PJSC “RussNeft”

Consolidated financial statements

for the year ended 31 December 2017
together with independent auditor’s report

PJSC “RussNeft”

Consolidated financial statements

for the year ended 31 December 2017

Contents

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Independent auditor's report

To the Shareholders of PJSC "RussNeft"

Opinion

We have audited the consolidated financial statements of PJSC "RussNeft" and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statement of profit or loss and other comprehensive income for the year 2017, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year 2017, and the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year 2017 in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the consolidated financial statements in the Russian Federation, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

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

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
Determination of the fair value of derivative financial instruments	
As described in Note 29 to the consolidated financial statements, the Group purchased derivative financial instruments for the first time in 2017. In the course of our audit, we treated this matter as one of the most significant matters due to the significance of the respective transactions for the consolidated financial statements, as well as due to the fact that the fair valuation of derivative financial instruments requires management to make significant judgments.	We performed procedures to assess the competence of the Group's internal expert engaged to determine the fair value of derivative financial instruments. Our audit procedures also included the review of the methodology and the assessment of the assumptions used by the expert, including with the engagement of our experts in this area. We also reviewed the respective disclosures in the consolidated financial statements.
Impairment of loans issued to related parties	
The calculation of the allowance for impairment of loans issued to related parties is an area of judgment for the Group's management. The identification of impairment indicators and the determination of the impairment loss represent a process involving the use of assumptions and the analysis of various factors, including the borrower's financial position and expected future cash flows. Due to the significance of loans issued to related parties and the significant use of professional judgment, the estimation of the impairment allowance is a key audit matter. Information on loans issued to related parties is disclosed in Note 19 to the consolidated financial statements.	We assessed the methodology for calculating the allowance for impairment of loans issued to related parties and reviewed the assumptions used by management of the Group as the basis for determining the amount of the impairment allowance. Key assumptions include forecasts of future cash flows and assessment of the borrower's financial position. During our audit procedures, we analyzed the consistency and reasonableness of judgments used by management of the Group in determining the value of loans issued to related parties.

Other matters

The information disclosed in the consolidated financial statements as additional financial information on page 66 in the section "Oil and gas reserves" is presented for the purposes of additional analysis and is not within the scope of IFRS. In the course of our audit of the accompanying consolidated financial statements, we performed no audit procedures with regard to this additional financial information and, consequently, do not express any opinion thereon.

Other information included in the 2017 Annual Report of PJSC "RussNeft"

Other information consists of the information included in the 2017 Annual Report of PJSC "RussNeft", other than the consolidated financial statements and our auditor's report thereon. Management is responsible for other information. The 2017 Annual Report of PJSC "RussNeft" is expected to be provided to us after the date of this auditor's report.

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

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

Responsibility of the management and the Audit Committee for the consolidated financial statements

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

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

The Audit Committee is responsible for overseeing the Group's financial reporting process.

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

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and have communicated with it all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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

The partner in charge of the audit resulting in this independent auditor's report is Igor Buyan.

I.A. Buyan
Partner
Ernst & Young LLC

26 March 2018

Details of the audited entity

Name: PJSC "RussNeft"
Record made in the State Register of Legal Entities on 17 September 2002; State Registration Number 1027717003467.
Address: Russia 115054, Moscow, Pyatnitskaya ul., 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 the Self-regulated Organization of Auditors "Russian Audit Chamber" (Association) ("SRO RSA"). 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 2017

(in millions of Russian rubles)

	Notes	Year ended 31 December 2017	Year ended 31 December 2016
Revenue	11	129,193	105,003
Cost of sales	12	(94,984)	(74,428)
Gross profit		**34,209**	**30,575**
Exploration expenses		(1,338)	(744)
Selling expenses	13	(10,096)	(9,343)
General and administrative expenses	13	(3,937)	(5,145)
Other operating expenses, net	15	(6,230)	(631)
Operating profit		**12,608**	**14,712**
Finance income	14	4,024	4,920
Finance expense	14	(5,699)	(11,702)
Foreign exchange differences, net		348	10,879
Profit before tax		**11,281**	**18,809**
Income tax expense	27	(3,976)	(5,372)
Profit for the period		**7,305**	**13,437**
Other comprehensive income			
Foreign currency translation gain		220	632
Total comprehensive income, net of tax		**7,525**	**14,069**
Profit/(loss) attributable to:			
Shareholders of the Parent		8,126	14,945
Non-controlling interests		(821)	(1,508)
Total comprehensive income/(loss) attributable to:			
Shareholders of the Parent		9,119	18,845
Non-controlling interests		(1,594)	(4,776)
Basic and diluted earnings per share (RUB)	23	20	50
Weighted average number of common shares (millions)		294	249

E.V. Tolochek
President

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

Authorized for issue on 26 March 2018

The accompanying notes on pages 12 to 68 are an integral part of these consolidated financial statements.

PJSC “RussNeft”

Consolidated Statement of Financial Position

as at 31 December 2017

(in millions of Russian rubles)

	Notes	31 December 2017	31 December 2016
Assets			
Non-current assets			
Oil and gas properties	16	121,634	111,791
Other property, plant and equipment	16	546	274
Goodwill	17	13,543	13,544
Deferred tax assets	27	16,380	17,777
Exploration and evaluation assets	18	247	41
Other long-term financial assets	19	49,610	50,218
Other non-current assets		260	229
Total non-current assets		**202,220**	**193,874**
Current assets			
Inventories	20	7,108	6,797
Trade and other receivables	21	8,034	6,022
Income tax receivable		41	226
VAT receivable		819	1,089
Other short-term financial assets	19	4,848	3,346
Cash and cash equivalents	22	1,962	3,068
Other current assets		11	33
Total current assets		**22,823**	**20,581**
Total assets		**225,043**	**214,455**
Equity and liabilities			
Equity attributable to Shareholders of the Parent			
Share capital	23	196	196
Share premium		60,289	60,289
Foreign currency translation reserve		2,842	1,849
Accumulated loss		(11,585)	(17,283)
Total equity attributable to Shareholders of the Parent		**51,742**	**45,051**
Non-controlling interests	8	15,084	16,656
Total equity		**66,826**	**61,707**
Long-term liabilities			
Long-term loans and borrowings	24	81,334	84,976
Deferred tax liabilities	27	6,435	6,238
Decommissioning liability	25	7,542	9,372
Other long-term liabilities	26	25,494	15
Total long-term liabilities		**120,805**	**100,601**
Short-term liabilities			
Short-term loans and borrowings	24	133	118
Trade and other payables and accrued liabilities	26	28,610	45,757
Taxes and levies payable (excluding income tax)	26	8,154	6,135
Income tax payable		165	17
Other short-term liabilities		350	120
Total short-term liabilities		**37,412**	**52,147**
Total liabilities and equity		**225,043**	**214,455**

The accompanying notes on pages 12 to 68 are an integral part of these consolidated financial statements.

