JSC Gazprom Neft

Consolidated Financial Statements

As of December 31, 2011 and 2010 and
for the years ended December 31, 2011, 2010 and 2009

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Report of Independent Auditors

To the Board of Directors and Shareholders of JSC Gazprom Neft:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of changes in shareholders' equity and of cash flows present fairly, in all material respects, the financial position of JSC Gazprom Neft and its subsidiaries as of December 31, 2011 and December 31, 2010, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

ZAO PricewaterhouseCoopers Audit

February 24, 2012

JSC Gazprom Neft
Consolidated Balance Sheets
As of December 31, 2011 and 2010 **(in millions of US Dollars)**

	Notes	December 31, 2011	December 31, 2010
Assets			
Current assets:			
Cash and cash equivalents	4	$ 914	$ 1,146
Short-term investments		80	110
Short-term loans receivable		449	108
Accounts receivable, net	5	3,562	2,600
Inventories	6	2,343	1,874
Assets held for sale	7	81	189
Other current assets, net	8	1,642	1,112
Total current assets		**9,071**	**7,139**
Long-term investments and loans receivable	9	6,453	6,994
Property, plant and equipment, net	10	19,313	16,466
Goodwill and other intangible assets	11	1,275	1,274
Other non-current assets		357	569
Non-current deferred income tax assets		214	220
Total assets		**$ 36,683**	**$ 32,662**
Liabilities and shareholders' equity			
Current liabilities:			
Short-term loans and current portion of long-term debt	12, 15	$ 1,277	$ 1,740
Accounts payable and accrued liabilities	13	2,078	1,923
Income and other taxes payable	14	997	884
Dividends payable		48	293
Liabilities associated with assets held for sale	7	17	134
Total current liabilities		**4,417**	**4,974**
Long-term debt	15	5,420	4,942
Asset retirement obligations		393	429
Other long-term liabilities		493	428
Deferred income tax liabilities		1,014	816
Total liabilities		**11,737**	**11,589**
Equity:			
Common stock (authorized, issued and outstanding: 4,741,299,639 shares, 0.0016 Ruble par value)		2	2
Additional paid-in-capital		731	677
Retained earnings		22,824	18,223
Less: Common stock held in treasury, at cost (23,359,582 shares as of December 31, 2011)		(45)	(45)
Total shareholders' equity		**23,512**	**18,857**
Non-controlling interest		1,434	2,216
Total equity		**24,946**	**21,073**
Total liabilities and shareholders' equity		**$ 36,683**	**$ 32,662**

A. V. Dyukov
Chief Executive Officer
JSC Gazprom Neft

A. V. Yankevich
Acting Chief Financial Officer
JSC Gazprom Neft

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

JSC Gazprom Neft
Consolidated Statements of Income **(in millions of US Dollars, except per share data)**
For the years ended December 31, 2011, 2010 and 2009

	Note	2011	2010	2009
Revenues				
Refined products and oil and gas sales		$ 43,268	$ 32,176	$ 23,773
Other		904	736	532
Total	22	**44,172**	**32,912**	**24,305**
Costs and other deductions				
Cost of purchased oil, gas and petroleum products		10,817	7,459	5,335
Operating expenses		2,464	2,126	1,896
Selling, general and administrative expenses		1,779	1,660	1,287
Transportation expenses		3,391	2,886	2,262
Depreciation, depletion and amortization		1,963	1,649	1,503
Export duties		8,092	6,631	3,948
Taxes other than income tax	14	8,038	5,301	4,027
Exploration expenses		74	91	147
Cost of other sales		575	436	297
Loss on sale of assets, net		-	-	142
Total		**37,193**	**28,239**	**20,844**
Operating income		**6,979**	**4,673**	**3,461**
Other (expense)/ income				
Share in net income of equity affiliates	9	248	229	212
Gain on sales of investments		104	9	470
Interest income		66	48	108
Interest expense		(329)	(347)	(380)
Other expense, net		(65)	(309)	(1)
Foreign exchange (loss) / gain, net		(172)	(24)	45
Total		**(148)**	**(394)**	**454**
Income before income taxes		**6,831**	**4,279**	**3,915**
Provision for income taxes		1,173	884	801
Deferred income tax expense / (benefit)	19	71	(43)	13
Total		**1,244**	**841**	**814**
Net income		**$ 5,587**	**$ 3,438**	**$ 3,101**
Less: Net income attributable to non-controlling interest		(235)	(287)	(75)
Net income attributable to Gazprom Neft		**$ 5,352**	**$ 3,151**	**$ 3,026**
Basic and Diluted Net income per Common Share attributable to Gazprom Neft (US$ per share)		1.13	0.67	0.64
Weighted-average number of common shares outstanding Basic and Diluted (millions)		4,718	4,718	4,718

For the years ended December 31, 2011, 2010 and 2009 (in millions of US Dollars)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Total Shareholders' Equity	Non-controlling Interest	Total Equity
Balance as of December 31, 2008	**$ 2**	**$ 776**	**$ 13,431**	**$ (45)**	**$ 14,164**	**$ 265**	**$ 14,429**
Net income for the period	-	13	3,013	-	3,026	75	3,101
Common stock dividends	-	-	(823)	-	(823)	-	(823)
Recognition of the financial effect of a transaction under common control	-	(30)	-	-	(30)	(18)	(48)
Changes in non-controlling interest and other	-	-	-	-	-	2,299	2,299
Balance as of December 31, 2009	**$ 2**	**$ 759**	**$ 15,621**	**$ (45)**	**$ 16,337**	**$ 2,621**	**$ 18,958**
Net income for the period	-	3	3,148	-	3,151	287	3,438
Common stock dividends	-	-	(546)	-	(546)	-	(546)
Recognition of the financial effect of a transaction under common control	-	(19)	-	-	(19)	(12)	(31)
Changes in non-controlling interest and other	-	(66)	-	-	(66)	(680)	(746)
Balance as of December 31, 2010	**$ 2**	**$ 677**	**$ 18,223**	**$ (45)**	**$ 18,857**	**$ 2,216**	**$ 21,073**
Net income for the period	-	2	5,350	-	5,352	235	5,587
Common stock dividends	-	-	(749)	-	(749)	(22)	(771)
Recognition of the financial effect of a transaction under common control	-	(116)	-	-	(116)	-	(116)
Changes in non-controlling interest and other	-	168	-	-	168	(995)	(827)
Balance as of December 31, 2011	**$ 2**	**$ 731**	**$ 22,824**	**$ (45)**	**$ 23,512**	**$ 1,434**	**$ 24,946**

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

For the years ended December 31, 2011, 2010 and 2009 (in millions of US Dollars)

	2011	2010	2009
Operating activities			
Net income	$ 5,587	$ 3,438	$ 3,101
Reconciliation of net income to net cash provided by operating activities:			
Share in income of equity affiliates, net of dividends received	314	49	11
Effect of foreign exchange	337	(50)	(143)
Deferred income tax expense / (benefit)	71	(43)	13
Depreciation, depletion and amortization	1,963	1,649	1,503
Asset retirement obligation accretion expense, net of spending on existing obligations	17	(17)	28
Allowance for doubtful accounts	61	36	(26)
Allowance for inventory obsolescence	65	19	11
Loss on disposal of property, plant and equipment	49	37	(6)
Gain on disposal of investments	(104)	14	(328)
Changes in assets and liabilities, net of acquisitions:			
Accounts receivable	(1,135)	285	(443)
Inventories	(607)	(323)	(249)
Other current assets	(717)	(205)	(277)
Other non-current assets	38	109	(64)
Accounts payable, accrued and other long-term liabilities	(89)	219	187
Income and other taxes payable	151	174	181
Net cash provided by operating activities	**6,001**	**5,391**	**3,499**
Investing activities			
Purchase of investments, net of cash acquired	(1,457)	(1,624)	(2,282)
Acquisition of investments held-to-maturity	(322)	(209)	(361)
Proceeds from sales of investments held-to-maturity	383	91	458
Loans issued	(393)	(233)	(345)
Loan proceeds received	43	209	247
Proceeds from sales of investments	301	215	10
Capital expenditures	(4,029)	(3,301)	(2,635)
Net cash used in investing activities	**(5,474)**	**(4,852)**	**(4,908)**
Financing activities			
Short and long-term loan proceeds received	2,774	4,003	5,702
Short and long-term loans repaid	(2,501)	(3,584)	(4,580)
Dividends paid	(1,025)	(728)	(937)
Net cash (used in)/ provided by financing activities	**(752)**	**(309)**	**185**
Increase in cash and cash equivalents	**(225)**	**230**	**(1,224)**
Cash and cash equivalents as of the beginning of the period	1,146	869	2,079
Effect of foreign exchange on cash and cash equivalents	(7)	47	13
Cash and cash equivalents as of the end of the period	**$ 914**	**$ 1,146**	**$ 868**
Supplemental disclosures of cash flows information			
Cash paid for interest, net of amount capitalized	304	325	329
Cash paid for income taxes	1,431	744	541

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

1. General

Description of Business

JSC Gazprom Neft (formerly OAO Siberian Oil Company) and its subsidiaries (the "Company") is a vertically integrated oil company operating in the Russian Federation, CIS and Europe. The Company's principal activities include exploration, production and development of crude oil and gas, production of refined petroleum products and distribution and marketing operations through its retail outlets.

OAO Siberian Oil Company (''Sibneft") was created by Presidential Decree Number 872 dated August 24, 1995. On September 29, 1995 Sibneft's charter was approved when the Government of the Russian Federation issued Resolution Number 972. The Omsk Registration Chamber officially registered Sibneft on October 6, 1995. In October 2005 OAO Gazprom ("Gazprom") completed its acquisition of a 75.68% stake in Sibneft which became a subsidiary of Gazprom. On May 30, 2006 Sibneft was renamed "JSC Gazprom Neft". In April 2009, Gazprom acquired an additional 20.00% interest in the Company and increased its interest to 95.68%.

