Consolidated financial statements
OJSC "Pharmstandard" and its subsidiaries
for the year ended 31 December 2014

with independent auditor's report

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Совершенствуя бизнес,
улучшаем мир

Independent auditor's report

To the Shareholders and Management of
OJSC "Pharmstandard"

We have audited the accompanying consolidated financial statements of OJSC "Pharmstandard" and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December 2014, and consolidated statement of comprehensive income, consolidated cash flow statement and consolidated statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information.

Audited entity's responsibility for the consolidated financial statements

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

Auditor's responsibility

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

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of OJSC "Pharmstandard" and its subsidiaries as at 31 December 2014, and their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

A.B. Khorovitch
Partner
Ernst & Young LLC

27 April 2015

Details of the audited entity

Name: OJSC "Pharmstandard"
Record made in the State Register of Legal Entities on 5 May 2006, State Registration Number 02№005162109.
Address: 141701, Russia, Moscow region, Dolgoprudny, Likhachevsky drive, 5 "b".

Details of the auditor

Name: Ernst & Young LLC
Record made in the State Register of Legal Entities on 5 December 2002, State Registration Number 1027739707203.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young LLC is a member of self-regulatory organization of auditors Non Profit partnership "Russian Audit Chamber" ("SRO NP APR"). Ernst & Young LLC is included in the control copy of the register of auditors and audit organizations, main registration number 10201017420.

OJSC "Pharmstandard"

Consolidated statement of financial position

As at 31 December 2014

(in thousands of Russian Roubles)

	Notes	2014	2013 (reclassified, Note 2)
Assets			
Non-current assets			
Property, plant and equipment	13	9,817,331	8,403,238
Intangible assets	14	3,122,597	3,202,517
Long-term financial assets	19	1,283,079	537,458
Investments in associates and joint venture	8, 9	6,319,310	1,478,561
Deferred tax asset	31	480,330	258,050
		21,022,647	**13,879,824**
Current assets			
Inventories	15	7,049,775	7,486,754
Trade and other receivables	16	19,432,066	23,969,063
VAT recoverable		116,304	337,772
Prepayments		319,287	373,745
Short-term financial assets	18	6,338,846	1,453,322
Cash and short term deposits	17	8,541,548	15,364,875
		41,797,826	**48,985,531**
Total assets		**62,820,473**	**62,865,355**
Equity and liabilities			
Equity attributable to equity holders of the parent			
Share capital	24	37,793	37,793
Treasury shares		(1,437)	(1,437)
Foreign currency translation reserve		729,560	24,846
Retained earnings		38,408,477	27,567,243
		39,174,393	**27,628,445**
Non-controlling interests		1,645,947	1,445,848
Total equity		**40,820,340**	**29,074,293**
Non-current liabilities			
Deferred tax liability	31	606,773	444,145
Other non-current liabilities	23	92,472	150,762
		699,245	**594,907**
Current liabilities			
Trade and other payables	22	15,834,351	24,931,724
Short-term borrowings and loans	20	4,002,941	7,024,080
Income tax payable		807,972	332,068
Taxes payable other than income tax	21	655,624	908,283
		21,300,888	**33,196,155**
Total liabilities		**22,000,133**	**33,791,062**
Total equity and liabilities		**62,820,473**	**62,865,355**

Signed and authorised for release on behalf of the Board of Directors of OJSC Pharmstandard

Chief Executive Officer V.M. Chupikov

Chief Financial Officer M.A. Markova

27 April 2015

The accompanying notes on pages 9-57 are an integral part of these consolidated financial statements.

OJSC "Pharmstandard"

Consolidated statement of comprehensive income

For the year ended 31 December 2014

(in thousands of Russian Roubles)

	Notes	2014	2013 (reclassified, Note 2)
Revenue	25	41,223,435	57,056,181
Cost of sales	26	(23,007,040)	(32,584,628)
Gross profit		**18,216,395**	**24,471,553**
Selling and distribution costs	27	(4,133,517)	(6,193,581)
General and administrative expenses	28	(2,300,426)	(1,930,313)
Other income	29	2,943,445	517,301
Other expenses	30	(1,032,936)	(1,068,144)
Interest income		323,446	290,074
Interest expense		(431,739)	(126,632)
Share in profit/(loss) of equity accounted investments, net	8, 9	235,062	(97,728)
Profit before income tax		**13,819,730**	**15,862,530**
Income tax expense	31	(2,724,267)	(3,942,091)
Profit for the year		**11,095,463**	**11,920,439**
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Exchange differences on translation of foreign operations		682,853	30,247
Other comprehensive income for the year to be reclassified to profit or loss in subsequent periods		**682,853**	**30,247**
Total comprehensive income for the year		**11,778,316**	**11,950,686**
Profit for the year			
Attributable to:			
Equity holders of the parent		10,841,234	11,805,787
Non-controlling interests		254,229	114,652
		11,095,463	**11,920,439**
Total comprehensive income for the year			
Attributable to:			
Equity holders of the parent		11,545,948	11,835,761
Non-controlling interests		232,368	114,925
		11,778,316	**11,950,686**
Earnings per share (in Russian roubles) - basic and diluted, based on profit for the year attributable to equity holders of the parent	24	298.2	340.92

Signed and authorised for release on behalf of the Board of Directors of OJSC Pharmstandard

Chief Executive Officer V.M. Chupikov

Chief Financial Officer M.A. Markova

27 April 2015

The accompanying notes on pages 9-57 are an integral part of these consolidated financial statements.

OJSC "Pharmstandard"

Consolidated cash flow statement

For the year ended 31 December 2014

(in thousands of Russian Roubles)

	Notes	2014	2013
Cash flows from operating activities			
Profit before income tax		13,819,730	15,862,530
Adjustments for:			
Depreciation and amortisation	13, 14	944,670	953,836
(Gain)/loss from impairment of trade and other receivables, net	16	(17,648)	136,928
Write-down of inventories to net realisable value, net	15	77,399	187,701
Impairment charge – property, plant and equipment	13, 29, 30	53,250	457
Reversal of impairment – financial assets	29	(61,213)	–
Write-off of cash restricted in Cyprus bank		–	9,269
Impairment charge – intangible assets	30	–	100,000
Gain from disposal of property, plant and equipment	13, 29	(39,418)	(47,912)
Share in net (profit)/loss of joint ventures and associate		(235,062)	97,728
Foreign exchange gain		(1,913,390)	(157,827)
Gain from transactions with promissory notes	29	(80,112)	–
Interest income		(323,446)	(290,074)
Interest expense		431,739	126,632
Operating cash flows before working capital changes		**12,656,499**	**16,979,268**
Decrease/(increase) in trade and other receivables	16	4,764,839	(9,157,513)
Decrease in inventories	15	359,580	858,269
Decrease/(increase) in VAT recoverable		221,468	(4,254)
Decrease/(increase) in prepayments		54,458	(97,493)
(Decrease)/increase in trade and other payables	22	(5,562,023)	8,997,618
Decrease in taxes payable other than income tax	21	(252,659)	(177,736)
Cash generated from operations		**12,242,162**	**17,398,160**
Income tax paid	31	(2,308,015)	(4,086,713)
Interest paid		(456,799)	(111,784)
Interest received		138,587	329,084
Net cash from operating activities		**9,615,935**	**13,528,747**
Cash flows from investing activities			
Purchase of property, plant and equipment	13	(2,380,677)	(1,475,004)
Payments for development expenditures	14	(45,627)	(98,740)
Cash paid for acquisition of share in associates	9	(3,858,103)	(1,206,457)
Acquisition of intangible assets	7, 14	(48,065)	(2,409,854)
Cash in new subsidiary (joint venture prior to 1 January 2013)	8.1	–	259,125
Proceeds from government grants	23	–	64,100
Cash received from sale property, plant and equipment		113,764	64,148
Cash paid for long-term bank deposit	19	(42,900)	(400,000)
Cash received from return of deposit	19	400,000	–
Cash paid for acquisition of financial assets available for sale	19	(575,824)	(65,458)
Cash received from return of short-term financial assets	18	303,575	2,951,958
Short-term bank deposit placed	18	(66,166)	(675,257)
Loans provided to third parties	18, 19	(1,864,349)	–
Loans provided to related parties	18	(3,335,159)	(1,945,978)
Loans repaid by related parties	12	1,432,735	2,751,469
Cash paid for purchase of promissory notes	12	(3,420,978)	–
Cash received from transactions with promissory notes	12	3,501,090	–
Net cash used in investing activities		**(9,886,684)**	**(2,185,948)**
Cash flows from financing activities			
Proceeds from loans and borrowings	20	4,000,000	7,721,700
Repayment of loans and borrowings	20	(7,021,139)	(700,000)
Cash distribution to OTCpharm	6, 22	(3,500,650)	–
Cash paid for acquisition of non-controlling interests	10	–	(360,730)
Cash paid for acquisition of treasury shares		–	(11,076,520)
Dividends paid by a subsidiary to non-controlling shareholders	34	(32,269)	(23,498)
Net cash used in financing activities		**(6,554,058)**	**(4,439,048)**
Net increase in cash and cash equivalents		**(6,824,807)**	**6,903,751**
Net foreign exchange differences		1,480	(1,858)
Cash and cash equivalents at the beginning of the year	17	15,364,875	8,462,982
Cash and cash equivalents at the end of the year	17	**8,541,548**	**15,364,875**

The accompanying notes on pages 9-57 are an integral part of these consolidated financial statements.

OJSC “Pharmstandard”

Consolidated statement of changes in equity

For the year ended 31 December 2014

(in thousands of Russian Roubles)

	Equity attributable to equity holders of the parent						
	Share capital	Treasury shares	Foreign currency translation reserve	Retained earnings	Total	Non-controlling Interests	Total equity
Balance at 1 January 2013	**37,793**	**(3,190)**	**(1,922)**	**37,533,953**	**37,566,634**	**1,651,138**	**39,217,772**
Profit for the year	–	–	–	11,805,787	**11,805,787**	114,652	**11,920,439**
Other comprehensive income for the year	–	–	29,974	–	**29,974**	273	**30,247**
Total comprehensive income for the year	**–**	**–**	**29,974**	**11,805,787**	**11,835,761**	**114,925**	**11,950,686**
Incorporation of subsidiary	–	–	–	–	**–**	250	**250**
Acquisition of subsidiary	–	–	–	–	**–**	21,643	**21,643**
Acquisition of non-controlling interests (Note 10)	–	–	–	(42,120)	**(42,120)**	(318,610)	**(360,730)**
Dividends paid by a subsidiary (Note 34)	–	–	–	–	**–**	(23,498)	**(23,498)**
Effect of spin-off of OTC business (Note 6)	–	–	(3,206)	(23,005,391)	**(23,008,597)**	–	**(23,008,597)**
Acquisition of treasury shares	–	(5,329)	–	(11,071,191)	**(11,076,520)**	–	**(11,076,520)**
Treasury shares exchange for intangible asset (Note 7)	–	7,082	–	12,346,205	**12,353,287**	–	**12,353,287**
Balance at 31 December 2013	**37,793**	**(1,437)**	**24,846**	**27,567,243**	**27,628,445**	**1,445,848**	**29,074,293**
Profit for the year	–	–	–	10,841,234	**10,841,234**	254,229	**11,095,463**
Other comprehensive income for the year	–	–	704,714	–	**704,714**	(21,861)	**682,853**
Total comprehensive income for the year	**–**	**–**	**704,714**	**10,841,234**	**11,545,948**	**232,368**	**11,778,316**
Dividends paid by a subsidiary (Note 34)	–	–	–	–	**–**	(32,269)	**(32,269)**
Balance at 31 December 2014	**37,793**	**(1,437)**	**729,560**	**38,408,477**	**39,174,393**	**1,645,947**	**40,820,340**

The accompanying notes on pages 9-57 are an integral part of these consolidated financial statements.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

1. Corporate information

The principal activity of OJSC “Pharmstandard” (“the Company”) and its subsidiaries (“the Group”) are production and wholesale distribution of pharmaceutical products and medical equipment. The Company was incorporated in the Russian Federation. Since May 2007, the Company’s shares are publicly traded (Note 24). The Group’s corporate office is in Dolgoprudny, Likhachevsky proezd, 5B, Moscow region, Russian Federation and its manufacturing facilities are based in Moscow region, Vladimir region, Kursk, Tomsk, Ufa, Tyumen (all Russian Federation) and Kharkov (Ukraine). The Company held interest in the following subsidiaries, associates and joint ventures as at 31 December 2014 and 2013:

Entity	Country of incorporation	Activity	2014 effective share	2013 effective share
Subsidiaries				
1. “Pharmstandard” LLC	Russian Federation	Central procurement	100	100
2. “Pharmstandard-Leksredstva” OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
3. “Pharmstandard-Tomskhimpharm” OJSC	Russian Federation	Manufacturing of pharmaceutical products	91	91
4. “Pharmstandard-Ufavita” OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
5. “Pharmstandard-Biolik” PJSC	Ukraine	Manufacturing of pharmaceutical products	96.93	96.93
6. “TZMOI” OJSC	Russian Federation	Manufacturing of medical equipment	100	100
7. MDR Pharmaceuticals	Cyprus	Finance and holding company	50.05	50.05
8. Bigpearl Trading Limited*	Cyprus	Intermediary holding company	50.005	50.005
9. “Pharmapark” LLC*	Russian Federation	Manufacturing of pharmaceutical products	50.005	50.005
10. “Biomed named after I.I. Mechnikov” OJSC*	Russian Federation	Manufacturing of pharmaceutical products	49.845	49.845
11. “Pharmatsevticheskiye innovatsii”*	Russian Federation	Assets holder	50.005	50.005
12. “PKB named after I.I. Mechnikov” CJSC* (a)	Russian Federation	Assets holder	–	49.845
13. “EKK” OJSC*	Russian Federation	Sundry activity	35.29	35.29
14. “Lekko” CJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
15. Moldildo Trading Limited	Cyprus	Intermediary holding company	75	75
16. “Pharmstandard-Medtechnika” LLC	Russian Federation	Distribution of medical equipment	75	75
17. Pharmstandard International S.A.	Luxembourg	Venture investments	100	100
18. “Sellthera Pharm” LLC	Russian Federation	Development and manufacturing Company	75	75
Joint ventures and associates				
19. “NauchTechStroy Plus” LLC (NTS +)	Russian Federation	Research and development Company	37.5	37.5
20. “Argos Therapeutics” Inc. (b)	The USA	Research and development Company	30.40	35
21. “Biocad Holdings Limited” (c)	Cyprus	Research, development and manufacturing of pharmaceutical products	20	–

* These subsidiaries comprised “Bioprocess” group of companies acquired by the Company in July 2012. The Group exercises control over these entities through its controlling interest in Bigpearl Trading Limited.

