PJSC "RussNeft"

Consolidated financial statements

for the year ended 31 December 2016
together with independent auditor's report

PJSC "RussNeft"

Consolidated financial statements

for the year ended 31 December 2016

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улучшаем мир

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Independent auditors' report

To the shareholders of Public joint stock company (PJSC) "RussNeft"

We have audited the accompanying consolidated financial statements of Public joint stock company (PJSC) "RussNeft" and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for 2016, and a summary of significant accounting policies and other explanatory information.

Audited entity's responsibility for the consolidated financial statements

Management of Public joint stock company (PJSC) "RussNeft" is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, 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.

Auditor's responsibility

Our responsibility is to express an opinion on the fairness of these consolidated financial statements based on our audit.

We conducted our audit in accordance with the federal standards on auditing effective in the Russian Federation. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Public joint stock company (PJSC) "RussNeft" and its subsidiaries as at 31 December 2016, and their financial performance and cash flows for 2016 in accordance with International Financial Reporting Standards.

Emphasis of matter

Without qualifying our opinion on the reliability of the consolidated financial statements, we draw attention to Note 1 "General information" to the consolidated financial statements, which indicates that the Company changed its legal form from a joint stock company to a public joint stock company on 14 September 2016.

I.A. Buyan
Partner
Ernst & Young LLC

27 March 2017

Details of the audited entity

Name: Public joint stock company (PJSC) "RussNeft"
Record made in the State Register of Legal Entities on 17 September 2002, State Registration Number 1027717003467.
Address: Russia 115054, Moscow, Pyatnitskaya st., 69.

Details of the auditor

Name: Ernst & Young LLC
Record made in the State Register of Legal Entities on 5 December 2002, State Registration Number 1027739707203.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050648.

PJSC "RussNeft"

Consolidated Statement of Profit or Loss and Other Comprehensive Income

for the year ended 31 December 2016

(in millions of Russian rubles)

	Notes	Year ended 31 December 2016	Year ended 31 December 2015
Revenue	11	105,003	104,790
Cost of sales	12	(74,428)	(79,237)
Gross profit		**30,575**	**25,553**
Exploration expenses		(744)	(946)
Selling expenses	13	(9,343)	(9,663)
General and administrative expenses	13	(5,145)	(4,123)
Other operating expenses, net	15	(631)	(1,117)
Operating profit		**14,712**	**9,704**
Finance income	14	4,920	21,101
Finance expense	14	(11,702)	(22,561)
Foreign exchange differences, net		10,879	(31,671)
Share in loss of associates and joint ventures	10	–	(2,558)
Profit/(Loss) before tax		**18,809**	**(25,985)**
Income tax (expense)/benefit	27	(5,372)	25
Profit/(Loss) for the period		**13,437**	**(25,960)**
Other comprehensive income			
Foreign currency translation gain		632	49
Total comprehensive income/(loss), net of tax		**14,069**	**(25,911)**
Profit/(Loss) attributable to:			
Shareholders of the Parent		14,945	(27,650)
Non-controlling interests		(1,508)	1,690
Total comprehensive income/(loss) attributable to:			
Shareholders of the Parent		18,845	(26,779)
Non-controlling interests		(4,776)	868
Basic and diluted earnings per share (RUB)	23	50	(138)
Weighted average number of the ordinary shares (millions of shares)		249	200

E.V. Tolochek
President

O.E. Prozorovskaya
Senior Vice-President
of Economics and Finance

Authorized for issue on 27 March 2017

The accompanying notes on pages 9 to 69 are an integral part of these consolidated financial statements.

PJSC "RussNeft"

Consolidated Statement of Financial Position

as at 31 December 2016

(in millions of Russian rubles)

	Notes	31 December 2016	31 December 2015
Assets			
Non-current assets			
Oil and gas properties	16	107,835	99,947
Other property, plant and equipment	16	4,230	5,107
Goodwill	17	13,544	13,730
Deferred tax assets	27	17,777	19,515
Exploration and evaluation assets	18	41	–
Other long-term financial assets	19	50,218	59,543
Investments in associates and joint ventures	10	–	–
Other non-current assets		229	302
Total non-current assets		**193,874**	**198,144**
Current assets			
Inventories	20	6,797	6,050
Trade and other receivables	21	6,022	5,082
Income tax receivable		226	820
Value added tax receivable		1,089	1,792
Other short-term financial assets	19	3,346	–
Cash and cash equivalents	22	3,068	1,943
Other current assets		33	31
Total current assets		**20,581**	**15,718**
Total assets		**214,455**	**213,862**
Equity and liabilities			
Equity attributable to Shareholders of the Parent			
Share capital	23	196	100
Share premium	23	60,289	–
Foreign currency translation reserve		1,849	(2,051)
Accumulated loss		(17,283)	(19,001)
Total equity attributable to Shareholders of the Parent		**45,051**	**(20,952)**
Non-controlling interests	8	16,656	(1,680)
Total equity		**61,707**	**(22,632)**
Long-term liabilities			
Long-term loans and borrowings	24	84,976	175,716
Deferred tax liabilities	27	6,238	5,546
Decommissioning liability	25	9,372	4,973
Other long-term liabilities		15	1
Total long-term liabilities		**100,601**	**186,236**
Short-term liabilities			
Short-term loans and borrowings	24	118	3,221
Trade and other payables and accrued liabilities	26	45,757	41,191
Taxes and duties payable (excluding income tax)	26	6,135	5,000
Income tax payable		17	8
Other short-term liabilities		120	838
Total short-term liabilities		**52,147**	**50,258**
Total liabilities and equity		**214,455**	**213,862**

The accompanying notes on pages 9 to 69 are an integral part of these consolidated financial statements.

PJSC "RussNeft"

Consolidated Statement of Changes in Equity

for the year ended 31 December 2016

(in millions of Russian rubles)

		Equity attributable to Shareholders of the Parent						
	Notes	Share capital	Share premium	Foreign currency translation reserve	Retained earnings / (Accumulated loss)	Shareholders' equity	Non-controlling interests	Total equity
31 December 2014		**100**	**–**	**(102,090)**	**(22,469)**	**(124,459)**	**22,660**	**(101,799)**
Profit/(Loss) for the period		–	–	–	(27,650)	(27,650)	1,690	(25,960)
Foreign currency translation reserve		–	–	871	–	871	(822)	49
Effect of change in functional currency		–	–	99,168	(99,168)	–	–	–
Total comprehensive income/(loss) for the period		**–**	**–**	**100,039**	**(126,818)**	**(26,779)**	**868**	**(25,911)**
Dividends	7	–	–	–	–	–	(6)	(6)
Changes in non-controlling interests in subsidiaries due to purchase of treasury shares by subsidiaries	7	–	–	–	(2)	(2)	(32)	(34)
Changes in non-controlling interests of subsidiaries		–	–	–	19,453	19,453	(25,006)	(5,553)
Forgiveness of debt by shareholders		–	–	–	82,645	82,645	–	82,645
Acquisition of subsidiaries		–	–	–	–	–	1	1
Changes in non-controlling interests in subsidiaries due to reorganization		–	–	–	165	165	(165)	–
Other transactions with shareholders	19	–	–	–	28,025	28,025	–	28,025
31 December 2015		**100**	**–**	**(2,051)**	**(19,001)**	**(20,952)**	**(1,680)**	**(22,632)**
Profit/(Loss) for the period		–	–	–	14,945	14,945	(1,508)	13,437
Foreign currency translation reserve		–	–	3,900	–	3,900	(3,268)	632
Total comprehensive income/(loss) for the period		**–**	**–**	**3,900**	**14,945**	**18,845**	**(4,776)**	**14,069**
Issue of common shares	23	47	33,299	–	–	33,346	–	33,346
Issue of preference shares	23	49	26,990	–	–	27,039	–	27,039
Dividends	7, 23	–	–	–	–	–	(2)	(2)
Dividends refund		–	–	–	–	–	9	9
Conversion of debt into equity of a subsidiary	7, 24	–	–	–	2,148	2,148	8,592	10,740
Disposal of subsidiaries		–	–	–	–	–	(858)	(858)
Non-controlling interests in shareholders' contribution to subsidiaries' equity		–	–	–	(69)	(69)	69	–
Changes in non-controlling interests of subsidiaries	7	–	–	–	(15,306)	(15,306)	15,302	(4)
31 December 2016		**196**	**60,289**	**1,849**	**(17,283)**	**45,051**	**16,656**	**61,707**

The accompanying notes on pages 9 to 69 are an integral part of these consolidated financial statements.

PJSC "RussNeft"

Consolidated Statement of Cash Flows

for the year ended 31 December 2016

(in millions of Russian rubles)

	Notes	Year ended 31 December 2016	Year ended 31 December 2015
Cash flows from operating activities			
Profit/(Loss) before tax		18,809	(25,985)
Profit/(Loss) before tax		**18,809**	**(25,985)**
Adjustments for non-cash items to reconcile profit before income tax to net cash flows			
Depreciation, depletion and amortization	12	10,428	10,581
Loss on disposal of property, plant and equipment	15	407	59
Impairment of financial investments	15	37	35
Impairment of property, plant and equipment and exploration and evaluation assets	15	150	566
Benefit obligations, bad debt allowance and other provisions		1,383	(361)
Dissolution of subsidiaries		(675)	–
Share in loss of joint ventures	10	–	2,558
Finance income	14	(4,920)	(21,101)
Finance expense	14	11,702	22,561
Foreign exchange differences, net		(10,879)	31,671
Other adjustments		(64)	494
Net operating cash flows before working capital changes		**26,378**	**21,078**
Working capital adjustments			
(Increase)/Decrease in inventories		(1,172)	84
(Increase)/Decrease in trade and other receivables		(1,133)	1,305
Increase in trade and other payables		4,466	5,329
Decrease in other current assets		28	54
Income tax paid		(1,246)	(1,155)
Net cash from operating activities		**27,321**	**26,695**
Cash flows from investing activities			
Purchase of property, plant and equipment and other non-current assets		(17,846)	(10,077)
Proceeds from disposal of property, plant and equipment		122	103
Acquisition of subsidiaries and joint ventures, net of cash acquired		–	(933)
Loans issued	19	(310)	(37,321)
Proceeds from loans issued	19	25	75,050
Interest received		–	14,178
Net cash used in / from investing activities		**(18,009)**	**41,000**
Cash flows from financing activities			
Acquisition of non-controlling interests in subsidiaries and purchase of treasury shares	7, 9	(4)	(5,488)
Proceeds from loans and borrowings received		46,951	136,466
Repayment of loans and borrowings received	24	(46,627)	(184,068)
Interest paid	24	(6,883)	(15,089)
Dividends paid to non-controlling shareholders	7	(2)	(13)
Net cash used in financing activities		**(6,565)**	**(68,192)**
Effect of foreign exchange rate changes on balances of cash and cash equivalents		(1,622)	377
Change in cash and cash equivalents		**1,125**	**(120)**
Cash and cash equivalents at the beginning of the period		1,943	2,063
Cash and cash equivalents at the end of the period		**3,068**	**1,943**

The accompanying notes on pages 9 to 69 are an integral part of these consolidated financial statements.

1. General information

The consolidated financial statements of Public Joint Stock Company "RussNeft" (the "Parent" or the "Company") and its subsidiaries (collectively referred to as the "Group") for the year ended 31 December 2016 were authorized for issue in accordance with a resolution of management on 27 March 2017.

The Group comprises joint stock companies and limited liability companies as defined in the Civil Code of the Russian Federation. In addition, the Group includes limited liability companies in the Republic of Belarus, the Republic of Azerbaijan, the United Kingdom of Great Britain and Northern Ireland, the Republic of Cyprus, the Islamic Republic of Mauritania, the British Virgin Islands and the Cayman Islands.

The principal activities of the Group are oil and gas exploration, development, production and marketing.

The Parent was incorporated on 17 September 2002. According to decision of the general meeting of the Company's shareholders, which took place on 14 September 2016, the Company's name in the Unified State Register of Legal Entities was changed to Public Joint Stock Company "RussNeft" (PJSC "RussNeft") due to a change of the legal form from joint stock company to public joint stock company.

The Parent is located at 69 Pyatnitskaya Street, Moscow, Russian Federation, tel.: +7 (495) 411-63-09, e-mail:russneft@russneft.ru, www.russneft.ru.

In November 2016, the Company's shareholders placed 20% of the Company's common shares (15% of its share capital) on the Moscow Exchange (Note 23).

As at 31 December 2016, the person which is able to control the actions of the Company is Mikhail Safarbekovich Gutseriev.

Principal subsidiaries included in the consolidated financial statements and respective ownership interests of the Company as at 31 December 2016 and 2015 are presented in Note 7.

In 2016, the average number of employees employed by the subsidiaries of the Group as at 31 December 2016 was 9,975 people (2015: 10,555 people).

2. Basis of preparation

Statement of compliance

The consolidated financial statements of the Group for the year ended 31 December 2016 have been prepared in accordance with International Financial Reporting Standards ("IFRS").

2. Basis of preparation (continued)

Basis of accounting

The Group’s companies, incorporated in the Russian Federation, maintain their accounting records in Russian rubles ("RUB") and prepare their financial statements in accordance with the Regulations on Accounting and Reporting in the Russian Federation. The consolidated financial statements are based on the statutory accounting records, with adjustments and reclassifications recorded for the purpose of fair presentation of information in accordance with IFRS. Management believes that these consolidated financial statements reflect all significant adjustments required to present fairly the Group’s financial position, performance results, and statements of changes in equity and cash flows for the reporting and comparable periods. The principal adjustments relate to the consolidation of subsidiaries, changes in non-controlling interests, goodwill recognition, accounting for jointly controlled transactions and investments in associates, expense and revenue recognition, valuation allowances for unrecoverable assets, depreciation and valuation of property, plant and equipment, use of fair values, impairment of assets, foreign currency translation, financial instruments, deferred tax and decommissioning liability.

Basis of measurement

These consolidated financial statements are prepared on a historical cost basis, except as disclosed in Note "Summary of significant accounting policies" below.

The consolidated financial statements are presented in Russian rubles, and all values are rounded to the nearest million ("RUB million"), unless otherwise indicated.

Functional currency and foreign currency translation

The financial statements of each of the Group's companies are measured using the currency of the primary economic environment in which the company operates (the "functional currency"). The functional currency of the Group's subsidiaries operating in Russia, the Parent and certain foreign subsidiaries of the Group incorporated due to the extension of the Parent's operations is the Russian ruble. The functional currency of other foreign subsidiaries is the US dollar.

In individual companies, transactions in foreign currencies are initially recorded in the functional currency by applying the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the official exchange rate set by the Central Bank of Russia (the "CBR") at the reporting date. All resulting exchange differences are included in the consolidated statement of profit or loss and other comprehensive income. Non-monetary assets and liabilities that are measured at historical cost and denominated in a foreign currency are translated into the functional currency using the rates of exchange as at the dates of the initial transactions. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated into the functional currency using the rate of exchange at the date the fair value was determined.

2. Basis of preparation (continued)

Functional currency and foreign currency translation (continued)

As at 31 December 2016, assets and liabilities (including related goodwill) of non-RUB functional currency subsidiaries, joint ventures and associates are translated in the consolidated financial statements into the presentation currency of the Group using the rate of exchange effective at the reporting date. The performance results and cash flows of non-RUB functional currency subsidiaries, joint ventures and associates are translated into Russian rubles using the average rates of exchange for the reporting period; in case of significant exchange rate fluctuations certain significant transactions are translated at the exchange rate ruling at the date of the transaction. The exchange differences arising on such translation are recorded as a separate equity component. On disposal of a company whose functional currency is different from the presentation currency, the deferred cumulative amount of the foreign currency translation reserve recorded within equity and related to that particular company is recognized in the consolidated statement of profit or loss and other comprehensive income.

In the Russian Federation, official exchange rates are set daily by the CBR. As at 31 December 2016 and 2015, the exchange rates used for the translation of USD-denominated transactions and balances were equal to the official CBR exchange rate of RUB 60.6569 and RUB 72.8827 per one US dollar, respectively. As at 27 March 2016, the official rate of exchange was RUB 57.4247 per one US dollar.

