# Integra Group

## Consolidated Interim Condensed Financial Information (Unaudited)
## as of and for the Six Months Ended
## 30 June 2007

PRICEWATERHOUSECOOPERS

**ZAO PricewaterhouseCoopers Audit**
Kosmodamianskaya Nab. 52, Bld. 5
115054 Moscow
Russia
Telephone +7 (495) 967 6000
Facsimile +7 (495) 967 6001
www.pwc.ru

## Review Report of Auditors

To the shareholders and Board of Directors of Integra Group

*Introduction*

1. We have reviewed the accompanying consolidated interim condensed balance sheet of Integra Group and its subsidiaries (the "Group") as of 30 June 2007 and the related consolidated interim condensed statements of income, of cash flows and of changes in shareholders' equity for the six-months then ended. Management is responsible for the preparation and fair presentation of this consolidated interim condensed financial information in accordance with International Accounting Standard No. 34, *Interim Financial Reporting*. Our responsibility is to express a conclusion on this consolidated interim condensed financial information based on our review.

*Scope of Review*

2. We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of consolidated interim condensed financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

*Conclusion*

3. Based on our review, nothing has come to our attention that causes us to believe that the accompanying consolidated interim condensed financial information is not presented, in all material respects, in accordance with International Accounting Standard No. 34, *Interim Financial Reporting*..

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation
10 September 2007

# Contents

**(expressed in thousands of US Dollars, except as indicated)**

| | | Six months ended 30 June: | |
|---|---|---|---|
| | **Note** | **2007** | **2006** |
| Sales | 6 | 487,892 | 176,400 |
| Cost of sales | 6,7 | (400,699) | (139,069) |
| **Gross profit** | | **87,193** | **37,331** |
| Selling, general and administrative expenses | 6,8 | (95,419) | (31,602) |
| Profit from disposal of property, plant and equipment | | 256 | - |
| Gain on acquisition/disposal of subsidiaries | 5 | 91 | 225 |
| Gain on acquisition of minority interests | 5 | 506 | - |
| **Operating (loss) profit** | | **(7,373)** | **5,954** |
| Interest income | | 5,170 | 474 |
| Interest expense | 18 | (40,189) | (16,155) |
| Exchange (loss) gain | | (896) | 7,289 |
| Share of results of associates | 14 | 1,352 | 335 |
| **Loss before taxation** | | **(41,936)** | **(2,103)** |
| Current income tax expense | | (14,978) | (4,482) |
| Deferred income tax benefit | | 5,372 | 1,995 |
| **Total tax expense** | 6,17 | **(9,606)** | **(2,487)** |
| **Loss for the period** | | **(51,542)** | **(4,590)** |
| (Loss) profit attributable to: | | | |
| - Minority interest | | (1,246) | 960 |
| - **Shareholders of Integra Group** | | **(50,296)** | **(5,550)** |
| Loss per share, basic and diluted (in US Dollars per share) | 21 | (9.56) | (1.80) |
| Weighted average shares outstanding, basic and diluted | 21 | 5,262,651 | 3,083,018 |

Approved and authorised for issue 10 September 2007

F. V. Lubashevsky
Chief Executive Officer

A. Polevoy
Chief Financial Officer

The accompanying notes are an integral part of these consolidated interim condensed financial information.

