PAO NOVATEK

IFRS CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2016

AND INDEPENDENT AUDITOR'S REPORT

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Independent Auditor's Report

To the Shareholders and Board of Directors of PAO NOVATEK:

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of PAO NOVATEK and its subsidiaries (together – the "Group") as at 31 December 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2016;
- the consolidated statement of income for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of cash flows for the year then ended;
- the consolidated statement of changes in equity for the year ended; and
- the notes to the consolidated financial statements, which include summary of significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report.

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

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements of the Auditor's Professional Ethics Code and Auditor's Independence Rules that are relevant to our audit of the consolidated financial statements in the Russian Federation. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our audit approach

Overview

Materiality

Overall group materiality: 7,000 million Russian Roubles ("RUB") which represents 4% of adjusted profit before tax excluding currency exchange differences, net gain on disposal of interests in joint ventures and the Group's share of joint ventures' currency exchange differences net of income tax.

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Audit scope

- We conducted audit work covering all significant components and balances in Russia, Switzerland, Singapore and Republic of Cyprus.
- The group engagement team visited all significant locations in Russia and Switzerland.
- Our audit scope addressed more than 99% of the Group's revenues and more than 99% of the Group's absolute value of underlying profit before tax.

Key audit matters

- Impairment of production assets and investments in joint ventures;
- Accounting for trading activities in Europe;
- Valuation of non-commodity financial derivatives.

We designed our audit by determining materiality and assessing the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, if any, both individually and in aggregate on the financial statements as a whole.

Overall group materiality	RUB 7,000 million
How we determined it	4% of adjusted profit before tax excluding currency differences, net gain on disposal of interests in joint ventures and share of joint ventures' currency differences net of income tax.
Rationale for the materiality benchmark applied	We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark. The use of adjusted profit before tax mitigates the effect of volatility (that could be material) caused by non-recurring factors such as gains on disposals of assets and foreign exchange differences that can be material and provides a more stable basis for determining materiality, focusing on the underlying profitability of the Group.

We chose 4% which is consistent with quantitative materiality thresholds used for profit-oriented companies in this sector which resulted in an increase in materiality of RUB 500 million or 7.7% as compared to the prior year that is consistent with the increase in operational performance.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the Key audit matter
Impairment of production assets and investments in joint ventures	
Due to the current economic environment in Russia and high volatility of prices for oil and oil products there is a possibility that property, plant and equipment, as well as investments in joint ventures may not be recoverable. We focused on this area due to the significant carrying values of property, plant and equipment of the Group and investments in joint ventures and the nature of the judgements and assumptions management are required to make in determining whether there are any impairment triggers or impairments.	We analyzed management's assessment of impairment triggers and did not identify any further triggers, which had not been considered by management. We critically evaluated the appropriateness and consistency of key assumptions of the impairment test models to ensure that the results of the performed tests are reasonable. Specific work that we performed over the impairment analysis included: • comparing the assumptions used within the impairment review model to approved budgets and business plans and other evidence of future intentions for individual properties, which we found to be consistent; • benchmarking of key assumptions including commodity prices and discount rates and inflation rates against generally accepted forecasts which we found to be consistent; • performing sensitivity analysis over key assumptions in the model in order to assess the potential impact of a range of possible outcomes; and • challenged management on the inclusion of all appropriate assets and liabilities in the cash-generating units and in particular, given that the recoverable amount is determined based on value in use, the inclusion or exclusion of certain tax related balances and agreed that all relevant balances had been included.

Key audit matter	How our audit addressed the Key audit matter
	None of the items noted above revealed an impairment charge.
Accounting for trading activities in Europe The Group conducts natural gas foreign trading in active markets under long-term and short-term purchase and sales contracts. The Group also purchases and sells various derivative instruments (with reference of the delivery points to the European natural gas hubs) in order to increase delivery optimization and decrease exposure to the risk of negative changes in natural gas prices. The fair value of long-term natural gas derivative contracts involving the physical delivery of natural gas is determined using internal models and other valuation techniques (the mark-to-market and mark-to-model analysis) due to the absence of quoted prices or other observable, market-corroborated data, for the duration of the contracts. We focused on this area because of the complexity of the models and because model parameters are inherently subject to judgement applied by management.	We critically evaluated the appropriateness and consistency of key valuation assumptions used for the measurement of the contracts to ensure that the resulting valuation is reasonable. We tested material valuations in detail and sought additional external evidence. We assessed the methodologies used, and the judgements and assumptions made. We identified the market data input used by the Group and tested them against independent data. We tested the appropriateness of the valuation methodology applied and the integrity of the models used, and noted no material issues. We also tested the accuracy of the contractual inputs and the appropriateness of key valuation inputs including price and discount rates, and noted no material issues. Where the Group entered into new significant contracts in the year, we tested the contracts and assumptions used to assess whether the accounting treatment adopted is in accordance with International Accounting Standard 39. We also gained an understanding of the controls that are in place for these trading activities. We identified no material issues.
Valuation of non-commodity financial derivatives Certain shareholders' loans provided by the Group to its joint ventures include embedded derivatives that modify the cash flows of the loans based on financial and non-financial variables. The terms and conditions of each of these loans related to those variables were defined as a single compound embedded derivative. The Group designated these loans as financial assets at fair value through profit or loss. In accordance with IFRS, such loans are measured at fair value at each reporting date. We focused on this area because of the significant impact of the valuation results on the financial	We evaluated the appropriateness and consistency of key valuation assumptions (such as expected free cash flows of the joint ventures, production volumes, and discount rates used) to ensure that the resulting valuation of the financial instruments is reasonable. Those assumptions mainly referred to the Group's projections of future expected free cash flows to be generated by the joint ventures and estimates of market interest rates applied in the valuation. We also tested the accuracy of the contractual inputs and analyzed the appropriateness of the valuation methodology.

Key audit matter	How our audit addressed the Key audit matter
statements of the Group and the fact that the measurement of the fair value of these loans is based on judgement and estimates applied by management which can be highly subjective.	We identified no material issues.

How we tailored our group audit scope

We tailored the scope of our audit in order to perform sufficient work to be able to give an opinion on the consolidated financial statements as a whole, taking into account the geographic and management structure of the Group, the accounting processes and controls and the industry in which the Group operates.

In establishing the overall group audit strategy and plan, we determined the type of work that needed to be performed at the reporting units by the group engagement team and by the component auditors from other PwC network firms. For each reporting unit we issued specific instructions to the audit teams of the component auditors within our audit scope. We determined the level of our and component auditors involvement we needed to be involved in the audit process at those reporting units so as to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the consolidated financial statements as a whole. We determined whether we required an audit of full scope of financial information or whether a defined scope of specified procedures was sufficient.

The group consolidation, financial statements disclosures and a number of complex items are audited directly by the PAO NOVATEK audit engagement team. These items include the assessment of accounting estimates performed by management in respect of fair values and classification of financial assets and liabilities, deferred income tax asset recognition, estimation of oil and gas reserves, impairment of financial and non-financial assets, impairment provision for trade receivables, pension obligations, asset retirement obligations and assessment of joint arrangements.

By performing the procedures described above at the individual component level, combined with the additional procedures performed at the group level, we have obtained sufficient and appropriate audit evidence regarding the financial information of the Group to provide a basis for our opinion on the consolidated financial statements.

Other information

Management is responsible for the other information. The other information comprises report "Management's discussion and analysis of financial condition and results of operations of PAO NOVATEK for the years ended 31 December 2016 and 2015" (but does not include the consolidated financial statements and our auditor's report thereon), which we obtained prior to the date of this auditor's report, and "Quarterly Issuer's Report of PAO NOVATEK for the first quarter of 2017" as well as "Annual Report Review of PAO NOVATEK for 2016", which are expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit 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 Group's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management;
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;

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- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The certified auditor on the audit resulting in this independent auditor's report is A.G. Yashkov.

21 February 2017
Moscow, Russian Federation

AO PricewaterhouseCoopers Audit

Wardell Jason Edward, Partner, for AO PricewaterhouseCoopers Audit

A.G. Yashkov, certified auditor (licence no. № 01-001391), AO PricewaterhouseCoopers Audit

Акционерное общество "ПрайсвотерхаусКуперс Аудит" ОГРН 1027700148431 PricewaterhouseCoopers Audit pwc Москва

Audited entity: PAO NOVATEK

State registration certificate №1461/94, issued by the administration of Oktyabrskiy district of Samara on 16 August 1994.

Certificate of inclusion in the Unified State Register of Legal Entities regarding the legal entity registered before 1 July 2002 No. 1026303117642 issued by the Inspectorate of the Russian Ministry of Taxes and Levies of Novokuybyshevsk, Samara Region on 20 August 2002.

Location of the Company according to the Charter: Russian Federation, Yamalo-Nenetski state, Purovsky region, Tarko-Sale

Mailing address: 629850, Yamalo-Nenetski state, Purovsky region, Tarko-Sale, Pobedi str., 22 "a".

Independent auditor: AO PricewaterhouseCoopers Audit

State registration certificate № 008.890, issued by the Moscow Registration Chamber on 28 February 1992

Certificate of inclusion in the Unified State Register of Legal Entities issued on 22 August 2002 under registration № 1027700148431

Member of Self-regulated organization of auditors «Russian Union of auditors» (Association)

ORNZ 11603050547 in the register of auditors and audit organizations

Consolidated Statement of Financial Position
(in millions of Russian roubles)

	Notes	At 31 December 2016	At 31 December 2015
ASSETS			
Non-current assets			
Property, plant and equipment	6	331,795	331,712
Investments in joint ventures	7	259,650	154,725
Long-term loans and receivables	8	209,145	230,799
Other non-current assets	9	30,484	34,316
Total non-current assets		**831,074**	**751,552**
Current assets			
Inventories	10	9,044	8,226
Current income tax prepayments		581	84
Trade and other receivables	11	41,586	37,564
Prepayments and other current assets	12	33,248	45,424
Cash and cash equivalents	13	48,301	29,187
Total current assets		**132,760**	**120,485**
Assets held for sale	5	**-**	**7,987**
Total assets		**963,834**	**880,024**
LIABILITIES AND EQUITY			
Non-current liabilities			
Long-term debt	14	161,296	252,050
Deferred income tax liabilities	26	24,656	23,706
Asset retirement obligations		7,605	4,149
Other non-current liabilities		3,766	2,273
Total non-current liabilities		**197,323**	**282,178**
Current liabilities			
Short-term debt and current portion of long-term debt	15	55,469	106,655
Trade payables and accrued liabilities	17	38,462	48,535
Current income tax payable		747	3,165
Other taxes payable		14,113	11,320
Total current liabilities		**108,791**	**169,675**
Total liabilities		**306,114**	**451,853**
Equity attributable to PAO NOVATEK shareholders			
Ordinary share capital		393	393
Treasury shares		(6,913)	(5,997)
Additional paid-in capital		31,297	31,297
Currency translation differences		(724)	(5,092)
Asset revaluation surplus on acquisitions		5,617	5,617
Retained earnings		618,680	399,861
Total equity attributable to PAO NOVATEK shareholders	18	**648,350**	**426,079**
Non-controlling interest		**9,370**	**2,092**
Total equity		**657,720**	**428,171**
Total liabilities and equity		**963,834**	**880,024**

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

L. Mikhelson
Chairman of the Management Committee

M. Gyetvay
Chief Financial Officer

21 February 2017

PAO NOVATEK
Consolidated Statement of Income
(in millions of Russian roubles, except for share and per share amounts)

	Notes	Year ended 31 December: 2016	2015
Revenues			
Oil and gas sales	19	533,857	472,007
Other revenues		3,615	3,318
Total revenues		**537,472**	**475,325**
Operating expenses			
Purchases of natural gas and liquid hydrocarbons	20	(134,268)	(120,504)
Transportation expenses	21	(133,462)	(130,229)
Taxes other than income tax	22	(44,053)	(36,630)
Depreciation, depletion and amortization	6	(34,631)	(19,980)
Materials, services and other	23	(19,133)	(14,551)
General and administrative expenses	24	(18,126)	(14,356)
Exploration expenses	6	(2,087)	(1,109)
Net impairment (expenses) reversals		(178)	204
Change in natural gas, liquid hydrocarbons and work-in-progress		439	2,113
Total operating expenses		**(385,499)**	**(335,042)**
Net gain on disposal of interests in joint ventures	5	73,072	989
Other operating income (loss), net		221	(542)
Profit from operations		**225,266**	**140,730**
Finance income (expense)			
Interest expense	25	(11,570)	(8,792)
Interest income	25	18,732	12,622
Change in fair value of non-commodity financial instruments	27	10,387	(10,505)
Foreign exchange gain (loss), net	25	(25,490)	(9,507)
Total finance income (expense)		**(7,941)**	**(16,182)**
Share of profit (loss) of joint ventures, net of income tax	7	90,839	(31,607)
Profit before income tax		**308,164**	**92,941**
Income tax expense			
Current income tax expense		(35,577)	(22,780)
Net deferred income tax benefit (expense)		(7,514)	3,958
Total income tax expense	26	**(43,091)**	**(18,822)**
Profit		**265,073**	**74,119**
Profit (loss) attributable to:			
Non-controlling interest		7,278	(277)
Shareholders of PAO NOVATEK		257,795	74,396
Basic and diluted earnings per share (in Russian roubles)		85.41	24.63
Weighted average number of shares outstanding (in millions)		*3,018.5*	*3,020.3*

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

(in millions of Russian roubles)

	Notes	Year ended 31 December: 2016	2015
Profit		**265,073**	**74,119**
Other comprehensive income (loss) that will not be reclassified subsequently to profit (loss):			
Remeasurement of pension obligations	16	(121)	(642)
Share of remeasurement of pension obligations of joint ventures		(21)	-
Total other comprehensive income (loss) that will not be reclassified subsequently to profit (loss)		**(142)**	**(642)**
Other comprehensive income (loss) that may be reclassified subsequently to profit (loss), net of income tax:			
Currency translation differences		4,368	(5,300)
Other comprehensive income (loss)		**4,226**	**(5,942)**
Total comprehensive income		**269,299**	**68,177**
Total comprehensive income (loss) attributable to:			
Non-controlling interest		7,278	(277)
Shareholders of PAO NOVATEK		262,021	68,454

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

(in millions of Russian roubles)

	Notes	Year ended 31 December: 2016	2015
Profit before income tax		**308,164**	**92,941**
Adjustments to profit before income tax:			
Depreciation, depletion and amortization		34,631	19,980
Impairment expenses (reversals), net		178	(204)
Foreign exchange loss (gain), net		25,490	9,507
Loss (gain) on disposal of assets, net		(73,072)	(941)
Interest expense		11,570	8,792
Interest income		(18,732)	(12,622)
Share of loss (profit) in joint ventures, net of income tax	7	(90,839)	31,607
Change in fair value of non-commodity financial instruments		(10,387)	10,505
Revaluation of commodity derivatives through loss (profit)		1,778	1,006
Increase in long-term advances given		(3,331)	(9,352)
Other adjustments		152	(10)
Working capital changes			
Decrease (increase) in trade and other receivables, prepayments and other current assets		2,592	(4,537)
Decrease (increase) in inventories		(861)	(2,280)
Increase (decrease) in trade payables and accrued liabilities, excluding interest and dividends payable		9,953	(310)
Increase (decrease) in taxes payable, other than income tax		2,836	2,009
Total effect of working capital changes		**14,520**	**(5,118)**
Dividends received from joint ventures		-	1,850
Interest received		1,983	1,454
Income taxes paid excluding actual payments relating to disposal of stakes in joint ventures		(28,314)	(16,531)
Net cash provided by operating activities		**173,791**	**132,864**
Cash flows from investing activities			
Purchases of property, plant and equipment		(28,170)	(42,224)
Payments for mineral licenses		(1,928)	-
Purchases of materials for construction		(929)	(2,313)
Payments for acquisition of subsidiaries net of cash acquired	5, 17	(2,961)	(3,630)
Additional capital contributions to joint ventures	7	(19,565)	-
Proceeds from disposal of stakes in joint ventures	5	84,978	-
Costs to sell stakes in joint ventures	5	(2,634)	-
Actual income tax payments relating to disposal of stakes in joint ventures		(9,932)	-
Interest paid and capitalized		(5,314)	(6,047)
Guarantee fees paid		(1,061)	-
Loans provided to joint ventures	8	(6,645)	(108,570)
Repayments of loans provided to joint ventures	8	6,038	3,710
Net cash provided by (used for) investing activities		**11,877**	**(159,074)**

(in millions of Russian roubles)

	Notes	Year ended 31 December: 2016	2015
Cash flows from financing activities			
Proceeds from long-term debt		6,373	71,345
Repayments of long-term debt		(82,753)	(42,240)
Proceeds from short-term debt with original maturity more than three months		-	21,300
Repayments of short-term debt with original maturity more than three months		(21,300)	-
Net increase (decrease) in short-term debt with original maturity three months or less		(5,040)	5,880
Interest paid		(11,423)	(7,149)
Dividends paid	18	(41,653)	(35,640)
Purchase of treasury shares	18	(916)	(782)
Net cash provided by (used for) financing activities		**(156,712)**	**12,714**
Net effect of exchange rate changes on cash and cash equivalents		(9,842)	1,365
Net increase (decrease) in cash and cash equivalents		**19,114**	**(12,131)**
Cash and cash equivalents at the beginning of the period		29,187	41,318
Cash and cash equivalents at the end of the period		**48,301**	**29,187**

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

PAO NOVATEK
Consolidated Statement of Changes in Equity
(in millions of Russian roubles, except for number of shares)

For the year ended 31 December 2015	*Number of ordinary shares (in millions)*	**Ordinary share capital**	**Treasury shares**	**Additional paid-in capital**	**Currency translation differences**	**Asset revaluation surplus on acquisitions**	**Retained earnings**	**Equity attributable to PAO NOVATEK shareholders**	**Non-controlling interest**	**Total equity**
1 January 2015	***3,020.4***	**393**	**(5,222)**	**31,297**	**208**	**5,617**	**352,462**	**384,755**	**2,369**	**387,124**
Profit (loss)	-	-	-	-	-	-	74,396	74,396	(277)	74,119
Other comprehensive income (loss)	-	-	-	-	(5,300)	-	(642)	(5,942)	-	(5,942)
Total comprehensive income (loss)	**-**	**-**	**-**	**-**	**(5,300)**	**-**	**73,754**	**68,454**	**(277)**	**68,177**
Dividends (Note 18)	-	-	-	-	-	-	(35,640)	(35,640)	-	(35,640)
Effect from other changes in joint ventures' net assets (Note 7)	-	-	-	-	-	-	9,285	9,285	-	9,285
Purchase of treasury shares (Note 18)	*(1.3)*	-	(775)	-	-	-	-	(775)	-	(775)
31 December 2015	***3,019.1***	**393**	**(5,997)**	**31,297**	**(5,092)**	**5,617**	**399,861**	**426,079**	**2,092**	**428,171**

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

PAO NOVATEK
Consolidated Statement of Changes in Equity
(in millions of Russian roubles, except for number of shares)

For the year ended 31 December 2016	*Number of ordinary shares (in millions)*	**Ordinary share capital**	**Treasury shares**	**Additional paid-in capital**	**Currency translation differences**	**Asset revaluation surplus on acquisitions**	**Retained earnings**	**Equity attributable to PAO NOVATEK shareholders**	**Non-controlling interest**	**Total equity**
1 January 2016	***3,019.1***	**393**	**(5,997)**	**31,297**	**(5,092)**	**5,617**	**399,861**	**426,079**	**2,092**	**428,171**
Profit (loss)	-	-	-	-	-	-	257,795	257,795	7,278	265,073
Other comprehensive income (loss)	-	-	-	-	4,368	-	(142)	4,226	-	4,226
Total comprehensive income (loss)	**-**	**-**	**-**	**-**	**4,368**	**-**	**257,653**	**262,021**	**7,278**	**269,299**
Dividends (Note 18)	-	-	-	-	-	-	(41,653)	(41,653)	-	(41,653)
Effect from other changes in joint ventures' net assets (Note 7)	-	-	-	-	-	-	2,819	2,819	-	2,819
Purchase of treasury shares (Note 18)	*(1.4)*	-	(916)	-	-	-	-	(916)	-	(916)
31 December 2016	***3,017.7***	**393**	**(6,913)**	**31,297**	**(724)**	**5,617**	**618,680**	**648,350**	**9,370**	**657,720**

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

1 ORGANIZATION AND PRINCIPAL ACTIVITIES

PAO NOVATEK (hereinafter referred to as "NOVATEK" or the "Company") and its subsidiaries (hereinafter jointly referred to as the "Group") is an independent oil and gas company engaged in the acquisition, exploration, development, production, processing, and marketing of hydrocarbons with its oil and gas operations located mainly in the Yamal-Nenets Autonomous Region ("YNAO") of the Russian Federation. The Group delivers its natural gas on the Russian Federation's domestic market and liquid hydrocarbons on both the Russian domestic and international markets.