Going concern

These consolidated financial statements have been prepared on a going concern basis that contemplates the sale of assets and the settlement of any liabilities (including contractual) in the normal course of business. This statement was made based on the assessment of Group's ability to continue as a going concern for at least twelve months after the end of the reporting period.

Basis of consolidation

Subsidiaries

Subsidiaries are the companies controlled by the Parent. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The Group has control over the investee when the following conditions are met:

- the Group has the power over the investee;
- the Group is exposed to, or has rights, to variable returns from its involvement with the investee;
- the Group has the ability to use its authority over the investee to affect its returns.

2. Basis of preparation (continued)

Basis of consolidation (continued)

Subsidiaries are consolidated from the date, on which control is transferred to the Group and are no longer consolidated from the date when control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the Parent, using consistent accounting policies. Where necessary, the accounting policies of the subsidiaries have been changed to ensure consistency with the policies adopted by the Group. All intercompany transactions, balances and unrealized gains on transactions between the Group entities are eliminated; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

A change in the ownership interest without a loss of control is accounted for as an equity transaction.

In case of a loss of control over a subsidiary the Group:

- derecognizes the assets and liabilities of the subsidiary including goodwill;
- derecognizes the carrying amount of any non-controlling interests;
- derecognizes the cumulative foreign currency translation recorded in equity;
- recognizes the fair value of the consideration received;
- recognizes the fair value of any investment retained;
- recognizes profit or loss due to a loss of control related to the controlling interest of the disposed subsidiary in the consolidated statement of profit or loss and other comprehensive income;
- reclassifies the Parent company's share of components previously recognized in other comprehensive income to profit or loss or retained earnings in accordance with IFRS requirements.

Non-controlling interests stand for the equity in subsidiaries not attributable, directly or indirectly, to the Parent company. Non-controlling interests are presented in the consolidated statement of financial position of the Group within equity, separately from the Parent's Shareholders' equity. Profit or loss, as well as every component within comprehensive income, are attributable to Shareholders of the Parent and non-controlling interests even if that results in a deficit balance of non-controlling interests.

Joint arrangements and joint venture

Joint arrangements stand for arrangements jointly controlled by two or more parties under contractual agreements. Joint arrangements can take the form of either a joint operation or a joint venture.

Joint venture is an agreement of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Generally joint ventures are established in form of a legal entity where the Group and other participants have respective equity interests.

2. Basis of preparation (continued)

Basis of consolidation (continued)

Joint control is contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

Joint operation implies that the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. According to its interest in a joint operation the Group recognizes its assets and share in joint obligations as well as in revenue from the sales of goods and expenses including the share in joint expenses.

Associates

Associates are those entities in which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but not to control or jointly control it.

When deciding whether significant influence or joint control exists, the Group considers the same factors used to evidence the existence of control in subsidiaries.

The Group accounts for investments in joint ventures and associates using the equity method. Under the equity method the investments in associates or joint ventures are initially recognized at cost. The carrying amount of investment is adjusted in subsequent periods for the post acquisition changes in the Group's share of the net assets of associates or joint ventures. Goodwill relating to the associate or joint venture is included in the carrying amount of the investment and is neither amortized nor individually tested for impairment; the entire carrying amount is tested for impairment where there is the evidence of impairment of an investment.

The consolidated statement of profit or loss and other comprehensive income reflects the Group's share in the results of the associate or joint venture. Changes in other comprehensive income of such investees are recognized in other comprehensive income of the Group. Besides, when there has been a change recognized directly in the equity of the associate or joint venture, the Group recognizes its share of any changes and discloses this, when applicable, in the consolidated statement of changes in equity.

Unrealized gains and losses resulting from transactions between the Group and the associate or joint venture are eliminated to the extent of the interest in the associate or joint venture.

The Group's share of profits or losses of the associate and joint venture is shown directly in the consolidated statement of profit or loss and other comprehensive income separately from the operating income of the Group. It is represented by profits or losses after tax and non-controlling interests in the subsidiaries of the associate or joint venture. The financial statements of the associate or joint venture are prepared for the same reporting period as the Group's financial statements. Adjustments are made where necessary to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognize an additional impairment loss on the Group's investment in the associate or joint venture. The Group determines at each reporting date whether there is any objective evidence that the investment in associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of an associate or joint venture and its carrying amount and recognizes the amount in the consolidated statement of profit or loss and other comprehensive income in line "Share in income/(loss) of associates and joint ventures".

2. Basis of preparation (continued)

Basis of consolidation (continued)

If the significant influence over the associate or joint venture is lost, the Group assesses and recognizes the investments retained at fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control and the fair value of the retained investment and proceeds from disposal is recognized in profit or loss.

Accounting policies

The accounting policies adopted are consistent with those of the previous reporting period. Effect of new and revised IFRS, amendments and interpretations, which became effective from 1 January 2016 is described below.

New standards, interpretations and amendments to existing standards and interpretations applied by the Group for the first time	**Summary of amendments to standards**	**Effect on the consolidated financial statements**
Amendments to IAS 1 *Presentation of Financial Statements*	These amendments are intended to improve quality of disclosures in the financial statements.	The amendments did not have any material effect on the financial statements as the Company prepares disclosures based on the principles of materiality and aggregation.
Amendments to IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets: Clarification of Acceptable Methods of Depreciation and Amortization*	The amendments clarify that a revenue-based depreciation method is not considered to be appropriate for measuring the consumption of the future economic benefits embodied in an asset.	These amendments had no impact on the Group as it does not apply revenue-based amortization method.
Amendments to IFRS 11 *Joint Arrangements: Accounting for Acquisitions of Interests*	These amendments explain accounting for investments in a joint operation that is a separate business and provide that the acquirer of an interest in a joint operation is required to apply the principles on business combinations accounting defined in IFRS 3.	These amendments had no impact on the financial statements as the Group did not acquire any interests in joint operations in the reporting period.
Annual Improvements 2012-2014 Cycle include amendments to IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, IFRS 7 *Financial Instruments: Disclosures*, IAS 19 *Employee Benefits*, IAS 34 *Interim Financial Reporting*	IFRS 5: The amendment clarifies that changing from one of these disposal methods to the other should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. IFRS 7: The amendment particularly clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. IAS 19: The amendment clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the bond is denominated, rather than the country where bond was issued. IAS 34: The amendment clarifies that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the greater interim financial report.	The amendments had no impact on the financial statements.
IFRS 14 *Regulatory Deferral Accounts*	The standard describes operations of the entities, whose activities are subject to rate-regulation.	Since the Group is not involved in activities, which are subject to rate-regulation, this standard had no impact on the financial statements.

3. Significant accounting judgments, estimates and assumptions

Judgments

In particular, information about significant areas of estimation uncertainty considered by management in preparing the consolidated financial statements is described in the following notes:

Note 9 − Business combinations, acquisition of associates and joint ventures and acquisition of non-controlling interests in subsidiaries;

Note 10 – Investments in associates and joint ventures;

Note 16 − Property, plant and equipment;

Note 17 − Goodwill;

Note 18 − Exploration and evaluation assets;

Note 19 − Other long-term and short-term financial assets;

Note 21 − Trade and other receivables;

Note 24 – Long-term and short-term loans and borrowings;

Note 25 – Decommissioning liability;

Note 27 – Income tax;

Note 29 – Fair value measurement;

Note 30 – Contingencies, commitments and operating risks;

Note 31 − Financial risk management;

Note 32 − Oil and gas reserves (unaudited).

In the process of applying the Group's accounting policies, management has made the following judgments, based on the professional experience, that have the most significant effect on the amounts recognized in the consolidated financial statements.

Reserves base

Oil and gas development and production properties are depreciated on a unit-of-production basis at a rate calculated by reference to total proved or proved developed reserves determined in accordance with the standards set by the Society of Petroleum Engineers (SPE standards for estimating reserves) and incorporating the estimated future cost of developing and extracting those reserves. Commercial reserves are determined using estimates of oil in place, recovery rates and expected oil prices. Future development costs are estimated using assumptions as to production facilities required to extract commercial reserves and their costs. The level of estimated commercial reserves is also a key determinant in assessing whether the carrying value of any of the Group's non-current assets, including goodwill, have been impaired. Revaluation according to new data is possible during the process of field development. Reserves base of the Group is disclosed in Note 32.

Carrying amount of oil and gas properties

Oil and gas properties, excluding wells, are depreciated using the unit-of-production (UOP) method over proved mineral reserves of certain fields and other oil and gas infrastructure facilities. Wells are depreciated over proved developed reserves. The calculation of the unit-of-production rate of depreciation could be impacted to the extent that actual production in the future is different from current forecast production based on proved developed reserves. This would generally result from significant changes in any of the factors or assumptions used in estimating reserves.

3. Significant accounting judgments, estimates and assumptions (continued)

Judgments (continued)

These factors could include:

- changes in proved or proved developed reserves;
- the effect on total proved or proved developed reserves of differences between actual commodity prices and commodity price assumptions;
- unforeseen operational issues.

Impairment indicators

The recoverable amounts of cash-generating units and individual assets have been determined based on the higher of value-in-use calculations and fair values less costs to sell. These calculations require the use of estimates and assumptions. It is reasonably possible that the oil price assumption may change which may then impact the estimated life of the field and may then require a material adjustment to the carrying value of goodwill and other non-current assets. The Group monitors internal and external indicators of impairment relating to its financial and non-financial assets.

Fair value of financial assets and liabilities

Fair value of financial assets and liabilities, except for financial instruments traded in major markets, is determined using various valuation techniques. Management applies professional judgment in accepting assumptions at each reporting date. The discounted cash flow analysis is applied in relation to financial assets and liabilities not traded in major markets. The effective interest rate is determined based on the market interest rates of financial instruments available to the Group. When such instruments are unavailable, the effective interest rate is determined based on the market interest rates as adjusted by the Group's management for the risks inherent to the Group. Fair values and sensitivity analysis of financial assets and liabilities are disclosed in Notes 29 and 31.

Decommissioning liability

Decommissioning costs will be incurred by the Group mainly at the end of the operating life of the fields. The ultimate decommissioning costs are uncertain and cost estimates can vary in response to many factors, including changes to relevant legal requirements, the emergence of new restoration techniques and/or experience at other production sites. The expected timing and amount of expenditure may also change, for example, in response to changes in reserves or changes in laws and regulations or their interpretation. As a result, there could be significant adjustments to the provisions recognized which, in turn, would affect future financial results.

Useful life of other property, plant and equipment

The Group assesses the remaining useful lives of items of other property, plant and equipment at least at each financial year-end. If expectations differ from the previous estimates, the changes are accounted for as a change in the accounting estimates in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and on depreciation recognized in the consolidated statement of profit or loss and other comprehensive income.

3. Significant accounting judgments, estimates and assumptions (continued)

Judgments (continued)

Bad debt allowance

Management maintains an allowance for doubtful accounts to account for estimated losses resulting from the inability of customers and other debtors to make required payments. When evaluating the adequacy of an allowance for doubtful accounts, management bases its estimates on the aging of accounts receivable balances and historical write-off experience, customer credit worthiness and changes in customer payment terms. If the financial condition of customers were to deteriorate, actual write-offs might be higher than expected.

Income tax

The Group recognizes the net future tax benefit related to deferred income tax assets to the extent that it is probable that the deductible temporary differences will reverse in the foreseeable future. Assessing the recoverability of deferred income tax assets requires the Group to make significant estimates related to expectations of future taxable income. Estimates of future taxable income are based on projected cash flows from operating activities and the application of existing tax laws in each jurisdiction.

To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Group to realize the net deferred tax assets recorded at the reporting date could be impacted. Additionally, future changes in tax laws in the jurisdictions in which the Group operates could limit the ability of the Group to obtain tax deductions in future periods.

Contingencies

By their nature, contingencies will be resolved only when one or more future events occur or fail to occur. The assessment of contingencies inherently involves the exercise of significant judgment and the use of estimates regarding the outcome of future events.

4. Summary of significant accounting policies

Business combinations and goodwill

Acquisitions by the Company of controlling interests in third parties (or interest in their share capital) are accounted for using the acquisition method. Acquisition date is the date when effective control over the acquiree passes to the Company.

The cost of an acquisition is measured as the aggregate of the consideration transferred measured at the acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the Company elects whether to measure the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree’s identifiable net assets. Acquisition-related costs are included in administrative expenses.

Any contingent consideration to be transferred by the acquirer should be recognized at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognized in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it will not be remeasured.

4. Summary of significant accounting policies (continued)

Business combinations and goodwill (continued)

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognized for the non-controlling interest over the net identifiable assets acquired and liabilities assumed. If the fair value of the net assets of the subsidiary acquired is in excess of the consideration, the difference is recognized in the consolidated statement of profit or loss and other comprehensive income.

Oil and natural gas exploration, evaluation expenditure

License and property acquisition costs

Exploration license and leasehold property acquisition costs are capitalized within exploration and evaluation assets. Each property is reviewed on an annual basis to confirm that drilling activity is planned and it is not impaired. If no future activity is planned, the balance of the license and property acquisition costs is written off. Upon determination of economically recoverable reserves ("proved reserves" or "commercial reserves"), and when development is approved by the Group, the relevant expenditure is transferred to oil and gas properties.

Exploration and evaluation costs

Prior to acquisition of the legal right to explore, all costs are recorded in the consolidated statement of profit or loss and other comprehensive income as incurred. Once such legal right has been acquired, exploration and evaluation costs directly associated with an exploration well are capitalized as exploration and evaluation assets until the drilling of the well is complete and the results have been evaluated. These costs include employee remuneration, materials and fuel used, rig costs and payments made to contractors. Other exploration and evaluation costs are expensed as incurred.

If extractable hydrocarbons are found and, subject to further appraisal activity, which may include the drilling of further wells, are likely to be developed commercially, the costs continue to be carried as an exploration and evaluation asset while sufficient/continued progress is made in assessing the commerciality of the hydrocarbons.

All such carried costs are subject to technical, commercial and management review for impairment at least once a year to confirm the continued intent of the Group to develop or otherwise extract value from the discovery.

When this is no longer the case, the costs are written off. When proved reserves of oil are determined and development is sanctioned, the relevant expenditure is transferred to oil and gas properties after impairment is assessed and any resulting impairment loss is recognized.

Development costs

Expenditure on the construction, installation or completion of infrastructure facilities such as pipelines and the drilling of development wells is capitalized within oil and gas properties.

4. Summary of significant accounting policies (continued)

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation and the initial estimate of the decommissioning obligation, if applicable. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset. The capitalized value of a finance lease is also included within property, plant and equipment.

At each reporting date, the Group management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management of the Group's entities estimates the recoverable amount which is determined as the higher of an asset's fair value less costs to sell and its value in use.

In assessing value in use the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded companies or other available fair value indicators.

The carrying amount is reduced to the recoverable amount, and the difference is recognized as an expense (impairment loss) in the consolidated statement of profit or loss and other comprehensive income. Impairment losses related to continuing operations are recognized in the consolidated statement of profit or loss and other comprehensive income in those expense categories that are consistent with the function of the impaired asset.

A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such increased amount is recognized in the consolidated statement of comprehensive income.

Depreciation

Oil and gas properties, except for wells, but including related future decommissioning costs are depreciated using the unit-of-production method over proved mineral reserves of the license areas and other infrastructural oil and gas properties. Wells are depreciated over proved developed reserves. The unit-of-production rate for the amortization of field development costs takes into account expenditures incurred to date, together with sanctioned future development expenditure.

Other property, plant and equipment are generally depreciated on a straight-line basis over their estimated useful lives. Property, plant and equipment held under finance leases are depreciated over the shorter of lease term and estimated useful life.

4. Summary of significant accounting policies (continued)

Depreciation (continued)

The depreciation periods, which represent the estimated remaining useful economic lives of the respective assets are as follows:

	Years
Buildings	10-60
Plant and machinery	3-15
Equipment and motor vehicles	5-10
Office and other equipment	3-10

Major maintenance and repairs

Expenditure on major maintenance refits or repairs comprises the cost of replacement assets or parts of assets and inspection costs.

Where an asset or part of an asset that was separately depreciated and is now written off is replaced and it is probable that future economic benefits associated with the item will flow to the Group, the expenditure is capitalized. Where part of the asset was not separately considered as a component, the replacement value is used to estimate the carrying amount of the replaced assets which is immediately written off. Inspection costs associated with major maintenance programs are capitalized and amortized over the period to the next inspection. All other maintenance costs are expensed as incurred.