PJSC “RussNeft”

Consolidated Statement of Changes in Equity

for the year ended 31 December 2017

(in millions of Russian rubles)

	Notes	Equity attributable to Shareholders of the Parent						
		Share capital	Share premium	Foreign currency translation reserve	Retained earnings / (Accumulated loss)	Shareholders’ equity	Non-controlling interests	Total equity
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		47	33,299	–	–	33,346	–	33,346
Issue of preference shares		49	26,990	–	–	27,039	–	27,039
Dividends		–	–	–	–	–	(2)	(2)
Dividends refund		–	–	–	–	–	9	9
Conversion of debt into equity of a subsidiary		–	–	–	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		–	–	–	(15,306)	(15,306)	15,302	(4)
31 December 2016		**196**	**60,289**	**1,849**	**(17,283)**	**45,051**	**16,656**	**61,707**
Profit/(Loss) for the period		–	–	–	8,126	8,126	(821)	7,305
Foreign currency translation reserve		–	–	993	–	993	(773)	220
Total comprehensive income/(loss) for the period		**–**	**–**	**993**	**8,126**	**9,119**	**(1,594)**	**7,525**
Dividends	7, 23	–	–	–	(2,360)	(2,360)	(4)	(2,364)
Dividends refund		–	–	–	–	–	6	6
Non-controlling interests in shareholders’ contribution to subsidiaries’ equity		–	–	–	(60)	(60)	60	–
Changes in non-controlling interests in subsidiaries due to purchase of treasury shares by subsidiaries	7	–	–	–	(9)	(9)	(40)	(49)
Other equity transactions		–	–	–	1	1	–	1
31 December 2017		**196**	**60,289**	**2,842**	**(11,585)**	**51,742**	**15,084**	**66,826**

The accompanying notes on pages 12 to 68 are an integral part of these consolidated financial statements.

PJSC "RussNeft"

Consolidated Statement of Cash Flows

for the year ended 31 December 2017

(in millions of Russian rubles)

	Notes	Year ended 31 December 2017	Year ended 31 December 2016
Cash flows from operating activities			
Profit before tax		11,281	18,809
Profit before tax		**11,281**	**18,809**
Adjustments for non-cash items to reconcile profit before income tax to net cash flows			
Depreciation, depletion and amortization	12	11,904	10,428
Loss on disposal of property, plant and equipment	15	3	407
Impairment of financial investments	15	713	37
Impairment of property, plant and equipment and exploration and evaluation assets	15	443	150
Benefit obligations, bad debt allowance and other provisions		397	1,383
Dissolution of subsidiaries		–	(675)
Loss on cash flow hedge	15	4,116	–
Finance income	14	(4,024)	(4,920)
Finance expense	14	5,699	11,702
Foreign exchange differences, net		(348)	(10,879)
Other adjustments		17	(64)
Net operating cash flows before working capital changes		**30,201**	**26,378**
Working capital adjustments			
Increase in inventories		(370)	(1,172)
Increase in trade and other receivables		(1,810)	(1,133)
Increase in trade and other payables		6,848	4,466
Decrease in other current assets		21	28
Income tax paid		(2,209)	(1,246)
Net cash from operating activities		**32,681**	**27,321**
Cash flows from investing activities			
Purchase of property, plant and equipment and other non-current assets		(25,781)	(17,846)
Proceeds from disposal of property, plant and equipment		156	122
Loans issued	19	(829)	(310)
Proceeds from loans issued	19	136	25
Interest received		104	–
Net cash used in investing activities		**(26,214)**	**(18,009)**
Cash flows from financing activities			
Acquisition of non-controlling interests in subsidiaries and purchase of treasury shares	7	(49)	(4)
Proceeds from loans and borrowings received		2,237	46,951
Repayment of loans and borrowings received	24	(1,858)	(46,627)
Interest paid	24	(5,318)	(6,883)
Dividends paid to Shareholders of the Parent	23	(2,382)	–
Dividends paid to non-controlling shareholders	7	(3)	(2)
Net cash used in financing activities	24	**(7,373)**	**(6,565)**
Effect of foreign exchange rate changes on balances of cash and cash equivalents		(200)	(1,622)
Change in cash and cash equivalents		**(1,106)**	**1,125**
Cash and cash equivalents at the beginning of the period		3,068	1,943
Cash and cash equivalents at the end of the period		**1,962**	**3,068**

The accompanying notes on pages 12 to 68 are an integral part of these consolidated financial statements.

1. Corporate 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 2017 were authorized for issue in accordance with a resolution of management on 26 March 2018.

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 exploration, development, production and marketing of oil and gas, oil products. Principal subsidiaries included in the consolidated financial statements and respective ownership interests of the Company as at 31 December 2017 and 2016 are presented in Note 7.

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. In November 2016, the Parent made a public placement of common shares on the Moscow Exchange.

As at 31 December 2017, the person who is able to control the actions of the Company is Mikhail Safarbekovich Gutseriev.

In 2017, the average number of employees employed by the Group companies as at 31 December 2017 was 9,818 people (2016: 9,975 people).

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.

2. Basis of preparation

Statement of compliance

The consolidated financial statements of the Group for the year ended 31 December 2017 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)

At the reporting date, 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 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 2017 and 2016, the exchange rates used for the translation of USD-denominated transactions and balances were equal to the official CBR exchange rate of RUB 57.6002 and RUB 60.6569 per one US dollar, respectively. As at 26 March 2018, the official rate of exchange was RUB 57.1072 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.

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 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.

2. Basis of preparation (continued)

Basis of consolidation (continued)

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’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.

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.

2. Basis of preparation (continued)

Basis of consolidation (continued)

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”.

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.

2. Basis of preparation (continued)

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 2017, 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 7 *Statement of Cash Flows: Disclosure Initiative*	The amendments require an entity to disclose changes in liabilities related to the financing activities, separating effect from cash and non-cash transactions.	The application of the amendments involves additional disclosures by the Group. The Group adopted the amendments starting from the annual period ending on 31 December 2017 (Note 24).
Amendments to IAS 12 *Income Taxes: Recognition of Deferred Tax Assets for Unrealized Losses*	These amendments require an entity to determine whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of the deductible temporary difference, as well as to evaluate future taxable profit.	These amendments have no significant effect on the consolidated financial statements.
Annual improvements 2014-2016 cycle – Amendments to IFRS 12 *Disclosure of Interests in Other Entities*	The amendments clarify the scope with respect to disclosures under IFRS 12.	The amendments 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.

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

Judgments (continued)

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.

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.

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

Judgments (continued)

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.

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.

4. Summary of significant accounting policies (continued)

Business combinations and goodwill (continued)

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.

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 and 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.

4. Summary of significant accounting policies (continued)

Oil and natural gas exploration and evaluation expenditure (continued)

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.

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.

4. Summary of significant accounting policies (continued)

Depreciation (continued)

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.

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.

Derivative financial instruments

Derivative financial instruments are recognized in the consolidated statement of financial position at fair value as financial assets or financial liabilities. Realized and unrealized gains and losses are shown in financial statements on a net basis in profit or loss, except for those financial instruments to which hedge accounting applies.

The fair value of derivative financial instruments is determined on the basis of mathematical models, using publicly available market information and other valuation methods, including forecast values.

4. Summary of significant accounting policies (continued)

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.

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.

4. Summary of significant accounting policies (continued)

Leases (continued)

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.

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.

4. Summary of significant accounting policies (continued)

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.

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.

4. Summary of significant accounting policies (continued)

Taxes (continued)

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.

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 of the Group. 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.

4. Summary of significant accounting policies (continued)

Employee benefits (continued)

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 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 has now developed a model to assess credit losses and plans to adopt the standard on the required effective date. The Company is currently performing a quantitative assessment of the impact of changes resulting from the adoption of IFRS 9.

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.

Based on the results of its analysis, the Group does not expect the standard to have a material effect on its consolidated financial statements.

5. Future changes in accounting policies (continued)

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

The 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 (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.

Amendments to IFRS 2 Classification and Measurement of Share-based Payment Transactions

The amendments to IFRS 2 *Classification and Measurement of Share-based Payment Transactions*, address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled. The amendments are effective for annual periods beginning on or after 1 January 2018. The Group is currently assessing the possible impact of these amendments on its 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 entities 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.