**(expressed in thousands of US Dollars, except as indicated)**

| | Note | 30 June 2007 | 31 December 2006 |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents | | 231,932 | 87,821 |
| Trade and other receivables | 10 | 346,288 | 235,777 |
| Inventories | 11 | 131,247 | 100,184 |
| **Total current assets** | | **709,467** | **423,782** |
| Goodwill and other intangible assets | 12 | 325,369 | 340,002 |
| Property, plant and equipment | 13 | 445,039 | 424,643 |
| Investments in associates | 14 | 16,995 | 15,375 |
| Deferred tax assets | | 1,002 | 1,925 |
| Loans provided and other assets | 15 | 45,005 | 34,331 |
| **Total non-current assets** | | **833,410** | **816,276** |
| **Total assets** | | **1,542,877** | **1,240,058** |
| **Liabilities and shareholders' equity** | | | |
| Accounts payable and accrued liabilities | 16 | 361,624 | 254,773 |
| Income taxes payable | | 15,409 | 18,425 |
| Other taxes payable | 17 | 26,928 | 22,689 |
| Short-term borrowings and current portion of long-term borrowings | 18 | 25,035 | 340,421 |
| **Total current liabilities** | | **428,996** | **636,308** |
| Long-term financial liabilities | 18 | 206,634 | 246,089 |
| Deferred tax liability | | 75,103 | 79,246 |
| Other non-current liabilities | | 1,527 | 1,601 |
| **Total non-current liabilities** | | **283,264** | **326,936** |
| **Total liabilities** | | **712,260** | **963,244** |
| **Shareholders' equity:** | | | |
| Class A common shares (5,858,206 and 2,085,844 shares issued and outstanding at 30 June 2007 and 31 December 2006, respectively; nominal value one ten thousandth of one US Dollar) | 19 | 1 | - |
| Class B common shares (940,000 shares issued and outstanding at 30 June 2007 and 31 December 2006, respectively; nominal value one ten thousandth of one US Dollar) | 19 | - | - |
| Convertible preferred shares (nil and 1,755,447 shares issued and outstanding at 30 June 2007 and 31 December 2006, respectively; nominal value one ten thousandth of one US Dollar) | 19 | - | - |
| Treasury shares | | (1,598) | (1,598) |
| Cumulative translation adjustment | | 27,540 | 12,434 |
| Warrants | | - | 116 |
| Share premium | 19 | 809,972 | 217,354 |
| Retained earnings | | (80,146) | (29,850) |
| **Total equity attributable to Integra Group shareholders** | | **755,769** | **198,456** |
| Minority interest | | 74,848 | 78,358 |
| **Total equity** | | **830,617** | **276,814** |
| **Total liabilities and equity** | | **1,542,877** | **1,240,058** |

**(expressed in thousands of US Dollars)**

| | Notes | Six months ended 30 June: 2007 | 2006 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Loss before taxation | | (41,936) | (2,103) |
| Adjustments for: | | | |
| Gain on acquisition/disposal of subsidiaries | 5 | (91) | (225) |
| Gain on acquisition of minority interest in subsidiaries | 5 | (506) | - |
| Depreciation and amortization | | 67,461 | 15,937 |
| Interest income | | (5,170) | (474) |
| Interest expense | 18 | 40,189 | 16,155 |
| Share-based compensation | 20 | 16,075 | 3,005 |
| Share of results of associates | 14 | (1,352) | (335) |
| Other | | 910 | 10 |
| **Operating cash flows before working capital changes** | | **75,580** | **31,970** |
| Change in trade and other receivables | | (91,031) | (39,353) |
| Change in inventories | | (29,959) | (18,530) |
| Change in accounts payable and accrued liabilities | | 153,045 | 25,795 |
| Change in other taxes payable | | 4,075 | 426 |
| **Operating cash flows before interest and income taxes** | | **111,710** | **308** |
| Income tax paid | | (19,707) | (9,281) |
| Interest paid | | (21,326) | (4,505) |
| **Net cash provided by (used in) operating activities** | | **70,677** | **(13,478)** |
| **Cash flows from investing activities:** | | | |
| Purchase of property, plant and equipment | | (70,409) | (67,188) |
| Proceeds from the disposal of property, plant and equipment | | 2,801 | 2,049 |
| Settlements for purchases of companies, net of cash acquired | | (58,367) | (28,838) |
| Disposal of subsidiaries | | - | 1,736 |
| Loans provided | | (1,972) | (2,541) |
| Repayment of loans provided | | 3,213 | - |
| Interest received | | 3,410 | 299 |
| Other | | (4) | (24) |
| **Net cash used in investing activities** | | **(121,328)** | **(94,507)** |
| **Cash flows from financing activities:** | | | |
| Proceeds from issuance of shares, net of certain transaction costs | 19 | 562,352 | 336 |
| Proceeds from exercise of warrants connected with Senior Notes and Facility Agreement | 19 | 17,167 | - |
| Proceeds from borrowings | | 15,862 | 126,947 |
| Repayment of borrowings | | (408,093) | (29,768) |
| **Net cash provided by financing activities** | | **187,288** | **97,515** |
| **Net increase (decrease) in cash and cash equivalents** | | **136,637** | **(10,470)** |
| Cash and cash equivalents at the beginning of the period | | 87,821 | 21,471 |
| Effect of exchange differences on cash balances | | 7,474 | 1,352 |
| **Cash and cash equivalents at the end of the period** | | **231,932** | **12,353** |