The Group sells its natural gas on the Russian domestic market at unregulated market prices (except for deliveries to residential customers); however, the majority of natural gas sold on the Russian domestic market by all producers is sold at prices regulated by the governmental agency of the Russian Federation that carries out state regulation of prices and tariffs for goods and services of natural monopolies in energy, utilities and transportation. The Group's natural gas sales volumes fluctuate on a seasonal basis mostly due to Russian weather conditions, with sales peaking in the winter months of December and January and troughing in the summer months of July and August.

The Group processes unstable gas condensate at its Purovsky Gas Condensate Processing Plant located in close proximity to its fields into stable gas condensate and liquefied petroleum gas. The majority of stable gas condensate is further processed at the Group's Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea into higher-value refined products (naphtha, jet fuel, gasoil and fuel oil). The remaining stable gas condensate volumes are sold on domestic and international markets. The Group sells its liquid hydrocarbons at prices that are subject to fluctuations in underlying benchmark crude oil, naphtha and other gas condensate refined products prices. The Group's liquids sales volumes are not subject to significant seasonal fluctuations.

The Group also purchases and sells natural gas on the European market under long-term and short-term supply contracts to carry out its foreign commercial trading activities.

In March 2016, the Group closed the transaction on the disposal of a 9.9 percent equity stake in OAO Yamal LNG, the Group's joint venture, to China's investment fund Silk Road Fund Co. Ltd. (see Note 5).

In September 2016, the Group and Eni S.p.A. (hereinafter referred to as the "Concessionaries"), through their wholly owned subsidiaries NOVATEK Montenegro B.V. and Eni Montenegro B.V., entered into a Concession Contract with the State of Montenegro for the exploration and production of hydrocarbons on four offshore blocks located in the Adriatic Sea (hereinafter referred to as the "Concession Contract"). The Concession Contract stipulates that the Concessionaries are assigned a 50 percent participating interest each and are committed to undertake specified joint upstream activities during the exploration phase within seven years (see Note 28). The Group considers that the Concession Contract constitutes a joint arrangement and classifies it as a joint operation in accordance with IFRS 11, *Joint Arrangements*.

On 12 October 2016, an amended version of NOVATEK's Charter was registered, according to which the Company's name was changed to PAO NOVATEK (former name – OAO NOVATEK). The Company's name was changed to comply with the current provisions of the Part 1 Chapter 4 of the Civil Code of the Russian Federation.

2 BASIS OF PREPARATION

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of available-for-sale financial assets and financial instruments categorised at fair value through profit or loss. In the absence of specific IFRS guidance for oil and gas producing companies, the Group has developed accounting policies in accordance with other generally accepted accounting principles for oil and gas producing companies, mainly US GAAP, insofar as they do not conflict with IFRS principles.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

2 BASIS OF PREPARATION (CONTINUED)

Most of the Group entities prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The Group's consolidated financial statements are based on the statutory records with adjustments and reclassifications recorded in the consolidated financial statements for the fair presentation in accordance with IFRS. The principal adjustments primarily relate to: (a) depreciation, depletion and amortization, and valuation of property, plant and equipment; (b) consolidation of subsidiaries; (c) business combinations; (d) accounting for income taxes; (e) revaluation of shareholders' loans provided by the Group to its joint ventures to fair value; and (f) valuation of unrecoverable assets, expense recognition and other provisions.

Functional and presentation currency. The consolidated financial statements are presented in Russian roubles, the Group's reporting (presentation) currency and the functional currency for the majority of the Group's entities. The assets and liabilities (both monetary and non-monetary) of the Group entities whose functional currency is not the Russian rouble are translated into Russian roubles at the closing exchange rate at each balance sheet date. All items included in the shareholders' equity, other than profit or loss, are translated at historical exchange rates. The financial results of these entities are translated into Russian roubles using average exchange rates for each reporting period. Exchange adjustments arising on the opening net assets and the profits for the reporting period are taken to other comprehensive income before the disposal of the foreign operation and reported as currency translation differences in the consolidated statement of changes in equity and the consolidated statement of comprehensive income.

Exchange rates for foreign currencies in which the Group conducted significant transactions or had significant monetary assets and/or liabilities in the reporting period were as follows:

			Average rate for the year ended 31 December:	
Russian roubles to one currency unit	At 31 December 2016	At 31 December 2015	2016	2015
US dollar (USD)	60.66	72.88	67.03	60.96
Euro (EUR)	63.81	79.70	74.23	67.78
Polish zloty (PLN)	14.44	18.79	17.03	16.18

Exchange rates and restrictions. The Russian rouble is not a fully convertible currency outside the Russian Federation and, accordingly, any remeasurement of Russian rouble amounts to US dollars or any other currency should not be construed as a representation that such Russian rouble amounts have been, could be, or will in the future be converted into other currencies at these exchange rates.

Reclassifications. Certain reclassifications have been made to the comparative figures to conform to the current period presentation with no effect on profit for the period or shareholder's equity. Insurance expenses relating to production assets and major part of expenses of the Group's research and development center are presented in these consolidated financial statements within materials, services and other expenses and exploration expenses depending on their function, which were previously disclosed within general and administrative expenses. Accordingly, expenses in the amount of RR 807 million were reclassified from general and administrative expenses to materials, services and other expenses and exploration expenses in the amount of RR 465 million and RR 342 million, respectively, for the year ended 31 December 2015.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Adoption of new and amended standards and interpretations. In 2016, the Group adopted all IFRS, amendments and interpretations which are effective 1 January 2016 and relevant to its operations. None of them had material impact on the Group's consolidated financial statements.

Principles of consolidation. Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvements with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date that control ceases.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Intercompany transactions, balances and unrealized gains on transactions between group companies are eliminated. The Group and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

Non-controlling interest is that part of the net results and of the equity of a subsidiary attributable to interests which are not owned, directly or indirectly, by the Group. Non-controlling interest forms a separate component of the Group's equity. Changes in the Group's ownership interest in a subsidiary that do not result in the loss of control are accounted for as equity transactions.

Business combinations. The acquisition method of accounting is used to account for acquisitions of subsidiaries. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest.

The Group measures non-controlling interest on an acquisition-by-acquisition basis, either at: (a) fair value, or (b) the non-controlling interest's proportionate share of net assets of the acquiree.

Goodwill is measured by deducting the net assets of the acquiree from the aggregate of the consideration transferred for the acquiree, the amount of non-controlling interest in the acquiree and fair value of an interest in the acquiree held immediately before the acquisition date. Any negative amount ("negative goodwill") is recognized in profit or loss, after management reassesses whether it identified all the assets acquired and all liabilities and contingent liabilities assumed and reviews appropriateness of their measurement.

The consideration transferred for the acquiree is measured at the fair value of the assets transferred, equity instruments issued and liabilities incurred or assumed, including fair value of assets or liabilities from contingent consideration arrangements but excludes acquisition related costs such as advisory, legal, valuation and similar professional services. Transaction costs incurred for issuing equity instruments are deducted from equity; transaction costs incurred for issuing debt are deducted from its carrying amount and all other transaction costs associated with the acquisition are expensed.

Joint arrangements. Investments in joint arrangements are classified as either joint ventures or joint operations depending on the contractual rights and obligations each investor has rather than the legal structure of the joint arrangement.

The Group's investments in joint ventures are accounted for using the equity method. Under the equity method, an investment in a joint venture is initially recognized at cost. The difference between the cost of an acquisition and the share of the fair value of the joint venture's identifiable net assets represents goodwill upon acquiring the joint venture.

Post-acquisition changes in the Group's share of net assets of a joint venture are recognized as follows: (a) the Group's share of profits or losses is recorded in the consolidated profit or loss for the year as share of financial result of joint ventures; (b) the Group's share of other comprehensive income or loss is recognized in other comprehensive income or loss and presented separately; (c) dividends received or receivable from a joint venture are recognized as a reduction in the carrying amount of the investment; (d) all other changes in the Group's share of the carrying value of net assets of joint ventures are recognized within retained earnings in the consolidated statement of changes in equity.

After application of the equity method, including recognizing the joint venture's losses, the entire carrying amount of the investment is tested for impairment as a single asset whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

When the Group's share of losses in a joint venture equals or exceeds its interest in the joint venture, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the joint ventures. The interest in a joint venture is the carrying amount of the investment in the joint venture together with any long-term interests that, in substance, form part of the Group's net investment in the joint venture, including receivables and loans for which settlement is neither planned nor likely to occur in the foreseeable future.

Unrealized gains on transactions between the Group and its joint ventures are eliminated to the extent of the Group's interest in joint ventures; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Accounting policies of joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Group.

The Group recognizes on a line-by-line basis in the consolidated financial statements its share of assets, liabilities, revenues and expenses of its joint operations in accordance with the provisions of the respective joint operation agreements.

Disposals of subsidiaries, associates or joint ventures. When the Group ceases to consolidate a subsidiary or account for an investment using the equity method because of a loss of control, joint control or significant influence, any retained interest in the entity is remeasured to its fair value, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognized in other comprehensive income are recycled to profit or loss.

If the ownership interest in a joint venture is reduced but joint control is retained or replaced with significant influence, the Group continues to apply the equity method and does not remeasure the retained interest; only a proportionate share of the amounts previously recognized in other comprehensive income are reclassified to profit or loss where appropriate.

Foreign currency transactions. Transactions denominated in foreign currencies are converted into the functional currency of each entity of the Group at the exchange rates prevailing on the date of transactions. Exchange gains and losses resulting from foreign currency remeasurement into the functional currency are included in the determination of profit (loss) for the reporting period.

Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency of each entity of the Group by applying the year end exchange rate and the effect is stated in the consolidated statement of income. Non-monetary assets and liabilities denominated in foreign currencies valued at cost are converted into the functional currency of each entity of the Group at the initial exchange rate. Non-monetary assets that are remeasured to fair value, recoverable amount or realizable value, are translated at the exchange rate applicable to the date of remeasurement.

Extractive activities. The Group follows the successful efforts method of accounting for its oil and gas properties and equipment whereby property acquisitions and development costs are capitalized, and exploration costs (geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity), excluding exploratory drilling expenditures and exploration license acquisition costs, are recognized within operating expenses in the consolidated statement of income as incurred.

Exploration license acquisition costs and exploratory drilling costs are recognized as exploration assets in line “property, plant and equipment” until it is determined whether proved reserves justifying their commercial development have been found. If no proved reserves are found, the relevant costs are charged to the consolidated statement of income. When proved reserves are determined, exploration license acquisition costs are reclassified to proved properties acquisition costs and exploratory drilling costs are reclassified to development expenditure categories within “property, plant and equipment’. Exploration license acquisition costs and exploratory drilling costs recognized as exploration assets are reviewed for impairment on an annual basis.

The cost of 3-D seismic surveys used to assist production, increase total recoverability and determine the desirability of drilling additional development wells within proved reservoirs are capitalized as development costs. All other seismic costs are expensed as incurred.

Production costs and overheads are charged to expense as incurred.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment. Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation, depletion, amortization and impairment.

The cost of self-constructed assets includes the cost of direct materials, direct employee related costs, a pro-rata portion of depreciation of assets used for construction and an allocation of the Group's overhead costs.

The present value of the estimated costs of dismantling oil and gas production facilities, including abandonment and site restoration costs, are recognized when the obligation is incurred and are included within the carrying value of property, plant and equipment, subject to depletion using the unit-of-production method.

Depreciation, depletion and amortization of oil and gas properties and equipment is calculated using the unit-of-production method for each field based upon total proved reserves for costs associated with acquisitions of proved properties and common infrastructure facilities, and proved developed reserves for other development costs, including wells.

The Group's principal oil and gas reserves have been independently estimated by internationally recognized petroleum engineers whereas other oil and gas reserves of the Group have been determined based on estimates of mineral reserves prepared by the Group's management in accordance with internationally recognized definitions.

A portion of the reserves used for depreciation, depletion and amortization calculations include reserves expected to be produced beyond license expiry dates. The Group's management believes that there is requisite legislation and past experience to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the current license expiry dates.

Where unit-of-production method does not reflect useful life and pattern of consumption of particular oil and gas assets, such as processing facilities serving several properties, those assets are depreciated on a straight-line basis.

Property, plant and equipment, other than oil and gas properties and equipment, are depreciated on a straight-line basis over their estimated useful lives. Land and assets under construction are not depreciated.

The estimated useful lives of the Group's property, plant and equipment, other than oil and gas properties and equipment, are as follows:

	Years
Machinery and equipment	5-15
Processing facilities	20-30
Buildings	25-50

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components that extend the life of property, plant and equipment items are capitalized and depreciated over the estimated remaining life of the major part or component. All components that are replaced are written off.

At each reporting date management assesses whether there is any indication of impairment in respect 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 selling costs and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash generating units). The carrying amount is reduced to the recoverable amount and the impairment loss is recognized in profit or loss for the respective period. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

Gains and losses on disposals of property, plant and equipment are determined by comparing proceeds with the carrying amount. Gains and losses are recognized within other operating profit (loss) in the consolidated statement of income.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Borrowing costs. Interest costs on borrowings and exchange differences arising from foreign currency borrowings (to the extent that they are regarded as an adjustment to interest costs) used to finance the construction of property, plant and equipment are capitalized during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are recognized in the consolidated statement of income.

Intangible assets. Intangible assets that have a finite useful life are amortized using the straight-line method over the period of their useful life. There were no intangible assets with indefinite useful lives held by the Group at the reporting dates.

Non-current assets held for sale. Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell.

The Group ceases to use the equity method of accounting in relation to the interest in a joint venture or an associate classified as an asset held for sale.

Inventories. Natural gas, gas condensate, crude oil and gas condensate refined products are valued at the lower of cost or net realizable value. The cost of inventories includes direct cost of materials, direct operating costs, and related production overhead expenses and is recorded on a first-in-first-out (“FIFO”) basis. Net realizable value is the estimate of the selling price in the ordinary course of business, less selling expenses.

Materials and supplies are carried at amounts which do not exceed their respective recoverable amounts in the normal course of business.

Effective interest method. The effective interest method is a method of calculating the carrying value of a financial asset or a financial liability held at amortized cost and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts future cash payments and receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying value of the financial asset or financial liability.

Derivatives. Derivative instruments are contracts: (a) whose value changes in response to the change in one or more observable variables; (b) that do not require any material initial net investment; and (c) that are settled at a future date. Derivative financial instruments are carried as financial assets when fair value is positive and as financial liabilities when fair value is negative. Gains or losses arising from changes in the fair value of derivative instruments are included in the consolidated statement of income. The Group does not apply hedge accounting.

Contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the Group’s expected purchase, sale or usage requirements, are accounted for as derivatives. Gains or losses arising from changes in the fair value of commodity derivatives are recognized within other operating income (loss) in the consolidated statement of income.

Derivatives embedded in other non-derivative financial instruments or in non-financial host contracts are recognized as separate derivatives when their risks and economic characteristics are not closely related to those of the host contracts, and the host contracts are not carried at fair value.

Where there is an active market for a commodity or other non-financial item subject of a purchase or sale contract, a pricing formula will, for instance, be considered to be closely related to the host purchase or sales contract if the price formula is related to the market for such host contracts. A price formula with indexation to other markets or products will however result in the recognition of a separate derivative. Where there is no active market for the commodity or other non-financial item in question, the Group assesses the characteristics of such a price related embedded derivative to be closely related to the host contract if the price formula is based on relevant indexations commonly used by other market participants. Contracts are assessed for embedded derivatives when the Group becomes a party to them, including at the date of a business combination.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Certain shareholders' loans provided by the Group to its joint ventures include embedded derivatives that modify cash flows of the loans based on financial (market interest rates) and non-financial (interest rate on borrowings of the lender and free cash flows of the borrower) variables. The risks relating to these variables are interrelated; therefore, terms and conditions of each of these loans related to those variables were defined as a single compound embedded derivative. The Group designated these loans as financial assets at fair value through profit or loss (see Note 27).

In accordance with IAS 39, *Financial instruments: recognition and measurement*, such loans are initially measured at fair value based on future expected cash flows discounted at benchmark interest rates adjusted for the borrower credit risk (Level 3 in the fair value measurement hierarchy described in Note 27). The difference between the loan proceeds and the initial fair value is recorded as the Group's investment in the joint ventures. Subsequently, the loans are measured at fair value at each reporting date with recognition of the revaluation through profit or loss. Interest income and foreign exchanges differences (calculated using the effective interest method), and remaining effect from fair value remeasurement are disclosed separately in the consolidated statement of income.

Non-derivative financial instruments. Non-derivative financial assets include cash and cash equivalents, trade receivables, other financial receivables, some of loans issued, and other investments. The Group classifies its non-derivative financial assets as loans and receivables.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Financial assets classified as loans and receivables are recognized initially at fair value, normally being the transaction price, plus directly attributable transaction costs, and subsequently carried at amortized cost using the effective interest method. Gains and losses are recognized in the consolidated statement of income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Loans and receivables are included in current assets, except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets.

Loans and receivables are analyzed for impairment on a debtor by debtor basis. A provision for impairment of loans and receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to their original terms. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of the provision is recognized within operating expenses in the consolidated statement of income. Subsequent recoveries of amounts previously written off are credited against the amount of the provision in the consolidated statement of income.

The Group's non-derivative financial liabilities are classified as financial liabilities measured at amortized cost.

Financial liabilities included in this category are initially recognized at fair value less directly attributable transaction costs. For interest-bearing debt, the liability is recognized at the fair value of the proceeds received net of associated issue costs. After initial recognition, financial liabilities included in this category are measured at amortized cost using the effective interest method. This category of financial liabilities includes trade and other payables and debt in the consolidated statement of financial position.

Offsetting financial instruments. Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognized amounts, and there is an intention to either settle on a net basis, or to realize the asset and settle the liability simultaneously. Such a right of set off (a) must not be contingent on a future event and (b) must be legally enforceable in all of the following circumstances: (i) in the normal course of business, (ii) in the event of default and (iii) in the event of insolvency or bankruptcy.

Financial guarantee contracts. Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognized initially as a liability at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the higher of the best estimate of the expenditure required to settle the present obligation at the reporting date and the amount recognized less cumulative amortization, if applicable.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Provisions for liabilities and charges. Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events; when 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.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be low.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. Provisions are reassessed at each reporting date and changes in the provisions resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain.