IFRIC 22 Foreign Currency Transactions and Advance Consideration

This clarification was issued on 8 December 2016 and is effective for annual periods beginning on or after 1 January 2018. IFRIC 22 explains how to determine the transaction date for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability arising from an advance consideration in a foreign currency. According IAS 21, the transaction date for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognizes a non-monetary asset or non-monetary liability arising from an advance consideration in a foreign currency. If there are multiple payments or receipts in advance, the entity must determine the date of each payment or receipt in advance. Based on the results of its analysis, the Group does not expect the standard to have a material effect on its consolidated financial statements.

IFRS 17 Insurance Contracts

This standard was issued on 18 May 2017 and is effective for annual periods beginning on or after 1 January 2021. IFRS 17 replaces IFRS 4, which allowed entities to continue to use the existing approaches to accounting for otherwise similar insurance contracts. IFRS 17 is a single principle-based standard for recording all types of insurance contracts, including re-insurance contracts. The Group does not expect the new standard to have an impact on its consolidated financial statements.

6. Segment information

Operations of the Group are represented by the 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 2017	Effective ownership 31 December 2016
Russneft (UK) Limited	Marketing of crude oil and petroleum products	United Kingdom	100%	100%
Russneft Cyprus Limited	Other	Republic of Cyprus	20%	20%
Kura Valley Petroleum Company	Evaluation and exploration of oil and gas	Cayman Islands	20%	20%
Kura Valley Development Company	Evaluation and exploration of oil and gas	Cayman Islands	20%	20%
Kura Valley Operating Company	Evaluation and exploration of oil and gas	Cayman Islands	16%	16%
Russneft (BVI) Limited	Other	B.V.I.	20%	20%
Edmarnton Limited	Other	B.V.I.	20%	20%
International Petroleum Grouping S.A.	Evaluation and exploration of oil and gas	Islamic Republic of Mauritania	11%	11%
CJSC IP Slavneftehim	Marketing of crude oil and petroleum products	Republic of Belarus	99%	99%
LLC Torgovy Dom Russneft	Other	Russian Federation	100%	100%
LLC M-Trade	Other	Russian Federation	100%	100%
JSC Belkam-Trade	Other	Russian Federation	100%	100%
LLC Rustrade	Other	Russian Federation	100%	100%
OJSC Saratovneftegaz	Extraction and marketing of crude oil and gas	Russian Federation	96%	96%
JSC Saratov-Burenie	Extraction and marketing of crude oil	Russian Federation	96%	96%
LLC SO Agro	Other	Russian Federation	96%	96%
JSC Upravlenie Povysheniya Nefteotdachi Plasta i Kapitalnogo Remonta Skvazhin	Other	Russian Federation	96%	96%
LLC Neftebytservis	Other	Russian Federation	96%	96%
JSC 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%
LLC Agan-Trans (under dissolution)	Other	Russian Federation	97%	97%

7. Subsidiaries of the Group (continued)

Company	Principal activity	Country of incorporation	Effective ownership 31 December 2017	Effective ownership 31 December 2016
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%
JSC 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 JSC 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%
JSC Nazymskaya Neftegazorazvedochnaya Ekspeditsiya	Extraction and marketing of crude oil and gas	Russian Federation	100%	100%
JSC Khanty-Mansiyskaya Neftyanaya Kompaniya	Extraction and marketing of crude oil and gas	Russian Federation	100%	100%
JSC 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 NK Russneft-Bryansk	Transportation services	Russian Federation	51%	51%
Global Energy Cyprus Limited	Other	Republic of Cyprus	20%	20%
GEA Holdings Limited	Other	B.V.I.	20%	20%
Kura Valley Holding Company	Other	Cayman Islands	20%	20%
Karasu Petroleum Company	Other	Cayman Islands	20%	20%
Karasu Development Company	Other	Cayman Islands	20%	20%
Karasu Operating Company[1]	Extraction and marketing of crude oil under PSA	Cayman Islands	17%	17%

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

7. Subsidiaries of the Group (continued)

In the reporting year, 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 4 million. As a result of these transactions, the treasury shares account for 1.90% and 1.23% of share capital on the balance sheets of OJSC Varyeganneft and OJSC MPK Aganneftegazgeologiya. In addition, OJSC Saratovneftegaz and OJSC Ulyanovskneft repurchased the treasury shares for RUB 30 million and RUB 0.2 million, respectively. As a result of these transactions, the treasury shares account for 0.105% and 0.003% of share capital, respectively. Purchased common shares become 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 is recorded in the consolidated statements of changes in equity.

At the annual shareholders meetings, OJSC Varyeganneft and OJSC Saratovneftegaz decided to pay dividends to preference shareholders for 2016, due to what these shares ceased to be voting at the reporting date. The dividends accrued on preference shares to non-controlling shareholders are recognized in the consolidated statement of changes in equity.

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

31 December 2017	**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	26,264	9,435	42,803
Current assets	9,690	16,817	11,174
Total assets	**35,954**	**26,252**	**53,977**
Long-term liabilities	(3,889)	(2,915)	(28,154)
Short-term liabilities	(11,024)	(2,762)	(7,640)
Total liabilities	**(14,913)**	**(5,677)**	**(35,794)**
Net assets	**21,041**	**20,575**	**18,183**
Equity attributable to Shareholders of the Parent	19,861	19,854	4,248
Equity attributable to non-controlling interests	1,180	721	13,935
Year ended 31 December 2017			
Revenue	**33,864**	**6,347**	**1,626**
Profit/(Loss) for the period	**1,903**	**(374)**	**(1,133)**
Profit/(Loss) attributable to Shareholders of the Parent	1,804	(358)	(215)
Profit/(Loss) attributable to non-controlling interests	99	(16)	(918)

7. Subsidiaries of the Group (continued)

Year ended 31 December 2017	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	2,093	346	3,837
Investing activities	(1,967)	(267)	(3,969)
Financing activities	(126)	(80)	(284)
Total change in cash for the period	**–**	**(1)**	**(416)**

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)

7. Subsidiaries of the Group (continued)

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 for the period	**–**	**(2)**	**(256)**

8. Non-controlling interests

The non-controlling interests include:

	31 December 2017		2017	31 December 2016		2016
	Non-controlling interests (%)	Non-controlling interests in net assets	Non-controlling interests in profit/ (loss)	Non-controlling interests (%)	Non-controlling interests in net assets	Non-controlling interests in profit/ (loss)
		RUB million	RUB million		RUB million	RUB million
Russneft Cyprus Limited and its subsidiaries and joint ventures	80, 84, 89%	13,935	(918)	80, 84, 89%	15,566	(1,491)
OJSC Varyeganneft and its subsidiaries	5%	1,180	99	5%	1,098	82
OJSC Saratovneftegaz and its subsidiaries	4%	721	(16)	4%	755	(17)
Other	1%-49%	(752)	14	1%-49%	(763)	(82)
Non-controlling interests at the end of the period		**15,084**	**(821)**		**16,656**	**(1,508)**

As at 31 December 2017, non-controlling voting interests in OJSC Varyeganneft, OJSC MPK Aganneftegazgeologiya and OJSC Saratovneftegaz comprise 1.543%, 2.231% and 0.859%, respectively. The voting interest of PJSC “RussNeft” in Russneft Cyprus Limited is 100%.

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.

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

Business combinations in 2017 and 2016

The Group did not acquire new assets in 2017 and 2016.

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 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 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.

