



**ROSNEFT**

O I L C O M P A N Y

OPEN JOINT STOCK COMPANY

**OJSC Oil Company Rosneft**

**Consolidated Financial Statements**

*as of December 31, 2007 and 2006 and  
for the years ended December 31, 2007, 2006 and 2005  
With Report of Independent Auditors*

OJSC Oil Company Rosneft

Consolidated Financial Statements

as of December 31, 2007 and 2006

and for the years ended December 31, 2007, 2006 and 2005

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## Report of Independent Auditors

Shareholders and the Board of Directors  
of OJSC Oil Company Rosneft

We have audited the accompanying consolidated balance sheets of OJSC Oil Company Rosneft, an open joint stock company (“the Company”), as of December 31, 2007 and 2006, and the related consolidated statements of income, changes in shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2007. These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. We were not engaged to perform an audit of the Company’s internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 3 to the consolidated financial statements, the Company has not presented pro-forma results of operations for the years 2005, 2006 and 2007 as though its significant acquisitions had been completed as of January 1, 2005. These disclosures are required by SFAS No. 141 “*Business Combinations*”.

In our opinion, except for the effects of the matters described in the preceding paragraph, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2007 and 2006, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America.

*Ernst & Young LLC*

April 7, 2008

# OJSC Oil Company Rosneft

## Consolidated Balance Sheets

(in millions of US dollars, except share amounts)

	Notes	As of December 31,	
		2007	2006
<b>ASSETS</b>			
<b>Current assets:</b>			
Cash and cash equivalents	5	998	505
Restricted cash	5	34	18
Short-term investments	6	338	460
Accounts receivable, net of allowance	7	9,785	4,850
Inventories	8	1,926	905
Current deferred tax assets	20	156	1,135
Prepayments and other current assets	9	1,731	1,589
<b>Total current assets</b>		<b>14,968</b>	<b>9,462</b>
<b>Non-current assets:</b>			
Long-term investments	10	2,646	568
Long-term bank loans granted, net of allowance of \$20 and \$6, respectively		260	110
Property, plant and equipment, net	11, 12	51,686	35,945
Goodwill	13	3,789	161
Intangible assets	13	285	7
Non-current deferred tax assets	20	57	110
Other non-current assets	14	1,114	427
<b>Total non-current assets</b>		<b>59,837</b>	<b>37,328</b>
<b>Total assets</b>		<b>74,805</b>	<b>46,790</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Current liabilities:</b>			
Accounts payable and accrued liabilities	15	4,035	1,998
Short-term debt	16	15,550	6,427
Income and other tax liabilities	18	2,346	2,472
Deferred tax liabilities	20	118	17
Other current liabilities		75	20
<b>Total current liabilities</b>		<b>22,124</b>	<b>10,934</b>
<b>Non-current liabilities:</b>			
Asset retirement obligations	21	2,130	748
Long-term debt	16	11,723	7,402
Deferred tax liabilities	20	7,626	5,446
Other non-current liabilities	23	2,485	160
<b>Total non-current liabilities</b>		<b>23,964</b>	<b>13,756</b>
<b>Minority interest</b>		<b>277</b>	<b>225</b>
<b>Shareholders' equity:</b>			
Common stock par value 0.01 RUB (shares outstanding: 9,598 million and 10,598 million as of December 31, 2007 and 2006, respectively)	17	20	20
Treasury shares (at acquisition cost: 1,000 million and nil shares as of December 31, 2007 and 2006, respectively)		(7,521)	–
Additional paid-in capital		13,075	11,352
Retained earnings		22,866	10,503
<b>Total shareholders' equity</b>		<b>28,440</b>	<b>21,875</b>
<b>Total liabilities and shareholders' equity</b>		<b>74,805</b>	<b>46,790</b>

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

OJSC Oil Company Rosneft  
Consolidated Statements of Income

*(in millions of US dollars, except earnings per share data)*

	Notes	For the years ended December 31,		
		2007	2006	2005
<b>Revenues</b>				
Oil and gas sales	24	29,902	23,499	16,152
Petroleum products and processing fees	24	18,531	9,250	7,374
Support services and other revenues		783	350	337
<b>Total</b>		<b>49,216</b>	<b>33,099</b>	<b>23,863</b>
<b>Costs and expenses</b>				
Production and operating expenses		3,870	2,197	1,623
Cost of purchased oil, gas, petroleum products and refining costs		1,610	1,320	637
General and administrative expenses		1,341	757	589
Pipeline tariffs and transportation costs		4,226	3,226	2,231
Exploration expenses		162	193	164
Depreciation, depletion and amortization		3,286	1,638	1,472
Accretion expense		78	34	35
Taxes other than income tax	20	10,890	6,990	5,326
Export customs duty	19	13,032	11,140	6,264
<b>Total</b>		<b>38,495</b>	<b>27,495</b>	<b>18,341</b>
<b>Operating income</b>		<b>10,721</b>	<b>5,604</b>	<b>5,522</b>
<b>Other income/(expenses)</b>				
Interest income		214	135	81
Interest expense		(1,470)	(724)	(775)
Loss on disposal of property, plant and equipment		(119)	(95)	(74)
Gain/(loss) on disposal of investments		36	3	(13)
Gain on sale of shares in CJSC Sevmorneftegaz		–	–	1,303
Equity share in affiliates' profits	10	23	17	51
Dividends and income from joint ventures		18	15	10
Gain from Yukos Oil Company bankruptcy proceedings	7	8,970	–	–
Other expenses, net		(195)	(320)	(136)
Foreign exchange gain/(loss)		(409)	(470)	245
<b>Total other income/(expenses)</b>		<b>7,068</b>	<b>(1,439)</b>	<b>692</b>
<b>Income before income tax and minority interest</b>		<b>17,789</b>	<b>4,165</b>	<b>6,214</b>
Income tax expense	20	(4,906)	(540)	(1,609)
<b>Income before minority interest</b>		<b>12,883</b>	<b>3,625</b>	<b>4,605</b>
Minority interest in subsidiaries' earnings, net of tax		(21)	(92)	(446)
<b>Net income</b>		<b>12,862</b>	<b>3,533</b>	<b>4,159</b>
Net earnings per share (in US\$) – basic and diluted		1.30	0.37	0.46
Weighted average number of shares outstanding (millions)		9,891	9,527	9,092

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

OJSC Oil Company Rosneft

Consolidated Statements of Changes in Shareholders' Equity

for the years ended December 31, 2007, 2006 and 2005

(in millions of US dollars, except share amounts)

	Number of shares (millions)	Common stock	Additional paid-in capital	Treasury shares	Retained earnings	Shareholders' equity
Balance at December 31, 2004	9,092	20	19	–	3,296	3,335
Net and comprehensive income for the year	–	–	–	–	4,159	4,159
Dividends declared on common stock	–	–	–	–	(61)	(61)
<b>Balance at December 31, 2005</b>	<b>9,092</b>	<b>20</b>	<b>19</b>	<b>–</b>	<b>7,394</b>	<b>7,433</b>
Net and comprehensive income for the year	–	–	–	–	3,533	3,533
Ordinary shares issued during Initial Public Offering (see Note 17)	285	–	2,115	–	–	2,115
Ordinary shares issued during Share Swap (see Note 17)	1,221	–	9,218	–	–	9,218
Dividends declared on common stock	–	–	–	–	(424)	(424)
<b>Balance at December 31, 2006</b>	<b>10,598</b>	<b>20</b>	<b>11,352</b>	<b>–</b>	<b>10,503</b>	<b>21,875</b>
Net and comprehensive income for the year	–	–	–	–	12,862	12,862
Purchase of shares	(1,000)	–	–	(7,521)	–	(7,521)
Recognition of the financial effect of a transaction with a related party under common control (see Note 17)	–	–	1,745	–	–	1,745
Dividends declared on common stock and other distributions to shareholders	–	–	(22)	–	(499)	(521)
<b>Balance at December 31, 2007</b>	<b>9,598</b>	<b>20</b>	<b>13,075</b>	<b>(7,521)</b>	<b>22,866</b>	<b>28,440</b>

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

OJSC Oil Company Rosneft  
Consolidated Statements of Cash Flows

*(in millions of US dollars)*

	Notes	For the years ended December 31,		
		2007	2006	2005
<b>Operating activities</b>				
Net income		12,862	3,533	4,159
Adjustments to reconcile net income to net cash provided by operating activities:				
Effect of foreign exchange		365	392	(115)
Gain on sale of shares in CJSC Sevmorneftegaz		–	–	(1,303)
Depreciation, depletion and amortization		3,286	1,638	1,472
Dry well expenses		93	20	17
Loss on disposal of property, plant and equipment		119	95	74
Deferred income tax	20	1,058	(1,845)	(79)
Accretion expense	21	78	34	35
Equity share in affiliates' profits	10	(23)	(17)	(51)
(Gain) / loss on disposal of investments		(36)	(3)	13
Increase / (decrease)/ in allowance for doubtful accounts and bank loans granted		21	(10)	4
Minority interests in subsidiaries' earnings		21	92	446
Gain from Yukos Oil Company bankruptcy proceedings	7	(8,970)	–	–
Cash received from Yukos Oil Company bankruptcy receiver	7	11,007	–	–
Acquisition of trading securities		(367)	(181)	(71)
Proceeds from sale of trading securities		501	9	75
Changes in operating assets and liabilities net of acquisitions:				
Increase in accounts receivable		(4,745)	(1,192)	(1,353)
Increase in inventories		(161)	(91)	(297)
(Increase)/decrease in restricted cash		(16)	5	2
Increase in prepayments and other current assets		(444)	(231)	(626)
(Increase)/decrease in other non-current assets		(197)	(124)	6
Increase in long-term bank loans granted		(164)	(41)	(23)
Increase in interest payable		123	36	158
Increase/(decrease) in accounts payable and accrued liabilities		1,505	678	(8)
Increase/(decrease) in income and other tax liabilities		1,228	(338)	414
(Decrease)/increase in other current and non-current liabilities		(34)	131	5
<b>Net cash provided by operating activities</b>		<b>17,110</b>	<b>2,590</b>	<b>2,954</b>

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

# OJSC Oil Company Rosneft

## Consolidated Statements of Cash Flows (continued)

*(in millions of US dollars)*

	Notes	<b>For the years ended December 31,</b>		
		<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Investment activities</b>				
Capital expenditures	11	(6,240)	(3,462)	(1,944)
Assets acquisitions	3	(540)	–	–
Acquisition of licences		(90)	(916)	(146)
Repayment of Sakhalin-1 carried costs		–	(1,339)	–
Proceeds from disposals of property, plant and equipment		58	27	30
Acquisition of short-term held-to-maturity securities		(219)	(277)	(622)
Acquisition of short-term available-for-sale securities		(25)	–	–
Proceeds from disposal of short-term investments, including				
Held-to-maturity securities		122	139	628
Available-for-sale securities		177	–	–
Acquisition of entities and additional shares in subsidiaries, net of cash acquired	3, 4	(17,061)	(194)	(366)
Proceeds from disposal of long-term investments, including				
Held-to-maturity securities		28	6	45
Available-for-sale securities		57	27	93
Proceeds from sale of shares in OJSC Tomskneft VNK	17	3,452	–	–
Settlement/(acquisition) of debt receivable	9	483	(463)	(20)
Acquisition of long-term investments, including				
Held-to-maturity securities		(251)	(50)	(33)
Available-for-sale securities		(46)	(11)	–
<b>Net cash used in investing activities</b>		<b>(20,095)</b>	<b>(6,513)</b>	<b>(2,335)</b>
<b>Financing activities</b>				
Proceeds from short-term debt		14,391	2,768	977
Repayment of short-term debt		(3,731)	(796)	(2,018)
Proceeds from long-term debt		3,435	2,887	2,547
Repayment of long-term debt		(2,598)	(3,250)	(1,829)
Proceeds from share issue, net of commission	17	–	2,115	–
Dividends paid and other distributions to shareholders		(521)	(424)	(61)
Cash paid for acquisition of treasury shares		(7,521)	–	–
Dividends paid to minority shareholders in subsidiaries		(15)	(75)	(74)
<b>Net cash provided by/(used in) financing activities</b>		<b>3,440</b>	<b>3,225</b>	<b>(458)</b>
Increase / (decrease) in cash and cash equivalents		455	(698)	161
Cash and cash equivalents at beginning of period		505	1,173	1,033
Effect of foreign exchange on cash and cash equivalents		38	30	(21)
<b>Cash and cash equivalents at end of period</b>		<b>998</b>	<b>505</b>	<b>1,173</b>
<b>Supplementary disclosures of cash flow information</b>				
Cash paid for interest (net of amount capitalized)		1,152	610	617
Cash paid for income taxes		4,267	2,157	1,636
<b>Supplementary disclosure of non-cash activities</b>				
Net assets of subsidiaries contributed by minority shareholders in exchange for shares issued by Rosneft	4	–	9,218	–
Income tax offsets		–	1	41
Non-cash capital expenditures		–	–	(32)

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



# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements

as of December 31, 2007 and 2006

and for the years ended December 31, 2007, 2006 and 2005

*(all amounts in tables are in millions of US dollars, except as noted otherwise)*

### 1. General

#### Nature of Operations

Open Joint Stock Company ("OJSC") Oil Company Rosneft ("Rosneft") and its subsidiaries, (collectively the "Company" or the "Group"), are principally engaged in exploration, development, production and sale of crude oil and gas and refining, transportation and sale of petroleum products in the Russian Federation and in certain international markets.

Rosneft State Enterprise was incorporated as an open joint stock company on December 7, 1995. All assets and liabilities previously managed by Rosneft State Enterprise were transferred to the Company at their book value effective on that date together with the Government of the Russian Federation ("State") ownership in other privatized oil and gas companies. The transfer of assets and liabilities was made in accordance with Resolution No. 971, "On the Transformation of Rosneft State Enterprise into an Open Joint Stock Company "Oil Company Rosneft", dated September 29, 1995. Such transfers represented a reorganization of assets under the common control of the State and, accordingly, were accounted for at their book value. In 2005, the State contributed the shares of Rosneft to the share capital of OJSC Rosneftegaz (see Note 17). As of December 31, 2005, 100% of the shares of Rosneft less one share were owned by OJSC Rosneftegaz and one share was owned by the Russian Federation Federal Agency for the Management of Federal Property. As of December 31, 2006 and 2007, OJSC Rosneftegaz maintains a 75.16% interest in Rosneft. The decrease in interest is attributable to sales of shares during Rosneft's Initial Public Offering ("IPO") in Russia, sales of Global Depository Receipts ("GDR") for the shares on London Stock Exchange and the share swap realized during the merger of Rosneft and certain subsidiaries during 2006 (see Note 1, Note 3 and Note 17).

Under Russian legislation, natural resources, including oil, gas, precious metals and minerals and other commercial minerals situated within the territory of the Russian Federation are the property of the State until they are extracted. Law of the Russian Federation No. 2395-1, *On Subsurface Resources*, regulates relations arising in connection with the geological study, use and protection of subsurface resources within the territory of the Russian Federation. Pursuant to the Law, subsurface resources may be developed only on the basis of a licence. The licence is issued by the regional governmental body and contains information on the site to be developed, the period of activity, financial and other conditions. The Company holds licences issued by regional authorities for geological studies, exploration and development of oil and gas blocks and fields in areas where its subsidiaries are located.

Due to the limited capacity of OJSC Transneft's pipeline system, the State Pipeline Commission sets export quotas for each oil company based on the legislation on equal access to the oil pipeline system. In addition, the Company exports certain quantities of crude oil bypassing the Transneft system thus enabling it to increase its export capacities. In 2007, 2006 and 2005, the Company's export sales were approximately 61%, 70% and 62% of produced crude oil, respectively. The remaining production was processed at the Company's refineries and other Russian refineries for further sales on domestic and international markets.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 1. General (continued)

#### Nature of Operations (continued)

On October 1, 2006, the Company undertook a legal reorganization whereby a number of subsidiaries were merged with OJSC Oil Company Rosneft via an exchange of shares, as approved by the respective shareholders ("Share Swap") of: OJSC Yuganskneftegaz, OJSC Rosneft-Purneftegaz, OJSC Selkupneftegaz, OJSC Severnaya Neft (Northern Oil), OJSC Rosneft-Krasnodarneftegaz, OJSC Rosneft-Stavropolneftegaz, OJSC Rosneft-Sakhalinmorneftegaz, OJSC Rosneft-Komsomolsky Refinery, OJSC Rosneft-Tuapse Refinery, OJSC Rosneft-Arkhangelsknefteproduct, OJSC Rosneft-Nakhodkanefteproduct, and OJSC Rosneft-Tuapsenefteproduct (each, a "Merging Subsidiary" and collectively, the "Merging Subsidiaries"). The primary purpose of the merger was to create a more efficient corporate and management structure with a single profit center. The Merging Subsidiaries were delisted from Unified State Register of Legal Entities from October 1, 2006. As a result of the Share Swap, OJSC Oil Company Rosneft issued its ordinary shares to the minority shareholders of the Merging Subsidiaries in exchange for ordinary and preferred shares owned by them. The shares of each Merging Subsidiary were exchanged at an agreed conversion ratio (see Note 4).

In December 2006, the Federal Tax Agency of the Russian Federation registered the increase in the Company's Share Capital resulting from the Share Swap.