Asset retirement obligations. An asset retirement obligation is recognized when the Group has a present legal or constructive obligation to dismantle, remove and restore items of property, plant and equipment whose construction is substantially completed. The amount of the obligation is the present value of the estimated expenditures expected to be required to settle the obligation, determined using discount rates reflecting adjustments for risks specific to the obligation. Changes in the obligation resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Changes in the obligation, reassessed at each balance sheet date, related to a change in the expected pattern of settlement of the obligation, or in the estimated amount of the obligation or in the discount rates, are treated as a change in an accounting estimate in the current period. Such changes are reflected as adjustments to the carrying value of property, plant and equipment and the corresponding liability.

The Group's exploration, development and production activities involve the use of wells, related equipment and operating sites, oil and gas gathering and treatment facilities and in-field pipelines. Generally, licenses and other regulatory acts require that such assets be decommissioned upon the completion of production, i.e. the Group is obliged to decommission wells, dismantle equipment, restore the sites and perform other related activities. The Group's estimates of these obligations are based on current regulatory or license requirements, as well as actual dismantling and related costs.

The Group's management believes that due to the limited history of gas condensate processing plants activities, the useful lives of these assets are indeterminable (while certain of the operating components and equipment have definite useful lives). Because of these reasons, and the lack of clear legal requirements as to the recognition of obligations, the present value of an asset retirement obligation for such processing facilities cannot be reasonably estimated and, therefore, legal or contractual asset retirement obligations related to these assets are not recognized.

Due to continuous changes in the Russian regulatory and legal environment, there could be future changes to the requirements and contingencies associated with the retirement of long-lived assets.

Pension obligations. The Group contributes to the Pension Fund of the Russian Federation on behalf of its employees based on gross salary payments. Mandatory contributions to the Pension Fund of the Russian Federation, which is a defined contribution plan, are expensed when incurred and are included in the employee compensation in the consolidated statement of income.

The Group also operates a non-contributory post-employment defined benefit plan based on employees' years of service and average salary (see Note 16).

The liability recognized in the consolidated statement of financial position in respect of the defined benefit pension plan is the present value of the defined benefit obligations at the balance sheet date. The present value of the pension obligations are determined by discounting the estimated future cash outflows and then attributing such present value to years of service of the respective employees. The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method. The discount rate was determined by reference to Russian rouble denominated bonds issued by the Government of the Russian Federation chosen to match the duration of the post-employment benefit obligations.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Actuarial gains and losses on assets and liabilities arising from experience adjustments and changes in actuarial assumptions are charged or credited to other comprehensive income in the period in which they arise. They are not reclassified to profit or loss in subsequent periods. Past-service costs are recognized in profit or loss in the period when a plan is amended, and curtailment gains and losses are accounted for as a past-service cost.

Non-financial guarantees. The Group issued a number of parent company guarantees that provide compensation to third parties if a joint venture fails to perform a contractual obligation. Such guarantees meet the definition of insurance contracts and are accounted for under IFRS 4, *Insurance contracts*. Liabilities for non-financial guarantee are recognized when an outflow of resources embodying economic benefits required to settle the obligation is probable. The liabilities are recognized in the amount of best estimates of such an outflow.

Income taxes. The income tax charge or benefit comprises current tax and deferred tax and is recognized in the consolidated statement of income unless it relates to transactions that are recognized, 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 tax authorities in respect of taxable profits or losses for the current and prior periods. Russian tax legislation contains an option to prepare and file a single, consolidated income tax declaration by the taxpayers' group comprised of a holding company and any number of entities with at least 90 percent ownership in each (direct or indirect). Eligible taxpayers' group must be registered with tax authorities and meet certain conditions and criteria. The tax declaration can be submitted then by any member of the group. The Group's management has chosen to adopt this option.

Deferred tax assets and liabilities are recognized in full for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. 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 balance sheet date which are expected to apply to the period when the temporary differences will reverse or when the tax loss carry forwards will be utilized. 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 utilized.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes balances relate to the same taxation authority and the same taxable entity, consolidated tax group of entities or different taxable entities where there is an intention to settle the balances on a net basis. Deferred tax assets and liabilities are netted only with respect to individual companies of the Group (for companies outside the consolidated tax group of companies) and within the consolidated tax payers' group of companies.

The Group controls the reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains upon their disposal. The Group does not recognize deferred tax liabilities on such temporary differences except to the extent that management expects the temporary differences to reverse in the foreseeable future.

Treasury shares. Where any Group company purchases PAO NOVATEK's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to PAO NOVATEK shareholders until the shares are cancelled or reissued or disposed. Where such shares are subsequently reissued or disposed, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to PAO NOVATEK shareholders. Treasury shares are recorded at weighted average cost. Gains or losses resulting from subsequent sales of shares are recorded in the consolidated statement of changes in equity, net of associated costs including taxation.

Dividends. Dividends are recognized as a liability and deducted from shareholders' equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed or declared after the balance sheet date but before the consolidated financial statements are authorized for issue.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition. Revenues represent the fair value of consideration received or receivable for the sale of goods and services in the normal course of business, net of discounts, export duties, value-added tax, excise and fuel taxes.

Revenues from oil and gas sales are recognized when such products are shipped or delivered to customers in accordance with the contract terms, the price is fixed or determinable, and the title has transferred. Revenues from services are recognized in the period in which the services are rendered.

Interest income is recognized as the interest accrues based on the net carrying amount of the financial asset using the effective interest method and presented within finance income in the consolidated statement of income.

General and administrative expenses. General and administrative expenses represent overall corporate management and other expenses related to the general management and administration of the business unit as a whole. They include management and administrative compensation, legal and other advisory expenses, insurance of administrative buildings, social expenses and compensatory payments of general nature not directly linked to the Group's oil and gas activities, charity and other expenses necessary for the administration of the Group.

Earnings per share. Earnings per share are determined by dividing the profit or loss attributable to PAO NOVATEK shareholders by the weighted average number of shares outstanding during the reporting period.

Consolidated statement of cash flows. Cash and cash equivalents comprises cash on hand, cash deposits held with banks and short-term highly liquid investments which are readily convertible to known amounts of cash and which are not subject to significant risk of change in value and have an original maturity of three months or less.

For the purposes of presentation of the consolidated statement of cash flows bank overdrafts are deducted from cash and cash equivalents. Bank overdrafts are shown within short-term debt in current liabilities in the consolidated statement of financial position.

The Group reports cash receipts and the repayments of short-term borrowings which have a maturity of three months or less on a net basis in the consolidated statement of cash flows.

Segment reporting. Operating segments are defined as components of the Group where separate financial information is available and reported regularly to the Group's chief operating decision maker (hereinafter referred to as "CODM", represented by the Management Committee of PAO NOVATEK). Segments whose revenues, results or assets are ten percent or more of the total segments are reported separately.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Consolidated financial statements prepared in accordance with IFRS require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period.

Management reviews these estimates and assumptions on a continuous basis, by reference to past experience and other factors considered as reasonable which form the basis for assessing the book values of assets and liabilities. Adjustments to accounting estimates and assumptions are recognized in the period in which the estimate is revised if the change affects only that period or in the period of the revision and subsequent periods, if both are affected. Management also makes certain judgments, apart from those involving estimations, in the process of applying the Group's accounting policies. Actual results may differ from such estimates if different assumptions or circumstances apply.

Judgments and estimates that have the most significant effect on the amounts reported in these consolidated financial statements and have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are described below.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Fair values of financial assets and liabilities. The fair value of financial assets and liabilities, other than financial instruments that are traded in active markets, is determined by applying various valuation methodologies. Management uses its judgment to make assumptions primarily based on market conditions existing at each reporting date.

Discounted cash flow analysis is used for loans and receivables as well as debt instruments that are not traded in active markets. The effective interest rate is determined by reference to the interest rates of financial instruments available to the Group in active markets. In the absence of such instruments, the effective interest rate is determined by reference to the interest rates of active market financial instruments available adjusted for the Group's specific risk premium estimated by management.

For commodity derivative contracts where observable information is not available, fair value estimations are determined using mark-to-market analysis and other acceptable valuation methods, for which the key inputs include future prices, volatility, price correlation, counterparty credit risk and market liquidity. Fair values of the Group's commodity derivative contracts and sensitivities are presented in Note 27.

Fair value estimation of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and free cash flows from the borrower's strategic plans approved by the shareholders of the joint ventures. Fair values of the shareholders' loans to joint ventures and sensitivities are presented in Note 27.

Deferred income tax asset recognition. Management assesses deferred income tax assets at each reporting date and determines the amount recorded to the extent that realization of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimations based on prior years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

Estimation of oil and gas reserves. Oil and gas reserves have a direct impact on certain amounts reported in the consolidated financial statements, most notably depreciation, depletion and amortization, as well as impairment expenses and asset retirement obligations. Depreciation rates on oil and gas assets using the unit-of-production method are based on proved developed reserves and total proved reserves estimated by the Group in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves. Assuming all variables are held constant, an increase in proved developed reserves for each field decreases depreciation, depletion and amortization expenses. Conversely, a decrease in the estimated proved developed reserves increases depreciation, depletion and amortization expenses. Estimated proved, probable and possible reserves are also used to calculate future cash flows from oil and gas properties, which serve as an indicator in determining their economic lives and whether or not property impairment is present.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. Proved reserves are estimated by reference to available reservoir and well information, including production and pressure trends for producing reservoirs. Furthermore, estimates of proved reserves only include volumes for which access to market is assured with reasonable certainty. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As those fields are further developed, new information may lead to further revisions in reserve estimates.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Although the possibility exists for changes or revisions in estimated reserves to have a critical effect on depreciation, depletion and amortization expenses and, therefore, reported profit for the year, it is expected that in the normal course of business the diversity of the Group's asset portfolio will mitigate the likelihood of this occurring.

Impairment of investments in joint ventures and property, plant and equipment. Management assesses whether there are any indicators of possible impairment of investments in joint ventures and property, plant and equipment at each reporting date based on events or circumstances that indicate that the carrying value of assets may not be recoverable. Such indicators include changes in the Group's business plans, changes in commodity prices leading to unprofitable performances, changes in product mixes, and for oil and gas properties, significant downward revisions of estimated proved reserves.

When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows.

Information about the carrying amounts of property, plant and equipment and long-term investments is presented in Notes 6 and 7.

Impairment provision for trade receivables. The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators to determine that the receivables are potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates.

When there is no expectation of recovering additional cash for an amount receivable, it is written off against the associated provision.

Future cash flows of trade receivables that are 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.

Pension obligations. The costs of defined benefit pension plans and related current service costs are determined using actuarial valuations. The actuarial valuations involve making demographic assumptions (mortality rates, age of retirement, employee turnover and disability) as well as financial assumptions (discount rates, expected rates of return on assets, future salary and pension increases). Due to the long-term nature of these plans, such estimates are subject to significant uncertainty.

Asset retirement obligations. Management makes provision for the future costs of decommissioning oil and gas production facilities, pipelines and related support equipment based on the best estimates of future cost and economic lives of those assets. In accordance with the guidelines of IFRIC 1, *Changes in Existing Decommissioning, Restoration and Similar Liabilities,* the amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the reporting date based on current legislation where the Group's respective operating assets are located, and is also subject to change because of modifications, revisions and changes in laws and regulations and their interpretation thereof. Estimating future asset retirement obligations is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future.

Changes in the measurement of existing obligations can result from changes in estimated timing, future costs or discount rates used in valuation.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

5 ACQUISITIONS AND DISPOSALS

Acquisition of Blue Gaz Sp. z o.o.

In December 2016, in order to expand activities on Polish market, the Group acquired a 100 percent participation interest in Blue Gaz Sp. z o.o., a company owning of a regasification station in Poland, for total cash consideration of RR 26 million (PLN 2 million), which was paid by the end of 2016. The financial and operational activities of Blue Gaz Sp. z o.o. would not have had a material impact on the Group's revenues and results for the year ended 31 December 2016 if the acquisition had occurred in January 2016.

Acquisition of OOO Evrotek-Yuh

In April 2016, the Group acquired a 100 percent participation interest equity stake in OOO Evrotek-Yuh for RR 6 million. Evrotek-Yuh is a holder of the license for exploration and production of hydrocarbons within Ladertoyskiy license area located on the Gydan peninsula in YNAO. Evrotek-Yuh had no notable operating activities up to and as at the acquisition date and accordingly, this acquisition is outside the definition of "business" as defined in IFRS 3, *Business Combinations*. The acquisition cost has been fully allocated to the cost of the license.

Disposal of an ownership interest in OAO Yamal LNG

In December 2015, the Group and China's investment fund Silk Road Fund Co. Ltd., signed the Share Purchase Agreement on the disposal of a 9.9 percent equity stake in Yamal LNG, the Group's joint venture, to the fund. The transaction contained a set of conditions precedent and, in accordance with IFRS 5, *Non-current assets held for sale and discontinued operations,* the Group's 9.9 percent share in Yamal LNG has been classified as an asset held for sale at 31 December 2015. The asset's carrying amount of RR 7,987 million was determined based on the net assets of Yamal LNG on the date of the agreement.

In March 2016, the transaction was closed upon the completion of the conditions precedent, and the Group recognized the disposal of the 9.9 percent stake in Yamal LNG. The transaction included a cash payment and the provision of a 15-year tenor loan to the Group for the purpose of financing the Yamal LNG project (see Note 14). Concurrently, the Group has committed to provide cash contributions to the capital of Yamal LNG with regard to the interest disposed on the same terms that were previously applied upon the entrance of TOTAL S.A. and China National Petroleum Corporation into the project.

The following table summarizes the consideration details and shows the gain on the sale of the ownership interest in Yamal LNG:

	RR million
Cash payment received (EUR 1,087 million at exchange rate of 78.18 to EUR 1.00)	84,978
Adjustment to fair value at initial recognition of the loan from Silk Road Fund, previously recorded as deferred income (see Note 14)	9,173
Less: 49.9 percent share in the Group's liability in relation to capital contributions to Yamal LNG (*) (USD 149 million at exchange rate of 70.15 to USD 1.00)	(10,458)
Less: carrying amount of the Group's disposed 9.9 percent interest in the equity investment previously classified as held for sale	(7,987)
Costs to sell	(2,634)
Gain on the sale of ownership interest before income tax	**73,072**

(*) – excluding the Group's 50.1 percent share in Yamal LNG's capital increase as a result of these contributions.

Consequently, the Group recognized a gain on the transaction of RR 57,677 million, net of associated income tax of RR 15,395 million.

As a result of this transaction, the Group's interest in Yamal LNG is 50.1 percent. The Group continues to exercise joint control over Yamal LNG and recognizes it as a joint venture, and, accordingly, accounts for this investment under the equity method.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

5 ACQUISITIONS AND DISPOSALS (CONTINUED)

Disposal of ownership interest in Artic Russia B.V.

In 2014, NOVATEK and PAO Gazprom Neft agreed in principle to conduct a series of transactions to achieve parity shareholdings in OOO SeverEnergia. As part of such agreement, in August 2015, NOVATEK contributed its 6.4 percent ownership interest in Artic Russia to the capital of OOO Yamal Development. Simultaneously, the Group and Gazprom Neft made contributions to the capital of Yamal Development by converting their loans and accrued interest in the amount of RR 2,512 million and RR 14,922 million, respectively. As a result of these transactions, the Group's effective participation interest in SeverEnergia decreased from 54.9 percent to 53.3 percent.

The gain on the disposal of the 6.4 percent ownership interest in Artic Russia is detailed below:

	RR million
The Group's share in the fair value of contributions to the capital of Yamal Development	14,922
Less: carrying amount of 6.4 percent ownership interest in Artic Russia contributed by the Group	(10,432)
Less: carrying amount of loan and accrued interest converted by the Group	(2,512)
Less: the Group's unrealized gain on the disposal	(989)
Gain on the disposal recognized in the consolidated statement of income before income tax	**989**

As a result of the aforementioned transactions, in August 2015, NOVATEK recognized a gain in the amount of RR 1,978 million. Due to the fact that NOVATEK contributed the equity stake in Artic Russia to the capital of Yamal Development, the Group's joint venture, in which it holds a 50 percent participation interest, the Group eliminated an unrealized gain on the disposal on the consolidation level in the amount of RR 989 million.

The Group's management expects that further steps to achieve parity shareholdings in SeverEnergia will be undertaken in the foreseeable future.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

6 PROPERTY, PLANT AND EQUIPMENT

Movements in property, plant and equipment, for the reporting periods are as follows:

	Oil and gas properties and equipment	Assets under construction and advances for construction	Other	Total
Cost	291,212	63,162	14,422	368,796
Accumulated depreciation, depletion and amortization	(74,962)	-	(2,108)	(77,070)
Net book value at 31 December 2014	**216,250**	**63,162**	**12,314**	**291,726**
Additions	1,558	55,695	306	57,559
Transfers	53,366	(53,882)	516	-
Changes in asset retirement costs	2,410	-	-	2,410
Depreciation, depletion and amortization	(19,009)	-	(552)	(19,561)
Disposals, net	(193)	(197)	(32)	(422)
Cost	348,268	64,778	15,195	428,241
Accumulated depreciation, depletion and amortization	(93,886)	-	(2,643)	(96,529)
Net book value at 31 December 2015	**254,382**	**64,778**	**12,552**	**331,712**
Additions	3,099	29,191	26	32,316
Transfers	58,674	(59,001)	327	-
Acquisition of subsidiaries	53	-	-	53
Changes in asset retirement costs	2,990	-	-	2,990
Depreciation, depletion and amortization	(33,836)	-	(522)	(34,358)
Disposals, net	(645)	(192)	(81)	(918)
Cost	412,352	34,776	15,402	462,530
Accumulated depreciation, depletion and amortization	(127,635)	-	(3,100)	(130,735)
Net book value at 31 December 2016	**284,717**	**34,776**	**12,302**	**331,795**

Included in additions to property, plant and equipment for the years ended 31 December 2016 and 2015 are capitalized interest and foreign exchange differences of RR 5,314 million and RR 8,515 million, respectively.

Included within assets under construction and advances for construction are advances to suppliers for construction and equipment of RR 1,438 million and RR 2,719 million at 31 December 2016 and 2015, respectively.

In 2016, the Group purchased through auctions oil and gas exploration and production licenses for the Nyakhartinsky and Syadorsky license areas located in the YNAO and Tanamskiy license area located in Krasnoyarsk Territory for the total amount of RR 1,928 million, which were included in additions to oil and gas properties and equipment.

During 2016, the major transfers to oil and gas properties and equipment related to the Yarudeyskoye and East-Tarkosalinskoye fields in the amount of RR 21,631 million and RR 11,524 million, respectively.

During 2015, the major transfers to oil and gas properties and equipment in the amount of RR 26,408 million related to the launch of commercial production at the Yarudeyskoye oil field.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The table below summarizes the Group's carrying values of total acquisition costs of proved and unproved properties included in oil and gas properties and equipment:

	At 31 December 2016	At 31 December 2015
Proved properties acquisition costs	47,243	46,343
Less: accumulated depreciation, depletion and amortization of proved properties acquisition costs	(16,782)	(15,540)
Unproved properties acquisition costs	10,069	7,874
Total acquisition costs	**40,530**	**38,677**

The Group's management believes these costs are recoverable as the Group has plans to explore and develop the respective fields.

Reconciliation of depreciation, depletion and amortization (DDA):

	Year ended 31 December:	
	2016	2015
Depreciation, depletion and amortization of property, plant and equipment	34,358	19,561
Add: DDA of intangible assets	554	566
Less: DDA capitalized in the course of intra-group construction services	(281)	(147)
DDA as presented in the consolidated statement of income	**34,631**	**19,980**

At 31 December 2016 and 2015, no property, plant and equipment were pledged as security for the Group's borrowings. No impairment was recognized in respect of oil and gas properties and equipment for the years ended 31 December 2016 and 2015.