Joint ventures of GEA group are as follows:

Company	Principal activity	Country of incorporation	Share in equity 31 December 2017[2]	Share in equity 31 December 2016[2]	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

[2] Excluding the interest of PJSC "RussNeft" 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 joint ventures is provided below.

The statement of financial position as at 31 December 2017 and 31 December 2016:

	31 December 2017 RUB million	31 December 2016 RUB million
Non-current assets	41,708	43,644
Current assets	2,446	2,366
including cash and cash equivalents	32	284
Long-term liabilities	(51,414)	(50,725)
including long-term financial liabilities	(50,317)	(50,034)
Short-term liabilities	(5,530)	(5,684)
including short-term financial liabilities	(3,547)	(3,279)
Total equity	**(12,790)**	**(10,399)**

The statement of profit or loss and other comprehensive income for 2017 and 2016:

	2017 RUB million	2016 RUB million
Revenue	5,739	5,023
Cost of sales	(4,834)	(5,498)
including depreciation, depletion and amortization	*(2,148)*	*(2,799)*
Other operating expenses, net	(93)	(4,136)
Operating profit/(loss)	**812**	**(4,611)**
Finance income	402	490
Finance expense	(4,013)	(4,315)
Loss before income tax	**(2,799)**	**(8,436)**
Income tax expense	(154)	(43)
Loss for the period	**(2,953)**	**(8,479)**
Group’s share in loss for the period	**(1,477)**	**(4,239)**
Unrecognized share in loss for the period	1,477	4,239
Share in loss of associates and joint ventures	**–**	**–**
Unrecognized share in loss for the period	(1,477)	(4,239)
Foreign currency translation reserve for the period	282	677
Total unrecognized share in loss at the end of the period	**(6,395)**	**(5,200)**

As at 31 December 2017 and 31 December 2016, the carrying amount of investments in associates and joint ventures equals to zero.

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 (Russia). The Group’s non-current assets are located primarily in the Russian Federation except for those disclosed in Note 10.

The information on revenue is presented in the table below:

	Europe and other export		CIS (other than Russia)		Russian Federation		Total	
	2017	2016	2017	2016	2017	2016	2017	2016
	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million	RUB million
Revenue from external customers								
Crude oil sales	39,576	33,950	9,084	6,812	74,977	59,110	123,637	99,872
Petroleum product sales	509	199	1,516	1,457	–	–	2,025	1,656
Gas sales	–	–	–	–	2,551	2,929	2,551	2,929
Other sales	–	–	–	–	980	546	980	546
Total revenue	**40,085**	**34,149**	**10,600**	**8,269**	**78,508**	**62,585**	**129,193**	**105,003**

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

		Geographical location	2017	2016
			RUB million	RUB million
Major customer 1	Crude oil sales	Russian Federation	26,261	10,820
Major customer 2	Crude oil sales	Europe and other export	22,726	27,806
Major customer 3[3]	Crude oil sales	Russian Federation	–	18,332
Total revenue from sales to major customers			**48,987**	**56,958**

12. Cost of sales

	2017	2016
	RUB million	RUB million
Mineral extraction tax	48,799	34,742
Depreciation, depletion and amortization	11,904	10,428
Cost of crude oil and petroleum products sold	7,869	4,072
Payroll and related taxes	6,728	6,692
Utilities	6,244	5,068
Raw materials and supplies used in production	2,943	2,367
Production services	2,857	2,908
Equipment repair, operation and maintenance	1,989	2,125
Transportation expenses	1,080	999
Processing fees	73	183
Other expenses	4,498	4,844
Total cost of sales	**94,984**	**74,428**

[3] Revenue from major customer 3 decreased in 2017 to RUB 4,755 million and does not exceed 10% of the Group’s total revenue.

13. Selling, general and administrative expenses

Selling expenses comprise:

	2017 RUB million	2016 RUB million
Pipeline tariffs and transportation expenses	9,948	9,107
Excise	128	208
Other selling expenses	20	28
Total selling expenses	**10,096**	**9,343**

General and administrative expenses comprise the following:

	2017 RUB million	2016 RUB million
Payroll and related taxes	2,281	2,518
Entertainment and business travel	362	317
Office rent	345	401
Management services	105	102
Consulting services	103	129
Repair and maintenance	92	107
Bank services	58	80
Taxes other than income tax, including fines and penalties	55	99
Allowance for inventory obsolescence	39	297
Operating leases	36	43
Bad debt allowance	29	586
Other expenses	432	466
Total general and administrative expenses	**3,937**	**5,145**

14. Finance income and expense

Finance income comprises the following:

	2017 RUB million	2016 RUB million
Interest income on loans	3,935	4,428
Other finance income (Note 24)	89	492
Total finance income	**4,024**	**4,920**

Finance expense comprises the following:

	2017 RUB million	2016 RUB million
Interest expense on loans and borrowings, for early payments[4]	4,735	10,968
Accretion expense (Note 25)	806	460
Other finance expense (Notes 19, 24)	158	274
Total finance expense	**5,699**	**11,702**

[4] The amount includes changes in previously recognized interest expense for early payments in the amount of RUB 2,626 million (USD 45 million).

15. Other operating income and expenses

	2017	2016
	RUB million	RUB million
Loss on cash flow hedge (Note 26)	4,116	–
Charity and other gratuitous expenses	961	793
Impairment of financial investments	713	37
Impairment of property, plant and equipment (Note 16)	443	150
Public service advertising	52	119
Other provisions	39	–
Loss on sale of inventories and other assets	5	231
Loss on disposal of property, plant and equipment	3	407
Income and expenses from services rendered or received	(41)	(93)
Operating leases	(5)	(75)
Dissolution of subsidiaries	–	(675)
Other income	(168)	(293)
Other expenses	112	30
Total other operating expenses, net	**6,230**	**631**

16. Property, plant and equipment

1 January 2016	**Oil and gas properties**	**Other property, plant and equipment**	**Construction in progress**	**Total**
	RUB million	**RUB million**	**RUB million**	**RUB million**
Cost	177,559	3,077	–	180,636
Accumulated depreciation and impairment	(72,792)	(2,790)	–	(75,582)
Net book value as at 1 January 2016	**104,767**	**287**	**–**	**105,054**
Additions	17,030	–	51	17,081
Decommissioning liability	3,995	–	–	3,995
Transfer from construction in progress	–	51	(51)	–
Depreciation	(10,379)	(49)	–	(10,428)
Impairment	(150)	–	–	(150)
Disposals, net	(761)	(11)	–	(772)
Foreign currency translation	(2,711)	(4)	–	(2,715)
31 December 2016				
Cost	186,691	3,087	–	189,778
Accumulated depreciation and impairment	(74,900)	(2,813)	–	(77,713)
Net book value as at 31 December 2016	**111,791**	**274**	**–**	**112,065**
Additions	26,185	274	51	26,510
Decommissioning liability	(2,609)	–	–	(2,609)
Transfer from construction in progress	–	51	(51)	–
Depreciation	(11,851)	(53)	–	(11,904)
Impairment	(675)	(1)	–	(676)
Reversal of impairment	232	1	–	233
Disposals, net	(774)	–	–	(774)
Foreign currency translation	(665)	–	–	(665)
31 December 2017				
Cost	207,232	3,390	–	210,622
Accumulated depreciation and impairment	(85,598)	(2,844)	–	(88,442)
Net book value as at 31 December 2017	**121,634**	**546**	**–**	**122,180**

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 2017 and 2016, the Group has no significant pledges of property, plant and equipment.