The accompanying notes are an integral part of these consolidated interim condensed financial information.

## Consolidated Interim Condensed Statements of Changes in Shareholders' Equity (Unaudited)

**(expressed in thousands of US Dollars, except as indicated)**

| | Note | Common shares | Preferred shares – Series A | Preferred shares – Series B | Treasury shares | Warrants | Share premium | Cumulative translation adjustment | Retained earnings | Equity attributable to Integra Group shareholders | Minority interest | Total equity |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Balance at 31 December 2005** | | - | - | - | - | **136** | **46,577** | **637** | **10,530** | **57,880** | **25,145** | **83,025** |
| Exercise of warrants | | - | - | - | - | (20) | 336 | - | 20 | 336 | - | 336 |
| Disposal of subsidiaries | | - | - | - | - | - | - | - | - | - | (18) | (18) |
| Share-based compensation | | - | - | - | - | - | 3,005 | - | - | 3,005 | - | 3,005 |
| ***Recognized income*** | | - | - | - | - | - | - | - | - | - | - | - |
| Translation adjustment | | - | - | - | - | - | - | 5,350 | - | 5,350 | - | 5,350 |
| Loss for the period | | - | - | - | - | - | - | - | (5,550) | (5,550) | 960 | (4,590) |
| **Total recognized income (loss)** | | - | - | - | - | - | - | **5,350** | **(5,550)** | **(200)** | **960** | **760** |
| **Balance at 30 June 2006** | | - | - | - | - | **116** | **49,918** | **5,987** | **5,000** | **61,021** | **26,087** | **87,108** |
| **Balance at 31 December 2006** | | - | - | - | **(1,598)** | **116** | **217,354** | **12,434** | **(29,850)** | **198,456** | **78,358** | **276,814** |
| Initial public offering | 19 | 1 | - | - | - | - | 559,260 | - | - | 559,261 | - | 559,261 |
| Exercise of warrants connected with Senior Notes | 19 | - | - | - | - | (116) | 1,533 | - | - | 1,417 | - | 1,417 |
| Exercise of warrants connected with Facility Agreement | 19 | - | - | - | - | - | 15,750 | - | - | 15,750 | - | 15,750 |
| Share-based compensation | 20 | - | - | - | - | - | 16,075 | - | - | 16,075 | - | 16,075 |
| Purchase of minority interest | 5 | - | - | - | - | - | - | - | - | - | (2,264) | (2,264) |
| ***Recognized income*** | | | | | | | | | | | | |
| Translation adjustment | | - | - | - | - | - | - | 15,106 | - | 15,106 | - | 15,106 |
| Loss for the period | | - | - | - | - | - | - | - | (50,296) | (50,296) | (1,246) | (51,542) |
| **Total recognized income (loss)** | | - | - | - | - | - | - | **15,106** | **(50,296)** | **(35,190)** | **(1,246)** | **(36,436)** |
| **Balance at 30 June 2007** | | **1** | - | - | **(1,598)** | - | **809,972** | **27,540** | **(80,146)** | **755,769** | **74,848** | **830,617** |

| **Supplemental information for minority interests:** | Six months ended 30 June: 2007 | 2006 |
|---|---|---|
| Share of profit attributable to holders of equity instruments with redemption rights classified as a liability | (14) | 196 |
| Share of loss attributable to holders of instruments classified as equity | 1,260 | (1,156) |
| **Loss (profit) attributable to minority interest** | **1,246** | **(960)** |

The accompanying notes are an integral part of these consolidated interim condensed financial information.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 1 General Information

Integra Group ("Integra"), together with its consolidated subsidiaries (collectively the "Group"), engage in the manufacture of drilling tools and equipment and in the provision of drilling, workover, formation evaluation and other oilfield services to the petroleum industry in the Russian Federation, in the Ukraine, Kazakhstan and Uzbekistan. The Group also has certain procurement and management activities in the United States of America and some of the Group's holdings are registered in Cyprus.