(a) In August 2014 “PKB named after I.I. Mechnikov” merged with “Biomed named after I.I. Mechnikov” OJSC.

(b) The Group’s share decreased due to dilution of interest (Note 9.1).

(c) On 27 July 2014 the Company acquired share in “Biocad Holdings Limited (Note 9.2).

These consolidated financial statements were authorised for issue by the Board of Directors of OJSC “Pharmstandard” on 27 April 2015.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

2. Changes in classification of comparative information

In the process of preparation of the consolidated financial statements for the year ended 31 December 2014 the Company reconsidered its approach to presentation of the following items:

1. In the consolidated financial statements ended on 31 December 2013 agency fee in the amount of RR 1,037,886 and contract manufacturing fee in the amount of RR 110,698 net of the corresponding expenses in the amount of RR 74,790 were presented as other income. As a result of OTC Branded business spin-off, commencing from 1 January 2014 the Group is treating the above profit or loss items as integral elements of the primary operations of the Group and consequently presents them on a gross basis as revenue or cost of sales. The comparative information was adjusted accordingly and the effects of these adjustments on amounts presented in the consolidated statement of comprehensive income for the year ended 31 December 2013 were as follows:

	As originally	**Adjustments**	**As adjusted**
Revenue	55,907,597	1,148,584	57,056,181
Cost of sales	(32,509,838)	(74,790)	(32,584,628)
Other income	1,508,995	(1,073,794)	435,201

2. In the consolidated financial statements ended 31 December 2013 Deferred tax liability was presented on a net basis as the individual amounts were immaterial for the readers. Commencing from 1 January 2014 due to increased materiality of the amounts the Group presents Deferred tax liability and Deferred tax asset on a gross basis. The comparative information was adjusted accordingly and the effects of these adjustments on amounts presented in the consolidated statement of financial position as at 31 December 2013 were as follows:

	As originally	**Adjustments**	**As adjusted**
Deferred tax asset	–	258,050	258,050
Deferred tax liability	(186,095)	(258,050)	(444,145)

3. In the consolidated financial statements ended 31 December 2013 Foreign exchange gain was presented on a net basis as the individual amounts were immaterial for readers. Commencing from 1 January 2014 due to increased materiality of the amounts the Group presents Foreign exchange gain and loss on gross basis. The comparative information was adjusted accordingly and the effects of these adjustments on amounts presented in the consolidated statement of comprehensive income for the year ended 31 December 2013 were as follows:

	As originally	**Adjustments**	**As adjusted**
Other income	435,201	82,100	517,301
Other expenses	(986,044)	(82,100)	(1,068,144)

3. Basis of preparation of the financial statements

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (IASB).

Basis of accounting

The Group’s Russian entities maintain their accounting records in Russian Roubles (“RR”) and prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The Group’s Ukrainian subsidiary maintains its accounting records in Ukrainian Hryvnia (“UAH”) and prepares its statutory financial statements in accordance with IFRS. The other Group’s foreign entities located in the USA, Cyprus and Luxembourg primarily maintain their accounting records in US dollars and Euro and prepare their statutory accounting records in accordance with US GAAP, IFRS and the local regulation respectively. When necessary the local statutory financial statements have been adjusted to present these consolidated financial statements in accordance with IFRS. These adjustments principally relate to valuation and depreciation of property, plant and equipment, valuation and amortisation of intangible assets, certain valuation allowances, using fair values for certain assets, acquisition accounting for business combinations and the resulting income tax effects, and also to consolidation of subsidiaries and equity accounting of associates and joint ventures.

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below. For example, certain short-term assets are recorded at fair value and non-current assets classified as held for sale are recorded at the lower of carrying amount and fair value less costs to sell.

Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial period except that the Group has adopted the following new and amended IFRS and IFRIC interpretations as at 1 January 2014.

The nature and the impact of each new standard and amendment is described below:

Amendments to Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27) provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under IFRS 10 *Consolidated Financial Statements* and must be applied retrospectively, subject to certain transition relief. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss. These amendments have no impact on the Group, since none of the entities in the Group qualifies to be an investment entity under IFRS 10.

Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities clarify the meaning of “currently has a legally enforceable right to set-off’ and the criteria for non-simultaneous settlement mechanisms of clearing houses to qualify for offsetting and is applied retrospectively. These amendments have no impact on the Group, since none of the entities in the Group has any offsetting arrangements.

3. Basis of preparation of the financial statements (continued)

Changes in accounting policies (continued)

Amendments to IAS 39 Novation of Derivatives and Continuation of Hedge Accounting provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria and retrospective application is required. These amendments have no impact on the Group as the Group has no derivative financial instruments.

IFRIC 21 Levies clarifies that an entity recognises a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated before the specified minimum threshold is reached. Retrospective application is required for IFRIC 21. This interpretation has no impact on the Group as it has applied the recognition principles under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* consistent with the requirements of IFRIC 21 in prior years.

In the 2010-2012 annual improvements cycle, the IASB issued seven amendments to six standards, which included an amendment to IFRS 13 *Fair Value Measurement*. The amendment to IFRS 13 is effective immediately and, thus, for periods beginning at 1 January 2014, and it clarifies in the Basis for Conclusions that short-term receivables and payables with no stated interest rates can be measured at invoice amounts when the effect of discounting is immaterial. This amendment to IFRS 13 has no impact on the Group.

IFRSs and IFRIC interpretations not yet effective

- *IFRS 9 Financial Instruments:* in July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before 1 February 2015. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group’s financial assets, but no impact on the classification and measurement of the Group’s financial liabilities.

- *Amendments to IAS 19 Defined Benefit Plans: Employee Contributions:* these amendments clarify that, if the amount of the contributions is independent of the number of years of service, an entity is permitted to recognise such contributions as a reduction in the service cost in the period in which the service is rendered, instead of allocating the contributions to the periods of service. It is not expected that this amendment would be relevant to the Group, since none of the entities within the Group has defined benefit plans with contributions from employees or third parties.

3. Basis of preparation of the financial statements (continued)

IFRSs and IFRIC interpretations not yet effective (continued)

- *Annual improvements 2010-2012 Cycle:* these improvements are effective from 1 July 2014 and are not expected to have a material impact on the Group. They include:
  - *IFRS 3 Business Combinations:* the amendment is applied prospectively and clarifies that all contingent consideration arrangements classified as liabilities (or assets) arising from a business combination should be subsequently measured at fair value through profit or loss whether or not they fall within the scope of IFRS 9 (or IAS 39, as applicable).
  - *IFRS 8 Operating Segments:* the amendments are applied retrospectively and clarifies that an entity must disclose the judgements made by management in applying the aggregation criteria in paragraph 12 of IFRS 8, including a brief description of operating segments that have been aggregated and the economic characteristics (e.g., sales and gross margins) used to assess whether the segments are 'similar' and the reconciliation of segment assets to total assets is only required to be disclosed if the reconciliation is reported to the chief operating decision maker, similar to the required disclosure for segment liabilities.
  - *IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets:* the amendment is applied retrospectively and clarifies in IAS 16 and IAS 38 that the asset may be revalued by reference to observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortisation is the difference between the gross and carrying amounts of the asset.
  - *IAS 24 Related Party Disclosures:* the amendment is applied retrospectively and clarifies that a management entity (an entity that provides key management personnel services) is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services.
- *Annual improvements 2011-2013 Cycle:* these improvements are effective from 1 July 2014 and are not expected to have a material impact on the Group. They include:
  - *IFRS 3 Business Combinations:* the amendment is applied prospectively and clarifies for the scope exceptions within IFRS 3 that joint arrangements, not just joint ventures, are outside the scope of IFRS 3 and this scope exception applies only to the accounting in the financial statements of the joint arrangement itself.
  - *IFRS 13 Fair Value Measurement:* the amendment is applied prospectively and clarifies that the portfolio exception in IFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of IFRS 9 (or IAS 39, as applicable).
  - *IAS 40 Investment Property:* the description of ancillary services in IAS 40 differentiates between investment property and owner-occupied property (i.e., property, plant and equipment). The amendment is applied prospectively and clarifies that IFRS 3, and not the description of ancillary services in IAS 40, is used to determine if the transaction is the purchase of an asset or business combination.

3. Basis of preparation of the financial statements (continued)

IFRSs and IFRIC interpretations not yet effective (continued)

- *IFRS 15 Revenue from Contracts with Customers:* IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue. The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2017 with early adoption permitted. The Group is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.
- *Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests:* the amendments to IFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business must apply the relevant IFRS 3 principles for business combinations accounting. These amendments are not expected to have any impact to the Group.
- *Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation:* the amendments clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are effective prospectively for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact to the Group given that the Group has not used a revenue-based method to depreciate its non-current assets.

4.1 Basis of consolidation

Subsidiaries

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date when such control ceases. All intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to the Group. The interests of non-controlling shareholders are initially measured at the non-controlling interests’ proportionate share of the fair value of the acquiree’s identifiable net assets. Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition plus the non-controlling interests’ share of subsequent changes in equity. Total comprehensive income within a subsidiary is attributed to the non-controlling interest even if that results in a deficit balance.

Non-controlling interest is presented as an equity item, separately from the equity of the owners of the parent.

4.1 Basis of consolidation (continued)

Business combinations

The acquisition method of accounting is used to account for business combinations by the Group. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. For each business combination, the Group measures the non-controlling interest in the acquired subsidiary at the proportionate share of the acquiree’s identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses.

The excess of purchase consideration over the Group’s share of the fair value of identifiable net assets is recorded as goodwill (Note 4.6). If the cost of the acquisition is less than the Group’s share of the fair value of identifiable net assets of the subsidiary acquired the difference is recognised directly in profit or loss.

Investments in associates and joint ventures

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The results and assets and liabilities of associates and joint ventures are included in these consolidated financial statements from the date on which the investee becomes an associate or a joint venture, using the equity method of accounting. The Group discontinues the use of the equity method from the date when the investment ceases to be an associate or a joint venture. Investments in associates and joint ventures are carried in the consolidated statement of financial position at cost and adjusted for by post-acquisition changes in the Group’s share of net assets of the associate or joint venture, less any impairment in the value of individual investments. Losses of an associate or joint venture in excess of the Group’s interest in that associate or joint venture (which includes any long term interests, that in substance form part of the Group’s net investment in the associate or joint venture) are recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate or joint venture.

Any excess of the cost of acquisition over the Group’s share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of that investment. Any excess of the Group’s share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition is recognised immediately in profit or loss in the period in which the investment is acquired.

4.2 Cash and short-term deposits

Cash and short-term deposits in the consolidated statement of financial position comprise cash at banks and in hand, short-term deposits with an original maturity of three months or less and cash deposits placed to secure participation in the state open auctions with an original maturity of three months or less.

4.3 Value added tax

The Russian and Ukrainian tax legislation permits settlement of value added tax (“VAT”) on a net basis within one legal entity.

VAT is payable upon invoicing and delivery of goods, performing work or rendering services, as well as upon collection of prepayments from customers. VAT on purchases, even if they have not been settled at the reporting date, is deducted from the amount of VAT payable.