2. Summary of Significant Accounting Policies

Basis of Presentation

The Company maintains its books and records in accordance with accounting and taxation principles and practices mandated by legislation in the countries in which it operates (primarily the Russian Federation). The accompanying consolidated financial statements were primarily derived from the Company's statutory books and records with adjustments and reclassifications made to present them in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

Subsequent events occurring after December 31, 2011 were evaluated through February 24, 2012, the date these financial statements were available to be issued.

Management Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities in the balance sheet as well as the revenues and expenses during the reporting periods. Certain significant estimates and assumptions for the Company include: recoverability and useful lives of long-term assets and investments; identifying assets acquired and liabilities assumed in business combinations and determining fair value; allowances for doubtful accounts receivable and inventory obsolescence; asset retirement obligations; legal and tax contingencies; depreciation, depletion and amortization; environmental remediation obligations; oil reserves; and recognition and disclosure of guarantees and other commitments. While management uses its best estimates and judgments, actual results could differ from those estimates and assumptions used.

Foreign Currency Translation

The management of the Company has determined the US Dollar is the functional and reporting currency of the Company as the majority of its revenues, debt and trade liabilities are either priced, incurred, payable or otherwise measured in US Dollars. Monetary assets and liabilities have been translated into US Dollars at the exchange rate as of the balance sheet date. Non-monetary assets and liabilities have been translated at historical rates. Revenues, expenses and cash flows are translated into US Dollars at average rates for the period or exchange rates prevailing on the transaction dates where practicable. Gains and losses resulting from the re-measurement into US Dollars are included in the consolidated statements of income.

The official exchange rates of the Ruble to the US Dollar as of December 31, 2011, 2010 and 2009 were 32.20 Rubles, 30.48 and 30.24 Rubles per US $1.00, respectively.

The translation of local currency denominated assets and liabilities into US Dollars for the purpose of these consolidated financial statements does not indicate that the Company could realize or settle, in US Dollars, the reported values of these assets and liabilities. Likewise, it does not indicate that the Company could return or distribute the reported US Dollar value of capital to its shareholders.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of majority-owned subsidiaries where no minority shareholder or group of minority shareholders exercise a majority of the substantive participating rights, and variable interest entities for which the Company is determined to be the primary beneficiary. Investments in entities that the Company does not control, but has the ability to exercise significant influence over their operating and financial policies, are accounted for under the equity method. Accordingly, the Company's share of net earnings from these companies is included in the consolidated statements of income as share in net income from equity affiliates. All other investments are recorded at cost and adjusted for impairment, as appropriate.

Business Combinations

The Company accounts for its business combinations according to FASB ASC 805, *Business Combinations*, and FASB ASC 810, *Consolidation*. The Company applies the acquisition method of accounting and recognizes the assets acquired, the liabilities assumed and any non-controlling interest in the acquiree at the acquisition date, measured at their fair values as of that date. Determining the fair value of assets acquired and liabilities assumed requires management's judgment and often involves the use of significant estimates and assumptions.

Acquisitions from entities under common control

Business combinations arising from transfers of interests in entities that are under the control of the same parent that controls the Company are accounted for in accordance with ASC 805-50 using historical carrying values accounting approach. The acquirer reflects in its financial statements the information regarding the acquisition since the date when common control was established by the parent. The acquirer revised in its financial statements all comparative information for the periods beginning after the date of establishing the common control by the parent.

The assets and liabilities acquired are measured at their carrying amounts in the accounts of the parent company that has common control at the date of transfer. Any difference at the date of transfer between the consideration paid and the carrying value of the net assets is recorded in equity (as a part of Additional Paid-In Capital).

Goodwill and Other Intangible Assets

Goodwill represents the excess of acquisition cost over the fair value of net assets acquired. The excess of the fair value of net assets acquired over acquisition cost represents negative goodwill which is recognized as a gain in the consolidated statement of income during the period of the acquisition.

In accordance with FASB ASC 350, *Intangibles – "Goodwill and Other"*, goodwill and intangible assets with indefinite useful lives are not amortized. Instead, they are tested for impairment at least on an annual basis. An impairment loss is recognized when the carrying value of goodwill exceeds its fair value. Impairment testing is a two-step process. Before running the two-step quantitative goodwill impairment test it is necessary to assess qualitative factors and if it is more likely than not that the fair value is more than the carrying amount the first step is not required. During the first step the fair value of the reporting unit compares unit with its carrying value, including goodwill. If the fair value of the reporting unit exceeds its carrying value, no impairment is recognized. Otherwise, the second step of the goodwill impairment test shall be performed to measure the amount of impairment loss resulting from the excess of the reporting unit's carrying value over its fair value. The loss recognized cannot exceed the carrying amount of goodwill. Subsequent reversal of previously recognized goodwill impairment loss is prohibited.

Intangible assets that have limited useful lives are amortized on a straight-line basis over the shorter of their useful lives or the period set by legislation. Useful lives with respect to intangible assets are determined as follows:

Intangible Asset Group	Average Life
Licenses and software	1-5 years
Land rights	25 years

Non-Controlling Interest

Certain changes in a parent's ownership interest are to be accounted for as equity transactions and when a subsidiary is deconsolidated, any non-controlling equity investment in the former subsidiary will be initially measured at fair value. In addition ownership interests in the Company's subsidiaries held by parties other than the parent are presented separately from the parent's equity on the consolidated balance sheet. The amount of consolidated net income attributable to the parent and the non-controlling interests are both presented on the face of the consolidated statements of income.

Cash and Cash Equivalents

Cash represents cash on hand and in bank accounts, which can be effectively withdrawn at any time without prior notice. Cash equivalents include all highly liquid short-term investments that can be converted to a certain cash amount and mature within three months or less from the date of purchase. They are recognized based on the cost of acquisition, which approximates fair value.

Loans and Accounts Receivable

Loans and accounts receivable are stated at net realizable value. Allowances are provided for estimated losses and for doubtful debts based on estimation of uncollectible amounts. Estimation is made based on aging of the receivable, past history of settlements with the debtor and existing economic conditions. Estimates of allowances require the exercise of judgment and the use of assumptions.

Inventories

Inventories, consisting primarily of crude oil, refined oil products and materials and supplies are stated at the lower of weighted average cost or market value. Market value should not exceed net realizable value (i.e. estimated selling price less reasonable predictable costs of completion and disposal), and should not be less than net realizable value reduced by an allowance for an estimated normal profit margin. Costs include both direct and indirect expenditures and charges incurred in bringing an item or product to its existing condition and location.

Financial Investments

In accordance with FASB ASC 825, *"Fair value option for financial assets and financial liabilities"* including amendment to ASC 320, financial investments are recorded at fair value. The fair value of investments is based on market quotes, if any, or on present value of expected cash flow with discount rates applied for their calculation in accordance with the level of risks associated with these investments.

All debt and equity securities held by the Company are classified as follows: trading securities, available-for-sale securities or held-to-maturity securities.

Trading securities are purchased and held primarily for resale in the nearest future. Held-to-maturity securities represent financial instruments that the Company has both the intent and the ability to hold to maturity. All other securities, which do not fall into these two categories, are classified as available-for-sale securities.

Unrealized gains or losses on trading securities and held-to-maturity securities are included in the consolidated statements of income. Unrealized gains or losses on available-for-sale securities less the related tax effect are recorded up to the date of their sale as a separate element of comprehensive income. Realized gains and losses on sale of securities designated as available-for-sale are determined separately for each type of security. Dividends and interest receivable are recorded on an accrual basis.

Oil and Gas Properties

In accordance with FASB ASC 932, *"Extractive Activities - Oil and Gas"*, oil and gas acquisition, exploration and development costs are recognized under the successful efforts method.

Acquisition costs include amounts paid for the acquisition of exploration and development licenses.

Exploration costs include:

- Costs of topographical, geological, and geophysical studies, rights of access to properties to conduct those studies;
- Costs of carrying and retaining undeveloped properties;
- Bottom hole contribution;
- Dry hole contribution; and
- Costs of drilling and equipping exploratory wells.

Exploration drilling costs are capitalized until it is determined that the well has proved oil and gas reserves and the reserves found are sufficient to justify its development. If the well is determined to be successful, the capitalized drilling costs will be reclassified as part of the cost of the well. The field is a cost centre. If proved reserves are not found, the capitalized drilling costs are charged to exploration expenses incurred in the period when it is determined that such cost would not bring additional proved oil and gas reserves.

Other exploration costs are charged to expense when incurred.

Development costs, which are capitalized within property plant and equipment, include expenditures incurred to:

- Gain access to and prepare well locations for drilling;
- Drill and equip development wells and service wells;
- Acquire, construct, and install production facilities; and
- Provide improved recovery systems.

Property, Plant and Equipment

Property, plant and equipment is stated at historical cost, net of accumulated depreciation. The cost of maintenance, repairs and replacement of minor items of property is charged to expense; renewals and betterments of assets are capitalized.

(in millions of US Dollars)

Upon sale or retirement of property, plant and equipment, the cost and related accumulated depreciation are eliminated from the accounts. Any resulting gains or losses are recorded in the consolidated statements of income.

Depreciation, Depletion and Amortization

Depletion of acquisition and development costs of proved oil and gas properties is calculated using the unit-of-production method based on the proved reserves and proved developed reserves, respectively. These costs are reclassified as proved properties when the relevant reserve reclassification is made. Acquisition costs of unproved properties are not amortized.