Construction in progress

Construction in progress includes all expenses related to acquisition of property, plant and equipment, including respective variable overheads directly attributable to the construction. Accrual of depreciation and amortization of these assets commences when they are actually put into operation. The Group measures the carrying value of the construction in progress on a regular basis to identify any indication of impairment of construction in progress and to accrue a respective allowance.

Goodwill and other intangible assets

Goodwill and other intangible assets are carried at the initial cost less any accumulated amortization and any accumulated impairment losses. The initial cost of intangible assets is the aggregate amount paid or the fair value of any other consideration given to acquire the asset at the moment of its acquisition or establishment. The cost of intangible assets acquired in a business combination is initially recognized at fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortization on a straight line basis over their useful lives (except goodwill) and any accumulated impairment losses. Internally generated intangible assets are not capitalized and expenditure is reflected in the consolidated statement of profit or loss and other comprehensive income in the reporting period in which the expenditure is incurred.

4. Summary of significant accounting policies (continued)

Non-current assets held for sale and discontinued operations

Non-current assets and disposal groups classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell. Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered mainly through a sale transaction rather than continuing use. This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition. Management must be committed to the sale which qualifies for recognition as a completed sale within one year from the date of classification.

In the consolidated statement of profit or loss and other comprehensive income for the reporting period, and the comparable period of the previous year, income and expenses from discontinued operations are reported separately from income and expenses from continuing activities, down to the level of profit after taxes, even when the Group retains a non-controlling interest in the subsidiary after the sale. The resulting profit or loss (after taxes) is reported in the consolidated statement of profit or loss and other comprehensive income.

Property, plant and equipment and intangible assets once classified as held for sale are not depreciated or amortized.

Impairment of non-financial assets

Impairment of intangible assets other than goodwill is determined in the way consistent to impairment of property, plant and equipment.

The Group conducts internal reviews of values of goodwill and indefinite life intangible assets annually at 31 December or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired. Impairment is determined for goodwill by assessing the recoverable amount of the cash-generating unit (or group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (or group of cash-generating units) is less than the carrying amount of the cash-generating unit (group of cash-generating units) to which goodwill has been allocated, an impairment loss is recognized in the consolidated statement of profit or loss and other comprehensive income.

The loss recognized in the reporting period on goodwill impairment is not reversible in the next reporting period.

Financial instruments

A financial instrument is any contract that gives rise to the Group's financial assets or liabilities. Financial assets within the scope of IAS 39 are classified as either financial assets recognized in the consolidated statement of profit or loss and other comprehensive income at fair value, loans issued and receivables, held to maturity investments, or available for sale financial assets, as appropriate.

Initially financial assets are recognized at fair value. In case investments are not classified as financial assets at fair value through the consolidated statement of profit or loss and other comprehensive income, directly attributable transaction costs are added to their fair value. The Group considers whether a contract contains an embedded derivative when it first becomes a party to it.

4. Summary of significant accounting policies (continued)

Financial instruments (continued)

Embedded derivatives are separated from the host contract which is not measured at fair value in the consolidated statement of profit or loss and other comprehensive income when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

The Group determines the classification of its financial assets at initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

Loans and receivables

Loans and accounts receivable are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, loans and receivables are subsequently carried at amortized cost using the effective interest method, less allowance for impairment. Amortized cost is calculated taking into account any granted discount or premium and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognized in the consolidated statement of profit or loss and other comprehensive income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Fair value

The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business on the reporting date (Level 1 of fair value hierarchy). Inputs which are not quoted prices included within Level 1 and which are observable for the asset or liability, either directly or indirectly, represent Level 2 of fair value hierarchy. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm’s length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis or other valuation models taking into account the possible adjustments of Level 2 inputs (Level 3 of fair value hierarchy). Generally, they include unobservable inputs for the asset or liability. Management of the Group uses its own judgment in allocating financial assets to a particular level of the fair value hierarchy. In view of significant adjustments of Level 2 and other inputs, management measures fair value of its financial instruments within Level 3 of fair value hierarchy.

Cash and cash equivalents

Cash and cash equivalents recorded in the statement of financial position comprise cash at banks and on hand, short-term deposits and other short-term highly liquid financial assets with an original maturity of three months or less. For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

4. Summary of significant accounting policies (continued)

Loans and borrowings and accounts payable

The Group's financial liabilities are classified as either accounts payable, or loans and borrowings.

All loans and borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest bearing loans and borrowings are subsequently measured at amortized cost using the effective interest method; any difference between the fair value of the consideration received (net of transaction costs) and the redemption amount is recognized as interest expense over the period of the loans or borrowings.

Income and expense are recognized in the consolidated statement of profit or loss and other comprehensive income when the liabilities are derecognized in the statement of financial position as well as through the amortization process.

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalized as part of the cost of the respective assets. Other borrowing costs are expensed in the period in which they are incurred. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowings.

Inventories

Finished goods are recorded at the lower of cost and net realizable value. Cost is determined by the weighted average method and comprises direct purchase costs, cost of production, transportation and manufacturing expenses. Raw materials are valued at cost using the weighted average cost method or net realizable value, whichever is the lower. The measurement unit for crude oil is one batch.

Leases

The determination of whether an arrangement is, or contains an operating lease or a finance lease is based on the substance of the arrangement at inception. Accordingly, it should be determined whether the execution of the agreement depends on the use of a certain asset or assets and whether the agreement conveys the right to use this asset as a result of this transaction.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the commencement of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between finance expenses and reduction of the lease liability. Finance charges are allocated to each period so as to achieve a constant rate of interest on the remaining balance of the liability and are recognized directly in the consolidated statement of profit or loss and other comprehensive income.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term.

Operating lease payments are recognized as an expense in the consolidated statement of profit or loss and other comprehensive income on a straight line basis over the lease term.

4. Summary of significant accounting policies (continued)

Provisions

General

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Where the Group expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated statement of profit and loss and other comprehensive income net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as finance expense.

Decommissioning liability

Decommissioning liability is recognized when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount of obligation can be made. In accordance with license agreements, the Group has to liquidate wells, oil and gas pipelines and to restore the surface. A corresponding amount equivalent to the provision is also recognized as part of the cost of the related property, plant and equipment. The amount recognized is the estimated cost of decommissioning, discounted to its present value.

Changes in the estimated timing of property, plant and equipment items decommissioning or abandonment cost estimates are dealt with prospectively by recording an adjustment to the provision, and corresponding adjustments to the carrying amount of property, plant and equipment. The unwinding of the discount on the decommissioning provision is accounted for as finance expense.

The Group does not recognize the deferred tax asset regarding the temporary difference on the decommissioning liability and the corresponding deferred tax liability regarding the temporary difference on a decommissioning asset.

Taxes

Income tax for the reporting period includes the amount of current tax and deferred tax.

Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date in each of the countries where the Group operates and generates taxable income. Current income tax relating to items recognized directly in equity is recognized in equity.

4. Summary of significant accounting policies (continued)

Taxes (continued)

Deferred income tax

Deferred income tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying values for financial reporting purposes at the reporting date.

Deferred income tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss;
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized, except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss;
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in jointly controlled entities, deferred income tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying value of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred income tax relating to items recognized directly in equity is recognized in equity. Deferred tax items are recognized in correlation to the underlying transaction either in other comprehensive income or directly in equity.

Deferred income tax assets and deferred income tax liabilities are offset if a legally enforceable right exists to set off current income tax assets against current tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

4. Summary of significant accounting policies (continued)

Equity

Share capital issued and outstanding

Common shares issued are classified as equity.

Non-controlling interests

Non-controlling interest is the interest in a subsidiary not held by the Group. Non-controlling interest as at the reporting date is the equity in a subsidiary not attributable, directly or indirectly, to the Parent and the non-controlling shareholders' portion of movements in equity since the date of the business combination. Non-controlling interest is presented within equity, separately from the Parent shareholders' equity.

Revenue and income recognition

Revenue from sale of crude oil, petroleum products and other products is recognized when the significant risks and rewards of ownership have been transferred, which is predominantly when the title passes to the customer. This generally occurs when the product is physically transferred into a vessel or other delivery mechanism, or at the date of traversal of the Russian border when the product is transported for export or delivered to the pipe if sold at the domestic market.

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods, provided in the normal course of business, net of discounts, export duties, value added tax and other similar levies.

Interest income is accrued on a regular basis by reference to the outstanding principal amount and the applicable effective interest rate, which is the rate that discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying value.

Dividend income is recognized where the shareholder's right to receive a dividend payment is established. The amount of retained earning distributable to the shareholders is determined on the basis of the financial statements of the subsidiaries prepared in accordance with Russian accounting principles and the financial statements of the foreign subsidiaries and these amounts may differ significantly from the amounts calculated on the basis of IFRS.

Employee benefits

The Group pays wages and salaries to its employees, quarterly bonuses for achieving key performance indicators ("KPI") by the Group companies, including annual bonuses after the year-end closing period. Vacations and sick leaves are paid in accordance with the existing collective labor agreements of the Group.

The Group makes contributions to the State Pension Plan of the Russian Federation. These payments are calculated by the employer as a percentage from gross salary expense and are expensed as accrued.

The Group provides its employees with various defined retirement benefits in accordance with the collective labor agreements. The Group uses defined contribution plans. Costs of providing such benefits are recognized in the consolidated statement of profit or loss and other comprehensive income. The Company concludes non-state pension insurance agreements and recognizes them as defined contribution pension plans in the consolidated financial statements.

5. Future changes in accounting policies

The following standards and interpretations shown below become effective subsequent to the reporting period and are not adopted early. They may result in consequential changes to the accounting policies and other disclosures in notes. Currently the Group evaluates the possible impact of certain new standards and amendments to the adopted standards on the consolidated financial statements.

IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard brings together all three phases of the financial instruments accounting project: classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. The Group is currently assessing the potential impact of the standard on its financial statements and plans to adopt the new standard on the required effective date.

IFRS 15 Revenue from Contracts with Customers

A new standard IFRS 15 *Revenue from Contracts with Customers* was issued in May 2014. The new standard represents a single guidance for revenue recognition and establishes a new five-step model that will apply to revenue arising from contracts with customers and includes a comprehensive set of the relevant disclosure requirements for financial statements. The new standard replaces IAS 18 *Revenue*, IAS 11 *Construction Contracts* and a number of IFRS interpretations on revenue recognition. IFRS 15 becomes effective for annual periods beginning on or after 1 January 2018. Early application is permitted. The Group is currently evaluating the impact of the provisions of the new standard on the consolidated financial statements.

Amendments to IFRS 10 Consolidated Financial Statements, IAS 28 Investments in Associates and Joint Ventures

Amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* were issued in September 2014. The amendments prescribe that gain or loss should be recognized in full if a transaction represents a sale of business or an asset contribution. Gain or loss should be recognized in part if a transaction covers assets that do not constitute a business as defined in IFRS 3 *Business Combinations*. The primary effective date (starting from 1 January 2016) was postponed for an indefinite period of time. These amendments will not have any material effect on the consolidated financial statements.

IFRS 16 Leases

A new standard IFRS 16 *Leases* was issued in January 2016 and becomes effective for annual periods beginning on or after 1 January 2019. The standard requires to recognize assets and liabilities for the majority of lease agreements similarly to the accounting for finance leases in IAS 17. Early application is permitted if the new standard IFRS 15 *Revenue from Contracts with Customers* was applied or applied simultaneously with IFRS 16. The Group is currently evaluating the impact of the provisions of the new standard on the consolidated financial statements.

5. Future changes in accounting policies (continued)

Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative

Amendments to *IAS 7 Statement of Cash Flows: Disclosure Initiative* were issued in January 2016 and require to disclose changes in liabilities related to the financing activities, separating effect from cash and non-cash transactions. The amendments become effective for the annual periods beginning on or after 1 January 2017, with early application permitted. The Group did not apply the amended standard in the reporting period. Application of amendments will result in additional disclosure provided by the Group.

Amendment to IAS 12 Income Tax: Recognition of Deferred Tax Assets on the Unrealized Loss

Amendment to IAS 12 *Income Tax: Recognition of Deferred Tax Assets on the Unrealized Loss* were issued in January 2016. These amendments require the entity to determine whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference, as well as to evaluate future taxable profit. Amendments become effective for annual periods beginning on or after 1 January 2017, with early application permitted. The Group does not expect these amendments to have a significant impact on its consolidated financial statements.

6. Segment information

Starting from 2015, operations of the Group are mainly represented by Exploration and production segment comprising the Parent, production subsidiaries and subsidiaries providing operator and other services relating to oil and gas exploration, development, production and transportation. Operating results of the other subsidiaries are generally insignificant and management of the Group does not use them for the purpose of taking financial and operational decisions.

Revenue from external customers broken down by key products and services and geographical areas as well as information about major customers are disclosed in Note 11 Revenue. Geographical distribution of the Group's non-current assets except for financial instruments, deferred tax assets and other assets is disclosed in Note 16 Property, plant and equipment.

7. Subsidiaries of the Group

Company	Principal activity	Country of incorporation	Effective ownership 31 December 2016	Effective ownership 31 December 2015
Russneft (UK) Limited	Marketing of crude oil and petroleum products	United Kingdom	100%	100%
Russneft Cyprus Limited	Other	Republic of Cyprus	20%	100%
Benodet Intestments Limited (dissolution)	Other	Republic of Cyprus	–	51%
Kura Valley Petroleum Company	Evaluation and exploration of oil and gas	Cayman Islands	20%	100%
Kura Valley Development Company	Evaluation and exploration of oil and gas	Cayman Islands	20%	100%
Kura Valley Operating Company	Evaluation and exploration of oil and gas	Cayman Islands	16%	80%
Russneft (BVI) Limited	Other	B.V.I	20%	100%
Edmarnton Limited	Other	B.V.I	20%	100%
International Petroleum Grouping S.A.	Evaluation and exploration of oil and gas	Islamic Republic of Mauritania	11%	54%
CJSC IP Slavneftehim	Marketing of crude oil and petroleum products	Republic of Belarus	99%	100%
LLC Torgovy Dom Russneft	Other	Russian Federation	100%	100%
LLC M-Trade	Other	Russian Federation	100%	100%
CJSC Belkam-Trade	Other	Russian Federation	100%	100%
LLC Rustrade	Other	Russian Federation	100%	100%
LLC INEKS (dissolution)	Other	Russian Federation	–	100%
LLC LITEN (dissolution)	Other	Russian Federation	–	100%
LLC ELIKON (dissolution)	Other	Russian Federation	–	100%
LLC NTC Russneft (takeover by PJSC “RussNeft”)	Services	Russian Federation	–	100%
OJSC Saratovneftegaz	Extraction and marketing of crude oil and gas	Russian Federation	96%	96%
CJSC Saratov-Burenie	Extraction and marketing of crude oil	Russian Federation	96%	96%
LLC SO Agro	Other	Russian Federation	96%	96%
CJSC Upravlenie Povyshenya Nefteotdachi Plasta i Kapitalnogo Remonta Skvazhin	Other	Russian Federation	96%	96%
LLC Neftebytservis	Other	Russian Federation	96%	96%
CJSC Geofizservis	Other	Russian Federation	96%	96%
CSJC Servis-Centr Neftepromyslovogo i Burovogo Oborudovania	Other	Russian Federation	96%	96%
LLC Saratovenergoneft	Other	Russian Federation	96%	96%
LLC Zavolzhskoe Upravlenie Technologicheskogo Transporta	Transportation services	Russian Federation	96%	96%
CJSC Upravlenie Promishlennoy Avtomatiki	Other	Russian Federation	96%	96%
LLC RedOil	Extraction and marketing of crude oil and gas	Russian Federation	96%	96%
PI DOC Rovesnik	Other	Russian Federation	96%	96%
OJSC MPK Aganneftegazgeologiya	Extraction and marketing of crude oil and gas	Russian Federation	97%	97%
CJSC TD Aganneftegazgeologiya (dissolution)	Other	Russian Federation	–	97%
LLC Agan-Trans	Other	Russian Federation	97%	97%