Integra was incorporated in the Cayman Islands on 15 March 2004. Since inception, management of the Group have completed numerous acquisitions as part of their strategy to become a leader in the oilfield services and oil and gas equipment manufacturing business in the Russian Federation and Commonwealth of Independent States ("CIS").

As discussed in Note 2, in February 2007, the Group completed an initial public offering of its shares.

Following are the principal operating subsidiaries of the Group at 30 June 2007 and 31 December 2006. Certain subsidiaries that provide only administrative functions are not presented. Segment information is provided in Note 6. Acquisitions during the period are discussed in Note 5.

| | Effective ownership at: | |
|---|---|---|
| | 30 June 2007 | 31 December 2006 |
| ***Drilling, workover and integrated project management*** | | |
| SE Management LLC | 100.0% | 100.0% |
| DP Smith Ukraine | 100.0% | 100.0% |
| Smith Overseas Services LLC | 100.0% | 100.0% |
| Smith Siberian Services LLC | 100.0% | 100.0% |
| Smith Production Technology LLC | 100.0% | 100.0% |
| Smith Drilling Services LLC | 100.0% | 100.0% |
| Smith Eurasia Limited | 100.0% | 100.0% |
| OOO Integra-Drilling | 100.0% | - |
| ZAO First National Drilling Company ("PNBK") | - | 100.0% |
| OOO Argillit | - | 100.0% |
| OOO PBN Group ("PBN") | 99.98% | 99.98% |
| OOO VNIIBT Drilling Instruments ("VNIIBT-BI") | 100.0% | 100.0% |
| OAO Pavlovsky Factory ("PMZ") | 90.8% | 90.8% |
| OAO NPO Drilling Technique ("NPO BT") | 55.9% | 55.9% |
| ZAO NPP Neftegaztechnika ("NGT-M") | 42.5% | 42.5% |
| OOO Orenburgtechservice ("OTS") | 100.0% | 100.0% |
| OOO BK Alliance ("Alliance") | 100.0% | 100.0% |
| OOO Alliance 3 ("Alliance 3") | 100.0% | 100.0% |
| OOO Alliance 5 ("Alliance 5") | 100.0% | 100.0% |
| OOO Paritet ("Paritet") | 100.0% | 100.0% |
| OOO Tarpan ("Tarpan") | 100.0% | 100.0% |
| OOO Burovaya Kompaniya Sever ("BKS") | - | 100.0% |
| OOO Integra KRS ("Integra KRS") | - | 100.0% |
| ***Formation Evaluation*** | | |
| OAO Yamalgeophysika ("YGF") | 52.9% | 50.7% |
| OOO Geophyzservice ("GFS") | 95.3% | 95.3% |
| OAO Russian Geophysical Company ("RGK") | 100.0% | 100.0% |
| OAO Purgeophysics ("PGF") | 57.2% | 57.2% |
| OAO Tyumenneftegeophysika ("TNGF") | 75.0% | 75.0% |
| JSC Azimuth Energy Services ("Azimuth") | 94.1% | 94.1% |
| OOO Tomsk Geophysical Company ("TGK") | 100.0% | 100.0% |
| JSC Geostan | 99.5% | 99.5% |
| OOO Yuganskpromgeophyzika ("YPGF") | 95.3% | 95.3% |
| ***Manufacturing*** | | |
| ZAO Uralmash VNIIBT | 100.0% | 100.0% |
| ZAO Uralmash Drilling Equipment ("URBO") | 100.0% | 100.0% |
| OAO Concern Stromneftemash | 100.0% | 100.0% |

In April 2007, the Group merged OOO Argillit, BKS, Integra KRS into Integra-Drilling, an entity created upon the reorganization of PNBK.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 1 General Information (Continued)

NGT-M is a 76 percent-owned subsidiary of NPO-BT. The Group exercises control over NGT-M by virtue of its control over NPO-BT.

