

Open Joint Stock Company AK TRANSNEFTEPRODUCT

**International Financial Reporting Standards
Consolidated Financial Statements and
Independent Auditor's Report**

31 December 2008

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INDEPENDENT AUDITOR'S REPORT

To the Shareholder and Board of Directors of OJSC AK Transnefteproduct:

- 1 We have audited the accompanying consolidated financial statements of Open Joint Stock Company AK Transnefteproduct and its subsidiaries (the "Group") which comprise the consolidated balance sheet as at 31 December 2008 and the consolidated income statement, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended and a summary of significant accounting policies and other explanatory Notes.

Management's Responsibility for the Financial Statements

- 2 Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

- 3 Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
- 4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
- 5 We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

- 6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2008, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

8 June 2009
Moscow, Russian Federation

**OJSC AK TRANSNEFTEPRODUCT****IFRS Consolidated Balance Sheet**

(in thousands of Russian roubles unless otherwise stated)

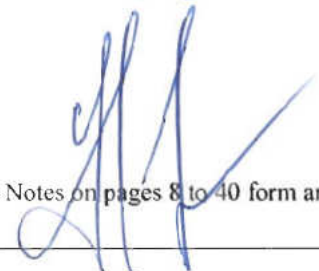
	Note	31 December 2008	31 December 2007
ASSETS			
Non-current assets			
Investment in associated undertaking	7	518,578	587,048
Available-for-sale financial assets	7	173,057	204,982
Recoverable VAT and other receivables	10	79,882	248,421
Property, plant and equipment	8	59,994,348	54,995,762
Other non-current assets		16,647	-
Total non-current assets		60,782,512	56,036,213
Current assets			
Inventories	9	473,274	484,461
Trade and other receivables	10	1,523,682	649,562
Recoverable VAT	10	3,556,108	6,091,395
Available-for-sale financial assets	7	-	24,301
Cash and cash equivalents	11	5,725,855	2,826,369
Total current assets		11,278,919	10,076,088
Total assets		72,061,431	66,112,301
EQUITY AND LIABILITIES			
Equity attributable to Company's equity holder			
Share capital	12	1,471,642	1,471,642
Retained earnings		38,666,650	38,064,300
Currency translation reserve	7	(834,933)	(846,666)
Other reserves		61,012	140,574
Total equity attributable to Company's equity holder		39,364,371	38,829,850
Minority interest		622,763	568,280
Total equity		39,987,134	39,398,130
Non-current liabilities			
Long-term borrowings and loans	13	16,643,075	20,162,752
Deferred tax liabilities	15	1,816,533	2,386,334
Provisions for liabilities and charges	16	2,797,034	425,435
Total non-current liabilities		21,256,642	22,974,521
Current liabilities			
Payables and advances from customers	14	2,806,034	2,488,823
Current portion of long-term borrowings and loans	13	7,598,077	1,038,385
Provisions for liabilities and charges	16	106,505	22,828
Profit tax and other tax liabilities	15	307,039	189,614
Total current liabilities		10,817,655	3,739,650
Total liabilities		32,074,297	26,714,171
Total equity and liabilities		72,061,431	66,112,301

Approved by:
M.G. Mezhtentsev
President

S.N. Suvorova

General director of OOO Transneft Finance,
a specialized organization, which performs the
accounting function for OAO AK Transnefteproduct

8 June 2009


The Notes on pages 8 to 40 form an integral part of these consolidated financial statements.



OJSC AK TRANSNEFTEPRODUCT
IFRS Consolidated Income Statement
(in thousands of Russian roubles unless otherwise stated)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Sales	17	18,451,551	15,751,748
Cost of sales	18	(10,785,818)	(7,979,534)
Gross profit		7,665,733	7,772,214
General and administrative expenses	19	(1,751,325)	(1,379,516)
Net other operating (expenses)/ income	20	34,915	911,404
Operating profit		5,949,323	7,304,102
Foreign exchange gain on borrowings and loans		1,340,230	1,837,752
Foreign exchange loss on borrowings and loans		(4,673,244)	(667,426)
Other financial income	21	101,965	87,160
Other financial expense	21	(2,193,142)	(1,858,138)
Share of loss of associated undertaking	7	(138,837)	(112,476)
Profit before profit tax		386,295	6,590,974
Profit tax benefit/(expense)	15	270,538	(1,782,352)
Profit for the year		656,833	4,808,622
Attributable to:			
Equity holder of the Company		602,350	4,714,995
Minority interest		54,483	93,627
Profit for the year		656,833	4,808,622

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OJSC AK TRANSNEFTEPRODUCT
IFRS Consolidated Statement of Cash Flows
(in thousands of Russian roubles unless otherwise stated)

	Year ended 31 December 2008	Year ended 31 December 2007
Cash flows from operating activities		
Cash receipts from customers	26,041,222	18,735,528
Cash paid to suppliers and employees, and taxes other than profit tax	(13,916,635)	(11,470,900)
Interest paid	(2,075,726)	(1,686,824)
Profit tax paid	(1,259,234)	(2,255,197)
Net cash from operating activities	8,789,627	3,322,607
Cash flows from investing activities		
Proceeds from sale of property, plant and equipment	249,413	2,464,643
Purchase of property, plant and equipment	(5,669,318)	(15,953,720)
Sale of long-term investments	45,338	1,888
Purchase of long-term investments	(112,601)	(4,965)
Interest received	99,092	87,366
Net cash used in investing activities	(5,388,076)	(13,404,788)
Cash flows from financing activities		
Repayments of long and short-term borrowings	(621,383)	-
Proceeds from long and short-term borrowings	-	10,252,342
Dividends	-	(100,000)
Net cash from financing activities	(621,383)	10,152,342
Net increase in cash and cash equivalents before effects of exchange rate changes	2,780,168	70,161
Effects of exchange rate changes	119,318	(7,186)
Net increase in cash and cash equivalents	2,899,486	62,975
Cash and cash equivalents at the beginning of the year	2,826,369	2,763,394
Cash and cash equivalents at the end of the period	5,725,855	2,826,369

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OJSC AK TRANSNEFTEPRODUCT
IFRS Consolidated Statement of Changes in Equity
(in thousands of Russian roubles unless otherwise stated)

Attributable to equity holder of the Company							
	Notes	Share capital	Retained earnings	Currency translation reserve (Note 7)	Other reserves	Minority interest	Total Equity
Balance at 1 January 2007		1,471,642	33,449,305	(860,785)	130,071	474,653	34,664,886
Currency translation differences		-	-	14,119	-	-	14,119
Gain from change in fair value of available-for-sale financial assets		-	-	-	11,363	-	11,363
Disposal of available-for-sale financial assets		-	-	-	(860)	-	(860)
Profit for the period		-	4,714,995	-	-	93,627	4,808,622
Total recognized income for the period		-	4,714,995	14,119	10,503	93,627	4,833,244
Dividends	12	-	(100,000)	-	-	-	(100,000)
Balance at 31 December 2007		1,471,642	38,064,300	(846,666)	140,574	568,280	39,398,130
Currency translation differences		-	-	11,733	-	-	11,733
Losses arising from change in fair value of available-for-sale financial assets		-	-	-	(37,466)	-	(37,466)
Disposal of available-for-sale financial assets		-	-	-	(42,096)	-	(42,096)
Profit for the period		-	602,350	-	-	54,483	656,833
Total recognized income/(loss) for the period		-	602,350	11,733	(79,562)	54,483	589,004
Balance at 31 December 2008		1,471,642	38,666,650	(834,933)	61,012	622,763	39,987,134

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OJSC AK TRANSNEFTEPRODUCT

Notes to the IFRS Consolidated Financial Statement – 31 December 2008

(in thousands of Russian roubles unless otherwise stated)

1. OPERATING ACTIVITIES

OJSC AK Transnefteproduct (the “Company”) was incorporated on 30 August 1993 by Resolution of the Russian Federation (“RF”) Government No. 871 under RF Presidential Decree No. 1403 dated 17 November 1992. In 2007 the only shareholder of the Company was the Federal Agency for Administration of Federal Property of Russia. To execute the order of the President of the Russian Federation from 13 April 2007 №473 and orders of the Government of the Russian Federation from 10 May 2007 №585-r, on 15 January 2008 100 % of share capital of the Company have been transferred to the OJSC AK Transneft. The Company’s registered office is at 14/1 Kollontai Street, Saint-Petersburg, Russia, 193318. In 2007 and 2008 the Group’s principal place of business was Moscow (2/36 Vishnyakovsky Pereulok, Moscow, Russia, 115184).

The principal activity of the Company and its subsidiaries (the “Group”) is the transportation of oil products via trunk pipelines. Other activities include trading, storage and loading of oil products. The Group operates a large oil products pipeline system in the Russian Federation and in the Republics of Belarus and Ukraine totalling approximately 18.7 thousand kilometers (2007: 19.1 thousand kilometres). Its associated undertaking operates an interconnected system in the Latvian Republic.

2. ECONOMIC ENVIRONMENT IN THE RUSSIAN FEDERATION

The Russian Federation displays certain characteristics of an emerging market, including relatively high inflation. Despite strong economic growth in recent years, the financial situation in the Russian market significantly deteriorated during 2008, particularly in the fourth quarter. As a result of global volatility in financial and commodity markets, among other factors, there has been a significant decline in the Russian stock market since mid-2008.

Since September 2008, there has been increased volatility in currency markets and the Russian rouble (RR) has depreciated significantly against some major currencies. The official US dollar (“USD”) exchange rate of the Central Bank of the Russian Federation (“CBRF”) increased from RR 25.3718 at 1 October 2008 to RR 29.3804 at 31 December 2008.