Principal subsidiary companies included in the consolidated financial statements and respective ownership interests of the Company as of December 31, 2007 are as follows:

Name	Nature of Business	Preferred and Common Shares	Voting Shares
<b><u>Exploration and production</u></b>			
RN-Yuganskneftegaz LLC	Oil and gas production operator services	100.00	100.00
RN-Purneftegaz LLC	Oil and gas production operator services	100.00	100.00
RN-Sakhalinmorneftegaz LLC	Oil and gas production operator services	100.00	100.00
RN-Krasnodarneftegaz LLC	Oil and gas production operator services	100.00	100.00
RN-Stavropolneftegaz LLC	Oil and gas production operator services	100.00	100.00
Rosneft Severnaya Neft LLC (Northern Oil)	Oil and gas production operator services	100.00	100.00
CJSC RN-Astra	Oil and gas development and production	100.00	100.00
CJSC Sakhalinmorneftegaz Shelf	Oil and gas development and production	100.00	100.00
CJSC Komsomolskneft	Oil and gas development and production	100.00	100.00
OJSC Dagneftegaz	Oil and gas development and production	81.22	94.96
OJSC Rosneft-Dagneft	Oil and gas development and production	68.70	91.60
OJSC Grozneftegaz	Oil and gas production operator services	51.00	51.00
CJSC Vostokshelf	Field survey and exploration	100.00	100.00
RN-Kazakhstan LLC	Field survey and exploration	100.00	100.00
RN-Kaiganneftegaz LLC	Field survey and exploration	100.00	100.00
CJSC Vostok-Smidt Neftegaz	Field survey and exploration	100.00	100.00
CJSC Zapad-Smidt Neftegaz	Field survey and exploration	100.00	100.00
CJSC Vankorneft	Field survey and exploration	100.00	100.00
Taymyrneft LLC	Investment activities	60.00	60.00
Vostok Smidt Invest LLC	Investment activities	100.00	100.00
Zapad Smidt Invest LLC	Investment activities	100.00	100.00
Vostok-Energy LLC	Field survey and exploration	51.00	51.00
OJSC East-Siberian Oil and Gas Company	Oil and gas development and production	70.78	70.78
Val Shatskogo LLC	Oil and gas development	100.00	100.00
OJSC Samaraneftegaz	Oil and gas development and production	100.00	100.00

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 1. General (continued)

#### Nature of Operations (continued)

Name	Nature of Business	Preferred and	Voting
		Common Shares	Shares
		%	%
<b><u>Refining, marketing and distribution</u></b>			
RN-Tuapse Refinery LLC	Petroleum refining	100.00	100.00
RN-Komsomolsky Refinery LLC	Petroleum refining	100.00	100.00
OJSC Rosneft-MZ Nefteproduct	Petroleum refining	65.42	87.23
OJSC Rosneft-ARTAG	Marketing and distribution	38.00	50.67
OJSC Rosneft-Altainefteproduct	Marketing and distribution	64.18	78.59
RN-Arkhangelsknefteproduct LLC	Marketing and distribution	100.00	100.00
OJSC Rosneft-Kabardino-Balkarskaya Toplivnaya Company	Marketing and distribution	88.66	92.91
OJSC Rosneft-Kubannefteproduct	Marketing and distribution	89.50	96.61
OJSC Rosneft-Karachaevo- Cherkessknefteproduct	Marketing and distribution	85.99	87.46
OJSC Rosneft-Kurgannefteproduct	Marketing and distribution	83.32	90.33
OJSC Rosneft-Murmansknefteproduct	Marketing and distribution	45.38	60.51
RN-Nakhodkanefteproduct LLC	Marketing and distribution	100.00	100.00
OJSC Rosneft-Smolensknefteproduct	Marketing and distribution	66.67	86.97
RN-Tuapsenefteproduct LLC	Marketing and distribution	100.00	100.00
OJSC Rosneft-Yamalnefteproduct	Marketing and distribution	49.52	66.03
RN-Vostoknefteproduct LLC	Marketing and distribution	100.00	100.00
OJSC Rosneft-Stavropolye	Marketing and distribution	99.49	99.49
RN-Trade LLC	Marketing and distribution	100.00	100.00
OJSC Nakhodka Oil Seatrade Port	Transshipment	97.51	97.51
CJSC Exponeft	Marketing and distribution	45.38	60.51
OJSC Angarsk Petrochemical Company	Petroleum refining	100.00	100.00
OJSC Achinsk Refinery VNK	Petroleum refining	100.00	100.00
OJSC Angarsk Polymer Plant	Petroleum refining	100.00	100.00
OJSC Kuybyshev Refinery	Petroleum refining	100.00	100.00
OJSC Novokuybyshev Refinery	Petroleum refining	100.00	100.00
OJSC Syzran Refinery	Petroleum refining	100.00	100.00
CJSC Neftegorsk Gas-Processing Plant	Gas processing	100.00	100.00
CJSC Otradny Gas-Processing Plant	Gas processing	100.00	100.00
CJSC Irkutsknefteproduct	Marketing and distribution	100.00	100.00
OJSC Samaranefteproduct	Marketing and distribution	100.00	100.00
Samara Terminal LLC	Marketing and distribution	100.00	100.00
OJSC Buryatnefteproduct	Marketing and distribution	97.48	98.88
CJSC Khakasnefteproduct VNK	Marketing and distribution	100.00	100.00
OJSC Tomsknefteproduct VNK	Marketing and distribution	100.00	100.00
OJSC Belgorodnefteproduct	Marketing and distribution	100.00	100.00
CJSC Bryansknefteproduct	Marketing and distribution	100.00	100.00
OJSC Voronezhnefteproduct	Marketing and distribution	100.00	100.00
CJSC Lipetsknefteproduct	Marketing and distribution	100.00	100.00
CJSC Orelnefteproduct	Marketing and distribution	100.00	100.00
CJSC Penzanefteproduct	Marketing and distribution	100.00	100.00
CJSC Tambovnefteproduct	Marketing and distribution	100.00	100.00
CJSC Ulyanovsknefteproduct	Marketing and distribution	100.00	100.00
Ulyanovsk Terminal LLC	Marketing and distribution	100.00	100.00
CJSC FPK KEDR M	Marketing and distribution	100.00	100.00
CJSC NBA Service	Marketing and distribution	100.00	100.00
OJSC Germes Moskva	Marketing and distribution	85.61	85.61
CJSC Contract Oil	Marketing and distribution	100.00	100.00
CJSC Mytischki Fuel Company	Marketing and distribution	100.00	100.00
OJSC Stavropolnefteproduct	Marketing and distribution	100.00	100.00
U-Kuban LLC	Marketing and distribution	100.00	100.00

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 1. General (continued)

#### Nature of Operations (continued)

Name	Nature of Business	Preferred and	Voting
		Common Shares	Shares
		%	%
<b>Other</b>			
Rosneft International Limited	Holding company	100.00	100.00
CJSC Rosneftflot	Transportation services	51.00	51.00
OJSC All-Russian Bank for Reconstruction and Development of Russian Regions (VBRR)	Banking	76.47	76.47
CJSC Sakhalinskije Proekty	Management company	100.00	100.00
RN-Burenie LLC	Drilling services	100.00	100.00
NK Rosneft NTC LLC	Research & development activities	100.00	100.00

All of the above subsidiaries, except for Rosneft International Ltd., are incorporated in the Russian Federation. Rosneft International Ltd. is registered in Ireland.

#### Currency Exchange and Control

Foreign currencies, in particular the US dollar and the Euro, play a significant role in the underlying economics of many business transactions in Russia. For the oil and gas sector in particular, substantial export arrangements as well as investing and financing activities are conducted in foreign currencies, primarily the US dollar.

### 2. Significant Accounting Policies

#### Form and Content of the Consolidated Financial Statements

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

The accompanying consolidated financial statements differ from the financial statements issued for statutory purposes in Russia in that they reflect certain adjustments, not recorded in the Company's statutory books, which are appropriate to present the financial position, results of operations and cash flows in accordance with US GAAP. The principal adjustments relate to: (1) recognition of certain expenses; (2) valuation and depreciation of property, plant and equipment; (3) foreign currency translation; (4) deferred income taxes; (5) valuation allowances for unrecoverable assets; (6) accounting for the time value of money; (7) accounting for investments in oil and gas property and conveyances; (8) consolidation principles; (9) recognition and disclosure of guarantees, contingencies, commitments and certain assets and liabilities; (10) accounting for asset retirement obligations; (11) business combinations and goodwill/negative goodwill; (12) accounting for derivative instruments.

Certain items in the consolidated balance sheet as of December 31, 2006 and the consolidated statements of income and cash flows for 2006 and 2005 were reclassified to conform to the current year presentation.

Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)**

**Management Estimates**

The preparation of the financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities in the balance sheet as well as the amounts of revenues and expenses recognized during the reporting periods. Certain significant estimates and assumptions for the Company include: estimation of economically recoverable oil and gas reserves; rights to and recoverability and useful lives of long-term assets and investments; impairment of goodwill; allowances for doubtful accounts receivable; asset retirement obligations; legal and tax contingencies; environmental remediation obligations; recognition and disclosure of guarantees and other commitments; fair value measurements; ability to renew operating leases and to enter into new lease agreements; classification of certain debt amounts. Some of the most significant estimates were made in connection with the acquisition of Yukos Oil Company assets (see Note 3). Management believes it has a reasonable and appropriate basis for its judgment pertaining to its estimates and assumptions. However, actual results could differ from those estimates.

**Foreign Currency Translation**

The management of the Company has determined the US Dollar as the functional and reporting currency for the purpose of financial reporting under US GAAP. Monetary assets and liabilities have been translated into US dollars using the official exchange rate as of the balance sheet date. Non-monetary assets and liabilities have been translated at historical rates. Revenues, expenses and cash flows are translated into US dollars at average exchange rates for the period or exchange rates prevailing on transaction dates where practicable.

Gains and losses resulting from the re-measurement into US dollars are included in the "Foreign exchange (loss)/gain" in the consolidated statements of income.

As of December 31, 2007 and 2006, the Central Bank of the Russian Federation ("CBR") official rates of exchange were 24.55 rubles and 26.33 rubles per US dollar, respectively. As of April 7, 2008, the official rate of exchange was 23.60 rubles ('RUB') per US dollar.

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

**Principles of Consolidation**

The consolidated financial statements include the accounts of majority-owned, controlled subsidiaries and variable interest entities where the Company is a primary beneficiary. All intercompany transactions and balances have been eliminated. The equity method is used to account for investments in affiliates in which the Company has the ability to exert significant influence over the affiliates' operating and financial policies. The investments in entities where the Company holds the majority of shares, but the minority shareholders have significant influence, are also accounted for using the equity method. The Company's share in net profit or loss of equity investees also includes any other-than-temporary declines in fair value recognized during the period. Investments in other companies are accounted for at cost and adjusted for estimated impairment.

## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Minority Interest**

Minority interests in the net assets and net results of consolidated subsidiaries are shown under "Minority interest" in the accompanying consolidated balance sheets and statements of income. For majority-owned subsidiaries that incur losses, the Company recognizes 100% of the losses, after first reducing the related minority interests' balances to zero, unless minority shareholders committed to fund the losses. Further, when a majority-owned subsidiary becomes profitable, the Company recognizes 100% of profits until such time as the excess losses previously recorded have been recovered. Thereafter, the Company recognizes profits in accordance with the underlying ownership percentage. The actual ruble-denominated balances attributable to minority interests may differ from these amounts presented in these consolidated financial statements.

**Cash and Cash Equivalents**

Cash represents cash on hand and in the Company's bank accounts and interest bearing deposits which can be effectively withdrawn at any time without prior notice or penalties reducing the principal amount of the deposit. Cash equivalents are highly liquid, short-term investments that are readily convertible to known amounts of cash and have original maturities of three months or less from their date of purchase. They are carried at cost plus accrued interest, which approximates fair value.

**Loans and Accounts Receivable**

Loans and accounts receivable are stated at their principal amounts outstanding net of loan losses and allowances for doubtful debts. Specific allowances are recorded against trade receivables whose recovery or collection has been identified as doubtful. Estimates of allowances require the exercise of judgment and the use of assumptions.

**Earnings per Share**

Basic earnings per share is calculated by dividing net earnings attributable to common shares by the weighted average number of common shares outstanding during the corresponding period. In the absence of any securities-to-shares conversion transactions, the amount of basic earnings per share stated in these financial statements is equal to the amount of diluted earnings per share.

**Inventories**

Inventories, consisting primarily of crude oil, petroleum products and materials and supplies, are stated at the lower of weighted average cost of acquisition or market value. Market value shall not exceed net realizable value (i.e. the price at which inventories can be sold after allowing for the cost of completion and sale), and shall not be lower than net realizable values less the amount of margin.

**Financial Investments**

All debt and equity securities held by the Company are classified into one of the following three categories: trading securities; available-for-sale securities; held-to-maturity securities.

Trading securities are purchased and held principally for the purpose of sale in the nearest future. Held-to-maturity securities represent financial instruments that the Company has both the intent and the ability to hold to maturity.

All other securities, which do not fall into these two categories, are classified as available-for-sale securities.

Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)**

**Financial Investments (continued)**

Trading securities and available-for-sale securities are carried at fair (market) value.

Held-to-maturity securities are stated at amortized cost.

Unrealized gains or losses on trading securities are included in the consolidated statements of income. Unrealized gains and losses on available-for-sale securities less related tax effects are recorded as a separate component of comprehensive income until the date of disposal.

Realized gains and losses from the sale of available-for-sale securities are reported separately for each type of security. Dividends and interest income are recognized in the consolidated statements of income on an accrual basis.

Investments in shares or interests of companies where the Company has less than 20% equity interest and no significant influence, which are not publicly traded, and whose market value is not readily available, are carried at cost.

If the decline in fair value of an investment below its carrying value is other than temporary, the carrying value of the investment is reduced and a loss in the amount of any such decline is recorded. Cost method investments are evaluated for impairment when events or changes in circumstances occur which may have a significant effect on the fair value of these investments. Fair value determination is based on quoted market prices, if available, or on the present value of expected cash flows using discount rates commensurate with the risks of the investment.

**Sale and Repurchase Agreements and Securities Lending**

Sale and repurchase agreements are treated as secured financing transactions. Securities sold under sale and repurchase agreements are included in trading securities. The corresponding liability is presented within short-term debt. The difference between the sale and repurchase price is treated as interest and is accrued over the life of repurchased agreements using the effective interest method.

**Oil and Gas Exploration and Development**

In accordance with Statement of Financial Accounting Standard ("SFAS") 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies*, oil and gas exploration and development costs are recognized under the successful efforts method. This method prescribes that exploration costs, including geological and geophysical costs and the costs of dry holes, are charged to expense when incurred.

Exploratory well costs (including costs associated with stratigraphic test wells) are temporarily capitalized pending determination of whether commercial oil and gas reserves have been discovered by the drilling effort. The length of time necessary for this determination depends on the specific technical or economic difficulties in assessing the recoverability of the reserves. If a determination is made that the well did not encounter oil and gas in economically viable quantities, the well costs are expensed and are reported in "exploration expenses".

Exploratory drilling costs are temporarily capitalized pending determination of whether the well has found proved reserves if both of the following conditions are met:

- The well has found a sufficient quantity of reserves to justify, if appropriate, its completion as a producing well, assuming that the required capital expenditure is made; and
- Satisfactory progress toward ultimate development of the reserves is being achieved, with the Company making sufficient progress assessing the reserves and the economic and operating viability of the project.

Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)**

**Oil and Gas Exploration and Development (continued)**

The Company evaluates the progress made on the basis of regular project reviews which take into account the following factors:

- First, if additional exploratory drilling or other exploratory activities (such as seismic work or other significant studies) are either underway or firmly planned, the Company deems there to be satisfactory progress. For these purposes, exploratory activities are considered firmly planned only if they are included in the Company's three-year exploration plan/budget. At December 31, 2007, exploratory drilling costs capitalized on this basis were not material.
- In cases where exploratory activity has been completed, the evaluation of satisfactory progress takes into account indicators such as the fact that costs for development studies are incurred in the current period, or that governmental or other third-party authorizations are pending or that the availability of capacity on an existing transport or processing facility awaits confirmation. At December 31, 2007, exploratory drilling costs capitalized on this basis were not material.

Should the project be deemed commercially viable, it is then transferred to the development stage, otherwise the costs are expensed.

Costs, including "internal" costs relating to drilling and equipping of development wells, including development dry holes, as well as costs required for drilling and equipping of injection wells in the process of oil and gas reserves development, are capitalized. These costs are included in exploration and development assets in the consolidated balance sheet.

**Property, Plant and Equipment**

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

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

**Depreciation, Depletion and Amortization**

Depletion expense of acquisition costs of proved oil and gas properties is calculated using the unit-of-production method based on total proved reserves. Depletion expense of other capitalized costs related to oil and gas production is calculated using the unit-of production method based on proved developed reserves. Management of the Company considers each extraction division as the appropriate level for these calculations.

Acquisition costs of unproved properties are not amortized. These costs are reclassified as proved properties when the relevant reserve reclassification is made. Acquisition costs of unproved properties are reviewed for impairment. In case of impairment these costs are expensed when incurred.

Depreciation and amortization charges with respect to property, plant and equipment other than oil and gas properties is computed using the straight-line method and based on their useful lives.



## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Depreciation, Depletion and Amortization (continued)**

Depreciation rates are applied to similar types of buildings, machinery and equipment having similar economic characteristics, as shown below:

<b>Asset Group</b>	<b>Average Useful Life</b>
Buildings and constructions	30 - 35 years
Plant and machinery	15 years
Vehicles and other equipment	6 years
Service vessels	20 years
Offshore drilling assets	20 years

**Interests in Joint Operations**

A joint operation is a contractual arrangement whereby two or more parties (participants) undertake an economic activity that is subject to joint control. Joint control is only exercised when strategic, financial and operating decisions relating to the joint activity are made unanimously by all the parties. A joint venture is a registered company, partnership or any other legal form for the purposes of handling joint operations.

Financial results, assets and liabilities arising from interests in incorporated joint ventures are recognized in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in joint ventures are recognized at the cost of financial investments increased by any change to the share of net assets from the date of inception of a joint venture, less distributed earnings and impairment of financial investments. The consolidated statements of income include the Company's share in gains and losses arising from joint ventures.

The Company discontinues the use of the equity method of accounting from the date on which it ceases to have joint control over, or have significant influence in, a jointly-controlled entity, or when its interest in a jointly-controlled entity is reclassified to assets held for sale.

Undivided interests in unincorporated oil and gas joint ventures are consolidated on a proportionate basis.

A part of an interest in a jointly-controlled oil and gas exploration and production entity may be assigned to other participants or third parties. In which case, in accordance with SFAS 19, such assignment is performed and accounted for under an arrangement called a "carried interest" whereby the assignee agrees to carry all costs of drilling, developing, and operating the property. The assignee is also entitled to all of the revenue from hydrocarbon production from the property, excluding any third party interest, until all of the assignee's costs, including the contractual rate of return, have been recovered, at such time the assignor will resume its participation in operating expenses and income.

**Impairment of Long-Lived Assets**

Long-lived assets, including blocks with proved oil and gas reserves, are assessed for potential impairment in accordance with SFAS 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*.

Oil and gas properties are assessed whenever events or circumstances indicate potential impairment. If the carrying value of oil and gas properties is not recoverable through undiscounted cash flows, an impairment is recognized. The impairment is determined on the basis of the estimated fair value of oil and gas properties which, in turn, is measured by discounting future net cash flows or with reference to current market prices of oil and gas properties, if available. Discounted future cash flows from oil and gas fields are based on the most reliable management estimates of future prices that rely on recent actual prices and published prices for forward transactions; such prices are applied to forecast production volumes at particular fields with further discounting for the expected risk level.

Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)**

**Impairment of Long-Lived Assets (continued)**

Forecast production volumes shall be understood as reserves, including probable reserves that are proposed to be extracted using a known amount of capital expenditures. Production volumes and prices correspond to the internal plans and forecasts, as well as other data in the published financial statements. Assumptions regarding future prices and costs used to assess oil and gas properties for impairment differ from those used in the standard procedure for discounting net cash flows from proved oil and gas reserves.

Individual assets are grouped for impairment purposes at the lowest level of identifiable cash flows that are largely independent of the cash flows from other groups of assets – generally on a field-by-field basis for exploration and production assets, for refining assets – at the entire refining unit, for service stations – at the site level. Long-lived assets intended by management for use during a period not exceeding one year are recorded at the lower of depreciated value or fair value, less selling expenses.

Acquisition costs of unproved oil and gas properties are assessed for impairment on a regular basis and any estimated impairment is charged to expenses.

**Business Combinations**

The Company accounts for its business acquisitions under the purchase method of accounting. The total cost of acquisitions is allocated to the underlying assets, including intangible assets, and liabilities based on their respective estimated fair values. Determining the fair value of assets acquired and liabilities assumed requires management's judgment and often involves the use of significant estimates and assumptions, including assumptions with respect to future cash inflows and outflows, discount rates, licence and other asset lives and market multiples, among other items.

**Goodwill and Other Intangible Assets**

Goodwill represents the excess of the acquisition cost over the fair value of net assets acquired. The excess of the fair value of the acquired share of net assets over their acquisition cost represents negative goodwill and is allocated among the non-current assets acquired, excluding investments and deferred tax assets, which may result in their value being reduced to zero.

For investees accounted for under the equity method, the excess of the cost to acquire a share in those entities over the fair value of the acquired share of net assets as of the acquisition date is treated as embedded goodwill and is considered in computing the Company's equity share in income/loss of equity investees.