7. Subsidiaries of the Group (continued)

Company	Principal activity	Country of incorporation	Effective ownership 31 December 2016	Effective ownership 31 December 2015
OJSC Ulyanovskneft	Extraction and marketing of crude oil	Russian Federation	100%	100%
LLC Geophisic	Other	Russian Federation	100%	100%
LLC KOLOS	Other	Russian Federation	100%	100%
OJSC Nefterazvedka	Extraction and marketing of crude oil	Russian Federation	51%	51%
OJSC Mohtikneft	Extraction and marketing of crude oil	Russian Federation	100%	100%
OJSC Varyeganneft	Extraction and marketing of crude oil and gas	Russian Federation	93%	93%
LLC Valyuninskoe	Extraction and marketing of crude oil	Russian Federation	93%	93%
LLC Novo-Aganskoe	Extraction and marketing of crude oil	Russian Federation	93%	93%
LLC Upravlenie Avtomatizatsii i Energetiki Neftyanogo Proizvodstva	Other	Russian Federation	93%	93%
LLC Upravlenie po Remontu i Obsluzhivaniyu Neftepromyslovogo Oborudovaniya	Other	Russian Federation	93%	93%
LLC Proizvodstvenno-Bytovoe Upravlenie	Other	Russian Federation	93%	93%
LLC Upravlenie Technologicheskogo Transporta	Transportation services	Russian Federation	93%	93%
ST CJSC Goloil	Extraction and sales of crude oil	Russian Federation	100%	100%
LLC Belye Nochi	Extraction and marketing of crude oil	Russian Federation	100%	100%
LLC INA-Neftetrans	Transportation services	Russian Federation	100%	100%
OJSC NAK Aki-Otyr	Extraction and marketing of crude oil	Russian Federation	100%	100%
CJSC Nazymskaya Neftegazorazvedochnaya Ekspeditsiya	Extraction and marketing of crude oil and gas	Russian Federation	100%	100%
CJSC Khanty-Mansiyskaya Neftyanaya Kompaniya	Extraction and marketing of crude oil and gas	Russian Federation	100%	100%
CJSC Chernogorskoe	Extraction and marketing of crude oil	Russian Federation	100%	100%
LLC Tomskaya neft	Extraction and marketing of crude oil	Russian Federation	100%	100%
LLC Sredne-Vasyuganskoe (takeover by LLC Tomskaya neft)	Extraction and marketing of crude oil	Russian Federation	–	100%
LLC Muromskoe (takeover by LLC Tomskaya neft)	Other	Russian Federation	–	100%
LLC NK Russneft-Bryansk	Transportation services	Russian Federation	51%	51%
Global Energy Cyprus Limited	Other	Republic of Cyprus	20%	100%
GEA Holdings Limited	Other	B.V.I	20%	100%
Kura Valley Holding Company	Other	Cayman Islands	20%	100%
Karasu Petroleum Company	Other	Cayman Islands	20%	100%
Karasu Development Company	Other	Cayman Islands	20%	100%
Karasu Operating Company[1]	Extraction and marketing of crude oil under PSA	Cayman Islands	17%	85%

[1] The company in which the Group participates in joint operations under production sharing agreement (Note 10).

7. Subsidiaries of the Group (continued)

As a result of issue of 4,000 class B shares (without voting rights) of Russneft Cyprus Limited in January 2016, which were owned by a related party, GCM Global Energy PLC, the Parent's interest in equity of Russneft Cyprus Limited decreased from 100% to 20%. Since the Parent's voting rights did not change and comprise 100%, the occurred change did not result in loss of control. Changes in non-controlling interest in the group of companies, shareholder of which is Russneft Cyprus Limited, are recorded in the consolidated statement of changes in equity and comprise RUB 15,308 million at a rate effective as at the date of issue of class B shares. The issue of these shares was settled through conversion of the financial liability (promissory note issued) recognized in these consolidated financial statements at amortized cost. Conversion of debt into equity of Russneft Cyprus Limited subsidiary is recognized as equity transaction (Note 24).

In January 2016, the subsidiaries LLC INEKS, LLC LITEN and LLC ELIKON transferred the shares of OJSC NAK Aki-Otyr (0.462%), OJSC Ulyanovskneft (0.24%), and OJSC Mohtikneft (4%) to the Parent since the above companies discontinued their operations due to dissolution during the reporting period.

In the second half of 2016, the following was made in the course of optimization of the Group's corporate structure: LLC NTC Russneft was taken over by the Parent, LLC Sredne-Vasyuganskoe and LLC Muromskoe were taken over by LLC Tomskaya neft; CJSC TD Aganneftegazgeologiya and Benodet Intestments Limited (the subsidiaries) discontinued their operations due to dissolution.

In August 2016, the Parent acquired 6,880 preference shares of OJSC Varyeganneft (0.026% of its share capital). The change in non-controlling interest was recognized in the statement of changes in equity and amounted to RUB 4 million.

In 2015, the subsidiaries OJSC Varyeganneft and OJSC MPK Aganneftegazgeologiya further repurchased the treasury shares from non-controlling shareholders in the amount of RUB 15 million and RUB 19 million. As a result of these transactions, the treasury shares interest in share capital on the balance of OJSC Varyeganneft is 1.829% and on the balance of OJSC MPK Aganneftegazgeologiya is 1.201%. Purchased common shares became non-voting and are not taken into consideration when counting votes at a shareholders meeting until their sale. The difference between the consideration paid and the carrying amount of the non-controlling interest was recorded in the consolidated statements of changes in equity.

At the annual meetings, OJSC Varyeganneft and OJSC Saratovneftegaz decided to pay dividends to preference shareholders for 2015, due to what these shares ceased to be voting. The dividends accrued on preference shares to non-controlling shareholders was recognized in the consolidated statement of changes in equity.

7. Subsidiaries of the Group (continued)

The summarized financial information on assets, liabilities, profit or loss and cash flows of the subsidiaries with material non-controlling interests is provided below:

31 December 2016	OJSC Varyeganneft and its subsidiaries	OJSC Saratovneftegaz and its subsidiaries	Russneft Cyprus Limited and its subsidiaries and joint ventures
	RUB million	RUB million	RUB million
Non-current assets	21,097	10,737	45,537
Current assets	11,684	16,132	9,851
Total assets	**32,781**	**26,869**	**55,388**
Long-term liabilities	(4,366)	(3,468)	(27,749)
Short-term liabilities	(8,838)	(2,405)	(7,392)
Total liabilities	**(13,204)**	**(5,873)**	**(35,141)**
Net assets	**19,577**	**20,996**	**20,247**
Equity attributable to Shareholders of the Parent	18,479	20,241	4,681
Equity attributable to non-controlling interests	1,098	755	15,566
Year ended 31 December 2016			
Revenue	**22,355**	**6,091**	**1,596**
Profit/(Loss) for the period	**1,554**	**(433)**	**(1,828)**
Profit/(Loss) attributable to Shareholders of the Parent	1,472	(416)	(337)
Profit/(Loss) attributable to non-controlling interests	82	(17)	(1,491)

Year ended 31 December 2016	OJSC Varyeganneft and its subsidiaries	OJSC Saratovneftegaz and its subsidiaries	Russneft Cyprus Limited and its subsidiaries and joint ventures
	RUB million	RUB million	RUB million
Operating activities	1,221	425	3,033
Investing activities	(1,207)	(12)	(3,078)
Financing activities	(14)	(415)	(211)
Total change in cash and cash equivalents for the period	**–**	**(2)**	**(256)**

7. Subsidiaries of the Group (continued)

31 December 2015	OJSC Varyeganneft and its subsidiaries	OJSC Saratovneftegaz and its subsidiaries	Russneft Cyprus Limited and its subsidiaries and joint ventures
	RUB million	RUB million	RUB million
Non-current assets	22,842	11,245	58,381
Current assets	4,299	15,273	8,180
Total assets	**27,141**	**26,518**	**66,561**
Long-term liabilities	(4,280)	(2,884)	(41,773)
Short-term liabilities	(4,796)	(2,207)	(9,298)
Total liabilities	**(9,076)**	**(5,091)**	**(51,071)**
Net assets	**18,065**	**21,427**	**15,490**
Equity attributable to Shareholders of the Parent	17,043	20,662	19,127
Equity attributable to non-controlling interests	1,022	765	(3,637)
Year ended 31 December 2015			
Revenue	**15,960**	**6,748**	**1,950**
Profit/(Loss) for the period	**730**	**(117)**	**(4,965)**
Profit/(Loss) attributable to Shareholders of the Parent	373	(112)	(4,868)
Profit/(Loss) attributable to non-controlling interests	357	(5)	(97)

Year ended 31 December 2015	OJSC Varyeganneft and its subsidiaries	OJSC Saratovneftegaz and its subsidiaries	Russneft Cyprus Limited and its subsidiaries and joint ventures
	RUB million	RUB million	RUB million
Operating activities	1,139	1,165	(336)
Investing activities	(1,080)	(852)	159
Financing activities	(60)	(317)	115
Total change in cash and cash equivalents for the period	**(1)**	**(4)**	**(62)**

8. Non-controlling interests

Non-controlling interests include:

	31 December 2016		2016	31 December 2015		2015
	Non-controlling interests (%)	**Non-controlling interests in net assets**	**Non-controlling interests in net profit/(loss)**	**Non-controlling interests (%)**	**Non-controlling interests in net assets**	**Non-controlling interests in net profit/(loss)**
		RUB million	**RUB million**		**RUB million**	**RUB million**
Russneft Cyprus Limited and its subsidiaries and joint ventures	80, 84, 89%	15,566	(1,491)	20, 46%	(3,637)	(96)
OJSC Varyeganneft and its subsidiaries	5%	1,098	82	5%	1,022	357
OJSC Saratovneftegaz and its subsidiaries	4%	755	(17)	4%	765	(5)
Other	1%-49%	(763)	(82)	2%-49%	170	1,434
Non-controlling interests at the end of the period		**16,656**	**(1,508)**		**(1,680)**	**1,690**

As at 31 December 2016, non-controlling voting interests in OJSC Varyeganneft, OJSC MPK Aganneftegazgeologiya and OJSC Saratovneftegaz comprise 1.638%, 2.262% and 1%, respectively.

As at 31 December 2015, non-controlling voting interests in OJSC Varyeganneft, OJSC MPK Aganneftegazgeologiya and OJSC Saratovneftegaz comprised 5%, 2% and 1%, respectively.

9. Business combinations, acquisition of associates and joint ventures and acquisition of non-controlling interests in subsidiaries

Business combinations in 2016 and 2015

The Group did not acquire new assets in 2016 and 2015.

Acquisitions of non-controlling interests in subsidiaries in 2015

The Company acquired non-controlling interests in the production subsidiaries from the related parties of the Glencore Group as part of the transactions to convert promissory notes payable to the Glencore Group. The total amount of the transactions is USD 85 million or RUB 5,552 million at the exchange rate at the date of the transaction. The transactions were fully paid in cash in 2015 in the amount of RUB 5,454 million at the exchange rate at the date of the payment. The difference of RUB 19,453 million between the consideration and the carrying amount of the acquired interests was recognized in equity in line "Retained earnings / (Accumulated loss)". Transaction costs of acquisitions of non-controlling interests were insignificant.

9. Business combinations, acquisition of associates and joint ventures and acquisition of non-controlling interests in subsidiaries (continued)

Acquisitions of non-controlling interests in subsidiaries in 2015 (continued)

	Acquisition date	Effective ownership	Carrying amount of acquired interests[2]	Consideration
		(%)	RUB million	RUB million
OJSC Varyeganneft	October 2015	41.93%	8,301	1,732
LLC Belye Nochi	October 2015	49%	5,188	2,624
OJSC NAK Aki-Otyr	October 2015	49%	3,712	339
OJSC Ulyanovskneft	October 2015	45.3%	3,134	163
LLC Tomskaya neft	October 2015	49%	2,407	274
OJSC Mohtikneft	October 2015	45%	1,393	376
CJSC Chernogorskoe	October 2015	49%	620	8
ST CJSC Goloil	October 2015	49%	251	37
			25,006	**5,553**

10. Investments in associates and joint ventures

GEA Holdings Limited Group

The Group recognizes its participation in the production sharing agreements (the "PSA") in the consolidated financial statements as joint operations involving the subsidiaries and joint ventures of GEA Holdings Limited group ("GEA group"). GEA Holdings Limited through its subsidiaries and joint ventures participates in exploration and extraction projects in the Republic of Azerbaijan under the scheme of PSA with the State Oil Company of the Republic of Azerbaijan (SOCAR) and SOCAR Oil Affiliate (SOA). Assets and liabilities, revenue and expenses of the operating companies in which the Group participates as a contractor under the PSA are recorded in accordance with the interests of the Group. Joint operations are structured through incorporation of separate legal entities (operating companies). Where the control is acquired or exercised jointly, the companies within GEA group are accounted for as business combinations (Note 7) or under the equity method. Considering the additional issue of class B shares by the parent company of GEA Holdings Limited, Russneft Cyprus Limited, in the reporting period, the change in non-controlling interests in all the companies of GEA group is recognized (Note 7). This change is recognized in the consolidated statement of changes in equity.

[2] Carrying amount of the acquired interests is calculated as carrying amount of interest in the net assets of the acquired company and its subsidiaries.

10. Investments in associates and joint ventures (continued)

GEA Holdings Limited Group (continued)

Joint ventures of GEA group are as follows:

Company	Principal activity	Country of incorporation	Effective ownership 31 December 2016[3]	Effective ownership 31 December 2015	Consolidation method
Global Energy Azerbaijan Limited	Other	B.V.I	50%	50%	Equity method
Global Energy Azerbaijan Management Limited	Other	B.V.I	50%	50%	Equity method
Neftechala Petroleum Limited	Other	B.V.I	50%	50%	Equity method
Neftechala Investments Limited	Other	B.V.I	50%	50%	Equity method
Neftechala Operating Company	Extraction and marketing of crude oil under PSA	B.V.I	40%	40%	Assets, liabilities, revenue and expenses related to the Group's interest
Absheron Petroleum Limited	Other	B.V.I	50%	50%	Equity method
Apsheron Investments Limited	Other	B.V.I	50%	50%	Equity method
Absheron Operating Company Limited	Extraction and marketing of crude oil under PSA	B.V.I	38%	38%	Assets, liabilities, revenue and expenses related to the Group's interest
Shirvan Petroleum Limited	Other	B.V.I	50%	50%	Equity method
Shirvan Investments Limited	Other	B.V.I	50%	50%	Equity method
Shirvan Operating Company Limited	Extraction and marketing of crude oil under PSA	B.V.I	40%	40%	Assets, liabilities, revenue and expenses related to the Group's interest
Repleton Enterprises Limited	Other	Republic of Cyprus	50%	50%	Equity method
AZEN OIL COMPANY B.V.	Other	Kingdom of the Netherlands	50%	50%	Equity method
Binagadi Oil Company	Extraction and marketing of crude oil under PSA	Cayman Islands	38%	38%	Assets, liabilities, revenue and expenses related to the Group's interest
Global Energy Caspian Limited	Other	B.V.I	50%	50%	Equity method

[3] Excluding the effect of change in the interest of RussNeft Group in the parent company of GEA group, Russneft Cyprus Limited (Note 7).

10. Investments in associates and joint ventures (continued)

GEA Holdings Limited Group (continued)

Summarized financial information of the joint ventures of the GEA group and carrying amounts of investments in the joint ventures is provided below.