Capital commitments are disclosed in Note 28.

Exploration for and evaluation of mineral resources. The amounts of assets, liabilities, expense and cash flows arising from the exploration and evaluation of mineral resources comprise the following:

	Year ended 31 December:	
	2016	2015
Net book value of assets value at 1 January	**14,744**	**12,726**
Additions	5,297	5,141
Expensed	(3)	(21)
Acquisition of subsidiaries	7	-
Reclassification to proved properties and development expenditures	(4,573)	(3,102)
Net book value of assets at 31 December	**15,472**	**14,744**
Liabilities	384	330
Cash flows used for operating activities	1,891	1,020
Cash flows used for investing activities	4,085	2,769

For the years ended 31 December 2016 and 2015, within operating expenses the Group has recognized exploration expenses in the amount of RR 2,087 million and RR 1,109 million, respectively. These expenses included employee compensations in the amount of RR 300 million and RR 263 million, respectively.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES

	At 31 December 2016	At 31 December 2015
Joint ventures:		
OAO Yamal LNG	126,688	38,798
OOO Yamal Development	55,228	43,551
ZAO Nortgas	51,222	50,298
Artic Russia B.V.	24,449	22,078
ZAO Terneftegas	2,063	-
Total investments in joint ventures	**259,650**	**154,725**

The Group considers that Yamal LNG, Yamal Development, Nortgas, Artic Russia and Terneftegas constitute jointly controlled entities on the basis of the existing contractual arrangements. The Charters and Shareholders' agreements of these entities stipulate that strategic and/or key decisions of a financial, operating and capital nature require effectively the unanimous approval by all shareholders or by a group of shareholders. The Group accounts for its shares in joint ventures under the equity method.

OAO Yamal LNG. The Group holds a 50.1 percent ownership in Yamal LNG, along with TOTAL S.A. (20 percent), China National Petroleum Corporation ("CNPC", 20 percent) and Silk Road Fund Co. Ltd. (9.9 percent). At 31 December 2015, the Group held a 60 percent ownership in the joint venture, including a 9.9 percent share classified as an asset held for sale, which was sold to Silk Road Fund Co. Ltd. in March 2016 (see Note 5). The joint venture is responsible for implementing the Yamal LNG project including the construction of production facilities for natural gas, gas condensate and liquefied natural gas ("LNG") based on the resources of the South-Tambeyskoye field, located on the Yamal peninsula in the YNAO. Yamal LNG is the holder of the LNG export license.

In 2016, Yamal LNG has signed agreements with a number of Russian and foreign banks to raise project financing in the form of credit lines for the total amount of EUR 13.9 billion and CNY 7.6 billion with a repayment period from December 2019 to June 2031. At 31 December 2016, the Group's 50.1 percent ownership in Yamal LNG was pledged in connection with these facility agreements.

ZAO Nortgas. The Group holds a 50 percent ownership in Nortgas, its joint venture with PAO Gazprom Neft. Nortgas operates the North-Urengoyskoye field, located in the YNAO.

Artic Russia B.V. The Group holds a direct 13.6 percent participation interest in Artic Russia, domiciled in the Netherlands. Artic Russia holds a 49 percent participation interest in OOO SeverEnergia.

OOO Yamal Development. The Group holds a 50 percent participation interest in Yamal Development, its joint venture with PAO Gazprom Neft (50 percent). Yamal Development holds a 51 percent participation interest in SeverEnergia and an 86.4 percent ownership interest in Artic Russia.

OOO SeverEnergia. The Group holds an effective 53.3 percent participation interest in SeverEnergia through two of the Group's other joint ventures, Yamal Development and Artic Russia. SeverEnergia through its wholly owned subsidiary OAO Arcticgas operates the Samburgskoye, Urengoyskoye and Yaro-Yakhinskoye fields, located in the YNAO.

ZAO Terneftegas. The Group holds a 51 percent ownership in Terneftegas, its joint venture with TOTAL S.A. (49 percent). Terneftegas operates the Termokarstovoye field, located in the YNAO.

The Group's investment in Terneftegas at 31 December 2015 was valued at RR nil in the consolidated statement of financial position due to the Group's proportionate share of accumulated losses exceeding the Group's cost of investment. The unrecognized share of accumulated losses of Terneftegas at 31 December 2015 was RR 1,409 million. During 2016, the Group's proportionate share of profit of Terneftegas exceeded the Group's share of previously unrecognized accumulated losses, thereafter the Group resumed recognizing its share of profits of Terneftegas.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

The table below summarizes the movements in the carrying amounts of the Group's joint ventures:

	Year ended 31 December:	
	2016	**2015**
At 1 January	**154,725**	**166,231**
Share of profit from operations	33,655	32,052
Share of finance income (expense)	74,236	(68,821)
Share of total income tax benefit (expense)	(17,052)	5,162
Share of profit (loss) of joint ventures, net of income tax	**90,839**	**(31,607)**
Share of other comprehensive loss of joint ventures	(21)	-
Effect from initial measurement of loans provided by the Group to joint ventures (see Note 27)	836	14,185
Contributions to equity	9,802	14,922
Disposal of stakes in joint ventures	-	(11,421)
Effect from other changes in joint ventures' net assets	2,819	9,285
Group's costs capitalized in investments	753	-
Elimination of the Group's share in profits of joint ventures from hydrocarbons balances purchased by the Group from joint ventures and not sold at the reporting date	(103)	1,117
Reclassification to assets held for sale	-	(7,987)
At 31 December	**259,650**	**154,725**

In September 2016, the capital of Yamal LNG was increased through a cash contribution made by the Group as a result of the disposal of the 9.9 percent stake in Yamal LNG (see Note 5) in the amount of RR 19,565 million. The Group's 50.1 percent share in Yamal LNG's capital increase was recorded in the Group's investment in Yamal LNG in the amount of RR 9,802 million. The Group's shareholding in Yamal LNG did not change notably as a result of this capital contribution.

In August 2015, the Group disposed of its 6.4 percent ownership interest in Artic Russia at cost of RR 11,421 million, including an unrealized gain on disposal. Simultaneously, the equity of Yamal Development was increased through proportional contributions by its participants totalling RR 29,844 million, of which RR 14,922 million was contributed by NOVATEK (see Note 5).

For the years ended 31 December 2016 and 2015, the Group recorded an increase in equity in the amount of RR 2,819 million and RR 3,329 million, respectively, from the initial measurement of the disproportional loans provided to Yamal LNG by other shareholders.

In December 2015, the capital of Yamal LNG was increased by RR 21,256 million through the conversions of loans obtained by the joint venture from TOTAL S.A. and CNPC. These capital contributions were made by TOTAL S.A. and CNPC as a settlement of the third tranche (USD 143 million each) representing a part of the consideration for the acquisition of the 20 percent interests in Yamal LNG by each of the companies in 2011 and 2013, respectively. The Group's share (50.1 percent ownership excluding the share classified as held for sale) in the increase of the capital of Yamal LNG amounted to RR 10,649 million. The excess of the Group's share in the contributions over the amount of the third tranche previously recognized within the investment in Yamal LNG amounted to RR 5,956 million and was recorded as an increase in the investment in Yamal LNG, with the corresponding effect recognized in the consolidated statement of changes in equity in accordance with the Group's accounting policy. The Group's shareholding in Yamal LNG did not change notably as a result of this transaction.

For the year ended 31 December 2016, the Group recorded commission fees in the amount of 753 million for the guarantee received from the State corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank)" (see Note 28) as an increase to the investment in Yamal LNG.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

The Group eliminates its share in profits of joint ventures from natural gas and liquid hydrocarbons balances purchased by the Group from its joint ventures and not sold at the reporting date.

The summarized statements of financial position for the Group's principal joint ventures are as follows:

At 31 December 2016	Yamal LNG	SeverEnergia	Nortgas
Property, plant and equipment and materials for construction	1,265,939	385,404	138,768
Other non-current non-financial assets	273	278	47
Non-current financial assets	6,061	120,655	11,213
Total non-current assets	**1,272,273**	**506,337**	**150,028**
Cash and cash equivalents	12,842	13,517	277
Other current financial assets	23,211	15,520	2,639
Current non-financial assets	14,314	1,013	631
Total current assets	**50,367**	**30,050**	**3,547**
Non-current financial liabilities	(1,016,196)	(130,872)	(24,795)
Non-current non-financial liabilities	(35,798)	(57,555)	(23,544)
Total non-current liabilities	**(1,051,994)**	**(188,427)**	**(48,339)**
Trade payables and accrued liabilities	(17,628)	(14,308)	(1,302)
Other current financial liabilities	-	(29,355)	-
Current non-financial liabilities	(148)	(11,669)	(1,490)
Total current liabilities	**(17,776)**	**(55,332)**	**(2,792)**
Net assets	**252,870**	**292,628**	**102,444**

At 31 December 2015	Yamal LNG	SeverEnergia	Nortgas
Property, plant and equipment and materials for construction	752,387	396,185	141,615
Other non-current non-financial assets	1	351	30
Non-current financial assets	135	96,221	10,204
Total non-current assets	**752,523**	**492,757**	**151,849**
Cash and cash equivalents	64,813	13,801	2,160
Other current financial assets	6,390	12,592	2,674
Current non-financial assets	22,811	1,849	468
Total current assets	**94,014**	**28,242**	**5,302**
Non-current financial liabilities	(753,099)	(161,051)	(24,841)
Non-current non-financial liabilities	(3,488)	(54,853)	(23,540)
Total non-current liabilities	**(756,587)**	**(215,904)**	**(48,381)**
Trade payables and accrued liabilities	(11,994)	(14,234)	(241)
Other current financial liabilities	-	(28,976)	(5,908)
Current non-financial liabilities	(514)	(9,110)	(2,025)
Total current liabilities	**(12,508)**	**(52,320)**	**(8,174)**
Net assets	**77,442**	**252,775**	**100,596**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

The summarized statements of comprehensive income of the Group's principal joint ventures are presented below:

For the year ended 31 December 2016	Yamal LNG	SeverEnergia	Nortgas
Revenue	2,722	133,229	25,697
Depreciation, depletion and amortization	(650)	(26,451)	(7,749)
Profit from operations	670	55,585	4,368
Change in fair value of non-commodity financial instruments	(25,223)	-	-
Foreign exchange gain (loss), net	200,485	25	-
Profit before income tax	176,043	47,806	2,436
Income tax expense	(28,952)	(7,930)	(574)
Profit, net of income tax	**147,091**	**39,876**	**1,862**
Other comprehensive loss	(27)	(23)	(14)
Total comprehensive income	**147,064**	**39,853**	**1,848**

For the year ended 31 December 2015	Yamal LNG	SeverEnergia	Nortgas
Revenue	2,606	126,129	28,893
Depreciation, depletion and amortization	(814)	(28,944)	(8,205)
Profit (loss) from operations	(1,829)	53,858	9,287
Change in fair value of non-commodity financial instruments	19,036	-	-
Foreign exchange gain (loss), net	(102,084)	(15)	-
Profit (loss) before income tax	(84,962)	47,049	5,793
Income tax benefit (expense)	13,655	(8,697)	(1,192)
Total comprehensive income (loss)	**(71,307)**	**38,352**	**4,601**

The information above reflects the amounts presented in the financial statements of the joint ventures adjusted for differences in accounting policies between the Group and the joint ventures.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

Reconciliation of the summarized financial information presented to the Group's share in net assets of the joint ventures:

As at and for the year ended 31 December 2016	Yamal LNG	SeverEnergia	Nortgas
Net assets at 1 January 2016	**77,442**	**252,775**	**100,596**
Profit (loss), net of income tax	147,091	39,876	1,862
Other comprehensive loss	(27)	(23)	(14)
Other equity movements	28,364	-	-
Net assets at 31 December 2016	**252,870**	**292,628**	**102,444**
Ownership	50.1%	53.3%	50%
Group's share in net assets	**126,688**	**156,059**	**51,222**
As at and for the year ended 31 December 2015			
Net assets at 1 January 2015	**96,936**	**216,534**	**95,995**
Profit (loss), net of income tax	(71,307)	38,352	4,601
Other equity movements	51,813	-	-
Disposal of stakes in joint ventures	-	(2,111)	-
Net assets at 31 December 2015	**77,442**	**252,775**	**100,596**
Ownership excluding interests classified as held for sale	50.1%	53.3%	50%
Group's share in net assets	**38,798**	**134,729**	**50,298**

At 31 December 2016 and 2015, the Group's cumulative investments in Artic Russia and Yamal Development totaled RR 79,677 million and RR 65,629 million, respectively, which differed from the Group's share in the net assets of SeverEnergia. The differences of RR 76,382 million and RR 69,100 million mainly relate to the Group's interest in debt liabilities of Yamal Development and goodwill relating to acquisition of Arctic Russia, through which entities the Group holds the investments in SeverEnergia.

8 LONG-TERM LOANS AND RECEIVABLES

	At 31 December 2016	At 31 December 2015
Long-term loans	184,621	214,051
Long-term interest receivable	24,390	16,190
Other long-term receivables	442	558
Total	**209,453**	**230,799**
Less: current portion of long-term loans	(308)	-
Total long-term loans and receivables	**209,145**	**230,799**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

8 LONG-TERM LOANS AND RECEIVABLES (CONTINUED)

The Group's long-term loans by borrowers are as follows:

	At 31 December 2016	At 31 December 2015
OAO Yamal LNG	173,845	196,533
OOO Yamal Development	7,575	13,105
ZAO Terneftegas	3,201	4,413
Total long-term loans	**184,621**	**214,051**

OAO Yamal LNG. In accordance with the Shareholders' agreement, the Group provided US dollar and Euro credit line facilities to Yamal LNG, the Group's joint venture. Under the terms of these credit line facilities, the Group provided loans to Yamal LNG prior to obtaining external project financing. During 2016 and 2015, the Group provided RR 6,645 million and RR 104,076 million, respectively, under these credit line facilities.

The loans interest rate in 2016 and 2015 was ranging from 4.29 to 4.46 percent per annum. The interest rate can be adjusted during subsequent periods subject to certain conditions. The repayment schedule is linked to free cash flows of the joint venture.

OOO Yamal Development. The Group provided Russian rouble denominated loans under agreed credit line facilities to Yamal Development, the Group's joint venture. The loans are repayable not later than 2021 and bear interest rates ranging from 9.25 to 10.90 percent per annum.

During 2015, the Group provided RR 4,494 million under these credit line facilities. In August 2015, the Group made a contribution to the capital of Yamal Development by converting a part of the loans in the amount of RR 2,200 million (see Note 5), and in December 2015, Yamal Development repaid a part of the loans to the Group in the amount of RR 2,550 million ahead of the maturity schedule.

During 2016, Yamal Development repaid to the Group a part of the loans in the total amount of RR 5,530 million ahead of the maturity schedule.

ZAO Terneftegas. In accordance with the Shareholders' agreement, the Group provided US dollar denominated loans to Terneftegas, the Group's joint venture.

For the year ended 31 December 2016, Terneftegas repaid to the Group a part of the loans and accrued interest in the total amount of RR 1,298 million. For the year ended 31 December 2015, Terneftegas repaid to the Group a part of the loans in the amount of RR 1,160 million.

The loans interest rate in 2016 and 2015 was ranging from 4.47 to 4.60 percent per annum. The interest rate can be adjusted during subsequent periods subject to certain conditions. The repayment schedule is linked to free cash flows of the joint venture.

No provisions for impairment of long-term loans and receivables were recognized at 31 December 2016 and 2015. The carrying values of long-term loans and receivables approximate their respective fair values.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

9 OTHER NON-CURRENT ASSETS

	At 31 December 2016	At 31 December 2015
Financial assets		
Commodity derivatives	1,172	1,511
Other financial assets	157	10
Non-financial assets		
Long-term advances	20,882	17,551
Deferred income tax assets	4,671	11,183
Materials for construction	2,004	2,407
Intangible assets, net	1,510	1,567
Other non-financial assets	88	87
Total other non-current assets	**30,484**	**34,316**

At 31 December 2016 and 2015, the long-term advances represented advances to OAO Russian Railways. The advances were paid in accordance with the Strategic Partnership Agreement signed with Russian Railways in 2012.

10 INVENTORIES

	At 31 December 2016	At 31 December 2015
Natural gas and liquid hydrocarbons	6,765	6,462
Materials and supplies (net of provision of RR 4 million at 31 December 2016 and 2015)	2,247	1,745
Other inventories	32	19
Total inventories	**9,044**	**8,226**

No inventories were pledged as security for the Group's borrowings or payables at both dates.

11 TRADE AND OTHER RECEIVABLES

	At 31 December 2016	At 31 December 2015
Trade receivables (net of provision of RR 196 million and RR 95 million at 31 December 2016 and 2015, respectively)	40,606	35,221
Other receivables (net of provision of RR 22 million and RR 18 million at 31 December 2016 and 2015, respectively)	980	2,343
Total trade and other receivables	**41,586**	**37,564**

Trade receivables in the amount of RR 5,362 million at 31 December 2016 are secured by letters of credit, issued by banks with investment grade rating. The Group does not hold any other collateral as security for trade and other receivables (see Note 27 for credit risk disclosures).

The carrying values of trade and other receivables approximate their respective fair values. Trade and other receivables were categorized as Level 3 in the fair value measurement hierarchy described in Note 27.

Trade and other receivables that are less than three months past due are generally not considered for impairment unless other indicators of impairment exist. Trade and other receivables of RR 4,269 million and RR 4,998 million at 31 December 2016 and 2015, respectively, were past due but not impaired. The Group has assessed the payment history of these accounts and recognized impairment where deemed necessary.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

11 TRADE AND OTHER RECEIVABLES (CONTINUED)

The ageing analysis of these past due but not impaired trade and other receivables is as follows:

	At 31 December 2016	At 31 December 2015
Up to 90 days past-due	3,628	3,624
91 to 360 days past-due	561	1,225
Over 360 days past-due	80	149
Total past due but not impaired	**4,269**	**4,998**
Not past due and not impaired	37,317	32,566
Total trade and other receivables	**41,586**	**37,564**

Movements in the Group provision for impairment of trade and other receivables are as follows:

	Year ended 31 December:	
	2016	2015
At 1 January	**113**	**317**
Additional provision recorded	269	79
Receivables written off as uncollectible	(68)	(58)
Provision reversed	(96)	(225)
At 31 December	**218**	**113**

The provision for impaired trade and other receivables has been included in the consolidated statement of income in impairment reversals (expenses), net.

12 PREPAYMENTS AND OTHER CURRENT ASSETS

	At 31 December 2016	At 31 December 2015
Financial assets		
Commodity derivatives	2,920	5,039
Current portion of long-term loans receivable (see Note 8)	308	-
Cash on special accounts	-	6,477
Non-financial assets		
Value-added tax receivable	10,456	13,437
Prepayments and advances to suppliers	5,998	5,304
Recoverable value-added tax	5,736	7,554
Deferred transportation expenses for liquid hydrocarbons	1,903	1,720
Deferred transportation expenses for natural gas	1,901	2,955
Prepaid customs duties	1,756	559
Deferred export duties for liquid hydrocarbons	1,643	2,251
Other non-financial assets	627	128
Total prepayments and other current assets	**33,248**	**45,424**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

13 CASH AND CASH EQUIVALENTS

	At 31 December 2016	At 31 December 2015
Cash at current bank accounts	31,525	11,243
Bank deposits with original maturity of three months or less	16,776	17,944
Total cash and cash equivalents	**48,301**	**29,187**

All deposits are readily convertible to known amounts of cash and are not subject to significant risk of change in value (see Note 27 for credit risk disclosures).