The provision for depreciation and amortization with respect to operations other than oil and gas producing activities is calculated using the straight-line method based on estimated economic lives. Depreciation rates are applied to similar types of buildings and equipment having similar economic characteristics, as shown below:

Asset Group	Average Life
Buildings and constructions	8-35 years
Machinery and equipment	8-20 years
Vehicles and other equipment	3-10 years

Impairment of Long-Lived Assets

Long-lived assets, including proved oil and gas properties at a field level, are assessed for possible impairment in accordance with FASB ASC 360 *"Property, Plant and Equipment"*. ASC 360-10-35 provides a list of events or changes in circumstances that may indicate the need to conduct a test for impairment of long-lived assets: (1) a significant decrease in the market price of a long-lived asset; (2) a significant adverse change in the extent or manner in which a long-lived asset is being used or in its physical condition; (3) a significant adverse change in legal factors or in the business climate; (4) an accumulation of costs significantly in excess of the amount originally expected for the acquisition of a long-lived asset; (5) a current-period operating or cash flow loss combined with a history of operating or cash flow losses or a negative projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset; or (6) a current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

Oil and gas properties are assessed whenever events or changes in circumstances indicate potential impairment. If the carrying value of oil and gas properties is not recoverable through undiscounted cash flows, an impairment is recognized. The impairment is determined on the basis of the estimated fair value of oil and gas properties which, in turn, is measured by discounting future net cash flows.

Discounted future net cash flows from oil and gas fields are based on management's best estimate of future prices, which are determined with reference to recent historical prices and published forward prices, applied to projected production volumes of individual fields and discounted at a rate commensurate with the risks involved. The projected production volumes represent reserves, including risk-adjusted probable and possible reserves, expected to be produced based on a stipulated amount of capital expenditure. The production volumes, prices and timing of production are consistent with internal projections and other externally reported information.

Individual assets are grouped for impairment purposes at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets - generally on a field-by-field basis for exploration and production assets, at an entire complex level for refining assets or at an operating unit level for other assets. Long-lived assets committed by management for disposal within one year are accounted for at the lower of amortized cost or fair value, less cost to sell. Acquisition costs of unproved oil and gas properties are evaluated periodically and any impairment assessed is charged to expense. No impairment has been recognized for the years ended December 31, 2011, 2010 and 2009.

Capitalized Interest

Interest is capitalized on expenditures made in connection with capital projects that could have been avoided if expenditures for the assets had not been made. Interest is only capitalized for the period when construction activities are actually in progress and until the resulting properties are put into operation. During 2011, 2010 and 2009 interest capitalized related to capital projects amounted to US$ 30 million, US$ 40 million and US$ 22 million, respectively.

Asset Retirement Obligations

The Company has asset retirement obligations associated with its core activities. The nature of the assets and potential obligations are as follow:

Exploration and Production: the Company's activities in exploration, development and production of oil and gas in the deposits are related to usage of such assets as wells, well equipment, oil gathering and processing equipment, oil storage tanks and infield pipelines. Generally, licenses and other permissions for mineral resources extraction require certain actions to be taken by the Company in respect of liquidation of these assets after oil field closure. Such actions include liquidation of wells, dismantling of equipment, soil recultivation and other remediation measures. Upon entire depletion of an oil field, the Company will incur costs related to well retirement and environmental protection measures associated with abandonment of such wells in accordance with ASC 410-20 *"Asset Retirement Obligations"*.

Refining, Marketing and Distribution: the Company's oil refining operations are carried out at large manufacturing facilities. Such manufacturing facilities have been operated for several decades. Based on principles of operations of such facilities, it is impossible to determine the ultimate date of decommissioning of sites and facilities, although some functioning parts and equipment have definite useful lives. Current regulatory and licensing rules do not provide for liabilities related to decommissioning of such manufacturing facilities and retail outlets. Therefore, the Company's management believes that there are no apparent legal or contractual obligations related to decommissioning or other disposal of these assets.

FASB ASC 410-20 calls for measurements of asset retirement obligations to include, as a component of expected costs, an estimate of the price that a third party would demand, and could expect to receive, for bearing the uncertainties and unforeseeable circumstances inherent in the obligations, sometimes referred to as a market-risk premium. To date, the oil and gas industry in the Russian Federation has few examples of credit-worthy third parties who are willing to assume this type of risk, for a determinable price, on major oil and gas production facilities and pipelines. Therefore, because determining such a market-risk premium would be an arbitrary process, it has been excluded from the Company's asset retirement obligation estimates.

As the regulatory and legal environment in the Russian Federation continues to evolve, there could be future changes to the requirements and costs associated with abandoning long-lived assets.

Income Taxes

Russian legislation does not contain the concept of a "consolidated tax-payer" and, accordingly, the Company is not subject to taxation on a consolidated basis. Current income taxes are provided on taxable profit of each subsidiary as determined under mostly the Russian Federation Tax Code at a rate of 20% after adjustments for certain items which are not deductible for taxation purposes. Subsidiaries operating in countries other than the Russian Federation are chargeable to income at the applicable statutory rate in the country in which they operate.

Deferred income tax assets and liabilities are recognized in the accompanying interim condensed consolidated financial statements in the amounts determined by the Company using the liability method in accordance with FASB ASC 740 *"Income Taxes"*. This method takes into account future tax consequences attributable to temporary differences between the carrying amounts of existing assets and liabilities for the purpose of the interim condensed consolidated financial statements and their respective tax bases and in respect of operating loss and tax credit carry-forwards. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse and the assets recovered and liabilities settled. A valuation allowance for deferred tax asset is recorded when management believes that it is more likely than not that this tax asset will not be realized in the future.

Derivative Instruments

The Company uses derivative instruments to manage its exposure to changes in foreign currency exchange rates. A substantial portion of the Company's sales revenues are received in US Dollars. Additionally, a significant portion of the Company's financing and investing activities is also undertaken in US Dollars. However, the Company's operating expenditures and capital spending are primarily denominated in Russian Rubles. Accordingly, a decline in the value of the US Dollar against the Russian Ruble will negatively impact the Company's operating results and cash flows. Therefore the Company enters into forward contracts to manage this risk.

Derivative instruments are recorded at fair value in either other assets or liabilities on the consolidated balance sheet. Realized and unrealized gains and losses are presented in the consolidated statements of income on a net basis. These transactions are not accounted for as hedges pursuant to FASB ASC 815 *"Derivatives and Hedging"*.

Common stock

Common stock represents the authorized capital of the Company, as stated in its charter document. The common shareholders are allowed one vote per share. Dividends paid to shareholders are determined by the Board of directors and approved at the annual shareholders' meeting.

Treasury stock

Common shares of the Company owned by the Group as of the balance sheet date are designated as treasury shares and are recorded at cost using the weighted-average method. Gains on resale of treasury shares are credited to additional paid-in capital whereas losses are charged to additional paid-in capital to the extent that previous net gains from resale are included therein or otherwise to retained earnings.

Earnings per Share

Basic and diluted earnings per common share have been determined by dividing the available income to common shareholders by the weighted average number of shares outstanding during the year. There are no potentially dilutive securities.

Contingencies

Certain conditions may exist as of the date these financial statements are issued, which may result in a loss to the Company, but which will only be resolved when one or more future events occur or fail to occur. The Company's management and legal counsel assess such contingent liabilities. The assessment of loss contingencies necessarily involves an exercise of judgment and is a matter of opinion. In assessing loss contingencies related to legal proceedings that are pending against the Company or unasserted claims that may result in such proceedings, the Company's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability would be accrued in the Company's financial statements. If the assessment indicates that a potentially material loss contingency is not probable, but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed. If loss contingencies can not be reasonably estimated, management recognizes the loss when information becomes available that allows a reasonable estimation to be made.

Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the nature of the guarantee would be disclosed. However, in some instances in which disclosure is not otherwise required, the Company may disclose contingent liabilities of an unusual nature which, in the judgment of management and its legal counsel, may be of interest to shareholders or others.

Retirement and Other Benefit Obligations

The Company and its subsidiaries do not have any substantial pension arrangements separate from the State pension scheme of the Russian Federation, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such contributions are charged to expense as incurred. In addition, the Company has no post-retirement benefits or significant other compensated benefits requiring accrual.

Stock-Based Compensation

In accordance with ASC 718-30 "*Compensation – Stock Compensation, Awards Classified as Liabilities*", the Company accounts for its best estimate of the obligation under cash-settled stock-appreciation rights ("SARs") granted to employees at fair value on the date of grant. The estimate of the final liability is re-measured to fair value at each reporting date and the compensation charge recognized in respect of SARs in the income statement is adjusted accordingly. Expenses are recognized over the vesting period.

Recognition of Revenues

Revenues from the sales of crude oil, petroleum products, gas and all other products are recognized when deliveries of products to final customers are made, title passes to the customer, collection is reasonably assured and sales price to final customers is fixed or determinable. Specifically, domestic crude oil sales and petroleum product and materials sales are recognized when they are shipped to customers, which is generally when title passes. For export sales, title generally passes at the border of the Russian Federation and the Company is responsible for transportation, duties and taxes on those sales.

Other revenues consist primarily of sales of services such as processing services, transportation, construction, utilities and other services and are recognized when goods are provided to customers and services are performed providing that the price for the service can be determined and no significant uncertainties regarding realization exist.

Buy/Sell Transactions

The Company accounts for buy/sell transactions in accordance with FASB ASC 845-10-15 *"Non-monetary Transactions"* which requires that two or more legally separate exchange transactions with the same counterparty, including buy/sell transactions, should be combined and considered as a single arrangement. The Company accounts for matching buy/sell arrangements entered into as exchanges of inventory.

Transportation Costs

Transportation expenses recognized in the consolidated statements of income represent all expenses incurred in the transportation of crude oil and oil products through the Transneft pipeline network, as well as cost incurred by maritime vessel and railway. Transportation expenses also include all other shipping and handling costs.

Maintenance and Repair

Maintenance and repair cost, which are not significant improvements, are expensed when incurred. The costs of refurbishing and preventive maintenance performed with respect to oil refining assets are expensed when incurred.

Accounting Standards Adopted

In January 2010 the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards updated 2010-06 Fair Value Measurements and Disclosures (Topic 820). The new provisions require that a reporting entity disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. Furthermore in reconciliation for fair value measurements using significant unobservable inputs (Level 3), a reporting entity should present separately information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number). The amendments also clarify the existing disclosures as to the requirement for management of a reporting entity to use judgment in determining the appropriate classes of assets and liabilities. The new provisions also require a reporting entity to provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements in either Level 2 or Level 3. The provisions are effective for annual and interim reporting periods beginning after December 15, 2009, except for the requirement to provide the Level 3 disclosure. This requirement is effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. Adoption of the second part of the update did not have an effect on the Company's consolidated financial statements.

