | 707,604 |
| Expense from discounting of financial assets | - | 243,644 |
| Foreign currency exchange losses | 7,668,542 | 5,328,502 |
| Unwinding of discount of provisions (see note 17) | 282,132 | 191,810 |
| | **9,862,912** | **7,949,357** |

## 26. CONTINGENCIES, COMMITMENTS AND OTHER RISKS

### (a) Tax legislation

Russian tax legislation which was enacted or substantively enacted at the end of the reporting period, is subject to varying interpretations when being applied to the transactions and activities of the Company. Consequently, tax positions taken by management and the formal documentation supporting the tax positions may be successfully challenged by relevant authorities. Russian tax administration is gradually strengthening, including the fact that there is a higher risk of review of tax transactions without a clear business purpose or with tax incompliant counterparties. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Russian transfer pricing legislation enacted during the current period is effective prospectively to new transactions from 1 January 2012. It introduces significant reporting and documentation requirements. The transfer pricing legislation that is applicable to transactions on or prior to 31 December 2011, also provides the possibility for tax authorities to make transfer pricing adjustments and to impose additional tax liabilities in respect of all controllable transactions, provided that the transaction price differs from the market price by more than 20%. Controllable transactions include transactions with interdependent parties, as determined under the Russian Tax Code, all cross-border transactions (irrespective of whether performed between related or unrelated parties), transactions where the price applied by a taxpayer differs by more than 20% from the price applied in similar transactions by the same taxpayer within a short period of time, and barter transactions. Significant difficulties exist in interpreting and applying transfer pricing legislation in practice. Any prior existing court decisions may provide guidance, but are not legally binding for decisions by other, or higher level, courts in the future.

Tax liabilities arising from transactions between companies are determined using actual transaction prices. It is possible, with the evolution of the interpretation of the transfer pricing rules, that such transfer prices could be challenged. The impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the entity.

### (b) Legal proceedings

The Company is subject of, or party to a number of court proceedings arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Company and which have not been accrued or disclosed in the interim condensed financial information.

### (c) Environmental matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Company periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage that have not already been provided for.

### (d) Capital commitments

At 31 December 2011, the Company had contractual commitments for capital expenditures of approximately RR 384,669 thousand (31 December 2010 – RR 256,727 thousand).

## 27. RELATED PARTY TRANSACTIONS

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

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

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***Transactions with shareholders***

The Company is under the control of OJSC Gazprom and is included in the Gazprom Group. OJSC Gazprom is the Immediate and Ultimate Parent entity. The Government of the Russian Federation is the ultimate controlling party of the Company. At the same time Wintershall Holding Gmbh, which is part of the BASF SE Group and E.ON Ruhrgas E&P Gmbh, which is part of the E.ON Group have significant influence on the Company (see note 1).

Transactions of the Company with its shareholders for the periods ended 31 December 2011 and 31 December 2010 are presented below:

| | **Year ended 31 December 2011** | **Year ended 31 December 2010** |
|---|---|---|
| Sales of gas to OJSC Gazprom | 10,415,358 | 14,760,760 |
| Sales of gas to CJSC Gazprom YRGM Trading | 9,113,439 | 12,915,664 |
| Sales of gas to CJSC Gazprom YRGM Development | 6,509,599 | 9,225,475 |
| Purchases of goods and services from Gazprom Group | 256,188 | 271,022 |
| Credit facility arrangement services from E.ON AG | - | 143,275 |
| Credit facility arrangement services from BASF SE | - | 414,075 |

All operations with Gazprom Group, BASF SE Group and E.ON Group were performed in accordance with signed agreements and on general market conditions.

Significant balances with shareholders are summarised as follows:

| **Short-term accounts receivable** | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Trade and other receivables from OJSC Gazprom | 1,226,402 | 3,305,223 |
| Trade and other receivables from CJSC Gazprom Development | 687,241 | 1,022,759 |
| Trade and other receivables from CJSC Gazprom YRGM Trading | 962,137 | 1,431,863 |
| Other receivables from Gazprom Group | 1,694 | 719 |
| | **2,877,474** | **5,760,564** |
| **Long-term accounts receivable** | | |
| Trade receivables from OJSC Gazprom | 309,439 | 381,779 |
| | **309,439** | **381,779** |

As at 31 December 2011 and 31 December 2010 short-term receivables of related parties were non-interest bearing, had maturity within one year and were denominated mostly in Russian Roubles.

| **Accounts payable** | **31 December 2011** | **31 December 2010** |
|---|---|---|
| Payables to the Gazprom Group | 41,025 | 131,020 |
| Payables to the E.ON AG | - | 3,261 |
| Payables to the BASF SE | - | 4,565 |
| | **41,025** | **138,846** |

**Transactions with Key Managment Personnel**

Management of the Company consists of the General director and his twelve deputies.

Key management compensation is presented below:

| **Key management benefits** | **Year ended 31 December 2011** | **Year ended 31 December 2010** |
|---|---|---|
| Short-term benefits | 196,614 | 145,825 |
| Other long-term benefits | 53,888 | 27,250 |
| | **250,502** | **173,075** |

The Shareholders' Meeting of OJSC Severneftegazprom held on September, 2011 decided to pay compensation to the members of the Board of directors amounting to RR 3,936 thousand.

The Shareholders' Meeting of OJSC Severneftegazprom held on September, 2010 decided to pay compensation to the members of the Board of directors amounting to RR 2,276 thousand.

### Transactions with parties under the control of the Government

The Company does not have transactions with parties under the control of the Government except for the Gazprom Group.

## 28. SUBSEQUENT EVENTS

There are no subsequent events to disclose.