14 LONG-TERM DEBT

	At 31 December 2016	At 31 December 2015
Corporate bonds		
Eurobonds – Ten-Year Tenor (par value USD 1 billion, repayable in 2022)	60,503	72,662
Eurobonds – Ten-Year Tenor (par value USD 650 million, repayable in 2021)	39,318	47,207
Eurobonds – Four-Year Tenor (par value RR 14 billion, repayable in 2017)	13,996	13,977
Eurobonds – Five-Year Tenor (par value USD 600 million, repayable in 2016)	-	43,725
Bank loans		
Syndicated term credit line facility	41,906	83,861
Other bank loans	6,381	-
Other borrowings		
Loan from Silk Road Fund	41,125	48,619
Other loans	13,536	19,268
Total	**216,765**	**329,319**
Less: current portion of long-term debt	(55,469)	(77,269)
Total long-term debt	**161,296**	**252,050**

Eurobonds. In December 2012, the Group issued US dollar denominated Eurobonds in the amount of USD 1 billion. The US dollar denominated Eurobonds were issued with an annual coupon rate of 4.422 percent, payable semi-annually. The Eurobonds have a ten-year tenor and are repayable in December 2022.

In February 2011, the Group issued US dollar denominated Eurobonds in an aggregate amount of USD 1,250 million. The US dollar denominated Eurobonds were issued at par in two tranches, a ten-year USD 650 million Eurobond with an annual coupon rate of 6.604 percent and a five-year USD 600 million Eurobond with an annual coupon rate of 5.326 percent. The coupons are payable semi-annually. The ten-year USD 650 million Eurobond is repayable in February 2021.The five-year USD 600 million Eurobond was fully repaid at its maturity date in February 2016.

In February 2013, the Group issued four-year tenor Russian rouble denominated Eurobonds in the amount of RR 14 billion. The Russian rouble denominated Eurobonds were issued with an annual coupon rate of 7.75 percent, payable semi-annually. Subsequent to the balance sheet date, in February 2017, the four-year RR 14 billion Eurobond was fully repaid at its maturity date.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

14 LONG-TERM DEBT (CONTINUED)

Syndicated term credit line facility. In June 2013, the Group obtained a USD 1.5 billion unsecured syndicated term credit line facility from a range of international banks and withdrew the full amount under the facility by June 2014. The loan is repayable until July 2018 by quarterly installments starting from June 2015. The facility includes the maintenance of certain restrictive financial covenants.

Other bank loans. In December 2016, the Group obtained a EUR 100 million loan from a Russian subsidiary of a foreign bank. The loan is repayable in December 2019. The facility includes the maintenance of certain restrictive financial covenants.

Loan from Silk Road Fund. As part of the transaction for the sale of the Group's 9.9 percent equity stake in OAO Yamal LNG, in December 2015, the Group obtained a loan from Silk Road Fund for financing of the Yamal LNG project (see Note 5).

In accordance with IAS 39, *Financial instruments: recognition and measurement*, the loan was recorded at fair value at initial recognition with the difference of RR 9,173 million between the fair value of the loan and cash received recognized as deferred income (see Note 17). In March 2016, the deferred income was included in the financial result on disposal of the 9.9 percent equity stake in Yamal LNG upon completion of the transaction (see Note 5).

The loan is repayable until December 2030 by semi-annual installments starting from December 2019 and includes the maintenance of certain restrictive financial covenants.

Other loans. At 31 December 2016 and 2015, other loans represented Russian rouble denominated loans, which were provided to one of the Group's subsidiaries by its non-controlling shareholder. The loans are repayable until the end of 2017. During the year ended 31 December 2016, a portion of the loans and accrued interest in the amount of RR 8,673 million was repaid ahead of maturity schedule.

The fair value of long-term debt including its current portion was RR 224,183 million and RR 319,191 million at 31 December 2016 and 2015, respectively. The fair value of the corporate bonds was determined based on market quote prices (Level 1 in the fair value measurement hierarchy described in Note 27). The fair value of other long-term loans was determined based on future cash flows discounted at the estimated risk-adjusted discount rate (Level 3 in the fair value measurement hierarchy described in Note 27).

Scheduled maturities of long-term debt at the reporting date were as follows:

Maturity period:	**At 31 December 2016**
1 January 2018 to 31 December 2018	13,968
1 January 2019 to 31 December 2019	8,169
1 January 2020 to 31 December 2020	3,576
1 January 2021 to 31 December 2021	42,894
After 31 December 2021	92,689
Total long-term debt	**161,296**

Available credit line facilities. At 31 December 2016, the Group had available long-term credit line facilities from Russian banks with credit limits in the amount of RR 50 billion and the equivalent of USD 750 million. The facilities include the maintenance of certain restrictive financial covenants.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

15 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT

	At 31 December 2016	At 31 December 2015
Loans with original maturity more than three months	-	21,300
Loans with original maturity three months or less	-	8,086
Total short-term debt	**-**	**29,386**
Add: current portion of long-term debt	55,469	77,269
Total short-term debt and current portion of long-term debt	**55,469**	**106,655**

Loans with original maturity more than three months. At 31 December 2015, short-term debt included a loan obtained by the Group under a non-revolving credit line facility from a Russian bank in the amount of RR 20 billion. In 2016, the loan was fully repaid.

At 31 December 2015, short-term debt also included loans obtained by one of the Group's subsidiaries from its non-controlling shareholder in the amount of RR 1,300 million. In 2016, these loans were fully repaid.

Loans with original maturity three months or less. In 2015 and 2016, the Group had available revolving credit line facilities under which obtained loans with original maturities three months or less to finance trade activities secured by cash revenues from specifically determined liquid hydrocarbons export sales contracts. At 31 December 2016, these loans were repaid.

Available credit line facilities. At 31 December 2016, the Group had available revolving credit line facilities from Russian banks, with total credit limits in the amount of RR 70 billion.

16 PENSION OBLIGATIONS

Defined contribution plan. For the years ended 31 December 2016 and 2015, total amounts recognized as an expense in respect of payments made by employer on behalf of employees to the Pension Fund of the Russian Federation were RR 1,853 million and RR 1,803 million, respectively.

Defined benefit plan. The Group operates a post-employment benefit program for its retired employees. Under the current terms of pension program, employees who are employed by the Group for more than five years and retire from the Group on or after the statutory retirement age will receive lump sum retirement benefit and monthly payments from NOVATEK for life unless they are actively employed. The amounts of payments to be disbursed depend on the employee's average salary, duration and location of employment.

The program represents an unfunded defined benefit plan and is accounted for as such under provisions of IAS 19, *Employee Benefits*. The present value of the defined benefit obligation is included in other non-current liabilities in the consolidated statement of financial position. The impact of the program on the consolidated financial statements is disclosed below.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

16 PENSION OBLIGATIONS (CONTINUED)

The movements in the present value of the defined benefit obligation are as follows:

	Year ended 31 December:	
	2016	2015
At 1 January	**1,905**	**1,167**
Interest cost	201	152
Current service cost	126	83
Benefits paid	(105)	(88)
Pension plan revision	-	(51)
Actuarial remeasurement arising from:		
- changes in financial assumptions	110	595
- changes in demographic assumptions	(24)	37
- experience adjustment	36	10
At 31 December	**2,249**	**1,905**
Defined benefit plan (benefits) costs were recognized in:		
Materials, services and other (as employee compensation)	184	107
General and administrative expenses (as employee compensation)	143	128
Other comprehensive (income) loss	122	642

The principal actuarial assumptions used are as follows:

	At 31 December 2016	At 31 December 2015
Weighted average discount rate	8.3%	10.0%
Projected annual increase in employee compensation	5.0%	5.6%
Expected increases to pension benefits	6.5%	5.6%

The assumed average salary and pension payment increases for Group employees have been calculated on the basis of inflation forecasts, analysis of increases of past salaries and the general salary policy of the Group. Inflation forecasts have been estimated to reduce from 5.4 percent in 2017 to 4.3 percent in 2022 and subsequent years.

Mortality assumptions are based on the Russian mortality tables published by the State Statistics Committee of the Russian Federation from the year 2010 adjusted for estimates of mortality improvements in the future periods, which management believes are the most conservative and prudent Russian whole-population mortality tables available.

Management has assessed that reasonable changes in the principal significant actuarial assumptions will not have a significant impact on the consolidated statement of income or the consolidated statement of comprehensive income or the liability recognized in the consolidated statement of financial position.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

17 TRADE PAYABLES AND ACCRUED LIABILITIES

	At 31 December 2016	At 31 December 2015
Financial liabilities		
Trade payables	25,828	23,989
Commodity derivatives	2,754	2,355
Interest payable	1,821	3,100
Other payables	463	3,401
Non-financial liabilities		
Advances from customers	2,483	4,099
Salary payables	338	494
Deferred income	-	9,173
Other liabilities and accruals	4,775	1,924
Total trade payables and accrued liabilities	**38,462**	**48,535**

At 31 December 2015, other payables included outstanding liability related to the acquisition of AO Office in August 2014 which was paid during 2016 in the amount of RR 2,929 million (USD 39 million). During 2015, the Group paid RR 3,630 million (USD 62 million) under this transaction.

The carrying values of trade payables and accrued liabilities approximate their respective fair values. Trade and other payables were categorized as Level 3 in the fair value measurement hierarchy described in Note 27.

18 SHAREHOLDERS' EQUITY

Ordinary share capital. Share capital issued and paid in consisted of 3,036,306,000 ordinary shares with a par value of RR 0.1 each at 31 December 2016 and 2015. The total authorized number of ordinary shares was 10,593,682,000 shares at both dates.

Treasury shares. In accordance with the *Share Buyback Programs* authorized by the Board of Directors, the Group's wholly owned subsidiary, Novatek Equity (Cyprus) Limited, purchases ordinary shares of PAO NOVATEK in the form of Global Depository Receipts (GDRs) on the London Stock Exchange (LSE) and ordinary shares on the Moscow Exchange through the use of independent brokers. NOVATEK also purchases its ordinary shares from shareholders where required by Russian legislation.

During the years ended 31 December 2016 and 2015, the Group purchased 1.4 million and 1.3 million ordinary shares (both ordinary shares and GDRs) at a total cost of RR 916 million and RR 775 million, respectively. At 31 December 2016 and 2015, the Group held in total (both ordinary shares and GDRs) 18.6 million and 17.2 million ordinary shares at a total cost of RR 6,913 million and RR 5,997 million, respectively. The Group has decided that these shares do not vote.

Dividends. Dividends (including tax on dividends) declared and paid were as follows:

	Year ended 31 December:	
	2016	2015
Dividends payable at 1 January	1	1
Dividends declared (*)	41,653	35,640
Dividends paid (*)	(41,653)	(35,640)
Dividends payable at 31 December	**1**	**1**
Dividends per share declared during the year (in Russian roubles)	13.80	11.80
Dividends per GDR declared during the year (in Russian roubles)	138.0	118.0

(*) – excluding treasury shares.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

18 SHAREHOLDERS' EQUITY (CONTINUED)

The Group declares and pays dividends in Russian roubles. Dividends declared in 2016 and 2015 were as follows:

Final for 2015: RR 6.90 per share or RR 69.0 per GDR declared in April 2016	20,951
Interim for 2016: RR 6.90 per share or RR 69.0 per GDR declared in September 2016	20,951
Total dividends declared in 2016	**41,902**
Final for 2014: RR 5.20 per share or RR 52.0 per GDR declared in April 2015	15,789
Interim for 2015: RR 6.60 per share or RR 66.0 per GDR declared in September 2015	20,040
Total dividends declared in 2015	**35,829**

Distributable retained earnings. The basis for distribution of profits of a company to shareholders is defined by Russian legislation as net profit presented in its statutory financial statements prepared in accordance with the Regulations on Accounting and Reporting of the Russian Federation, which may differ significantly from amounts calculated on the basis of IFRS. At 31 December 2016 and 2015, NOVATEK's closing balances of the accumulated profit including the respective year's net statutory profit totalled RR 366,928 million and RR 260,842 million, respectively.

19 OIL AND GAS SALES

	Year ended 31 December:	
	2016	**2015**
Natural gas	229,716	222,180
Naphtha	103,103	95,588
Crude oil	64,952	14,873
Other gas and gas condensate refined products	57,163	61,902
Stable gas condensate	47,271	43,997
Liquefied petroleum gas	31,652	33,467
Total oil and gas sales	**533,857**	**472,007**

20 PURCHASES OF NATURAL GAS AND LIQUID HYDROCARBONS

	Year ended 31 December:	
	2016	**2015**
Unstable gas condensate	93,854	91,078
Natural gas	38,119	27,715
Other liquid hydrocarbons	2,295	1,711
Total purchases of natural gas and liquid hydrocarbons	**134,268**	**120,504**

The Group purchases 50 percent of the natural gas volumes produced by its joint venture ZAO Nortgas, some volumes of natural gas produced by its joint venture OOO SeverEnergia (through its wholly owned subsidiary, OAO Arcticgas) and, commencing May 2015, all volumes of natural gas produced by its joint venture ZAO Terneftegas (see Note 30).

The Group purchases all volumes of unstable gas condensate produced by its joint ventures Nortgas, SeverEnergia (through its wholly owned subsidiary, Arcticgas) and Terneftegas (from May 2015) at ex-field prices based on benchmark crude oil prices (see Note 30).

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

21 TRANSPORTATION EXPENSES

	Year ended 31 December: 2016	2015
Natural gas transportation by trunk and low-pressure pipelines	84,808	86,025
Stable gas condensate and liquefied petroleum gas transportation by rail	31,838	29,273
Gas condensate refined products, stable gas condensate and crude oil transportation by tankers	9,997	13,378
Crude oil transportation by trunk pipelines	6,654	1,476
Other	165	77
Total transportation expenses	**133,462**	**130,229**

22 TAXES OTHER THAN INCOME TAX

The Group is subject to a number of taxes other than income tax, which are detailed as follows:

	Year ended 31 December: 2016	2015
Unified natural resources production tax	40,997	33,656
Property tax	2,793	2,603
Other taxes	263	371
Total taxes other than income tax	**44,053**	**36,630**

23 MATERIALS, SERVICES AND OTHER

	Year ended 31 December: 2016	2015
Employee compensation	7,558	6,004
Repair and maintenance	3,026	1,959
Complex of services for preparation, transportation and processing of hydrocarbons	2,062	1,756
Materials and supplies	1,838	1,305
Electricity and fuel	1,101	938
Liquefied petroleum gas volumes reservation expenses	1,017	768
Security services	660	470
Transportation services	641	452
Insurance expenses	372	267
Rent expenses	257	59
Other	601	573
Total materials, services and other	**19,133**	**14,551**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

24 GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December:	
	2016	2015
Employee compensation	12,327	9,364
Social expenses and compensatory payments	2,184	1,347
Legal, audit, and consulting services	1,019	1,036
Business travel expense	624	634
Fire safety and security expenses	387	313
Advertising expenses	370	253
Rent expenses	214	196
Repair and maintenance expenses	200	458
Other	801	755
Total general and administrative expenses	**18,126**	**14,356**

Auditor's fees. AO PricewaterhouseCoopers Audit has served as the independent external auditor of PAO NOVATEK for each of the reported financial years. The independent external auditor is subject to appointment at the Annual General Meeting of shareholders based on the recommendations from the Board of Directors. The aggregate fees for audit and other services rendered by PricewaterhouseCoopers Audit to the parent company of the Group included within legal, audit, and consulting services are as follows:

	Year ended 31 December:	
	2016	2015
Audits of PAO NOVATEK (audit of the Group's consolidated financial statements and audit of statutory financial statements of PAO NOVATEK)	34	31
Other services	9	10
Total auditor's fees and services	**43**	**41**

25 FINANCE INCOME (EXPENSE)

	Year ended 31 December:	
Interest expense (including transaction costs)	2016	2015
Interest expense on fixed rate debt	11,469	11,110
Interest expense on variable rate debt	4,828	3,439
Subtotal	**16,297**	**14,549**
Less: capitalized interest	(5,314)	(6,047)
Interest expense on debt	**10,983**	**8,502**
Provisions for asset retirement obligations: effect of the present value discount unwinding	587	290
Total interest expense	**11,570**	**8,792**

	Year ended 31 December:	
Interest income	2016	2015
Interest income on loans receivable	17,597	11,206
Interest income on cash, cash equivalents and deposits	1,135	1,416
Total interest income	**18,732**	**12,622**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

25 FINANCE INCOME (EXPENSE) (CONTINUED)

	Year ended 31 December:	
Foreign exchange gain (loss), net	2016	2015
Gains	41,124	72,303
Losses	(66,614)	(81,810)
Total foreign exchange gain (loss), net	**(25,490)**	**(9,507)**

26 INCOME TAX

Reconciliation of income tax. The table below reconciles actual income tax expense and theoretical income tax, determined by applying the statutory tax rate to profit before income tax.

	Year ended 31 December:	
	2016	2015
Profit before income tax	308,164	92,941
Theoretical income tax expense at statutory rate of 20 percent	61,633	18,588
Increase (decrease) due to:		
Non-deductible (non-taxable) differences in respect of the Group's share of loss (profit) joint ventures	(18,147)	6,098
Non-deductible (non-taxable) differences in respect of net gain on disposal of interests in joint ventures	781	(396)
Deferred taxes relating to assets held for sale	-	(4,316)
Tax benefits relating to priority investment projects	(1,540)	(1,333)
Other differences	364	181
Total income tax expense	**43,091**	**18,822**

A number of the Group's investment projects were included by the government authorities in the list of priority projects, in respect of them the Group was able to apply a reduced income tax rate of 15.5 percent.

Domestic and foreign components of current income tax expense were:

	Year ended 31 December:	
	2016	2015
Russian Federation income tax	35,025	21,837
Foreign income tax	552	943
Total current income tax expense	**35,577**	**22,780**

Effective income tax rate. The Group's Russian statutory income tax rate for 2016 and 2015 was 20 percent. For the years ended 31 December 2016 and 2015, the consolidated Group's effective income tax rate was 14.0 percent and 20.3 percent, respectively.

The Group recognizes in profit before income tax its share of net profit (loss) from joint ventures, which influences the consolidated profit of the Group but does not result in additional income tax expense (benefit) at the Group's level. Net profit (loss) of joint ventures was recorded in their financial statements on an after-tax basis. The Group holds at least a 50 percent interest in each of its joint ventures, and dividend income from these joint ventures is subject to a zero withholding tax rate according to the Russian tax legislation. In addition, during the year ended 31 December 2015, the Group recognized a deferred tax asset of RR 4,316 million related to expected disposal of 9.9 percent participation interest in OAO Yamal LNG.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

26 INCOME TAX (CONTINUED)

Without the effect of net profit (loss) and dividends from joint ventures, and the deferred tax asset relating to the 9.9 percent interest in Yamal LNG classified as held for sale, the effective income tax rate for the years ended 31 December 2016 and 2015 was 19.8 percent and 18.7 percent, respectively.

In respect of PAO NOVATEK and majority of its Russian subsidiaries, the Group submits a single consolidated income tax return in accordance with Russian tax legislation (See Note 3).

Deferred income tax. Differences between IFRS and Russian statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes.

Deferred income tax balances are presented in the consolidated statement of financial position as follows:

	At 31 December 2016	At 31 December 2015
Long-term deferred income tax asset (other non-current assets)	4,671	11,183
Long-term deferred income tax liability	(24,656)	(23,706)
Net deferred income tax liability	**(19,985)**	**(12,523)**

Deferred income tax assets expected to be realized within twelve months as of 31 December 2016 and 2015 were RR 1,556 million and RR 5,193 million, respectively. Deferred tax liabilities expected to be reversed within twelve months of 31 December 2016 and 2015 were RR 131 million and RR 212 million, respectively.