Where allowance has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

4.4 Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost is determined on a first in, first out basis. The cost of finished goods and work in progress comprises raw material, direct labour, other direct costs and related production overheads (based on normal operating capacity), but excludes borrowing costs. The cost of third parties products comprise expenditures directly attributable to purchase of these products. Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

4.5 Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Depreciation is calculated on a straight-line basis. The depreciation periods, which represent the estimated useful economic lives of the respective assets, are as follows:

	Number of years
Buildings	10 to 50
Plant and machinery	5 to 30
Equipment, motor vehicles and other	2 to 7

The asset’s residual values, useful lives and depreciation methods are reviewed, and adjusted as appropriate, at each financial year end. Land is not depreciated.

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised, and the assets replaced are derecognised. Gains and losses arising from the retirement of property, plant and equipment are included in profit or loss as incurred.

4.6 Goodwill

Goodwill on an acquisition of a subsidiary is included in intangible assets. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group’s cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes.

4.6 Goodwill (continued)

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

4.7 Intangible assets other than goodwill

Intangible assets acquired separately from business combinations are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

Intangible assets with a finite life are amortised on a straight-line basis over the useful economic lives (for trademarks useful economic life is estimated between 15 and 20 years; for patents useful economic life is estimated accordingly to period which is reflected in patent, but not more than 20 years) and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in profit or loss in the expense category consistent with the function of the intangible asset.

Development is the application of research findings or other knowledge to a plan or design for the production of a new product before commercial production or use of the product has begun. Development costs are all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Development costs are capitalised as an intangible asset if all of the following criteria are met:

(a) The technical feasibility of completing the asset so that it will be available for use or sale;

(b) The intention to complete the asset and use or sell it;

(c) The ability to use or sell the asset;

(d) The asset will generate probable future economic benefits and demonstrate the existence of a market or the usefulness of the asset if it is to be used internally;

(e) The availability of adequate technical, financial and other resources to complete the development and to use or sell it; and

(f) The ability to measure reliably the expenditure attributable to the intangible asset.

Amortisation of development costs starts upon receipt of regulatory approval when the asset becomes available for use and transferred to the designated category of intangible assets other than goodwill.

Expenditure on an intangible item that was initially recognised as an expense shall not be recognised as part of the cost of an intangible asset at a later date.

4.8 Investments and other financial assets

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. The Group does not have held-to-maturity investments and financial assets at fair value through profit or loss.

When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets on initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end. All regular way purchases and sales of financial assets are recognised on the trade date, which is the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the market place.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are carried at amortised cost using the effective interest method less any allowance for impairment. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process. Interest receivable on deposits is classified as other receivables.

Available-for-sale financial investments

Available-for-sale (“AFS”) financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any other categories. After initial measurement available-for-sale investments are measured at fair value with changes in fair value recognised in other comprehensive income. If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the profit or loss, is transferred from other comprehensive income to profit or loss. Reversals in respect of equity instruments classified as available-for-sale are not recognised in profit or loss. Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the reporting date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm’s length market transactions; reference to the current market value of another instrument which is substantially the same; discounted cash flow analysis or other valuation models.

Amortised cost

Loans and receivables are measured at amortised cost. This is computed using the effective interest method less any allowance for impairment. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

4.8 Investments and other financial assets (continued)

Impairment of financial assets

The Group assesses at each reporting date whether a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset’s original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss shall be recognised in profit or loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date. Any subsequent reversal of an impairment loss is recognised in profit or loss.

Available-for-sale financial investments

For AFS financial assets, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired. In the case of equity investments classified as AFS, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. ‘Significant’ is evaluated against the original cost of the investment and ‘prolonged’ against the period in which the fair value has been below its original cost. When there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of profit or loss – is removed from OCI and recognised in the statement of profit or loss. Impairment losses on equity investments are not reversed through profit or loss; increases in their fair value after impairment are recognised in OCI.

The determination of what is ‘significant’ or ‘prolonged’ requires judgement. In making this judgement, the Group evaluates, among other factors, the duration or extent to which the fair value of an investment is less than its cost.

4.9 Borrowings

Borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortised cost using the effective interest method.

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the asset. All other borrowing costs are expensed.

4.10 Income taxes

Income tax expense comprises current and deferred tax. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

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

Deferred tax assets and deferred tax liabilities can be offset only if: (a) a Group entity has a legally enforceable right to set off current tax assets against current tax liabilities; and (b) the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority on either: (i) the same taxable entity; or (ii) different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

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

In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The effect from a change in tax rates is recognised in profit or loss except to the extent that it relates to items previously charged or credited to other comprehensive income.

4.11 Leases

Operating lease payments are recognised as an expense in profit or loss on a straight line basis over the lease term.

4.12 Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when the rights to receive cash flows from the asset have expired.

4.12 Derecognition of financial assets and liabilities (continued)

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

4.13 Provisions

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

Expense relating to any provision is presented in profit or loss. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects where appropriate the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

4.14 Equity

Share capital

Ordinary shares are classified as equity.

Dividends

Dividends declared by the Group are recognised as a liability and deducted from equity at the reporting date only if they are declared before or on the reporting date. Such dividends are disclosed when they are proposed before the reporting date or proposed or declared after the reporting date but before the consolidated financial statements are authorised for issue.

Treasury shares

Own equity instruments that are reacquired are recognised at cost and deducted from equity. No gain or loss is recognised in the consolidated statement of comprehensive income on the purchase, sale, issue or cancellation of the Group’s own equity instruments. Any difference between the face value of shares and the consideration paid for treasury shares is recognised in retained earnings.

4.15 Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable excluding discounts and rebates, taking into account contractually defined terms of payment and excluding taxes or duty.

4.16 Employee benefits

In 2014, under provision of the Russian legislation, social contributions are made through a social tax ("ST") allocated to state pension and social insurance funds calculated by the Group by the application of a ST regressive rate from 30% applicable only to the gross remuneration of individual employee not more than RR 624 p.a. to 10%. The Group's contributions relating to ST are expensed in the year to which they relate.

Total contributions for ST amounted to RR 869,928 during the year ended 31 December 2014 (2013: RR 887,978) and they were classified as labour costs in these consolidated financial statements.

In 2015, the threshold for application of 30% ST rate for individual employee was raised to RR 670 p.a. for social insurance fund and RR 711 p.a. for state pension fund.

4.17 Foreign currency transactions

The consolidated financial statements are presented in Russian Roubles, which is the functional currency of the Company and its Russian subsidiaries. Transactions in foreign currencies are initially recorded in the functional currency at the exchange rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. All resulting differences are taken to profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

At 31 December 2014, the exchange rates used for translation foreign currency balances were US$ 1 = 56.26 roubles; Euro 1 = 68.34 roubles; 1 Ukrainian Hryvnia = 3.56 roubles (2013: US$ 1 = 32.73 roubles; Euro 1 = 44.97 roubles; 1 Ukrainian Hryvnia = 3.97 roubles).

The functional currency of the Ukrainian subsidiary is the Ukrainian Hryvnia. The functional currencies of the other foreign operations are the United States dollar (US$) and the Euro. As at the reporting date, the assets and liabilities of those subsidiaries having functional currency different from the Russian Rouble are translated into the presentation currency of the Group (the Russian Rouble) at the rate of exchange ruling at the reporting date and its statement of comprehensive income and cash flow statement are translated at the exchange rate prevailing at the date of transaction. The exchange differences arising on the translation are taken to a separate component of equity through other comprehensive income.

4.18 Impairment of non-financial assets

At each reporting date the Group assesses whether there is any indication that an asset or cash generating unit (CGU) may be impaired. The assets or CGUs subject to such assessment are primarily property, plant and equipment and trade marks. If any such indication exists, the Group makes an estimate of the asset's or CGU's recoverable amount. An asset's or CGU's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset or CGU is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the assets or CGUs.

4.19 Government grants

Government grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed. When the grant relates to an asset, it is recognised as income in accordance with amortisation of the related asset.

4.20 Share-based payments

For equity-settled share-based payment transactions, the Group measures the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the Group cannot estimate reliably the fair value of the goods or services received, the Group measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

5. Significant accounting judgements and estimates

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of non-financial assets, except for goodwill

The determination of impairments involves the use of estimates that include, but are not limited to, the cause, timing and amount of the cash flow. The determination of the recoverable amount of an asset or cash-generating unit involves the use of estimates by management. Methods used to determine the value in use include discounted cash flow-based methods, which require the Group to make an estimate of the expected future cash flows from the asset or cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. These estimates, including the methodologies used, may have a material impact on the fair value and ultimately the amount of any asset impairment.

The following factors are considered in assessing impairment of major specific assets of the Group:

- *Property, plant and equipment:* changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists.
- *Trade marks, patents and licenses:* changes in current competitive conditions, changes in the regulations, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, introduction of alternative products on the market and other changes in circumstances that indicate impairment exists.

5. Significant accounting judgements and estimates (continued)

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2014 is RR 1,730,040 (2013: RR 1,769,556). More details are provided in Note 14.

Allowance for doubtful accounts receivable

The Group maintains an allowance for doubtful accounts receivable to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful accounts receivable, management bases its estimates on the aging of accounts receivable balances and historical write-off experience, customer credit worthiness and changes in customer payment terms. If the financial conditions of customers were to deteriorate, actual write-offs might be higher than expected. As at 31 December 2014, allowances for doubtful accounts receivable amounted to RR 225,186 (2013: RR 244,764). More details are provided in Note 16.

Write-down of inventories to net realisable value

The Group determines the adjustment for write-down of inventories to net realisable value based on their expected future use and realisable value. The net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of sale or distribution. Selling prices and costs to sale are subject to change as new information becomes available. Revisions to the estimates may significantly affect future operating results.

Current taxes

Russian and Ukrainian tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group’s entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Group’s entities may be assessed additional taxes, penalties and interest, which can be significant. In Russia and Ukraine the periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As of 31 December 2014 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group’s tax, currency and customs positions will be sustained. More details are provided in Note 32.

Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

6. Spin-off of Branded OTC business

In July-September 2013, the Board of Directors and the shareholders of the Company approved a plan of spin-off of the Group’s Branded OTC business into a newly founded separate legal entity “OTCpharm” OJSC (“OTCpharm”) with the purpose to increase the combined value of the Group and OTCpharm.

On 23 December 2013 OTCpharm was registered; its shares were proportionally distributed among the shareholders of the Company and the Group distributed to OTCpharm the assets related to Branded OTC business and also recognised liability on cash distribution to OTCpharm in the amount of RR 3,500,650. Total effect from disposal of assets and liabilities due to spin-off directly recognised in equity of the Group was as follows:

	Effect on equity (increase/ (decrease))
Intangible assets	(19,398,032)
Receivables and other current assets	19,917
Total assets	**(19,378,115)**
Deferred tax liability	492,449
Trade and other payables and advanced received	(745,122)
Income tax and other taxes	126,047
Liability on cash distribution*	(3,500,650)
Total liabilities	**(3,627,276)**
Net effect on equity	**(23,005,391)**

* In January 2014, this liability was settled in full.

The purpose of the cash distribution was to provide OTCpharm with initial working capital to launch its independent operations. Further the cash distributed was ultimately used by OTCpharm to pay primarily for the Group supplies of the respective active pharmaceutical ingredients and finished goods (Note 12).

Although the trade marks were transferred out to OTCpharm the Group continued to use them until its re-registration to OTCpharm in accordance with the regulation. On 1 April 2014, the Group sold to OTCpharm all finished goods under OTCpharm trade marks and the respective active pharmaceutical ingredients (“APIs”) balance (Note 12). Since 1 April 2014 OTCpharm started its operations independently from the Group and personnel of the Company involved in operation of branded OTC business was transferred to OTCpharm.

7. Acquisition of Bever

In August 2013, the Group acquired 100% of share capital of “Bever Pharmaceutical Pte Ltd” (“Bever”) controlled by Alexander Shuster, one of the Company’s Directors. Bever is a single asset entity that holds a 20 year-length contract that provides exclusive purchase rights for unique raw materials – APIs used for manufacturing of the Group’s leading OTC products Arbidol and Afobazol and also sale of these APIs in Russia and CIS. This acquisition was related to the plan of spin-off of Branded OTC business.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

7. Acquisition of Bever (continued)

The Group accounted for acquisition of Bever as acquisition of intangible asset (i.e. the exclusive favorable purchase contract). Considering that this acquisition was partly settled in the parent company’s shares it was accounted for an equity-settled share-based payment transaction. Intangible asset was measured at recognition at its fair value of RR 13,936,025 with the corresponding increase in equity of RR 12,353,287 related to consideration paid in shares (the remaining amount of RR 1,582,738 was paid in cash).

On 23 December 2013, Bever was transferred to OTCpharm as a result of spin-off of the OTC-branded business (see Note 6).

8. Investments in joint ventures

8.1 Investments in joint venture Medtekhnika

On 1 January 2013, the Company and the other participant, “DGM Trading Limited” signed an amendment to the shareholders’ agreement whereupon the Group obtained control over a “Moldildo Trading Limited” – holder of 100% interest in “Pharmstandard-Medtechnika”. In accordance with the terms of this new agreement operational decisions are taken by simple majority. In particular, the Group received a pre-emptive right to approve key management personnel of “Pharmstandard-Medtechnika” and to control operating activity of this entity. Consequently, since 1 January 2013 the Group recognised “Pharmstandard-Medtechnika” as a subsidiary and accounted for it in accordance with the requirements of IFRS 10.