16. Property, plant and equipment (continued)

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 443 million and RUB 150 million in 2017 and 2016, respectively. The allowance as at 31 December 2017 and 31 December 2016 amounts to RUB 4,873 million and RUB 5,974 million, 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
1 January 2016	**13,730**
Disposal of subsidiaries	(183)
Foreign currency translation	(3)
31 December 2016	**13,544**
Foreign currency translation	(1)
31 December 2017	**13,543**

Goodwill impairment test

The Group conducts its regular goodwill impairment test. Based on the assessment as at 31 December 2017 and 2016, 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.

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 (11.8%).
- Forecast oil price – price basis for Brent oil is in the range of USD 53-79 per barrel which is adjusted with regard 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.

17. Goodwill (continued)

Goodwill impairment test (continued)

A 1% increase in the discount rate revealed no evidence of impairment.

Change in forecast oil price	Effect on profit before tax 2017	Effect on profit before tax 2016
	RUB million	RUB million
-10	(338)	(5,150)

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

		31 December 2017	31 December 2016
		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	95
Other		389	390
		13,543	**13,544**

18. Exploration and evaluation assets

At the reporting date, the allowance for impairment of exploration and evaluation assets under some projects in the Republic of Azerbaijan and the Islamic Republic of Mauritania, which was recognized in previous reporting periods, amounts to RUB 6,501 million. As at 31 December 2016, the allowance for impairment of exploration and evaluation assets amounted to RUB 6,846 million.

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

	Currency	31 December 2017	31 December 2016
		RUB million	RUB million
Long-term loans issued to related parties	USD	49,222	50,015
Long-term loans issued to related parties	RUB	206	203
Long-term loans issued to other companies	RUB	2,378	2,293
Long-term loans issued to other companies	BYN	182	–
Allowances for impairment of long-term loans issued		(2,378)	(2,293)
		49,610	**50,218**
Short-term loans issued to related parties	USD	4,848	3,098
Short-term loans issued to other companies	BYN	–	248
		4,848	**3,346**

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

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 "Other finance expense" in the amount of RUB 122 million following the substantial modification of the initial conditions of a loan (Note 14).

The Parent records loans issued to related parties by GEA group companies under the equity method as long-term financial assets in these consolidated financial statements (Note 10). As at 31 December 2017 and 2016, the loan payable (including accumulated interest) was respectively USD 758 million and USD 707 million (RUB 43,643 million and RUB 42,901 million at the exchange rate as at the respective reporting date).

As at 31 December 2017 and 2016, 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 87 million and USD 81 million (RUB 5,037 million and RUB 4,940 million).

As at 31 December 2017 and 2016, RUB-denominated loans to Claymon Enterprises Limited were fully covered by allowances in the amount of RUB 2,363 million and RUB 2,279 million, respectively.

20. Inventories

	31 December 2017 RUB million	31 December 2016 RUB million
Crude oil	3,904	3,776
Raw materials and components	3,694	3,555
Petroleum products	191	132
Allowance for inventory obsolescence	(681)	(666)
Total inventories	**7,108**	**6,797**

21. Trade and other receivables

	31 December 2017 RUB million	31 December 2016 RUB million
Trade receivables	5,445	4,586
Prepayments	1,610	1,051
Other receivables	1,884	1,296
Allowance for bad debt and impairment	(905)	(911)
Total trade and other receivables	**8,034**	**6,022**

21. Trade and other receivables (continued)

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

	31 December 2017 RUB million	31 December 2016 RUB million
As at 1 January	**(911)**	**(378)**
Charge	(29)	(581)
Allowance used	25	9
Foreign currency translation	10	39
As at 31 December	**(905)**	**(911)**

22. Cash and cash equivalents

	31 December 2017 RUB million	31 December 2016 RUB million
Foreign currency-denominated cash at bank and on hand	1,125	569
RUB-denominated cash at bank and on hand	835	61
Deposits and other cash equivalents	2	2,438
Total cash and cash equivalents	**1,962**	**3,068**

23. Share capital

As at the reporting date, the Parent placed 294,120,000 common shares and 98,032,000 cumulative preference shares with nominal value RUB 0.5 each.

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.

Interests in the share capital of the Parent as at the reporting date are presented below (shareholders owning at least 5 percent of share capital or at least 5 percent of common shares):

Name	Percentage of share capital, %	Percentage of common shares, %
OJSC IC Nadezhnost	4.95	6.60
CJSC Mlada	7.70	10.27
RAMBERO HOLDING AG	23.46	31.28
BELYRIAN HOLDINGS LIMITED	19.19	25.59
JSC ROST BANK	27.75	3.66

The annual general shareholders meeting of the Company held in June 2017 declared dividends on cumulative preference shares for 2016: the dividends per one share were declared in the amount of USD 0.40803 at the CBR rate effective at the date of actual payment. The declared dividends totaled USD 40 million or RUB 2,360 million at the exchange rate as at the date of dividend accrual. As at the reporting date, the declared dividends were fully paid, with the payment amounting to RUB 2,382 million. In the reporting period and for 2016, no dividends were declared or paid on the Parent’s common shares.

23. Share capital (continued)

Pursuant to the Russian legislation, basis for the dividend distribution is net profit calculated in accordance with the Russian Accounting Standards (“RAS”). As a rule, these amounts differ from those calculated in accordance with IFRS in the consolidated financial statements. The RAS retained earnings of the Parent for the years ended 31 December 2017 and 31 December 2016 amounts to RUB 11,254 million and RUB 2,809 million, respectively.

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 profit attributable to shareholders of the Parent was adjusted. As at the date of the 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.

The average weighted number of the Company’s outstanding common shares did not change in the reporting period. The Group did not place securities, which may have a potential diluting effect, therefore basic and diluted earnings per share are the same.

		2017	2016
Profit attributable to Shareholders of the Parent	RUB million	8,126	14,945
Dividends on cumulative preference shares[5]	RUB million	(2,304)	(2,426)
Profit attributable to Shareholders of the Parent, as adjusted	RUB million	**5,822**	**12,519**
Weighted average number of common shares outstanding	million	294	249
Effect of dilution		–	–
Basic and diluted earnings per share	RUB per share	20	50

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

	Currency	Weighted average interest rate as at 31 December 2017	31 December 2017
		%	RUB million
Long-term loans and borrowings			
Bank loans	USD	7.16%	72,766
Borrowings	USD	8.60%	7,866
Borrowings	RUB	6.50%	702
Total long-term loans and borrowings			**81,334**
Short-term loans and borrowings			
Bank loans	USD	7.16%	129
Borrowings	RUB	7.00%	4
Total short-term loans and borrowings			**133**

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

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

	Currency	Weighted average interest rate as at 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**

In May 2015, 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) to the Company with an original maturity in March 2023 and an original fixed interest rate of 8.3%. The parties revised the loan agreement with PJSC VTB Bank several times. The last amendment in the terms of PJSC VTB Bank loan to the Company under an addendum signed in December 2016, taking into account the specifics of complying with conditions precedent, became effective in March 2017. The payment schedule and final settlement (extended until March 2026) were revised. The interest rate was 3m LIBOR + margin 5.5% p.a. Restructuring of the financial liability under the loan from PJSC VTB Bank does not meet criteria of the substantial modification of the previously recognized financial liability.

The loan from PJSC VTB Bank was secured by pledge of the ordinary 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 repays accrued interest on a quarterly basis in accordance with the schedule and an interest rate as at the date of payment. During 2017, the Company made scheduled interest payments of USD 87 million or RUB 5,068 million at the exchange rate effective at the payment date under the loan issued by PJSC VTB Bank. Outstanding principal payable to PJSC VTB Bank amounts to RUB 72,766 million or USD 1,263 million at the exchange rate as at the date of the financial statements. Current interest payable amounts to RUB 129 million (USD 2 million at the exchange rate as at the date of the financial statements).