In accordance with requirements of SFAS 142, *Goodwill and Other Intangible Assets*, goodwill and intangible assets with indefinite useful lives are not amortized. Instead, they are tested at least annually for impairment.

Intangible assets that have a finite useful life are amortized using the straight-line method over the shorter of their useful life or the term established by legislation.

**Assets Held for Sale**

The Company accounts its assets as held for sale in accordance with SFAS 144, *Accounting for the Impairment or Disposal of Long-Lived Asset*. A long-lived asset (disposal group) to be sold is classified as held for sale in the period in which all of the held-for-sale criteria are met, and measured at the lower of its carrying amount or fair value less cost to sell. A long-lived asset is not depreciated (amortized) while it is classified as held for sale.

## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Capitalized Interest**

Interest expense related to the use of borrowed funds used for capital construction projects and acquisition of properties, plant and equipment is capitalized provided such interest expense could have been avoided if the Company had not made capital investments. Interest is capitalized only during the period when construction activities are actually in progress and until the resulting properties are put into operation. The Company capitalized US\$ 178 million, US\$ 109 million and US\$ 79 million of interest expenses on loans and borrowings in 2007, 2006 and 2005, respectively.

**Leasing Agreements**

Capital leases, which transfer to the Company substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the interest charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liabilities. Interest charges are charged directly to the consolidated statements of income.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term unless leased assets are capitalized because the terms of the lease agreement grant the Company ownership rights over the leased assets by the end of the lease term or containing a bargain purchase option. In the latter cases capitalized assets are depreciated over the estimated useful life of the asset regardless of the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the assets are classified as operating leases. Operating lease payments are recognized as an expense in the consolidated statements of income on a straight-line basis over the lease term.

**Asset Retirement Obligations**

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

Exploration and Production – The Company's exploration, development and production activities involve the use of the following assets: wells, related equipment and operating sites, oil gathering and treatment facilities, tank farms and in-field pipelines. Generally, licences and other regulatory acts require that such assets be decommissioned upon the completion of production. According to these requirements, the Company is obliged to decommission wells, dismantle equipment, restore the sites and perform other related activities. The Company's estimates of these obligations are based on current regulatory or licence requirements, as well as actual dismantling and other related costs. Asset retirement obligations are calculated in accordance with the provisions of SFAS 143, *Accounting for Asset Retirement Obligations*.

Refining, Marketing and Distribution – This business segment covers refining operations, marine and other distribution terminals, and retail sales. The Company's refining operations consist of major petrochemical operations and industrial complexes. These industrial complexes have been in operation for several decades. The Company's management believes that given the nature of the operations, the useful lives of these industrial complexes are indeterminable, while certain of their operating components and equipment have definite useful lives. Legal or contractual asset retirement obligations related to petrochemical, oil refining, marketing and distribution activities are not recognized due to the limited history of such activities in these segments, the lack of clear legal requirements as to the recognition of obligations, as well as the fact that useful lives of such assets are not determinable.

## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Asset Retirement Obligations (continued)**

The Company's marine and other distribution terminals, including its retail network, operate under the regulatory requirements of local authorities and lease arrangements. These requirements generally provide for elimination of the consequences of the use of those assets, including dismantling of equipment, restoration of land, etc. The Company's estimate of asset retirement obligations takes into account the above requirements.

SFAS 143 calls for measurements of asset retirement obligations to include, as a component of expected costs, an estimate of the price that a third party would demand, and could expect to receive, for bearing the uncertainties and unforeseeable circumstances inherent in the obligations, sometimes referred to as a market-risk premium. To date, the oil and gas industry has few examples of credit-worthy third parties which are willing to assume this type of risk, for a determinable price, on major oil and gas production facilities and pipelines. Therefore, because determining such a market-risk premium would be an arbitrary process, it has been excluded from the SFAS 143 estimates.

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

Because of the reasons described above the fair value of an asset retirement obligation cannot be reasonably estimated.

**Fair Value of Financial Instruments**

SFAS 107, *Disclosures about Fair Value of Financial Instruments*, defines the fair value of a financial instrument as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Financial assets and financial liabilities recognized in the accompanying consolidated balance sheets include cash and cash equivalents, short-term and long-term investments, accounts receivable and payable, short-term and long-term debt and other current and non-current assets and liabilities.

The Company, using available market information, management's estimates and appropriate valuation methodologies, has determined the approximate fair values of financial instruments.

**Income Taxes**

Russian legislation does not contain the concept of a 'consolidated tax payer' and, accordingly, the Company is not subject to Russian taxation on a consolidated basis but rather on an individual company basis. Income taxes are provided on taxable profit as determined under the Russian Federation Tax Code. Deferred income tax assets and liabilities are recognized in the accompanying consolidated financial statements in the amount determined by the Company using the liability method in accordance with SFAS 109, *Accounting for Income Taxes*. This method takes into account future tax consequences, based on the effective tax rate, associated with differences between the carrying values of assets and liabilities and their taxable base, which gives immediate income statement effect to changes in income tax laws, including changes in the tax rates. A valuation allowance for a deferred tax asset is recorded when management believes that it is more likely than not that this tax asset will not be realized.

## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Income Taxes (continued)**

Starting from January 1, 2007 the Company accounts for uncertain tax positions in accordance with FIN 48 *Accounting for Uncertainty in Income Taxes*. Liabilities for unrecognized income tax benefits under the provisions of FIN 48 together with corresponding interest and penalties are recorded in the consolidated statement of income as income tax expense. The adoption of FIN 48 had an insignificant impact on the consolidated financial statements.

**Derivative Instruments**

All derivative instruments are recorded on the consolidated balance sheets at fair value in either other current assets, other non-current assets, other current liabilities or other non-current liabilities. Recognition and classification of the gain or loss that results from recording and adjusting a derivative to fair value depends on the purpose for issuing or holding the derivative. Gains and losses from derivatives that are not accounted for as hedges under SFAS 133, *Accounting for Derivative Instruments and Hedging Activities*, are recognized immediately in the consolidated statement of income.

**Recognition of Revenues**

Revenues are recognized when title passes from the seller to the customer, the contract price is fixed or determinable and collectability of the receivable is reasonably assured. Specifically, domestic sales of crude oil and gas, as well as petroleum products and materials are recognized when title passes. For export sales, title generally passes at the border of the Russian Federation and the Company covers transportation expenses (except freight), duties and taxes on those sales. Revenues include excise taxes and custom duties (see Note 19).

Sales of support services are recognized as services are performed provided that the service price can be determined and no significant uncertainties regarding the receipt of revenues exist.

**Transportation Expenses**

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

**Refinery Maintenance Costs**

The Company recognizes the costs of overhauls and preventive maintenance performed with respect to oil refining assets as expenses when incurred.

**Environmental Liabilities**

Environmental expenditures are expensed or capitalized, depending upon their future economic benefit. Expenditures that relate to an existing condition caused by past operations, and do not have a future economic benefit, are expensed. Liabilities for these expenditures are recorded on an undiscounted basis when environmental assessments or clean-ups are probable and the costs can be reasonably estimated.

Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)**

**Guarantees**

The fair value of a guarantee is determined and recorded as a liability at the time when the guarantee is issued. The initial guarantee amount is subsequently remeasured to reflect the changes in the underlying liability. The expense is included in the related line items of the consolidated statements of income, based on the nature of the guarantee. When the likelihood of performing on a guarantee becomes probable, a liability is accrued, provided it is reasonably determinable on the basis of the facts and circumstances at that time.

**Comprehensive Income**

The Company applies SFAS 130, *Reporting Comprehensive Income*, which establishes standards for the calculation and reporting of the Company's comprehensive income (net income plus all other changes in net assets from non-owner sources) and its components in consolidated financial statements. As of December 31, 2007, 2006 and 2005, there are no material comprehensive income items and, therefore, comprehensive income for 2007, 2006 and 2005 equals net income.

**Accounting for Contingencies**

Certain conditions may exist as of the date of these consolidated financial statements which may further result in a loss to the Company, but which will only be resolved when one or more future events occur or fail to occur. The Company's management makes an assessment of such contingent liabilities which is based on assumptions and is a matter of opinion. In assessing loss contingencies relating to legal or tax proceedings that involve the Company or unasserted claims that may result in such proceedings, the Company, after consultation with legal or tax advisors, evaluates the perceived merits of any legal or tax proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a loss will be incurred and the amount of the liability can be estimated, then the estimated liability is accrued in the Company's consolidated financial statements. If the assessment indicates that a potentially material loss contingency is not probable, but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed.

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

**Taxes Collected from Customers and Remitted to Governmental Authorities**

Excise taxes are reported gross within sales and other operating revenues and taxes other than income taxes, while value-added tax is recorded net in taxes other than income taxes.

## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Recent Accounting Standards**

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements*. The standard defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements. Accordingly, this standard does not require any new fair value measurements. In February 2008, the FASB issued a FASB Staff Position (FSP) on SFAS 157 that permits a one-year delay of the effective date for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The Company will adopt this standard effective January 1, 2008, with the exceptions allowed under the FSP SFAS 157 described above. The Company does not expect SFAS 157 to have a material impact on the Company's consolidated financial statements, other than additional disclosures.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. The standard permits all entities to choose to elect, at specified election dates, to measure eligible financial instruments at fair value. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date, and recognize upfront costs and fees related to those items in earnings as incurred and not deferred. This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company will apply this standard for financial statements issued for fiscal year beginning from January 1, 2008. The Company does not expect this standard to have a material impact on the Company's financial position and results of operations.

In May 2007, the FASB issued FSP FIN 39-1, *Amendment of FASB Interpretation No. 39* ("FSP FIN 39-1"), to amend paragraph 10 of FIN 39, *Offsetting of Amounts Related to Certain Contracts* ("FIN 39"), to permit a reporting entity that is party to a master netting arrangement to offset the receivable or payable recognized upon payment or receipt of cash collateral against the fair value amounts recognized against derivative instruments that had been offset under the same master netting arrangement in accordance with paragraph 10. FSP FIN 39-1 also amends paragraph 3 of FIN 39 to replace the terms, "conditional contracts" and "exchange contracts," with the broader term, "derivative contracts," as defined in SFAS 133. FSP FIN 39-1 applies to fiscal years beginning after November 15, 2007, with early application permitted. The Company does not expect FSP FIN 39-1 to have a material impact on the Company's consolidated financial statements.

In December 2007, FASB issued SFAS 141 (Revised), *Business Combinations* ("SFAS 141(R)"). This Statement retains the fundamental requirements in SFAS 141 that acquisition method of accounting be used for all business combinations and for an acquirer to be identified for each business combination, but expands the scope of acquisition accounting to all transactions and circumstances under which control of business is obtained. SFAS 141(R) shall be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Earlier application is prohibited. The Company will apply this standard for its consolidated financial statements issued for fiscal periods beginning January 1, 2009. This standard will not have a material impact on the Company's consolidated financial position and results of operations until the Company makes a significant acquisition.

## Notes to Consolidated Financial Statements (continued)

**2. Significant Accounting Policies (continued)****Recent Accounting Standards (continued)**

In December 2007, FASB issued SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements* ("SFAS 160"). This Statement amends Accounting Research Bulletin ("ARB") 51, *Consolidated Financial Statements*, to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 shall be effective for fiscal periods beginning on or after December 15, 2008. Earlier adoption is prohibited. The Company will apply this standard for its consolidated financial statements issued for fiscal year beginning January 1, 2009. The Company has not yet identified the impact this standard will have on the Company's consolidated financial position and results of operations.

In March 2008, FASB issued SFAS 161, *Disclosures about Derivative Instruments and Hedging Activities* ("SFAS 161"). This Statement changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 shall be effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. Early application is encouraged. SFAS 161 encourages but does not require disclosures for earlier periods presented for comparative purposes at initial adoption. In years after initial adoption, SFAS 161 requires comparative disclosures only for periods subsequent to initial adoption. The Company will apply this standard for its consolidated financial statements issued for fiscal periods beginning January 1, 2009. Application of SFAS 161 will have no impact on the Company's financial position and results of operations, other than additional disclosures.

**3. Significant Acquisitions**

From April through August 2007, Neft-Aktiv LLC, the Company's wholly owned subsidiary, won a number of auctions for the sale of certain assets of Yukos Oil Company following the bankruptcy proceedings of Yukos Oil Company. The following discussion summarises these acquisitions.

On April 18, 2007, Neft-Aktiv LLC won an auction for the sale of interests in several service companies located in Western Siberia regions of the Russian Federation providing oilfield services to RN-Yuganskneftegaz LLC, the Company's wholly owned subsidiary. The acquisition price amounted to RUB 1.03 billion (US\$ 40 million at the CBR official exchange rate as of the dates of acquisitions). The acquisition of these assets was executed to further improve of oil production efficiency at the Company's West-Siberian oil fields.

As a result of the preliminary allocation the acquisition price was fully allocated to the fair value of assets acquired and liabilities assumed.



# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 3. Significant Acquisitions (continued)

On May 3, 2007, Neft-Aktiv LLC won an auction for the sale of interests in 37 exploration and production, refining and marketing companies in Western and Eastern Siberia region of the Russian Federation. The acquisition price amounted to RUB 175.70 billion (US\$ 6.82 billion at the CBR official exchange rate as of the dates of acquisitions). In particular, the following assets were acquired:

Name	Nature of Business	Equity interest acquired
		%
OJSC Tomskneft VNK	Oil and gas development and production	100.00
OJSC Angarsk Petrochemical Company	Petroleum refining	100.00
OJSC Achinsk Refinery VNK	Petroleum refining	100.00
OJSC Angarsk Polymer Plant	Petroleum refining	100.00
Strezhevskoy Refinery LLC	Petroleum refining	100.00
OJSC East-Siberian Oil and Gas Company	Oil and gas development and production	70.78
OJSC Tomskaya Raspersdelitelnaya Company	Electricity transmission and distribution	25.88
OJSC Tomskaya Energosbytovaya Company	Electricity distribution	25.88
OJSC Tomskie Magistralnye Seti	Electricity transmission and distribution	25.88
OJSC Tomskelektrosetremont	Electricity networks repair services	25.88
OJSC Tomskeneregomont	Electricity networks repair services	25.88
OJSC Tomskenergo	Electricity transmission and distribution	25.88
CJSC Irkutsknefteprodukt	Marketing and distribution	100.00
OJSC Buryatnefteprodukt	Marketing and distribution	95.10
CJSC Khakasnefteprodukt VNK	Marketing and distribution	100.00
OJSC Tomsknefteprodukt VNK	Marketing and distribution	100.00

As a result of the preliminary allocation the acquisition price was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 5.24 billion (see also Note 17).

On May 10, 2007, Neft-Aktiv LLC won an auction for the sale of interests in 28 exploration and production, refining and marketing companies in the Samara region of the Russian Federation. The acquisition price amounted to RUB 165.53 billion (US\$ 6.42 billion at the CBR official exchange rate as of the dates of acquisitions). In particular, the following assets were acquired:

Name	Nature of Business	Equity interest acquired
		%
OJSC Samaraneftgaz	Oil and gas development and production	100.00
OJSC Kuybyshev Refinery	Petroleum refining	100.00
OJSC Novokuybyshev Refinery	Petroleum refining	100.00
OJSC Syzran Refinery	Petroleum refining	100.00
CJSC Neftegorsk Gas-Processing Plant	Gas processing	98.10
CJSC Otradny Gas-Processing Plant	Gas processing	98.10
OJSC Samaranefteprodukt	Marketing and distribution	100.00
Samara Terminal LLC	Marketing and distribution	100.00

As a result of the preliminary allocation the acquisition price was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 5.04 billion.

On May 16, 2007, Neft-Aktiv LLC won an auction for the sale of interests in several small service and information technology companies. The acquisition price amounted to RUB 1.80 billion (US\$ 70 million at the CBR official exchange rate as of the dates of acquisitions).

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 3. Significant Acquisitions (continued)

As a result of the preliminary allocation the acquisition price was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 70 million.

On June 15, 2007, Neft-Aktiv LLC acquired from Unitex LLC assets that were previously owned by Yukos Oil Company, including interests in companies engaged in retail and wholesale of petroleum products and providing services related to storage of petroleum products in the European part of the Russian Federation. The Company acquired these assets to develop its own oil product distribution network following the growth of oil refining capacity as well as to expand its presence in the European part of the Russian Federation oil products market. The acquisition price amounted to RUB 16.32 billion (US\$ 627 million at the CBR official exchange rate as of the dates of acquisitions). In particular, the following assets were acquired:

Name	Nature of Business	Equity interest acquired
		%
OJSC Belgorodnefteprodukt	Marketing and distribution	100.00
CJSC Bryansknefteprodukt	Marketing and distribution	100.00
OJSC Voronezhnefteprodukt	Marketing and distribution	100.00
CJSC Lipetsknefteprodukt	Marketing and distribution	100.00
CJSC Orelnefteprodukt	Marketing and distribution	100.00
CJSC Penzanefteprodukt	Marketing and distribution	100.00
CJSC Tambovnefteprodukt	Marketing and distribution	100.00
CJSC Ulyanovsknefteprodukt	Marketing and distribution	100.00
Ulyanovsk Terminal LLC	Marketing and distribution	100.00
CJSC FPK KEDR M	Marketing and distribution	100.00
CJSC NBA Service	Marketing and distribution	100.00
OJSC Germes Moskva	Marketing and distribution	82.80
CJSC Contract Oil	Marketing and distribution	100.00
CJSC Mytischki Fuel Company	Marketing and distribution	100.00

As a result of the preliminary allocation the acquisition price was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 627 million.

At the end of June 2007 Rosneft and Neft-Aktiv LLC acquired from Prana LLC (further 'Prana') assets that were previously owned by Yukos Oil Company, including the 100% interest in Dubininskoe LLC which owns office property, and the 100% interest in Trade House Yukos-M LLC which owns operational and management assets of exploration and production and refining and marketing companies. The main purposes of the purchase were to acquire the relevant fixed and working capital assets, to facilitate the integration processes in relation to recently acquired oil production, refining and marketing companies that had previously been managed by these entities acquired from Prana and also to minimize operational, financial and other intragroup risks of the assets previously acquired. The acquisition price amounted to RUB 87.58 billion (US\$ 3.38 billion at the CBR official exchange rate as of the dates of acquisitions).

As a result of the preliminary allocation the acquisition price was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 2.0 billion.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 3. Significant Acquisitions (continued)

In early July 2007 Neft-Aktiv LLC acquired shares and interests in oil production and marketing companies located in the South region of the Russian Federation. Pursuant to the decision of the Yukos Oil Company Creditors' Committee dated May 16, 2007, Neft-Aktiv LLC, being a runner-up in the auction of May 3, 2007 was granted the right to enter into the agreement for sale and purchase of assets earlier sold at that auction. In June 2007 Neft-Aktiv LLC signed the sale and purchase agreement and the transaction was completed in early July 2007. The Company acquired these assets to develop its retail network following the growth of the refining capacity as well as to expand its presence in the European part of the Russian Federation. The acquisition price amounted to RUB 4.9 billion (US\$ 190 million at the CBR official exchange rate as of the dates of acquisitions). In particular, the following assets were acquired:

Name	Nature of Business	Equity interest acquired %
OJSC Caspian Oil Company	Oil and gas development and production	49.89
Val Shatskogo LLC	Oil and gas development and production	100.00
OJSC Stavropolnefteproduct	Marketing and distribution	100.00
U-Kuban LLC	Marketing and distribution	51.00
OJSC Kuban Generating Company	Electricity generation	26.26
OJSC Kuban Energosbytovaya Company	Electricity distribution	26.26
OJSC Kubanskiye Magistralnye Seti	Electricity transmission and distribution	26.26
OJSC Kubanenergo	Electricity transmission and distribution	26.26

As a result of the preliminary allocation the acquisition price was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 158 million.