In December 2010, the Financial Accounting Standards Board ("FASB") issued ASU 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts, (Topic 350 Intangibles – Goodwill and Other). ASU 2010-28 amends Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment exists. The amendments are effective for interim and annual reporting periods beginning after December 15, 2010. Early adoption is prohibited. Adoption did not have an effect on the Company's consolidated financial statements.

In December 2010, the Financial Accounting Standards Board ("FASB") issued ASU 2010-29, Disclosure of Supplementary Pro Forma Information for Business Combinations (Topic 805 Business Combinations). ASU 2010-29 specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures under Topic 805 to include a description and amount of material, non recurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. Early adoption is permitted. Adoption did not have an effect on the Company's consolidated financial statements.

Recently Issued Accounting Standards

In May 2011, the Financial Accounting Standards Board ("FASB") issued ASU 2011-04: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and IFRSs. These amendments generally represent clarifications of Topic 820, but also include some instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. These amendments result in common principles and requirements for measuring fair value and for disclosing information about fair value measurements in accordance with US GAAP and IFRSs. The Board concluded that for nonpublic entities, these amendments should be effective for annual periods beginning after December 15, 2011, with early adoption permitted; however, adoption may be no earlier than for interim periods beginning after December 15, 2011. The management does not believe the amendments will have a significant impact on the Company's financial position, results of operations and cash flows.

In June 2011, the Financial Accounting Standards Board ("FASB") issued ASU 2011-05: Presentation of Comprehensive Income Under the amendments to Topic 220, Comprehensive Income. Under these amendments an entity has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. These amendments eliminate the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. These amendments do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The Board decided that for nonpublic entities, the amendments should be effective for annual periods ending after December 15, 2012, and interim and annual periods thereafter. The management does not believe the amendments will have a significant impact on the Company's financial position, results of operations and cash flows.

In September 2011 the Financial Accounting Standards Board ("FASB") issued ASU 2011-08: Testing Goodwill for Impairment (Intangibles – Goodwill and Other [Topic 350]).The amendments in this Update will allow an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Under these amendments, an entity would not be required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. The amendments include a number of events and circumstances for an entity to consider in conducting the qualitative assessment. The Board decided that the amendments are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance. The management does not believe the amendments will have a significant impact on the Company's financial position, results of operations and cash flows.

In December 2011 FASB has issued ASU 2011-12—Comprehensive Income (Topic 220). The amendments in this Update supersede certain pending paragraphs in Accounting Standards Update No. 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income, to effectively defer only those changes in Update 2011-05 that relate to the presentation of reclassification adjustments out of accumulated other comprehensive income. The amendments will be temporary to allow the Board time to redeliberate the presentation requirements for reclassifications out of accumulated other comprehensive income for annual and interim financial statements for public, private, and non-profit entities. Taking into account that Update 2011-05 will have not a significant impact on the Company's financial position, results of operations and cash flows the Update 2011-12 also will have no significant impact on the Company's financial position, results of operations and cash flows.

Reclassifications

Certain reclassifications have been made to previously reported amounts to conform to the current year's presentation; such reclassifications have no effect on net income, net cash flow or shareholders' equity.

3. Business Combinations

Acquisition of non-controlling interest in NIS

On March 18, 2011 the Company finalized its offer made in January 2011 to buy out the free float shares in NIS (a maximum 19.12% of the NIS equity was available for purchase). Approximately 8.4 million NIS shares were submitted for purchase amounting to 5.15% of NIS authorized share capital. Based on the previously announced offer price the Company paid US$ 58 million for acquiring these shares increasing its interest in NIS from 51% to 56.15%.

The Company has accounted for the acquisition of the additional interest in NIS as an acquisition of non-controlling interest where control is maintained. As a result of the transaction the Company recognized a credit of US$ 17 million in additional paid-in-capital in shareholders' equity for the year ended December 31, 2011. The US$ 17 million represents the excess of the carrying value of the investments acquired of US$ 75 million over the consideration paid.

Acquisition of non-controlling interest in Sibir Energy

On February 14, 2011 the Board of Directors of Sibir Energy adopted a resolution to reduce the share capital by 86.25 million shares (22.39%). Central Fuel Company, an affiliate to the Moscow Government, made a decision to withdraw membership in Sibir Energy for a compensation of US$ 740 million. Starting from February 15, 2011 the Company has 100% interest in Sibir.

As a result of the transaction the Company recognized a credit of US$ 21 million in additional paid-in-capital in shareholders' equity for the year ended December 31, 2011. The US$ 21 million represents the excess of the carrying value of the investments acquired of US$ 761 million over the consideration paid to Central Fuel Company.

Following the reduction in share capital of Sibir Energy, the Company has increased its effective interest in Moscow refinery from 69.02% to 77.72%. As a result of the increase in effective interest in Moscow refinery the Company recognized a credit of approximately US$ 177 million in additional paid-in-capital in shareholders' equity for the year ended December 31, 2011.

Acquisition of Orenburg assets

On August 30, 2011 the Company acquired 100% of CJSC Centre of Science-Intensive Technologies, which holds exploration and production licenses for the Tsarichanskoye field. Furthermore, on October 18, 2011 the Company completed its purchase of a 61.8% stake in CJSC Gazprom Neft Orenburg from JSC Gazprom (the parent company). This entity holds the license for the Eastern part of the Orenburg field. The Company is also preparing to buy the remaining shares in CJSC Gazprom Neft Orenburg (belonging to Gazprom Dobycha Orenburg) and part of the field's infrastructure (owned by Gazprom). Finally, during November and December, 2011, the Company acquired 87.5% stake in JSC Yuzhuralneftegaz, which owns a license for the Kapitonovskoye field. All together these three assets form a new production cluster in the Orenburg region.

(in millions of US Dollars)

The acquisition of CJSC Centre of Science-Intensive Technologies and JSC Yuzhuralneftegaz meets the definition of FASB ASC 805, *Business Combinations*, which requires the Company to apply the acquisition method of accounting and the following table summarizes the estimates of fair value of the assets and liabilities acquired:

	As of the acquisition date
Current assets	$ 11
Property, plant and equipment	615
Other non-current assets	-
Total assets acquired	**626**
Current liabilities	(27)
Other non-current liabilities	(110)
Total liabilities assumed	**(137)**
Total identifiable assets acquired and liabilities assumed	**489**
NCI	(34)
Consideration paid	**(455)**
Goodwill	**-**

The acquisition of CJSC Gazprom Neft Orenburg from JSC Gazprom (the parent company) was deemed to have occurred between entities under common control and therefore was accounted for at Gazprom's historical cost. The difference between the cash consideration paid of 3.576 billion rubles (approximately US$ 116 million paid in cash) and the historical cost of 4.272 billion rubles (approximately US$ 139 million) was charged to additional paid-in-capital in shareholders' equity for the year ended December 31, 2011.

The following tables present information of CJSC Gazprom Neft Orenburg as of December 31, 2011 and 2010 and for the periods ending December 31, 2011, 2010 and 2009:

	December 31, 2011	December 31, 2010
Assets		
Current assets	53	46
Property, plant and equipment, net	456	552
Total assets acquired	**$ 509**	**$ 598**
Liabilities and shareholders' equity		
Current liabilitites	131	123
Non-current liabilitites	140	200
Total liabilities assumed	**271**	**323**
Total shareholders' equity	147	170
Non-controlling interest	91	105
Total liabilities and shareholders' equity	**$ 509**	**$ 598**

(in millions of US Dollars)

	2011	2010	2009
Revenues	161	140	139
Depreciation	33	30	28
Other operating costs	117	95	79
Total	**150**	**125**	**107**
Operating income	**11**	**15**	**32**
Total other expense	**(3)**	**(13)**	**(14)**
Income before income taxes	**8**	**2**	**18**
Total income tax	**(8)**	**(3)**	**(2)**
Net income	**$ 16**	**$ 5**	**$ 20**

4. Cash and Cash Equivalents

Cash and cash equivalents as of December 31, 2011 and 2010 comprise the following:

	2011	2010
Cash in bank – Rubles	$ 265	$ 120
Cash in bank – foreign currency	244	101
Bank deposits and other cash equivalents	390	918
Cash on hand	15	7
Total cash and cash equivalents	$ 914	$ 1,146

As of December 31, 2011 and 2010 the majority of bank deposits are held in Russian Rouble. Bank deposits represent deposits with original maturities of less than three months.

5. Accounts Receivable, net

Accounts receivable as of December 31, 2011 and 2010 comprise the following:

	2011	2010
Trade receivables	$ 2,167	$ 1,616
Value added tax receivable	791	682
Related party receivables	222	117
Other receivables	778	541
Less allowance for doubtful accounts	(396)	(356)
Total accounts receivable	$ 3,562	$ 2,600

Trade receivables represent amounts due from customers in the ordinary course of business, denominated primarily in US Dollars, and are short-term in nature. Other receivables consist of taxes receivable and other miscellaneous receivables.

6. Inventories

Inventories as of December 31, 2011 and 2010 consist of the following:

	2011	2010
Crude oil	$ 441	$ 339
Petroleum products	1,119	807
Materials and supplies	515	587
Other	268	141
Total inventories	$ 2,343	$ 1,874

(in millions of US Dollars)

As part of the management of crude inventory, the Company may enter transactions to buy and sell crude oil from the same counterparty. Such transactions are referred to as buy/sell transactions and are undertaken in order to reduce transportation costs or to obtain alternate quality grades of crude oil. The total value of buy / sell transactions undertaken for the years ended December 31, 2011, 2010 and 2009 is as follows:

	2011	2010	2009
Buy/sell crude oil transactions	$ 2,598	$ 1,698	$ 1,227

7. Assets held for sale

In April 2010, the Company's management approved the decision to sell the Company's oil field services business. In July 2010 the Company started the marketing stage of the process and as a result, the assets of oil field services entities and liabilities associated with these assets were classified as held for sale for the purposes of these consolidated financial statements. In 2011 the Company sold eight of nine oil field services entities for the total consideration of US$ 304 million.