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 is USD 71 million or RUB 4,070 million at the exchange rate at the date of the financial statements.

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

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

Due to the new requirement of IAS 7 *Statement of Cash Flows*, according to which entities must disclose changes in liabilities related to financing activities, the Group prepared a disclosure for comparative periods.

Reconciliation of movements in financing activities from the consolidated statement of cash flows with long-term and short-term loans and borrowings from the consolidated statement of financial position:

	2017			2016		
	Short-term and long-term loans and borrowings	**Other financial liabilities**	**Total**	**Short-term and long-term loans and borrowings**	**Other financial liabilities**	**Total**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**	**RUB million**
At the beginning of the period	**85,094**	**–**	**85,094**	**178,937**	**–**	**178,937**
Cash flow used in financing activities	(4,939)	–	(4,939)	(6,559)	–	(6,559)
Interest accrued	5,585	–	5,585	9,069	–	9,069
Equity transactions	–	–	–	(69,812)	–	(69,812)[6]
Discounting of financial liabilities	(52)	–	(52)	(492)	–	(492)
Foreign exchange difference	(3,823)	–	(3,823)	(25,528)	–	(25,528)
Foreign currency translation	(398)	–	(398)	(521)	–	(521)
At the end of the period	**81,467**	**–**	**81,467**	**85,094**	**–**	**85,094**
Other cash flows used in financing activities, including:	–	(2,434)	(2,434)	–	(6)	(6)
Dividends paid	–	(2,385)	(2,385)	–	(2)	(2)
Other movements	–	(49)	(49)	–	(4)	(4)
Net cash used in financing activities	**(4,939)**	**(2,434)**	**(7,373)**	**(6,559)**	**(6)**	**(6,565)**

25. Decommissioning liability

	2017		2016	
	Decommis-sioning liability	**Land restoration liability**	**Decommis-sioning liability**	**Land restoration liability**
	RUB million	**RUB million**	**RUB million**	**RUB million**
At the beginning of the period	**7,413**	**1,959**	**4,161**	**812**
Acquisitions	295	457	136	44
Disposals	(355)	(197)	(17)	(176)
Change in estimation	(2,239)	(580)	2,805	1,203
Accretion expense	637	169	384	76
Foreign currency translation	(17)	–	(56)	–
At the end of the period	**5,734**	**1,808**	**7,413**	**1,959**

[6] Equity transactions reflect the effect from the conversion of debt into share capital in 2016, excluding the effect of deferred income tax write-off to equity (Note 27).

25. Decommissioning liability (continued)

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 10.48% (2016: 8.61%).

The decommissioning liability represents the present value of decommissioning costs relating to oil and gas properties which are expected to be incurred up to 2092 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. Other long-term liabilities, trade and other payables and accrued liabilities

Other long-term liabilities	**31 December 2017**	**31 December 2016**
	RUB million	**RUB million**
Long-term advances received	21,502	–
Derivative instruments at fair value (Note 29)	2,890	–
Long-term trade payables	1,090	–
Other long-term payables and accrued liabilities	12	15
Total other long-term liabilities	**25,494**	**15**

Trade and other payables and accrued liabilities	**31 December 2017**	**31 December 2016**
	RUB million	**RUB million**
Trade payables	13,248	13,580
Advances received	11,986	29,106
Other short-term payables and accrued liabilities	2,150	3,071
Derivative instruments at fair value (Note 29)	1,226	–
Total trade and other payables and accrued liabilities	**28,610**	**45,757**

26. Other long-term liabilities, trade and other payables and accrued liabilities (continued)

In December 2017, the Group signed agreements to restructure payables related to advances received in previous periods, including interest for early payments. These agreements revised the amount of previously accrued interest expense for early payments (Notes 14, 28), increased the period for payables repayment and changed the rates for early payments.

Taxes and levies payable (excluding income tax)	**31 December 2017**	**31 December 2016**
	RUB million	**RUB million**
Mineral extraction tax	5,331	4,089
Value added tax	2,152	1,373
Property tax	345	304
Other taxes and levies (excluding income tax)	326	369
Total taxes and levies payable (excluding income tax)	**8,154**	**6,135**

27. Income tax

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

	2017	**2016**
	RUB million	**RUB million**
Current income tax		
Current income tax expense	1,941	1,355
Current income tax relating to previous years	441	274
Deferred income tax		
Relating to origination and reversal of temporary differences	2,095	3,615
Change in deferred income tax relating to previous periods	(501)	128
Income tax expense reported in the consolidated statement of profit or loss and other comprehensive income	**3,976**	**5,372**

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

	2017	**2016**
	RUB million	**RUB million**
Accounting profit before tax	**11,281**	**18,809**
Income tax at applicable tax rate (20%)	**2,256**	**3,762**
Tax effect of non-deductible expense and non-taxable income	1,489	716
Tax effect of rates other than 20%	125	195
Change in unrecognized deferred tax assets	124	276
Change in deferred income tax relating to previous periods	(501)	128
Current income tax relating to previous years	441	274
Other	42	21
Income tax expense reported in the consolidated statement of profit or loss and other comprehensive income	**3,976**	**5,372**

Generally, the subsidiaries of the Group incorporated in the Russian Federation used a 20% tax rate in 2017 and 2016; 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 2017 by the lines of the consolidated statement of financial position as well as their movements in 2017 are presented below:

	Consolidated statement of financial position	**Consolidated statement of profit or loss and other comprehensive income**	**Consolidated statement of financial position**
	31 December 2016	**2017**	**31 December 2017**
	RUB million	**RUB million**	**RUB million**
Deferred tax liabilities			
Oil and gas properties	(7,952)	(746)	(8,698)
Inventories	(492)	(54)	(546)
Loans and borrowings payable	–	–	–
Other	(180)	100	(80)
Deferred tax assets			
Tax loss carry forward	21,438	(569)	20,869
Oil and gas properties	390	(52)	338
Inventories	99	(68)	31
Trade and other receivables	10	5	15
Other	1,041	(86)	955
Unrecognized deferred tax assets	(2,815)	(124)	(2,939)
Total deferred tax liabilities and assets	**11,539**	**(1,594)**	**9,945**
Deferred income tax expense	**–**	**1,594**	**–**
Consolidated statement of financial position			
Deferred tax assets	17,777	–	16,380
Deferred tax liabilities	(6,238)	–	(6,435)

27. Income tax (continued)

Deferred income tax (continued)

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[7]	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**	**–**
Consolidated statement of financial position					
Deferred tax assets	19,515	–	–	–	17,777
Deferred tax liabilities	(5,546)	–	–	–	(6,238)

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 Russian 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 tax assets in light of the above amendments and based on its estimates of the probability of receiving sufficient taxable profit, including under certain business transactions.

[7] The previously recognized deferred tax on discounted financial liabilities was taken to other movements in equity upon conversion of debt into share capital in 2016.

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 2017 and 2016 or had significant balances outstanding as at 31 December 2017 and 2016 are detailed below.