The commodities market was also impacted by the latest events on the financial markets. The spot Free On Board price per barrel of Urals oil decreased from USD 91.15 at 29 September 2008 to USD 41.83 at 31 December 2008.

The ongoing global liquidity crisis has resulted in among other things, a lower level of capital market funding, and lower liquidity levels across the Russian banking sector, and higher interbank lending rates. The crisis has also led to bank failures and bank rescues in the United States of America, Western Europe and in Russia. Growth of credit, currency, price risks has led to the negative trends in economy among which it is necessary to allocate a considerable rise in prices, volatility exchange quotations of securities, industrial production reduction, increase in quantity of non-returns under credits, bankruptcies of the organisations. Management is unable to predict all developments in the economic environment which could have an impact on the Group’s operations and consequently what effect, if any, they could have on the financial position of the Group. Management’s estimation of the potential influence of the crisis is based on the facts confirming presence of the crisis trends as of the reporting date and which with high probability will have a negative influence on the Group in the future reporting periods.

The influence of the crisis on the Group activity in 2008 is mainly connected with the growth of the leading world currencies exchange rates against Russian rouble. During the years of 2006-2007 the Group had obtained considerable long-term loans nominated in a foreign currency (US dollars) for the purpose of financing of the project «North» concerned with construction of a new pipeline «Kstovo-Jaroslavl-Kirishi-Primorsk» and a sea terminal in Primorsk. US dollars exchange rate growth in relation to the Russian rouble in 4th quarter of 2008 led to a proportional increase in a Russian rouble estimation of the obligations nominated in US dollars and a significant foreign exchange loss and, accordingly, significant decrease in profit of the Group in 2008. The Group tries to minimize losses from strengthening of US dollars against Russian rouble by placing of free cash in the assets nominated in currency of the debt obligations (bank deposits, see Note 11).

The Group does not expect reduction in demand and the prices for services in 2009. Expected volumes of transportation of oil products are above volumes of 2008 as a result of transportation increase in direction «Kstovo-Jaroslavl-Kirishi-Primorsk» put in operation on May 2008. Besides, the significant share of transportation services,



OJSC AK TRANSNEFTPRODUCT

Notes to the IFRS Consolidated Financial Statement – 31 December 2008

(in thousands of Russian roubles unless otherwise stated)

2. ECONOMIC ENVIRONMENT IN THE RUSSIAN FEDERATION (CONTINUED)

rendered by the Group is export, and the Group has practical possibility to raise tariffs for the export transportation services which are established in roubles, in line with growth of US dollar exchange rate and corresponding decrease in a share of transportation expenses of exporters of oil products compared to their revenue.

As the Group uses prepayments system of settlement with buyers, the Group does not have significant risks connected with insolvency of buyers and occurrence of bad debts.

The Group also does not have significant investments into other companies, except subsidiaries and associate undertaking (see Note 7).

Thus, the Management of the Group believes that the financial crisis influence on the Group activity is limited. The Management of the Group undertakes necessary efforts to maintain a sustainable development of activities of the Group. The Group expects that the future cash flow from operating activities will be sufficient to service its obligations under the loan agreements.

The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and frequent changes, and other legal and fiscal impediments also contribute to the challenges faced by entities of the Group currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

3. CHANGES IN ACCOUNTING ESTIMATES

In order to comply with established practice of the parent company (OJSC AK Transneft) the management of the Group at 31 December 2008 established provision for dismantlement for the expected cost of dismantling parts of the existing pipeline network with the reference to the average current cost per kilometer of removal according to an estimated plan of replacement over the long term. The provision calculation is based on the assumption that dismantlement activities are expected to cover the same number of kilometers each year over the useful life of the network. As integration of practices and policies of the Group with those of AK Transneft occurred towards the end of financial year of 2008, therefore the provision for dismantlement was created at the end of 2008.

In addition the Group provided for prospective dismantlement or decommissioning of specific underground storage reservoirs, pipelines and related infrastructure which were taken out of operation before 2008 (Refer to Note 6 and Note 16). For specific underground storage reservoirs, pipelines and related infrastructure which are taken out of operations starting from 2008 the Group does not create the dismantlement provision as management, have analysed all available information, came to the conclusion that the Group does not have any legal or constructive obligations with respect to this assets

In 2008 Management of the Group analyzed the estimated useful lives of property, plant and equipment and consequently concluded that useful life period for pipelines should be increased from 45 years to 50 years. The effect of this change was reflected prospectively from 1 January 2008 (Refer to Note 4 and Note 8) in these consolidated financial statements. Would the Group used 45 years for depreciation of pipelines depreciation charge for the year ended 31 December 2008 would be approximately RR 84 million higher.

4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

4.1 Basis of presentation

These consolidated financial statements are prepared in accordance with, and comply with, International Financial Reporting Standards (“IFRS”).

The consolidated financial statements of the Group are prepared under the historical cost convention except as described further in Notes 4 and 6. The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.



OJSC AK TRANSNEFTPRODUCT

Notes to the IFRS Consolidated Financial Statement – 31 December 2008

(in thousands of Russian roubles unless otherwise stated)

4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

4.2 Group accounting

Subsidiary undertakings

Subsidiary undertakings that are controlled by the Group have been consolidated. Control occurs when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Minority interest at the balance sheet date represents the minority shareholders' portion of the fair values of the identifiable assets and liabilities of the subsidiary at the acquisition date, and the minorities' portion of movements in equity since the date of the combination. Minority interest is presented within equity in the consolidated financial statements.

Investments in associated undertaking

Associated undertaking is an undertaking over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence occurs when the Group has the power to participate in the financial and operating policy decisions of an entity but has no control or joint control over those policies. Associated undertaking is accounted for using the equity method.

4.3 Property, plant and equipment

Basis of valuation

All property, plant and equipment is initially recorded at historical cost, including, where appropriate, the net present value of the estimated dismantlement or removal cost of the asset at the end of its estimated useful life, less accumulated depreciation. Assets under construction are carried at historical cost and depreciated from the time when the assets are available for use by the Group.

Management approves specific plans for prospective dismantlement or decommissioning of sections of pipeline and related facilities on an annual basis and, at that time, the estimated useful life of the related asset is revised and the annual depreciation charge is amended, if applicable. In the event that a decision is made to abandon a construction project in progress or to significantly postpone its planned completion date, or if there are other indications of potential impairment, the carrying value of the asset is reviewed.

Depreciation

Depreciation is calculated on the historic amounts of property, plant and equipment on a straight-line basis. The depreciation periods, which approximate to the estimated useful economic lives of the respective assets, are as follows:

Buildings and, constructions	8-50 years
Machinery and equipment	2-20 years
Pipelines	50 years
Other	3-25 years

Disposals and liquidation

The gain or loss arising on the disposal or liquidation of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the consolidated income statement.



OJSC AK TRANSNEFTPRODUCT

Notes to the IFRS Consolidated Financial Statement – 31 December 2008

(in thousands of Russian roubles unless otherwise stated)

4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

Renewal, improvement, repairs and maintenance costs

Major renewals and improvements are capitalised and the assets replaced are retired. Major spare parts and stand-by equipment are capitalised as items of property, plant and equipment. Maintenance and repairs and minor renewals are expensed as incurred. Minor renewals include all expenditures which do not result in a technical enhancement of the asset beyond its original capability.

Borrowing costs

Interest costs on borrowings to finance the construction of property, plant and equipment are expensed as incurred.

Linefill

Oil products used for technical operation of the pipeline network (“linefill”) owned by the Group are treated as a separate component of the pipeline class of asset, which is not depreciated as its residual value exceeds its carrying amount. Any additions to linefill over the period are recognized at market value, and any disposals are recognized at the weighted average carrying value of linefill. Differences between linefill carrying value and proceeds on disposals are charged or credited to the consolidated income statement.

4.4 Provisions

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

Provisions are reassessed annually, and are included in the consolidated financial statements at their expected net present values using the discount rate appropriate to the Group in the economic environment in which assets are located at each balance sheet date.

Changes in the provisions resulting from the passage of time are reflected in the consolidated income statement for the year as financial expense. Other changes in provisions, related to a change in the expected pattern or estimated cost of settlement of the obligation, are treated as a change in accounting estimate in the period of the change by adjusting corresponding asset or expense.

The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognized as expenses immediately, following the principle of conservatism, unless they extend the life of the related property or mitigate or prevent future environmental contamination, in which case they are capitalised.

4.5 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is assigned using the weighted average method. Net realisable value is the estimated selling price in the ordinary course of business, less related selling expenses.

4.6 Financial assets – key measurement terms

The Group classifies its financial assets into the following measurement categories: (a) loans and receivables; (b) available-for-sale financial assets and (c) financial assets held to maturity.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. The group’s loans and receivables comprise ‘trade and other receivables’ and cash and cash equivalents in the balance sheet.



OJSC AK TRANSNEFTPRODUCT

Notes to the IFRS Consolidated Financial Statement – 31 December 2008

(in thousands of Russian roubles unless otherwise stated)

4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Held-to-maturity assets include quoted non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has both the intention and ability to hold to maturity. Management determines the classification of investment securities held to maturity at their initial recognition and reassesses the appropriateness of that classification at each balance sheet date.

The fair value of marketable securities and quoted investments is based on quoted market values at each balance sheet date. In assessing the fair value of securities and investments which are not publicly traded, the Group uses a variety of methods and assumptions based on market conditions and risk existing at each balance sheet date, including quoted market prices for similar investments, discounted value of estimated future cash flows, and replacement cost. Estimated cash flows are discounted at current market rates available to the Group for similar financial instruments.