The statement of financial position as at 31 December 2016 and 2015:

	31 December 2016 RUB million	31 December 2015 RUB million
Non-current assets	43,644	57,809
Current assets	2,366	2,150
including cash and cash equivalents	*284*	*572*
Long-term liabilities	(50,725)	(60,633)
including long-term financial liabilities	*(50,034)*	*(59,860)*
Short-term liabilities	(5,684)	(2,601)
including short-term financial liabilities	*(3,279)*	*(220)*
Total equity	**(10,399)**	**(3,275)**

The statement of profit or loss and other comprehensive income for 2016 and 2015:

	2016 RUB million	2015 RUB million
Revenue	5,023	5,549
Cost of sales	(5,498)	(6,218)
including depreciation, depletion and amortization	*(2,799)*	*(2,857)*
Other operating expenses, net	(4,136)	(3,268)
Operating loss	**(4,611)**	**(3,937)**
Finance income	490	352
Finance expense	(4,315)	(4,081)
Loss before income tax	**(8,436)**	**(7,666)**
Income tax expense	(43)	(189)
Loss for the period	**(8,479)**	**(7,855)**
The Group’s share in loss for the period	**(4,239)**	**(3,928)**
Unrecognized share in loss for the period	4,239	1,370
Share in loss of associates and joint ventures	**–**	**(2,558)**
Unrecognized share in loss for the period	(4,239)	(1,370)
Foreign currency translation reserve for the period	677	(268)
Total unrecognized share in loss for the period	**(5,200)**	**(1,638)**

10. Investments in associates and joint ventures (continued)

GEA Holdings Limited Group (continued)

As at 31 December 2016 and 2015, investments in associates and joint ventures comprised the following:

	31 December 2016 RUB million	31 December 2015 RUB million
Carrying amount at the beginning of the period	**–**	**2,361**
Loss for the period	–	(2,558)
Foreign currency translation reserve	–	197
Carrying amount at the end of the period	**–**	**–**

11. Revenue

Revenue from external customers broken down by geographical segments is presented based on the location of customers.

The Group operates in three principal geographical areas: Europe, the Commonwealth of Independent States (the "CIS") and the Russian Federation. The Group's non-current assets are located primarily in the Russian Federation.

The information on revenue is presented in the table below:

	Europe and other export		CIS (other than Russian Federation)		Russian Federation		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million
Revenue from external customers								
Crude oil sales	33,950	33,336	6,812	4,312	59,110	61,023	99,872	98,671
Petroleum product sales	199	241	1,457	3,231	–	30	1,656	3,502
Gas sales	–	–	–	–	2,929	2,174	2,929	2,174
Other sales	–	–	–	–	546	443	546	443
Total revenue	**34,149**	**33,577**	**8,269**	**7,543**	**62,585**	**63,670**	**105,003**	**104,790**

Revenue includes revenue from three customers (revenue from each customer exceeds 10% of the total revenue), net of export duty.

		Geographical location	2016 RUB million	2015 RUB million
Major customer 1	Crude oil sales	Europe and other export	27,806	31,458
Major customer 2	Crude oil sales	Russian Federation	18,332	23,406
Major customer 3	Crude oil sales	Russian Federation	10,820	12,511
Total revenue from sales to major customers			**56,958**	**67,375**

12. Cost of sales

	2016 RUB million	2015 RUB million
Mineral extraction tax	34,742	42,701
Depreciation, depletion and amortization	10,428	10,581
Payroll and related taxes	6,692	7,311
Utilities	5,068	5,372
Cost of crude oil and petroleum products sold	4,072	1,695
Production services	2,908	2,037
Raw materials and supplies used in production	2,367	2,136
Equipment repair, operation and maintenance	2,125	1,657
Transportation expenses	999	1,036
Processing fees	183	385
Other expenses	4,844	4,326
Total cost of sales	**74,428**	**79,237**

13. Selling, general and administrative expenses

Selling expenses comprise:

	2016 RUB million	2015 RUB million
Pipeline tariffs and transportation expenses	9,107	9,406
Excise	208	235
Other selling expenses	28	22
Total selling expenses	**9,343**	**9,663**

General and administrative expenses comprise the following:

	2016 RUB million	2015 RUB million
Payroll and related taxes	2,518	1,599
Charge/(Reversal) of bad debt allowance	586	(36)
Office rent	401	414
Entertainment and business travel	317	324
Allowance for inventory obsolescence	297	130
Consulting services	129	73
Repair and maintenance	107	209
Taxes other than income tax, including fines and penalties	99	104
Bank services	80	1,012
Operating leases	43	36
Insurance	5	19
Other expenses	563	239
Total general and administrative expenses	**5,145**	**4,123**

14. Finance income and expense

Finance income comprises the following:

	2016 RUB million	2015 RUB million
Interest income on loans	4,428	6,754
Other finance income (Notes 19, 24)	492	14,347
Total finance income	**4,920**	**21,101**

Finance expense comprises the following:

	2016 RUB million	2015 RUB million
Interest expense on loans and borrowings	10,968	22,134
Accretion expense (Note 25)	460	427
Other finance expense (Notes 19, 24)	274	–
Total finance expense	**11,702**	**22,561**

15. Other operating income and expenses

Other operating income and expenses comprise the following:

	2016 RUB million	2015 RUB million
Charity and other gratuitous expenses	793	304
Loss on disposal of property, plant and equipment	407	59
Loss on disposal of inventories	251	70
Impairment or property, plant and equipment (Note 16)	150	566
Public service advertising	119	128
Impairment of financial investments	37	35
Dissolution of subsidiaries	(675)	–
Income and expenses from services rendered or received	(93)	20
Operating leases	(75)	(78)
Other expenses	30	279
Other income	(313)	(266)
Total other operating expenses, net	**631**	**1,117**

16. Property, plant and equipment

	Oil and gas properties	Buildings	Machinery and equipment	Transpor-tation	Construction in progress	Total
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Cost						
As at 1 January 2015	**154,393**	**4,656**	**1,767**	**2,200**	**1,880**	**164,896**
Additions	11,497	–	–	57	925	12,479
Acquisition of subsidiaries	–	4	–	–	–	4
Decommissioning liability	1,558	–	–	–	–	1,558
Disposals	(1,465)	(186)	(50)	(746)	(60)	(2,507)
Transfer from construction in progress	253	279	152	223	(907)	–
Intragroup reclassifications	368	127	57	(189)	(363)	–
Foreign currency translation	4,172	–	1	33	–	4,206
As at 31 December 2015	**170,776**	**4,880**	**1,927**	**1,578**	**1,475**	**180,636**
Additions	16,400	–	–	10	668	17,078
Decommissioning liability	3,995	–	–	–	–	3,995
Disposals	(1,304)	(144)	(133)	(180)	(31)	(1,792)
Disposal of subsidiaries	(7,281)	–	–	–	–	(7,281)
Transfer from construction in progress	329	19	219	140	(707)	–
Intragroup reclassifications	376	122	(99)	(399)	–	–
Foreign currency translation	(2,757)	(81)	(1)	(19)	–	(2,858)
As at 31 December 2016	**180,534**	**4,796**	**1,913**	**1,130**	**1,405**	**189,778**
Depreciation and impairment losses						
As at 1 January 2015	**59,541**	**2,906**	**1,458**	**1,356**	**29**	**65,290**
Depreciation	9,864	236	155	326	–	10,581
Disposals	(511)	(24)	(38)	(355)	–	(928)
Impairment	542	13	–	–	11	566
Intragroup reclassifications	1,332	(979)	(149)	(204)	–	–
Foreign currency translation	61	–	1	11		73
As at 31 December 2015	**70,829**	**2,152**	**1,427**	**1,134**	**40**	**75,582**
Depreciation	9,580	238	174	436	–	10,428
Disposals	(697)	(30)	(118)	(178)	–	(1,023)
Impairment	32	110	4	–	4	150
Disposal of subsidiaries	(7,281)	–	–	–	–	(7,281)
Intragroup reclassifications	368	30	(81)	(317)	–	–
Foreign currency translation	(132)	–	(2)	(9)	–	(143)
As at 31 December 2016	**72,699**	**2,500**	**1,404**	**1,066**	**44**	**77,713**
Net book value						
As at 1 January 2015	**94,852**	**1,750**	**309**	**844**	**1,851**	**99,606**
As at 31 December 2015	**99,947**	**2,728**	**500**	**444**	**1,435**	**105,054**
As at 31 December 2016	**107,835**	**2,296**	**509**	**64**	**1,361**	**112,065**

16. Property, plant and equipment (continued)

The Group's non-current assets are located primarily in the Russian Federation, except for assets located in the Republic of Azerbaijan in accordance with the Group's participation in PSA (Note 10).

As at 31 December 2016 and 2015, the Group has no significant pledges of property, plant and equipment.

Impairment losses

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. Based on the assessment, the Group recorded an allowance in the amount of RUB 150 million and RUB 566 million in 2016 and 2015, respectively.

Given the specifics of the Group's activities, in general, the information on assets fair value is difficult to obtain, unless there are negotiations with potential buyers. As a result, recoverable amount used for the purposes of assessment of impairment accrued is determined based on discounted cash flow model.

17. Goodwill

	RUB million
As at 1 January 2015	**13,726**
Foreign currency translation	4
As at 31 December 2015	**13,730**
Disposal of subsidiaries	(183)
Foreign currency translation	(3)
As at 31 December 2016	**13,544**

Goodwill impairment test

The Group conducts its regular goodwill impairment test. Based on the assessment as at 31 December 2016 and 2015 no impairment of goodwill was identified.

For goodwill impairment test purposes the Group uses the discounted cash flow model. The main assumptions used are represented by estimates made by the Company's management with regard to the future development trends in oil and gas sector, and are based on the external and internal data sources. Future cash flows are based on the reports on oil and gas reserves prepared by Miller and Lents, Ltd within the range of 20 years.

17. Goodwill (continued)

Goodwill impairment test (continued)

The Company uses the following assumptions, sensitivity to which may significantly affect the valuation results:

- Discount rate: determines the current estimates of time value of money and risks. It is equal to weighted average cost of capital in Russian rubles (WACC) for the Russian peer companies (14.6%).
- Forecast oil price – price basis for Brent oil is in the range of USD 53-64 per barrel which is adjusted with regard to the difference between Brent and Urals oil prices, transportation expenses and changes in mineral extraction tax (MET).
- Sales structure by markets (export, CIS, domestic market) remains the same during the valuation period.
- Difference in the netback (net price) existing in the markets (export, CIS, domestic market) remains unchanged.

Changes in discount rate ranging from -1% to +1% did not identify additional evidence of impairment.

Change in forecast oil price	**Effect on profit before tax 2016**	**Effect on profit before tax 2015**
	RUB million	**RUB million**
-10	(5,150)	(16,470)

The carrying amount of goodwill is allocated to each of the cash-generating units as follows:

		31 December 2016	**31 December 2015**
		RUB million	**RUB million**
OJSC Saratovneftegaz	Exploration and production	9,046	9,046
OJSC MPK Aganneftegazgeologiya	Exploration and production	3,161	3,161
OJSC Varyeganneft	Exploration and production	624	624
OJSC Ulyanovskneft	Exploration and production	228	228
OJSC NAK Aki-Otyr	Exploration and production	95	278
Other		390	393
		13,544	**13,730**

18. Exploration and evaluation assets

Starting from 2011, the Group has been participating in projects under exploration and evaluation stage in the Republic of Azerbaijan and the Islamic Republic of Mauritania. These purchases were included in "Exploration and evaluation assets". As at the reporting date, allowance for impairment of exploration and evaluation assets amounts to RUB 6,846 million.

Management of the Group considers plans to withdraw from projects in the Islamic Republic of Mauritania and the Republic of Azerbaijan (Kura Valley Development Company).

19. Other long-term and short-term financial assets

	Currency	31 December 2016	31 December 2015
		RUB million	RUB million
Long-term loans issued to related parties	USD	50,015	59,344
Long-term loans issued to related parties	RUB	203	199
Long-term loans issued to other companies	RUB	2,293	2,207
Allowances for impairment of long-term loans issued		(2,293)	(2,207)
		50,218	**59,543**
Short-term loans issued to related parties	USD	3,098	–
Short-term loans issued to other companies	BYR	248	–
		3,346	**–**

During the reporting period the Group did not perform significant operations on loans issued. Loans issued and repaid are recorded within investing activities in the consolidated statement of cash flows and within other long-term and short-term financial assets in the consolidated statement of financial position. The loans issued are recognized in these consolidated financial statements at amortized cost; finance expense incurred due to the use of the effective interest method was recorded within within "Other finance expense" in the amount of RUB 274 million following the substantial modification of the initial conditions of the loan issued to the related party of GEA group (Note 14).

The Parent records loans issued to related parties of GEA group companies under the equity method as long-term financial assets in these consolidated financial statements (Note 10). As at 31 December 2016 and 2015, the loans issued (including accrued interest) were respectively USD 707 million and USD 655 million (RUB 42,901 million and RUB 47,724 million at the exchange rate as at the respective reporting date).

As at 31 December 2016 and 2015, outstanding balances related to long-term and short-term financial investments (including interest) comprise the outstanding balances of loans issued to related parties by GEA group companies in the amount of USD 81 million and USD 79 million (RUB 4,940 million and RUB 5,770 million).

As at 31 December 2016 and 2015, RUB-denominated loans to Claymon Enterprises Limited were fully covered by allowances in the amount of RUB 2,279 million and RUB 2,195 million, respectively.

In 2015, the Company issued new foreign currency-denominated loans to the companies with significant influence over the Parent in the total amount of RUB 37,211 million, or USD 737 million. The loans issued were recorded within investing activities in the consolidated statement of cash flows. These loans were initially recognized in the consolidated financial statements at fair value; finance income incurred due to the use of the effective interest method was recorded within "Other finance income" in the amount of RUB 1,875 million (Note 14). In Q4 2015, companies with significant influence over the Parent repaid these loans and the loans issued in 2013-2014, totaling RUB 61,192 million, including accrued interest. The effect of settlement of these loans recorded at amortized cost was recognized within "Other finance income" in the amount of RUB 2,012 million (Note 14). As at 31 December 2016 and 2015, the outstanding balance due from related companies amounts to RUB 203 million and RUB 199 million, respectively, including interest.

19. Other long-term and short-term financial assets (continued)

Loans issued which were not recognized in the consolidated financial statements at the date of the Group's transition to IFRS were repaid in 2015. The repayment, including accrued interest, amounted to RUB 28,025 million and was recognized within "Other transactions with shareholders" in the consolidated statement of changes in equity.

Loans issued and repaid and interest paid are recorded as investing activities in the consolidated statement of cash flows and as other long-term and short-term financial assets in the consolidated statement of financial position.

20. Inventories

Inventories comprise:

	31 December 2016	31 December 2015
	RUB million	**RUB million**
Crude oil	3,776	3,449
Raw materials and components	3,555	2,829
Petroleum products	132	207
Allowance for inventory obsolescence	(666)	(435)
Total inventories	**6,797**	**6,050**

21. Trade and other receivables

Trade and other receivables comprise:

	31 December 2016	31 December 2015
	RUB million	**RUB million**
Trade receivables	4,586	2,745
Prepayments	1,051	1,621
Other receivables	1,296	1,094
Allowance for bad debt and impairment	(911)	(378)
Total trade and other receivables	**6,022**	**5,082**

Movements in bad debt allowance for trade and other receivables are as follows:

	31 December 2016	31 December 2015
	RUB million	**RUB million**
As at 1 January	**(378)**	**(368)**
(Charge)/Reversal	(581)	36
Allowance used	9	39
Foreign currency translation	39	(85)
As at 31 December	**(911)**	**(378)**

22. Cash and cash equivalents

Cash and cash equivalents comprise:

	31 December 2016 RUB million	31 December 2015 RUB million
Deposits and other cash equivalents	2,438	476
Foreign currency-denominated cash at bank and on hand	569	972
RUB-denominated cash at bank and on hand	61	495
Total cash and cash equivalents	**3,068**	**1,943**

As at 31 December 2016, deposits mainly include foreign-currency denominated deposits in the amount of USD 22 million (RUB 1,346 million at the exchange rate as at the reporting date) with an interest rate of 1.5% p.a. maturing within 11 days, RUB-denominated deposits in the amount of RUB 700 million with an interest rate of 9.3% p.a. maturing within 10 days and RUB-denominated deposits in the amount of RUB 350 million with an interest rate of 9.45% p.a. maturing within 11 days.

As at 31 December 2015, deposits represent a deposit in the amount of RUB 475 million with an interest rate of 10.8% p.a. maturing within 12 days.

23. Share capital

Initially, the Parent issued 100,000 common shares at par value of RUB 1,000 each. All shares were fully paid at their issue.

In the reporting period, the Parent performed a two-staged issue of additional common and cumulative preference shares. In Q1 2016, the shareholders' meeting of the Parent decided to increase share capital to RUB 180 million by issuing additional common and cumulative preference shares. The additional share issues were registered by the Bank of Russia in March 2016 (hereinafter, the "first issue"). In June 2016, an additional issue of 47,059 registered uncertified common shares with a nominal value of RUB 1,000 each and 33,333 registered uncertified cumulative preference shares with a nominal value of RUB 1,000 each was placed by the Parent via private subscription.