8.2 Investments in joint venture NTS+

Main purpose of "NTS+" is to participate in building of a research and development center in the Vladimir region of the Russian Federation specialised in bioengineering medical products and universal diagnostic researches.

Summarised financial information of this joint venture, based on its IFRS financial statements, and reconciliation with the carrying amount of the investment in consolidated financial statements are set out below:

	2014	2013
Current assets including cash and cash equivalents RR 39,205 (2013: RR 3,539)	83,299	55,544
Property, plant and equipment and other non-current assets	1,371,115	1,224,080
Current liabilities	(193,173)	(108,739)
Long-term loans and other non-current liabilities	(329,368)	(331,920)
Equity	**931,873**	**838,965**
Proportion of the Group’s ownership	37.5%	37.5%
Carrying amount of the investment	**349,452**	**314,612**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

8. Investments in joint venture (continued)

8.2 Investments in joint venture NTS+ (continued)

Summarised statement of profit or loss of “NTS+” is detailed below:

	2014	2013
General and administrative expenses	(123,600)	(128,341)
Financial expenses, net	(30,064)	(31,651)
Other income, including income from non-core operations and rent RR 128,667 (2013: RR 92,875)	262,512	102,995
Other expenses	(70,648)	(45,771)
Profit/(loss) before income tax	**38,200**	**(102,768)**
Income tax benefit/(expense)	54,707	(49,877)
Profit/(loss) and total comprehensive income for the year	**92,907**	**(152,645)**
Group’s share of profit/(loss) and total comprehensive income for the year	**34,840**	**(57,242)**

The Group has no any commitments in respect of the joint venture.

9. Investments in associates

9.1 Investments in “Argos Therapeutics, Inc”

In 2013, Pharmstandard International S.A. invested US$ 36.8 million (RR 1,206,457) to purchase about 35% of voting preferred shares of Argos Therapeutics, Inc. (“Argos”) incorporated in the USA, Delaware. Further in February 2014, Pharmstandard International S.A. additionally invested US$ 10.2 million (RR 354,233). In February 2014, Argos converted voting preferred shares to voting ordinary shares and issued certain additional number of voting ordinary shares. As a result of these transactions the Group’s interest in Argos was diluted to 30.4%. Dilution was accounted for as deemed disposal which resulted in additional loss on deemed disposal in the amount of RR 1,669 including RR 9,382 accumulated foreign exchange gains reclassified to profit for the year. On 7 February 2014 Argos became listed on NASDAQ.

Argos is a biopharmaceutical company focused on the development and commercialisation of fully personalised immunotherapies for the treatment of cancer and infectious diseases based on its Arcelis™ technology platform. In accordance with the purchase agreement the Company received the right to appoint two members of the Board of Directors therefore the Company received a significant influence over Argos and recognised it as an associate applying the equity method for its accounting.

Summarised financial information of this associate, based on its financial statements is set out below:

	2014	2013
Cash and cash equivalents	2,094,140	1,089,816
Other current assets	1,141,691	531,217
Property, plant and equipment and other non-current assets	385,346	52,454
Current liabilities	(185,470)	(103,533)
Non-current liabilities	(1,671,905)	(329,914)
Equity	**1,763,802**	**1,240,040**
Proportion of the Group’s ownership	30.4%	35%
Carrying value of net assets	**536,196**	**434,014**
Goodwill arising of acquisition of associate	1,093,699	729,935
Carrying amount of investments	**1,629,895**	**1,163,949**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

9. Investments in associates (continued)

9.1 Investments in “Argos Therapeutics, Inc” (continued)

Summarised statement of comprehensive income of Argos is detailed below:

	2014	2013
Revenue	75,814	10,322
Research and development expenses	(1,747,436)	(101,948)
General and administrative expenses	(330,268)	(23,364)
Other expenses	(84,301)	(684)
Loss and total comprehensive income for the period	**(2,086,191)**	**(115,674)**
Group’s share of loss for the year (35% before 7 February 2014 and 30.4% after 7 February 2014)	**(634,202)**	**(40,486)**

Foreign exchange differences related to the associate recognised in other comprehensive income amounted of RR 747,584 (2013: 0).

9.2 Investments in “Biocad Holding Limited”

On 30 April 2014, the Company signed contract with shareholders of “Biocad Holdings Limited” (“Biocad”), a company registered under the law of Cyprus with the purpose of acquiring 20% of the outstanding Biocad shares for the total cash consideration of US$ 100 million (RR 3,503,870).

Biocad is the controlling shareholder in several companies involved in the research and development, production and distributing of various pharmaceutical and biopharmaceutical products, primarily in Russian Federation. These major subsidiaries are Russian legal entities: “Biocad” CJSC, “Biocad Pharm” LLC, “I-Mab” LLC. Biocad has also several insignificant subsidiaries registered under the law of other countries.

On 27 July 2014, the Company finalised the acquisition. In accordance with the shareholder’s agreement the Company obtained significant influence over strategic and operating policies of the Biocad and recognised it as associate applying the equity method of accounting.

Summarised financial information of Biocad, based on its consolidated financial statements is set out below:

	31 December 2014	Fair value on the date of acquisition 27 July 2014
Cash and cash equivalents	6,806,030	52,243
Other current assets	2,199,192	2,113,041
Property, plant and equipment	1,041,489	1,024,130
Intangible assets	4,116,858	3,992,676
Trade and other payables	(2,913,790)	(324,628)
Other current liabilities	(349,693)	(93,441)
Non-current liabilities	(722,149)	(766,551)
Equity	**10,177,937**	**5,997,470**
Proportion of the Group’s ownership	20%	20%
Carrying value of net assets	**2,035,587**	**1,199,494**
Goodwill arising on acquisition of associate	2,304,376	2,304,376
Carrying amount of investments	**4,339,963**	**3,503,870**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

9. Investments in associates (continued)

9.2 Investments in "Biocad Holding Limited" (continued)

Summarised consolidated statement of profit or loss of Biocad since the date of recognition of associate 27 July to 31 December 2014 is detailed below:

Revenue	7,303,972
Cost of sales	(1,074,982)
Research expenses	(149,446)
General and administrative expenses	(1,204,130)
Other income and expenses	263,989
Income tax expenses	(958,936)
Profit for the period	**4,180,467**
Group's share of profit for the period	**836,093**

10. Acquisition of non-controlling interests

In August 2013, the Company acquired about 11% of non-controlling interests in Donelle Company Limited ("Donelle"). Total consideration paid in cash for the acquired non-controlling interests was RR 235,112. On December 2013, Donelle was transferred to OTCpharm as a result of spin-off of the OTC-branded business (see Note 6).

In May 2013, the Company acquired a 41.93% interest in "Pharmstandard-Biolik" PJSC resulting in an increase in the Company's interests to 96.93%. Total consideration paid in cash for the acquired non-controlling interests was RR 125,253.

11. Segment information

For the management purposes, the Group is organised into two reportable operating segments: (1) production and wholesale of pharmaceutical products and (2) production and wholesale of medical equipment.

No operating segments have been aggregated to form the above reportable operating segments.

Management monitors the segments' assets, liabilities, sales, gross profit, segments' results and budgets of these business segments separately for the purpose of making decisions about resource allocation and performance assessment. For the management purposes, budgets of income and expense are planned and analysed for each of operating segments separately.

Segment result is segment revenue less segment expenses. Segment expenses consist of cost of sales, selling and distribution costs, general and administrative expenses, other income and expenses that can be directly attributed to the segment on a reasonable basis.

Segment assets consist primarily of property, plant and equipment, intangible assets including goodwill allocated to specified segment, inventories, financial assets, receivables and operating cash. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate liabilities. Capital expenditure comprises additions to property, plant and equipment.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

11. Segment information (continued)

There were no significant intercompany transactions between these operating segments.

The following tables present revenue and profit information regarding the Group’s operating segments:

Year ended 31 December 2014	Production and wholesale of pharmaceutical products (“Pharmaceutical products”)	Production and wholesale of medical equipment	Group
Sales to external customers	40,103,232	1,120,203	41,223,435
Total revenue	**40,103,232**	**1,120,203**	**41,223,435**
Gross profit	17,798,480	417,915	18,216,395
Segment result	**13,699,491**	**(6,530)**	**13,692,961**
Financial income, net			(108,293)
Share in profit of joint venture and associates, net			235,062
Profit before income tax			**13,819,730**
Income tax expense			(2,724,267)
Profit for the year			**11,095,463**
Segment assets	60,689,995	1,650,148	62,340,143
Unallocated assets			480,330
Total assets			**62,820,473**
Segment liabilities	16,293,365	289,082	16,582,447
Unallocated liabilities			5,417,686
Total liabilities			**22,000,133**
Acquisition of property, plant and equipment (Note 13)	2,382,508	8,880	2,391,388
Depreciation and amortisation (Notes 13 and 14)	907,267	37,403	944,670
Property, plant and equipment impairment (charge)/reversal (Note 13)	(63,841)	10,591	(53,250)

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

11. Segment information (continued)

As at 31 December 2014 the net unallocated liabilities of RR 4,937,356 consist of loans and borrowings of RR 4,002,941, income tax payable of RR 807,972 and net deferred tax liability of RR 126,443.

Year ended 31 December 2013	**Production and wholesale of pharmaceutical products ("Pharmaceutical products")**	**Production and wholesale of medical equipment**	**Group**
Sales to external customers	56,007,903	1,048,278	57,056,181
Total revenue	**56,007,903**	**1,048,278**	**57,056,181**
Gross profit	24,129,245	342,308	24,471,553
Segment result	**15,770,067**	**26,749**	**15,796,816**
Financial income, net			163,442
Share in loss of joint venture and associate, net			(97,728)
Profit before income tax			**15,862,530**
Income tax expense			(3,942,091)
Profit for the year			**11,920,439**
Segment assets	61,141,673	1,465,632	62,607,305
Unallocated assets			258,050
Total assets			**62,865,355**
Segment liabilities	25,875,572	115,197	25,990,769
Unallocated liabilities			7,800,293
Total liabilities			**33,791,062**
Acquisition of property, plant and equipment (Note 13)	1,427,978	65,805	1,493,783
Depreciation and amortisation (Notes 13 and 14)	915,753	38,083	953,836
Property, plant and equipment impairment (charge)/reversal (Note 13)	(1,488)	1,031	(457)
Impairment of intangible assets (Note 30)	100,000	–	100,000

As at 31 December 2013 the net unallocated liabilities of RR 7,542,243 consist of loans and borrowings of RR 7,024,080, income tax payable of RR 332,068 and net deferred tax liability of RR 186,195.

Major assets of the Group are placed in Russian Federation and major revenue is generated from the operation in Russian Federation.

Revenues from certain customers in the Pharmaceutical products segment individually approximated or exceeded 10% of total Group's segment revenue.

The table below shows the revenue from these customers:

Customer	**2014**	**2013**
The Ministry of Health of Russian Federation and its regional branches (federal state open auctions only)	5,313,862	13,214,240
Customer 1	3,661,399	5,862,567
Customer 2*	2,639,325	5,541,438
Customer 3	2,320,332	5,121,244

* In 2014, more than 93% of total revenue from this customer was attributed to medicine Velcade®.

The Group's sales to the Ministry of Health of Russian Federation and its regional branches represent about 13% of the total Group's revenue in 2014 (2013: 23%).

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

12. Balances and transactions with related parties

Related parties may enter into transactions which unrelated parties might not enter, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the related party relationships for those related parties with whom the Group entered into transactions in 2014 and 2013 or had balances outstanding at 31 December 2014 and 2013 are detailed below.

Balances with related parties

2014	Short-term financial assets – (a), Note 18	Long-term financial assets – (b), Note 19	Cash and short-term deposits placed in related bank – Note 17	Trade and other receivables and prepayments – (c) Note 16	Trade and other payables – (d) Note 22
Parent	4,050,605	–	–	152,904	–
Other related parties[1]	172,000	42,900	6,455,195	5,939,141	2,509,714
Joint venture	37,000	–	–	79,540	–
Total	**4,259,605**	**42,900**	**6,455,195**	**6,171,585**	**2,509,714**

2013	Short-term financial assets – (a), Note 18	Long-term financial assets – (a), Note 19	Cash and short term deposits placed in related bank – Note 17	Trade and other receivables and prepayments – (c) Note 16	Trade and other payables – (d) Note 22
Parent	752,772	–	–	–	–
Other related parties	227,530	72,000	10,050,603	100,082	6,948,528
Total	**980,302**	**72,000**	**10,050,603**	**100,082**	**6,948,528**

(a) This item is detailed in sub-sections "Loans provided to parent" and "Loans provided to other related parties" below.

(b) This item is primarily comprised of long-term deposits placed in related bank with maturity in 2016 and interest rate of 6.5%-8% p.a.

(c) This item is primarily comprised of receivables from OTCpharm for sale of raw materials and finished goods as a part of spin off (Note 6), interest receivable from Augment, agency fee receivables from sale of certain related party products and prepayments for rent and other services.