Regular purchases and sales of financial assets are recognised on the trade-date – the date on which the group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of securities classified as available-for-sale are recognized in equity and shown net of respective deferred income tax in the consolidated statement of changes in equity. When securities classified as available-for-sale are sold, the accumulated fair value adjustments are included in the consolidated statement of income as gains (losses) on disposal of available-for-sale financial assets.

4.7 Accounts receivable

Accounts receivable are carried at original invoice amount (which approximates their amortized cost for short-term accounts receivable) inclusive of value added taxes less provision made for impairment. A provision for impairment is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the contract. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the market rate of interest for similar borrowers at the date of origination of the receivables.

The amount of the provision is recognized in the consolidated income statement. The primary factors that the Group considers whether a receivable is impaired are its overdue status and realisability of related collateral, if any.

The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss might have occurred:

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

4.8 Cash and cash equivalents

Cash and cash equivalents consist of cash, bank balances, and highly liquid investments which are readily convertible to known amounts of cash, subject to insignificant risk of changes in value, and which have maturities of three months or less at the date of acquisition.



4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

4.9 Deferred taxes

Deferred tax assets and liabilities are calculated in respect of temporary differences using the balance sheet liability method. Deferred income taxes are provided for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. The principal temporary differences arise from the inflationary difference resulting from the application of IAS 29 Financial Reporting in Hyperinflationary Economies (IAS 29), depreciation on property, plant and equipment, and income, provisions and expenses which are included in the consolidated income statement before they become taxable or deductible for tax purposes.

A deferred income tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and an associate, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

If the tax relates to items that are credited or charged directly to the consolidated statement of changes in equity, corresponding deferred tax is also charged or credited directly to the consolidated statement of changes in equity.

4.10 Foreign currency transactions

Items included in the financial statements of each of the Group companies are measured using the currency of the primary economic environment in which the entity operates (“the functional currency”). The functional currency for all Group companies and the presentation currency for the consolidated financial statements is the Russian rouble, (“RR”).

The results and financial position of the associated undertaking that has a functional currency different from the presentation currency adopted by the Group for these financial statements are translated into the presentation currency as follows:

- assets and liabilities in each balance sheet presented are translated at the exchange rate at the date of that balance sheet;
- income and expenses in each statement of income (and cash flows in each statement of cash flows) presented are translated at the average exchange rates for the year;
- all resulting exchange differences are recognized as a separate component of equity.

Monetary assets and liabilities held by Group entities denominated in foreign currencies are translated into RR at the exchange rate prevailing at the balance sheet date. Foreign currency transactions are accounted for at the exchange rate prevailing at the date of the transaction. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currency are recognized in the consolidated income statement.

4.11 Revenue recognition

Revenues from transportation services are recognized when the services are provided as evidenced by the delivery of oil products to the owner or the owner’s customer in accordance with the contract. Revenues from loading and storage of goods are recognized when the services have been provided. Revenues from trading in oil products are recognized upon shipment of goods to the customer, when the goods cease to be under physical control of the Group and risks of ownership have been transferred to the buyer. Revenues are shown net of value added tax and discounts.



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4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

4.12 Value added tax

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

4.13 Retirement benefit obligations

The Group makes all statutory payments, which are calculated as a percentage of current gross salary payments, to the State Pension Scheme of the Russian Federation in respect of its employees and such expense is charged to the consolidated income statement.

Any discretionary payments to retired employees are recognized as expenses in the period in which they are incurred.

4.14 Social commitments

Expenses for the support of the housing fund stipulated by agreements with local governments are provided for in accordance with the provisions of respective annual agreements. Voluntary contributions to finance and support social programs and other similar expenses are recognized as incurred.

The Group incurs costs related to the provision of benefits to employees such as health services and kindergartens. These amounts are charged to cost of sales as they are considered a cost of employment.

4.15 Share capital and dividends

Ordinary shares are classified as equity. Dividends are recognized as a liability and deducted from equity on the date on which they are approved. Dividends proposed or approved between the balance sheet date and the date of issuing the consolidated financial statements are disclosed.

4.16 Segment reporting

The Group's risks and rates of return are affected predominantly by the nature of services it provides; therefore the primary format for reporting segment information is reportable business segments. The Group is considered by management to have a single main activity and its activities comprise one business segment.

Other sales and cost of sales are shown separately in the relevant Notes, but these activities do not result in significant assets and liabilities and do not constitute a primary reportable segment as defined by IAS 14, *Segment reporting* (IAS 14).

The main activity is performed in Russian Federation. Operations of subsidiaries located in foreign countries are not significant and do not satisfy the disclosure requirements of secondary reportable segment as defined by IAS 14.

4.17 Amendments after issue

Any further changes to these consolidated financial statements require approval of the Group's Management who authorized these consolidated financial statements for issue.



4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

4.18 Recent accounting pronouncements

Three new interpretations became effective from 1 January 2008. Effective 1 January 2008 the Group adopted all of those interpretations, which are relevant to its operations. The adoption of interpretations effective 1 January 2008 did not result in substantial changes to the Group's accounting policies and financial position.

New accounting developments

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2009 or later periods and which the Group has not early adopted:

IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009). The standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organization for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

Puttable financial instruments and obligations arising on liquidation—IAS 32 and IAS 1 Amendment (effective from 1 January 2009). The amendment requires classification as equity of some financial instruments that meet the definition of a financial liability. The Group does not expect the amendment to affect its consolidated financial statements.

In 2007, an amendment to IAS 23 Borrowing costs ("IAS 23") was made with an effective date of periods after 1 January 2009. The amendment removes the option of immediately recognizing as an expense borrowing costs that relate to assets that take substantial period of time to get ready for use or sale. Accordingly, the Group's accounting policy for Property, plant and equipment – Borrowing costs is expected to change upon adoption.

IAS 1, Presentation of Financial Statements (revised September 2007; effective for annual periods beginning on or after 1 January 2009). The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which will also include all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities will be allowed to present two statements: a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The Group expects the revised IAS 1 to affect the presentation of its financial statements but to have no impact on the recognition or measurement of specific transactions and balances.

IAS 27, Consolidated and Separate Financial Statements (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

IFRS 3, Business Combinations (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed.



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4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

Instead, goodwill will be measured as the difference at acquisition date between the fair value of any investment in the business held before the acquisition, the consideration transferred and the net assets acquired. Acquisition-related costs will be accounted for separately from the business combination and therefore recognized as expenses rather than included in goodwill. An acquirer will have to recognize at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognized in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

Vesting Conditions and Cancellations—Amendment to IFRS 2, Share-based Payment (issued in January 2008; effective for annual periods beginning on or after 1 January 2009). The amendment clarifies that only service conditions and performance conditions are vesting conditions. Other features of a share-based payment are not vesting conditions. The amendment specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment. The Group does not expect the amendment to affect its consolidated financial statements.

On 13 October 2008, the IASB issued amendments to IAS 39 Financial Instruments: Recognition and Measurement and IFRS 7 Financial Instruments: Disclosures that, under limited circumstances, permit the reclassification of certain financial assets previously classified as 'held for trading' or 'available for sale' to another category of financial assets. The amendments have an effective date of 1 July 2009. The Group is currently assessing the impact of the amendment on its consolidated financial statements.

IFRIC 13, Customer Loyalty Programmes (issued in June 2007; effective for annual periods beginning on or after 1 July 2008). IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. IFRIC 13 is not relevant to the Group's operations because no Group companies operate any loyalty programmes.

IFRIC 15, Agreements for the Construction of Real Estate (effective for annual periods beginning on or after 1 January 2009). The interpretation applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors, and provides guidance for determining whether agreements for the construction of real estate are within the scope of IAS 11 or IAS 18. It also provides criteria for determining when entities should recognize revenue on such transactions. The Group does not expect the amendment to affect its consolidated financial statements.

IFRIC 16, Hedges of a Net Investment in a Foreign Operation (effective for annual periods beginning on or after 1 October 2008). The interpretation explains which currency risk exposures are eligible for hedge accounting and states that translation from the functional currency to the presentation currency does not create an exposure to which hedge accounting could be applied. The IFRIC allows the hedging instrument to be held by any entity or entities within a group except the foreign operation that itself is being hedged. The interpretation also clarifies how the gain or loss recycled from the currency translation reserve to profit or loss is calculated on disposal of the hedged foreign operation. Reporting entities will apply IAS 39 to discontinue hedge accounting prospectively when their hedges do not meet the criteria for hedge accounting in IFRIC 16. IFRIC 16 does not have an impact on these consolidated financial statements as the Group does not apply hedge accounting.

Improvements to International Financial Reporting Standards (issued in May 2008). In 2007, the International Accounting Standards Board decided to initiate an annual improvements project as a method of making necessary, but non-urgent, amendments to IFRS. The amendments issued in May 2008 consist of a mixture of substantive changes, clarifications, and changes in terminology in various standards. The substantive changes relate to the following areas: classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary; possibility of presentation of financial instruments held for trading as non-current under IAS 1; accounting for sale of IAS 16 assets which were previously held for rental and classification of the related cash flows under IAS 7 as cash flows from operating activities; clarification of definition of a curtailment under IAS 19; accounting for below market interest rate government loans in accordance with IAS 20; making the definition of borrowing costs in IAS 23 consistent with the effective interest method; clarification of accounting for subsidiaries held for sale under IAS 27 and IFRS 5; reduction in the disclosure requirements relating to associates and joint ventures under IAS 28 and IAS 31; enhancement of disclosures required by IAS 36; clarification of accounting for advertising costs under IAS 38; amending the definition of the fair value through profit or loss category to be consistent with hedge accounting under IAS 39;



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4. BASIS OF PRESENTATION AND ACCOUNTING POLICIES (CONTINUED)

introduction of accounting for investment properties under construction in accordance with IAS 40; and reduction in restrictions over manner of determining fair value of biological assets under IAS 41. Further amendments made to IAS 8, 10, 18, 20, 29, 34, 40, 41 and to IFRS 7 represent terminology or editorial changes only, which the IASB believes have no or minimal effect on accounting. The Group does not expect the amendments to have any material effect on its consolidated financial statements.