Movements in deferred income tax assets and liabilities during the years ended 31 December 2016 and 2015 are as follows:

	At 31 December 2016	Statement of Income effect	Statement of Comprehensive Income effect	At 31 December 2015
Property, plant and equipment	(26,805)	(1,521)	2	(25,286)
Intangible assets	(313)	66	-	(379)
Other	(676)	1,411	(14)	(2,073)
Deferred income tax liabilities	**(27,794)**	**(44)**	**(12)**	**(27,738)**
Less: deferred tax assets offset	*3,138*	*(894)*	-	*4,032*
Total deferred income tax liabilities	**(24,656)**	**(938)**	**(12)**	**(23,706)**
Tax losses carried forward	2,542	(616)	(2)	3,160
Loans receivable	1,975	(2,261)	-	4,236
Inventories	1,029	485	(1)	545
Assets held for sale	-	(4,316)	-	4,316
Asset retirement obligations	1,464	634	-	830
Trade payables and accrued liabilities	558	(1,445)	59	1,944
Other	241	49	8	184
Deferred income tax assets	**7,809**	**(7,470)**	**64**	**15,215**
Less: deferred tax liabilities offset	*(3,138)*	*894*	-	*(4,032)*
Total deferred income tax assets	**4,671**	**(6,576)**	**64**	**11,183**
Net deferred income tax liabilities	**(19,985)**	**(7,514)**	**52**	**(12,523)**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

26 INCOME TAX (CONTINUED)

	At 31 December 2015	Statement of Income effect	Statement of Comprehensive Income effect	At 31 December 2014
Property, plant and equipment	(25,286)	(3,341)	(2)	(21,943)
Intangible assets	(379)	(126)	-	(253)
Other	(2,073)	(1,220)	(16)	(837)
Deferred income tax liabilities	**(27,738)**	**(4,687)**	**(18)**	**(23,033)**
Less: deferred tax assets offset	*4,032*	*2,062*	-	*1,970*
Total deferred income tax liabilities	**(23,706)**	**(2,625)**	**(18)**	**(21,063)**
Tax losses carried forward	3,160	1,346	4	1,810
Loans receivable	4,236	1,293	-	2,943
Inventories	545	(172)	(2)	719
Assets held for sale	4,316	4,316	-	-
Asset retirement obligations	830	532	-	298
Trade payables and accrued liabilities	1,944	1,347	(67)	664
Other	184	(17)	14	187
Deferred income tax assets	**15,215**	**8,645**	**(51)**	**6,621**
Less: deferred tax liabilities offset	*(4,032)*	*(2,062)*	-	*(1,970)*
Total deferred income tax assets	**11,183**	**6,583**	**(51)**	**4,651**
Net deferred income tax liabilities	**(12,523)**	**3,958**	**(69)**	**(16,412)**

At 31 December 2016, the Group had recognized deferred income tax assets of RR 2,542 million (31 December 2015: RR 3,160 million) in respect of unused tax loss carry forwards of RR 13,102 million (31 December 2015: RR 17,400 million). In accordance with tax legislation of Russian Federation effective 1 January 2017, taxable profits can be reduced for the amount of tax losses carried forward during an unlimited period of time, and in 2017-2020 tax losses carried forward cannot be offset by more than 50 percent of taxable profits. Until 2017, tax legislation set limitation for the period of tax losses be carried forward for relief against taxable profits for ten years after they were incurred. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments including expectations regarding the Group's ability to generate sufficient future taxable income and the projected time period over which deferred tax benefits will be realized.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS

The accounting policies and disclosure requirements for financial instruments have been applied to the line items below:

	At 31 December 2016		At 31 December 2015	
Financial assets	Non-current	Current	Non-current	Current
Loans and receivables				
Loans receivable	7,575	-	13,105	-
Trade and other receivables	24,832	41,586	16,748	37,564
Cash on special accounts	-	-	-	6,477
Cash and cash equivalents	-	48,301	-	29,187
Other	157	-	10	-
At fair value through profit or loss				
Loans receivable	176,738	308	200,946	-
Commodity derivatives	1,172	2,920	1,511	5,039
Total financial assets	**210,474**	**93,115**	**232,320**	**78,267**
Financial liabilities				
At amortized cost				
Long-term debt	161,296	55,469	252,050	77,269
Short-term debt	-	-	-	29,386
Trade and other payables	-	28,112	-	30,490
At fair value through profit or loss				
Commodity derivatives	1,517	2,754	368	2,355
Total financial liabilities	**162,813**	**86,335**	**252,418**	**139,500**

Fair value measurement. The Group evaluates the quality and reliability of the assumptions and data used to measure fair value in accordance with IFRS 13, *Fair Value Measurement,* in the three hierarchy levels as follows:

i. quoted prices in active markets (Level 1);
ii. inputs other than quoted prices included in Level 1 that are directly or indirectly observable in the market (externally verifiable inputs) (Level 2);
iii. inputs that are not based on observable market data (unobservable inputs) (Level 3).

Commodity derivative instruments. The Group conducts natural gas foreign trading in active markets under long-term and short-term purchase and sales contracts, as well as purchases and sells various derivative instruments (with reference to the European natural gas hubs) for delivery optimization and to decrease exposure to the risk of negative changes in natural gas world prices.

These contracts include pricing terms that are based on a variety of commodities and indices, and/or volume flexibility options that collectively qualify them under the scope of IAS 39, *Financial instruments: recognition and measurement*, although the activity surrounding certain contracts involves the physical delivery of natural gas. All contracts mentioned above are recognized in the consolidated statement of financial position at fair value with movements in fair value recognized in the consolidated statement of income.

The fair value of long-term natural gas derivative contracts involving the physical delivery of natural gas is determined using internal models and other valuation techniques (the mark-to-market and mark-to-model analysis) due to the absence of quoted prices or other observable, market-corroborated data, for the duration of the contracts. Due to the assumptions underlying their fair value, the gas contracts are categorized as Level 3 in the fair value hierarchy, described above.

The fair value of short-term natural gas derivative contracts involving the physical delivery of natural gas and likewise contracts used for the price risk management and delivery optimization is determined based on available futures quotes in the active market (mark-to-market analysis) (Level 1).

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The amounts recognized by the Group in respect of the natural gas derivative contracts measured in accordance with IAS 39, *Financial instruments: recognition and measurement,* are as follows:

Commodity derivatives	At 31 December 2016	At 31 December 2015
Within other non-current and current assets	4,092	6,550
Within other non-current and current liabilities	(4,271)	(2,723)

	Year ended 31 December:	
Included in other operating income (loss)	2016	2015
Operating income from natural gas foreign trading	1,970	206
Change in fair value	(1,778)	(1,006)

The table below represents the effect on the fair value estimation of natural gas derivative contracts that would occur from price changes by ten percent by one megawatt-hour in 12 months after the reporting date:

	Year ended 31 December:	
Effect on the fair value (RR million)	2016	2015
Increase by ten percent	(1,673)	(1,678)
Decrease by ten percent	1,673	1,678

Recognition and remeasurement of the shareholders' loans to joint ventures. Terms and conditions of the shareholders' loans provided by the Group to its joint ventures OAO Yamal LNG and ZAO Terneftegas contain certain financial (benchmark interest rates adjusted for the borrower credit risk) and non-financial (actual interest rates on the borrowings of shareholders, expected free cash flows of the borrower and expected maturities) variables and in accordance with the Group's accounting policy were classified as financial assets at fair value through profit or loss.

The following table summarizes the movements in the carrying amounts of shareholders' loans provided to Yamal LNG and Terneftegas and related interest receivable:

	Year ended 31 December:	
	2016	2015
At 1 January	**216,136**	**88,726**
Loans provided	6,645	104,076
Repayment of the loans and accrued interest	(1,298)	(1,160)
Initial measurement at fair value allocated to increase the Group's investments in joint ventures (see Note 7)	(836)	(14,185)
Subsequent remeasurement at fair value recognized in profit (loss) as follows:		
– Interest income (using the effective interest rate method)	16,248	9,596
– Foreign exchange gain (loss), net	(48,828)	39,588
– Remaining effect from changes in fair value (attributable to free cash flows of the borrowers and interest rates)	10,387	(10,505)
At 31 December	**198,454**	**216,136**

Fair value measurement of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and free cash flows models based on the borrower's strategic plans approved by the shareholders of the joint ventures. Due to the assumptions underlying fair value estimation, shareholders' loans are categorized as Level 3 in the fair value hierarchy, described above.

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The fair value of the shareholders' loans is sensitive to benchmark interest rates changes. The table below represents the effect on fair value of the shareholders' loans that would occur from one percent changes in the benchmark interest rates.

	Year ended 31 December:	
Effect on the fair value (RR million)	**2016**	**2015**
Increase by one percent	(13,038)	(12,034)
Decrease by one percent	14,272	12,924

Financial risk management objectives and policies. In the ordinary course of business, the Group is exposed to market risks from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on the degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial results. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position.

The Group's principal risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to these limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

Market risk. Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Group's financial results or the value of its holdings of financial instruments. The primary objective of mitigating these market risks is to manage and control market risk exposures, while optimizing the return on risk.

The Group is exposed to market price movements relating to changes in commodity prices such as crude oil, oil and gas condensate refined products and natural gas (commodity price risk), foreign currency exchange rates, interest rates, equity prices and other indices that could adversely affect the value of the Group's financial assets, liabilities or expected future cash flows.

(a) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to the US dollar and Euro. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble, the US dollar and Euro. The Group may utilize foreign currency derivative instruments to manage the risk exposures associated with fluctuations on certain firm commitments for sales and purchases, debt instruments and other transactions that are denominated in currencies other than the Russian rouble, and certain non-Russian rouble assets and liabilities.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The carrying amounts of the Group's financial instruments are denominated in the following currencies:

At 31 December 2016	Russian rouble	US dollar	Euro	Other	Total
Financial assets					
Non-current					
Long-term loans receivable	7,575	79,484	97,254	-	184,313
Trade and other receivables	3,530	13,815	7,487	-	24,832
Commodity derivatives	-	-	1,172	-	1,172
Other	-	-	-	157	157
Current					
Trade and other receivables	23,525	15,297	1,841	923	41,586
Current portion of long-term loans receivable	-	308	-	-	308
Commodity derivatives	-	-	2,920	-	2,920
Cash and cash equivalents	10,346	18,116	19,544	295	48,301
Financial liabilities					
Non-current					
Long-term debt	-	(154,915)	(6,381)	-	(161,296)
Commodity derivatives	-	-	(1,517)	-	(1,517)
Current					
Current portion of long-term debt	(27,532)	(27,937)	-	-	(55,469)
Trade and other payables	(23,593)	(2,319)	(2,064)	(136)	(28,112)
Commodity derivatives	-	-	(2,754)	-	(2,754)
Net exposure	**(6,149)**	**(58,151)**	**117,502**	**1,239**	**54,441**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

At 31 December 2015	Russian rouble	US dollar	Euro	Other	Total
Financial assets					
Non-current					
Long-term loans receivable	13,105	90,650	110,296	-	214,051
Trade and other receivables	2,341	11,515	2,862	30	16,748
Commodity derivatives	-	-	1,511	-	1,511
Other	-	-	-	10	10
Current					
Trade and other receivables	19,160	14,665	3,058	681	37,564
Commodity derivatives	-	-	5,039	-	5,039
Cash on special accounts	-	-	6,477	-	6,477
Cash and cash equivalents	10,171	7,223	11,499	294	29,187
Financial liabilities					
Non-current					
Long-term debt	(33,246)	(218,804)	-	-	(252,050)
Commodity derivatives	-	-	(368)	-	(368)
Current					
Current portion of long-term debt	-	(77,269)	-	-	(77,269)
Short-term debt	(21,300)	-	(8,086)	-	(29,386)
Trade and other payables	(20,243)	(7,653)	(2,373)	(221)	(30,490)
Commodity derivatives	-	-	(2,355)	-	(2,355)
Net exposure	**(30,012)**	**(179,673)**	**127,560**	**794**	**(81,331)**

The Group chooses to provide information about market risk and potential exposure to hypothetical loss from its use of financial instruments through sensitivity analysis disclosures in accordance with IFRS requirements.

The sensitivity analysis depicted in the table below reflects the hypothetical loss that would occur assuming a 10 percent increase in exchange rates and no changes in the portfolio of instruments and other variables at 31 December 2016 and 2015, respectively:

		Year ended 31 December:	
Effect on profit before income tax	Increase in exchange rate	2016	2015
RUB / USD	10%	(5,815)	(17,967)
RUB / EUR	10%	11,750	12,756

The effect of a corresponding 10 percent decrease in exchange rate is approximately equal and opposite.

(b) Commodity price risk

The Group's overall commercial trading strategy in natural gas and liquid hydrocarbons is centrally managed. Changes in commodity prices could negatively or positively affect the Group's results of operations. The Group manages the exposure to commodity price risk by optimizing its core activities to achieve stable price margins.

Natural gas supplies on the Russian domestic market. As an independent natural gas producer, the Group is not subject to the government's regulation of natural gas prices, except for those volumes sold to residential customers. Nevertheless, the Group's prices for natural gas sold are strongly influenced by the prices regulated by the governmental agency of the Russian Federation that carries out state regulation of prices and tariffs for goods and services of natural monopolies in energy, utilities and transportation.

There were no changes in regulated natural gas prices on the domestic market (excluding residential customers) from 1 January 2014 until 30 June 2015. Effective from 1 July 2015, natural gas prices were increased on average by 7.5 percent and remained unchanged through the end of 2016.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

Management believes it has limited downside commodity price risk for natural gas in the Russian Federation and does not use commodity derivative instruments for trading purposes. All of the Group's natural gas purchase and sales contracts in the domestic market are entered to meet supply requirements to fulfil contract obligations or for own consumption and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*. However, to effectively manage the margins achieved through its natural gas trading activities, management has established targets for volumes sold to wholesale traders, end-customers and to the natural gas exchange.

Natural gas trading activities on the European and other foreign markets. The Group purchases and sells natural gas on the European and other foreign markets under long-term and short-term supply contracts, as well as purchases and sells different derivative instruments based on formulas with reference to benchmark natural gas prices quoted for the North-Western European natural gas hubs, crude oil and oil products prices and/or a combination thereof. Therefore, the Group's results from natural gas foreign trading and derivative instruments foreign trading are subject to commodity price volatility based on fluctuations or changes in the respective benchmark reference prices.

Natural gas foreign trading activities and respective foreign derivative instruments are executed by Novatek Gas & Power GmbH, the Group's wholly owned subsidiary, and are managed within the Group's integrated trading function.

Liquid hydrocarbons. The Group sells its crude oil, stable gas condensate and gas condensate refined products under spot contracts. Naphtha and stable gas condensate volumes sold to the Asian-Pacific Region, European and North American markets are based on benchmark reference crude oil prices of Brent IPE and Dubai and/or naphtha prices, mainly of Naphtha Japan and Naphtha CIF NWE or a combination thereof, plus a margin or discount, depending on current market situation. Other gas condensate refined products volumes sold mainly to the European market are based on benchmark reference jet fuel prices of Jet CIF NWE and gasoil prices of Gasoil 0.1 percent CIF NWE plus a margin or discount, depending on current market situation. Crude oil sold internationally is based on benchmark reference crude oil prices of Brent dated, minus a discount, or Dubai, plus a premium, and on a transaction-by-transaction basis for volumes sold domestically.

As a result, the Group's revenues from the sales of liquid hydrocarbons are subject to fluctuations in the crude oil and gas condensate refined products benchmark reference prices. All of the Group's liquid hydrocarbons purchase and sales contracts are entered to meet supply requirements to fulfill contract obligations or for own consumption and are not within the scope of IAS 39, *Financial instruments: recognition and measurement.*

(c) Cash flow and fair value interest rate risk

The Group is subject to interest rate risk on financial liabilities with variable interest rates. Changes in interest rates impact primarily debt by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). To mitigate this risk, the Group's treasury function performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In cases where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favorable interest rate terms.

The interest rate profiles of the Group's interest-bearing financial instruments were as follows:

	At 31 December 2016		**At 31 December 2015**	
	RR million	**Percent**	**RR million**	**Percent**
At fixed rate	161,323	*74%*	254,276	*71%*
At variable rate	55,442	*26%*	104,429	*29%*
Total debt	**216,765**	***100%***	**358,705**	***100%***

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The Group centralizes the cash requirements and surpluses of controlled subsidiaries and the majority of their external financing requirements, and applies, on its consolidated net debt position, a funding policy to optimize its financing costs and manage the impact of interest rate changes on its financial results in line with market conditions. In this way, the Group is able to ensure that the balance between the floating rate portion of its debt and its cash surpluses has a low level of exposure to any change in interest rates over the short term. This policy makes it possible to significantly limit the Group's sensitivity to interest rate volatility.

The Group’s financial results are sensitive to changes in interest rates on the floating rate portion of the Group’s debt portfolio. If the interest rates applicable to floating rate debt were to increase by 100 basis points (one percent) at the reporting dates, assuming all other variables remain constant, it is estimated that the Group’s profit before taxation would decrease by the amounts shown below:

	Year ended 31 December:	
Effect on profit before income tax	**2016**	**2015**
Increase by 100 basis points	554	1,044

The effect of a corresponding 100 basis points decrease in interest rate is approximately equal and opposite.

The Group is examining various ways to manage its cash flow interest rate risk by using a combination of floating and fixed interest rates. No swaps or other similar instruments were in place at 31 December 2016 and 2015, or during the years then ended.

Credit risk. Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if a counterparty defaults on its contractual obligations.

Credit risk is managed on a Group level and arises from cash and cash equivalents, including short-term deposits with banks, as well as credit exposures to customers, including outstanding trade receivables and committed transactions. Cash and cash equivalents are deposited only with banks that are considered by the Group during the whole deposit period to have minimal risk of default.

The Group’s trade and other receivables consist of a large number of customers, spread across diverse industries and geographical areas. The Group has developed standard credit payment terms and constantly monitors the status of trade and other receivables and the creditworthiness of the customers.

Most of the Group’s international liquid hydrocarbons sales are made to customers with independent external ratings; however, if the customer has a credit rating below BBB, the Group requires the collateral for the trade receivable to be in the form of letters of credit from banks with an investment grade rating. Most of domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis.

As a result of the domestic regional natural gas trading activities, the Group is exposed to the risk of payment defaults of small and medium-sized industrial users and individuals. To minimize credit risk the Group monitors the recoverability of these debtors by analyzing ageing of receivables by type of customers and their respective prior payment history.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the consolidated statement of financial position.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The table below highlights the Group's trade and other receivables to published credit ratings of its counterparties and/or their parent companies:

Moody's, Fitch and/or Standard & Poor's	At 31 December 2016	At 31 December 2015
Investment grade rating	12,913	13,143
Non-investment grade rating	5,062	8,880
No external rating	23,611	15,541
Total trade and other receivables	**41,586**	**37,564**

The table below highlights the Group's cash and cash equivalents balances to published credit ratings of its banks and/or their parent companies:

Moody's, Fitch and/or Standard & Poor's	At 31 December 2016	At 31 December 2015
Investment grade rating	38,087	24,542
Non-investment grade rating	10,194	4,627
No external rating	20	18
Total cash and cash equivalents	**48,301**	**29,187**

Investment grade ratings classification referred to as Aaa to Baa3 for Moody's Investors Service, and as AAA to BBB- for Fitch Ratings and Standard & Poor's.

In addition, the Group provides long-term loans to its joint ventures for development, construction and acquisitions of oil and gas assets. Required amount of loans and their maturity schedules are based on the budgets and strategic plans approved by the shareholders of the joint ventures.

Liquidity risk. Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. In managing its liquidity risk, the Group maintains adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows and matches the maturity profiles of financial assets and liabilities.