Transactions with related parties in 2017 and 2016:

2017	**Sales**	**Other transac-tions**	**Purchases**	**Interest income**	**Interest expense**	**Dividends accrued**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Entities/Individuals with significant influence over the Group	22,726[8]	–	89	–	(850)[9]	2,360[10]
Associates and joint ventures	134	121	756	3,560	439	–
Other related parties	31,145	(687)	7,271	403	–	–
Total	**54,005**	**(566)**	**8,116**	**3,963**	**(411)**	**2,360**

2016	**Sales**	**Other transac-tions**	**Purchases**	**Interest income**	**Interest expense**	**Other equity transac-tions**
	RUB million	**RUB million**	**RUB million**	**RUB million**	**RUB million**	**RUB million**
Entities/Individuals with significant influence over the Group	27,806[11]	–	75	–	2,702	10,740[12]
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**

8 Excluding export duty.

9 The amount includes changes in previously recognized interest expense for early payments in the amount of RUB 2,626 million (USD 45 million) (Note 14).

10 At the rate as at the date of dividends declaration on cumulative preference shares (Note 23).

11 Excluding export duty.

12 Conversion of debt into a subsidiary’s equity.

28. Transactions with related parties (continued)

As at 31 December 2017 and 31 December 2016, amounts due to and due from related parties are as follows:

31 December 2017	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	199	–	29,508	–	–	–
Associates and joint ventures	273	48,680	287	4,988	–	–
Other related parties	2,721	5,596	2,912	–	59	21,234
Total	**3,193**	**54,276**	**32,707**	**4,988**	**59**	**21,234**

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**

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 2017, key management personnel compensation expense, consisting of salaries and payroll taxes, totaled RUB 1,207 million (2016: RUB 818 million).

In 2017, the Company adopted a new three-year long-term motivation program for senior and medium management. The Group recognizes the phantom shares to be paid off in cash as a liability expensed to bonuses during the period of rendering services. Planned payments are calculated upon reaching the target program criteria in each reporting period. At the end of 2017, the Company accrued RUB 109 million (including insurance contributions) for the first year of the program based on the planned performance progress.

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, current financial assets, short-term trade payables and short-term loans and borrowings is equal to their carrying amount. The fair value of long-term loans and borrowings received by the Group, long-term trade payables 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 2017, management classified the risk of default as remote.

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

	31 December 2017		31 December 2016	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
	RUB million		**RUB million**	
Loans and receivables				
Loans issued	54,458	54,148	53,564	55,067
Trade and other receivables	5,417	5,417	4,539	4,539
Cash and cash equivalents	1,962	1,962	3,068	3,068
Financial liabilities measured at amortized cost				
Trade and other payables	14,338	14,145	14,767	14,767
Loans and borrowings	81,467	89,819	85,094	83,946

In 2017, the Company entered into a number of agreements to hedge future cash flows with banks, including non-deliverable put options (in foreign currency) and call options (in Russian rubles). Fair values of derivative financial options are measured using designated mathematical models at the reporting date; the revaluation effect (loss) of RUB 4,116 million was recognized within other operating expenses in the consolidated statement of profit or loss and other comprehensive income. Given the complex structure of the instruments (the combination of the foreign currency and RUB components for measurement), the Group does not apply hedge accounting on the options through other comprehensive income.

Derivative financial instruments at fair value	31 December 2017	31 December 2016
	RUB million	**RUB million**
Long-term derivative financial assets	727	–
Short-term derivative financial assets	68	–
Long-term derivative financial liabilities	(3,617)	–
Short-term derivative financial liabilities	(1,294)	–
Total	**(4,116)**	**–**

29. Fair value measurement (continued)

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 2017	Effect on profit before tax for the year ended 31 December 2016
		RUB million	RUB million
Long-term loans issued	+1%	(985)	(1,460)
Long-term loans issued	-1%	1,016	1,518
Long-term loans and borrowings received	+1%	4,282	2,691
Long-term loans and borrowings received	-1%	(4,617)	(2,846)
Long-term trade payables	+1%	33	–
Long-term trade payables	-1%	(35)	–

30. Contingencies, commitments and operating risks

Operating environment of the Group

The Group 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. The pertaining sanctions imposed against the Russian Federation still induce reduced capital availability, higher costs of capital and uncertainty regarding economic growth, thus giving rise to the risk of an adverse effect on the Group’s financial position, performance and business prospects. The existing trends can persist for an indefinite period of time.

The consolidated financial statements reflect management 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 assessment.

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.

Taxation

Russian tax, currency and customs legislation is subject to varying interpretation and changes which can occur frequently. Management 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 tax assessments. 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.

30. Contingencies, commitments and operating risks (continued)

Taxation (continued)

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 authorities 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 2016 and 2017 exceed RUB 1 billion for the respective calendar year. In case the domestic transaction resulted in an accrual of additional income tax liabilities for one party, another party may correspondingly adjust its income tax liabilities.

In 2016 and 2017, 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. With respect to transactions for 2017, the tax base will be adjusted in the annual income tax return for 2017. Based on the comments of the Federal Tax Service, the Company improved the draft Pricing Agreement for the Company’s controlled purchases of oil from the Group’s subsidiaries (the “Agreement”) for the year 2014 and signed the improved version in March 2017. In May 2017, the Company reported on compliance with the terms of the Agreement, submitted tax returns for 2014 revised by the parties of the Agreement, paid additional tax charged and adjusted the amount of loss. In July 2017, the Federal Tax Service confirmed that the parties complied with the terms of the Agreement.

There are control procedures applied to all types of controlled transactions to ensure consistency between the prices used in the controlled transactions 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 of the Group. In 2016, the Company and a number of its subsidiaries determined their tax liabilities arising from controlled transactions using actual transaction prices or, in case the transaction price deviated from the market price, using prices adjusted pursuant to the Russian Tax Code. Symmetric adjustments were made, and the revised income tax returns were filed.

Due to the uncertainty and absence of current practice of the 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 a tax authority regarding accrual of additional tax liabilities.

30. Contingencies, commitments and operating risks (continued)

Taxation (continued)

To ensure compliance with the legislation governing taxation of controlled foreign companies and mitigate related tax risks, the Group’s management developed a set of internal routine procedures. The legislation governing taxation of controlled foreign companies requires that the Company’s income tax calculation for 2016 should include financial results of individual controlled foreign companies of the Group, whose income is subject to taxation as part of income of the Parent. Such calculation will also be submitted together with the Company’s income tax return for 2017.

The Group takes measures to reduce its tax risks on a regular basis. Management believes that the Group has complied with all regulations, and paid and accrued all taxes that are applicable. The Group’s companies are subject to periodic tax reviews.

Based on the results of the field tax audit for 2012-2013, 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 was recognized in full in the 2016 consolidated financial statements. Court proceedings concerning the results of the tax audit are still in progress. The Company filed an appeal to the Supreme Court of Russia.

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. The majority of licenses were transferred from subsidiaries to the Parent in the previous reporting periods.

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.

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 matters. 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.

30. Contingencies, commitments and operating risks (continued)

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 facilities 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 Facility 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. Regulation on Non-state Pension Benefits for the Group’s Employees was developed.

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.

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 tax authorities in April 2014. Decision of the FTS Interregional Inspectorate for Major Taxpayers No. 1 became effective in December 2014. The above-mentioned amount was 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 Chamber on Economic Disputes of the Supreme Court of the Russian Federation (hereinafter, the “Judicial Chamber”). In July 2016, the Company filed an appeal to the Deputy Chief Justice of the Supreme Court of the Russian Federation on annulment of the Determination. The appeal was dismissed in September 2016. In June 2017, the Company submitted an appeal to Deputy Chief Justice of the Supreme Court to annul the determination to deny the hearing of the cassation appeal at the Judicial Chamber. The cassation appeal was dismissed in the reporting period. 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 decided 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 Moscow Arbitration Court 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. Additional tax liabilities were settled in full. In August 2017, the 9th Appeal Arbitration Court upheld the Decision of the Moscow Arbitration Court. The Company will appeal the Decision in full at the Arbitration Court of Moscow District. The Company assesses the possibility of a positive opinion as medium.