IFRIC 17, Distribution of Non-Cash Assets to Owners (effective for annual periods beginning on or after 1 July 2009). The amendment clarifies when and how distribution of non-cash assets as dividends to the owners should be recognized. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets will be recognized in profit or loss when the entity settles the dividend payable. IFRIC 17 is not relevant to the Group's operations because it does not distribute non-cash assets to owners.

IFRS 1, First-time Adoption of International Financial Reporting Standards (following an amendment in December 2008, effective for the first IFRS financial statements for a period beginning on or after 1 July 2009). The revised IFRS 1 retains the substance of its previous version but within a changed structure in order to make it easier for the reader to understand and to better accommodate future changes. The Group concluded that the revised standard does not have any effect on its financial statements.

IFRIC 18, Transfers of Assets from Customers (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers. IFRIC 18 is not expected to have any impact on the Group's financial statements.

Improving Disclosures about Financial Instruments - Amendment to IFRS 7, Financial Instruments: Disclosures (issued in March 2009; effective for annual periods beginning on or after 1 January 2009). The amendment requires enhanced disclosures about fair value measurements and liquidity risk. The entity will be required to disclose an analysis of financial instruments using a three-level fair value measurement hierarchy. The amendment (a) clarifies that the maturity analysis of liabilities should include issued financial guarantee contracts at the maximum amount of the guarantee in the earliest period in which the guarantee could be called; and (b) requires disclosure of remaining contractual maturities of financial derivatives if the contractual maturities are essential for an understanding of the timing of the cash flows. An entity will further have to disclose a maturity analysis of financial assets it holds for managing liquidity risk, if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk. The Group is currently assessing the impact of the amendment on disclosures in its financial statements.

Embedded Derivatives - Amendments to IFRIC 9 and IAS 39 (effective for annual periods ending on or after 30 June 2009). The amendments clarify that on reclassification of a financial asset out of the 'at fair value through profit or loss' category, all embedded derivatives have to be assessed and, if necessary, separately accounted for. The amendments are not expected to have any impact on the Group's financial statements.

5. CHANGES IN OPENING BALANCE AND COMPARATIVE INFORMATION

Until 2008 the Group accounted for revaluation of marketable available-for-sale financial assets through profits and losses for the period as impact of revaluation of the given category of financial assets on equity of the Group was not considerable. In 2008 in connection with significant decline in fair value of the given category of financial assets such effect was reclassified to «Other reserves» line in equity of the Group in accordance with reassessment of IAS 39. As a consequence the opening balance as at 31 December 2007 was reclassified. Also the Group has reassessed impact of taxable temporary differences related to accumulated reserve of revaluation of marketable available-for-sale financial assets and as a consequence additional deferred tax liability amounted to RR 28,332 was recognized at 31 December 2007. The effect of recalculation on balance at 31 December 2007 and profit for the year ended 31 December 2007 is not material and shown in tables below:

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5. CHANGES IN OPENING BALANCE AND COMPARATIVE INFORMATION (CONTINUED)

	31 December 2007 (as presented)	31 December 2007 (restated)	Increase/ (decrease)
EQUITY AND LIABILITIES			
Equity attributable to Company's equity holder			
Retained earnings	38,233,206	38,064,300	(168,906)
Other reserves	-	140,574	140,574
Total equity attributable to Company's equity holder	38,858,182	38,829,850	(28,332)
Minority interest	568,280	568,280	-
Total equity	39,426,462	39,398,130	(28,332)
Non-current liabilities			
Deferred tax liabilities	2,358,002	2,386,334	28,332
Total non-current liabilities	22,946,189	22,974,521	28,332
Total liabilities	26,685,839	26,714,171	28,332

	Year ended 31 December 2007 (as presented)	Year ended 31 December 2007 (restated)	Increase/ (decrease)
Net other operating income/(expenses)	925,223	911,404	(13,819)
Operating profit	7,317,921	7,304,102	(13,819)
Profit before profit tax	6,604,793	6,590,974	(13,819)
Profit tax expense	(1,776,840)	(1,782,352)	(5,512)
Profit for the year	4,827,953	4,808,622	(19,331)

6. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

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

Useful lives of property, plant and equipment

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



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6. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

Impairment of assets

At each balance sheet date the Group assesses whether there is any indication that the recoverable amount of the Group's assets has declined below the carrying value. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. When such a decline is identified, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recorded in the consolidated statement of income in the period in which the reduction is identified. If conditions change and management determines that the asset value has increased, the impairment provision will be fully or partially reversed.

Accounting for impairment includes provisions against construction projects, investments, including investments in the Group's associated undertaking, unrecoverable accounts receivable and inventory obsolescence. The Group records impairment when its assessments indicate that it is probable that an asset will not be recovered, and an amount can be reasonably estimated. Actual results may vary from the estimates, and the Group's estimates can be revised in the future, either negatively or positively, depending upon the outcome or expectations based on the facts surrounding each exposure.

Dismantlement provision

Provision is established for the expected cost of dismantling parts of the operated pipeline network based on the average current cost per kilometre of removal according to an estimated plan of replacement over the long term. The provision calculation is based on the assumption that dismantlement activities are expected to cover the same number of kilometres each year over the useful life of the network. Changes in this assumption or assumptions with regard to expected costs, technical change, and discount rate may result in adjustments to the established provisions and assets.

The Group's estimates for provision for dismantlement are based on currently available facts and the Group's estimates of the ultimate outcome or resolution of the liability in the future. Actual results may differ from the estimates, and the Group's estimates can be revised in the future, either negatively or positively, depending upon the outcome or expectations based on the facts surrounding each exposure.

Group provides for prospective dismantlement or decommissioning of specific underground storage reservoirs, pipelines and related infrastructure which were taken out of operation before 2008. Estimating the amounts and timing of those obligations that should be recorded requires significant judgment. This judgment is based on anticipated cost using currently available technology, timing of the dismantlement in accordance with the Group's current and long-term plans and is based on current economic conditions. Should the average current cost of dismantlement per reservoir increase by 100%, profit of the Group for the year ended 31 December 2008 would be RR 139,344 lower (2007: RR 112,576)

Tax legislation

Russian tax and customs legislation is subject to varying interpretations (see Note 23).

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7. STRUCTURE OF THE GROUP AND INVESTMENTS

The consolidated subsidiaries and an associate of the Company at 31 December 2008 and at 31 December 2007 are as follows:

Name	Country of incorporation	Percentage of ownership
Consolidated subsidiaries		
OAo Mostransnefteproduct	Russia	100
OAo Yugo-Zapad transnefteproduct	Russia	100
OAo Sredne-Volzhsytransnefteproduct	Russia	100
OAo Peterburgtransnefteproduct	Russia	100
OAo Ryazantransnefteproduct	Russia	100
OAo Severo-Kavkazsky transnefteproduct	Russia	100
OAo Sibtransnefteproduct	Russia	100
OOO Balttransnefteproduct	Russia	100
OOO ChOP Spetstransnefteproduct	Russia	100
OAo Trade House transnefteproduct	Russia	100
OAo Telecomnefteproduct	Russia	100
OAo Podvodspetstransnefteproduct	Russia	100
OAo Institute Nefteproductproect	Russia	100
OOO Sot-Trans	Russia	100
OOO BalttransServis	Russia	100
ChUP Zapad-Transnefteproduct	Belarus	100
DP Prikarpatzapadtrans	Ukraine	100
DP Rovensky Tsekhn Elektrosvyazi	Ukraine	100
ChUP Zapad-Telecomnefteproduct	Belarus	100
OOO OP Spetstransnefteproduct Severo-Zapad	Russia	100
OOO ChOP Spetstransnefteproduct	Russia	100
OOO ChOP Spetstransnefteproduct – Ryazan	Russia	100
OOO ChOP Spetstransnefteproduct – Ural	Russia	100
OOO Spetstransnefteproduct – Yugo-Zapad	Russia	100
OOO Spetstransnefteproduct – Zapad	Russia	100
OOO ChOP Spetstransnefteproduct – Sibir	Russia	100
OOO ChOP Spetstransnefteproduct – Kstovo	Russia	100
OOO Spetstransnefteproduct – Volga	Russia	100
OOO ChOP Spetstransnefteproduct – Yaroslavl	Russia	100
OAo Uraltransnefteproduct	Russia	86.2
Equity accounted associated undertaking		
SIA LatRosTrans	Latvia	34

Minority interests represent a 13.8% share at 31 December 2008 and 31 December 2007 in the consolidated subsidiary OAo Uraltransnefteproduct held by the Ministry of Land and Property Relations of the Republic of Bashkortostan (former State Committee of the Republic of Bashkortostan for Administration of State Property).

Investment in associated undertaking

	31 December 2008	31 December 2007
At the beginning of the period	587,048	680,947
Loss for the period	(138,837)	(112,476)
Currency translation differences	70,367	18,577
At the end of the period	518,578	587,048

Carrying amount of investment in SIA LatRosTrans is shown net of impairment provision of RR 1,749,146 as at 31 December 2008 and RR 1,523,462 as at 31.12.2007 (the amount of provision in Latvian lat was LVL 29,729 at 31 December 2008 and 2007, difference was caused only by foreign exchange rate changes).