The Group prepares various financial plans (monthly, quarterly and annually) which ensures that the Group has sufficient cash on demand to meet expected operational expenses, financial obligations and investing activities for a period of 30 days or more. The Group has entered into a number of short-term credit facilities. Such credit lines and overdraft facilities can be drawn down to meet short-term financing needs. To fund cash requirements of a more permanent nature, the Group will normally raise long-term debt in available international and domestic markets.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The following tables summarize the maturity profile of the Group's financial liabilities, except of natural gas derivative contracts, based on contractual undiscounted payments, including interest payments:

At 31 December 2016	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years	Total
Debt at fixed rate					
Principal	14,000	-	56,358	98,633	168,991
Interest	8,179	7,636	20,823	10,841	47,479
Debt at variable rate					
Principal	41,532	13,998	-	-	55,530
Interest	866	144	-	-	1,010
Trade and other payables	28,112	-	-	-	28,112
Total financial liabilities	**92,689**	**21,778**	**77,181**	**109,474**	**301,122**
At 31 December 2015					
Debt at fixed rate					
Principal	71,816	14,000	7,605	170,958	264,379
Interest	11,288	9,531	26,798	20,049	67,666
Debt at variable rate					
Principal	34,938	52,906	16,819	-	104,663
Interest	1,644	867	144	-	2,655
Trade and other payables	30,490	-	-	-	30,490
Total financial liabilities	**150,176**	**77,304**	**51,366**	**191,007**	**469,853**

The following table represents the maturity profile of the Group's derivative commodity contracts based on undiscounted cash flows:

At 31 December 2016	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years	Total
Cash inflow	39,310	25,336	57,713	13,704	136,063
Cash outflow	(39,144)	(25,871)	(57,570)	(13,655)	(136,240)
Net cash flows	**166**	**(535)**	**143**	**49**	**(177)**
At 31 December 2015					
Cash inflow	36,518	27,380	65,825	37,164	166,887
Cash outflow	(33,838)	(26,067)	(65,889)	(37,278)	(163,072)
Net cash flows	**2,680**	**1,313**	**(64)**	**(114)**	**3,815**

Capital management. The primary objectives of the Group's capital management policy are to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain investor, market and creditor confidence to support its business activities.

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

Prior to 2015, the Group had investment grade credit ratings of Baa3 by Moody's Investors Service, BBB- by Fitch Ratings, and BBB- by Standard & Poor's. In February 2015, following the decrease of the sovereign credit rating of the Russian Federation by both Standard & Poor's and Moody's Investors Service, the Group's investment grade credit rating was also downgraded to noninvestment level BB+ and Ba1, respectively. In November 2016, the Group's credit rating was upgraded to investment level BBB- by Standard & Poor's. The Group has established certain financial targets and coverage ratios that it monitors on a quarterly and annual basis to maintain its credit ratings.

The Group manages its capital on a corporate-wide basis to ensure adequate funding to sufficiently meet the Group's operational requirements. The majority of external debts raised to finance NOVATEK's wholly owned subsidiaries are centralized at the parent level, and financing to Group entities is facilitated through inter-company loan arrangements or additional contributions to share capital.

The Group has a stated dividend policy that distributes not less than 30 percent of the Group's consolidated net profit determined according to IFRS, adjusted for one-off profits (losses). The dividend payment for a specific year is determined after taking into consideration future earnings, capital expenditure requirements, future business opportunities and the Group current financial position. Dividends are recommended by the Board of Directors of NOVATEK and approved by the NOVATEK's shareholders.

The Group defines the term "capital" as equity attributable to PAO NOVATEK shareholders plus net debt (total debt less cash and cash equivalents). There were no changes to the Group's approach to capital management during 2016. At 31 December 2016 and 2015, the Group's capital totaled RR 816,814 million and RR 755,597 million, respectively.

28 CONTINGENCIES AND COMMITMENTS

Operating environment. The Russian Federation continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is in practice not convertible in most countries outside of the Russian Federation, and relatively high inflation. In addition, the Russian economy is particularly sensitive to world oil and gas prices; therefore, significant prolonged declines in world oil prices have a negative impact on the Russian economy. The tax, currency and customs legislation is subject to varying interpretations, frequent changes and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

The Group's business operations are primarily located in the Russian Federation and are thus exposed to the economic and financial markets of the Russian Federation.

Developments in Ukraine during 2014 and 2015 and the subsequent negative reaction of the world community have had and may continue to have a negative impact on the Russian economy, including difficulties in obtaining international funding, devaluation of national currency and high inflation. These and other events, in case of escalation, may have a significant negative impact on the operating environment in the Russian Federation.

Sectoral sanctions imposed by the U.S. government. On 16 July 2014, the Office of Foreign Assets Control (OFAC) of the U.S. Treasury included PAO NOVATEK on the Sectoral Sanctions Identification List (the "List"), which prohibits U.S. persons or persons within the United States from providing new financing to the Group for longer than 90 days, whereas all other transactions, including financial, carried out by U.S. persons or within the United States with the Group are permitted. The inclusion on the List has not impacted the Group's business activities, in any jurisdiction, nor does it affect the Group's assets, listed shares and debt.

Management has reviewed the Group's capital expenditure programs and existing debt portfolio and has concluded that the Group has sufficient liquidity, through internally generated (operating) cash flows, to adequately fund its core oil and gas business operations including finance of planned capital expenditure programs of its subsidiaries, as well as to repay and service all Group's short-term and long-term debt existing at the current reporting date and, therefore, inclusion on the List does not adversely impact the Group's operational activities.

28 CONTINGENCIES AND COMMITMENTS (CONTINUED)

The Group together with its foreign partners currently raises necessary financing for our joint ventures from non-US debt markets and lenders.

Contractual commitments. At 31 December 2016, the Group had contractual capital expenditures commitments aggregating approximately RR 13 billion (at 31 December 2015: RR 23 billion) mainly for development at the Yarudeyskoye (through 2017), the Salmanovskoye (Utrenneye) (through 2018), the East-Tarkosalinskoye (through 2019) and the Yurkharovskoye (through 2018) fields all in accordance with duly signed agreements.

The Group's commitments with regard to its joint operation in Montenegro relate to performance obligations of the Concessionaries to conduct mandatory work program exploration activities as stipulated by the Concession Contract (see Note 1). The maximum amount to be paid to the State of Montenegro by the Group in case of non-performance during the first exploration period of up to four years ending in 2020 is EUR 42.5 million. The outflow of resources embodying economic benefits required to settle this contingent liability is not probable; therefore, no provision for this liability was recognized in the consolidated financial statements.

The Group has entered into a number of agreements, maturing after the twelve months from the reporting date, relating to time chartering of marine tankers with service terms up to six years for transportation of liquid hydrocarbons. At 31 December 2016, the future minimum payments under these time charter agreements amounted to RR 11.5 billion (at 31 December 2015: RR 10.3 billion).

Non-financial guarantees. The aggregated amount of non-financial guarantees in respect of the Yamal LNG project issued by the Group to a number of third parties (the Ministry of Finance of the Russian Federation, Russian and foreign banks, LNG plant constructors, LNG-vessels owners, LNG-terminal owners) in favor of the Group's joint venture OAO Yamal LNG and its subsidiary totaled USD 3.0 billion and EUR 3.1 billion at 31 December 2016 (at 31 December 2015: USD 3.6 billion and EUR 0.1 billion). These non-financial guarantees have various terms depending mostly on the successful project completion (finalization of the LNG plant construction and achievement of its full production capacity). For certain factors as stipulated in the project financing agreements, the Group plans to issue in the future non-financial guarantees covering the project post-completion period.

With regard to the Group's obligations under the non-financial guarantee issued to the banks providing project financing to Yamal LNG, the State Corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank)" issued in favor of the banks a counter guarantee for the amount not exceeding the equivalent of USD 3 billion.

The outflow of resources embodying economic benefits required to settle the obligations under these non-financial guarantees issued by the Group is not probable; therefore, no provision for these liabilities was recognized in the consolidated financial statements.

Taxation. Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Correspondingly, the relevant regional and federal tax authorities may periodically challenge management's interpretation of such taxation legislation as applied to the Group's transactions and activities. Furthermore, events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in its interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. 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.

Management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued in the consolidated financial statements.

Mineral licenses. The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its mineral licenses. Management cooperates with governmental authorities to agree on remedial actions necessary to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties or license limitation, suspension or revocation. The Group's management believes any issues of non-compliance will be resolved through negotiations or corrective actions without any material adverse effect on the Group's financial position, results of operations or cash flows.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

28 CONTINGENCIES AND COMMITMENTS (CONTINUED)

The major of the Group's oil and gas fields and license areas are located in the YNAO. Licenses are issued by the Federal Agency for the Use of Natural Resources of the Russian Federation and the Group pays unified natural resources production tax to produce crude oil, natural gas and unstable gas condensate from these fields and contributions for exploration of license areas. The principal licenses of the Group and its joint ventures and their expiry dates are:

Field	License holder	License expiry date
	Subsidiaries:	
Salmanovskoye (Utrenneye)	OOO Arctic LNG 2	2031
Yurkharovskoye	OOO NOVATEK-Yurkharovneftegas	2034
Geofizicheskoye	OOO Arctic LNG 1	2034
East-Tarkosalinskoye	OOO NOVATEK-Tarkosaleneftegas	2043
North-Russkoye	OOO NOVATEK-Tarkosaleneftegas	2031
Khancheyskoye	OOO NOVATEK-Tarkosaleneftegas	2044
Urengoyskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftegas	2059
Dobrovolskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftegas	2059
East-Tazovskoye	OOO NOVATEK-Tarkosaleneftegas	2033
Kharbeyskoye	OOO NOVATEK-Tarkosaleneftegas	2036
North-Khancheyskoye + Khadyryakhinskoye	OOO NOVATEK-Tarkosaleneftegas	2029
Dorogovskoye	OOO NOVATEK-Tarkosaleneftegas	2033
Yarudeyskoye	OOO Yargeo	2029
Malo-Yamalskoye	OOO NOVATEK-Yarsaleneftegas	2034
	Joint ventures:	
South-Tambeyskoye	OAO Yamal LNG	2045
Urengoyskoye (within the Samburgskiy and Yevo-Yakhinskiy license areas)	OAO Arcticgas(*)	2034
Yaro-Yakhinskoye	OAO Arcticgas	2034
Samburgskoye	OAO Arcticgas	2034
North-Chaselskoye	OAO Arcticgas	Life of field
Yevo-Yakhinskoye	OAO Arcticgas	2034
North-Urengoyskoye	ZAO Nortgas	2038
Termokarstovoye	ZAO Terneftegas	2097

(*) Subsidiary of OOO SeverEnergia

Management believes the Group has the right to extend its licenses beyond the initial expiration date under the existing legislation and intends to exercise this right on all of its fields.

Environmental liabilities. The Group operates in the oil and gas industry in the Russian Federation and abroad. The enforcement of environmental regulation in the Russian Federation and other countries of operation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations and, as obligations are determined, they are recognized as an expense immediately if no future benefit is discernible. Potential liabilities arising as a result of a change in interpretation of existing regulations, civil litigation or changes in legislation cannot be estimated. Under existing legislation, management believes that there are no probable liabilities, which will have a material adverse effect on the Group's financial position, results of operations or cash flows.

Legal contingencies. The Group is subject of, or party to a number of court proceedings (both as a plaintiff and a defendant) 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 Group and which have not been accrued or disclosed in the consolidated financial statements.

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

29 PRINCIPAL SUBSIDIARIES AND JOINT VENTURES

The principal subsidiaries and joint ventures of the Group and respective effective ownership in the ordinary share capital at 31 December 2016 and 2015 are set out below:

	Ownership percent at 31 December:		Country of	
	2016	**2015**	**incorporation**	**Principal activities**
Subsidiaries:				
OOO NOVATEK-Yurkharovneftegas	100	100	Russia	Exploration and production
OOO NOVATEK-Tarkosaleneftegas	100	100	Russia	Exploration and production
OOO Yargeo	51	51	Russia	Exploration, development and production
OOO NOVATEK-Purovsky ZPK	100	100	Russia	Gas Condensate Processing Plant
OOO NOVATEK-Transervice	100	100	Russia	Transportation services
OOO NOVATEK-Ust-Luga	100	100	Russia	Fractionation and Transshipment Complex
OOO NOVATEK-AZK	100	100	Russia	Wholesale and retail trading
OOO NOVATEK-Chelyabinsk	100	100	Russia	Trading and marketing
OOO NOVATEK-Kostroma	100	100	Russia	Trading and marketing
OOO NOVATEK-Perm	100	100	Russia	Trading and marketing
OOO NOVATEK Moscow Region	100	100	Russia	Trading and marketing
Novatek Gas & Power GmbH	100	100	Switzerland	Trading and marketing
Novatek Gas & Power Asia PTE. Ltd	100	100	Singapore	Trading and marketing
Novatek Polska Sp. z o.o.	100	100	Poland	Trading and marketing
Joint ventures:				
OAO Yamal LNG	50,1	60(*)	Russia	Exploration and development, construction of LNG plant
ZAO Terneftegas	51	51	Russia	Exploration and production
ZAO Nortgas	50	50	Russia	Exploration and production
OOO Yamal Development	50	50	Russia	Holding company
Artic Russia B.V.	56,8	56,8	Netherlands	Holding company
OOO SeverEnergia (includes a producing subsidiary, see Note 7)	53,3	53,3	Russia	Holding company

(*) Includes a 9.9 percent ownership classified as an asset held for sale (see Note 5)

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

30 RELATED PARTY TRANSACTIONS

Transactions between NOVATEK and its subsidiaries, which are related parties of NOVATEK, have been eliminated on consolidation and are not disclosed in this Note.

For the purposes of these consolidated financial statements, 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 or joint control over the other party in making financial and operational decisions. Management has used reasonable judgments in considering each possible related party relationship with attention 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 affected on the same terms, conditions and amounts as transactions between unrelated parties.

	Year ended 31 December:	
Related parties – joint ventures	**2016**	**2015**
Transactions		
OOO SeverEnergia and its subsidiary:		
Purchases of natural gas and liquid hydrocarbons	(82,420)	(75,412)
Other revenues	195	182
OOO Yamal Development:		
Interest income on loans issued	1,275	1,517
ZAO Nortgas:		
Purchases of natural gas and liquid hydrocarbons	(17,180)	(20,064)
Other revenues	60	84
ZAO Terneftegas:		
Purchases of natural gas and liquid hydrocarbons	(12,898)	(7,922)
Interest income on loans issued	173	262
Other revenues	90	86
OAO Yamal LNG:		
Interest income on loans issued	16,075	9,334
Other revenues	498	356
Materials, services and other	(77)	(11)

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

30 RELATED PARTY TRANSACTIONS (CONTINUED)

Related parties – joint ventures	At 31 December 2016	At 31 December 2015
Balances		
OOO SeverEnergia and its subsidiary:		
Trade payables and accrued liabilities	11,986	6,733
OOO Yamal Development:		
Long-term loans receivable	7,575	13,105
Interest on long-term loans receivable	3,088	1,813
ZAO Nortgas:		
Trade payables and accrued liabilities	1,829	1,751
ZAO Terneftegas:		
Long-term loans receivable	2,893	4,413
Current portion of long-term loans receivable	308	-
Interest on long-term loans receivable	106	813
Trade payables and accrued liabilities	1,589	1,133
OAO Yamal LNG:		
Long-term loans receivable	173,845	196,533
Interest on long-term loans receivable	21,302	14,377
Trade receivables	245	134

The terms and conditions of the loans receivable from the joint ventures are disclosed in Note 8.

The Group issued non-financial guarantees in favor of its joint ventures as described in Note 28.

Related parties – parties under control of key management personnel	Year ended 31 December:	
	2016	2015
Transactions		
OOO Transoil:		
Liquid hydrocarbons transportation by rail	(9,405)	(8,907)
OOO Nova:		
Purchases of construction services (capitalized within property, plant and equipment)	(530)	(2,626)
Materials, services and other	(72)	(75)
PAO SIBUR Holding and its subsidiaries (under control until December 2015):		
Sales of natural gas and liquid hydrocarbons	-	19,052
Purchases of natural gas and liquid hydrocarbons	-	(15,501)
Liquid hydrocarbons transportation by rail	-	(3,747)
Materials, services and other	-	(1,868)
PAO Pervobank (under control until November 2015):		
Interest income	-	431

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

30 RELATED PARTY TRANSACTIONS (CONTINUED)

Related parties – parties under control of key management personnel	At 31 December 2016	At 31 December 2015
Balances		
OOO Transoil:		
Prepayments and other current assets	478	412
Trade payables and accrued liabilities	263	316
OOO Nova:		
Advances for construction	23	75
Trade payables and accrued liabilities	8	262

In December 2015, following the change in the ownership structure and corporate governance in PAO SIBUR Holding, the Chairman of the Management Committee of NOVATEK ceased to be its controlling shareholder, and as the result, SIBUR Holding ceased to be a related party of the Group.

In November 2015, the Chairman of the Management Committee of NOVATEK sold a controlling stake in PAO Pervobank to a third party, and as the result, Pervobank ceased to be a related party of the Group.

Transactions with related parties also included loans which were provided to one of the Group's subsidiaries by its non-controlling shareholder (see Notes 14, 15).

Key management personnel compensation. The Group paid to key management personnel (members of the Board of Directors and the Management Committee) short-term compensation, including salary, bonuses, and excluding dividends the following amounts:

	Year ended 31 December:	
Related parties – members of the key management personnel	2016	2015
Board of Directors	132	147
Management Committee	1,956	2,042
Total compensation	**2,088**	**2,189**

Such amounts include personal income tax and are net of payments to non-budget funds made by the employer. Some members of key management personnel have direct and/or indirect interests in the Group and receive dividends under general conditions based on their respective shareholdings. The Board of Directors consists of nine members. Starting from March 2016, the Management Committee consists of twelve members (earlier – nine members).

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

31 SEGMENT INFORMATION

The Group's activities are considered by the chief operating decision maker (hereinafter referred to as "CODM", represented by the Management Committee of NOVATEK) to comprise one operating segment: "exploration, production and marketing".

Segment information is provided to the CODM in accordance with Regulations on Accounting and Reporting of the Russian Federation ("RAR") with reconciling items largely representing adjustments and reclassifications recorded in the consolidated financial statements for the fair presentation in accordance with IFRS.

The CODM assesses reporting segment performance based on profit before income tax, since income tax is not allocated. No business segment assets or liabilities (except for capital expenditures for the period) are provided to the CODM for decision-making.