On August 8, 2007 the Company won an auction for the sale of shares and interests in eight marketing and service companies together with certain other assets which primarily included property, plant and equipment located in the West Siberia region of the Russian Federation and related to the exploration, production and transportation of crude oil. The acquisition price of shares and interests in companies amounted to RUB 9.05 billion (US\$ 360 million at the CBR official exchange rate as of the dates of acquisitions), and the acquisition price of property, plant and equipment amounted to RUB 7.97 billion (US\$ 311 million at the CBR official exchange rate as of the dates of acquisitions). The principle acquisition is a 100% interest in CJSC YUKOS-Transservice located in the Samara region of the Russian Federation. CJSC YUKOS-Transservice provides petroleum products transportation services.

As a result of the preliminary allocation the acquisition price attributable to the interests in eight marketing and service companies was allocated to the fair value of assets acquired and liabilities assumed in the amount of US\$ 360 million. The remaining US\$ 311 million represents asset acquisitions and were allocated in full to the fair value of wells and related facilities located on fields where the Company already had the necessary licences.

Over the course of the acquisitions in the second and third quarters of 2007, the Company acquired more than 140 legal entities, including three large upstream subsidiaries with significant current production and estimated proved and probable reserves, five refineries with significant aggregate economic distillation capacity, a significant number of retail stations as well as management assets, including real estate, information technology, personnel, and know-how which for previous years had been operating the assets. These acquisitions amounted to US\$14.3 billion, net of cash received for the sale of 50% interest in OJSC Tosmskneft VNK and certain other assets (see Note 17). As a result, the Company significantly increased its crude oil production and refining capacity, entered new geographical markets and substantially expanded its retail network and customer base creating a platform to achieve better downstream margins and added flexibility in netback options. Through such increased margins and incremental flexibility, management is confident that these acquisitions increase Rosneft's ability to earn a higher rate of return across its asset portfolio. Such value stems from the synergies which exist between the assets acquired both across lots and with Rosneft's historical assets as well as strategic benefits drawn from the new markets and geographic regions to which the Company now has access.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 3. Significant Acquisitions (continued)

Based on the preliminary purchase price allocation, total goodwill in the amount of US\$ 4.37 billion is attributed primarily to the refinery, marketing and distribution segment (US\$ 2.92 billion), as well as to the exploration and production segment (US\$ 1.45 billion) which are both expected to benefit from the synergies of the acquisitions. Included in the latter is US\$ 743 million related to OJSC Tosmskneft VNK and certain other assets, 50% of which was sold in December 2007 (see Note 17). None of the goodwill is deductible for tax purposes.

The Company consolidated the operating results of the acquired assets starting from the date on which ownership was transferred. The transfer date is different for every asset and depends on the date of signing the transfer act (for joint-stock companies) or the notice date (for limited liability companies).

The following table summarizes the Company's preliminary purchase price allocation to the fair value of assets acquired and liabilities assumed:

	Preliminary purchase price allocation	Purchase price allocation adjustments	Current preliminary purchase price allocation
<b>ASSETS</b>			
<b>Current assets:</b>			
Cash and cash equivalents	1,197	(12)	1,185
Short-term investments	633	65	698
Accounts receivable	3,398	(276)	3,122
Inventories	849	11	860
Prepayments and other current assets	543	3	546
<b>Total current assets</b>	<b>6,620</b>	<b>(209)</b>	<b>6,411</b>
Long-term investments	161	48	209
Property, plant and equipment	13,825	1,395	15,220
Intangible assets	–	274	274
Deferred tax assets	114	81	195
Other non-current assets	204	37	241
<b>Total non-current assets</b>	<b>14,304</b>	<b>1,835</b>	<b>16,139</b>
<b>Total assets</b>	<b>20,924</b>	<b>1,626</b>	<b>22,550</b>
<b>LIABILITIES</b>			
Accounts payable	1,282	(56)	1,226
Short-term loans and borrowings and current portion of long-term debt	2,512	(14)	2,498
Income and other tax liabilities	649	(140)	509
Deferred tax liability	280	(43)	237
Other current liabilities	344	43	387
<b>Total current liabilities</b>	<b>5,067</b>	<b>(210)</b>	<b>4,857</b>
Asset retirement obligations	497	411	908
Long-term debt	978	(27)	951
Deferred tax liability	1,935	462	2,397
Other non-current liabilities	152	41	193
<b>Total non-current liabilities</b>	<b>3,562</b>	<b>887</b>	<b>4,449</b>
<b>Total liabilities</b>	<b>8,629</b>	<b>677</b>	<b>9,306</b>
<b>Total net assets acquired</b>	<b>12,295</b>	<b>949</b>	<b>13,244</b>
<b>Minority interest</b>	<b>(11)</b>	<b>3</b>	<b>(8)</b>
<b>Purchase price</b>	<b>17,551</b>	<b>56</b>	<b>17,607</b>
<b>Goodwill</b>	<b>5,267</b>	<b>(896)</b>	<b>4,371</b>

Property, plant and equipment includes mineral rights in the amount of US\$ 219 million.

Notes to Consolidated Financial Statements (continued)

**3. Significant Acquisitions (continued)**

Other current liabilities and other non-current liabilities include accrued liabilities for preacquisition contingencies in the amount of US\$ 198 million and US\$ 55 million, respectively. These contingent liabilities arose from lawsuits against the newly acquired companies. Tax related preacquisition contingencies in the amount of US\$ 179 million are included within income and other tax liabilities.

The preliminary purchase price allocation, which already included adjustments, made in the third quarter of 2007, was adjusted due to the revisions made in the fourth quarter of 2007 of fair values of the assets acquired and liabilities assumed which primarily include refinement of the fair values of property, plant and equipment, recognition of additional accounts receivable (see Note 7), additional tax and other liabilities and additional asset retirement obligations identified.

This purchase price allocation and the allocation of goodwill among reporting units is still preliminary and the Company expects to finalize the allocation following the conclusion of the fair values determination of all the assets acquired and liabilities assumed.

Pro forma financial information assuming that the acquisition of assets occurred as of the beginning of 2005, which is required by SFAS 141 has not been presented herein as the Company does not have access to reliable US GAAP financial information regarding the acquired assets for the periods prior to the acquisition.

**4. Other Acquisitions and Share Swap**

**Asset Acquisitions**

On July 12, 2007 the Company won an auction for the sale of certain assets which primarily include property, plant and equipment, as well as licences related to the exploration and production of crude oil in Western and Eastern Siberia and in the Samara regions of the Russian Federation. The acquisition price amounted to RUB 5.8 billion (US\$ 229 million at the CBR exchange rate as of the dates of acquisitions).

On August 15, 2007 the Company won an auction for the sale of the rights to claim the accounts receivable of Yukos Oil Company. The acquisition price amounted to RUB 11.56 billion (US\$ 445 million at the CBR exchange rate as of the date of acquisition). The majority of the acquired receivables pertains to amounts due from former Yukos subsidiaries acquired by the Company at the previous auctions for the sale of the assets of Yukos Oil Company and totals RUB 7.93 billion (US\$310 million at the CBR exchange rate as of the date of acquisition) (see Note 7).

**OJSC Ohinskaya TETS**

In January 2007, the Company paid RUB 629 million (US\$ 24 million at the CBR exchange rate as of the transaction date) to acquire 55,331,951 ordinary shares of OJSC Ohinskaya TETS. Immediately after this acquisition, the Company's ownership interest became 85.61% of OJSC Ohinskaya TETS's total equity. Further in April 2007, the Company acquired 9,876,869 of additional ordinary shares of OJSC Ohinskaya TETS, increasing its share in the entity's total equity to 87.52%. The purchase price amounted to RUB 112 million (US\$ 4 million at the CBR exchange rate as of the dates of acquisition).

OA O Ohinskaya TETS is a local Sakhalin producer and seller of electrical power and heat. One of the main consumers of OJSC Ohinskaya TETS's output is RN-Sakhalinmorneftegaz LLC, the Company's subsidiary.

The primary reason for this acquisition was to improve electricity supply management. The purchase price was fully allocated to the fair value of assets acquired and liabilities assumed. The results of operations of OJSC Ohinskaya TETS are not significant and therefore pro forma financial information has not been disclosed herein.

**4. Other Acquisitions and Share Swap (continued)**

**OJSC Verkhnechonskneftegaz**

In January 2007, the Company bought 339,582 additional ordinary shares of OJSC Verkhnechonskneftegaz for RUB 201 million (US\$ 7.6 million at the CBR exchange rate as of the transaction date). Through this purchase the Company maintained its previous share of 25.94% in this investment.

**CJSC Yukos-Mamontovo**

On April 3, 2007, the Company received the title to 100% interest in CJSC Yukos-Mamontovo in settlement of an ownership claim brought by the Company. The title to this asset was transferred in accordance with the court ruling issued by the Moscow Arbitration Court. CJSC Yukos-Mamontovo is the owner of service facilities leased by RN-Yuganskneftegaz LLC and used in crude oil production. The receipt of this interest was accounted for as a revision to the original purchase accounting of OJSC Yuganskneftegaz with no material effect on the Company's consolidated financial statements.

**CJSC Vlakra**

In late June 2007, the Company acquired 5,860 ordinary shares of OJSC Vlakra which accounted for 50% of the total number of ordinary shares issued by this entity. CJSC Vlakra has the right to use a land plot and office premises located in Moscow.

The purchase price of the above shares amounted to US\$ 108 million and was paid for in cash. The acquisition price was fully allocated to the fair values of the acquired assets and liabilities. The Company accounts for this investment under the equity method of accounting.

**Acquisition of Oil Products Retail Networks**

*OJSC JV ANTARES*

In August 2007 the Company acquired a 100% interest in OJSC JV ANTARES, an indirect owner of a network of gas stations and an oil tank farm in the Moscow Region, for US\$ 55 million.

*Oxoil Limited*

In September 2007 the Company acquired a 100% interest in Oxoil Limited (Cyprus), an indirect owner of a network of gas stations in the Moscow Region, for US\$ 42 million.

*Rokada Market LLC*

In August 2007 a subsidiary of the Company – OJSC Rosneft-Stavropolye acquired a 100% interest in Rokada Market LLC for RUB 1,482 million (US\$ 57.8 million at the CBR exchange rate as of the transaction date). Rokada Market LLC is the owner of a network of gas stations and an oil tank farm in the Stavropol Region of the Russian Federation.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 4. Other Acquisitions and Share Swap (continued)

#### Acquisition of Oil Products Retail Networks (continued)

The following table summarizes the Company's preliminary purchase price allocation of OJSC JV ANTARES, Oxoil Limited and Rokada Market LLC to the estimated fair values of assets acquired and liabilities assumed:

Current assets	27
Non-current assets	157
<b>Total assets</b>	<b>184</b>
Current Liabilities	25
Non-current liabilities	4
<b>Total liabilities</b>	<b>29</b>
<b>Total net assets acquired</b>	<b>155</b>

This purchase price allocation is preliminary pending final determination of the fair values of assets acquired and liabilities assumed. The results of operations of OJSC JV ANTARES, Oxoil Limited and Rokada Market LLC are not material and therefore pro forma financial information has not been disclosed herein.

#### E&P Vankor Ltd

In October 2007, Anglo Siberian Oil Company Limited, the Company's wholly owned indirect subsidiary, bought 100% of the shares of E&P Vankor Ltd for US\$ 88 million. E&P Vankor Ltd is the beneficiary of a successful legal claim against Anglo Siberian Oil Company Limited. The Company has accrued US\$ 134 million in respect of this claim as of December 31, 2006 (see also Note 15). E&P Vankor Ltd does not own any other significant assets and has no liabilities other than a related tax liability of US\$ 46 million. Accordingly this transaction has been accounted for as an asset acquisition.

#### Share Swap

In June 2006, the shareholders of Rosneft and of the Merging Subsidiaries (see Note 1) approved the conversion of shares of the Merging Subsidiaries into the Company's shares at agreed conversion ratios. Subsequent to this, the Merging Subsidiaries were merged with the Company. 1,220,939,458 shares of Rosneft were issued to acquire the shares of minority shareholders of these Merging Subsidiaries (11.52% of the Rosneft's share capital).

This acquisition of minority interest was accounted for as a purchase, in accordance with SFAS 141, *Business Combinations*. The fair value of purchase consideration, that is Rosneft shares, issued for the Share Swap, was determined based on the market value of the shares as of the date nearest to the date on which all the terms of the deal were agreed upon and amounted to US\$ 9,218 million. The excess of the fair value of the shares issued over the fair value of minority interests acquired in the amount of US\$ 69 million was recorded as goodwill and relates to the refining and marketing segment. The Company attributes this goodwill to the synergy effects from the merger. The majority of the purchase price was allocated to oil and gas properties, property, plant and equipment and mineral rights. Where the fair value of the net assets acquired exceeded the purchase price, negative goodwill existed which has reduced, on a pro rata basis, the amounts assigned to the non-current assets acquired.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 5. Cash and Cash Equivalents

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

	2007	2006
Cash on hand and in bank accounts in RUB	474	244
Cash on hand and in bank accounts in foreign currencies	111	192
Deposits and other	413	69
<b>Total cash and cash equivalents</b>	<b>998</b>	<b>505</b>

Restricted cash as of December 31 comprises the following:

	2007	2006
Obligatory reserve with the CBR	25	18
Other restricted cash	9	–
<b>Total restricted cash</b>	<b>34</b>	<b>18</b>

The obligatory reserve with the CBR represents the amounts deposited by the Company's subsidiary bank, VBRR with the CBR for securing the current operating activity of the bank. Credit institutions are required to maintain a non-interest earning cash deposit (obligatory reserve) with the CBR, which amount depends on the level of funds raised by the credit institution and this amount has certain restrictions for use.

Cash accounts denominated in foreign currencies represent primarily cash in US dollars.

Deposits and other represent primarily bank deposits denominated in RUB that may be readily convertible into cash and may be withdrawn by the Company at any time without prior notice or penalties.

As part of its cash management and credit risk function, the Company regularly evaluates the creditworthiness of financial and banking institutions where it deposits cash. Banking relationships are primarily with Russian subsidiaries of international banking institutions and certain large Russian banks.

### 6. Short-Term Investments

Short-term investments as of December 31 comprise the following:

	2007	2006
Short-term loans granted	4	2
Loans to related parties	25	34
Promissory notes held to maturity	123	–
Trading securities		
Promissory notes	1	91
Corporate and state bonds	149	170
Other	4	39
Available-for-sale securities	18	120
Bank deposits	5	–
Other	9	4
<b>Total short-term investments</b>	<b>338</b>	<b>460</b>



# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 6. Short-Term Investments (continued)

State bonds primarily represent federal loan bonds issued by the Ministry of Finance of the Russian Federation with maturities ranging from May 2008 to February 2036, coupon yields in 2007 ranging from 3.0% p.a. to 12.5% p.a.

Corporate bonds represent bonds issued by large Russian corporations and bonds issued by the CBR with maturities ranging from October 2008 to September 2010 and interest rates ranging from 5.0% to 14.0%.

Short-term promissory notes held to maturity are denominated in RUB and bear interest rates ranging from 8.0% to 14.0%.

### 7. Accounts Receivable, Net

Accounts receivable as of December 31 comprise the following:

	<b>2007</b>	<b>2006</b>
Trade receivables	<b>3,812</b>	1,176
Value-added tax receivable	<b>4,029</b>	2,092
Other taxes	<b>499</b>	117
Banking loans to customers	<b>996</b>	580
Accounts receivable from Yukos Oil Company	–	810
Other	<b>521</b>	140
Less: allowance for doubtful accounts	<b>(72)</b>	(65)
<b>Total accounts receivable, net</b>	<b>9,785</b>	4,850

The Company's trade accounts receivable are denominated primarily in US dollars. Credit risk is managed through the use of letters of credit.

Value added tax receivable ("VAT") primarily includes input VAT associated with export sales, which is reimbursed from the budget in accordance with Russian tax legislation.

In June and October 2007, the Company received approximately RUB 294.3 billion (US\$ 11.5 billion at the CBR exchange rate as of the date of receipt) from the receiver as a result of Yukos Oil Company bankruptcy proceedings. The amount of US\$ 483 (see Note 9) million was recorded in these consolidated financial statements as a repayment of debt receivable previously acquired, and US\$ 8,970 million was recorded as income in the consolidated statement of income. The remaining US\$ 2,037 million was recognized as a repayment of previously recorded accounts receivable.

Other accounts receivable include those acquired by the Company through the auction on August 15, 2007 from Yukos Oil Company (see Note 4). As of December 31, 2007, the amount of unsettled receivables was US\$ 140 million.

### 8. Inventories

Inventories as of December 31 comprise the following:

	<b>2007</b>	<b>2006</b>
Materials and supplies	<b>503</b>	348
Crude oil and gas	<b>516</b>	329
Petroleum products	<b>907</b>	228
<b>Total inventories</b>	<b>1,926</b>	905

Materials and supplies mostly include spare parts. Petroleum products also include those designated for sale as well as for own use.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 9. Prepayments and Other Current Assets

Prepayments and other current assets as of December 31 comprise the following:

	2007	2006
Prepayments to suppliers	803	599
Insurance prepayments	21	27
Customs	814	442
Acquired debt receivable	–	483
Other	93	38
<b>Total prepayments and other current assets</b>	<b>1,731</b>	<b>1,589</b>

Customs primarily represent export duty prepayments related to the export of crude oil and petroleum products (see Note 19).

The acquired debt receivable was fully repaid in June 2007 (see Note 7).

### 10. Long-Term Investments

Long-term investments as of December 31 comprise the following:

	2007	2006
<b>Equity method investments</b>		
OJSC Tomskneft VNK	1,419	–
Polar Lights Company LLC	153	132
JV Rosneft-Shell Caspian Ventures Limited	27	26
OJSC Daltransgaz	49	57
OJSC Verkhnechonskneftegaz	222	225
Taihu Ltd	–	–
CJSC Vlakra	108	–
OJSC Kubanenergo	102	–
OT Belokamenka LLC	2	2
CJSC Kaspiy-1	–	–
Other	208	4
<b>Total</b>	<b>2,290</b>	<b>446</b>
<i>Available-for-sale securities</i>		
Russian government bonds	1	1
OJSC TGK-11	43	–
Long-term promissory notes	7	14
<i>Held-to-maturity securities</i>		
Long-term loans granted	3	9
Long-term loans to equity investees	279	80
Cost method investments	19	17
Other	4	1
<b>Total long-term investments</b>	<b>2,646</b>	<b>568</b>

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 10. Long-Term Investments (continued)

Equity share in income/(loss) of material investments recorded using the equity method:

	Participation interest (percentage) as of December 31, 2007	Share in income/(loss) of equity investees		
		2007	2006	2005
Polar Lights Company LLC	50.00	36	47	42
CJSC Kaspiy-1	41.22	–	(29)	–
OJSC Verkhnechonskneftegaz	25.94	(11)	(6)	1
JV Rosneft-Shell Caspian Ventures Limited	51.00	6	7	7
OJSC Tomskneft VNK	50.00	5	–	–
Taihu Ltd	51.00	–	–	–
OJSC Daltransgaz	25.00	(8)	–	–
Other	various	(5)	(2)	1
<b>Total equity share</b>		<b>23</b>	<b>17</b>	<b>51</b>

#### Polar Lights Company LLC ("PLC")

PLC is a limited liability company owned 50% by Conoco Phillips Timan-Pechora Inc., and 50% by the Company. PLC is primarily engaged in the development of the Ardalin and satellite fields in the Timan-Pechora Basin located 125 kilometers south of the Barents Sea above the Arctic Circle. Development of the Ardalin field commenced in late 1992 and the first oil was produced in 1994.