In May 2011 the Company agreed on sale of JSC Meretoyakhaneftegaz in the middle of 2012.

The following table summarizes the financial information of assets held for sale as of December 31, 2011 and 2010:

	2011	2010
Accounts receivable, net	$ 13	$ 22
Inventories	5	36
Other current assets	1	22
Property, plant and equipment, net	38	108
Other intangible assets	3	1
Non-current deferred income tax assets	21	-
Assets held for sale	$ 81	$ 189
Accounts payable and accrued liabilities	13	106
Income and other taxes	3	24
Deferred income tax liabilities	1	4
Liabilities associated with assets held for sale	$ 17	$ 134

8. Other Current Assets, net

Other current assets as of December 31, 2011 and 2010 consist of the following:

	2011	2010
Prepaid customs duties	$ 811	$ 499
Advances paid	792	476
Prepaid expenses	12	28
Other assets	27	109
Total other current assets	$ 1,642	$ 1,112

(in millions of US Dollars)

9. Long-Term Investments and Loans Receivable

Long-Term Investments

None of the companies listed below are publicly traded in Russia. The significant equity and other long-term investments as of December 31, 2011 and 2010 are summarized below:

	Ownership Percentage	Net book value as of	
Investments in equity affiliates:	**December 31, 2011**	**December 31, 2011**	**December 31, 2010**
JSC Slavneft	49.9	$ 2,556	$ 2,798
JSC Tomskneft VNK	50.0	1,249	1,334
Salym Petroleum Development N.V.	50.0	1,395	1,287
SeverEnergy	25.5	781	894
Others		108	59
Total investments in equity affiliates		$ 6,089	$ 6,372
Total long-term investments, at cost		278	290
Long-term loans receivable		86	332
Total long-term investments		$ 6,453	$ 6,994

The Company's share in income of equity affiliates including share in non-controlling interest consists of the following for the periods ended December 31:

	2011	**2010**	**2009**
Equity affiliates:			
JSC Slavneft	$ 10	$ 92	$ 113
JSC Tomskneft VNK	101	55	138
Salym Petroleum Development N.V.	108	82	(44)
SeverEnergy	(10)	(5)	-
Others	39	5	5
Total share of income in equity affiliates	$ 248	$ 229	$ 212

The Company's investment in JSC Slavneft and various minority stakes in Slavneft subsidiaries ("Slavneft") are held through a series of off-shore entities and an investment trust. During 2005, the Company and TNK-BP agreed to jointly manage the production and the refineries of the Slavneft group with each party purchasing its share of production, refer also to Note 21 "Related Party Transactions".

The following table summarizes the financial information of Slavneft as of December 31, 2011 and 2010 and for the years ended December 31, 2011 and 2010:

	2011	**2010**
Current assets	$ 963	$ 1,158
Long-term assets	7,125	6,807
Total liabilities	3,003	2,589
Revenues	5,427	4,311
Net income	20	185

In December 2007 the Company acquired a 50% equity interest in JSC Tomskneft VNK ("Tomskneft") and its subsidiaries from a subsidiary of OJSC Oil Company Rosneft ("Rosneft"). As part of this transaction, the Company and Rosneft agreed to jointly manage the business operations of Tomskneft and to each purchase their respective share of Tomskneft's annual production.

(in millions of US Dollars)

The following table summarizes the financial information of Tomskneft as of December 31, 2011 and 2010 and for the years ended December 31, 2011 and 2010:

	2011	2010
Current assets	$ 617	$ 631
Long-term assets	3,251	3,420
Total liabilities	2,062	2,093
Revenues	3,524	2,652
Net income	203	111

As part of the acquisition of Sibir Energy in June 2009 the Company acquired a 50.0% equity interest in Salym Petroleum Development N.V. ("Salym"). Salym is owned 50.0% by Sibir and 50.0% by Shell Salym Development B.V., a member of the Royal Dutch/Shell group of companies. The operations of Salym relate to the development of the Salym group of oil fields located in the Khanti-Mansiysky autonomous region of the Russian Federation.

The following table summarizes the financial information of Salym as of December 31, 2011 and 2010 and for the years ended December 31, 2011 and 2010:

	2011	2010
Current assets	$ 389	$ 294
Long-term assets	890	934
Total liabilities	619	798
Revenues	2,161	1,567
Net income	429	332

In December 2010 Yamal Razvitie LLC (a joint venture between the Company and JSC Novatek) acquired a 51% equity interest in SeverEnergy LLC (SeverEnergy) from JSC Gazprom for US$ 1.9 billion. The respective purchase price paid by the Company comprised US$ 898 million. SeverEnergy is developing through its subsidiaries the Samburgskoye and Evo-Yakhinskoye oil fields and some other small oil and gas fields located in the Yamalo-Nenetskiy autonomous region of the Russian Federation.

During 2011 Yamal Razvitie LLC (a joint venture between the Company and JSC Novatek) finalized purchase price allocation on SeverEnergy.

The following table summarizes the financial information of SeverEnergy as of December 31, 2011 and 2010 and for the year ended December 31, 2011:

	2011	2010
Current assets	$ 156	$ 162
Long-term assets	5,161	4,671
Total liabilities	1,885	1,232
Net loss	(115)	(18)

<u>Long-Term Loans Receivable</u>

Long-term loans receivable of US$ 86 million and US$ 332 million are mostly due from related parties as of December 31, 2011 and 2010, respectively. These loans bear interest at rates ranging from nil to 15.0%. The fair value of these loans is approximately US$ 65 million and US$ 279 million as of December 31, 2011 and 2010 assuming an average discount rate of 8.13% and 8.03% for the periods ended December 31, 2011 and 2010, respectively (CBR interbank refinancing rate).

(in millions of US Dollars)

10. Property, Plant and Equipment

As of December 31, 2011 property, plant and equipment comprise the following:

	Cost	Accumulated DD&A	Net book value
Exploration and production	$ 25,041	$ (12,891)	$ 12,150
Refining	5,272	(2,129)	3,143
Marketing and distribution	2,326	(431)	1,895
Other	303	(24)	279
Assets under construction	1,846	-	1,846
Total	$ 34,788	$ (15,475)	$ 19,313
Comparative balance as of December 31, 2010	$ 30,420	$ (13,954)	$ 16,466

11. Goodwill and intangible assets

The goodwill balance of US$ 523 million as of December 31, 2011 and 2010 relates to acquisitions of NIS, Sibir Energy and Orton for which goodwill in the amount of US$ 349 million, US$ 140 million and US$ 34 million, was recognized, respectively. The goodwill recognized for these acquisitions was assigned to the respective downstream assets acquired. The Company assessed the carrying value of goodwill related to each acquisition for impairment as of December 31, 2011. No impairment of goodwill was recognized as of December 31, 2011.

Other intangible assets as of December 31, 2011 and 2010 comprise the following:

	2011	2010
Licenses	$ 28	$ 20
Software	191	172
Land rights	493	535
Other intangible assets	40	24
Total other intangible assets	$ 752	$ 751

Land rights relate to the right to use land plots at the Moscow Refinery location and certain other retail and wholesale sites in Moscow and the Moscow region where the Company owns and operates refining and retail assets. Accumulated depreciation with respect to land rights is US$ 55 million and US$ 33 million as of December 31, 2011 and 2010.

12. Short-Term Debt

As of December 31, 2011 and 2010 the Company has short-term loans outstanding as follows:

	2011	2010
Banks	-	$ 71
Related parties	223	244
Other	24	10
Current portion of long- term debt	1,030	1,415
Total short-term loans	$ 1,277	$ 1,740

As of December 31, 2011 and 2010 the Company has several interest-free loans from Tomskneft in the amount of US$ 206 million (US$ 231 million as of December 31, 2010), repayable in Rubles which mature in the period to September 2012. Tomskneft is a related party to the Company.

(in millions of US Dollars)

13. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities as of December 31, 2011 and 2010 comprise the following:

	2011	2010
Trade accounts payable	$ 981	$ 853
Advances received from customers	318	342
Related party accounts payable	305	223
Accrued interest	71	46
Other payables	403	459
Total accounts payable	$ 2,078	$ 1,923

14. Income and Other Taxes Payable

Income and other taxes payable as of December 31, 2011 and 2010 comprise the following:

	2011	2010
Mineral extraction tax	$ 386	$ 346
Value added tax	310	207
Excise tax	123	99
Income tax	62	137
Property tax	42	46
Other taxes	74	49
Total income and other taxes payable	$ 997	$ 884

Taxes other than income tax expense for the years ended December 31, 2011, 2010 and 2009 comprise the following:

	2011	2010	2009
Mineral extraction tax	$ 4,614	$ 3,107	$ 2,256
Excise tax	2,845	1,743	1,412
Property tax	213	182	127
Other taxes	366	269	232
Total taxes other than income tax expense	$ 8,038	$ 5,301	$ 4,027

15. Long-Term Debt

As of December 31, 2011 and 2010 the Company has long-term outstanding loans as follows:

Bonds and Bank Loans:	2011	2010
Russian Ruble bonds	$ 2,112	$ 1,247
Pre-Export Finance	1,500	1,500
Other bank loans outstanding	2,754	3,455
Other borrowings	84	155
Less current portion of long- term debt	(1,030)	(1,415)
Total Bonds and Bank Loans	$ 5,420	$ 4,942

(in millions of US Dollars)

On April 21, 2009, the Company placed Ruble Bonds (04 series) with the total par value of RUR 10 billion (US$ 311 million all non-current as of December 31, 2011 and US$ 328 million all current as of December 31, 2010). In April, 2011 an option to redeem the bonds earlier was exercised and in August, 2011 the Company completed a secondary placement of RUR 6.1 billion or approximately US$ 192 million. The bonds maturing in 2019 bear interest of 8.2% per year and have semi-annual coupon payments.