Segment information for the year ended 31 December 2016 is as follows:

For the year ended 31 December 2016	References	Exploration, production and marketing	Segment information as reported to CODM	Reconciling items	Total per consolidated financial statements
External revenues		537,461	537,461	11	537,472
Operating expenses	*a, b, h*	(380,448)	(380,448)	(5,051)	(385,499)
Other operating income (loss)	*c, d, h*	54,287	54,287	19,006	73,293
Interest expense	*e, h*	(15,921)	(15,921)	4,351	(11,570)
Interest income	*f*	13,317	13,317	5,415	18,732
Change in fair value of non-commodity financial instruments	*g*	-	-	10,387	10,387
Foreign exchange gain (loss), net	*c*	(26,177)	(26,177)	687	(25,490)
Segment result		**182,519**	**182,519**	**34,806**	**217,325**
Share of profit (loss) of joint ventures, net of income tax					90,839
Profit before income tax					**308,164**
Depreciation, depletion and amortization	*a*	32,554	32,554	2,077	34,631
Capital expenditures	*e*	32,367	32,367	2,992	35,359

Reconciling items mainly related to:

a. different methodology in calculating depreciation, depletion and amortization for intangible assets and for oil and gas properties between IFRS (units of production method) and management accounting (straight-line method), which resulted in additional recognition of operating expenses of RR 2,077 million under IFRS;

b. different methodology in accounting for exploration costs between IFRS and management accounting, which resulted in additional recognition of operating expenses of RR 1,293 million under IFRS;

c. different methodology in calculating gain on disposal of a 9.9 percent equity stake in OAO Yamal LNG, the Group's joint venture, between IFRS and management accounting, which resulted in additional recognition of other operating income of RR 20,041 million and foreign exchange gain of RR 695 million under IFRS;

d. different methodology in valuation of commodity derivatives under IFRS and management accounting, which resulted in additional recognition of other operating loss of RR 1,778 million under IFRS;

e. different methodology in borrowing costs capitalization policy and certain recognition policy differences in capital expenditures between IFRS and management accounting, which resulted in additional recognition of capital expenditures of RR 2,992 million under IFRS;

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

31 SEGMENT INFORMATION (CONTINUED)

f. different methodology in recognizing effect of the present value discount unwinding of long-term financial assets under IFRS and management accounting, which requires additional recognition of interest income of RR 5,354 million under IFRS;

g. different methodology in valuation of shareholders' loans provided by the Group to its joint ventures classified as financial assets at fair value through profit or loss between IFRS and management accounting, which requires additional gain recognition of RR 10,387 million under IFRS; and

h. other differences relating to recognition of natural gas storage expenses, employee compensation, bad debt provisions, exploration expenses, valuation of inventory balances, effect of the present value discount unwinding of asset retirement obligations.

Segment information for the year ended 31 December 2015 is as follows:

For the year ended 31 December 2015	References	Exploration, production and marketing	Segment information as reported to CODM	Reconciling items	Total per consolidated financial statements
External revenues		475,356	475,356	(31)	475,325
Operating expenses	*a, f*	(338,518)	(338,518)	3,476	(335,042)
Other operating income (loss)	*b, f*	1,091	1,091	(644)	447
Interest expense	*c, f*	(9,670)	(9,670)	878	(8,792)
Interest income	*d*	9,612	9,612	3,010	12,622
Change in fair value of non-commodity financial instruments	*e*	-	-	(10,505)	(10,505)
Foreign exchange gain (loss), net	*c*	(12,065)	(12,065)	2,558	(9,507)
Segment result		**125,806**	**125,806**	**(1,258)**	**124,548**
Share of profit (loss) of joint ventures, net of income tax					(31,607)
Profit before income tax					**92,941**
Depreciation, depletion and amortization	*a*	24,124	24,124	(4,144)	19,980
Capital expenditures	*c*	54,904	54,904	5,065	59,969

Reconciling items mainly related to:

a. different methodology in calculating depreciation, depletion and amortization for intangible assets and for oil and gas properties between IFRS (units of production method) and management accounting (straight-line method), which resulted in reversal of RR 4,442 million in operating expenses under IFRS;

b. different methodology in valuation of commodity derivatives under IFRS and management accounting, which requires additional recognition of other operating loss of RR 1,006 million under IFRS;

c. different methodology in borrowing costs capitalization policy and certain recognition policy differences in capital expenditures between IFRS and management accounting, which resulted in additional recognition of capital expenditures of RR 5,065 million under IFRS, including capitalized interest of RR 856 million;

d. different methodology in recognizing effect of the present value discount unwinding of long-term financial assets under IFRS and management accounting, which requires additional recognition of interest income of RR 2,934 million under IFRS;

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

31 SEGMENT INFORMATION (CONTINUED)

e. different methodology in valuation of shareholders' loans provided by the Group to its joint ventures classified as financial assets at fair value through profit or loss between IFRS and management accounting, which requires additional loss recognition of RR 10,505 million under IFRS; and

f. other differences relating to recognition of natural gas storage expenses, employee compensation, bad debt provisions, exploration expenses, valuation of inventory balances, effect of the present value discount unwinding of asset retirement obligations.

Geographical information. The Group operates in the following geographical areas:

- *Russian Federation* – exploration, development, production and processing of hydrocarbons, and sales of natural gas, stable gas condensate, liquefied petroleum gas, crude oil and gas condensate refined products;
- *Countries of Europe (primarily, Denmark, Belgium, the Netherlands, Finland, Poland and Montenegro)* – exploration activities within joint operations, sales of naphtha, stable gas condensate, gas condensate refined products, crude oil and liquefied petroleum gas;
- *Countries of the Asia-Pacific region (primarily, China, Taiwan, South Korea and Japan)* – sales of naphtha, stable gas condensate and crude oil;
- *Countries of the Middle East (primarily, Oman) and North America (primarily, the USA)* – sales of naphtha and crude oil.

Geographical information for the year ended 31 December 2016 and 2015 is as follows:

For the year ended 31 December 2016	Natural gas	Stable gas condensate and naphtha	Crude oil	Other gas and gas condensate refined products	Liquefied petroleum gas	Total oil and gas sales
Russia	229,716	21,920	42,754	2,655	18,811	315,856
Europe	-	44,989	13,902	61,122	12,841	132,854
The Asia-Pacific region	-	71,752	13,184	-	-	84,936
North America	-	24,757	1,295	-	-	26,052
The Middle East	-	6,469	947	-	-	7,416
Less: export duties	-	(19,513)	(7,130)	(6,614)	-	(33,257)
Total outside Russia	-	128,454	22,198	54,508	12,841	218,001
Total	**229,716**	**150,374**	**64,952**	**57,163**	**31,652**	**533,857**

For the year ended 31 December 2015	Natural gas	Stable gas condensate and naphtha	Crude oil	Other gas and gas condensate refined products	Liquefied petroleum gas	Total oil and gas sales
Russia	222,180	19,110	9,244	2,235	20,543	273,312
Europe	-	51,580	7,913	70,512	12,891	142,896
The Asia-Pacific region	-	90,616	-	-	-	90,616
North America	-	14,662	-	-	-	14,662
The Middle East	-	1,712	423	-	322	2,457
Less: export duties	-	(38,095)	(2,707)	(10,845)	(289)	(51,936)
Total outside Russia	-	120,475	5,629	59,667	12,924	198,695
Total	**222,180**	**139,585**	**14,873**	**61,902**	**33,467**	**472,007**

31 SEGMENT INFORMATION (CONTINUED)

Revenues are based on the geographical location of customers even though all revenues are generated from assets located in the Russian Federation. Substantially all of the Group's operating assets are located in the Russian Federation.

Major customers. For the year ended 31 December 2016, the Group had one major customer to whom individual revenue exceeded 10 percent of total external revenues, which represented 18 percent (RR 97.7 billion) of total external revenues. For the year ended 31 December 2015, the Group had two major customers to whom individual revenue exceeded 10 percent of total external revenues, which on an individual basis represented 13 percent and 10 percent (RR 61.2 billion and RR 47.2 billion) of total external revenues, respectively. All of the Group's major customers reside within the Russian Federation.

32 NEW ACCOUNTING PRONOUNCEMENTS

The following amended standards and interpretations became effective for the Group from 1 January 2016:

Amendments to IAS 1, *Presentation of Financial Statements* (issued in December 2014 and effective for annual periods on or after 1 January 2016). The Standard was amended to clarify the concept of materiality and explains that an entity does need not to provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material, even if the IFRS contains a list of specific requirements or describes them as minimum requirements. The Standard also provides new guidance on subtotals in financial statements. The adoption of the amendments had no material impact on the Group's consolidated financial statements.

The following new standards have been issued that the Group has decided to early adopt starting from the annual period beginning on 1 January 2017:

IFRS 15, *Revenue from Contracts with Customers* (issued in May 2014, further amended in April 2016 and effective for annual periods beginning on or after 1 January 2018, early adoption is permitted). The new standard introduces the core principle that revenue must be recognized when the goods or services are transferred to the customer, at the transaction price. Any discounts on the contract price must generally be allocated to the separate elements of contracts with customers. When the consideration varies for any reason, minimum amounts must be recognized if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalized and amortized over the period when the benefits of the contract are consumed. The Group assesses that the adoption of this standard did not have a material impact on the Group's consolidated financial position as of the date of transition.

IFRS 16, *Leases* (issued in January 2016 and effective for annual periods beginning on or after 1 January 2019, early application is permitted, provided the new revenue standard, IFRS 15, *Revenue from Contracts with Customers*, has been applied, or is applied at the same date as IFRS 16). The standard requires lessees to recognize assets and liabilities for most leases. For lessors, there is a minor change to the existing accounting treatment in IAS 17, *Leases*. The Group assesses that the adoption of this standard did not have a material impact on the Group's consolidated financial position as of the date of transition.

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2017, and which the Group has not early adopted:

Amendments to IAS 7, *Statement of Cash Flows* (issued in January 2016 and effective for annual periods on or after 1 January 2017, early adoption is permitted). The amended IAS 7 will require disclosure of a reconciliation of movements in liabilities arising from financing activities.

32 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

Amendments to IFRS 10, *Consolidated financial statements,* and IAS 28, *Investments in associates and joint ventures* (issued in September 2014, in November 2015 the effective date was postponed indefinitely). These amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The amendments stipulate that a full gain or loss is recognized when a transaction involves a business. A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are held by a subsidiary. The Group is considering the implications of these amendments for the Group's consolidated financial statements, and the timing of their adoption by the Group.

IFRS 9, *Financial Instruments: Classification and Measurement* (issued in July 2014 and effective for annual periods beginning on or after 1 January 2018, early adoption is permitted). The standard introduces new requirements for classification and measurement of financial instruments, impairment, and hedge accounting. The Group is considering the implications of this standard for the Group's consolidated financial statements, and the timing of its adoption by the Group.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). In the absence of specific IFRS guidance for the oil and gas industry, the Group has reverted to other relevant disclosure standards, mainly US GAAP, that are consistent with norms established for companies in the oil and gas industry. While not required under IFRS, this section provides unaudited supplemental information on oil and gas exploration and production activities but excludes disclosures regarding the standardized measures of discounted cash flows related to oil and gas activities.

The Group's exploration and production activities are mainly within the Russian Federation; therefore, majority of the information provided in this section pertains to this country. The Group operates through various oil and gas production subsidiaries, and also has an interest in oil and gas companies that are accounted for under the equity method.

Oil and Gas Exploration and Development Costs

The following tables set forth information regarding oil and gas acquisition, exploration and development activities. The amounts reported as costs incurred include both capitalized costs and costs charged to expense, these costs do not include LNG liquefaction and transportation operations (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2016	**2015**
Costs incurred in exploration and development activities		
Acquisition of unproved properties	1,928	-
Exploration costs	4,828	4,357
Development costs	23,550	53,427
Total costs incurred in exploration and development activities	**30,306**	**57,784**
The Group's share in joint ventures' cost incurred in exploration and development activities	71,408	39,899

	At 31 December 2016	At 31 December 2015
Capitalized costs relating to oil and gas producing activities		
Wells, related equipment and facilities	293,449	252,716
Support equipment and facilities	88,202	68,895
Uncompleted wells, related equipment and facilities	30,138	61,745
Total capitalized costs relating to oil and gas producing activities	**411,789**	**383,356**
Less: accumulated depreciation, depletion and amortization	(119,674)	(88,103)
Net capitalized costs relating to oil and gas producing activities	**292,115**	**295,253**
The Group's share in joint ventures' capitalized costs relating to oil and gas producing activities	343,096	285,445

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Results of Operations for Oil and Gas Producing Activities

The Group's results of operations for oil and gas producing activities are shown below. The results of operations for oil and gas producing activities do not include general corporate overhead or its associated tax effects. Income tax is based on statutory rates. In the following table, revenues from oil and gas sales are comprised of the sale of hydrocarbons produced by the Group's subsidiaries and include processing costs, related to processing facilities of the Group's subsidiaries as well as transportation expenses to customers (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2016	**2015**
Revenues from oil and gas sales	276,037	248,673
Lifting costs	(14,233)	(10,102)
Transportation expenses	(76,356)	(83,574)
Taxes other than income tax	(43,844)	(36,296)
Depreciation, depletion and amortization	(32,049)	(17,522)
Exploration expenses	(2,087)	(1,109)
Total production costs	**(168,569)**	**(148,603)**
Results of operations for oil and gas producing activities before income tax	107,468	100,070
Less: related income tax expenses	(21,494)	(20,014)
Results of operations for oil and gas producing activities of the Group's subsidiaries	**85,974**	**80,056**
Share of profit (loss) of joint ventures	29,821	28,957
Total results of operations for oil and gas producing activities	**115,795**	**109,013**

Proved Oil and Gas Reserves

The Group's oil and gas reserves estimation and reporting process involves an annual independent third party reserve appraisal as well as internal technical appraisals of reserves. The Group maintains its own internal reserve estimates that are calculated by qualified engineers and technical staff working directly with the oil and gas properties. The Group's technical staff periodically updates reserve estimates during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The Group estimates its oil and gas reserves in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves.

The oil and gas reserve estimates reported below are determined by the Group's independent petroleum reservoir engineers, DeGolyer and MacNaughton ("D&M"). The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for the reserve determination. The Group's and D&M's technical staffs meet to review and discuss the information provided, and upon completion of this process, senior management reviews and approves the final reserve estimates issued by D&M.

The following reserve estimates were prepared using standard geological and engineering methods generally accepted by the petroleum industry. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

The following information presents the quantities of proved oil and gas reserves and changes thereto as at and for the years ended 31 December 2016 and 2015.

Extensions of production licenses are assumed to be at the discretion of the Group. Management believes that proved reserves should include quantities which are expected to be produced after the expiry dates of the Group's production licenses. The principal licenses of the Group for exploration and production expire between 2029 and 2059, with the most significant licenses for Yurkharovskoye and East-Tarkosalinskoye fields, expiring in 2034 and 2043, respectively. Legislation of the Russian Federation states that, upon expiration, a license is subject to renewal at the initiative of the license holder provided that further exploration, appraisal, production or remediation activities are necessary and provided that the license holder has not violated the terms of the license. Management intends to extend its licenses for properties expected to produce beyond the license expiry dates.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

Proved developed reserves are those reserves which are expected to be recovered through existing wells with existing equipment and operating methods. Undeveloped reserves are those reserves which are expected to be recovered as a result of future investments to drill new wells, to re-complete existing wells and/or install facilities to collect and deliver the production.

Net reserves exclude quantities due to others when produced.

The reserve quantities below include 100 percent of the net proved reserve quantities attributable to the Group's consolidated subsidiaries and the Group's ownership percentage of the net proved reserves quantities of the joint ventures. A portion of the Group's total proved reserves are classified as either developed non-producing or undeveloped. Of the non-producing reserves, a portion represents existing wells which are to be returned to production at a future date.

For convenience, reserves estimates are provided both in English and Metric units.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of natural gas are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	Billions of cubic feet	*Billions of cubic meters*	*Billions of cubic feet*	*Billions of cubic meters*	*Billions of cubic feet*	*Billions of cubic meters*
Reserves at 31 December 2014	**35,956**	**1,018**	**25,879**	**733**	**61,835**	**1,751**
Changes attributable to:						
Revisions of previous estimates	1,035	30	1,210	34	2,245	64
Extension and discoveries	1,247	35	68	2	1,315	37
Disposals (1)	-	-	(325)	(9)	(325)	(9)
Production	(1,735)	(49)	(662)	(19)	(2,397)	(68)
Reserves at 31 December 2015 (2)	**36,503**	**1,034**	**26,170**	**741**	**62,673**	**1,775**
Changes attributable to:						
Revisions of previous estimates	824	23	1,630	47	2,454	70
Extension and discoveries	633	18	360	10	993	28
Disposals (2)	-	-	(1,823)	(52)	(1,823)	(52)
Production	(1,631)	(46)	(703)	(20)	(2,334)	(66)
Reserves at 31 December 2016	**36,329**	**1,029**	**25,634**	**726**	**61,963**	**1,755**
Net proved developed reserves (included above)						
At 31 December 2014	17,039	482	8,086	229	25,125	711
At 31 December 2015	16,598	470	7,785	220	24,383	690
At 31 December 2016	13,994	396	8,241	233	22,235	629
Net proved undeveloped reserves (included above)						
At 31 December 2014	18,917	536	17,793	504	36,710	1,040
At 31 December 2015	19,905	564	18,385	521	38,290	1,085
At 31 December 2016	22,335	633	17,393	493	39,728	1,126

(1) In August 2015, the Group contributed a 6.4 percent interest in Artic Russia to Yamal Development. As a result, the Group's effective participation interest in SeverEnergia decreased from 54.9 percent to 53.3 percent.

(2) At 31 December 2015, the Group's share in proved reserves of natural gas of joint ventures included reserves attributable to 9.9 percent interest in OAO Yamal LNG classified as asset held for sale of 1,823 billion of cubic feet or 52 billion of cubic meters. In March 2016, the Group recognized the disposal of the 9.9 percent stake in Yamal LNG. As a result, the Group's interest in Yamal LNG decreased from 60.0 percent to 50.1 percent.

The net proved reserves reported in the table above included reserves of natural gas attributable to non-controlling interest of 147 billion of cubic feet (four billion cubic meters) and 112 billion of cubic feet (three billion cubic meters) at 31 December 2016 and 2015, respectively.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of crude oil, gas condensate and natural gas liquids are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	Millions of barrels	*Millions of metric tons*	*Millions of barrels*	*Millions of metric tons*	*Millions of barrels*	*Millions of metric tons*
Reserves at 31 December 2014	**512**	**62**	**680**	**78**	**1,192**	**140**
Changes attributable to:						
Revisions of previous estimates	14	2	34	3	48	5
Extension and discoveries	59	8	3	1	62	9
Disposals [(1)]	-	-	(14)	(2)	(14)	(2)
Production	(34)	(4)	(43)	(5)	(77)	(9)
Reserves at 31 December 2015 [(2)]	**551**	**68**	**660**	**75**	**1,211**	**143**
Changes attributable to:						
Revisions of previous estimates	116	11	58	8	174	19
Extension and discoveries	15	1	18	3	33	4
Disposals [(2)]	-	-	(13)	(2)	(13)	(2)
Production	(59)	(7)	(46)	(5)	(105)	(12)
Reserves at 31 December 2016	**623**	**73**	**677**	**79**	**1,300**	**152**
Net proved developed reserves (included above)						
At 31 December 2014	216	26	271	31	487	57
At 31 December 2015	305	38	302	34	607	72
At 31 December 2016	275	33	326	37	601	70
Net proved undeveloped reserves (included above)						
At 31 December 2014	296	36	409	47	705	83
At 31 December 2015	246	30	358	41	604	71
At 31 December 2016	348	40	351	42	699	82

(1) In August 2015, the Group contributed a 6.4 percent interest in Artic Russia to Yamal Development. As a result, the Group's effective participation interest in SeverEnergia decreased from 54.9 percent to 53.3 percent.

(2) At 31 December 2015, the Group's share in proved reserves of crude oil, gas condensate and natural gas liquids of joint ventures included reserves attributable to 9.9 percent interest in OAO Yamal LNG classified as asset held for sale of 13 million of barrels or two million of metric tons. In March 2016, the Group recognized the disposal of the 9.9 percent stake in Yamal LNG. As a result, the Group's interest in Yamal LNG decreased from 60.0 percent to 50.1 percent.

The net proved reserves reported in the table above included reserves of crude oil, gas condensate and natural gas liquids attributable to non-controlling interest of 66 million of barrels (nine million metric tons) and 49 million of barrels (six million metric tons) at 31 December 2016 and 2015, respectively.

PAO NOVATEK was incorporated as a joint stock company in accordance with the Russian law and is domiciled in the Russian Federation.

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