#### JV Rosneft-Shell Caspian Ventures Limited

JV Rosneft-Shell Caspian Ventures Limited ("JV") is a joint venture in which the Company holds a 51% interest. The Articles of Incorporation of this joint venture stipulate, however, that key decisions regarding its business shall be subject to unanimous approval by both participants and none of the participants has a preferential voting right.

On February 6, 1997, the Company, through the JV, signed an agreement with eight oil and gas companies and government agencies of the Russian Federation and the Republic of Kazakhstan for the establishment of Caspian Pipeline Consortium ("CPC"). The purpose of the consortium is to design, finance, construct and operate a pipeline from the oil fields located in Western Kazakhstan through Russia to the port of Novorossiysk. The interest of the JV in the CPC is 7.5%. In October 2001, the CPC pipeline was put in operation.

#### OJSC Daltransgaz

OJSC Daltransgaz is an operator for the program to supply gas to the Sakhalin Region and the Khabarovsk and Primorye Territories.

#### OJSC Verkhnechonskneftegaz

OJSC Verkhnechonskneftegaz holds the licence for the development of the Verkhnechonskoye oil and gas condensate deposit, which is the largest oil deposit in the Irkutsk region.

#### CJSC Kaspiy-1

In 1997, a subsidiary of the Company made a contribution to the share capital of CJSC Kaspiy-1 which was founded to construct an oil refinery in Makhachkala (the Republic of Dagestan). The refinery has been commissioned. Due to significant and continuous capacity underutilization, the Company considered that decline in fair value is other-than temporary and the carrying amount of this investment was fully written-down in 2006 in the amount of US\$ 29 million.

**10. Long-Term Investments (continued)**

**Taihu Ltd / OJSC Udmurtneft**

In November 2006, the Company acquired a 51% equity share in Taihu Ltd, a joint venture incorporated with the intention of managing the activity of OJSC Udmurtneft. The Company paid 5,100 Cyprus Pounds (approximately US\$ 11 thousand) for this investment which has been included within equity method investments. The other party to the joint venture is China Petrochemical Corporation ("Sinopec") with a respective share of 49%.

The Shareholder Agreement in respect of this joint venture stipulates that key decisions regarding its business shall be subject to unanimous approval by both participants and none of the participants has a preferential voting right.

In December 2006, Taihu Ltd, through its wholly owned subsidiary, acquired a 96.86% equity interest in OJSC Udmurtneft for US\$ 3,541 million. The credit facility for financing the purchase of 96.86% shares of OJSC Udmurtneft was provided to Taihu Ltd by Bank of China and principally secured by OJSC Udmurtneft's shares, without recourse to the Company.

OJSC Udmurtneft is located in the Volga-Ural region of the Russian Federation and holds the licences for the development of 24 productive oil and gas condensate deposits. OJSC Udmurtneft is a group of 17 companies.

**OJSC Tomskneft VNK**

In December 2007, the Company finalized the sale of 50% equity interests in OJSC Tomskneft VNK, Strezhevskoy Refinery LLC and several other companies which had been previously acquired through the auction for the sale of the assets of Yukos Oil Company (see Note 3 and Note 17). The Shareholder Agreement provides that key decisions regarding the business operations of OJSC Tomskneft VNK shall be subject to unanimous approval by both participants and none of the participants has a preferential voting right. The investment in OJSC Tomskneft VNK includes goodwill of US\$ 368 million.

**OJSC TGK-11, OJSC Kubanenergo and Other Electric Power Companies**

The Company acquired interests in OJSC Tomskenergo, OJSC Kubanenergo and other electric power generation, transmission, distribution and maintenance companies located in the Tomsk region and in the south of Russia (see Note 3) through the auctions for the sale of the assets of Yukos Oil Company that were held in May and July 2007. In 2007 the above interests were accounted for under equity method.

As part of the current reform of the Russian electric power industry, the above companies are being merged into larger territorial power generation companies (TGKs) or interregional distribution grid companies (MRSKs) located in the corresponding regions of the Russian Federation.

As a result of the restructuring process, the shares of the above companies are being converted into the shares of TGKs and MRSKs. Following such conversion, the Group's interest in the share capitals of the corresponding TGKs and MRSKs will be reduced as compared to that in the acquired companies. Consequently, the Group's investments will be accounted for as available for sale securities.

In the fourth quarter of 2007 OJSC Tomskenergo was merged into OJSC TGK-11. Following the conversion of OJSC Tomskenergo's shares as a result of the above merger, the Company's interest in the share capital of OJSC TGK-11 amounted to 5.28%. The Company is disputing the merger and the conversion of the shares in court. As of December 31, 2007, this investment was accounted for as an available for sale security.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 11. Property, Plant and Equipment, Net

	Initial cost		Accumulated depreciation		Net carrying amount	
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
Exploration and production	47,837	38,553	(8,410)	(5,814)	39,427	32,739
Refining, marketing and distribution	12,873	3,493	(2,370)	(703)	10,503	2,790
Other	2,107	523	(351)	(107)	1,756	416
<b>Total property and equipment</b>	<b>62,817</b>	<b>42,569</b>	<b>(11,131)</b>	<b>(6,624)</b>	<b>51,686</b>	<b>35,945</b>

Exploration and production assets include costs to acquire unproved properties in the amount of US\$ 4,165 million as of December 31, 2007, and US\$ 3,878 million as of December 31, 2006. The Company plans to explore and develop the respective properties. The Company's management believes these costs are recoverable.

For the purposes of evaluation of the reserves as of December 31, 2007 and 2006 the Company used oil and gas reserves data prepared by DeGolyer and MacNaughton, independent reservoir engineers. The Company used the reserve report to calculate depreciation, depletion and amortization relating to oil and gas properties for 2007 and 2006. The reserve report was also used for the assessment of impairment of oil and gas assets and for the required supplemental disclosure for oil and gas activities (see supplementary oil and gas disclosure).

As described in the "Depreciation, Depletion and Amortization" section of Note 2, the Company calculates depletion using the unit-of-production method over proved or proved developed oil and gas reserves depending on the nature of the costs involved. The proved or proved developed reserves used in the unit of production method assume the extension of the Company's production licences beyond their current expiration dates until the end of the economic lives of the fields as discussed below in further detail.

The Company's oil and gas fields are located principally in the territory of the Russian Federation. The Company obtains licences from the governmental authorities to explore and produce oil and gas from these fields. The Company's existing production licences generally expire during the period 2009 to 2044. Expiration dates of licences for the most significant fields are between 2013 and 2044, and the licence for the largest field, Priobskoye, expires in 2044. The economic lives of the major licenced fields extend significantly beyond these dates. Under Russian law, the Company is entitled to renew the licences to the end of the economic lives of the fields, provided certain conditions are met. Article 10 of the Subsoil Law provides that a licence to use a field "shall be" extended at its scheduled termination at the initiative of the subsoil user if necessary to finish production of the field, provided that there are no violations of the conditions of the licence.

The legislative history of Article 10 indicates that the term "shall" replaced the term "may" in August 2004, clarifying that the subsoil user has an absolute right to extend the licence term so long as it has not violated the conditions of the licence. In 2006, no licences came up for renewal. In 2007, the Company filed 42 applications for the extension of the licence terms and has currently extended 22 of its main production licences for the period equivalent to the expected life of the fields. During the above period, none of the applications filed by the Company for the extension of the licence terms was turned down by the authorized government bodies. The Company's current production plans are based on the assumption, which management considers to be reasonably certain, that the Company will be able to extend all other existing licences. These plans have been designed on the basis that the Company will be producing crude oil through the economic lives of the fields and not with a view to exploiting the Company's reserves to maximum effect only through the licence expiration dates.

Notes to Consolidated Financial Statements (continued)

**11. Property, Plant and Equipment, Net (continued)**

Accordingly, management has included in proved reserves in the supplementary information on oil and gas exploration and production activities of the consolidated financial statements as of and for the year ended December 31, 2007 all reserves that otherwise meet the standards for being characterized as "proved" and that the Company estimates it can produce through the economic lives of Company's licensed fields.

Proved reserves should generally be limited to those that can be produced through the licence expiration date unless there is a long and clear track record which supports the conclusion that extension of the licence will be granted as a matter of course. The Company believes that extension of the licences will occur as a matter of course as fully described above.

**Sakhalin-1**

The Company's primary investment in production sharing agreements ("PSA") is through the Sakhalin-1 project (PSA 1), which is operated by ExxonMobil, one of the PSA participants. In February 2001, the Company signed an agreement with Oil and Natural Gas Corporation ("ONGC") in relation to its interest in the PSA 1 which reduced the Company's interest to 20%. The Company recorded the investment in its retained share under the "carried interest" method.

On July 31, 2006, the Company repaid US\$ 1.34 billion (including accumulated interest) to ONGC with respect to the costs of the Company carried by ONGC in previous years. Following this settlement the Company recovered the right to receive the income equivalent to its interest in the project. US\$ 1.33 billion of the US\$ 1.34 billion paid was recorded as oil and gas properties. The remaining amount was reflected in the appropriate lines of the balance sheet and the statement of income based on the nature of the cost originally incurred.

**Sakhalin-5**

The participants of the project are subsidiaries of the Company and BP p.l.c. In March 2004, the licence for geological study of the Kaigansko-Vasyukansky block held by the Company was transferred to CJSC Elvari Neftegaz, which is a wholly owned subsidiary of Elvary Neftegaz Holdings B.V., an entity jointly established by the participants of the project.

The Shareholders and Operating Agreement was signed between the participants and the operator in June 2004. In accordance with the terms of the agreement, during the exploration stage project funding will be fully provided by BP p.l.c., while during the development stage BP p.l.c. will carry a portion of payments due from the Company and will provide credit support to obtain project funding.

The Company recognizes this investment using the equity method of accounting.

**Other Projects**

The Company is a party to other projects associated with the exploration and development of the Sakhalin shelf (Zapadno-Shmidtovsky and Vostochno-Shmidtovsky blocks). Under those arrangements, the other participant (BP p.l.c.) carries the costs associated with the exploration of these offshore blocks. Exploration and development of these projects is still at an early stage. The Company's costs (currently insignificant) associated with these projects were capitalized.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 11. Property, Plant and Equipment, Net (continued)

#### Other Projects (continued)

In July 2005, the Company entered into a PSA agreement with the Kazakhstan Government for the joint development of the Kurmangazy oil and gas prospect. The participants of the project are a subsidiary of the Company, RN Kazakhstan LLC, and a subsidiary of Kazakhstan State JSC KazMunaiGaz, JSC "NK KazMunaiGaz – KazMunaiTeniz" ("KazMunaiTeniz"), with equal shares of 50%. The agreement provided for a signing bonus in the amount of US\$ 50 million. The Company's share of US\$ 25 million is recognized within mineral rights. In accordance with the terms of the agreement, upon a commercial discovery the Russian Federation has an option to buy a 25% share in the project at a future market price, by reducing the share of RN-Kazakhstan LLC in the project. If the Russian Federation does not exercise its option, this share shall be sold to third parties at a market price or redistributed between the participants in equal parts. If the share is sold, the proceeds from the sale shall be used to cover the expenses already incurred, including those borne by RN Kazakhstan LLC which are attributable to the disposed share. Any excess of the proceeds from the sale of share over the expenses shall be equally distributed between RN Kazakhstan LLC and KazMunaiTeniz.

#### Cash Flows Details

Capital expenditures in the consolidated statements of cash flows comprise the following:

	2007	2006	2005
Acquisition and construction of property, plant and equipment	5,931	3,293	1,944
Construction materials	309	169	–
<b>Total capital expenditures</b>	<b>6,240</b>	<b>3,462</b>	<b>1,944</b>

### 12. Leased Property, Plant and Equipment, Net

The following is the analysis of the property, plant and equipment under capital leases as of December 31:

	2007	2006
Oil and gas properties	42	26
Less: accumulated depletion	(6)	(1)
Oil and gas properties, net	36	25
<i>Other property, plant and equipment</i>		
Buildings and constructions	5	–
Plant and machinery	39	3
Vehicles	174	3
Total	218	6
Less: accumulated depreciation	(24)	(2)
Property, plant and equipment, net	194	4
<b>Total net book value of leased property</b>	<b>230</b>	<b>29</b>

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 12. Leased Property, Plant and Equipment, Net (continued)

Below is the analysis of the repayment of capital lease obligations as of December 31:

	<b>2007</b>
2008	66
2009	55
2010	50
2011	43
2012 and after	13
<b>Imputed interest</b>	<b>(24)</b>
<b>Present value of capital lease payments</b>	<b>203</b>

### Operating Lease

The Company has obligations which are primarily related to the operating lease of oil and gas facilities in the amount of US\$ 19 million for 2008.

The total amount of operating lease expenses was as follows:

	<b>2007</b>	<b>2006</b>	<b>2005</b>
Total lease expenses	127	115	120
Total sublease revenues	5	15	3

### 13. Goodwill and Intangible Assets

Goodwill in the amount of US\$ 2,914 million and US\$ 714 million represents the excess of the purchase price of additional shares in various entities in the refining, marketing and distribution segment and exploration and production segment, respectively, acquired during 2007, over the fair value of the corresponding share in net assets (see Note 3).

The remaining goodwill of US\$ 161 million, which relates to the refining, marketing and distribution segment, was tested for impairment as of December 31, 2007 and 2006, and no impairment was identified.

Intangible assets represent primarily land rights in the amount of US\$ 274 million acquired during 2007. The land rights have useful lives of 20 years, on average.

### 14. Other Non-Current Assets

Other non-current assets as of December 31 comprise the following:

	<b>2007</b>	<b>2006</b>
Payment made in favor of Factorias Vulcano S.A	233	145
Advances paid for capital construction	610	142
Debt issue cost	40	22
Long-term VAT	85	32
Other non-current assets	146	86
<b>Other non-current assets</b>	<b>1,114</b>	<b>427</b>

An advance payment was made in favor of Factorias Vulcano S.A for the construction of three twin-hull shuttle oil tankers (see Note 16). As of December 31, 2007 the vessels were in the final stage of construction. The remaining part of the advance to be paid in 2008 is approximately US\$ 7 million.



# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 15. Accounts Payable and Accrued Liabilities

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

	2007	2006
Trade accounts payable	2,034	851
Salary and other benefits payable	286	130
Advances received	568	350
Dividends payable	2	2
Banking customer accounts	818	386
Promissory notes payable	–	2
Obligations under Total E&P Vankor claim	–	134
Other	327	143
<b>Total accounts payable and accrued liabilities</b>	<b>4,035</b>	<b>1,998</b>

The Company's accounts payable are denominated primarily in RUB.

In October 2007, the Company acquired 100% of the shares of E&P Vankor Ltd which is the beneficiary under the succeeded legal claim against the Company (see Note 4). Consequently, this no longer represents a liability to the Company.

### 16. Short-Term Loans and Long-Term Debt

Short-term loans and borrowings as of December 31 comprise the following:

	2007	2006
Bank loans – foreign currencies	10,352	79
Bank loans – RUB denominated	51	2,517
Customer deposits – foreign currencies	20	29
Customer deposits – RUB denominated	291	164
Promissory notes payable	50	93
Promissory notes payable – Yukos related	904	678
Borrowings – RUB denominated	234	6
Borrowings – RUB denominated – Yukos related	728	497
Borrowings – US\$ denominated	–	2
	12,630	4,065
Current portion of long-term debt	2,920	2,362
<b>Total short-term loans and borrowings and current portion of long-term debt</b>	<b>15,550</b>	<b>6,427</b>

Foreign currency denominated short-term bank loans primarily represent financing received from a consortium of international banks.

In March-May 2007, the Company obtained bridge financing from a consortium of international banks in the total amount of US\$ 22.0 billion to finance planned acquisitions (see Note 3). These bridge loans were partially refinanced in February 2008 in the amount of US\$ 2.97 billion (see Note 26) so the respective amount of this short-term debt is classified as long-term as of December 31, 2007. As of December 31, 2007, the amount outstanding under these short-term bridge financing facilities which were not refinanced was US\$ 8.73 billion bearing interest of London Interbank Offering Rate ("LIBOR") plus 0.45% p.a. and is included in the Bank loans – foreign currencies denominated.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 16. Short-Term Loans and Long-Term Debt (continued)

In June-August 2007, the Company obtained three loans from Russian state controlled banks in the total amount of US\$ 1,580 million bearing interest of 6.75%-7.0% p.a. for one year.

Customer deposits represent fixed-term deposits placed by customers with the Company's subsidiary bank, denominated in RUB and foreign currencies. Customer deposits denominated in RUB bear an interest rate ranging from 0.5% p.a. to 12.0% p.a. Customer deposits denominated in foreign currencies bear an interest rate ranging from 3.0% p.a. to 8.0% p.a.

Promissory notes are primarily payable on demand. The promissory notes bear interest rates ranging from 0% to 9% p.a. The promissory notes are recorded at amortized cost.

Promissory notes payable – Yukos related represent financing originally received from the entities that were related to Yukos at the date of the notes issue. The promissory notes are primarily payable on demand and bear interest rates ranging from 0% to 18% p.a. The promissory notes are recorded at amortized cost.

RUB denominated borrowings represent interest-free loans received from equity investees.

RUB denominated borrowings – Yukos related primarily include borrowings provided by Yukos Capital S.a.r.l., which bore interest of 9% p.a. and matured at the end of 2007 (see Note 23).

Long-term debt as of December 31 comprises the following:

	<b>2007</b>	<b>2006</b>
Bank loans – foreign currency denominated	<b>9,611</b>	4,826
Bank loans raised for funding the acquisition of OJSC Yuganskneftegaz – US\$ denominated	<b>3,737</b>	4,780
Borrowings – US\$ denominated	<b>12</b>	30
Borrowings – RUB denominated	<b>20</b>	2
Borrowings – RUB denominated – Yukos related	<b>12</b>	–
Customer deposits – foreign currencies	<b>10</b>	15
Customer deposits – RUB denominated	<b>146</b>	85
Bonds of the subsidiary bank – RUB denominated	<b>24</b>	4
Promissory notes payable	<b>50</b>	22
Promissory notes payable – Yukos related	<b>1,021</b>	–
	<b>14,643</b>	9,764
Current portion of long-term debt	<b>(2,920)</b>	(2,362)
<b>Total long-term debt</b>	<b>11,723</b>	7,402

The interest rates on the Company's long-term bank loans denominated in foreign currencies range from 4.35% p.a. to 7.73% p.a. Weighted average interest rates on these loans were 5.22% and 5.96% (LIBOR plus 0.62%, LIBOR plus 0.64%) as of December 31, 2007 and December 31, 2006, respectively. These bank loans are primarily secured by contracts for the export of crude oil.