(d) This item primarily comprised of (i) payables to OTCpharm for sales of OTC branded products under agency agreement in the amount of RR 646,502 and (ii) payables to Bever for purchase of API in the amount of RR 1,182,822 (Note 7); (iii) payables to other related party for purchase of Koagil VII in the amount of RR 453,640.

[1] Other related parties, represent entities under control of the Company's parent and key management.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

12. Balances and transactions with related parties (continued)

Significant transactions with related parties

Statement of comprehensive income caption	Relationship	2014	2013
Agency fee income (included in revenue) (A)	Other related parties	888,638	27,122
Contractual manufacturing income from OTCpharm (included in revenue) (B)	Other related parties	1,373,268	–
Revenue from sale of active pharmaceutical ingredients to OTCpahrm (included in revenue) (C)	Other related parties	1,586,941	–
Revenue from sale of finished goods to OTCpharm (included in revenue) (C)	Other related parties	2,355,984	–
Revenue from sale of third-parties products (included in revenue)	Associate	620,020	–
Revenue from sale of third-parties products to OTCpharm (included in revenue) (C)	Other related parties	55,076	–
Interest income from deposits placed in a related bank	Other related parties	19,225	18,335
Interest income from loans provided to parent and other related parties	Parent and other related parties	110,766	38,511
License fee (included in distribution costs) (D)	Other related parties	(123,783)	(3,515)
Warehouse rental expenses (included in distribution costs)	Other related parties	(127,670)	(113,171)
Office rental expenses (included in general and administrative expenses)	Other related parties	(69,419)	(64,606)
Cost of sales (E)	Other related parties	(2,608,314)	(3,083,333)
Consulting on venture investments (included in general and administrative expenses) (F)	Other related parties	(106,099)	–
Other income (G)	Other related parties	274,859	12,301
Other income	Joint venture	70,159	–
Research and development expenditure	Other related parties	(31,454)	–
Cession of rights for loan issued by third party (H)	Other related parties	727,882	–
Purchase of promissory notes from related bank (I)	Other related parties	3,420,978	–

(A) Agency fee income

The Company holds agency contracts with related parties for distribution and sales of certain products owned by those related parties (see Note 25).

(B) Contractual manufacturing income

The Group holds contractual manufacturing contracts for production of OTC branded medicines with OTCpharm (Note 25).

(C) Revenue from sales to OTCpharm

The Group sold to OTCpharm inventory related to OTC business to enable to launch independent operations of OTCpharm since 1 April 2014 (Notes 6 and 25).

Also since 1 April 2014, the Group is supplying certain API to OTCpharm under regular sales contracts (Note 25).

(D) License fee

The Group paid license fee to OTCpharm for usage of trade marks before 1 April 2014 (Note 6).

12. Balances and transactions with related parties (continued)

Significant transactions with related parties (continued)

(E) Cost of sales

The Group holds a purchase contracts for supply of third-party products, primarily Koagil VII, manufactured by a related party. The total cost of RR 2,608,314 (2013: RR 3,083,333) includes the cost of this product in the amount of RR 1,776,376 (2013: RR 2,814,606) sold by the Group primarily through open state auctions. The remaining amount included in cost of sales primarily represents cost of raw materials and third-parties products purchased from other related parties.

(F) Consulting on venture investments

This item primarily represents consulting expenses incurred to related party in connection with identification, analysis and monitoring of R&D start up companies – potential targets of investment by Pharmstandard International S.A.

(G) Other income

Other income primarily includes income from operating lease of cars and warehouses to OTCpharm, income from royalty, utilities, sale of materials and other income from transactions with other related parties (Note 29).

(H) Cession of rights for loan issued by third party

On 24 December 2014, the Company signed with a related party cession agreement. Based on this agreement the Company paid to the related party RR 727,882 and received legal right of claim from a third party of short-term loan of US$ 12,500 thousand (RR 689,165) bearing interest rate of 6.5% p.a. (Note 18) and interest receivable of RR 61,255.

(I) Purchase of promissory notes

In 2014, the Company purchased from the related bank promissory notes of RR 3,420,978 at their pair value. Further the Company sold those promissory notes to a third party for cash consideration of RR 3,501,090 and recognised income from this transaction in the amount of RR 80,112 (Note 29).

Loans provided to parent

In 2013 and 2014, the Company’s parent “Augment Investments Limited” (“Augment”), a company registered under the laws of Cyprus (see Note 24), applied to the Company with request to provide short-term interest loans for the purpose of financing the current business activity of Augment not related to the Group.

In October 2013, the Group provided unsecured US$ denominated short-term loan to Augment of US$ 60,000 thousand (RR 1,935,978 at the exchange rate as of date of issue of loan) with maturity date of 14 October 2014 and fixed interest rate of 5.25%. In November and December 2013, Augment partly repaid this loan in the amount of US$ 37,000 thousand (RR 1,209,971). Outstanding of principal amount of loan payable as at 31 December 2014 is US$ 23,000 thousand (RR 1,293,943). In October 2014, the Company signed an additional agreement to extend the maturity date to 12 October 2015.

12. Balances and transactions with related parties (continued)

Loans provided to parent (continued)

During 2014, the Group provided additional unsecured US$ denominated short-term loans to Augment with maturity in 2015 in the total amount of US$ 64,000 thousand (RR 2,560,159) with fixed interest rate from 2.75% to 5.25% p.a. During 2014, Augment partly repaid those loans in the amount of US$ 15,000 thousand (RR 784,305). Outstanding of principal amount of loans payables as at 31 December 2014 is US$ 49,000 thousand (RR 2,756,662).

Loans provided to other related parties

In December 2012, the Company provided an unsecured short-term loan to other related party of RR 72,000 with maturity date of 27 December 2013 and fixed interest rate of 12% p.a. This loan provided for the purpose of financing the current business activity of that related party.
In December 2013, the Company signed an additional agreement to extend the maturity date to 19 October 2015 (Note 18).

In August 2014, the Company provided an unsecured short-term loan to other related party of RR 75,000 with maturity date of 31 December 2015 and fixed interest rate of 12% p.a. (Note 18). The amount of RR 38,000 of this loan was repaid in 2014.

In October 2014, the Company provided an unsecured short-term loan to other related party of RR 700,000 with maturity date of 31 December 2015 and fixed interest rate of 10% p.a. (Note 18). Of this loan the amount of RR 600,000 was repaid in 2014.

Compensation to key management personnel

Total compensation to key management personnel, amounted to RR 55,599 for the year ended 31 December 2014 (2013: RR 54,753). Such compensation represents the payroll and bonuses included in general and administrative expenses.

Transactions with key management

In August 2013, the Group acquired 100% share capital of Bever controlled by Alexander Shuster, one of the Company’s Directors (Note 7). In August 2013, the Group also acquired from Alexander Shuster 5.465% of non-controlling interest in Donelle for the total agreed consideration of RR 117,556 settled in cash (Note 10).

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

13. Property, plant and equipment

Property, plant and equipment consist of the following:

31 December 2014	Land	Buildings	Plant and machinery	Equipment, motor vehicles and other	Assets under construction	Total
Cost						
Balance at 1January 2014	**442,564**	**4,804,039**	**4,562,537**	**811,079**	**1,553,569**	**12,173,788**
Additions	–	3,508	43,964	187,619	2,156,297	**2,391,388**
Transfers	–	234,246	1,389,863	13,267	(1,637,376)	**–**
Disposals	–	(1,322)	(38,204)	(89,658)	(47,279)	**(176,463)**
Foreign exchange differences	–	(15,391)	(19,033)	(1,473)	(12,238)	**(48,135)**
Balance at 31 December 2014	**442,564**	**5,025,080**	**5,939,127**	**920,834**	**2,012,973**	**14,340,578**
Accumulated depreciation and impairment						
Balance at 1 January 2014	**–**	**664,019**	**2,707,851**	**359,364**	**39,316**	**3,770,550**
Depreciation charge	–	152,441	521,803	136,330	–	**810,574**
Disposals	–	(763)	(21,565)	(78,069)	(1,720)	**(102,117)**
Impairment charge/(reversal)	–	(6,724)	(3,945)	–	63,919	**53,250**
Foreign exchange differences	–	(1,837)	(4,594)	(574)	(2,005)	**(9,010)**
Balance at 31 December 2014	**–**	**807,136**	**3,199,550**	**417,051**	**99,510**	**4,523,247**
Net book value						
Balance at 1 January 2014	**442,564**	**4,140,020**	**1,854,686**	**451,715**	**1,514,253**	**8,403,238**
Balance at 31 December 2014	**442,564**	**4,217,944**	**2,739,577**	**503,783**	**1,913,463**	**9,817,331**

31 December 2013	Land	Buildings	Plant and machinery	Equipment, motor vehicles and other	Assets under construction	Total
Cost						
Balance at 1 January 2013	**442,564**	**4,166,479**	**4,014,742**	**597,494**	**1,547,101**	**10,768,380**
Additions	–	6,194	66,712	252,121	1,168,756	**1,493,783**
Transfers	–	623,902	479,970	45,149	(1,149,021)	**–**
Disposals	–	(774)	(16,870)	(87,662)	(9,193)	**(114,499)**
Acquisition through business combination	–	–	9,015	3,221	–	**12,236**
Foreign exchange differences	–	8,238	8,968	756	(4,074)	**13,888**
Balance at 31 December 2013	**442,564**	**4,804,039**	**4,562,537**	**811,079**	**1,553,569**	**12,173,788**
Accumulated depreciation and impairment						
Balance at 1 January 2013	**–**	**529,315**	**2,256,690**	**330,725**	**36,943**	**3,153,673**
Depreciation charge	–	134,015	458,179	113,297	–	**705,491**
Disposals	–	(264)	(8,959)	(84,967)	–	**(94,190)**
Impairment charge/(reversal)	–	–	796	–	(339)	**457**
Foreign exchange differences	–	953	1,145	309	2,712	**5,119**
Balance at 31 December 2013	**–**	**664,019**	**2,707,851**	**359,364**	**39,316**	**3,770,550**
Net book value						
Balance at 1 January 2013	**442,564**	**3,637,164**	**1,758,052**	**266,769**	**1,510,158**	**7,614,707**
Balance at 31 December 2013	**442,564**	**4,140,020**	**1,854,686**	**451,715**	**1,514,253**	**8,403,238**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

13. Property, plant and equipment (continued)

In 2014 and 2013, the Group did not borrow money for capital construction and there were no new qualifying assets, therefore no borrowing costs were capitalised.

The Group assets include only an insignificant portion of land on which the Group's factories and buildings, comprising the Group's principal manufacturing facilities, are located, whilst the major portion of the land is held under operating lease agreements with the state municipal bodies. The lease agreements specify lease terms between 1 and 20 years. Long-term agreements have an option to prolong the lease term for another 10 years and include a purchase option after termination of the lease. Purchase price will be determined based on fair value of the land as determined by the municipal authorities. The total amount of rental payments for the use of the land during 2014 was RR 32,105 (2013: RR 25,090). Such payments are reassessed by the state authorities on an annual basis. No such reassessment has been completed for 2015 and beyond as of the date of approval of these consolidated financial statements for issue.

In 2014, the Group signed with OTCpharm operating lease agreements. In accordance with agreements the Group leased out to OTCpharm cars and warehouses with net book value at 31 December 2014 RR 144,669. Income from operating lease in the amount of RR 77,161 is recognised as other income (Note 12 and Note 29).

14. Intangible assets

31 December 2014	**Goodwill**	**Trademarks, patents and licenses**	**Development costs**	**Total**
Cost				
Balance at 1 January 2014	**1,769,556**	**1,286,573**	**279,100**	**3,335,229**
Additions	–	48,065	45,627	**93,692**
Transfers	–	143,845	(143,845)	**–**
Foreign exchange differences	(39,516)	–	–	**(39,516)**
Balance at 31 December 2014	**1,730,040**	**1,478,483**	**180,882**	**3,389,405**
Accumulated amortisation and impairment				
Balance at 1 January 2014	**–**	**132,712**	**–**	**132,712**
Amortisation expense	–	134,096	–	**134,096**
Balance at 31 December 2014	**–**	**266,808**	**–**	**266,808**
Net book value				
Balance at 1 January 2014	**1,769,556**	**1,153,861**	**279,100**	**3,202,517**
Balance at 31 December 2014	**1,730,040**	**1,211,675**	**180,882**	**3,122,597**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

14. Intangible assets (continued)

31 December 2013	**Goodwill**	**Trademarks, patents and licenses**	**Development costs**	**Total**
Cost				
Balance at 1 January 2013	**2,584,302**	**7,186,198**	**180,360**	**9,950,860**
Additions (a)	–	14,786,962	98,740	**14,885,702**
Reclassification to assets held for distribution (Note 6)	(835,000)	(20,686,587)	–	**(21,521,587)**
Foreign exchange differences	20,254	–	–	**20,254**
Balance at 31 December 2013	**1,769,556**	**1,286,573**	**279,100**	**3,335,229**
Accumulated amortisation and impairment				
Balance at 1 January 2013	**–**	**1,907,922**	**–**	**1,907,922**
Amortisation expense	–	248,345	–	**248,345**
Reclassification to assets held for distribution (Note 6)	–	(2,023,555)	–	**(2,023,555)**
Balance at 31 December 2013	**–**	**132,712**	**–**	**132,712**
Net book value				
Balance at 1 January 2013	**2,584,302**	**5,278,276**	**180,360**	**8,042,938**
Balance at 31 December 2013	**1,769,556**	**1,153,861**	**279,100**	**3,202,517**

(a) In 2013 the Group acquired (i) Bever which is a holder of exclusive contracts of RR 13,936,025 (Note 7) and (ii) exclusive license on manufacturing patent and distribution of product named of Sirturo® of RR 850,937.