The issued shares were paid by offsetting promissory notes issued by the Parent to Belirian Holdings Limited which became the shareholder of the Company holding the interest of 32% in the common shares of the Parent. The amount of transaction totaled RUB 54,313 million or USD 846 million. Promissory notes to be offset included a promissory note of USD 300 million issued by the Company in December 2015 (RUB 21,236 million at the exchange rate as at the date of issuance) and recognized in the consolidated financial statements as at 31 December 2015 at amortized cost using the market discount rate of 7.5%. The unwinding of discount on this promissory note was recorded as share premium of RUB 4,684 million or USD 75 million at the exchange rate as at the date of shares issue.

In June 2016, the shareholders' meeting of the Parent decided to increase share capital to RUB 196 million by issuing 1 common and 15,683 cumulative preference shares at par value of RUB 1,000 each. The additional share issue was registered by the Bank of Russia in August 2016 (hereinafter, the "second issue"). Terms of issue and payment of the second additional issue of shares were the same as for the first issue. The amount of transaction (the second issue) totaled RUB 10,755 million as at the date of placement or USD 166 million.

23. Share capital (continued)

The difference between the issue cost of common and cumulative preference shares placed via private subscription and their nominal value was recognized as share premium less previously recognized discount on one of the promissory notes. As at the reporting date such difference amounted to RUB 60,289 million.

In October 2016, the Company issued additional common and cumulative preference shares placed via conversion of shares subject to split. Split ratio was 2,000. As a result of this issue, the number of the Company's shares increased, whereas their nominal value reduced from RUB 1,000 to RUB 0.5 per share. The amount of share capital remained the same. As a result, the Company placed 294,120,000 common shares and 98,032,000 cumulative preference shares with a nominal value RUB 0.5 each, which totaled RUB 147 million and RUB 49 million, respectively. The Group calculated its net earning per share (basic and diluted) for the reporting period and for the comparable 12-months period of 2015 based on this new number of outstanding shares.

As at the reporting date, the Company may place 105,880,000 more common shares and 101,968,000 more cumulative preference shares with the same nominal value of RUB 0.5 each.

On 25 November 2016, shareholders of the Parent made a public placement of 58,822,000 common shares of the Company (20% of the total number of common shares and 15% of the Company's share capital) at the offering price of RUB 550 per share or RUB 32,352 million at Moscow Exchange.

Following changes occurred during the reporting period, the authorized body registered all amendments to the Company's Charter mentioned above. Besides, the Group determined rights of holders of common and cumulative preference shares, including procedure for dividend calculation and distribution among holders of cumulative preference shares.

No dividends on shares were distributed or paid by the Parent in the reporting period.

For the year ended 31 December 2016, dividends on cumulative preference shares were preliminary estimated as RUB 2,426 million at the exchange rate as at the reporting date or USD 40 million. Decision of dividends distribution should be made by the general meeting of the shareholders. Preliminary amount of dividends is not included in the Group's liabilities in these consolidated financial statements.

Pursuant to the Russian legislation, basis for the dividend distribution is net profit calculated in accordance with the Russian Accounting Standards ("RAS"). These amounts differ from those calculated in accordance with IFRS in the consolidated financial statements. As at 31 December 2016, RAS retained earning of the Parent amounted to RUB 2,809 million (31 December 2015: accumulated loss of RUB 11,310 million).

Earnings per share

Basic earnings per share are calculated by dividing the profit for the year attributable to common equity holders of the Parent, as adjusted, by the weighted average number of common shares outstanding during the year. The Company made preliminary estimates of potential amount of dividends distributable among holders of cumulative preference shares, for which income (loss) attributable to shareholders of the Parent was adjusted. As at the date of the consolidated financial statements, the general meeting of shareholders did not make a decision on the dividend distribution, when the decision will be actually made, the respective amounts might be different.

23. Share capital (continued)

Earnings per share (continued)

During the reporting period, the average weighted number of outstanding common shares was calculated based on changes in the share capital, which occurred due to two additional issues and due to an issue related to the split of outstanding shares. The Group did not place securities, which may have a potential diluting effect, therefore basic and diluted earnings (loss) per share are the same.

		2016	2015
Profit/(Loss) attributable to Shareholders of the Parent	RUB million	14,945	(27,650)
Dividends on cumulative preference shares[4]	RUB million	(2,426)	–
Profit/(Loss) attributable to shareholders of the Parent, as adjusted	RUB million	**12,519**	**(27,650)**
Weighted average number of common shares outstanding	million	249	200[5]
Effect of dilution		–	–
Basic and diluted earnings/(loss) per share	RUB per share	50	(138)

24. Long-term and short-term loans and borrowings

Loans and borrowings comprise the following:

	Currency	Weighted average interest rate 31 December 2016	31 December 2016
		%	RUB million
Long-term loans and borrowings			
Bank loans	USD	5.99%	76,628
Borrowings	USD	8.55%	7,839
Borrowings	RUB	6.00%	509
Total long-term loans and borrowings			**84,976**
Short-term loans and borrowings			
Bank loans	USD	5.99%	113
Borrowings	RUB	7.00%	5
Total short-term loans and borrowings			**118**

4 Dividends on cumulative preference shares for the reporting period are preliminary as the general meeting of shareholders did not make a dividend payment decision as at the date of the consolidated financial statements.

5 Weighted average number of common shares outstanding during 2015 was adjusted using the split ratio in order to ensure the comparability. The share split took place in 2016.

24. Long-term and short-term loans and borrowings (continued)

	Currency	Weighted average interest rate 31 December 2015	31 December 2015
		%	RUB million
Long-term loans and borrowings			
Bank loans	USD	8.69%	143,465
Promissory notes issued	USD	6.93%	25,746
Borrowings	USD	7.12%	8,827
Borrowings	RUB	5.99%	593
			178,631
Current portion of long-term debt			(2,915)
Total long-term loans and borrowings			**175,716**
Short-term loans and borrowings			
Bank loans	USD	8.69%	298
Borrowings	RUB	7.00%	8
Current portion of long-term debt			2,915
Total short-term loans and borrowings			**3,221**

In May 2015, as a result of restructuring several loan facilities in one, PJSC VTB Bank issued a loan of USD 2,302 million (RUB 115,048 million at the exchange rate as at the date of receipt) with an original maturity in March 2023 and fixed interest rate of 8.3%. In December 2015, upon mutual agreement of the parties, the Group made a partial early repayment of principal amounting to USD 300 million (RUB 21,240 million at the exchange rate as at date of payment).

The parties several times revised a loan agreement with PJSC VTB Bank. The latest revision took place in December 2016 and included an addenda regulating debt servicing. According to the addenda, the principal maturity was extended until March 2026; repayment schedule and interest rate were also amended. Due to specifics of conditions subsequent stipulated by the addendum to the loan agreement, that should be fulfilled prior to 22 March 2017, the Company does not recognize this modification as at the reporting date. Previous amendment to the loan agreement with PJSC VTB Bank, which became effective in July 2016 and included transition from fixed to the floating interest rate, was recognized in these consolidate financial statements as a significant modification of "Other finance income" amounting to USD 7 million or RUB 461 million at the exchange rate as at the modification date (Note 14).

In Q1 2016, the Company made scheduled principal payments of USD 8.5 million or RUB 585 million under the loan issued by PJSC VTB Bank. In April 2016, upon agreement with PJSC VTB Bank, the Company made a partial early repayment of principal amounting to USD 700 million (RUB 45,613 million at the exchange rate as at the date of payment). Outstanding payables to PJSC VTB Bank amounts to RUB 76,741 million or USD 1,265 million at the exchange rate as at the date of the consolidated financial statements, including interest payable of RUB 113 million (USD 2 million at the exchange rate as at the date of the consolidated financial statements). The Company repays interest on a quarterly basis, in accordance with the schedule and an interest rate as at the date of payment.

24. Long-term and short-term loans and borrowings (continued)

The loan from PJSC VTB Bank was secured by pledge of the common shares of the Parent and the equity interests that the Parent holds in certain subsidiaries. At the same time, certain subsidiaries of the Group and other related parties are joint guarantors to the creditor with regard to the Parent's liabilities.

The loan agreement contains a number of financial and operational covenants that the Company shall comply with during the term of the agreement. Non-fulfillment of some of the agreed covenants makes the creditor entitled to claim early repayment of principal amount and accrued interest, including interest penalties.

The Company made unscheduled payment to settle the loan from PJSC VTB Bank with the funds received from the related party under the promissory note agreement in the amount of USD 700 million, or RUB 46,673 million at the exchange rate at the date of receipt of the borrowed funds. The Parent issued promissory notes denominated in US dollars, bearing an interest rate of 4.04% p.a. and maturing on demand but not later than December 2025. The amount payable under the promissory note is subordinate to the loan from PJSC VTB Bank. The Company adopted an approved two-step plan of converting these promissory notes into shares. The first stage of conversion was completed in June 2016 and the second stage was carried out in August 2016 (Note 23).

Offsetting of the promissory note issued by the Company in December 2015 in the amount of USD 300 million (RUB 21,236 million at the exchange rate effective at the date of issue) carried at amortized cost of USD 212.5 million (RUB 13,640 million at the exchange rate effective at the offset date) was recorded as share premium adjusted for the recognized effect of discounting in the amount of RUB 4,684 million or USD 75 million, net of deferred tax. The remaining portion of promissory notes issued by the Company in April 2016 to be offset against claims of Belirian Holdings Limited in payment of shares issued in June 2016 (Note 23) was recognized in these consolidated financial statements at carrying amount of USD 536.5 million, or RUB 34,430 million plus accrued interest in the amount of USD 3.8 million, or RUB 247 million at the exchange rate effective at the offset date.

The second additional issue made in August 2016 was paid under similar conditions by offsetting counter claims on promissory notes of Belirian Holdings Limited in the amount of RUB 10,755 million or USD 166 million at the rate effective as at the offsetting date, including interest outstanding in the amount of RUB 136 million or USD 2 million at the rate effective as at the offsetting date (Note 23).

In January 2016, Russneft Cyprus Limited, a subsidiary, placed an additional issue of B class preference shares (Note 7) to a related party in the amount of USD 160 million or RUB 11,636 million at the date of issue. Payment for shares was performed by offsetting counter claims on promissory note of Russneft Cyprus Limited previously issued to GCM Global Energy PLC and recorded in these consolidated financial statements at amortized cost using the effective interest rate. These transactions are recorded as equity transactions with subsidiaries in line "Conversion of debt into equity of a subsidiary" of the consolidated statement of changes in equity in the amount of RUB 10,740 million at the exchange rate effective as at the offset date, including the effect of discounting in the amount of RUB 896 million, or USD 12 million.

The outstanding amount payable under the loan in foreign currency received from the related party by a GEA group company is recorded at fair value using the market discount rate of 8.5% p.a. The outstanding amount payable is USD 68 million, or RUB 4,153 million.

Interest accrued is primarily repaid simultaneously with the principal amount, unless otherwise specified in loan agreements, and presented as long-term loans and borrowings.

25. Decommissioning liability

	2016 RUB million	2015 RUB million
As at 1 January	**4,973**	**2,967**
Acquisitions	180	180
Disposals	(193)	(167)
Change in estimation	4,008	1,545
Accretion expense	460	427
Foreign currency translation	(56)	21
As at 31 December	**9,372**	**4,973**

The Group makes provision for the future cost of decommissioning oil production facilities on a discounted basis as the facilities are put into operation or sites are damaged. The Group estimated the provision subject to existing oil extraction technologies and current estimates of decommissioning costs (adjusted for inflation projections) and discounted the provision at the rate of 8.61% (2015: 9.3%).

The decommissioning liability represents the present value of decommissioning costs relating to oil and gas properties which are expected to be incurred up to 2090 depending on the recovery period of proved reserves for each group of oil and gas fields. Management makes assumptions based on the current economic environment and believes that they are a reasonable basis upon which the future liability is estimated. These estimates are reviewed regularly to take into account any material changes in the assumptions. Actual decommissioning costs will ultimately depend upon future market prices for the necessary decommissioning work which will reflect specific market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This, in its turn, will depend on future oil and gas prices, which are inherently uncertain.

26. Trade and other payables and accrued liabilities

Trade and other payables comprise the following:

	31 December 2016 RUB million	31 December 2015 RUB million
Trade payables	13,580	10,107
Advances received	29,106	29,385
Other payables and accrued liabilities	3,071	1,699
Total trade and other payables and accrued liabilities	**45,757**	**41,191**

Taxes and duties payable (excluding income tax) comprise the following:

	31 December 2016 RUB million	31 December 2015 RUB million
Value added tax	1,373	2,016
Mineral extraction tax	4,089	2,379
Property tax	304	300
Other taxes and duties (excluding income tax)	369	305
Total taxes and duties payable (excluding income tax)	**6,135**	**5,000**

27. Income tax

The major components of income tax benefit and income tax expense are:

	2016 RUB million	2015 RUB million
Current income tax		
Current income tax expense	1,355	1,329
Current income tax relating to previous years	274	51
Deferred income tax		
Relating to origination and reversal of temporary differences	3,615	(1,615)
Change in deferred tax assets/liabilities relating to previous periods	128	210
Income tax expense/(benefit) reported in the consolidated statement of profit or loss and other comprehensive income	**5,372**	**(25)**

Reconciliation between income tax benefit / tax expense and accounting profit multiplied by the Group's country of origin official tax rate is as follows:

	2016 RUB million	2015 RUB million
Accounting profit before tax from continuous operations	**18,809**	**(25,985)**
Income tax at applicable tax rate (20%)	**3,762**	**(5,197)**
Tax effect of non-deductible expense and non-taxable income	716	4,256
Tax effect of rates other than 20%	195	182
Change in unrecognized deferred tax assets	276	394
Change in deferred tax assets/liabilities relating to previous periods	128	210
Current income tax relating to previous years	274	51
Other	21	79
Income tax expense/(benefit) reported in the consolidated statement of profit or loss and other comprehensive income	**5,372**	**(25)**

Generally, the subsidiaries of the Group incorporated in the Russian Federation used a 20% tax rate in 2016 and 2015; the separate subsidiaries engaged in exploration activities applied a reduced income tax rate in accordance with regional tax legislation. The subsidiaries incorporated outside the Russian Federation applied rates and exemptions stipulated by local legislation.

27. Income tax (continued)

Deferred income tax

Deferred tax assets and liabilities as at 31 December 2016 by the lines of the consolidated statement of financial position as well as their movements in 2016 are presented below:

	Consolidated statement of financial position	**Other movements in equity**[6]	**Consolidated statement of profit or loss and other comprehen-sive income**	**Disposal of subsidiaries**	**Consolidated statement of financial position**
	31 December 2015	**2016**	**2016**	**2016**	**31 December 2016**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Deferred tax liabilities					
Oil and gas properties	(6,945)	–	(1,007)	–	(7,952)
Inventories	(275)	–	(217)	–	(492)
Loans and borrowings payable	(1,373)	1,313	60	–	–
Other	(365)	–	185	–	(180)
Deferred tax assets					
Tax loss carry forward	23,781	–	(2,322)	(21)	21,438
Oil and gas properties	1,834	–	87	(1,531)	390
Inventories	23	–	76	–	99
Trade and other receivables	14	–	(4)	–	10
Other	1,345	–	(304)	–	1,041
Unrecognized deferred tax assets	(4,070)	–	(276)	1,531	(2,815)
Total deferred tax liabilities and assets	**13,969**	**1,313**	**(3,722)**	**(21)**	**11,539**
Deferred income tax expense	**–**	**–**	**3,722**	**21**	**–**
Reported in the consolidated statement of financial position as follows:					
Deferred tax assets	19,515	–	–	–	17,777
Deferred tax liabilities	(5,546)	–	–	–	(6,238)

[6] The previously recognized deferred tax on discounted financial liabilities also was taken other movements in equity upon conversion of debt into share capital (Note 24).