Principal equity associates of the Group as of 30 June 2007 and 31 December 2006 were as follows:

| | | Effective ownership at: | |
|---|---|---|---|
| **Entity** | **Nature of activities** | **30 June 2007** | **31 December 2006** |
| OAO Nizhnevartovskgeophysika ("NNGF") | Formation evaluation services | 29.0% | 29.0% |
| OAO Stavropolneftegeophysika ("SNGF") | Formation evaluation services | 25.4% | 25.4% |
| ZAO Neftegeotechnology ("NGT-G") | Formation evaluation services | 59.3% | 59.3% |

The Group's investment in NGT-G is accounted for as an associate, because NGT-G is a subsidiary of NNGF, which is not controlled by the Group.

***Seasonality.*** The Group's drilling service revenues can be negatively affected by severe winter weather conditions in certain regions and by winter thawing since large volumes of drilling equipment and drilling rigs situated in certain regions can only be transported during winter when the ground is sufficiently frozen to create access roads. There is also a limited season for providing seismic services in certain Siberian regions of the Russian Federation as due to flood-like conditions from winter thawing. Such conditions generally restrict the provision of seismic services in Siberia from December to April.

## 2 Initial Public Offering

In February 2007, the Group completed its Initial Public Offering ("IPO" or "Offering") of 1,492,537 Class A common shares on the London Stock Exchange ("LSE") in the form of 29,850,740 Global Depository Receipts ("GDRs"), each with a nominal value of 0.0001 per common share and one common share representing twenty GDRs. In addition, the Group issued 299,139 common shares in the form of 5,982,780 GDRs to cover over allotments in the offering. The offering was priced at $335.00 per common share or $16.75 per one GDR. The over-allotment option was utilized in full at the offering.

From both the IPO and over-allotment, the Group raised $600.2 million of cash consideration, gross of $29.6 million of fees charged at the offering. Additionally, the shareholders' equity was reduced by $11.3 million of transaction costs directly related to the IPO.

Using the proceeds from the IPO, the Group repaid $199.6 million of short-term borrowings and $195.0 million of long-term borrowings outstanding at 31 December 2006. Management believes that the Group has sufficient resources to meet its operational, financing and investment needs. For the six months ended 30 June 2007, the Group reported a net cash inflow from operating activities of $70.7 million and at 30 June 2007, the Group had a net working capital surplus of $280.5 million. Accordingly, management believes that a going concern basis for the preparation of these consolidated interim condensed financial statements is appropriate.

## 3 Basis of Presentation

These consolidated interim condensed financial statements have been prepared in accordance with the International Accounting Standard 34 *Interim Financial Reporting* ("IAS 34"). These financial statements should be read together with the consolidated financial statements for the year ended 31 December 2006 prepared in accordance with International Financial Reporting Standards ("IFRS").

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 3 Basis of Presentation (Continued)

The United States Dollar ("$") is the presentation currency for the Group's consolidated operations. Management have used the US Dollar to manage most financial risks and exposures, agree terms for acquisitions and to measure performance of the Group. Management has concluded that the functional currency of Integra Group, the parent company, is the US Dollar. The functional currency of most other Group entities is the Russian Rouble. For subsidiaries whose functional currency is other than the US Dollar, balance sheet items have been translated into US Dollars using the exchange rate at the respective balance sheet date. The income statement items were translated into US Dollars using the exchange rates at the respective transaction dates or using a period average exchange rate as an approximation. The exchange differences resulting from the translation of assets, liabilities and the net result for the period from functional currency to US Dollars were included within cumulative translation adjustment in the statement of changes in shareholders' equity.

The US Dollar to Russian Rouble exchange rate was 25.82, 26.33 and 27.08 as of 30 June 2007, 31 December 2006 and 30 June 2006, respectively.