Carrying amount and remaining amortisation period of major trademarks and patents as of 31 December are as follows:

	Carrying amount		**Remaining amortisation period (years)**	
Name	**2014**	**2013**	**2014**	**2013**
Sirturo®	767,763	844,539	9	10
Epostim®	143,519	162,655	8	9
Pegaltevir ®	134,256	–	5	–

Impairment testing of goodwill

Goodwill acquired through business combinations has been allocated for impairment testing purposes to the following groups of cash-generating units, which are also reportable segments of the Group:

- production and wholesale of pharmaceutical products group of units (“Pharmaceuticals”); and
- production and wholesale of medical equipment group of units (“Equipment”).

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

14. Intangible assets (continued)

Impairment testing of goodwill (continued)

Carrying amount of goodwill allocated to each group of cash generating units:

	Pharmaceuticals		**Equipment**		**Total**	
	2014	**2013**	**2014**	**2013**	**2014**	**2013**
Carrying amount of goodwill	1,511,186	1,550,702	218,854	218,854	**1,730,040**	**1,769,556**

The recoverable amount of the cash-generating units has been determined based on a value in use calculation using cash flow projections developed on the basis of financial budgets approved by management covering a five-year period and cash flows beyond the five-year period are extrapolated using a 5% growth rate that is the same as the mid-term average growth rate for pharmaceuticals and medical equipment market (2013: 5%). The discount rate applied to cash flow projections is 18% (2013: 14.8%).

Key assumption used in value in use calculations

The calculation of value in use for both Pharmaceuticals and Equipment groups of cash-generating units are most sensitive to the following assumptions:

- Discount rates;
- Raw material price inflation;
- Currency rates changes;
- Growth rate used to extrapolate cash flows beyond the budget period.

Discount rates – Discount rates reflect management's estimate of the risks specific to each unit. This is the benchmark used by management to assess operating performance and to evaluate future investment proposals. In determining appropriate discount rates for each group of units, regard has been given to the Capital Assets Pricing Model calculation at the reporting date.

Raw material price inflation – past actual raw materials price movements, including the effect of the devaluation of the Russian Rouble for US dollar denominated raw materials, have been used as an indicator of future price movements.

Currency exchange rates changes – estimated based on current trends on the foreign currency market.

Growth rate estimates – rates are based on published industry research.

Sensitivity to changes in assumptions

Management believes that no reasonably possible change in any of the above key assumptions would cause the carrying value of the group of units to materially exceed its recoverable amount.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

15. Inventories

Inventories consist of the following:

	2014	2013
Raw materials – at cost	2,124,480	2,294,666
Work in progress – at cost	474,208	451,305
Finished goods – at net realisable value	4,451,087	4,740,783
	7,049,775	**7,486,754**

The write-downs of inventories to net realisable value and reversal of write-downs were as follows:

	2014	2013
Balance at 1 January	**216,842**	**234,389**
Additional write-downs	99,257	206,520
Unused amounts reversed	(21,858)	(18,819)
Utilised during the year	(152,755)	(206,664)
Foreign exchange differences	(5,277)	1,416
Balance at 31 December	**136,209**	**216,842**

16. Trade and other receivables

	2014	2013
Trade receivables (net of allowance for impairment of receivables of RR 225,186 (2013: RR 244,764))	13,236,008	23,201,077
Interest receivable – third parties	33,519	23,900
Interest receivable – related parties (Note 12)	181,221	21,278
Trade receivables – related parties (Note 12)	5,863,421	60,449
Other receivables – related parties (Note 12) (a)	117,897	–
Other receivables (a)	–	662,359
	19,432,066	**23,969,063**

(a) Other receivables represent cash rebates on procurement due from vendors.

At 31 December 2014 RR 3,108,066 of trade and other receivables were denominated in currencies other than Russian Roubles, primarily in US$.

At 31 December 2013 RR 792,800 of trade and other receivables were denominated in currencies other than Russian Roubles, primarily in Euro.

Movements in allowance for impairment of trade receivables were as follows:

	2014	2013
Balance at 1 January	**244,764**	**107,118**
Additional allowance	160,158	175,725
Unused amounts reversed	(177,806)	(38,797)
Utilised during the year	(1,642)	(133)
Translation differences	(288)	851
Balance at 31 December	**225,186**	**244,764**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

17. Cash and short-term deposits

Cash and short-term deposits consist of the following:

	2014	2013
Cash in bank – Russian Roubles	499,072	9,966,621
Cash in bank – US$ and Euro	4,537,243	28,101
Cash in bank – Ukrainian Hryvnia	33,147	1,444
Short-term bank deposits – Russian Roubles (a)	500,000	5,130,500
Short-term bank deposits – US$ and Euro (a)	1,128,389	–
Short-term bank deposits – Ukrainian Hryvnia	10,670	–
Short-term bank deposits placed in related bank – Russian Roubles (a)	1,635,300	80,000
Short-term bank deposits placed in related bank – US$ (b)	71,364	–
Short-term deposits on state open auctions – Russian Roubles (c)	126,363	158,209
	8,541,548	**15,364,875**

Substantially all cash and short-term deposits of the Group are placed in the related bank (Note 12). Cash balances with the related bank carry no interest.

(a) Deposits denominated in RR bear an interest rate of 1.5%-20% p.a. (2013: 5%-9.5% p.a.). Deposits denominated in US$ and Euro bear an interest rate of 3.6% p.a.

(b) These cash deposits are restricted for use as placed to secure participation in state open auctions.

18. Short-term financial assets

	2014	2013
Accounted for as loans and receivables		
Short-term loans provided to the parent – US$ – (Note 12)	4,050,605	752,772
Short-term loan provided to third parties – Russian Roubles (a)	887,669	–
Short-term loans provided – US$ – (Note 12) (a)	689,165	–
Promissory notes – Russian Roubles	427,580	433,325
Short-term loan provided to related parties – Russian Roubles – (Note 12)	209,000	10,430
Short-term bank deposits – US$	66,166	–
Short-term bank deposits placed in related bank – Russian Roubles – (Note 12)	–	217,100
Short-term bank deposits – Ukrainian Hryvnia	–	25,262
Accounted for as financial assets available for sale		
Securities and other	8,661	14,433
	6,338,846	**1,453,322**

(a) In 2014 the Company provided unsecured short-term loans to third parties with maturity in 2015 and fixed interest rates of 10%-18% p.a.

Short-term loans to third parties in the amount of RR 1,189,165 were provided for financing of certain investment projects of potential future interest for the Group. Recoverability of short-term loans is guaranteed by future economic benefits from these projects assessed by Group management based on long-term business plans.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

19. Long-term financial assets

	2014	2013
Long-term loans and deposits		
Long-term loan provided to third party – Russian Roubles (a)	40,000	–
Long-term loan provided to related parties – Russian Roubles – (Note 12)	–	72,000
Long-term bank deposits placed in related bank – Russian Roubles – (Note 12)	42,900	–
Long-term loan provided to third party – US$ (b)	253,163	–
Long-term bank deposit – Russian Roubles	–	400,000
AFS financial assets at fair value through OCI		
Unquoted equity shares (c)	328,174	65,458
Quoted equity shares (c)	618,842	–
	1,283,079	**537,458**

(a) On 9 June 2014 the Company provided unsecured long-term loan to third party with maturity on 27 December 2017 and fixed interest rate of 15% p.a.

(b) On 19 December 2014 the Company provided unsecured long-term loan to third party with maturity on 31 December 2017 and fixed interest rate of 9% p.a. Long-term loan was provided for financing of certain investment project of potential future interest for the Group, recoverability of this loan is guaranteed by future economic benefits from this project assessed by Group management based on long-term business plan.

(c) As at 31 December 2014 other financial investments include: (i) RR 225,034 (31 December 2013: RR 65,458) investments in preferred shares of Protagonist Therapeutics, Inc. (“Protagonist”) located in the USA, Delaware; Protagonist is a peptide and peptidomimetic therapeutics company pursuing technology platform driven discovery and development of disulfade rich peptides (DRPs); (ii) RR 618,842 investments in preferred shares of Proteon Therapeutics, Inc. located in the USA, Delaware; Proteon is a biopharmaceutical company developing novel, first-in-class pharmaceuticals for patients with renal and vascular diseases; Proteon is listed on NASDAQ, fair value of investment in Proteon is determined by reference to published price quotations on active market and (iii) RR 103,140 investments in preferred shares of Allena Pharmaceuticals located in the USA, Commonwealth of Massachusetts; Allena is a company developing and commercialising non-systemic protein therapeutics to treat metabolic and orphan diseases. The Group has no control or significant influence over these entities.

20. Short-term borrowings and loans

	2014	2013
Short-term loan – Russian Roubles (a)	4,000,000	7,021,700
Other loans	2,941	2,380
	4,002,941	**7,024,080**

(a) As at 31 December 2014 this balance included RR 4,000,000 (2013: RR 4,021,700) unsecured loan provided by Citibank under interest rate of 11.39% p.a. (2013: 8.65% p.a.). As at 31 December 2013 this balance also included RR 3,000,000 unsecured loan provided by Nordea bank under interest rate of 8.79% p.a.; in February 2014, this loan was fully repaid by the Company.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

21. Taxes payable other than income tax

Taxes payable, other than income tax, are comprised of the following:

	2014	2013
Value-added tax	533,505	777,722
Social taxes	72,205	70,849
Property tax	24,648	16,765
Other taxes	25,266	42,947
	655,624	**908,283**

22. Trade and other payables

	2014	2013
Trade payables	4,658,904	3,981,641
Payable to OTCPharm (Notes 6 and 12)	–	3,500,650
Payables for products procurement – third parties (a)	7,032,004	12,562,998
Payables for products procurement, raw materials and other payables – related parties (Note 12)	1,863,212	3,447,878
Issued promissory notes – US$ and Euro (b)	431,401	255,260
Payables to employees	517,065	426,493
Payable to OTCPharm (agency contract) – related party (Note 12)	646,502	–
Other payables (c)	685,263	756,804
	15,834,351	**24,931,724**

(a) These balances represent payables for branded third parties products manufactured by other pharmaceutical companies.

(b) This balance primarily represents interest free promissory notes issued by the Company’s Ukrainian subsidiary “Pharmstandard-Biolik” before the date of acquisition. The promissory notes are payable to the companies affiliated with the former non-controlling shareholders of “Pharmstandard-Biolik”. These promissory notes are payable on demand.

(c) These balances primarily represent payables to third parties for services and equipment and other payables to the companies affiliated with the former non-controlling shareholders of “Pharmstandard-Biolik” for research activity performed before the date of acquisition.

At 31 December 2014 RR 3,760,587 (2013: RR 3,281,531) of total payables were denominated in currencies other than Russian Rouble, primarily in US$ and Euro.

23. Other non-current liabilities

	2014	2013
Deferred income	69,000	139,100
Other	23,472	11,662
	92,472	**150,762**

The subsidiary of the Group “Pharmapark” LLC received government grants to finance certain development costs. This amount represents cash proceeds from government grants and it will be credited to profit or loss over useful life of the intangible asset recognised upon completion of the development stage.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

24. Share capital

In accordance with its charter documents the share capital of the Company is RR 37,793. The authorised number of ordinary shares is 37,792,603 with par value of 1 (one) Russian Rouble. All authorised shares are issued and fully paid. The Company holds 3.8% of issued shares as treasury shares.

As of 31 December 2014 and 2013 54.32% of voting shares of OJSC "Pharmstandard" were held by Augment controlled by Victor Kharitonin, a Russian citizen.

23.58% of ordinary shares are traded on the London Stock Exchange (LSE) and 18.3% on the Moscow Stock Exchange.

Earnings per share are calculated by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period. The Company has no dilutive potential ordinary shares; therefore, the diluted earnings per share equal to basic earnings per share.