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7. STRUCTURE OF THE GROUP AND INVESTMENTS (CONTINUED)

Summarised financial information of an associate at 31 December 2008 and 31 December 2007 and for the years then ended is as follows:

Year	Name	Country of incorporation	Assets	Liabilities	Revenue	Loss for the year
2007	SIA LatRosTrans	Latvia	5,617,089	43,046	491,700	330,812
2008	SIA LatRosTrans	Latvia	6,015,160	72,546	379,403	408,345

Management of the Group at each balance sheet date assesses whether there is an indication that an impairment provision in relation to SIA LatRosTrans property, plant and equipment, which was recognised in the Group consolidated financial statements in prior years in order to reduce investments to their estimated recoverable amount may no longer exist or may have decreased or increased. Have analysed all the available information management concluded that the impairment provision at 31 December 2008 should not be changed.

Currency translation reserve

The conversion of SIA LatRosTrans' financial statements into Russian roubles results in a currency translation reserve.

The cumulative effects of the movements in foreign exchange rates and the associated deferred taxation at the end of each year are shown below:

	31 December 2008	31 December 2007
Exchange rates	(1,043,668)	(1 114 035)
Deferred taxation	208,735	267,369
Currency translation reserve	(834,933)	(846,666)

The exchange rates of the Central Bank of the Russian Federation at 31 December 2008 and 31 December 2007 were RR 58.84 and RR 51.25 per 1 Latvian Lat, respectively.

Available-for-sale financial assets

	31 December 2008	31 December 2007
Long-term financial assets		
Marketable securities	82 395	195 099
Investments in other Russian companies and banks	90 662	9 883
	173 057	204 982
Short-term financial assets		
Marketable securities	-	24 301
	-	24 301

Marketable securities include investments in corporate shares and government currency bonds. Government currency bonds are nominated in US dollars.



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8. PROPERTY, PLANT AND EQUIPMENT

	Buildings and construc- tions	Machinery and equipment	Pipelines	Linefill	Assets under construction including prepayments	Other	TOTAL
Cost at 1 January 2007	9,337,160	7,820,449	21,224,998	5,216,891	21,979,539	412,531	65,991,568
Additions	-	-	-	3,329,463	9,912,028	-	13,241,491
Transfers	3,786,806	1,665,325	4,144,670	-	(9,618,177)	21,376	-
Disposals	(96,627)	(158,929)	(126,012)	(860,166)	-	(7,043)	(1,248,777)
Cost at 31 December 2007	13,027,339	9,326,845	25,243,656	7,686,188	22,273,390	426,864	77,984,282
Accumulated depreciation and impairment at 1 January 2007	(4,602,099)	(5,001,999)	(12,082,402)	-	-	(222,208)	(21,908,708)
Depreciation for the period	(317,928)	(642,484)	(404,647)	-	-	(42,791)	(1,407,850)
Change in impairment provision	(12,944)	1,458	-	-	-	(2)	(11,488)
Disposals	76,758	148,118	109,650	-	-	5,000	339,526
Accumulated depreciation and impairment at 31 December 2007	(4,856,213)	(5,494,907)	(12,377,399)	-	-	(260,001)	(22,988,520)
Net book value at 1 January 2007	4,735,061	2,818,450	9,142,596	5,216,891	21,979,539	190,323	44,082,860
Net book value at 31 December 2007	8,171,126	3,831,938	12,866,257	7,686,188	22,273,390	166,863	54,995,762
Cost at 1 January 2008	13,027,339	9,326,845	25,243,656	7,686,188	22,273,390	426,864	77,984,282
Additions	-	-	-	311,386	4,701,747	-	5,013,133
Change in dismantlement provision (Note 16)	5,353	-	2,503,489	-	-	-	2,508,842
Transfers	9,139,819	3,053,842	12,065,404	-	(24,376,237)	117,172	-
Disposals	(98,266)	(154,702)	(436,843)	(268,043)	-	(9,096)	(966,950)
Cost at 31 December 2008	22,074,245	12,225,985	39,375,706	7,729,531	2,598,900	534,940	84,539,307
Accumulated depreciation and impairment at 1 January 2008	(4,856,213)	(5,494,907)	(12,377,399)	-	-	(260,001)	(22,988,520)
Depreciation for the period	(705,881)	(930,002)	(515,046)	-	-	(38,550)	(2,189,479)
Change in impairment provision	939	394	-	-	-	4	1,337
Disposals	62,081	148,917	413,916	-	-	6,789	631,703
Accumulated depreciation and impairment at 31 December 2008	(5,499,074)	(6,275,598)	(12,478,529)	-	-	(291,758)	(24,544,959)
Net book value at 31 December 2008	16,575,171	5,950,387	26,897,177	7,729,531	2,598,900	243,182	59,994,348



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8. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The assets transferred to the Group companies upon privatisation did not include the land on which the Group's buildings and constructions, and under which its pipelines, are located. Many of the assets are situated on land which is leased for an indefinite period from federal, regional and municipal authorities. The rights to use the tracts of land under which pipelines are located are typically contained in similar leases of indefinite duration, or in some cases are not presently defined in any legal documents. The Group companies have the option to purchase or lease this land upon application to the state registration body or to continue occupying this land under a rental agreement. This option should be exercised by 1 January 2010 (for pipelines – until 1 January 2013) in accordance with the state law (Federal law № 212-FZ issued 24 July 2007).

In 2008 Management of the Group analyzed the estimated useful lives of property, plant and equipment and consequently concluded that useful life period for pipelines should be increased from 45 years to 50 years. The effect of this change was reflected prospectively from 1 January 2008 (Refer to Note 3 and Note 4) in these consolidated financial statements. Would the Group used 45 years for depreciation of pipelines depreciation charge for the year ended 31 December 2008 would be approximately RR 84 million higher.

9. INVENTORIES

	31 December 2008	31 December 2007
Materials and supplies	409,638	347,666
Oil products for resale	32,379	120,963
Other	31,257	15,832
	473,274	484,461

10. TRADE AND OTHER RECEIVABLES

	31 December 2008	31 December 2007
Long-term receivables		
Non-financial receivables		
Long-term recoverable VAT	-	168,570
	-	168,570
Financial receivables		
Other receivables	79,882	79,851
	79,882	79,851
	79,882	248,421
	31 December 2008	31 December 2007
Current receivables		
Financial receivables		
Trade receivables	160,053	77,410
Other receivables	160,946	98,118
	320,999	175,528
Non-financial receivables		
Advances to suppliers	257,006	160,547
Profit tax assets	931,016	296,456
Other tax assets	14,661	17,031
	1,202,683	474,034
	1,523,682	649,562

Receivables are stated net of a provision for impairment of RR 34,071 at 31 December 2008 (31 December 2007 – RR 34,252).

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10. TRADE AND OTHER RECEIVABLES (CONTINUED)

The provision for impairment of accounts receivable was calculated based on analysis of collectability. The movement of the provision is shown in the table below:

	Year ended 31 December 2008		Year ended 31 December 2007	
	Trade receivables	Other receivables	Trade receivables	Other receivables
As at 1 January	13,679	20,573	24,070	16,361
Reversal of provision	(12,851)	(3,801)	(12,361)	(1,573)
Accrued provision	742	15,729	1,970	5,785
At the period end	1,570	32,501	13,679	20,573

Management has determined the provision for impairment of accounts receivable based on specific customer identification, customer payment trends, subsequent receipts and settlements and analysis of expected future cash flows.

According to the analysis of accounts receivable in respect to the payment dates the Group has the following overdue balances not included in the provision for accounts receivable as at 31 December 2008 and 31 December 2007:

Overdue period	31 December 2008		31 December 2007	
	Trade receivables	Other receivables	Trade receivables	Other receivables
Less than 90 days	19,567	1,678	4,437	886
More than 90 days but less than 365 days	22,095	4,869	3,963	1,185
Over 365 days	1,872	8,439	27,323	6,617
	43,534	14,986	35,723	8,688

Management of the Group believes that Group entities will be able to realize the net receivable amount through direct collections and other non-cash settlements, and therefore the recorded value of accounts receivable approximates their fair value.

Breakdown of accounts receivable by currency both for long-term and short-term balances is presented in the tables below:

Long-term receivables	RUR	BYR*	UAH**	Other	Total
31 December 2008					
other receivables	76,836	1,564	509	973	79,882
	76,836	1,564	509	973	79,882
31 December 2007					
other receivables	77,108	1,066	1,085	592	79,851
	77,108	1,066	1,085	592	79,851

* BYR – hereinafter Belorussian rouble

** UAH – hereinafter Ukrainian hryvnya

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10. TRADE AND OTHER RECEIVABLES (CONTINUED)

Short-term receivables	USD	RUR	BYR	UAH	Other	Total
31 December 2008						
trade receivables	24,944	42,682	87,165	4,997	265	160,053
other receivables	5	146,890	4,137	7,017	2,897	160,946
	24,949	189,572	91,302	12,014	3,162	320,999
31 December 2007						
trade receivables	3,679	71,670	507	1,554	-	77,410
other receivables	1,305	89,857	2,005	2,860	2,091	98,118
	4,984	161,527	2,512	4,414	2,091	175,528

Recoverable VAT

Short-term recoverable VAT of RR 3,556,108 at 31 December 2008 (RR 6,091,395 – 31 December 2007) includes VAT related to purchases of materials and services used for construction of property, plant and equipment, RR 1,718,538 of which in accordance with the Tax Code of the Russian Federation was reclaimed from budget through tax returns but was not physically settled as at the reporting date.

11. CASH AND CASH EQUIVALENTS

	31 December 2008	31 December 2007
Cash in banks and at hand	3,306,668	1,451,613
Deposits	2,419,187	1,374,756
	5,725,855	2,826,369

Balance of cash and cash equivalents as at 31 December 2008 includes short-term bank deposits mainly denominated in USD. As at 31 December 2008 deposits were placed mainly with Vneshtorgbank (VTB) for less than 1 month. As at 31 December 2007 deposits were placed mainly with MDM-Bank for less than 1 month.