***Change in the Group balances as of 31 December 2006.*** During the six months ended 30 June 2007, the Group performed fair valuation of Azimuth's property plant and equipment, intangible and other assets and liabilities at the date of acquisition in December 2006. As a result, the fair values of Azimuth's net assets acquired by the Group increased by $10,755,000 from $19,425,000 to $30,180,000 with an associated decrease in goodwill from the acquisition from $17,133,000 to $6,378,000.

The details of the changes in the purchase accounting are as follows:

| | **31 December 2006 As previously reported** | **Fair value amendments** | **31 December 2006 Revised** |
|---|---|---|---|
| Cash and cash equivalents | 2,805 | - | 2,805 |
| Trade and other receivables | 5,539 | 2,251 | 7,790 |
| Inventories | 2,405 | (3) | 2,402 |
| Other current assets | 2,803 | (2,129) | 674 |
| Property, plant and equipment | 18,246 | 13,013 | 31,259 |
| Intangible assets | 1,292 | 3,551 | 4,843 |
| Short-term borrowings | (761) | - | (761) |
| Other current liabilities | (7,135) | (70) | (7,205) |
| Long-term borrowings | (4,555) | - | (4,555) |
| Deferred tax liability | (114) | (5,378) | (5,492) |
| Less: minority interest not acquired | (1,100) | (480) | (1,580) |
| Share in net assets (liabilities) acquired | 19,425 | 10,755 | 30,180 |
| Purchase consideration | 36,558 | - | 36,558 |
| **Goodwill** | **17,133** | **(10,755)** | **6,378** |

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 3 Basis of Presentation (Continued)

As a result of the changes in the fair values of Azimuth's assets and liabilities the Group's balance sheet as of 31 December 2006 changed as follows:

| | 31 December 2006 As previously reported | Fair value amendments | 31 December 2006 Revised |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents | 87,821 | - | 87,821 |
| Trade and other receivables | 233,526 | 2,251 | 235,777 |
| Inventories | 100,187 | (3) | 100,184 |
| Goodwill and other intangible assets | 347,206 | (7,204) | 340,002 |
| Property, plant and equipment | 411,630 | 13,013 | 424,643 |
| Investments in associates | 15,375 | - | 15,375 |
| Deferred tax assets | 1,925 | - | 1,925 |
| Loans provided and other assets | 36,460 | (2,129) | 34,331 |
| **Total assets** | **1,234,130** | **5,928** | **1,240,058** |
| **Liabilities and shareholders' equity** | | | |
| Accounts payable and accrued liabilities | 254,703 | 70 | 254,773 |
| Income taxes payable | 18,425 | - | 18,425 |
| Other taxes payable | 22,689 | - | 22,689 |
| Short-term borrowings and current portion of long-term borrowings | 340,421 | - | 340,121 |
| Long-term financial liabilities | 246,089 | - | 246,089 |
| Deferred tax liability | 73,868 | 5,378 | 79,246 |
| Other non-current liabilities | 1,601 | - | 1,601 |
| Total equity attributable to Integra Group shareholders | 198,456 | - | 198,456 |
| Minority interest | 77,878 | 480 | 78,358 |
| **Total liabilities and equity** | **1,234,130** | **5,928** | **1,240,058** |

There were no significant adjustments related to purchase accounting other than Azimuth.

***Purchase of minority interest.*** On acquisition of shares from minority interests the share of the net assets acquired is measured at historical amount based on the fair valuation of net assets made when the subsidiary was consolidated into the Group. The difference between the acquisition cost and the value of the share of net assets acquired is recognized in the consolidated statements of income.

***Critical estimates and judgments.*** Management makes estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes judgements, apart from those involving estimates, in the process of applying the accounting policies. Judgments that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities are outlined below.

***Fair values of acquired assets and liabilities.*** During 2005 and 2006, the Group completed numerous significant acquisitions. IFRS 3 requires that, at the date of acquisition, all assets and liabilities, including intangible assets, of an acquired entity be recorded at their respective fair values. The estimation of fair values requires significant management judgment.