Earnings per share

Earnings per share are as follows:

	2014	**2013**
Weighted average number of ordinary shares outstanding	36,355,683	34,629,722
Profit for the year attributable to the ordinary shareholders	10,841,234	11,805,787
Basic and diluted earnings per share, Russian Roubles	298.2	340.92

25. Revenue

Revenue breakdown by product groups comprised the following:

	2014	**2013**
Pharmaceutical products		
Over the Counter ("OTC") – (a)	5,547,561	16,457,827
Prescription		
Branded	5,924,459	5,974,312
Non-branded	1,006,400	801,474
	6,930,859	**6,775,786**
Third parties products (b)	19,024,923	30,451,243
Other – substances and APIs (a)	2,856,044	1,174,463
Clearance sale of OTC branded inventory to OTCpharm due to spin-off (e)	2,411,060	–
Total pharmaceutical products	**36,770,447**	**54,859,319**
Contractual manufacturing (Note 12) – (c)	1,503,922	110,698
Agency fee income (Note 12) – (d)	1,828,863	1,037,886
Medical equipment	1,120,203	1,048,278
	41,223,435	**57,056,181**

(a) On 1 April 2014 OTCpharm started its operation independently of the Group and since this date revenue from sale of the most of OTC branded products is being recognised by OTCpharm.

(b) Third parties products sales include sales of branded pharmaceutical products such as Velcade, Mabtera, Koagil VII, Mildronate, IRS®-19, Imudon®, Prezista, Revlimid, Cerezim, Pulmozim and other manufactured by other pharmaceutical companies.

(c) Since 2014, the Group provides contract manufacturing services primarily to OTCpharm (Note 12).

(d) The Company holds agency contracts for distribution and sale of certain products owned by related and third parties.

(e) In April and May 2014, the Group sold outstanding inventory balance related to OTC business to OTCpharm to enable it to launch independent operations (Notes 6 and 12).

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

26. Cost of sales

The components of cost of sales were as follows:

	2014	**2013**
Materials and components	6,149,948	6,515,683
Third parties products	13,570,790	23,162,756
Production overheads	2,039,923	1,574,557
Depreciation and amortisation	746,956	789,301
Direct labour costs	499,423	542,331
	23,007,040	**32,584,628**

The total amount of cost of sales includes (i) RR 1,063,576 of cost of the clearance sales of OTC-branded products to OTCpharm and (ii) RR 1,462,459 of cost of active pharmaceutical ingredients sold by the Group to OTCpharm.

27. Selling and distribution costs

Selling and distribution costs were as follows:

	2014	**2013**
Advertising	1,573,496	3,537,001
Labour costs	1,503,273	1,570,834
Freight, communication and insurance of goods in transit	221,799	260,670
Trainings and other services	68,792	54,255
Certification expenses	113,209	115,868
Rent	140,196	125,001
Commission and license fee	144,573	78,079
Materials, maintenance and utilities	122,376	139,738
Travel and representative expenses	129,799	191,001
Depreciation	71,849	80,659
Other expenses	44,155	40,475
	4,133,517	**6,193,581**

28. General and administrative expenses

General and administrative expenses were as follows:

	2014	**2013**
Labour costs	1,404,360	1,278,439
Services, legal, audit and consulting expense	305,449	115,651
Travel and representative expenses	33,571	41,484
Taxes other than income tax	23,781	21,373
Property and other insurance	21,303	21,272
Communication expenses	29,695	29,787
Depreciation	125,865	83,876
Rent	132,115	118,681
Materials, maintenance and utilities	167,866	164,448
Other	56,421	55,302
	2,300,426	**1,930,313**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

29. Other income

Other income comprised the following:

	2014	2013
Foreign exchange gain	2,166,253	238,668
Income from non-core operations – related party (Note 12)	259,539	–
Gain from disposal of property, plant and equipment	39,418	47,912
Income received as penalties	96,018	127,977
Reversal of impairment – property, plant and equipment (Note 13)	14,943	2,091
Reversal of impairment – financial assets	61,213	–
Gain from transactions with promissory notes (Note 12)	80,112	–
Other income	225,949	100,653
	2,943,445	**517,301**

30. Other expenses

Other expenses comprised the following:

	2014	2013
Foreign exchange loss	525,425	82,100
Charity	31,116	10,527
Bank charges	28,210	30,958
Other taxes and penalties (a)	129,603	410,681
Biolik expenses resulting from suspension of production (Note 32)	95,973	124,811
Research expenses (b)	36,881	168,675
Impairment of property, plant and equipment (Note 13)	68,193	2,548
Impairment of intangible assets (Note 6)	–	100,000
Other	117,535	137,844
	1,032,936	**1,068,144**

(a) Other taxes and penalties primarily include property tax expenses and penalties accrual as a result of tax audit.

(b) These expenses represent certain non-recurring research projects.

31. Income tax

	2014	2013
Income tax expense – current	2,783,919	4,044,679
Deferred tax benefit – origination and reversal of temporary differences	(59,652)	(102,588)
Income tax expense	**2,724,267**	**3,942,091**

Income before taxation for financial reporting purposes is reconciled to tax expense as follows:

	2014	2013
Profit before income tax	**13,819,730**	**15,862,530**
Theoretical tax charge at Russian statutory rate of 20%	2,763,946	3,172,506
Effect of the difference in tax rates in countries other than Russia	(1,067)	(23,149)
Tax effect from treasury shares settlement (Note 7)	–	556,767
Effect from intra-group dividends eliminated in consolidation (taxed at rate of 5-10%)	7,261	19,457
Share of results of associates and joint ventures	(47,012)	19,546
Tax effect of items which are not deductible or assessable for taxation purposes:		
Non-deductible expenses	1,139	196,964
Income tax expense	**2,724,267**	**3,942,091**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

31. Income tax (continued)

Movements in deferred tax balances were as follows:

	1 January 2013	Temporary differences recognition and reversal in profit and loss	Effect of spin-off (Note 6)	Effect from obtaining control over joint venture (Note 8.1)	31 December 2013	Temporary differences recognition and reversal in profit and loss	31 December 2014
Tax effects of taxable and deductible temporary differences – asset (liability)							
Property, plant and equipment	(571,480)	33,726	–	(244)	(537,998)	(23,865)	(561,863)
Intangible assets	(515,890)	(10,922)	492,449	61	(34,302)	60,955	26,653
Trade and other receivables	32,231	(93,589)	–	–	(61,358)	(23,602)	(84,960)
Inventories	205,057	147,715	–	109	352,881	84,122	437,003
Trade and other payables	36,163	2,610	–	1,611	40,384	(24,294)	16,090
Financial instruments	2,442	4,980	–	–	7,422	(7,422)	–
Other	28,809	18,068	–	(1)	46,876	(6,242)	40,634
Total net deferred tax liability	**(782,668)**	**102,588**	**492,449**	**1,536**	**(186,095)**	**59,652**	**(126,443)**

The recognition and reversals of temporary differences primarily relates to the following:

- depreciation of property, plant and equipment in excess of the depreciation for tax purposes;
- write down of inventory to net realisable value, unrealised profit due to intragroup purchases of materials, discounts recognised in taxation as other income;
- fair value adjustments on acquisition;
- fair value of financial instruments in excess of the cost of these instruments for tax purpose;
- impairment of trade receivables;
- amortisation of trade marks in excess of the amortisation for tax purposes; and
- deemed cost adjustments upon conversion to IFRS.

The aggregate amount of temporary differences associated with investments in subsidiaries for which deferred tax liabilities have not been recognised was approximately RR 23,632,865 as at 31 December 2014 (2013: RR 19,084,856).

32. Contingencies, commitments and operating risks

Operating environment of the Group

Russia, where majority of the Group’s operations are located, 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 2014, the Russian economy was negatively impacted by a significant drop in crude oil prices and a significant devaluation of the Russian Rouble, as well as sanctions imposed on Russia by several countries. In December 2014, the Rouble interest rates have increased significantly after the Central Bank of Russia raised its key rate to 17%.The combination of the above resulted in reduced access to capital, a higher cost of capital, increased inflation and uncertainty regarding economic growth, which could negatively affect the Group’s future financial position, results of operations and business prospects.

32. Contingencies, commitments and operating risks (continued)

Operating environment of the Group (continued)

The Group also operates in Ukraine. In 2014, the economic and political situation in Ukraine deteriorated significantly. As a result, Ukraine has experienced a fall in gross domestic product, a significant negative balance of payments and a sharp reduction in foreign currency reserves. Furthermore in 2014 the Ukrainian Hryvnia significantly devalued to major foreign currencies and the National Bank of Ukraine imposed certain restrictions on foreign currency operations. Restrictions have also been introduced for certain cross-border settlements, including payments of dividends. International rating agencies have downgraded sovereign debt ratings for Ukraine. Currently, a loan programme extension, which may necessitate certain austerity measures, is being negotiated by Ukraine with the International Monetary Fund. The combination of the above events has resulted in a deterioration of liquidity and much tighter credit conditions where credit is available.

Management believes it is taking appropriate measures to support the sustainability of the Group’s business in the current circumstances.

Taxation

Russian tax, currency and customs legislation can be interpreted in different ways and is susceptible to frequent changes. The interpretation made by the Company’s management of the legislation in question as applied to the operations and activities of the Company’s enterprises may be challenged by the relevant regional or federal authorities.

In addition, certain amendments to tax legislation were passed in 2014 and enter into force from 2015 which are aimed at combating tax evasion through the use of low-tax jurisdictions and aggressive tax planning structures. In particular, those amendments include definitions of the concepts of beneficial ownership and tax residence of legal entities at their actual place of business, and an approach to the taxation of controlled foreign companies.

These changes, as well as recent trends in the application and interpretation of certain provisions of Russian tax legislation, indicate that the tax authorities may take a tougher line in interpreting the law and checking tax returns. As a result, tax authorities may raise questions about transactions and accounting methods which they did not question before. This may result in significant amounts of additional tax charges, penalties and fines being imposed. It is not possible to determine claim amounts for suits which may be, but have not actually been, filed, or to assess the likelihood of an adverse outcome. Tax audits may cover the three calendar years immediately preceding the year in which the audit occurs. In certain circumstances an audit can also cover earlier periods.

The management is of the opinion that, as at 31 December 2014, it has correctly interpreted the relevant provisions of law, and it is highly likely that the Company’s position in regard to tax, currency and customs legislation will remain unchanged.

Because of the uncertainties associated with the Russian tax and legal systems, the ultimate amount of taxes, penalties and interest assessed, if any, may be in excess of the amount expensed to date and accrued as at 31 December 2014. Should the tax authorities decide to issue a claim and prove successful in the court, they would be entitled to recover the amount claimed, together with fines (in Russia amounting to 20% of such amount and interest at the rate of 1/300 of the Central Bank of the Russian Federation rate for each day of delay for late payment of such amount). Management believes that it is not probable that the ultimate outcome of such matters would result in a liability. Therefore, no provision for these contingencies was recorded in these consolidated financial statements.

32. Contingencies, commitments and operating risks (continued)

Russian transfer pricing legislation

The new Russian transfer pricing legislation, which came into force on 1 January 2012, allows the Russian tax authority to apply transfer pricing adjustments and impose additional profits tax liabilities in respect of all “controlled” transactions if the transaction price differs from the market level of prices. A list of “controlled” transactions includes transactions performed with related parties based on domestic and cross-border agreements and certain types of cross-border transactions with independent parties. For domestic transactions the transfer pricing rules apply only if the amount of all transactions with related party exceeds 1 billion roubles in 2014 (apart from some exceptions provided by the Tax Code); all cross-border transactions with related parties are controlled without application of any financial thresholds. In cases where the domestic transaction resulted in an accrual of additional tax liabilities for one party, another party could apply the symmetrical adjustment to its profit tax liabilities according a special notification issued by the authorised body in due course.

The current Russian transfer pricing rules have considerably increased the compliance burden for the taxpayers compared to the transfer pricing rules which were in effect before 2012 due to, inter alia, shifting the burden of proof from the Russian tax authorities to the taxpayers. These rules are applicable not only to the transactions taking place in 2012-2014 but also to the prior transactions with related parties if related income and expenses were recognised in 2012-2014. Special transfer pricing rules apply to transactions with securities and derivatives.

In 2012-2014 the Group determined its tax liabilities arising from “controlled” transactions using actual transaction prices.

Due to the uncertainty and absence of current practice of application of the current Russian transfer pricing legislation the Russian tax authorities may challenge the level of prices applied by the Group under the “controlled” transactions and assess additional tax liabilities unless the Group is able to demonstrate the use of market prices with respect to the “controlled” transactions, and that there has been proper reporting to the Russian tax authorities, supported by appropriate available transfer pricing documentation.

Insurance policies

The Group holds insurance policies in relation to its property, plant and equipment, which cover majority of property, plant and equipment items. The Group holds no insurance policies in relation to its operations, or in respect of public liability.

Operating lease agreements

The Group entered into a number of operating lease agreements for warehouses and land. Rental agreements are revised on an annual basis.

Commitment liabilities and guarantees

In 2012, the Group provided certain unsecured guaranties with maturity period from two years to three years for related parties to provide some state contracts signed by these related parties. Outstanding amount of guaranties at 31 December 2014 is RR 88,740 with maturity period February 2016. The management believes that provided guaranties have remote financial risk for the Group.

32. Contingencies, commitments and operating risks (continued)

Commitment liabilities and guarantees (continued)

In July 2014, the Company provided unsecured financial guaranties in the total amount of RR 500,000 with maturity period not later than March-April 2015 to certain pharmacy chains to facilitate increase of direct sales of Group’s products to these pharmacy chains. The management believes that provided guarantees would result in remote financial risks for the Group.