In May 2007, the Company signed a loan agreement with the syndicate of international banks for US\$ 2 billion with a term of five years and a cost of LIBOR plus 0.5% p.a. for the first three years and LIBOR plus 0.575% p.a. for the remaining two years. Additional syndication under this loan agreement resulted in an increase of the facility to US\$ 3.1 billion in July 2007. The funds raised were used to refinance part of the bridge facilities raised earlier in 2007 for acquisitions. These borrowings are included within Bank loans – foreign currency denominated in the table above.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 16. Short-Term Loans and Long-Term Debt (continued)

In January 2006, a subsidiary of the Company registered in Cyprus signed a loan agreement with a major international bank for an amount of Euro ("EUR") 188 million (US\$ 275 million using the CBR rate as of December 31, 2007). The loan bears interest at the European Interbank Offering Rate ("EURIBOR") plus 0.35% p.a. As of December 31, 2007, the drawdown amount was of EUR 158 million (US\$ 231 million using the CBR rate as of December 31, 2007). Funds borrowed are to be invested in the construction of three twin-hull shuttle oil tankers for crude oil transportation purposes in north-western regions of the Russian Federation (See Note 14). The loan is scheduled to be repaid within the twelve years following the completion of tanker construction. This borrowing is included within Bank loans – foreign currency denominated in the table above.

As of December 31, 2007 the bank loans raised for funding the acquisition of OJSC Yuganskneftegaz represent a long-term loan obtained through a government-owned bank at a rate of LIBOR plus 0.7% p.a. repayable in equal monthly installments. It is scheduled for repayment in 2011 in full. This loan is secured by the Company's receivables under a long-term contract for the supply of crude oil (see Note 23).

Customer deposits represent fixed-term deposits placed by customers with the Company's subsidiary bank, denominated in RUB and foreign currencies. The RUB-denominated deposits bear interest rates ranging from 3.0% p.a. to 12.7% p.a. Deposits denominated in foreign currencies bear interest rates of 5.75%-12.98% p.a.

Promissory notes payable represent interest-free promissory notes which mature primarily in 2009. The promissory notes are recorded at amortized cost.

Promissory notes payable – Yukos related represent financing originally received from the entities that were related to Yukos on the debt issue date. The promissory notes bear interest rates ranging from 0% to 12% p.a and mature primarily in 2008-2009. The promissory notes are recorded at amortized cost.

Generally, long-term loans are secured by oil export contracts. Usually, under the terms of such contracts, the lender is provided with an express right of claim for contractual revenue which must be remitted directly to transit currency (US\$ denominated) accounts with those banks, should the Company fail to repay its debt in time.

The Company is obliged to comply with a number of restrictive financial and other covenants contained within its loan agreements. Restrictive covenants include maintaining certain financial ratios.

As a result of the Company's acquisition of OJSC Yuganskneftegaz in December 2004, and the resulting debt incurred and assets and liabilities, including contingent liabilities, consolidated, the Company was not in compliance with various financial and other covenants of existing loan agreements as of December 31, 2004.

In July 2005, the creditors waived violations related to restrictive financial ratios and agreed to amend the financial ratio covenants in line with the Company's new structure and new scope of activities. The creditors also waived other events of default arising from the breach of other covenant provisions. Effective January 1, 2007, the creditors granted amendments to the loan agreements which remove these provisions and have included new provisions which state that the Company must:

- redeem, secure, discharge in full or restructure (and comply with any restructuring plans once it is agreed upon) all OJSC Yuganskneftegaz's tax liabilities by January 3, 2008 (see Note 23);
- pay any arbitration award relating to Moravel Litigation (see Note 23) or the Yukos Capital S.a.r.l. (further "Yukos Capital") Litigation against OJSC Yuganskneftegaz if any such arbitration award is granted by a court of the Russian Federation, within the time frame provided for such payment under Russian Law.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 16. Short-Term Loans and Long-Term Debt (continued)

These conditions also apply to certain new borrowings obtained throughout 2007. Additionally, in November 2007, the creditors waived certain possible violations and/or events of default under the loan agreements with respect to the loans payable to Yukos Capital by OJSC Tomskneft VNK and OJSC Samaraneftegaz (see Note 23), effective through January 3, 2009. In December 2007, the Company obtained an extension to the waivers with respect to the condition related to OJSC Yuganskneftegaz's tax liabilities described above, effective through January 3, 2009.

As of December 31, 2007, the Company is in compliance with all restrictive financial covenants contained within its loan agreements.

The scheduled aggregate maturity of long-term debt outstanding as of December 31, 2007 is as follows:

	<u>2007</u>
2008	2,920
2009	4,939
2010	3,577
2011	1,713
2012 and after	1,494
<b>Total long-term debt</b>	<u><u>14,643</u></u>

### 17. Shareholders' Equity

In July 2006, the shareholders of Rosneft undertook an initial public offering of ordinary shares of Rosneft in Russia, as well as GDRs for these shares on the London Stock Exchange. 1,126 million of the Company's ordinary shares were sold by the Company's shareholders. Additionally, the Company issued 285 million new ordinary shares. As a result of the offering, the Company's proceeds from the sale of new shares amounted to US\$ 2,115 million (net of commissions and expenses). The difference between the nominal value of the shares issued (US\$ 105 thousand) and the amount received for shares (US\$ 2,115,408 thousand) was recognized as additional paid-in capital.

In December 2006, the Federal Tax Service of the Russian Federation registered the change in the Company's share capital, which was increased due to an additional share issue for the purposes of the Share Swap and consolidation of the Merging Subsidiaries (see Notes 1 and 3). The Company's issued ordinary share capital was increased by 1,221 million shares to 10,598 million shares. The fair value of the shares issued was determined to be US\$ 9,218 million (see Note 4). The difference between the par value (US\$ 456 thousand) and the fair value (US\$ 9,218,093 thousand) of the issued shares was recognized as additional paid-in capital of the Company.

In April 2007, a subsidiary of the Company received title to 1 billion ordinary shares (9.44% of common stock) of Rosneft after it had won the auction for the acquisition of the above shares previously owned by Yukos Oil Company. For consolidated financial reporting purposes, the purchase price amounted to RUB 194.05 billion for Rosneft shares, or RUB 194.05 par value (US\$ 7.52 billion and US\$ 7.52 per share at the CBR exchange rate as of the date of the auction, respectively). These shares were recorded at their purchase price and treated as treasury shares and therefore shown as deduction from shareholders' equity.

In June 2007, the annual general shareholders' meeting approved dividends on the Company's common shares for 2006 in the amount of RUB 14.1 billion (US\$ 546 million at the CBR exchange rate as at the date of decision), or RUB 1.33 or US\$ 0.05 per share. US\$ 499 million of the above related to outstanding shares.

As of December 31, 2007 and 2006, the number of common shares authorized (in addition to shares issued) was 6,333 million. As of December 31, 2007 and 2006, the total amount of shares authorized was 16,931 million.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 17. Shareholders' Equity (continued)

#### Result of the Transaction with a Related Party under Common Control

In December 2007, the Company sold 50% of its interests in OJSC Tomskneft VNK, Imushchestvo-Service-Strezhevoy LLC, Strezhevskoy Refinery LLC and OJSC Tomskneftegeofizika and several other companies which had been previously acquired through the auction for the sale of the assets of Yukos Oil Company (see Note 3). The proceeds from the sale amounted to RUB 88.18 billion (US\$ 3,570 million at the CBR exchange rate as of the transaction date.) The net result of the sale amounted to US\$ 1,745 million, net of income tax effect (US\$ 285 million). Since the transaction was executed with a related party under common control, the Company recorded this result, net of income tax effect, as a component of additional paid-in capital.

Upon the completion of the sale, the investment in the above entities remaining with the Company is accounted for using the equity method of accounting (see Note 10).

#### Amounts Available for Distribution to Shareholders

Amounts available for distribution to shareholders are based on OJSC Oil Company Rosneft's statutory accounts prepared in accordance with Russian accounting standards, which differ significantly from US GAAP (see Note 2). Russian legislation identifies the basis of distribution as the current period consolidated net profit calculated in accordance with statutory accounting standards. According to Russian legislation, dividends cannot exceed the accounting income for the reporting year. However, this legislation and other statutory laws and regulations dealing with distribution rights are open to different legal interpretations.

### 18. Income and Other Tax Liabilities

Income and other tax liabilities as of December 31 comprise the following:

	2007	2006
Mineral extraction tax	1,084	1,156
Value added tax	214	615
Excise tax	184	73
Personal income tax	24	15
Property tax	23	36
Income tax	651	454
Other	166	123
<b>Total income and other tax liabilities</b>	<b>2,346</b>	<b>2,472</b>

### 19. Revenue Related Taxes

Revenue related taxes for the years ended December 31, comprise the following:

	2007	2006	2005
<i>Oil and gas sales</i>			
Export customs duty	10,754	9,763	5,322
<i>Petroleum products and processing fees</i>			
Export customs duty	2,278	1,377	942
<b>Total revenue related taxes</b>	<b>13,032</b>	<b>11,140</b>	<b>6,264</b>

Petroleum products sales also include excise taxes which are presented in Note 20.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 20. Income and Other Taxes

Income tax expenses for the years ended December 31 comprise the following:

	2007	2006	2005
Current income tax expense	3,848	2,385	1,688
Deferred income tax expense/(benefit)	1,058	(1,845)	(79)
<b>Total income tax expense</b>	<b>4,906</b>	540	1,609

The Company does not file a consolidated tax return, rather each legal entity files separate tax returns with various authorities, primarily in the Russian Federation.

Temporary differences between these consolidated financial statements and tax records gave rise to the following deferred income tax assets and liabilities as of December 31:

	2007	2006
Deferred income tax asset arising from tax effect of:		
Tax loss carry-forward	33	100
Asset retirement obligations	77	60
Property, plant and equipment	50	70
Prepayments and other current assets	15	9
Accounts receivable	27	1,135
Accounts payable and accruals	63	8
Inventories	16	9
Long-term investments	4	6
Other	63	25
Total	348	1,422
Valuation allowance for deferred income tax asset	(135)	(177)
Deferred income tax asset	213	1,245
Deferred income tax liability arising from tax effect of:		
Mineral rights	(3,996)	(3,720)
Other properties, plant and equipment and other	(3,748)	(1,743)
Deferred income tax liability	(7,744)	(5,463)
<b>Net deferred income tax liability</b>	<b>(7,531)</b>	<b>(4,218)</b>

The increase of deferred income tax liability arising from tax effect of mineral rights and oil and gas properties, plant and equipment and other was due to significant asset acquisitions (see Note 3).

The change in deferred income tax asset arising from tax effect of accounts receivable was due to the full repayment of accounts receivable from Yukos Oil Company in 2007.

Classification of deferred taxes:

	2007	2006
Current deferred tax assets	156	1,135
Non-current deferred tax assets	57	110
Current deferred tax liabilities	(118)	(17)
Non-current deferred tax liabilities	(7,626)	(5,446)

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 20. Income and Other Taxes (continued)

Although the Company does not pay tax on a consolidated basis, a reconciliation of expected income tax expense to the actual tax expense for the years ended December 31 is as follows:

	2007	2006	2005
Income before income taxes and minority interest	17,789	4,165	6,214
Statutory income tax rate	24.00%	24.00%	24.00%
Theoretical income tax expense	4,269	1,000	1,491
Add/(deduct) tax effect of:			
Change in valuation allowance	(42)	(94)	155
Effect of income tax preferences	(135)	(77)	(128)
Previously unrecognized deferred tax asset	–	(539)	(24)
Adjustments of income tax for prior periods	(36)	(30)	–
Unrecognized income tax benefits	18	–	–
Permanent accounting differences arising from:			
Non-deductible items, net	202	86	45
Foreign exchange effects, net	276	113	(59)
Accrued tax interest	177	–	–
Other	177	81	129
<b>Income taxes</b>	<b>4,906</b>	<b>540</b>	<b>1,609</b>

Effect of income tax preferences, in the above table, represents the impact of lower income tax rates for Rosneft and certain of its subsidiaries under applicable regional laws. These laws provide that the income tax exemptions, ranging from 3.5 to 4%, are granted to the oil and gas producing companies which make capital investments, agreed with regional administrations, within the respective region and participate in various social projects. These exemptions are granted on an annual basis.

As of January 1, 2007 and December 31, 2007 the Company analyzed its tax positions for uncertainties affecting recognition and measurement thereof. Following the analysis, the Company believes that it is more likely than not that all tax positions stated in the income tax return would be sustained upon the examination by the tax authorities. This is supported by the results of the examinations of the income tax returns which have been conducted to date.

During 2007, the tax authorities resumed examinations of the Company's income tax returns for 2004-2005 and for the first nine months of 2006. There are no other tax years or periods prior to 2004 that remain subject to examination.

The following table shows a reconciliation of the beginning and ending unrecognized tax benefits for 2007.

	2007
Unrecognized tax benefits at January 1	–
Increase for tax positions of prior years	12
Increase for tax position of prior years due to 2007 acquisitions	1
Increase for tax position of current year due to 2007 acquisitions	5
Unrecognized tax benefits at December 31	18

The total amount of unrecognized tax benefits that, if recognized, would affect the effective income tax rate is US\$ 12 million and nil as of December 31, 2007 and January 1, 2007, respectively.

Accrued liabilities for interest and penalties for income tax totaled US\$ 211 million as of January 1, 2007 and US\$ 300 million as of December 31, 2007. Interest for income tax in the amount of US\$ 89 million were accrued in the consolidated statement of income in 2007.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 20. Income and Other Taxes (continued)

In addition to income tax, the Company incurred other taxes as follows:

	2007	2006	2005
Mineral extraction tax	9,323	6,342	4,716
Excise tax	861	329	286
Social security	291	154	118
Property tax	186	107	73
Land tax	15	7	14
Transport tax	4	2	2
Other taxes and payments	210	49	117
<b>Total taxes, other than income tax</b>	<b>10,890</b>	<b>6,990</b>	<b>5,326</b>

### 21. Asset Retirement Obligations

The movement of asset retirement obligations is as follows:

	2007	2006
Asset retirement obligations as of the beginning of the reporting period	748	566
Recognition of additional obligations for new wells	11	16
Accretion expense	78	34
Increase as a result of changes in estimates	909	132
Acquired liabilities	908	–
Disposed liabilities of OJSC Tomskneft VNK	(521)	–
Spending on existing obligations	(3)	–
<b>Asset retirement obligations as of the end of the reporting period</b>	<b>2,130</b>	<b>748</b>

Asset retirement obligations represent an estimate of costs of wells liquidation, recultivation of sand pits, slurry ponds, disturbed lands and dismantling pipelines and power transmission lines.

Increase as a result of changes in estimates in the amount of US\$ 909 is primarily a result of more stringent interpretation of the current environmental and construction legislation with regard to pipeline dismantlement by the respective regulatory bodies.

Russian legislation does not stipulate any funds reservation for purposes of settling asset retirement obligations.



# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 22. Related Party Transactions

In the course of its usual activity, the Company regularly enters into transactions with other enterprises which are directly or indirectly controlled by the Russian Government. Such enterprises are business units of RAO UES, OJSC Gazprom, OJSC Russian Railways, OJSC Sberbank, Vnesheconombank, OJSC Bank VTB, OJSC Gazprombank, OJSC AK Transneft and federal agencies including tax authorities. Management considers these business relations as part of regular activities in the Russian Federation and believes that they will remain unchanged in the normal course of business.

Total amounts of transactions with companies controlled by the Government of the Russian Federation for each of the reporting periods ending December 31, as well as related party balances are provided in the table below:

	2007	2006	2005
<b>Revenues</b>			
Oil and gas sales	99	27	19
Sales of petroleum products and processing fees	218	148	195
Support services and other revenues	13	8	2
	<b>330</b>	183	216
<b>Costs and expenses</b>			
Pipeline tariffs and transportation costs	2,873	2,032	1,305
Other expenses	182	22	1
	<b>3,055</b>	2,054	1,306
<b>Other operations</b>			
Acquisitions of property, plant and equipment	7	87	9
Sale of short-term and long-term investments	–	4	38
Acquisition of short-term and long-term investments	–	14	38
Sale of shares in CJSC Sevmorneftegaz	–	–	1,303
Proceeds from short-term and long term debt	3,654	2,463	1,527
Repayment of short-term and long term debt	5,675	2,104	3,458
Deposits placed	90	374	1,945
Deposits paid	55	499	1,762
Borrowings issued		131	574
Repayment of borrowings issued		134	574
Interest expense	335	384	487
Interest income	9	25	–
Banking fees	13	13	12
<b>Assets</b>			
Cash and cash equivalents	139	69	376
Accounts receivable and other current assets	106	20	23
Prepayments	239	137	154
Short-term and long-term investments	90	172	180
	<b>574</b>	398	733
<b>Liabilities</b>			
Accounts payable	16	24	4
Short-term and long-term debt (including interest)	5,322	7,282	6,890
	<b>5,338</b>	7,306	6,894

A sale of 50% interest in OJSC Tomskneft VNK to a related party is disclosed in Note 17.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 22. Related Party Transactions (continued)

Total amounts of transactions with other related parties, excluding the companies controlled by the Government of the Russian Federation, primarily equity investees and joint ventures, for each of the reporting periods ending December 31, as well as related party balances are provided in the table below:

	2007	2006	2005
<b>Revenues</b>			
Oil and gas sales	34	31	27
Petroleum products and processing fees	158	84	50
Support services and other revenues	103	26	60
	<b>295</b>	141	137
<b>Costs and expenses</b>			
Purchase of oil and petroleum products	621	103	1
Other expenses	179	74	64
	<b>800</b>	177	65
<b>Other operations:</b>			
Acquisitions of property, plant and equipment	30	2	73
Lease payments	–	–	29
Sale of short-term and long-term investments	1	–	514
Acquisition of short-term and long-term investments	8	48	345
Proceeds from short-term and long-term debt	13	33	–
Repayment of short-term and long-term debt	23	51	8
Borrowings issued	64	88	61
Repayment of borrowings issued	24	22	46
Interest expense	3	4	–
Interest income	44	8	–
Dividends received	28	13	19
<b>Assets</b>			
Accounts receivable and other current assets	201	33	13
Prepayments	16	42	–
Short-term and long-term investments	297	121	128
	<b>514</b>	196	141
<b>Liabilities</b>			
Accounts payable	941	193	24
Short-term and long-term debt (including interest)	235	9	2
	<b>1,176</b>	202	26

### 23. Commitments and Contingencies

#### Russian Business Environment

Whilst there have been improvements in the Russian economic situation, such as an increase in gross domestic product and a reduced rate of inflation, Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government. In addition laws and regulations, including interpretations, enforcement and judicial processes, continue to evolve in Russia. Other laws and regulations and certain other restrictions producing a significant effect on the Company's industry, including, but not limited to the following issues: rights to use subsurface resources, environmental matters, site restoration, transportation and export, corporate governance, taxation, etc.

Notes to Consolidated Financial Statements (continued)

**23. Commitments and Contingencies (continued)**

**Taxation**

Legislation and regulations regarding taxation in Russia continue to evolve. The various legislation and regulations are not always clearly written and their interpretation is subject to the opinions of the local, regional and national tax authorities. Instances of inconsistent opinions are not unusual.

The current regime of penalties and interest related to reported and discovered violations of Russia's laws, decrees and related regulations is severe. Interest and penalties are levied when an understatement of a tax liability is discovered. As a result, the amounts of penalties and interest can be significant in relation to the amounts of unreported taxes.

In Russia tax returns remain open and subject to inspection for a period of up to three years. The fact that a year has been reviewed does not close that year, or any tax return applicable to that year, from further review during the three-year period.