RR 2,397,646 of cash are denominated in US dollars at 31 December 2008 (RR 254,078 – 31 December 2007). RR 1,072 of cash are denominated in euro at 31 December 2008 (RR 934 – 31 December 2007).

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11. CASH AND CASH EQUIVALENTS (CONTINUED)

Bank	Currency	Deposit interest rate, % p.a.	31 December 2008	31 December 2007
VTB	USD	4	1,116,455	-
VTB	USD	4.9	1,028,314	-
VTB	USD	9	14,685	-
VTB	RUR	0.9	106,900	208,000
VTB	RUR	0.8	75,000	-
VTB	RUR	0.7	-	97,800
VTB	RUR	0.6	-	46,960
VTB	RUR	0.08	53,000	-
MDM-Bank	RUR	11	15,000	-
MDM-Bank	RUR	5.5	-	1,000,000
Finance and Kredit	UAH	14.2	4,048	5,065
Indeks-Bank	UAH	14.1	-	1,206
Prominvestbank	UAH	17	5,785	-
Prominvestbank	UAH	14	-	8,200
Prominvestbank	UAH	13	-	7,235
Kredit-Bank	UAH	13.5	-	290
			2,419,187	1,374,756

12. SHARE CAPITAL

	Nominal value, RR thousand	Amounts per Balance sheet	
		31 December 2008	31 December 2007
Authorized, issued and fully paid ordinary shares of par value RR 1 each			
1,263,952,668 shares	1,263,953	1,471,642	1,471,642

Dividends

No dividends for 2007 year were distributed by the decision made at the General Shareholders Meeting held in June 2008.

In June 2007, the following dividends were approved at the General Shareholders Meeting for the year ended 31 December 2006:

	Russian roubles per share	Total
Ordinary shares	0.08	100,000
		100,000

The dividends were paid in July 2007.



OJSC AK TRANSNEFTPRODUCT

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13. BORROWINGS AND LOANS

Long-term borrowings and loans

	Currency	31 December 2008	31 December 2007
Secured borrowings and loans	USD	21,703,889	18,671,343
Unsecured borrowings and loans	RUR	2,537,263	2,529,794
Total borrowings and loans		24,241,152	21,201,137
Less: current portion of borrowings and loans		(7,598,077)	(1,038,385)
		16,643,075	20,162,752
Maturity of non-current borrowings and loans			
Due for repayment, based on discounted contractual cash flows:			
One to two years from the balance sheet date		4,622,506	6,346,784
Two to five years from the balance sheet date		12,020,569	11,585,807
After five years from the balance sheet date		-	2,230,161
		16,643,075	20,162,752

Secured borrowings and loans

In October 2005 the Company signed a long-term loan facility of USD 753 million from the Bank of International Trade, of which USD 753 million had been drawn by 31 December 2007. The loan was used for the financing of the Project “North”. In terms of the loan agreement the security means the right of the bank to write-off cash from the Company's account in case of delay in the loan repayment. The loan bears interest at an annual rate of 10%, which is paid quarterly. The loan was repayable by April 2013 in 19 quarterly instalments starting October 2008. On 27 April 2009 the Company has amended loan agreement and repayment schedule was changed (see Note 25). The outstanding liability as at 31 December 2008 in amount of RR 21,703,889 is included in these consolidated financial statements. This amount includes RR 438,298 of interest payable.

Unsecured borrowings and loans

In April 2007 the Company signed a long-term loan facility of RR 2,500 million from the White Nights Finance B.V., of which RR 2,500 million had been drawn by 31 December 2007. The above loan was received in connection with the issuance of RR 2,500 million of Credit Linked Notes due October 2009 issued by Nights Finance B.V. at an interest rate of 8.15% which is paid half-yearly. The loan was used for the financing of the Project “North”. The outstanding liability as at 31 December 2008 in amount of RR 2,537,263 is included in these consolidated financial statements. This amount includes RR 44,146 of interest payable.

14. PAYABLES AND ADVANCES FROM CUSTOMERS

	31 December 2008	31 December 2007
Financial liabilities		
Trade payables	554,886	887,307
	554,886	887,307
Non-financial liabilities		
Advances from customers	1,867,471	1,119,375
Wages payable	62,865	100,502
Other payables	320,812	381,639
	2,251,148	1,601,516
	2,806,034	2,488,823

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14. PAYABLES AND ADVANCES FROM CUSTOMERS (CONTINUED)

Breakdown of accounts payable by currency is presented in the table below:

	USD	RUR	BYR	UAH	Other	Total
31 December 2008						
trade payables	29	506,908	42,693	5,182	73	554,886
	29	506,908	42,693	5,182	73	554,886
31 December 2007						
trade payables	3,844	869,314	8,765	5,340	44	887,307
	3,844	869,314	8,765	5,340	44	887,307

15. PROFIT TAX AND OTHER TAX LIABILITIES

Taxes payable were as follows:

	31 December 2008	31 December 2007
Payroll taxes	46,703	26,934
VAT	165,371	59,087
Property tax	39,614	17,585
Personal income tax (as tax agent)	12,081	18,914
Profit tax	30,853	52,690
Other taxes and charges payable	12,417	14,404
	307,039	189,614

Profit tax (benefit)/expense was as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Current profit tax expense	328,759	2,120,559
Deferred profit tax benefit – origination and reversal of temporary differences	(599,297)	(338,207)
	(270,538)	1,782,352

The following is a reconciliation of theoretical profit tax expense computed at the statutory tax rate to the actual income before tax:

	Year ended 31 December 2008	Year ended 31 December 2007
Profit before profit tax	386,295	6,590,974
Theoretical profit tax at 24%	92,711	1,581,834
Increase/(reduction) due to:		
Effect of reduction in tax rate to 20% enacted in 2008 with effect from 1 January 2009	(363,307)	-
Correction of profit tax of previous years	(160,909)	-
Penalties on profit tax	6,523	-
Non-taxable income	(55,030)	(38,056)
Non-taxable expenses	177,384	204,070
Other reconciling items	32,090	34,504
Profit tax (income)/expense	(270,538)	1,782,352

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15. PROFIT TAX AND OTHER TAX LIABILITIES (CONTINUED)

Deferred tax liabilities and assets consist of the following:

	31 December 2008	Changes in equity	Profit/(loss)	1 January 2008
Tax effects of taxable temporary differences:				
Property, plant and equipment	2,567,159	-	(164,418)	2,402,741
Inventories and revenue recognition	12,295	-	(6,645)	5,650
Long-term investments	91,085	(29,496)	129,134	190,723
Tax effects of deductible temporary differences:				
Tax loss carryforward	(184,126)	-	184,126	-
Impairment of assets	(55,758)	-	809	(54,949)
Dismantlement provision	(580,708)	-	473,125	(107,583)
Other	(33,414)	-	(16,834)	(50,248)
Net deferred tax liability	1,816,533	(29,496)	599,297	2,386,334

	31 December 2007	Changes in equity	Profit/(loss)	1 January 2007
Tax effects of taxable temporary differences:				
Property, plant and equipment	2,402,741	-	270,370	2,673,111
Inventories and revenue recognition	5,650	-	6,620	12,270
Long-term investments	190,723	(7,775)	26,239	209,187
Tax effects of deductible temporary differences:				
Impairment of assets	(54,949)	-	18,965	(35,984)
Dismantlement provision	(107,583)	-	1,670	(105,913)
Other	(50,248)	-	14,342	(35,906)
Net deferred tax liability	2,386,334	(7,775)	338,206	2,716,765

Most companies of the Group were subject to tax rates of 24% on taxable profits for both 2008 and 2007. Deferred tax assets and liabilities are measured at the rate of 20% as at 31 December 2008 and at the rate of 24% as at 31 December 2007.

On the 26 November 2008 by the legislation of the Russian Federation was enacted reduction of the statutory income tax rate from 24 percent to 20 percent. Since this reduction in the statutory income tax rate was enacted prior to 31 December 2008, the effect of the change reduced net deferred liability by RR 363,307 which has been recognized in these consolidated financial statements.

The Group has not recognized a deferred tax liability in respect of RR 8,952,046 (2007: RR 8,582,569) of taxable temporary differences associated with its investments in subsidiaries as the Company is able to control the timing of their reversal and does not believe they will reverse in the foreseeable future.



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16. PROVISIONS FOR LIABILITIES AND CHARGES

Dismantlement provision

	Year ended 31 December 2008	Year ended 31 December 2007
At 1 January	448,263	441,306
Additions to property, plant and equipment (Note 8)	2,508,842	-
Changes in estimates	(92,718)	-
Utilisation	(10,224)	-
Unwinding of the present value discount (Note 21)	49,376	6,957
At 31 December	2,903,539	448,263
Including:		
Short-term	106,505	22,828
Long-term	2,797,034	425,435

The cost of dismantlement is added to the cost of property, plant and equipment and depreciated over the useful economic life of the pipeline network.

Additional provisions are made when the total length of the network increases and reductions occur when sections of the pipeline are decommissioned. Other changes are made when the expected pattern or unit cost of dismantlement is changed. The expected costs at the dates of dismantlement have been discounted to net present value using a nominal rate 9.7% per year (31 December 2007 – 7.0% per year).

17. SALES

	Year ended 31 December 2008	Year ended 31 December 2007
Oil products transportation	16,077,556	13,866,849
Trading in oil products	503,675	354,099
Loading services	521,109	393,959
Storage services	420,732	530,148
Throughput and handling operations	504,018	-
Other revenue	424,461	606,693
	18,451,551	15,751,748

Other revenue includes mainly pre-project engineering works, rent and commission fees.