30. Contingencies, commitments and operating risks (continued)

Litigations (continued)

LLC Mobile Drilling Division filed a claim against OJSC Varyeganneft, a subsidiary, to recover an amount of RUB 132 million payable under a construction agreement and a penalty of RUB 5 million. OJSC Varyeganneft filed a counter claim. In February 2017, 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. Court proceedings were terminated and the payables were repaid in full during the reporting period.

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 an outstanding balance (including interest) of RUB 72,895 million, or USD 1,265 million at the exchange rate as at the date of the financial statements (Note 24).

The Parent concluded independent guarantee agreements 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 3,954 million and with PJSC VTB Bank with regard to the liabilities of a related party in the total amount of USD 300 million, or RUB 17,280 million at the exchange rate as at the date of the financial statements (the underlying liability is to be repaid on or before 28 April 2025).

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. In September 2017, the Company entered into a number of agreements to hedge future cash flows (Note 29). 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.

31. Financial risk management (continued)

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 in 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 2017, the Group had derivative financial instruments in relation to commodity price risk and foreign currency risks on future cash flows.

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 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 2017 and 2016, the carrying amount 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 2017	RUB	USD	EUR	Other currencies
	RUB million	RUB million	RUB million	RUB million	RUB million
Trade and other receivables	5,417	3,753	1,418	–	246
Loans issued	54,458	206	54,070	–	182
Cash and cash equivalents	1,962	837	816	303	6
Derivative financial instruments at fair value[13]	795	–	795	–	–

Financial liabilities	31 December 2017	RUB	USD	EUR	Other currencies
	RUB million	RUB million	RUB million	RUB million	RUB million
Loans and borrowings received	(81,467)	(706)	(80,761)	–	–
Trade and other payables	(14,338)	(12,598)	(1,738)	–	(2)
Derivative financial instruments at fair value[13]	(4,911)	(4,911)	–	–	–

[13] Recorded net within derivative financial liabilities in the consolidated statement of financial position.

31. Financial risk management (continued)

Foreign currency risk (continued)

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)

An 11.00% strengthening or weakening of RUB against USD as at 31 December 2017, and a 20.00% strengthening or weakening as at 31 December 2016, 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 2017	Effect on profit before tax for the year ended 31 December 2016
	RUB million	RUB million
+11.00%	2,532	
-11.00%	(2,532)	
+20.00%		5,610
-20.00%		(5,610)

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

The analysis of sensitivity of the net position in derivative financial instruments to the strengthening or weakening of RUB against USD is provided below.

Relative strengthening/(weakening) of RUB against USD	Effect on profit before tax for the year ended 31 December 2017	Effect on profit before tax for the year ended 31 December 2016
	RUB million	RUB million
+11.00%	(87)	–
-11.00%	87	–

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 assesses the interest rate risk as related to long-term financial liabilities with a floating interest rate.

31. Financial risk management (continued)

Interest rate risk (continued)

In 2017 and 2016, interest rates on foreign currency denominated loans generally tended to increase due to the growing LIBOR rate. 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 floating interest rate pegged to the USD 3M LIBOR. In December 2017, the Company restructured the loans issued to GEA group companies and changed the rate to a floating 1Y LIBOR + 4.1% rate.

Financial instrument		**Effect on profit before tax for the year ended 31 December 2017**	**Effect on profit before tax for the year ended 31 December 2016**
		RUB million	**RUB million**
Loans and borrowings received	+0.70%	(516)	
	-0.08%	56	
	+0.6%		(508)
	-0.08%		68
Loans issued	+0.90%	275	
	-0.10%	(31)	

As at 31 December 2017, the Group did not enter into any transactions, in particular, any interest rate swaps, aimed to reduce its interest rate risk exposure.

The Group controls this risk by ongoing monitoring of 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 hedging instruments as a tool for credit risk management in this period.

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 creditworthiness.

31. Financial risk management (continued)

Credit risk (continued)

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 the 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 2017	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	54,458	4,848	44,038	5,390	182
Trade and other receivables	5,417	5,408	–	9	–
Derivative financial instruments at fair value[13]	795	68	293	434	–

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 receivables	4,539	4,527	–	12	–

As at 31 December 2017, the Group believes that its maximum exposure to credit risk is the carrying amount of its financial assets recognized in the consolidated statement of financial position.

The Group did not receive any collateral 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 mentioned factors 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 grace period provided by PJSC VTB Bank with regard to the principal amount of the loan for the next two years.

As at 31 December 2017, the excess of the Group's short-term liabilities over its current assets decreased and amounted to RUB 14,589 million (31 December 2016: RUB 31,566 million), due to, inter alia, the extended maturities of advances received (Note 26).

31. Financial risk management (continued)

Liquidity risk (continued)

The Group’s management performed current analysis with regard to 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.

The following table shows undiscounted contractual cash flows for the financial liabilities, including estimated interest liability, as at 31 December 2017 and 2016.

Financial liabilities	31 December 2017	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	14,338	13,248	174	349	567
Loans and borrowings received	117,078	5,216	16,723	19,530	75,609
Derivative financial instruments at fair value[13]	4,911	1,294	1,674	1,943	–

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 received	105,215	4,604	19,426	41,200	39,985

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 a 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.

International ratings

In April 2017, Moody’s rating agency assigned the B1 (previously − B2) rating with a “positive” outlook to the Company. The revision of the rating was driven by the analysis of financial results and cash flows for the reporting period and the Group’s improved operating profile.

In December 2017, the Company was assigned the B rating with a “stable” outlook by the Fitch rating agency.

31. Financial risk management (continued)

International ratings (continued)

The Company’s management plans to implement measures which may help 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 2018.

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 2017 on a fixed price basis (SPE-PRMS standard) using price and cost information provided by “Exploration and Production” segment 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 2017, oil and gas reserves of the Group’s companies 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	1,070.2	854.4	1,212.60
including:			
Proved developed	403.6	412.1	472.28
Proved undeveloped	666.6	442.3	740.32
Probable	473.6	352.5	532.35
Possible	684.7	193.8	717.00

As at 31 December 2017, the share of non-controlling shareholders of subsidiaries in total proved oil and gas reserves was 18 million bbl and 31.3 billion cu ft, respectively, in probable oil and gas reserves – 0.8 million bbl and 1.5 billion cu ft, respectively, in possible oil and gas reserves – 0.9 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 2017, 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	68.5	–	68.5
including:			
Proved developed	44.7	–	44.7
Proved undeveloped	23.8	–	23.8
Probable	9.9	–	9.9
Possible	9.3	–	9.3

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 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).

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

33. Subsequent events

In January 2018, the Company purchased 52,442 common shares (49% of the share capital) in OJSC Nefterazvedka for RUB 0.33 million.

In February 2018, the Company purchased shares recorded on the balance sheet of the following subsidiaries: OJSC Varyeganneft – 1.90% of the share capital for RUB 426 million, OJSC MPK Aganneftegazgeologiya – 1.23% of the share capital for RUB 121 million, OJSC Saratovneftegaz – 0.105% of the share capital for RUB 32 million, OJSC Ulyanovskneft – 0.003% of the share capital for RUB 0.4 million.

In January 2018, the period of the guarantee issued for the Group’s related party to LLC VTB Capital Trading was extended till 30 April 2019 for the amount up to RUB 4,330 million.