Statutory inspection of “Pharmstandard-Biolik” PJSC (“Biolik”)

In December 2012, the Ukrainian authorities performed an extraordinary inspection of “Biolik” compliance with the applicable production quality standards. The inspection revealed certain formal deficiencies in the controls over production quality resulting in suspension in “Biolik” production process until resolution of those deficiencies. Those deficiencies were primarily due to the reconstruction of production and maintenance work to improve the quality of “Biolik’s” products. In December 2013, “Biolik” production process was restarted for certain products. In 2014, the issues revealed by the inspection were completely resolved and “Biolik” restarted its normal operations.

33. Financial instruments and financial risk management objectives and policies

Fair values

Management believes that fair value of cash and cash equivalents, short-term financial assets, trade and other receivables and payables and short-term borrowings and loans approximate their carrying amounts due to their short maturity.

The Group has no long-term borrowings and loans and derivative financial instruments as of 31 December 2014 and 31 December 2013.

Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly;
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

33. Financial instruments and financial risk management objectives and policies (continued)

Fair value hierarchy (continued)

31 December 2014	**Total**	**Level 1**	**Level 2**	**Level 3**
Assets measured at fair value				
Unquoted equity shares (Note 19)	**328,174**	–	–	328,174
Quoted equity shares (Note 19)	**618,842**	618,842	–	–
Assets for which fair values are disclosed				
Short-term loans provided (Note 18)	**5,836,439**	–	–	5,836,439
Long-term loans provided (Note 19)	**293,163**	–	–	293,163
Securities (Notes 18)	**8,253**	5,830	–	2,423

31 December 2013	**Total**	**Level 1**	**Level 2**	**Level 3**
Assets measured at fair value				
Unquoted equity shares (Note 19)	**65,458**	–	–	65,458
Assets for which fair values are disclosed				
Short-term loans provided (Note 18)	**763,202**	–	–	763,202
Long-term loans provided (Note 19)	**72,000**	–	–	72,000
Securities (Note 18)	**13,574**	10,826	–	2,748

Financial risk management objectives and policies

The Group's principal financial instruments comprise bank loans, short-term and long-term bank deposits and cash and cash equivalents. The main purpose of these financial instruments is to raise finance for the Group's operations and investment activities. The Group has various other financial assets and liabilities such as promissory notes, trade receivables, trade and other payables, which relate directly to its operations. During the year the Group did not undertake active trading in financial instruments.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and credit risk. Management reviews and agrees policies for managing each of these risks which are summarised below.

Interest rate risk

Management believes that the Group does not have significant interest rate risk as at 31 December 2014 and 31 December 2013. The Group has certain short-term financial investments (loans and bank deposits, see Notes 17, 18 and 19), at fixed interest rates based on current market rates at the date of initial recognition and has short-term borrowings and loans (Note 20) at fixed interest rates based on current market rates at the date of initial recognition. Therefore, the Group has no risk to interest rates changes due to possible changes in market interest rates.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

33. Financial instruments and financial risk management objectives and policies (continued)

Financial risk management objectives and policies (continued)

Foreign exchange risk

The Group has certain US dollar and Euro denominated cash and short-term deposits (Note 17), short-term financial assets (Note 18), trade and other payables (Note 22) and trade and other receivables (Note 16). Therefore, the Group is exposed to foreign exchange risk.

The Group monitors the foreign exchange risk by analysing changes in exchange rates in the currencies in which its cash, financial assets and payables are denominated. However, the Group does not have formal arrangements to mitigate this foreign exchange risk.

The tables below shows the sensitivity to a reasonably possible change in the US dollar and Euro exchange rates, with all other variables held constant, of the Group’s profit before tax:

	Increase/ decrease in US$ rate	Effect on profit before tax
As at 31 December 2014		
US$/Roubles exchange rate	+28.54%	2,657,819
US$/Roubles exchange rate	-28.54%	(2,657,819)

	Increase/ decrease in US$ rate	Effect on profit before tax
As at 31 December 2013		
US$/Roubles exchange rate	+20%	(157,781)
US$/Roubles exchange rate	-10%	78,891

	Increase/ decrease in Euro rate	Effect on profit before tax
As at 31 December 2014		
Euro/Roubles exchange rate	+29.58%	383,984
Euro/Roubles exchange rate	-29.58%	(383,984)

	Increase/ decrease in Euro rate	Effect on profit before tax
As at 31 December 2013		
Euro/Roubles exchange rate	+20%	(101,901)
Euro/Roubles exchange rate	-9%	45,855

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

33. Financial instruments and financial risk management objectives and policies (continued)

Financial risk management objectives and policies (continued)

	Increase/ decrease in US$ rate	Effect on profit before tax
As at 31 December 2014		
US$/Ukrainian Hryvnia exchange rate	+28.93%	(152,991)
US$/Ukrainian Hryvnia exchange rate	-28.93%	152,991

	Increase/ decrease in US$ rate	Effect on profit before tax
As at 31 December 2013		
US$/Ukrainian Hryvnia exchange rate	+30%	(91,233)
US$/Ukrainian Hryvnia exchange rate	-5%	15,206

Liquidity risk

The Group’s policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of committed credit facilities to meet its operating and financial commitments. The Group performs continuous monitoring of cash deficit risks and continuous monitoring of repayment of its financial liabilities on time. The Group performs daily planning and control cash flow procedures.

The table below summarises the maturity profile of the Group’s non-derivative financial liabilities based on contractual undiscounted payments including interest.

As at 31 December 2014	Total	Less than 4 months	4 to 6 months	6 to 12 months	More than 12 months
Borrowings and loans (Note 20)	**4,342,739**	151,451	75,725	4,115,563	–
Trade and other payables	**15,402,950**	15,402,950	–	–	–
Other non-current liabilities	**23,472**	–	–	–	23,472
Total	**19,769,161**	**15,554,401**	**75,725**	**4,115,563**	**23,472**

As at 31 December 2013	Total	Less than 4 months	4 to 6 months	6 to 12 months	More than 12 months
Borrowings and loans (Note 20)	**7,347,389**	3,180,184	57,821	4,109,384	–
Other current liabilities (a)	**3,500,650**	3,500,650	–	–	–
Trade and other payables	**21,175,814**	21,175,814	–	–	–
Other non-current liabilities	**1,879**	–	–	–	1,879
Total	**32,025,732**	**27,856,648**	**57,821**	**4,109,384**	**1,879**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

33. Financial instruments and financial risk management objectives and policies (continued)

Financial risk management objectives and policies (continued)

Credit risk

Financial assets, which potentially are subject to credit risk, consist principally of trade receivables. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. Sales to customers are made in accordance with annually approved Marketing and Credit policy. The Group daily monitors sales and receivables conditions using appropriate internal control procedures.

The carrying amount of accounts receivable, net of allowance for impairment, represents the maximum amount exposed to credit risk. Although collection of receivables could be affected by economic factors, management believes that there is no significant risk of loss to the Group beyond the allowance already recorded.

Cash and deposits are mainly held in related bank and the Group assessed the credit risk as low.

The table below summarises the Group’s trade and other receivables aging:

			Not impaired but past due				
	Total	**Neither impaired nor past due**	**Less 1 month**	**1-2 months**	**2-3 months**	**3 to 6 months**	**>6 months**
31 December 2014	**19,432,066**	14,242,641	814,441	733,756	480,738	2,728,979	431,511
31 December 2013	**23,969,063**	21,930,722	1,185,580	255,609	268,224	209,417	119,511

Sales concentration to a small group of customers

The Group works with five distributors that together represent about 37% of the Group’s revenue for 2014 excluding sales to the Ministry of health of the Russian Federation under state open auctions and the clearance sales to OTCpharm in April-May 2014. It is common practice of the Russian pharmaceutical market to work with the limited number of large distributors.

Capital management

The Group’s objectives when managing capital are to safeguard the Group’s ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

33. Financial instruments and financial risk management objectives and policies (continued)

Capital management (continued)

The Group monitors capital using a gearing ratio, which is net debt divided by total capital plus net debt. The Group's policy is to keep the gearing ratio not more than 60%. The Group includes within net debt borrowings and loans, trade and other payables less cash and cash equivalents. Capital includes equity attributable to the equity holders of the parent.

	2014	2013
Borrowings and loans	4,002,941	7,024,080
Trade and other payables	15,834,351	24,931,724
Less: cash and short-term deposits	(8,541,548)	(15,364,875)
Net debt	**11,295,744**	**16,590,929**
Capital	39,174,393	27,628,445
Capital and net debt	**50,470,137**	**44,219,374**
Gearing ratio	22%	38%

34. Material partly-owned subsidiaries

Proportion of equity interest held by non-controlling interests is summarized below:

Name	Country of incorporation and operation	2014 % share	2013 % share
"Pharmstandard-Tomskhimpharm" OJSC	Russian Federation	9	9
Other			
"Pharmstandard-Biolik" PJSC (Note 10)	Ukraine	3.07	3.07
MDR Pharmaceuticals	Cyprus	49.95	49.95
Bigpearl Trading Limited	Cyprus	49.995	49.995
"Pharmapark" LLC	Russian Federation	49.995	49.995
"Biomed named after I.I.Mechnikov" CJSC	Russian Federation	50.155	50.155
"PKB named after I.I.Mechnikov" CJSC (Note 1)	Russian Federation	–	50.155
"Pharmatsevticheskiye innovatsii" LLC	Russian Federation	49.995	49.995
"EKK" OJSC	Russian Federation	64.71	64.71
Moldildo trading Limited	Cyprus	25	25
"Pharmstandard-Medtechnika" LLC	Russian Federation	25	25
"Sellthera Pharm" LLC	Russian Federation	25	25

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

34. Material partly-owned subsidiaries (continued)

The summarised financial information of these subsidiaries is provided below. This information is based on amounts before inter-company eliminations:

Summarised statement of profit or loss for 2014	**Pharmstandard-Tomskkhimpharm**	**Other**
Revenue	3,129,735	2,607,780
Cost of sales	(1,949,704)	(1,180,736)
Selling and distribution costs	(693,541)	(379,799)
Administrative expenses	(121,758)	(378,162)
Other income (expense), net	85,289	(312,407)
Financial income (expense), net	–	(3,777)
Profit before income tax	**450,021**	**352,899**
Income tax	(93,163)	(123,622)
Profit for the year	**356,858**	**229,277**
Attributable to non-controlling interests	32,117	222,112

Summarised statement of profit or loss for 2013	**Pharmstandard-Tomskkhimpharm**	**Other**
Revenue	4,286,883	1,994,187
Cost of sales	(2,095,413)	(1,020,938)
Selling and distribution costs	(1,674,197)	(444,289)
Administrative expenses	(102,449)	(315,791)
Other income (expense), net	83,419	(86,944)
Financial income (expense), net	–	10,682
Profit before income tax	**498,243**	**136,907**
Income tax	(101,071)	(78,290)
Profit for the year	**397,172**	**58,617**
Attributable to non-controlling interests	35,746	78,906

Summarised statement of financial position as at 31 December 2014	**Pharmstandard-Tomskkhimpharm**	**Other**
Inventories, receivables, cash and short-term deposits and other current assets	3,326,916	2,693,010
Property, plant and equipment, intangible assets and other non-current financial assets	465,401	2,379,916
Trade, other payables and other current liabilities	(263,959)	(2,169,288)
Deferred tax liabilities and other non-current liabilities	(23,710)	(419,456)
Total equity	**3,504,648**	**2,484,182**
Attributable to:		
Non-controlling interests	315,418	1,330,529

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

34. Material partly-owned subsidiaries (continued)

Summarised statement of financial position as at 31 December 2013	Pharmstandard-Tomskkhimpharm	Other
Inventories, receivables, cash and short-term deposits and other current assets	3,131,075	2,208,844
Property, plant and equipment, intangible assets and other non-current financial assets	461,561	2,007,924
Trade, other payables and other current liabilities	(415,358)	(1,320,151)
Deferred tax liabilities and other non-current liabilities	(29,489)	(480,837)
Total equity	**3,147,789**	**2,415,780**
Attributable to:		
Non-controlling interests	283,301	1,162,547

Dividends paid by a subsidiary

In 2014, an amount of RR 32,269 was paid by the Company's subsidiary "Bigpearl Trading Limited" (Cyprus) to non-controlling shareholders (2013: RR 23,498).

35. Events after the reporting period

On 6 January 2015 Pharmstandard International S.A. acquired preferred shares of enGene Inc. for cash consideration of 770 thousand US$ (RR 43,644) which represent 4.18% of company's share. Engene Inc. is a company incorporated in Monreal, Canada and focused on a highly flexible nucleotide delivery technology targeting mucosal tissues to treat numerous prevalent, chronic diseases via the induction or suppression of protein expression levels.

On 17 April 2015 Pharmstandard International S.A. acquired preferred shares of Jounce Therapeutics for cash consideration of 5 million US$ (RR: 252,647) which represent 2.4% of company's share. Jounce Therapeutics is a company incorporated in the USA and focused on a creation of highly durable treatment for cancer by optimal use of the immune system.