Tariff structure

The Group's revenue from oil products transportation services is derived from distance-related tariffs, which are denominated and payable in RR and revised periodically after approval by the Federal Tariffs Service for transportation of oil products to destinations in Russia, Belarus and Ukraine on the pipeline networks in those countries. The tariffs set by the Federal Tariffs Service represent the maximum amount that may be charged for each journey, and actual tariffs are frequently lower.

The actual tariffs are calculated based on total operating costs calculated in accordance with RAS (russian accounting standards), with certain exclusions, based on normal levels of activity and profit margin.

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18. COST OF SALES

	Year ended 31 December 2008	Year ended 31 December 2007
Staff costs:		
Wages and salaries	2,856,119	2,077,885
Unified Social Fund contributions	701,346	523,239
Depreciation	2,102,230	1,319,735
Fuel and electricity	1,494,795	1,194,060
Materials and supplies	868,390	762,268
Third party repair, maintenance and diagnostic	882,420	540,557
Purchase of oil products	492,749	336,348
Social expenses	130,402	185,135
Telecommunication services	123,051	108,697
Business trip expenses	119,883	105,640
Rent payments	184,005	91,781
Taxes other than profit tax:		
Property tax	143,567	98,439
Land royalty	21,782	16,164
Other taxes and charges	100,271	122,284
Insurance services	82,411	83,889
Other	482,397	413,413
	10,785,818	7,979,534

Taxes included in cost of sales are calculated on amounts prepared in accordance with RAS. Property tax is assessed at a maximum of 2.2% for 2008 and 2007 on the average annual net book value of property, plant and equipment. Specific legislation provides for the exclusion of trunk pipelines from the taxable base.

19. GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December 2008	Year ended 31 December 2007
Staff costs:		
Salaries and bonuses of management personnel	1,160,912	871,791
Unified Social Fund contributions	164,923	143,714
Depreciation	55,688	61,167
Legal and consulting services	103,550	70,942
Telecommunication services	33,482	27,942
Other administrative costs	232,770	203,960
	1,751,325	1,379,516

20. NET OTHER OPERATING INCOME/(EXPENSES)

	Year ended 31 December 2008	Year ended 31 December 2007
Change in impairment provision on financial assets	(11,607)	50,759
Gain/(loss) on property, plant and equipment disposals	(45,093)	1,209,897
Change in provision for impairment of fixed assets	1,336	(11,488)
Change in dismantlement provision	102,942	-
Other operating expenses	(12,663)	(337,764)
	34,915	911,404

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21. OTHER FINANCIAL INCOME/OTHER FINANCIAL EXPENSE

Other financial income for the year ended 31 December 2008 was interest income in amount of RR 101,965 (for the year ended 31 December 2007 – RR 87,160).

Other financial expenses for the year ended 31 December 2008 and 2007 were as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Interest expense on borrowings and loans	2,143,766	1,851,181
Unwinding of discount in provisions (Note 16)	49,376	6,957
	2,193,142	1,858,138

22. FINANCIAL INSTRUMENTS AND FINANCIAL RISK

The accounting policies for financial instruments have been applied to the items below:

	Loans and receivables	Available-for-sale financial assets
Assets as per balance sheet		
31 December 2008		
Cash and cash equivalents (see Note 11)	5,725,855	-
Available-for-sale financial assets (see Note 7)	-	173,057
Accounts receivable (see Note 10)	400,881	-
	6,126,736	173,057
31 December 2007		
Cash and cash equivalents (see Note 11)	2,826,369	-
Available-for-sale financial assets (see Note 7)	-	229,283
Accounts receivable (see Note 10)	255,379	-
	3,081,748	229,283
	Financial liabilities as at 31 December 2008	Financial liabilities as at 31 December 2007
Liabilities as per balance sheet		
Accounts payable (see Note 14)	554,886	887,307
Borrowings and loans (see Note 13)	24,241,152	21,201,137
	24,796,038	22,088,444

Financial risk factors

The Group's activities expose it to a variety of financial risks, including the effects of changes in foreign currency exchange rates, changes in interest rates, and the collectability of receivables.

Credit risk

The Group's policy is to place cash and cash equivalents with banks which are considered to have a minimum risk of default. Its trade accounts receivable are unsecured, and the largest single credit exposure related to advances paid for construction materials (based on combined figures of accounts receivable from and advances to the same entity) at 31 December 2008 was RR 173,947 (at 31 December 2007 - RR 199,568).

Financial assets with potential credit risk include mainly trade receivables. The Group has developed procedures for ensuring that goods and services are sold only to customers having an appropriate credit history. Most sales are on an

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22. FINANCIAL INSTRUMENTS AND FINANCIAL RISK (CONTINUED)

advance payment basis. The maximum credit exposure is limited to cash and cash equivalents and accounts receivable. The Group has no material concentration of credit risk. Although the collection of receivables may be affected by economic factors, management believes that there is no significant risk of loss in excess of the impairment provisions included in the consolidated financial statements.

The cash has been deposited in the financial institutions with minimal exposure to the default risk at the time of account opening.

Credit risk is managed on a Group basis. For wholesale customers there is no independent rating and therefore Group assesses the credit quality of the customer, taking into account its financial position, past experience and other factors.

The tables below show the balances of the ten major counterparties and three major banks at the balance sheet dates:

Narrative	Rating at 31 December 2008	Rating agency	Currency	31 December 2008
Accounts receivable and prepayments				
OA0 "Trest Uralneftegazstroy"	unrated	-	RUR	173,947
OOO "ESTA-MSK"	unrated	-	RUR	112,864
OA0 LOESK	unrated	-	RUR	91,090
OA0 "CASEO"	unrated	-	RUR	30,676
Ulbino Consalting inc.	unrated	-	RUR	29,057
OA0 "Beltruboprovodstroy"	unrated	-	RUR	16,903
PPS Pipeline Systems GmbH	unrated	-	RUR	10,701
OA0 "Belspecelektrostroy"	unrated	-	RUR	9,417
OOO "BK-centre"	unrated	-	RUR	9,360
OOO "Protos"	unrated	-	RUR	8,609
				492,624
Deposits				
VTB	BBB/A-3 negative	S&P	various	2,394,354
MDM-Bank	BB-/B/Credit Watch negative	S&P	RUR	15,000
				2,409,354
Cash in banks				
VTB	BBB/A-3 negative	S&P	various	2,768,448
Alfa-Bank	BB-/B stable	S&P	various	353,179
MDM-Bank	BB-/B/Credit Watch negative	S&P	various	4,810
				3,126,437

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22. FINANCIAL INSTRUMENTS AND FINANCIAL RISK (CONTINUED)

Narrative	Rating at 31 December 2007	Rating agency	Currency	31 December 2007
Accounts receivable and prepayments				
OAo “Novgorodenergo”	unrated	-	RUR	199,568
OAo “Trest Uralneftegazstroy”	unrated	-	RUR	137,367
OOO “Peterburgenergostroy”	unrated	-	RUR	68,256
ZAO “Inginiringovaya korporaciya “Transstroy”	unrated	-	RUR	58,127
OOO “Ingenerny centr “Alteren”	unrated	-	RUR	38,029
PPS Pipeline Systems GmbH	unrated	-	RUR	36,238
OOO “Evrotrans Avto”	unrated	-	RUR	24,360
OOO “SK “Transstroy montazh konstrukciya”	unrated	-	RUR	19,318
OAo “CASEO”	unrated	-	RUR	17,312
ZAO “Trest №68”	unrated	-	RUR	17,133
				615,708
Deposits				
VTB	BBB+/A-2 stable	S&P	RUR	352,760
Alfa-Bank	BB/B stable	S&P	RUR	-
MDM-Bank	BB/B stable	S&P	RUR	1,000,000
				1,352,760
Cash in banks				
VTB	BBB+/A-2 stable	S&P	various	607,819
Alfa-Bank	BB/B stable	S&P	various	523,018
MDM-Bank	BB/B stable	S&P	various	84,680
				1,215,517

Liquidity risk

Prudent liquidity risk management includes maintaining sufficient cash and the availability of funding from an adequate amount of committed credit facilities.

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22. FINANCIAL INSTRUMENTS AND FINANCIAL RISK (CONTINUED)

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years
At 31 December 2008				
Trade accounts payable	554,886	-	-	-
Loans and borrowings	9,274,764	6,153,978	13,952,025	-
At 31 December 2007				
Trade accounts payable	887,307	-	-	-
Loans and borrowings	3,094,687	8,210,915	14,251,377	2,335,501

Foreign exchange risk

The Group has foreign currency and contracts denominated in currencies other than the Russian rouble. The Group does not hedge its currency transactions risks. The Central Bank of the Russian Federation rates and cross-rates of exchange at 31 December 2008 were RR 29.38, UAH 7.62, and BYR 2,201 to 1 US dollar, respectively (at 31 December 2007 – RR 24.55, UAH 5.09, and BYR 2,155, to 1 US dollar, respectively). Assets and liabilities denominated in Ukrainian hryvna or Belarusian rouble giving rise to foreign currency exchange exposure are insignificant.

At 31 December 2008 and 31 December 2007 the outstanding balances denominated in Ukrainian hryvna and Belarusian roubles were as follows:

	31 December 2008	31 December 2007
Trade and other receivables	103,316	11,747
Cash and cash equivalents	35,941	20,952
Trade and other payables	62,069	50,864
Profit tax and other tax liabilities	36,555	23,305

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar and the Euro. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and net investments in foreign operations.