On July 21, 2009, the Company placed seven-year Ruble Bonds (03 series) with the total par value of RUR 8 billion (US$ 248 million, all current as of December 31, 2011 and US$ 263 million as of December 31, 2010, all non-current). The bonds bear interest of 14.75% per year with three year put option and have semi-annual coupon payments.

On April 13, 2010, the Company placed three-year Ruble Bonds (05 and 06 series) with the total par value of RUR 20 billion (US$ 621 million all non-current as of December 31, 2011 and US$ 656 million as of December 31, 2010, all non-current). The bonds bear interest of 7.15% per year and have semi-annual coupon payments.

On February 08, 2011, the Company placed five-year Ruble Bonds (08 series) with the total par value of RUR 10 billion (US$ 311 million as of December 31, 2011, non-current). The bonds bear interest of 8.5% per year and have semi-annual coupon payments.

On February 08, 2011, the Company placed ten-year Ruble Bonds (09 series) with the total par value of RUR 10 billion (US$ 311 million as of December 31, 2011, non-current). The bonds bear interest of 8.5% per year with a five year put option and have semi-annual coupon payments.

On February 08, 2011, the Company placed ten-year Ruble Bonds (10 series) with the total par value of RUR 10 billion (US$ 311 million as of December 31, 2011, non-current). The bonds bear interest of 8.9% per year with a seven year put option and have semi-annual coupon payments.

In July 2010 the Company had syndicated a five-year Pre-Export Term Loan Facility Agreement for the amount of US$ 1.5 billion (US$ 309 million current as of December 31, 2011). The Bank of Tokyo-Mitsubishi UFJ, Natixis SA and Societe Generale were appointed as Initial Mandated Lead Arrangers and Bookrunners. The facility bears an interest rate of LIBOR plus 1.6% and matures in July 2015 (LIBOR plus 2.1% as of December 31, 2010).

As of December 31, 2011 the Company has US$ 2,754 million in long term loans from a number of banks, primarily denominated in US Dollars (including current portion of US$ 470). As of December 31, 2010 the Company had US$ 3,455 million in long term loans from a number of banks (including current portion of US$ 1,059). Interest rates under the loans varied from LIBOR plus 0.5% to LIBOR plus 5% and from fixed interest rate of 5% to fixed interest rate of 6.75% .

The loan agreements contain financial covenants that require the Company to comply with certain levels of financial ratios namely Consolidated EBITDA to Consolidated Interest Payable, Consolidated Indebtedness to Consolidated Tangible Net Worth and Consolidated Indebtedness to Consolidated EBITDA. Management believes the Company is in compliance with these covenants as of December 31, 2011 and December 31, 2010, respectively.

Maturities of long-term loans as of December 31, 2011 are as follows:

Year due	Amount due
2012	$ 1,030
2013	2,187
2014	928
2015	621
2016 and further	1,684
	$ 6,450

(in millions of US Dollars)

16. Asset Retirement Obligations

The following table summarizes the activity of the Company's asset retirement obligations:

	2011	2010
Beginning balance as of January 1	$ 429	$ 381
Change in estimate	(58)	49
New obligations incurred	19	16
Spending on existing obligations	(32)	(44)
Accretion expense	35	27
Ending balance as of December 31, 2011 / December 31, 2010	$ 393	$ 429

17. Cash-settled Stock Appreciation Rights

On January 12, 2010 the Board approved the implementation of a cash-settled stock appreciation rights (SAR) compensation plan. The plan forms part of the long term growth strategy of the Company and is designed to reward management for increasing shareholder value over a specified period. The awards are subject to certain market and service conditions that determine the amount that may ultimately be paid to eligible employees. The expense was based on the vesting period which expires on December 31, 2011.

The fair value of the liability under the plan is estimated using the Black-Scholes-Merton option-pricing model by reference primarily to the Company's share price, historic volatility in the share price, dividend yield and interest rates for periods comparable to the remaining life of the award. Any changes in the estimated fair value of the liability award will be recognized in the period the change occurs subject to the vesting period.

In the consolidated statement of income for the periods ended December 31, 2011 and 2010 the Company recognized compensation expense, net of the deferred tax benefit, of US$ 10 million and US$ 38 million related to the SAR plan, accordingly. This expense is included within selling, general and administrative expenses. A provision of US$ 59 million and US$ 47 million has been recorded within other liabilities in respect of the Company's obligations under the plan as of December 31, 2011 and 2010.

18. Fair Value of Financial Instruments

The estimated fair values of financial instruments are determined with reference to various market information and other valuation methodologies as considered appropriate, however considerable judgment is required in interpreting market data to develop these estimates. Accordingly, the estimates are not necessarily indicative of the amounts that the Company could realize in a current market situation. Certain of these financial instruments are with major financial institutions and expose the Company to market and credit risk. The creditworthiness of these institutions is routinely reviewed and full performance is anticipated.

The Company's only assets and liabilities measured at fair value on a recurring basis are its derivative financial instruments and the obligation under SAR's, which have been valued using Level 2 inputs under the fair value hierarchy.

The Company uses derivative financial instruments to manage its exposure to changes in foreign currency exchange rates. A majority of Company's revenues are received in US Dollars, a growth or a decline in the value of the US Dollar against the Russian Ruble impacts the Company's operating results and cash flows. These transactions are not accounted for as hedges pursuant to the Fair Value Measurements and Disclosures Topic of the Codification.

(in millions of US Dollars)

The company has certain Level 3 foreign currency derivative instruments. These have been valued using a Monte Carlo model, key inputs to which include assumptions for forward curves and exchange rate volatility.

The Company does not purchase, hold or sell derivative financial instruments unless it has an existing asset or obligation or anticipates a future activity that is likely to occur that will result in an exposure to foreign exchange risk. The Company does not enter into any derivative instruments for speculative purposes. As of December 31, 2011 and 2010 the Company has outstanding forward currency exchange contracts for a total notional value of US$ 3,609 million and US$ 1,265 million respectively.

The following table presents the fair values and corresponding balance sheet captions of the Company's derivative instruments as of December 31, 2011 and 2010:

	2011	2010
Assets		
Other current assets	$ 2	$ 96
Other non-current assets	-	97
Total assets	$ 2	$ 193
Liabilities		
Other non-current liabilities	213	-
Total liabilities	$ 213	-
Unrealized (loss) / gain for the years ended December 31	(404)	59

19. Income Taxes

The Company's provision for income taxes as reported in the accompanying consolidated statements of income for the years ended December 31 is as follows:

	2011	2010	2009
Current income taxes expense	$ 1,173	$ 884	$ 801
Deferred income tax (benefit)/expense	71	(43)	13
Total provision for income taxes	$ 1,244	$ 841	$ 814

The current portion of income taxes represents the total income tax expense for the Company and each of its subsidiaries. Although the Company does not pay tax on a consolidated basis, a reconciliation of expected income tax expense to the actual tax expense for the years ended December 31 is as follows:

	2011	2010	2009
Income before income taxes	$ 6,831	$ 4,279	$ 3,915
Statutory income tax rate	20.0%	20.0%	20.0%
"Expected" income tax expense	1,366	856	783
Add (deduct) tax effect of:			
Foreign income taxed at different rates	(105)	(7)	(4)
Difference between enacted tax rate and taxes to be withheld from dividends	-	(21)	(15)
Non-deductible expenses and other permanent accounting differences	(17)	13	50
Income taxes	1,244	841	814
Effective tax rate	18.2%	19.7%	20.8%

(in millions of US Dollars)

Temporary differences between the Russian and other local statutory accounts and these financial statements give rise to the following deferred income tax assets and liabilities as of December 31:

	2011	2010
Assets and liabilities arising from the tax effect of:		
Inventory provision	16	-
Prepaid expenses	3	-
Current deferred income tax assets	$ 19	-
Asset retirement obligation	74	84
Tax loss carryforward	19	18
Fixed assets and other non-current assets and liabilities	121	118
Non-current deferred income tax assets	$ 214	$ 220
Equity investments	-	(10)
Fixed assets and other non-current assets	(1,014)	(806)
Deferred income tax liability	$ (1,014)	$ (816)
Net deferred income tax liability	(781)	(596)

For income tax purposes, certain subsidiaries of the Company have accumulated tax losses totaling US$ 95 million and US$ 90 million as of December 31, 2011 and 2010, resulting in associated deferred income tax assets of US$ 19 million and US$ 18 million, respectively. Tax loss carry-forward as of December 31, 2011 expire between 2012 and 2020.

20. Commitments and Contingencies

Taxes

The Russian Tax Authorities completed reviews over the operations of JSC Gazprom Neft and its Russian subsidiaries for the year ended December 31, 2008. Tax claims rose after these reviews did not result in significant tax risk for the Company. In 2011 the Russian tax authorities initiated reviews of the Company and its significant Russian subsidiaries for the period ended 31 December 2010. As of the date of signing of the Consolidated Financial Statements the Management is not aware of any significant tax claims to be raised after these reviews.

Russian tax and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation, including the allocation of tax payments to the Federal and Regional budgets, as applied to the transactions and activity of the Group may be challenged by the relevant authorities. The Russian tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. The Supreme Arbitration Court issued guidance to lower courts on reviewing tax cases providing a systemic roadmap for anti-avoidance claims, and it is possible that this will significantly increase the level and frequency of tax authorities scrutiny. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for the preceding three calendar years. Under certain circumstances reviews by tax authorities may cover longer periods. The years 2009, 2010 and 2011 are currently open for review. Management believes it has adequately provided for any probable losses that might arise from these matters.

(in millions of US Dollars)

Operating Environment

While there have been improvements in the economic situation in the Russian Federation in recent years, the country continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in any countries outside of the Russian Federation, restrictive currency controls, and a high level of inflation. The prospects for future economic stability in the Russian Federation are largely dependent upon the effectiveness of economic measures undertaken by the government, together with legal, regulatory, and political developments.

Environmental Matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Company periodically evaluates its potential obligations under environmental regulation. Management is of the opinion that the Company has met the government's requirements concerning environmental matters, and therefore believes that the Company does not have any material environmental liabilities.