Russian transfer pricing rules were introduced in 1999, giving Russian tax authorities the right to make transfer pricing adjustments and impose additional tax liabilities in respect of all controlled transactions, provided that the transaction price deviates from the market price by more than 20%. Controlled transactions include transactions between related entities and certain other types of transactions between independent parties, such as foreign trade transactions with significant (by more than 20%) price fluctuations.

The Russian transfer pricing rules are vaguely drafted, leaving wide scope for interpretation by Russian tax authorities and courts. Due to the uncertainties in interpretation of transfer pricing legislation, the tax authorities may challenge the Group's prices and propose an adjustment. If such price adjustments are upheld by the Russian courts and implemented, it could have an adverse effect on the Group's financial condition and results of operations. The Company's management believes that such transfer pricing related income tax positions taken by the Company are sustainable and will not have any significant negative impact on the Company's consolidated financial position or results of operations.

During 2005, tax audits of several subsidiaries for the years 2002-2003 took place. The results of these tax audits are currently being appealed with the tax authorities. The Company's management believes that the final outcome of these tax audits will not have any significant negative impact on the Company's consolidated financial position or results of operations.

During 2007, the tax authorities periodically resumed tax audits of the Company's for the years 2004-2005 and for the first nine months of 2006. The Company's management believes that the final outcome of these tax audits will not have any significant impact on the Company's consolidated financial position or results of operations.

The Company provides finance for operations of its subsidiaries by various means which may lead to certain tax risks. The Company's management believes that the related tax positions are sustainable and will not have any significant negative impact on the Company's consolidated financial position or results of operations.

The Company is currently challenging a number of decisions made by the tax authorities to accrue additional VAT and not to reimburse VAT paid to suppliers in the amount of RUB 11,583 million (US\$ 472 million at the CBR exchange rate as of December 31, 2007). The claims of RUB 9,838 million (US\$ 401 million at the CBR exchange rate as of December 31, 2007) have been upheld by various courts, however they are subject to further appeal by the tax authorities. The claims of RUB 774 million (US\$ 32 million at the CBR exchange rate as of December 31, 2007) have not been upheld by the courts, however the Company has the right and intends to appeal them vigorously. The remaining claims of RUB 971 million (US\$ 40 million at the CBR exchange rate as of December 31, 2007) are still being heard in the courts.

## Notes to Consolidated Financial Statements (continued)

**23. Commitments and Contingencies (continued)****Taxation (continued)**

The Company's management believes that the outcome of these tax audits will not have any significant impact on the Company's consolidated financial position or results of operations. Overall, management believes that the Company has paid or accrued all taxes that are applicable. For taxes other than income tax, where uncertainty exists, the Company has accrued tax liabilities based on management's best estimate of the probable outflow of resources embodying economic benefits, which will be required to settle these liabilities. Possible liabilities which were identified by management at the balance sheet dates as those that can be subject to different interpretations of the tax laws and regulations are not accrued in the consolidated financial statements.

As of December 31, 2007, the Company's subsidiaries which were acquired at the auctions, described in Note 3, have various disputes with tax authorities for the total amount of US\$ 99 million, US\$ 51 million of which were recorded within income and other tax liabilities.

In May 2007, by an Order of the Government of the Russian Federation, Rosneft was included in the list of strategic companies of Russia. As such Rosneft became generally eligible for the tax restructuring process. Following the intention of the Company to proceed with the tax restructuring process in respect of OJSC Yuganskneftegaz back-taxes, the tax authorities retroactively cancelled the suspension of certain interest accruals for them to be fully included in the tax restructuring plan. These tax liabilities were already fully accrued in the consolidated financial statements in prior periods together with all penalties and a portion of interest before such interest accrual was suspended following the Company's applications for restructuring. As a result of the cancellation, additional interest of US\$ 456 million was due as of December 31, 2007. The total amount of interest and penalties payable as of December 31, 2007 with respect to tax liabilities of OJSC Yuganskneftegaz amounted to US\$ 1,000 million. The interest continued to accrue until the restructuring plan was approved by the Government of the Russian Federation and the respective regional and local government authorities, as discussed below. The total principle amount subject to tax restructuring provisions was US\$ 1,336 million.

In February and March 2008, the Company received a signed resolution of the Government of the Russian Federation and relevant regional and local authorities regarding the restructuring of the respective tax liabilities. The total restructured tax liabilities amounted to RUB 57.3 billion (US\$ 2,336 million at the CBR exchange rate as of December 31, 2007), of which tax arrears amount to RUB 32.8 billion (US\$ 1,336 million at the CBR exchange rate as of December 31, 2007), and interest and penalties amount to RUB 24.5 billion (US\$ 1,000 million at the CBR exchange rate as of December 31, 2007). Under the tax restructuring plan, the outstanding tax liabilities shall be repaid quarterly within five years starting from March 2008 pursuant to the repayment schedule stated therein. Consequently, US\$ 2,146 million has been reclassified into other non-current liabilities in the consolidated balance sheet as of December 31, 2007. The Company intends to undertake all possible actions to comply with the tax restructuring plan in full.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 23. Commitments and Contingencies (continued)

#### Other Non-current Liabilities

Other non-current liabilities as of December 31 comprise the following:

	<b>2007</b>	<b>2006</b>
Restructured tax liabilities	<b>2,146</b>	–
Long-term lease obligations	<b>147</b>	4
Deferred income	<b>115</b>	132
Liabilities to municipalities under amicable agreements	<b>48</b>	–
Other	<b>29</b>	24
<b>Total non-current liabilities</b>	<b>2,485</b>	160

#### Capital Commitments

The Company and its subsidiaries are engaged in ongoing capital projects for exploration and development of production facilities and modernization of refineries and the distribution network.

The budgets for these projects are generally set on an annual basis. Depending on the current market situation, actual expenditures may vary from the budgeted amounts.

It is planned that future costs will be primarily self-financed. In addition, the Company is seeking external sources of financing. Management believes that the Company will receive all the financing required to complete both existing and scheduled projects.

#### Environmental Matters

Due to the nature of its business, Rosneft and its subsidiaries are subject to federal legislation regulating environmental protection. The majority of environmental liabilities arise as a result of accidental oil spills and leaks that pollute land, and air pollution. The Company considers fines paid and other environmental liabilities as immaterial, given the scale of its operations.

In the course of its operations, the Company seeks to comply with international environmental standards and monitors compliance therewith on a regular basis. With a view to improve environmental activities, the Company takes specific measures to mitigate the adverse impact of its current operations on the environment.

Legislation that regulates environmental protection in the Russian Federation is evolving, and the Company evaluates its liabilities in accordance therewith.

Currently it is not possible to reasonably estimate the liabilities of the Company which may be incurred should the legislation be amended.

The management believes that, based on the existing legislation, the Company is unlikely to have liabilities that need to be accrued in addition to the amounts already recognized in the interim consolidated financial statements and that may have a material adverse effect on the operating results or financial position of the Company.

#### Social Commitments

The Company is required to maintain certain social infrastructure assets (not owned by the Company and not recorded in the consolidated financial statements) for use by its employees.

The Company incurred US\$ 55 million, US\$ 64 million, and US\$ 66 million in social infrastructure and similar expenses in 2007, 2006 and 2005, respectively. These expenses are presented as other expenses in the consolidated statements of income.

Notes to Consolidated Financial Statements (continued)

**23. Commitments and Contingencies (continued)**

**Charity and Sponsorship**

During 2007, 2006 and 2005, the Company made donations of US\$ 117 million, US\$ 41 million, and US\$ 25 million, respectively, for charity and sponsorship in various regions of Russia where the Company operates. These expenses are presented as other expenses in the consolidated statements of income.

**Pension Plans**

The Company and its subsidiaries make payments to the State Pension Fund of the Russian Federation. These payments are calculated by the employer as percentage from the salary expense and are expensed as accrued.

The Company contributes to corporate pension fund to finance non-state pensions of its employees. These payments are made based on the defined contribution plan. In 2007, 2006 and 2005, the Company made contributions to non-state corporate pension fund amounting to US\$ 67 million, US\$ 41 million, and US\$ 16 million, respectively.

In 2007, the Company paid special termination benefits to the retiring employees in the amount of US\$ 12.7 million.

**Insurance**

The Company insures its assets with OJSC Sogaz, a related party.

As of December 31, 2007 and 2006, the amount of coverage on assets for such insurance was US\$ 11,706 million and US\$ 2,209 million, respectively.

**Guarantees and Indemnity**

As of December 31, 2007, the Company has provided guarantees for certain debt agreements of its subsidiaries. In accordance with the debt agreements, the Company is obliged to perform on the guarantee and to pay all amounts of outstanding guaranteed liabilities, including interest.

The Company cannot substitute guarantees issued by any novation agreement or mutual offset. The Company's obligations under guarantees issued are valid in case of any change in loan agreements. After the full payment and settlement of all obligations under the guarantees, the Company has the right to subrogate its respective part of all claims against the debtor in accordance with the loan agreements. In the event the Company makes payments under guarantees issued, it has a right to claim the amounts paid from the debtor.

In January 2007, the Company signed a guarantee agreement in respect of all the obligations of CJSC Vankorneft per the irrevocable documentary letter of credit for the amount of US\$ 62 million and for the period of up to 730 days. In the event of default, as specified in the agreement, the bank may request the Company to place a deposit in the amount necessary to ensure all of the Company's existing and potential obligations are payable for the period of validity of such letter of credit.

In January 2007, RN-Yuganskneftegaz LLC signed a guarantee agreement in respect of all the obligations of RN Energo LLC, the Company's wholly owned subsidiary, under the contract for electricity supply with OJSC Tyumenskaya Energosbytovaya Companiya for the period through January 31, 2010, in the amount of US\$ 58 million.

## Notes to Consolidated Financial Statements (continued)

**23. Commitments and Contingencies (continued)****Guarantees and Indemnity (continued)**

During 2007-2008, the Company has successfully defended its position in various courts as to the invalidity of guarantees provided by OJSC Yuganskneftegaz, OJSC Samaraneftgaz and OJSC Tomskneft VNK related to the Yukos Oil Company indebtedness of US\$ 1,600 million to Moravel Investments Limited. Along with the fact that all or most of the relevant indebtedness was collected by the principal creditor, it enabled the Company to conclude that the probability of any unfavorable outcome in relation to the matter is now remote.

**Yukos Capital Litigation**

Yukos Capital, a subsidiary of Yukos Oil Company, initiated arbitral proceedings against OJSC Yuganskneftegaz before the International Court of Commercial arbitration ("ICCA") at the Russian Federation Chamber of Commerce and Industry alleging default under four rouble-denominated loans. The ICCA issued its decisions on September 19, 2006 ruling in favor of Yukos Capital and awarding damages to Yukos Capital, including accrued interest and arbitration costs, in the total amount of RUB 12,937 million (approximately US\$ 527 million at the CBR exchange rate at December 31, 2007). The Company challenged the ICCA ruling in the Arbitration Court of Moscow. On May 23, 2007, the Moscow Arbitration Court satisfied the Company's petition on the discharge of the ICCA decisions and invalidated the ICCA decisions. Yukos Capital appealed the decisions of the first instance court to a cassation court. On August 13, 2007, the cassation court upheld the decisions of the lower court and rejected Yukos Capital's claims. On December 10, 2007 the Supreme Arbitration Court of Russia upheld the decisions of the lower courts and rejected Yukos Capital's claims. In executing the ICCA decisions against the Company in the Netherlands, on December 19, 2006, the Amsterdam Court, acting on a petition of Yukos Capital, issued an attachment order against the Company with respect to certain receivables. On December 11, 2007, the Amsterdam Court examined Yukos Capital's petition on enforcement of the ICCA decisions in the Netherlands and on February 28, 2008 ruled against enforcement of the said ICCA decisions in the Netherlands. Yukos Capital has the right to appeal this ruling until April 29, 2008.

In addition, Yukos Capital initiated arbitral proceedings against OJSC Tomskneft VNK before the International Court of Arbitration at the International Chamber of Commerce ("ICC") alleging default under three rouble-denominated loans. On February 12, 2007, the ICC International Court of Arbitration ruled in favor of Yukos Capital and issued an award to Yukos Capital, including US\$ 275 million of principal, interest, damages and arbitration costs. In addition, the award amount accrues interest at 9% p.a. to the date of payment. No enforcement proceedings have been initiated in Russia (or elsewhere).

In January 2006, Yukos Capital initiated arbitral proceedings against OJSC Samaraneftgaz before the ICC International Court of Arbitration alleging default under two rouble-denominated loans and claiming early redemption of these loans and accrued interest. On August 15, 2007, the ICC ruled in favor of Yukos Capital and issued an award to Yukos Capital, including US\$ 121 million of principal, interest, arbitration and legal costs. In addition, the principal and interest amounts awarded to Yukos Capital against OJSC Samaraneftgaz accrue interest at 9% p.a. to the date of payment. No enforcement proceedings have been initiated in Russia (or elsewhere).

A subsidiary of Rosneft that holds shares in OJSC Tomskneft VNK and OJSC Samaraneftgaz has filed claims in Russia seeking to have OJSC Tomskneft VNK's and OJSC Samaraneftgaz's loans described above declared void as a matter of Russian law. Preliminary hearings on the claim by Rosneft's subsidiary against Yukos Capital and OJSC Tomskneft VNK were rescheduled for the summer 2008. Preliminary hearings on the claim by the Rosneft's subsidiary against Yukos Capital and OJSC Samaraneftgaz are scheduled for May 28, 2008.

## Notes to Consolidated Financial Statements (continued)

**23. Commitments and Contingencies (continued)****Yukos Capital Litigation (continued)**

Rosneft shareholder has filed claims seeking to have OJSC Yuganskneftegaz loans from Yukos Capital described above declared void as a matter of Russian law. Preliminary hearings on the claim by the shareholder of Rosneft against Yukos Capital and Rosneft were rescheduled for April 9, 2008.

The Company believes that any payment in excess of US\$ 728 million, being the carrying amount of the respective loans (see Note 16), is remote.

**Other Litigations, Claims and Assessments**

The Company is a co-defendant in the litigation in the United States of America in respect of the acquisition of OJSC Yuganskneftegaz. This litigation was brought by certain holders of American Depository Receipts (ADR) of Yukos Oil Company seeking unspecified damages due to the fall in the market value of the ADRs. On July 13, 2006, plaintiffs filed an amended complaint. The amended complaint seeks to recover alleged losses resulting from events surrounding Yukos Oil Company, including levying of taxes upon Yukos Oil Company by the Russian Federation and the arrest of certain assets of Yukos Oil Company to pay owed taxes. Defendants filed motions to dismiss the claim on numerous grounds. On November 26, 2007, the United States District Court for the District of Columbia, granted motions to dismiss Rosneft, its officers and other defendants from the action on jurisdictional grounds. The appeal term for these dismissals has expired.

The Company is also a co-defendant in litigation in the Moscow Arbitration Court with respect to the auction for the common shares of OJSC Yuganskneftegaz. This litigation was brought by Yukos Oil Company. The claimant is seeking to recover all the common shares of OJSC Yuganskneftegaz and also damages in the total amount of RUR 388 billion (US\$ 15.8 billion at the CBR exchange rate as of December 31, 2007). In February 2007, the Moscow Arbitration Court dismissed Yukos Oil Company's claim and the dismissal was upheld on appeal on May 30, 2007. This ruling was also upheld in cassation court on October 12, 2007. Yukos Oil Company was liquidated on November 21, 2007 therefore the probability of further litigation is negligible.

In September 2007, Ecolnat Prim, a Moldavian company acting on behalf of a company called New Century Securities Management Anstald ("New Century Securities", Principality of Liechtenstein), filed a claim in the District Economic Court of Chisinau in Moldova against the OJSC Angarsk Petrochemical Company, Fericire-Faleshti SRL and LLC Metmar regarding repayment under a promissory note, which was alleged to have been issued by OJSC Angarsk Petrochemical Company in 1996, this being denied by OJSC Angarsk Petrochemical Company, for the aggregate amount of US\$ 446 million, including principal, interest and penalties. New Century Securities earlier initiated court proceedings against the OJSC Angarsk Petrochemical Company and AKB Rostrabank demanding payment of the principal amount, interest and penalties under this promissory note in Russia. Although the first instance court ruled in favor of New Century Securities in 2005, the appellate court, the cassation court and the Supreme Arbitration Court of Russia dismissed the claim by New Century Securities during 2006-2007 based on the failure of New Century Securities to provide the original of the promissory note to the first instance court. On July 17, 2007, the Constitutional Court of Russia rejected the claim by New Century Securities challenging the compliance of certain rules of both Russian substantive and procedural law with the Constitution of the Russian Federation. On December 24, 2007, the court proceedings in respect of the claim by Ecolnat Prim relating to the Angarsk Refinery Promissory Note were terminated. This decision is subject to appeal. Rosneft plans to vigorously contest the claim by Ecolnat Prim and believes that the risk of any negative outcome is remote.

The Company's and its subsidiaries are involved in other litigations which arise from time to time in the course of their business activities. The Company's management believes that the ultimate result of these litigations will not significantly affect the operating results or financial position of the Company.



Notes to Consolidated Financial Statements (continued)

**23. Commitments and Contingencies (continued)**

**Licence Agreements**

In accordance with certain licence agreements or separate agreements concluded from time to time with the local and regional authorities the Company is required to maintain certain levels of expenditures for health, safety and environmental protection, as well as maintain certain level of capital expenditures. Generally these expenditures are within the normal operating and capital budgets and are accounted for when incurred in accordance with existing accounting policies for respective costs and expenses.

**Oil Supplies**

In January 2005, the Company entered into a long-term contract for the term through 2010 with China National United Oil Corporation for export of crude oil in the total amount of 48.4 million tons to be delivered in equal annual amounts. The prices are determined based on usual commercial terms for crude oil deliveries (See Note 16).

**24. Segment Information**

Presented below is information about the Company's operating segments in accordance with SFAS 131, *Disclosures about Segments of an Enterprise and Related Information*. The Company determines its operating segments based on the nature of their operations. The performance of these operating segments is assessed by management on a regular basis. The exploration and production segment is engaged in field exploration and development and production of crude oil and natural gas. The refinery, marketing and distribution segment is engaged in processing crude oil and other hydrocarbons into petroleum products, as well as purchasing, sale and transportation of crude oil and petroleum products. Corporate assets are allocated between Exploration and production and Refining, marketing and distribution in proportion to sales of these segments. Drilling services, construction services, banking and finance services, and other activities are combined in All other. Substantially all of the Company's operations are conducted in the Russian Federation. Further, the geographical regions within the Russian Federation have substantially similar economic and regulatory conditions. Therefore, the Company has not presented any separate geographical disclosure.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 24. Segment Information (continued)

The significant accounting policies applied to each operating segment are consistent with those applied to the consolidated financial statements. Sales transactions for goods and services between the operating segments are carried out using prices agreed upon between Rosneft and its subsidiaries.