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble, Euro or the US dollar, and it does not use foreign exchange or forward contracts. Management has not set any limit on its exposure to foreign exchange risk but periodically review its exposure of foreign exchange. The main assets and liabilities denominated in US dollars and Euro are listed in Notes 10, 11, 13 and 14. Management believes the Group's exposure to fluctuations in foreign exchange rates is limited to as the aforementioned and to the proceeds from export sales.

The sensitivity analysis of the foreign exchange risk is shown in the table below.

The group's sensitivity to changes in Euro exchange is low as most of the Group's borrowings and deposits, denominated in foreign currency, are in US dollar.



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22. FINANCIAL INSTRUMENTS AND FINANCIAL RISK (CONTINUED)

At 31 December 2008, if the US dollar had weakened/strengthened by 20% against the Russian roubles with all other variables held constant, post tax profit for the year and equity would be higher or lower by the following:

	Year ended 31 December 2008	Year ended 31 December 2007
Effect on post tax profit	3,209,451	3,079,684
Effect on equity	3,209,451	3,079,684

Post tax profit is higher/lower mainly as a result of foreign exchange gains/losses on translation of US Dollar denominated trade receivables, available-for-sale financial assets and borrowings.

The group's sensitivity to the US dollar exchange rate is high. The Group tries to minimize losses from strengthening of US Dollars in relation to Russian rouble by placing of free cash and cash equivalents in the assets nominated in currency of obligations. See also Note 2.

Cash flow and fair value interest rate risk

The Group is exposed to fair value interest rate risk through market value fluctuations of interest-bearing long-term borrowings all of which in 2008 and 2007 are at fixed interest rates.

The Group does not use any hedging instruments to manage its exposure to changes in interest rates because management considers that there is no necessity to do so.

Commodity price risk

The Group's main activity requires it to maintain and replace the existing pipeline network, and to construct new pipelines which need to be filled with oil products as linefill, which necessitates the purchase of a significant amount of steel pipe each year for new and replacement pipelines, and of oil products as linefill. The Group has no long-term contracts with manufacturers of pipe or producers of oil products, and does not use derivative contracts to manage its exposure to fluctuations in the price of steel or oil products.

Fair value

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Russian Federation continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

The fair value of financial assets and liabilities did not differ materially from their carrying value at 31 December 2008 and 31 December 2007.

Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholder and benefits to other stakeholders and to maintain optimal capital structure to reduce the cost of capital.



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22. FINANCIAL INSTRUMENTS AND FINANCIAL RISK (CONTINUED)

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to the shareholder, issue new shares or sell assets to reduce debt.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings, as shown in the consolidated balance sheet, less cash and cash equivalents. Total capital is calculated as equity, as shown in the consolidated balance sheet, plus net debt.

During 2007 and 2008 the Group's strategy was to maintain the gearing ratio not be greater than 0.5 in order to comply with financial covenants under loan agreement with White Nights Finance B.V. (see Note 13).

The gearing ratios at 31 December 2008 and at 31 December 2007 were as follows:

	31 December 2008	31 December 2007
Total borrowings	24,241,152	21,201,137
Less: cash and cash equivalents	(5,725,855)	(2,826,369)
Net debt	18,515,297	18,374,768
Total equity	39,987,133	39,398,130
Total capital	58,502,430	57,772,898
Gearing ratio	0.32	0.32

In addition to gearing ratio the Group also monitors financial liabilities/net assets ratio in accordance with loan agreement with White Nights Finance B.V. The above ratio is calculated as total loans and borrowings to total equity and should be not more than 1:1. The financial liabilities/net assets ratio as at 31 December 2008 was 0.6:1 (at 31 December 2007 was 0.5:1).

23. CONTINGENT LIABILITIES AND OTHER RISKS

Legal proceedings

In 2008, the Group was involved in a number of court proceedings arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or claims outstanding at 31 December 2008, which could have a material adverse effect on the results of operations or financial position of the Group.

Management assesses an unfavorable outcome of the matters discussed below as possible.

As of the date of issuing these consolidated financial statements the courts of the first to third instances confirmed the right of the Company to claim RR 1 049 639 of VAT paid during the period January 2004 – September 2007 at a rate of 18% to its subsidiaries for oil products transportation services. Such services were consumed by the Company in the process of rendering oil product transportation to external buyers.

However, the tax authorities in their continued effort to contest the courts rulings in favour of the Company filed an appeal applications to the Supreme Arbitration Court of the Russian Federation. Resulting from the hearing of one of those applications on 25 February 2009, the Presidium of the Supreme Arbitration Court invalidated the decisions of the lower courts with regard to settlement of RR 68 619 and transferred the case to the court of the first instance.

Taxation

Tax, currency and customs legislation in the countries in which the Group operates is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments. As a result, significant additional taxes, penalties and interest may be



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23. CONTINGENT LIABILITIES AND OTHER RISKS (CONTINUED)

assessed. Fiscal periods remain open to review by the authorities in respect of taxes in the Russian federation for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As at 31 December 2008 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Accordingly, at 31 December 2008 no provision for potential tax liabilities had been recorded (at 31 December 2007: no provision).

Commitments

In the normal course of business, the Group prepares a plan for the construction, reconstruction and development of the pipeline network on an annual basis, and revises it periodically during the year. At 31 December 2008, current plans and commitments provided for RR 2,613,282 to be spent during 2009.

Environmental reclamation, restoration and protection costs

The Group is subject to various environmental laws regarding the handling, storage and disposal of certain products. Existing legislation does not require the removal of the pipeline and associated infrastructure at the end of its useful economic life. The enforcement of environmental regulations in Russian Federation is evolving, and the enforcement posture of government authorities is continually being reconsidered. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

Other

The legal status of ownership of the Group's pipeline in the territory of Ukraine is proved by the temporary Agreement between the Russian Federation and Ukraine on the mutual recognition of rights and regulation of ownership relations signed 15 January 1993. Until the final decision on the specified Agreement is made the financial implications of that decision can not be estimated with a reasonable degree of probability. DP «PrikarpatZapadtrans» has the license for the transportation of oil products in the territory of Ukraine, expiring in 2010. The Group is working on the licence extension, and at the date of authorization of these consolidated financial statements for issue the Group is not aware of any facts indicating that the license will not be extended.

24. RELATED PARTY BALANCES AND TRANSACTIONS AND COMPENSATION TO KEY MANAGEMENT PERSONNEL

The only shareholder of the Company in 2007 was the Federal Agency for Administration of Federal Property of Russia. Since 15 January 2008 the only shareholder of the Company is OJSC AK Transneft, which is under control of the Russian Federation. Related parties therefore include all branches of the government of the Russian Federation and entities which the Russian Federation own or control. The Russian Federation has an arrangement with the Group under which reserves of oil products are stored in the Group's network, in return for which the Group benefits through improved operational flexibility.

At 31 December 2008 and 31 December 2007 the outstanding balances with related parties were as follows:

	31 December 2008	31 December 2007
Long-term available-for-sale financial assets	76,751	142,701
Short-term available-for-sale financial assets	-	24,301
Trade and other receivables	239,134	26,502
Cash in banks	2,774,271	615,117
Deposits	2,394,354	352,760
Payables and advances from customers	1,044,143	531,502
Long-term borrowings and loans	16,643,075	20,162,752
Current portion of long-term borrowings and loans	7,598,077	1,038,385



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24. RELATED PARTY BALANCES AND TRANSACTIONS AND COMPENSATION TO KEY MANAGEMENT PERSONNEL (CONTINUED)

Borrowings and loans include loan from VTB because it is controlled by the Russian Federation and loan from White Nights Finance B.V. as it is a special purpose entity sponsored by VTB Bank Europe plc and therefore related to VTB.

The income and expenses items with related parties for years ended 31 December 2008 and 31 December 2007 were as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Sales:		
Transportation services	6,566,869	5,082,393
Other revenue	203,159	17,392
Cost of sales:		
Electricity	195,984	351,474
Third party repair, maintenance and diagnostic	93,022	-
Other expenses	270,347	204,613
General and administrative expenses:		
Legal and consulting services	47,095	-
Interest income	9,019	22,136
Interest expense	2,143,766	1,703,165

Transportation services include revenue received from OAO NK Rosneft and OAO Gazpromneft because they are controlled by the Russian Federation.

Tax balances are disclosed in the balance sheet and Notes 10 and 15. Tax transactions are detailed in the income statement and Note 18.

Compensation to key management personnel

Key management personnel of the Group includes members of the Board of Directors (comprising 9 people) and the Management Committee (comprising 9 people until 11 December 2008 and 5 people after that date). Compensation to the members of the Board of Directors in 2008 and 2007 has not been paid. Compensation to the members of the Management Committee of the Company is determined by the terms of employment contracts. The amounts of such compensation are included in general and administrative expenses and comprised 168,667 RR for the year ended 31 December 2008 (RR 135,631 - year ended 31 December 2007). All key management compensations plans are short-term.

Compensation amounts were as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Salaries and bonuses	154,209	132,240
Termination benefits	7,175	-
Other	7,283	3,391
	168,667	135,631

25. POST BALANCE SHEET EVENTS

On 27 April 2009 the Company has amended loan agreement with the Bank of International Trade (Note 13) so the loan is payable quarterly from 12 April 2011 to 12 April 2013, each payment amounted to 1/9 of the outstanding loan amount at the date of loan agreement amendment. Outstanding loan amount at the date of amendment was USD 708 million.



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25. POST BALANCE SHEET EVENTS (CONTINUED)

In 2009 the Board of Directors of the Company has recommended to Shareholders not to pay dividends for the year ended 31 December 2008. Nevertheless, final decision will be made on General Shareholders Meeting which has not been held on the date of authorization of these consolidated financial statements for issue.

In June 2009 the Company has offered to holders of Credit Linked Notes possibility of their early redemption in June 2009 at the quote of 95.5%.