21. Related Party Transactions

JSC Moscow Oil Refinery (Moscow Refinery)

For the year ended December 31, 2009 up to the date control was obtained the Company processed crude oil based on processing agreements in Moscow Refinery. Such transactions were in the ordinary course of business and on terms available to other suppliers.

	2009
Processing fees	$ 34
Crude, gas and oil products purchased	1

Following the acquisition of Sibir on June 23, 2009, the results of operations, cash flows and financial position of Moscow Refinery are included in the consolidated financial statements.

Slavneft Group (Slavneft)

The Company conducts a number of transactions with Slavneft or its subsidiaries. The Company and TNK-BP have split Slavneft's production based on each party's respective interest. The information on transactions with Slavneft for the years ended December 31, 2011, 2010 and 2009 is presented below:

	2011	2010	2009
Processing fees	$ 276	$ 258	$ 218
Crude, gas and oil products purchased	2,371	1,750	1,729
Crude and oil products sales	1,427	1,160	720

As of December 31, 2011 the Company has US$ 377 million in payables to Slavneft and US$ 111 million in receivables from Slavneft. As of December 31, 2010 the Company had US$ 46 million in payables to Slavneft and US$ 41 million in receivables from Slavneft.

Gazprom Group (Gazprom)

The Company conducted a number of transactions with Gazprom, the primary shareholder of the Company, or its subsidiaries. As a result of acquisition 61.8% share in CJSC Gazprom Neft Orenburg the Company included transactions of Gazprom Neft Orenburg with Gazprom to related party disclosure (Refer to Note 3).

(in millions of US Dollars)

The information on transactions with Gazprom for the years ended December 31, 2011, 2010 and 2009 is presented below:

	2011	2010	2009
Crude, gas and oil products sales	$ 194	$ 154	$ 157

As of December 31, 2011 the Company has US$ 33 million in payables to Gazprom and US$ 49 million in receivables from Gazprom. As of December 31, 2010 the Company had US$ 9 million in payables to Gazprom and US$ 27 million in receivables from Gazprom.

The Company has cash and short-term deposits in Gazprombank of US$ 127 million and US$ 176 million as of December 31, 2011 and as of December 31, 2010, respectively.

As of December 31, 2010 a loan facility of US$ 624 million included in long-term bank loans outstanding is held from Gazprombank (Switzerland) Ltd. which is a related party to the Company. In August 2011, the loan was fully repaid.

Tomskneft Group (Tomskneft)

The Company conducted a number of transactions with Tomskneft and its subsidiaries. The information on transactions with Tomskneft for the years ended December 31, 2011, 2010 and 2009 is presented below:

	2011	2010	2009
Crude, gas and oil products purchased	$ 1,574	$ 1,148	$ 997

As of December 31, 2011 the Company has US$ 20 million in payables to Tomskneft and US$ 9 million in receivables from Tomskneft. As of December 31, 2010 the Company had US$ 15 million in payables to Tomskneft and US$ 11 million in receivables from Tomskneft.

Salym Petroleum Development (SPD)

Since June 23, 2009 (the date of acquisition of Sibir), the Company conducts a number of transactions with Salym Petroleum development (SPD). The information on transactions with SPD for the years ended December 31, 2011, 2010 and 2009 is presented below:

	2011	2010	2009
Crude purchased	$ 1,107	$ 871	$ 554

As of December 31, 2011 the Company has US$ 5 million in receivables from SPD and US$ 98 million in payables to SPD. As of December 31, 2010 the Company had US$ 86 million in payables to SPD and US$ 4 million in receivables from SPD.

22. Segment Information

Presented below is information about the Company’s operating segments for the years ended December 31, 2011, 2010 and 2009. The Company determined its operating segments based on differences in the nature of their operations considering the regular review by the Company’s Chief Executive Officer to make decisions about resources to be allocated and to assess performance of the Company.

The exploration and production segment explores, develops and produces crude oil and natural gas and sells its production to the refining, marketing and distribution segment. The refining, marketing and distribution segment processes crude oil into refined products and purchases, sells and transports crude oil and refined petroleum products.

(in millions of US Dollars)

Adjusted EBITDA represents the Company's EBITDA and its share in equity affiliates' EBITDA. Management believes that adjusted EBITDA represents useful means of assessing the performance of the Company's ongoing operating activities, as it reflects the Company's earnings trends without showing the impact of certain charges. EBITDA represents earnings before interest, income tax, depreciation and amortization. EBITDA (Earnings Before Interest, Income Tax, Depreciation and Amortization) is a supplemental non-GAAP financial measure used by management to evaluate operations.
Operating Segments as of and for the year ended December 31, 2011 are presented below:

	Exploration and Production	**Refining, Marketing and Distribution**	**Elimination**	**Consolidated**
Revenues from external customers	$ 430	$ 43,742	-	$ 44,172
Inter-segment revenues	10,431	88	(10,519)	-
Total	10,861	43,830	(10,519)	44,172
Adjusted EBITDA	4,646	5,512	-	10,158
Capital expenditures	2,365	1,664	-	4,029
Depreciation, depletion and amortization	1,473	490	-	1,963
Income tax expense	206	1,038	-	1,244
Segment assets as of December 31, 2011	20,148	29,189	(12,654)	36,683

Operating Segments as of and for the year ended December 31, 2010 are presented below:

	Exploration and Production	**Refining, Marketing and Distribution**	**Elimination**	**Consolidated**
Revenues from external customers	$ 293	$ 32,619	-	$ 32,912
Inter-segment revenues	7,207	392	(7,599)	-
Total	7,500	33,011	(7,599)	32,912
Adjusted EBITDA	3,109	4,162	-	7,271
Capital expenditures	2,430	871	-	3,301
Depreciation, depletion and amortization	1,292	357	-	1,649
Income tax expense	183	658	-	841
Segment assets as of December 31, 2010	18,669	24,921	(10,928)	32,662

Operating Segments for the year ended December 31, 2009 are presented below:

	Exploration and Production	**Refining, Marketing and Distribution**	**Elimination**	**Consolidated**
Revenues from external customers	$ 215	$ 24,090	-	$ 24,305
Inter-segment revenues	6,519	66	(6,585)	-
Total	6,734	24,156	(6,585)	24,305
Adjusted EBITDA	3,301	2,736	-	6,037
Capital expenditures	2,053	582	-	2,635
Depreciation, depletion and amortization	1,330	173	-	1,503
Income tax expense	150	664	-	814

(in millions of US Dollars)

Adjusted EBITDA for the years ended December 31, 2011, 2010 and 2009 is reconciled below:

	2011	2010	2009
Adjusted EBITDA	$ 10,158	$ 7,271	$ 6,037
The Company's share in EBITDA of equity affiliates	(1,216)	(949)	(931)
Gain on sales of investments	104	9	470
Share in net income of equity affiliates	248	229	212
Foreign exchange (loss) / gain, net	(172)	(24)	45
Other expense, net	(65)	(309)	(143)
Interest expense	(329)	(347)	(380)
Interest income	66	48	108
Depreciation, depletion and amortization	(1,963)	(1,649)	(1,503)
Income before income taxes	$ 6,831	$ 4,279	$ 3,915

For the years ended December 31, 2011, 2010 and 2009 the Company had one customer which accounted for approximately 6.4%, 13.5%, and 18.5% of the Company's sales, respectively. Management does not believe the Company is reliant on any particular customer.

The geographical segmentation of the Company's revenue for the years ended December 31, 2011, 2010 and 2009 is presented below:

	2011	2010	2009
Export and international sales	$ 23,531	$ 18,828	$ 14,154
Domestic	17,788	11,676	8,251
CIS	2,853	2,408	1,900
Total revenues from external customers	$ 44,172	$ 32,912	$ 24,305

The Company's long-lived assets are mostly located in the Russian Federation.

23. Subsequent Events

On February 7, 2012 the Company placed ten-year Ruble Bonds (11 series) for total amount of RUB 10 billion (approximately US$ 332 million). The bonds bear interest of 8.25% per year. The bonds have an early redemption offer to be made 3 years following the placement.

Supplementary Information on Oil and Gas Activities (Unaudited) (in millions of US Dollars)

As required by FASB ASC 932.235, *"Extractive Activities – Oil and Gas",* the Company makes certain supplemental disclosures about its oil and gas exploration and production operations. While this information was developed with reasonable care and disclosed in good faith, it is emphasized that some of the data is necessarily imprecise and represents only approximate amounts because of the subjective judgments involved in developing such information. Accordingly, this information may not necessarily represent the current financial condition of the Company or its expected future results.

The proved oil and gas reserve quantities and related information regarding standardized measure of discounted future net cash flows do not include reserve quantities or standardized measure information related to the Company's Serbian subsidiary, NIS, as disclosure of such information is prohibited by the Government of the Republic of Serbia. The disclosures regarding capitalized costs relating to and results of operations from oil and gas activities do not include the relevant information related to NIS.

With the exception of NIS and certain PSA's and other contracts, the Company's exploration and development activities are exclusively within the Russian Federation; therefore, all of the information provided in relation to reserve quantities and standardized measure of future net cash flows pertain entirely to the Russian Federation.