27. Income tax (continued)

Deferred income tax (continued)

Deferred tax assets and liabilities as at 31 December 2015 by the lines of the consolidated statement of financial position as well as their movements in 2015 are presented below:

	Consolidated statement of financial position	Other movements in equity[7]	Consolidated statement of profit or loss and other comprehen-sive income	Acquisition of subsidiaries	Consolidated statement of financial position
	31 December 2014	2015	2015	2015	31 December 2015
	RUB million	RUB million	RUB million	RUB million	RUB million
Deferred tax liabilities					
Oil and gas properties	(6,353)	–	(592)	–	(6,945)
Inventories	(277)	–	2	–	(275)
Loans and borrowings payable	(3,299)	4,765	(2,839)	–	(1,373)
Other	(480)	–	115	–	(365)
Deferred tax assets					
Tax loss carry forward	18,345	–	5,435	1	23,781
Oil and gas properties	2,044	–	(210)	–	1,834
Inventories	105	–	(82)	–	23
Trade and other receivables	24	–	(10)	–	14
Other	1,365	–	(20)	–	1,345
Unrecognized deferred tax assets	(3,676)	–	(394)	–	(4,070)
Total deferred tax liabilities and assets	**7,798**	**4,765**	**1,405**	**1**	**13,969**
Deferred income tax benefit	**–**	**–**	**(1,405)**	**–**	**–**
Reported in the consolidated statement of financial position as follows:					
Deferred tax assets	13,164	–	–	–	19,515
Deferred tax liabilities	(5,366)	–	–	–	(5,546)

Deferred tax liabilities in respect of the retained earnings of the subsidiaries are not recognized because the Group has the power to control future distributions among investors and has no intention to do so in the foreseeable future.

Pursuant to amendments to Russia’s tax legislation, in effect since 1 January 2017, there is no longer a time limit on offsetting current and prior period losses against taxable profit that could be previously offset only within 10 years after the date such losses were incurred. At the same time, the amount of tax losses that may be offset has been limited to no more than 50% of the amount of taxable profit for the period of 2017-2020. Management has revised its estimates and assumptions regarding the potential offset of the Group’s tax assets in light of the above amendments and based on its estimates of the probability of receiving sufficient taxable profit, including under certian business transactions.

[7] The previously recognized deferred tax on discounted forgiven financial liabilities in the amount of RUB 4,765 million also was taken to other movements in equity (Note 24).

28. Transactions with related parties

The Group's transactions with its subsidiaries that are related parties are excluded from the consolidated financial statements and are not disclosed in this Note. Transactions with joint ventures before consolidation adjustments are fully disclosed herein.

The nature of the related party relations for those related parties with whom the Group entered into significant transactions in 2016 and 2015 or had significant balances outstanding as at 31 December 2016 and 2015 are detailed below.

Transactions with related parties in 2016 and 2015:

2016	Sales	Other disposals	Purchases	Interest income	Interest expense	Other equity transactions
	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million
Entities/Individuals with significant influence over the Group	27,806[8]	–	75	–	2,702	10,740[9]
Associates and joint ventures	33	100	231	3,929	490	–
Other related parties	29,302	53	4,678	446	63	–
Total	**57,141**	**153**	**4,984**	**4,375**	**3,255**	**10,740**

2015	Sales	Other disposals	Purchases	Interest income	Interest expense	Other equity transactions
	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million
Entities/Individuals with significant influence over the Group	5,245[10]	–	–	2,674	261	77,880[11]
Associates and joint ventures	–	9	76	3,559	352	–
Other related parties	47,072	30	1,774	413	3,079	–
Total	**52,317**	**39**	**1,850**	**6,646**	**3,692**	**77,880**

As at 31 December 2016 and 2015, amounts due to and due from related parties are as follows:

31 December 2016	Receivables	Loans issued	Payables	Loans received	Guarantees issued	Guarantees issued to secure liabilities
	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million
Entities/Individuals with significant influence over the Group	772	–	26,351	–	–	–
Associates and joint ventures	196	47,841	298	4,934	–	–
Other related parties	2,965	5,475	4,084	–	59	3,177
Total	**3,933**	**53,316**	**30,733**	**4,934**	**59**	**3,177**

8 Excluding export duty.

9 Conversion of debt into a subsidiary's equity.

10 Excluding export duty.

11 The debt forgiven is recognized in the IFRS consolidated statement of changes in equity at amortized cost which is different from the amount under the debt forgiveness agreement (Note 24).

28. Transactions with related parties (continued)

31 December 2015	Receivables	Loans issued	Payables	Loans received	Guarantees issued
	RUB million	RUB million	RUB million	RUB million	RUB million
Entities/Individuals with significant influence over the Group	–	199	19,715	14,966	–
Associates and joint ventures	219	53,494	289	5,305	–
Other related parties	2,008	5,850	3,166	–	59
Total	**2,227**	**59,543**	**23,170**	**20,271**	**59**

Pricing policy

The Group determines prices for related party transactions within the range of market prices. In addition, the Group's management performs control envisaged by the regulation governing transactions between related parties.

Key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, either directly or indirectly, including directors (executive and other directors) of the Group. There were no significant transactions carried out during the reporting period with directors and key management personnel.

In 2016, key management personnel compensation expense, consisting of salaries and payroll taxes, totaled RUB 818 million (2015: RUB 1,332 million).

The Company implements a three-year (2014-2016) incentive program for the top management. Under this program, the managers involved subject to their continuous service in the Company are provided with phantom shares of the Company for each year of the program. The Group recognizes the phantom shares to be paid off in cash as a liability expensed to bonuses during the period of rendering services. In the reporting period, the Company did not repay the amounts due to top management for the second year of the ongoing three-year incentive program due to the implementation of an anti-crisis program. In 2015, the Company paid a total of RUB 64 million for the first year of the ongoing three-year incentive program.

29. Fair value measurement

All financial instruments are measured at fair value using a valuation model based on Level 3 non-market observable inputs that require additional evaluations and corrections. There have been no transfers between the levels of the fair value hierarchy during the reporting period.

Management believes that the fair value of the Group's cash, short-term financial assets, trade payables and short-term loans and borrowings is equal to their carrying amounts. The fair value of long-term loans and borrowings received by the Group, and loans issued is determined using a discounted cash flow model based on the discount rates that are equal to the market rates effective at the reporting date. As at 31 December 2016, management classified risk of default as remote.

Analysis of fair value sensitivity to changes in unobservable inputs did not identify any significant volatility of fair value measurements.

29. Fair value measurement (continued)

The accounting classification of each category of financial instruments, and their carrying and fair values, are as follows:

	31 December 2016		31 December 2015	
	Carrying value	Fair value	Carrying value	Fair value
	RUB million		RUB million	
Loans and receivables				
Loans issued	53,564	55,067	59,543	59,814
Trade and other receivables	4,539	4,539	3,402	3,402
Cash and cash equivalents	3,068	3,068	1,943	1,943
Financial liabilities measured at amortized cost				
Trade and other payables	14,767	14,767	10,419	10,419
Loans and borrowings	85,094	83,946	178,937	182,396

The sensitivity of fair value of long-term loans issued and loans and borrowings received to a fluctuation in the interest rate by 1% is disclosed below. This analysis has been based on the assumption that the change in foreign exchange rates had occurred at the reporting date and had been applied to the foreign currency balances, while all other variables, in particular payment schedules, remain constant.

	Change in the interest rate	Effect on profit before tax for the year ended 31 December 2016	Effect on profit before tax for the year ended 31 December 2015
		RUB million	RUB million
Long-term loans issued	+1%	(1,460)	(2,106)
Long-term loans issued	-1%	1,518	2,207
Long-term loans and borrowings received	+1%	2,691	7,634
Long-term loans and borrowings received	-1%	(2,846)	(8,180)

30. Contingencies, commitments and operating risks

Operating environment of the Group

The Group's principal activities are performed in the Russian Federation. Business operations in the Russian Federation involve risks that typically do not exist in other markets. Russian economy is characterized by significant vulnerability to the world price for crude oil, market downturns and economic slowdowns elsewhere in the world. Sanctions imposed against the Russian Federation have resulted in reduced capital availability, higher costs of capital and uncertainty regarding economic growth, thus giving rise to the risk of adverse effect on the Group's financial position, performance and business prospects. The existing trends can persist for indefinite period of time.

The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the financial position and performance of the Group. The future business environment may differ from the current management's assessment.

30. Contingencies, commitments and operating risks (continued)

Operating environment of the Group (continued)

The Company's management regularly monitors the potential risks, including the analysis of country risks. Should any risk occur, the Company will develop measures to minimize potential adverse effects on the Group. The extent of such effects cannot currently be determined.

The Group's management believes that the developed strategy allows to implement the Company's potential, which is defined by one of the highest level of reserve replacement in the industry, in the most effective way.

Taxation

Russian tax, currency and customs legislation is subject to varying interpretation and changes which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group's entities may be challenged by the relevant regional and federal authorities. The tax authorities can take a more assertive position in their interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. It is therefore possible that transactions and accounting methods that have not been challenged in the past may be challenged by the tax authorities. As such, 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. The fact that a year has been reviewed does not close that year, or any tax return applicable to that year, from further review during the three-year period.

For taxes where uncertainty exists, the Group has accrued tax liabilities based on management’s best estimate of the probable outflow of resources embodying economic benefits which will be required to settle these liabilities.

Russian transfer pricing legislation allows the Russian tax authority to apply transfer pricing adjustments and impose additional profits tax liabilities in respect of all "controlled" transactions if the transaction price differs from the market price.

The list of controlled transactions includes transactions performed with related parties and foreign trade transactions. The adopted Russian transfer pricing rules have considerably increased the compliance burden for the taxpayer compared to the transfer pricing rules which were in effect earlier. Pursuant to the new rules, the taxpayer shall justify the prices applied for such transactions. The new provisions apply for both foreign trade and domestic transactions. Transactions between related parties in the domestic market are deemed controlled if the proceeds (the amount of all transactions) between related parties in 2015 and 2016 exceeds RUB 1 billion for proper calendar period. In cases where the domestic transaction resulted in an accrual of additional income tax liabilities for one party, another party could correspondingly adjust its income tax liabilities.

30. Contingencies, commitments and operating risks (continued)

Taxation (continued)

In 2015 and 2016, the Company determined its tax liabilities arising from these controlled transactions using actual transaction prices or, in case where the transaction price deviated from the market price, using prices adjusted pursuant to the Russian Tax Code. Based on the comments of the Federal Tax Service, the Company improved and submitted for signing to the Federal Tax Service draft Pricing Agreement for the Company's controlled purchases of oil from the Group's subsidiaries that took place in 2014 (Note 33). As for other controlled transactions, there are control procedures to ensure consistency between the prices used in the controlled transaction prices and the level of market prices for the purposes of taxation, which are updated on an annual basis taking into account current legal requirements. The activities performed focus on minimizing tax risks.

Due to the uncertainty and absence of current practice of application of the current Russian transfer pricing legislation, the Russian tax authorities may challenge the level of prices applied by the Group under the controlled transactions and accrue additional tax liabilities unless the Group is able to prove the use of market prices with respect to the controlled transactions, and that there has been proper reporting to the Russian tax authorities, supported by appropriate available transfer pricing documentation. At the same time, the Company will be entitled to symmetrical adjustments with regard to the arrears provided that a party to a controlled transaction exercises the decision of the tax authority regarding accrual of additional tax liabilities. The Federal Tax Service of the Russian Federation did not make a decision of review of transactions between the related parties for 2012 and 2013 reporting periods, due to what the limitation period for review with regard to those periods expired. In accordance with the tax legislation, in 2015 certain companies of the Group and the Parent exercised a taxpayer's right to implement a symmetric adjustments on controlled transactions and filed adjusted income tax returns.

In 2014, new legislation governing taxation of controlled foreign companies was enacted. To ensure compliance with the new legislation and mitigate related tax risks, the Group's management developed a set of internal routine procedures.

Based on the results of the field tax audit for 2012-2013, the tax authorities issued claims against the Parent in the total amount of RUB 233 million, including penalties of RUB 5 million. Before the decision of the tax authorities entered into force, the Company filed an appeal to the Federal Tax Service of Russia. The decision of the tax authority became effective in July 2016. This amount is recognized in full in these consolidated financial statements.

Management believes that the Group has complied with all regulations, and paid and accrued all taxes that are applicable.

Compliance with license agreements

Licenses for subsoil use are issued by the Russian Federal Subsoil Use Agency. Management believes that under current legislation, the Group is entitled to renew the licenses for all available fields after expiry of the initially stated periods. During the reporting period, licenses continued to be transfered from the subsidiaries to the Parent. A major part of licenses were updated on a one-time basis to extend their term.

The authorized state agencies regularly review the Group's activity for compliance with the license agreements for subsoil use. Failure to meet the terms of the license agreements may result in penalty accruals and sanctions, including license suspension or revocation. Management takes appropriate measures to comply with the license agreements, including rectification of all shortcomings identified during reviews and instructions of the authorized state agencies within the established timeframes.

30. Contingencies, commitments and operating risks (continued)

Liabilities concerning environmental and safety matters

In recent years, the Russian environmental and safety legislation has been rapidly developing considering general requirements and international law enforcement practice in this field.

Management of the Group understands its responsibilities concerning environmental and safety matters and undertakes to comply with the requirements of federal, regional and industry regulations concerning environmental protection, rational use of mineral resources and safety, including international environmental and labor safety management standards. The Group implements the corporate policy concerning environmental protection and safety matters in accordance with the requirements of the Russian legislation and international standards related to environmental and safety issues. Management believes that, considering existing controls and current legislation, the Group is not imposed to significant risks and liabilities except for those that are recognized in these consolidated financial statements and relate to ordinary business operations.

Insurance

The Group does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents at the Group's property or relating to the Group's operations.

The Group applies the Insurance Policy, which describes the Company's key insurance principles and procedures. In accordance with the applied Insurance Policy, the Group insured its major oil and gas extraction facilities. The Group's subsidiaries insure especially hazardous facilities pursuant to Federal Law No. 225-FZ *On Compulsory Insurance of Civil Liability of the Owner of a Hazardous Object for Damages Caused by an Accident.* The Group also provides selective car insurance for vehicles. In addition, the Group purchases mandatory car liability insurance policies for all automobiles, special purpose equipment, trailers and other vehicles.

Retirement and post-retirement benefit obligations

The Group makes contributions to the Pension Fund of the Russian Federation. These payments are calculated by the employer as a percentage from gross salary expense and are expensed as accrued. The Group applies the Regulation on Non-state Pension Benefits for the Group's Employees.

The Group's subsidiaries entered into pension insurance agreements with NPF Elektroenergetiki. The subsidiaries make pension contributions for all employees eligible by age and length of service.

30. Contingencies, commitments and operating risks (continued)

Litigations

According to the results of the field tax review for 2010-2011, additional income tax, penalties and fines in the amount of RUB 248 million were assessed by the tax authorities in April 2014. Decision of the FTS Interregional Inspectorate for Major Taxpayers No. 1 became effective in December 2014. The abovementioned amount is settled and recognized in full in the 2014 consolidated financial statements. The Company litigated the Decision in the Arbitration Court of the City of Moscow. In April 2015, the Company's claim was satisfied in full. In October 2015, following the hearing of the tax authority's appeal, the Decision of the Arbitration Court of the City of Moscow was reversed. In February 2016, the Company's cassation appeal was dismissed. The Company appealed the Ruling of the cassation court at the Supreme Court of the Russian Federation. In June 2016, the Supreme Court of the Russian Federation determined to deny the hearing of the cassation appeal (hereinafter, the "Determination") by the Judicial Panel for Economic Disputes of the Supreme Court of the Russian Federation (hereinafter, the "Judicial Panel"). In July 2016, the Company filed an appeal to the Deputy Chairman of the Supreme Court of the Russian Federation on annulment of the Determination. The appeal was dismissed in September 2016. As at the date of the consolidated financial statements, the Company prepared an appeal to the Chairman of the Supreme Court to annul the Determination and conduct the hearing of the appeal at the Judicial Panel. The Company assesses the possibility of a positive opinion as low.