Operating segments in 2007:

	<b>Exploration and production</b>	<b>Refining, marketing and distribution</b>	<b>All other</b>	<b>Total elimination</b>	<b>Consolidated</b>
Revenues from external customers	2,145	46,631	440	–	49,216
Intersegmental revenues	9,788	2,197	2,104	(14,089)	–
<b>Total revenues</b>	<b>11,933</b>	<b>48,828</b>	<b>2,544</b>	<b>(14,089)</b>	<b>49,216</b>
Operating expenses and cost of purchased oil and petroleum products	2,634	2,472	374	–	5,480
Depreciation, depletion and amortization	2,828	374	84	–	3,286
Operating income	4,980	18,052	1,778	(14,089)	10,721
Total other income, net					7,068
<b>Income before income tax and minority interest</b>					<b>17,789</b>
Total assets	41,888	25,445	7,472	–	74,805

Operating segments in 2006:

	<b>Exploration and production</b>	<b>Refining, marketing and distribution</b>	<b>All other</b>	<b>Total elimination</b>	<b>Consolidated</b>
Revenues from external customers	442	32,460	197	–	33,099
Intersegmental revenues	10,465	1,287	903	(12,655)	–
<b>Total revenues</b>	<b>10,907</b>	<b>33,747</b>	<b>1,100</b>	<b>(12,655)</b>	<b>33,099</b>
Operating expenses and cost of purchased oil and petroleum products	1,670	1,635	212	–	3,517
Depreciation, depletion and amortization	1,420	201	17	–	1,638
Operating income	2,126	15,367	766	(12,655)	5,604
Total other expenses, net					(1,439)
<b>Income before income tax and minority interest</b>					<b>4,165</b>
Total assets	33,934	10,757	2,099	–	46,790

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### 24. Segment Information (continued)

Operating segments in 2005:

	<b>Exploration and production</b>	<b>Refining, marketing and distribution</b>	<b>All other</b>	<b>Total elimination</b>	<b>Consolidated</b>
Revenues from external customers	378	23,151	334	–	23,863
Intersegmental revenues	9,534	797	297	(10,628)	–
<b>Total revenues</b>	<b>9,912</b>	<b>23,948</b>	<b>631</b>	<b>(10,628)</b>	<b>23,863</b>
Operating expenses and cost of purchased oil and petroleum products	1,333	863	64	–	2,260
Depreciation, depletion and amortization	1,320	143	9	–	1,472
Operating income	1,781	13,902	467	(10,628)	5,522
Total other income, net					692
<b>Income before income tax and minority interest</b>					<b>6,214</b>
Total assets	23,005	5,841	1,170	–	30,016

Below is a breakdown of revenues by domestic and export sales, with a classification of export sales based on the country of incorporation of the foreign customer.

	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Oil and gas sales</b>			
Export sales of crude oil – Europe	<b>19,876</b>	15,888	11,489
Export sales of crude oil – Asia	<b>6,255</b>	5,145	2,303
Export sales of crude oil – CIS	<b>2,220</b>	1,620	1,491
Export sales of crude oil – other directions	<b>691</b>	435	94
Domestic sales of crude oil	<b>521</b>	214	600
Domestic sales of gas	<b>339</b>	197	175
<b>Total oil and gas sales</b>	<b>29,902</b>	<b>23,499</b>	<b>16,152</b>
<b>Petroleum products and processing fees</b>			
Export sales of petroleum products – Europe	<b>5,875</b>	3,152	2,827
Export sales of petroleum products – Asia	<b>3,489</b>	1,941	1,618
Export sales of petroleum products – CIS	<b>338</b>	202	64
Domestic sales of petroleum products	<b>8,672</b>	3,953	2,865
Sales of petrochemical products	<b>113</b>	–	–
Processing fees	<b>44</b>	2	–
<b>Total petroleum products and processing fees</b>	<b>18,531</b>	<b>9,250</b>	<b>7,374</b>

During the reporting periods, the Company had one customer in 2007, three customers in 2006 and one customer in 2005, all being international oil traders which accounted for 10% or more of total revenues. These customers accounted for revenues of US\$ 8,046 million, US\$ 18,001 million, and US\$ 5,041 million or 16%, 54% and 21% of total revenues, respectively. These revenues are recognized mainly under the Refining, Marketing and Distribution segment. Management does not believe that the Company is dependent on any particular customer.

Notes to Consolidated Financial Statements (continued)

**25. Fair Value of Financial Instruments and Risk Management**

The Company, in connection with its current activities, is exposed to various financial risks, such as foreign currency risks, interest rate risks and credit risks. The Company manages these risks and monitors its exposure on a regular basis.

The fair value of cash and cash equivalents, held to maturity securities, accounts receivable and accounts payable, other current assets, approximates their carrying value recognized in these financial statements. The Company's management believes that accounts receivable recorded net of allowance for doubtful accounts will be recovered in full during an acceptable time period. The fair value of long-term debt differs from the amounts recognized in the consolidated financial statements. The estimated fair value of long-term debt discounted using the estimated market interest rate for similar financial liabilities amounted to US\$ 14,911 million and US\$ 9,710 million as of December 31, 2007 and 2006, respectively. These amounts include all future cash outflows related to the repayment of long-term loans, including their current portion and interest expenses.

A substantial portion of the Company's sales revenues is received in US dollars. In addition, substantial financing and investing activities, obligations and commitments are also undertaken in US dollars. However, significant operating and investing expenditures, other obligations and commitments as well as tax liabilities are denominated in rubles. As a result of any decline of the US dollar against the ruble, the Company is exposed to the corresponding currency risk.

The Company enters into contracts to economically hedge certain of its risks associated with ruble appreciation and increased interest expense accrued on loans received by the Company but these contracts are not accounted for as hedges pursuant to SFAS 133.

During 2007, the Company entered into forward and option foreign currency contracts to hedge its foreign currency risk of forecasted operating expense. These financial exposures are managed as an integral part of the Company's risk management program, which seeks to reduce the potentially adverse effect that the volatility of the exchange rate markets may have on operating results. Presently, the maximum term over which the Company has economically hedged exposures to the variability of the currency exchange rates under its derivative instruments is 3 months.

As a result of the above mentioned forward and option foreign currency contracts entered in 2007, the fair value of forward and option contracts in the amount of US\$ 61.9 million was recorded as prepayments and other current assets in the consolidated balance sheet as of December 31, 2007 and the change in fair value was recognized as a foreign exchange gain in the amount of US\$ 47.1 million in the consolidated statement of income, net of tax effects.

In December 2007, the Company entered into a five year interest rate swap contract with a notional amount of US\$ 3 billion. Under the terms of the contract, a floating LIBOR rate may be converted into a certain fixed rate. The other party has a call option to terminate. The fair value of the interest swap contract was recorded in the consolidated balance sheet as of December 31, 2007 as other current liabilities in the amount of US\$ 13.5 million. The change in fair value was recorded in the consolidated statement of income as a component of interest expense in the amount of US\$ 13.5 million.

Fair values of foreign currency forward and option contracts, and interest rate swap contracts are based on estimated amounts that the Company would pay or receive upon termination of the contracts as of December 31, 2007.

Notes to Consolidated Financial Statements (continued)

**26. Subsequent Events**

In January 2008, one of the Company's subsidiaries acquired through an auction sale a right for a three-year lease of nine land plots in Saint Petersburg for the total consideration of US\$ 4.2 million (RUB 103.0 million at the CBR exchange rate as of December 31, 2007). The above land plots will be used for construction of gas stations.

In the first quarter of 2008 the Company won an auction for the right to explore and produce hydrocarbons in Umotkinskiy Block located in the Irkutsk region. The consideration amounted to RUB 1.12 billion (US\$ 46 million at the CBR exchange rate as of December 31, 2007) and was paid in cash.

In February 2008, the Company raised a syndicated loan for US\$ 3.0 billion that was provided by the group of international banks at the interest rate of LIBOR plus 0.95%. The loan matures in 5 years and is secured by oil export contracts. The funds were mainly used to refinance a portion of the bridge financing (See Note 16).

In February 2008, the Company bought 237,572 additional ordinary shares of OJSC Verhnechonskneftegaz for RUB 285 million (US\$ 11.7 million at the CBR exchange rate as of the transaction date). Through this purchase the Company maintained its previous share of 25.94% in this investment.

In March 2008, the Company repaid a portion of the bridge financing in the amount of US\$ 2.23 billion and during the first quarter of 2008 the Company also made all scheduled planned repayments under its various banking facilities of US\$ 0.57 billion, representing the total scheduled maturities for the first quarter of 2008.

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### Supplementary Oil and Gas Disclosure (unaudited)

In accordance with SFAS 69, *Disclosures about Oil and Gas Producing Activities*, the Company makes certain supplemental disclosures about its oil and gas exploration and production operations. While this information was developed with reasonable care and disclosed in good faith, it is emphasized that the data represents management's best estimates. Accordingly, this information may not necessarily represent the current financial condition of the Company and its expected future financial results.

All of the Company's activities are conducted in Russia, which is considered as one geographic area.

### *Capitalized Costs Relating to Oil and Gas Producing Activities*

	<b>As of December 31, 2006</b>	
	<b>2007</b>	<b>2006</b>
Oil and gas properties related to proved reserves	<b>43,708</b>	34,259
Oil and gas properties related to unproved reserves	<b>4,165</b>	3,878
<b>Total</b>	<b>47,873</b>	38,137
Accumulated depreciation, depletion and amortization, and valuation allowances	<b>(7,942)</b>	(5,178)
<b>Net capitalized costs</b>	<b>39,931</b>	32,959

The share of the Company in the capitalized costs of equity investees on December 31, 2007 and December 31, 2006 was US\$ 2,331 million and US\$ 388 million, respectively. Net book value of mineral rights on December 31, 2007 and December 31, 2006 was US\$ 17.7 billion and US\$ 18.4 billion, respectively.

### *Cost Incurred in Oil and Gas Property Acquisition, Exploration and Development Activities*

	<b>2007</b>	<b>2006</b>	<b>2005</b>
Acquisition of proved oil and gas properties	<b>4,825</b>	8,392	3,475
Acquisition of unproved oil and gas properties	<b>287</b>	2,350	487
Exploration costs	<b>162</b>	193	164
Development costs	<b>4,624</b>	2,795	1,606
<b>Total costs incurred</b>	<b>9,898</b>	13,730	5,732

The share of the Company in acquisition, exploration and development expenditures of its equity investees was US\$ 440 million and US\$ 46 million in 2007 and 2006, respectively, and was not significant during 2005.

### *Results of Operations for Oil & Gas Producing Activities*

	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Revenues:</b>			
External sales	<b>15,896</b>	11,246	9,313
Transfers to other operations	<b>11,006</b>	5,216	4,416
<b>Total revenues</b>	<b>26,902</b>	16,462	13,729
Production costs (excluding production taxes)	<b>2,638</b>	1,632	1,333
Selling, general and administrative expenses	<b>729</b>	480	229
Exploration expenses	<b>162</b>	193	164
Accretion expense	<b>78</b>	34	35
Depreciation, depletion and amortization	<b>2,828</b>	1,420	1,426
Taxes other than income tax	<b>9,772</b>	6,636	4,735
Income tax	<b>2,173</b>	1,384	1,274
<b>Results of operation for producing activities</b>	<b>8,522</b>	4,683	4,533

## Notes to Consolidated Financial Statements (continued)

**Supplementary Oil and Gas Disclosure (unaudited) (continued)*****Results of Operations for Oil & Gas Producing Activities (continued)***

In prior periods the Company presented revenues within results of operations for oil and gas producing activities consistent with those presented in the Company's operating segment disclosure. In 2007 and 2006, the Company changed the presentation of results of operations for oil and gas producing activities for all periods presented to include revenues based on market prices determined at the point of delivery from production units. The presentation of results of operations for previous reporting periods was changed accordingly.

The Company's share in the results of operations for oil and gas production of equity investees in 2007, 2006 and 2005 was US\$ 256 million, US\$ 59 million and US\$ 35 million, respectively.

***Reserve Quantity Information***

For the purposes of evaluation of reserves as of December 31, 2007, 2006 and 2005 the Company used the oil and gas reserve information prepared by DeGolyer and MacNaughton, independent reservoir engineers, prepared in accordance with United States Securities and Exchange Commission definitions. Proved reserves are those estimated quantities of crude oil and gas which, by analysis of geological and engineering data, demonstrate with reasonable certainty to be recoverable in the future from existing reservoirs under the existing economic and operating conditions. In certain cases, recovery of such reserves may require considerable investments in wells and related equipment. Proved reserves also include additional oil and gas reserves that will be extracted after the expiry date of licence agreements or may be discovered as a result of secondary and tertiary extraction which have been successfully tested and checked for commercial benefit. Proved developed reserves are the quantities of crude oil and gas expected to be recovered from existing wells using existing equipment and operating methods.

Proved undeveloped oil and gas reserves are reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion. Reserves on undrilled acreage are limited to those drilling units offsetting productive units that are reasonably certain of production when drilled. Proved reserves for other undrilled units can be claimed only where it can be demonstrated with certainty that there is continuity of production from the existing productive formation. Under no circumstances are estimates of proved undeveloped reserves attributable to any acreage for which an application of fluid injection or other improved recovery technique is contemplated, unless those techniques have been proved effective by actual tests in the area and in the same reservoir. Due to inherent industry uncertainties and the limited nature of deposit data, estimates of reserves are subject to change as additional information becomes available.

The Company included in proved reserves those reserves which the Company intends to extract after the expiry of the current licences. The licences for the development and production of hydrocarbons currently held by the Company generally expire between 2009 and 2031, and the licences for the most important deposits expire between 2013 and 2019. In accordance with the effective version of the law of the Russian Federation, *On Subsurface Resources* (the "Law"), licences are currently granted for a production period determined on the basis of technological and economic criteria applied to the development of a mineral deposit which guarantee rational use of subsurface resources and necessary environmental protection. In accordance with the Law and upon gradual expiration of old licences issued under the previous version of the Law, the Company extends its hydrocarbon production licences for the whole productive life of the fields. Extension of the licences depends on both current and future compliance with the terms set forth in the licence agreements. As of the date of these financial statements, the Company is generally in compliance with all the terms of the licence agreements and intends to continue complying with such terms in the future (see Note 11).

# OJSC Oil Company Rosneft

## Notes to Consolidated Financial Statements (continued)

### Supplementary Oil and Gas Disclosure (unaudited) (continued)

#### *Reserve Quantity Information (continued)*

The Company's estimates of net proved oil and gas reserves and changes thereto for the years ended December 31, 2007, 2006 and 2005 are shown in the table below and expressed in million barrels of oil equivalent (oil production data was recalculated from tonnes to barrels using a ratio of 7.3 barrels per tonne, gas production data was recalculated from cubic meters to barrels of oil equivalent using a ratio of 35.3/6 cubic meters per barrel):

	<b>2007</b>	<b>2006</b>	<b>2005</b>
	<i>mln. boe.</i>	<i>mln. boe.</i>	<i>mln. boe.</i>
<b>Beginning of year reserves</b>	<b>12,671</b>	11,813	12,744
Revisions of previous estimates	<b>62</b>	1,142	(373)
Extension and discovery of new reserves	<b>558</b>	297	63
Acquisitions of new properties	<b>1,039</b>	74	–
Production	<b>(792)</b>	(655)	(621)
	<b>13,538</b>	12,671	11,813
<b>End of year reserves</b>	<b>13,538</b>	12,671	11,813
Of which:			
Proved reserves under PSA Sakhalin 1	<b>62</b>	71	–
Proved developed reserves	<b>10,456</b>	9,891	8,507
Minority interest in total proved reserves	<b>22</b>	15	2,393
Minority interest in proved developed reserves	<b>15</b>	15	1,732

The Company's share in the proved reserves of equity investees in 2007, 2006 and 2005 was 915 million barrels of oil equivalent, 330 million barrels of oil equivalent and 46 million barrels of oil equivalent, respectively.

The Company's share in the proved developed reserves of equity investees in 2007, 2006 and 2005 was 689 million barrels of oil equivalent, 281 million barrels of oil equivalent and 45 million barrels of oil equivalent, respectively.

The minority interest in proved developed and total proved reserves in 2005 mainly relates to OJSC Yuganskneftegaz.

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

The standardized measure of discounted future net cash flows related to the above oil and gas reserves is calculated in accordance with the requirements of SFAS 69. Estimated future cash inflows from oil and gas production are computed by applying year-end prices for oil and gas to year-end quantities of estimated net proved reserves. Adjustment in this calculation for future price changes is limited to those required by contractual arrangements in existence at the end of each reporting period. Future development and production costs are those estimated future expenditures necessary to develop and produce estimated proved reserves as of year-end based on year-end cost indices and assuming continuation of year end economic conditions. Estimated future income taxes are calculated by applying appropriate year-end statutory tax rates. These rates reflect allowable deductions and tax credits and are applied to estimated future net pre-tax cash flows, net of the tax bases of related assets.

Discounted future net cash flows are calculated using a 10% discount factor. Discounting requires a year-by-year estimates of future expenditures to be incurred in the periods when the reserves will be extracted.



OJSC Oil Company Rosneft

Notes to Consolidated Financial Statements (continued)

**Supplementary Oil and Gas Disclosure (unaudited) (continued)**

***Standardized Measure of Discounted Future Net Cash Flows and Changes therein Relating to Proved Oil and Gas Reserves (continued)***

The information provided in the tables below does not represent management's estimates of the Company's expected future cash flows or of the value of its proved oil and gas reserves. Estimates of proved reserves change over time as new information becomes available. Moreover, probable and possible reserves which may become proved in the future are excluded from the calculations. The arbitrary valuation prescribed under SFAS 69 requires assumptions as to the timing and the amount of future development and production costs. The calculations should not be relied upon as an indication of the Company's future cash flows or of the value of its oil and gas reserves.

	<b>2007</b>	<b>2006</b>	<b>2005</b>
Future cash inflows	<b>551,015</b>	308,051	274,619
Future development costs	<b>(20,656)</b>	(16,426)	(12,507)
Future production costs	<b>(261,712)</b>	(154,045)	(80,564)
Future income tax expenses	<b>(64,589)</b>	(31,991)	(43,291)
Future net cash flows	<b>204,058</b>	105,589	138,257
Discount of estimated timing of cash flows	<b>(121,681)</b>	(64,019)	(87,100)
<b>Discounted value of future cash flows as of the end of year</b>	<b>82,377</b>	41,570	51,157

	<b>2007</b>	<b>2006</b>	<b>2005</b>
Discounted value of future cash flows as of the beginning of year	<b>41,570</b>	51,157	29,176
Sales and transfers of oil and gas produced, net of production costs and taxes other than income taxes	<b>(12,154)</b>	(7,714)	(7,432)
Changes in price estimates, net	<b>45,039</b>	(22,018)	26,798
Changes in future development costs	<b>(3,693)</b>	(4,084)	3,471
Development costs incurred during the period	<b>4,500</b>	2,795	1,752
Revisions of previous reserves estimates	<b>2,207</b>	4,034	1,097
Discovery of new reserves, less respective expenses	<b>3,213</b>	1,177	115
Net change in income taxes	<b>(11,761)</b>	3,580	(5,743)
Accretion of discount	<b>4,157</b>	5,116	2,918
Purchase of new oil and gas fields	<b>7,395</b>	1,464	–
Other	<b>1,904</b>	6,063	(995)
<b>Discounted value of future cash flows as of the end of year</b>	<b>82,377</b>	41,570	51,157

The Company's share in the discounted value of future cash flows related to the oil and gas reserves of equity investees in 2007, 2006 and 2005 was US\$ 9,324 million, US\$ 1,086 million and US\$ 549 million, respectively.

Discounted value of future cash flows as of December 31, 2007, 2006 and 2005 includes the interest of other (minority) shareholders in the amount of US\$ 114 million, US\$ 25 million and US\$ 10,574 million, respectively.