Capitalized Costs Relating to Oil and Gas Producing Activities

The following tables set forth information regarding oil and gas exploration and development costs. The amounts reported as costs incurred include both capitalized costs and costs charged to expense during the period ended December 31, 2011, 2010 and 2009:

	2011	2010	2009
Consolidated subsidiaries			
Unproved oil and gas properties	$ 40	-	-
Proved oil and gas properties	24,028	21,910	19,563
Less: Accumulated depreciation, depletion and amortization	(12,581)	(11,634)	(10,494)
Net capitalized costs of oil and gas properties	$ 11,447	$ 10,276	$ 9,069
Company's share of equity method investees			
Proved oil and gas properties	$ 7,247	$ 6,962	$ 6,092
Less: Accumulated depreciation, depletion and amortization	(2,829)	(2,215)	(1,693)
Net capitalized costs of oil and gas properties	$ 4,418	$ 4,747	$ 4,399
Total capitalized costs consolidated and equity interests	**$ 15,865**	**$ 15,023**	**$ 13,468**

Cost Incurred in Oil and Gas Property Acquisition, Exploration and Development

	2011	2010	2009
Consolidated subsidiaries			
Exploration costs	$ 74	$ 91	$ 147
Development costs	2,229	2,351	1,976
Costs incurred	$ 2,303	$ 2,442	$ 2,123
Company's share of equity method investees			
Exploration costs	$ 39	$ 37	$ 25
Development costs	882	785	722
Costs incurred	$ 921	$ 822	$ 747
Total costs incurred consolidated and equity interests	$ 3,224	$ 3,264	$ 2,870

Supplementary Information on Oil and Gas Activities (Unaudited) (in millions of US Dollars)

Results of Operations from Oil and Gas Producing Activities

The Company's results of operations from oil and gas producing activities are shown below.

Sales are derived from realized prices applicable to third party crude oil sales to the Company's various markets (export, domestic and CIS). Transfers to the Company's refining operations represent prices equivalent to those that could be obtained in an arm's-length transaction.

Results of operations for oil and gas producing activities do not include general corporate overhead and monetary effects, or their associated tax effects. Income tax is based on statutory rates for the years ended, respectively, adjusted for tax deductions, tax credits and allowances. For the period ended December 31, 2011, 2010 and 2009 results of operations are as follow:

	2011	2010	2009
Consolidated subsidiaries			
Revenues:			
Sales	$ 6,756	$ 5,841	$ 5,428
Transfers	7,127	5,190	3,842
Total revenues	13,883	11,031	9,270
Production costs	(1,478)	(1,236)	(1,217)
Exploration expenses	(74)	(91)	(147)
Depreciation, depletion and amortization	(1,514)	(1,290)	(1,330)
Taxes other than income tax	(8,091)	(6,343)	(4,486)
Pretax income from producing activities	2,726	2,071	2,090
Income tax expenses	(620)	(398)	(404)
Results of oil and gas producing activities	$ 2,106	$ 1,673	$ 1,686
Company's share of equity method investees			
Revenues:			
Sales	$ 5,206	$ 3,719	$ 3,071
Total revenues	5,206	3,719	3,071
Production costs	(942)	(783)	(674)
Exploration expenses	(21)	(25)	(16)
Depreciation, depletion and amortization	(898)	(692)	(551)
Taxes other than income tax	(2,940)	(1,895)	(1,351)
Pretax income from producing activities	405	324	479
Income tax expenses	(61)	(62)	(96)
Results of oil and gas producing activities	344	262	383
Total consolidated and equity interests in results of oil and gas producing activities	$ 2,450	$ 1,935	$ 2,069

Proved Oil and Gas Reserve Quantities

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

Management believes that proved reserves should include quantities, which are expected to be produced after the expiry dates of the Company's production licenses. These licenses expire between 2013 and 2050, with the most significant licenses expiring in 2013 and 2014. Management believes the licences may be extended at the initiative of the Company and management intends to extend such licenses for properties expected to produce subsequent to their license expiry dates. The Company has disclosed information on total proved oil and condensate and gas reserve quantities and standardized measure of discounted future net cash flows.

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

The reserve quantities shown below include 100% of the net reserve quantities attributable to the Company's consolidated subsidiaries with the exception of NIS.

As determined by the Company's independent reservoir engineers, DeGolyer and MacNaughton, the following information presents the balances of proved oil and gas reserve quantities (in millions of barrels and billions of cubic feet respectively) as of December 31:

Proved Oil Reserves Quantities - in MMBbl

	2011	2010	2009
Consolidated subcidiaries			
Beginning of year	3,605	3,385	3,004
Production	(233)	(233)	(225)
Purchases of minerals in place	262	-	15
Revision of previous estimates	404	453	591
End of year	4,038	3,605	3,385
Minority's share included in the above proved reserves	(91)	(5)	(2)
Proved reserves, adjusted for minority interest	3,947	3,599	3,383
Proved developed reserves	2,218	2,038	2,121
Proved undeveloped reserves	1,820	1,567	1,264
Company's share of equity method investees			
Beginning of year	1,679	1,933	1,541
Production	(137)	(137)	(125)
Purchases of minerals in place	-	80	277
Revision of previous estimates	175	(197)	240
End of year	1,717	1,679	1,933
Proved developed reserves	918	930	1,340
Proved undeveloped reserves	799	749	593
Total consolidated and equity interests in reserves - end if year	5,665	5,278	5,316

Supplementary Information on Oil and Gas Activities (Unaudited) (in millions of US Dollars)

Proved Gas Reserves Quantities - in Bcf	**2011**	**2010**	**2009**
Consolidated subcidiaries			
Beginning of year	2,795	1,650	1,458
Production	(346)	(172)	(162)
Purchases of minerals in place	8	-	-
Revision of previous estimates	1,875	1,318	354
End of year	4,332	2,795	1,650
Minority's share included in the above proved reserves	-	-	-
Proved reserves, adjusted for minority interest	4,332	2,795	1,650
Proved developed reserves	2,843	1,603	782
Proved undeveloped reserves	1,489	1,192	868
Company's share of equity method investees			
Beginning of year	2,615	871	812
Production	(51)	(49)	(43)
Purchases of minerals in place	-	2,016	-
Revision of previous estimates	1,189	(223)	102
End of year	3,753	2,615	871
	-	-	-
Proved developed reserves	609	504	792
Proved undeveloped reserves	3,144	2,111	79
Total consolidated and equity interests in reserves - end if year	8,085	5,410	2,521

Standardized Measure of Discounted Future Net Cash Flows and Changes Therein Relating to Proved Oil and Gas Reserves

The standardized measure of discounted future net cash flows, related to the above oil and gas reserves, is calculated in accordance with the requirements of FASB ASC 932.235. Estimated future cash inflows from production are computed by applying average first-day-of-the-month price for oil and gas for each month within the 12 month period before the balance sheet date to year-end quantities of estimated proved reserves. Adjustment in this calculation for future price changes is limited to those required by contractual arrangements in existence at the end of each reporting period. Future development and production costs are those estimated future expenditures necessary to develop and produce year-end proved reserves based on year-end cost indices, assuming continuation of year end economic conditions. Estimated future income taxes are calculated by applying appropriate year-end statutory tax rates. These rates reflect allowable deductions and tax credits and are applied to estimated future pre-tax cash flows, less the tax bases of related assets. Discounted future net cash flows have been calculated using a 10% discount factor. Discounting requires a year-by-year estimate of when future expenditures will be incurred and when reserves will be produced.

The information provided in tables set out below does not represent management's estimate of the Company's expected future cash flows or of the value Company's proved oil and gas reserves. Estimates of proved reserves quantities are imprecise and change over time, as new information becomes available. Moreover, probable and possible reserves, which may become proved in the future, are excluded from the calculations. The valuation prescribed under FASB ASC 932.235 requires assumptions as to the timing and the amount of future development and production costs. The calculations should not be relied upon as an indication of the Company's future cash flows or of the value of its oil and gas reserves.

Supplementary Information on Oil and Gas Activities (Unaudited) (in millions of US Dollars)

	2011	2010	2009
Consolidated subsidiaries			
Future cash inflows	$ 278,337	$ 180,418	$ 136,982
Future production costs	(181,278)	(124,810)	(87,936)
Future development costs	(13,182)	(9,898)	(7,434)
Future income tax expenses	(14,200)	(6,778)	(6,558)
Future net cash flow	69,677	38,932	35,054
10% annual discount for estimated timing of cash flow	(37,015)	(20,892)	(17,230)
Standardized measure of discounted future net cash flow	$ 32,662	$ 18,040	$ 17,824
Company's share of equity method investees			
Future cash inflows	134,642	100,158	80,870
Future production costs	(101,964)	(77,813)	(38,781)
Future development costs	(7,450)	(6,542)	(20,300)
Future income tax expenses	(4,385)	(2,799)	(4,488)
Future net cash flow	20,843	13,004	17,301
10% annual discount for estimated timing of cash flow	(10,304)	(6,587)	(8,827)
Standardized measure of discounted future net cash flow	10,539	6,417	8,474
Total consolidated and equity interests in the standardized measure of discounted future net cash flow	$ 43,201	$ 24,457	$ 26,298

Supplementary Information on Oil and Gas Activities (Unaudited) (in millions of US Dollars)

Changes in the Standardized Measure of Discounted Cash Flows

	2011	2010	2009
Consolidated subsidiaries			
Discounted present value as of beginning of year	$ 18,039	$ 17,824	$ 12,085
Sales and transfers of oil produced, net of production costs and other operating expenses	(4,363)	(3,451)	(3,568)
Net change in prices received per barrel, net of production costs and other operating expenses	12,836	(276)	4,801
Changes in future development costs	(2,291)	(865)	(1,997)
Development costs incurred during the period	2,303	2,442	2,123
Revisions of previous quantity estimates and acquisitions	6,215	4,045	4,079
Accretion of discount	(3,037)	(264)	(946)
Net change in income taxes	3,851	2,127	2,092
Other	(890)	(3,543)	(845)
Discounted present value as of the end of year	$ 32,663	$ 18,039	$ 17,824
Company's share of equity method investees			
Discounted present value as of beginning of year	$ 6,418	$ 8,473	$ 3,553
Sales and transfers of oil produced, net of production costs and other operating expenses	(3,337)	(2,447)	(880)
Net change in prices received per barrel, net of production costs and other operating expenses	3,598	(3,001)	3,085
Changes in future development costs	(966)	(1,532)	(219)
Development costs incurred during the period	977	822	661
Revisions of previous quantity estimates	551	257	647
Accreation of discount	(2,143)	1,405	(701)
Net change in income taxes	2,869	1,007	1,058
Net change due to purchases and sales of minerals in place	-	767	2,299
Other	2,572	666	(1,029)
Discounted present value as of the end of year	$ 10,539	$ 6,417	$ 8,474