Based on the results of the field tax audit for 2012-2013, the tax authority made a decision to charge additional income tax in the amount of RUB 228 million and penalty in the amount of RUB 5 million. In June 2016, the Company filed a suit to the Arbitration Court of the Russian Federation against the above mentioned decision. In July 2016, in accordance with the decision based on the results of the field tax audit for 2012-2013, the Company recorded income tax in the amount of RUB 228 million and penalty in the amount of RUB 5 million for tax accounting purposes. Currently, the Company’s claim is considered by a court of the first instance. The Company assesses the possibility of a positive opinion as medium.

LLC Mobile Drilling Division has filed a claim against OJSC Varyeganneft, a subsidiry, to recover an amount of RUB 132 million payable under a construction agreement and a penalty of RUB 5 million. OJSC Varyeganneft has filed a counter claim. As at the date of the consolidated financial statements, the parties entered into a settlement agreement on agreed terms, according to which, the amount payable by the subsidiary was reduced to RUB 118 million (Note 33).

Management believes that there are no current claims outstanding which could have a material effect on the results of operations or financial position of the Group and which have not been accrued or disclosed in these consolidated financial statements.

Guarantees issued in favor of third parties

The Group's subsidiaries are joint guarantors to PJSC VTB Bank with regard to the Parent's liabilities under the loan agreement with the outstanding balance (including interest) of RUB 76,741 million at the exchange rate effective at the date of the consolidated financial statements (Note 24).

The Group companies and the Parent are joint guarantors to VTB Capital Trading Limited with regard to a prepayment received under an oil supply contract of Russneft (UK) Limited in the amount of RUB 3,248 million (USD 53.6 million) at the exchange rate as at the date of the consolidated financial statements.

30. Contingencies, commitments and operating risks (continued)

Guarantees issued in favor of third parties (continued)

In 2016, the Parent concluded a guarantee agreement with LLC VTB Capital Trading with regard to the liabilities of a related party under an oil supply contract in the total amount of RUB 3,177 million as at the date of the consolidated financial statements.

31. Financial risk management

The Group's principal financial instruments include bank loans and borrowings received, and accounts payable. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities, such as trade receivables and trade payables, loans issued and cash and cash equivalents, which arise directly from its operations. During the year the Group did not undertake trading in financial instruments.

The main risks that could adversely affect the Group's financial assets, liabilities and future cash flows are market risk (including foreign currency risk, interest rate risk, and commodity and service price risk), credit risk and liquidity risk. The Group applies the Risk Management Policy, which includes procedures (performed on a regular basis) to identify and measure risks inherent in the key activities and to assess the possible impact of the identified risks. Based on the annual risk assessment results, the Group's management can revise its approach to managing each type of risk. The Group's most significant financial risks are disclosed below.

Market risk

Market risk is the risk that the fair value of financial instruments or cash flows will fluctuate as a result of changes in market prices. The Group manages market risk through periodic estimation of potential losses that could arise from adverse changes in market conditions.

Commodity price risk

Commodity price risk is the risk of changes in prices for hydrocarbons and refining products and their potential influence on the Group's financial and performance indicators. Reduction of prices may result in decrease in net profit and cash flows. If the prices for hydrocarbons remain low during a lengthy period, it may result in reduction of capital spending on exploration, development of fields and subsequent reduction in hydrocarbon production and, thus, negatively affect the Group's ability to fulfill its contractual obligations. However, stable oil prices and their potential growth will enable the Group to successfully pursue its strategy aimed at increasing production output in the coming years.

The Group's management calculates budgets by scenario depending on projected oil prices, exchange rates and other indicators in order to assess a potential effect of the risk of changes in the price of main commodities on the Group's management reports. The Group enters into standard agreements on sale of oil and oil products with customers. As at 31 December 2016 and 2015, the Group did not utilize derivative instruments in relation to commodity price risk.

31. Financial risk management (continued)

Foreign currency risk

The Group is exposed to transaction foreign currency risks. Foreign currency risk exposure arises from sales, purchases and borrowing in currencies other than the respective functional currency. The Group is not engaged in any significant hedging activity to mitigate its foreign currency risk. The Group limits foreign currency risk by monitoring changes in exchange rates of the currencies in which its cash and loans and borrowings are denominated. Meanwhile, the Group is a party to contracts on export oil sales denominated in foreign currency.

As at 31 December 2016 and 2015, the carrying value of the Group's financial assets and liabilities denominated in the currency used by the Group's companies is as follows:

Financial assets	**31 December 2016**	**RUB**	**USD**	**EUR**	**Other currencies**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Trade and other receivables	4,539	3,176	1,056	–	307
Loans issued	53,564	203	53,113	–	248
Cash and cash equivalents	3,068	1,153	1,742	143	30

Financial liabilities	**31 December 2016**	**RUB**	**USD**	**EUR**	**Other currencies**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Loans and borrowings received	(85,094)	(514)	(84,580)	–	–
Trade and other payables	(14,767)	(12,174)	(2,591)	–	(2)

Financial assets	**31 December 2015**	**RUB**	**USD**	**EUR**	**Other currencies**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Trade and other receivables	3,402	2,313	868	–	221
Loans issued	59,543	199	59,344	–	–
Cash and cash equivalents	1,943	971	756	92	124

Financial liabilities	**31 December 2015**	**RUB**	**USD**	**EUR**	**Other currencies**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Loans and borrowings received	(178,937)	(601)	(178,336)	–	–
Trade and other payables	(10,419)	(9,369)	(1,041)	–	(9)

31. Financial risk management (continued)

Foreign currency risk (continued)

A 20.00% strengthening or weakening of RUB against USD as at 31 December 2016, and a 13.00% strengthening or 40.00% weakening as at 31 December 2015, respectively, with all other variables held constant, would have changed profit before tax by the amounts shown below. This analysis has been determined assuming that the change in foreign exchange rates had occurred at the reporting date and had been applied to the foreign currency balances to which the Group has significant exposure, and that all other variables, in particular interest rates, remain constant.

Relative strengthening/(weakening) of RUB against USD	**Effect on profit before tax for the year ended 31 December 2016**	**Effect on profit before tax for the year ended 31 December 2015**
	RUB million	**RUB million**
+20.00%	5,610	–
-20.00%	(5,610)	–
+13.00%	–	13,581
-40.00%	–	(41,788)

The Group's exposure to foreign currency risk for other currencies is not material.

Interest rate risk

Interest rate risk is the risk that the fair value and future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group assessed the interest rate risk as related to long-term financial liabilities with a floating interest rate.

In 2016, interest rates on foreign currency denominated loans tended to increase in general. The Group’s management assessed interest rate risks as significant, as the Parent’s borrowings are mostly represented by a foreign currency denominated loan with a flowing interest rate pegged to the USD 3M Libor. As at 31 December 2016, an increase in the Libor rate by 0.6% would decrease profit before tax by RUB 508 million, while a decrease in Libor by 0.08% would increase profit before tax by RUB 68 million.

As at 31 December 2016, the Group did not enter into any transactions, in particular, any interest rate swaps, aimed to reduce its interest rate risk exposure.

The effect of interest rate risk arising from long-term loans and borrowings on the 2015 consolidated financial statements is insignificant, as the Group did not have any financial instruments bearing floating interest rates.

The Group controls this risk by ongoing monitoring market expectations in respect of interest rates and adjusting budget as well as expected cash flow to allocate sufficient financial resources for interest repayment.

Credit risk

Credit risk is the risk that a customer or counterparty will fail to meet their obligation under financial assets causing financial loss to the Group. The Group's credit risk principally arises from cash and cash equivalents, and from financial stability of its customers and loans provided to third parties.

The Group has not used any financial instruments as a tool for credit risk management in this period.

31. Financial risk management (continued)

Credit risk (continued)

The Group maintains accounts only with high quality banks and financial institutions and believes that it therefore does not have a material credit risk in relation to its cash or cash equivalents.

The Group trades only with recognized, creditworthy third parties. The individual risk of a counterparty is managed through the assessment of its credit worthiness.

It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. The Group has a policy to negotiate advance payment terms where excessive concentration of credit risk exists. In addition, trade receivable balances are monitored on an ongoing basis to ensure that the Group's exposure to bad debts is not significant. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the allowance already recorded. The details of allowance for bad debts are disclosed in Notes 19 and 21. The information on the major types of financial assets and their maturity is presented below:

Financial assets	**31 December 2016**	**Within one year**	**1 to 2 years**	**2 to 4 years**	**Over 4 years**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Loans issued	53,564	3,346	1,606	48,421	191
Trade and other receivables	4,539	4,527	–	12	–

Financial assets	**31 December 2015**	**Within one year**	**1 to 2 years**	**2 to 4 years**	**Over 4 years**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Loans issued	59,543	–	3,697	49,996	5,850
Trade receivables	3,402	3,402	–	–	–

As at 31 December 2016, the Group believes that its maximum exposure to credit risk is the carrying value of its financial assets recognized in the consolidated statement of financial position.

No collateral is held as security for any financial assets.

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 operating cash flow is subject to fluctuations resulting from high volatility of oil prices as well as changes in exchange rates and the amounts of taxes and duties paid. The above can affect the amount of the Group’s cash flow and, thus, its liquidity. In order to manage liquidity risk, the Group monitors and projects liquidity requirements on a regular basis. The Group's management ensures that sufficient funds are available to meet any commitments as they arise, prepares detailed budgets and plan-to-fact analyses on an annual, quarterly and monthly basis. The Group's liquidity risk management procedures are centralized. The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and borrowings, including loans from related parties, bank guarantees, advances received for the future oil deliveries, deferral of payments under current agreements, and loan repayment holiday provided by PJSC VTB Bank with regard to the principal amount of the loan for the next few years.

31. Financial risk management (continued)

Liquidity risk (continued)

As at 31 December 2016, the excess of the Group’s short-term liabilities over its current assets decreased and amounted to RUB 31,566 million (31 December 2015: RUB 34,540 million).

The Group's management performed current analysis with regard liquidity risk based on operating cash flows from ordinary activities, existing arrangements with major creditors and possible deferred settlement of payables to the Group's shareholders. Moreover, during the reporting period, the debt was partially converted into share capital as part of an additional issue of the Parent's shares, and the repayment schedule of the outstanding principal amount was revised (Notes 23, 24).

The following table shows undiscounted contractual cash flows for the financial liabilities, including estimated interest liability, as at 31 December 2016 and 2015.

Financial liabilities	**31 December 2016**	**Within one year**	**1 to 2 years**	**2 to 4 years**	**Over 4 years**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Trade and other payables	14,767	14,767	–	–	–
Loans and borrowings	105,215	4,604	19,426	41,200	39,985

Financial liabilities	**31 December 2015**	**Within one year**	**1 to 2 years**	**2 to 4 years**	**Over 4 years**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Trade and other payables	10,419	10,419	–	–	–
Loans and borrowings	243,030	15,377	15,385	77,375	134,893

The Company has the Insurance Policy and the Risk Management Policy in place. In the long-term, the application of these policies will help to reduce operating cash flow volatility and will have positive effect on both long-term and short-term liquidity.

The Group's management controls on a regular basis the interest coverage ratio (EBITDA / interest expense) and the debt to EBITDA ratio, as well as the amount of crude oil production and movements in EBITDA in the reporting periods. Meanwhile, the algorithm for calculating EBITDA applied by the Group as required by creditors can differ from that used by other companies.

Capital management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to maintain an optimal capital structure to reduce cost of capital and to support its business and maximize shareholder value.

The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. In the reporting period, the Company's shareholders and management completed a number of measures to improve the capital structure, including the conversion of part of the Company's long-term debt into capital, which included an additional issue of common and cumulative preference shares of the Parent in two stages and conversion of a subsidiary's debt into capital (Notes 7, 23 and 24).

31. Financial risk management (continued)

International ratings

In April 2016, Moody's rating agency confirmed the B2 corporate credit rating with a "stable" outlook for the Company. The agency appreciated the efforts taken by the Company's management to reduce debt burden by restructuring the loans provided by PJSC VTB Bank and the Company's shareholders.

The Company's management plans to implement measures which will allow it to keep the rating at the current level or increase it in the next 12 months after the reporting date. The next rating revision is scheduled within 2017.

32. Oil and gas reserves (unaudited)

The Group's oil and gas reserves were evaluated by Miller and Lents Ltd. in accordance with the standards of the Society of Petroleum Engineers as at 31 December 2016 on a fixed price basis (SPE-PRMS standard) using price and cost information provided by "Exploration and Production" segment's companies and current Russian tax laws. Reserves were measured both within the term of license agreements and beyond − to the point in time when the threshold of economically viable extraction is achieved.

The Group's oil and gas reserves are located in the Western Siberian, Central Siberian and Povolzhye regions of the Russian Federation.

As at 31 December 2016, oil and gas reserves of the Group's subsidiaries are disclosed below and comprise the following (on a 100% basis):

Reserves	**Oil and condensate**	**Gas**	**Oil and condensate + gas**
	million bbl	**billion cu ft**	**million bbl oil equivalent**
Total proved	1,080.4	918.0	1,233.40
including:			
Proved developed	413.7	461.8	490.67
Proved undeveloped	666.7	456.2	742.73
Probable	465.9	371.1	527.75
Possible	648.9	148.2	673.60

As at 31 December 2016, the share of non-controlling shareholders of the subsidiaries in total proved oil and gas reserves was 20.1 million bbl and 31.8 billion cu ft, respectively, in probable oil and gas reserves − 2.9 million bbl and 1.4 billion cu ft, respectively, in possible oil and gas reserves − 3.9 million bbl and 1.5 billion cu ft, respectively.

The Group participates in development and extraction projects in the Republic of Azerbaijan under the scheme of production sharing agreements (PSA) with the State Oil Company of Azerbaijan Republic (SOCAR) and SOCAR Oil Affiliate (SOA).

32. Oil and gas reserves (unaudited) (continued)

As at 31 December 2016, oil reserves in the Republic of Azerbaijan explored by the Group under five production sharing agreements comprise the following (on a 100% basis):

Reserves	**Oil and condensate**	**Gas**	**Oil and condensate + gas**
	million bbl	**billion cu ft**	**million bbl oil equivalent**
Total proved	66.9	−	66.9
including:			
Proved developed	44.1	−	44.1
Proved undeveloped	22.8	−	22.8
Probable	8.3	−	8.3
Possible	7.8	−	7.8

As at 31 December 2015, oil and gas reserves of the Group's subsidiaries are disclosed below and comprise the following (on a 100% basis):

Reserves	**Oil and condensate**	**Gas**	**Oil and condensate + gas**
	million bbl	**billion cu ft**	**million bbl oil equivalent**
Total proved	1,085.5	909.6	1,237.10
including:			
Proved developed	411.9	470.2	490.27
Proved undeveloped	673.6	439.4	746.83
Probable	459.5	326.0	513.83
Possible	737.8	191.8	769.77

As at 31 December 2015, the share of non-controlling shareholders of the subsidiaries in total proved oil and gas reserves was 22.8 million bbl and 34.3 billion cu ft, respectively, in probable oil and gas reserves − 3.1 million bbl and 1.5 billion cu ft, respectively, in possible oil and gas reserves − 4.1 million bbl and 1.3 billion cu ft, respectively.

As at 31 December 2015, oil reserves in the Republic of Azerbaijan explored by the Group under five PSA comprise the following (on a 100% basis):

Reserves	**Oil and condensate**	**Gas**	**Oil and condensate + gas**
	million bbl	**billion cu ft**	**million bbl oil equivalent**
Total proved	69.9	−	69.9
including:			
Proved developed	39.9	−	39.9
Proved undeveloped	30.0	−	30.0
Probable	8.8	−	8.8
Possible	8.8	−	8.8

33. Subsequent events

In February 2017, in the course of economic dispute, OJSC Varyeganneft acting as a defendant and LLC Mobile Drilling Division acting as a plaintiff entered into an amicable agreement, whereby the debt payable from OJSC Varyeganneft shall amount to RUB 118 million and be settled in February-March 2017 in three installments. As at the reporting date, the subsidiary repaid the amount of RUB 89 million (Note 30). Court proceedings with regard to this case were terminated.

22 March 2017, the Company complied with all the conditions subsequent stipulated by the addendum to the loan agreement concluded with PJSC VTB Bank. On 22 March 2017, the Company made an interest payment at a new interest rate according to the schedule.

On 20 March 2017, the Company signed the Pricing Agreement for the controlled purchases of oil from the Group's subsidiaries.