## 3 Basis of Presentation (Continued)

***Fair values of acquired assets and liabilities (continued).*** To assess fair values of monetary assets and liabilities management uses all information available to determine whether an asset is recoverable or whether it is probable that an event will result in outflows of resources from the Group, including assessment of such factors as the current overall economic conditions, specific customer, counterparty or industry conditions and the current overall legal environment. Changes in any of these conditions may result in adjustments to fair values of monetary assets and liabilities recorded by the Group.

Management also engaged independent experts to advise as to the fair values of acquired property, plant and equipment and intangible assets. Changes in any of the estimates subsequent to the finalization of acquisition accounting may result in losses in future periods.

The Group determines the fair values of identifiable assets, liabilities and contingent liabilities for acquired companies provisionally and recognises any adjustments to those provisional values as a result of completing the initial accounting within twelve months of the acquisition date. Upon the completion of the initial accounting the comparative information presented for the periods before the initial accounting for the business combination is complete will be presented as if the initial accounting had been completed from the acquisition date.

***Estimated impairment of goodwill.*** The Group tests goodwill for impairment at least annually. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of estimates about the future profitability of cash-generating units to which goodwill have been allocated.

***Useful lives of property, plant and equipment.*** Items of property, plant and equipment are stated net of accumulated depreciation. The estimation of the useful life of an item of property, plant and equipment is a matter of management judgment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, residual value, physical wear and tear and the environment in which the asset is operated.

***Deferred income tax asset recognition.*** Deferred tax assets represent income taxes recoverable through future deductions from taxable profits. Deferred income tax assets are recorded on the Group's consolidated balance sheets to the extent that realisation of the related tax benefits is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future, management makes judgements and applies estimates based on recent years' taxable profits and expectations of future taxable income.

***Assessment of the percentage of completion on services or construction contracts.*** Certain of the Group's revenue is recognized under the percentage of completion method. The estimation of the extent of revenue to be recognized under the percentage of completion method is a matter of management judgment based upon expectations of future costs to be incurred to complete the respective contracts. Differences between such estimate and actual results may result in losses in future periods.

***Fair values of financial instruments.*** Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price. The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies where no market information is available. However, judgement is necessarily required to interpret market data to determine the estimated fair value.

***Estimation of share-based compensation*** The Group applies the Black-Scholes option valuation model to determine the fair value of traded options that have no vesting restrictions and are fully transferable. This option valuation model requires the input of highly subjective assumptions including the expected stock price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate.

## 4 Summary of Significant Accounting Policies

The principal accounting policies followed by the Group are consistent with those disclosed in the consolidated financial statements for the year ended 31 December 2006.

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2008 or later periods and which the Group has not early adopted.

***IAS 23, Borrowing Costs (revised March 2007; effective for annual periods beginning on or after 1 January 2009).*** The Standard will eliminate the option of recognizing the borrowing costs immediately as an expense to the extent that they are directly attributable to the acquisition, construction or production of a qualifying asset. An entity is, therefore, required to capitalize such borrowing costs as part of the cost of the asset. The revised Standard applies prospectively to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after 1 January 2009. Management believes that the adoption of this standard will not have a significant impact on the Group's financial statements.

***IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009).*** The Standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information. Management believes that the adoption of this standard will not have a significant impact on the Group's financial statements.

***Other new standards or interpretations.*** The Group has not early adopted the following other new standards or interpretations:

- IFRIC 11, IFRS 2 - Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008);
- IFRIC 13, Customer Loyalty Programmes (effective for annual periods beginning on or after 1 July 2008);
- IFRIC 14, IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective for annual periods beginning on or after 1 January 2008).

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Group's financial statements.

***Initial application of new standards and interpretations from 2007.*** From 2007, the Group adopted new standards and interpretations:

- IFRS 7, *Financial Instruments: Disclosures* and a Complementary Amendment to IAS 1, *Presentation of Financial Statements - Capital Disclosures* (effective from 1 January 2007);
- IFRIC 7, *Applying the Restatement Approach under IAS 29* (effective for annual periods beginning on or after 1 March 2006);
- IFRIC 8, *Scope of IFRS 2* (effective for annual periods beginning on or after 1 May 2006);
- IFRIC 9, *Reassessment of Embedded Derivatives* (effective for annual periods beginning on or after 1 June 2006);
- IFRIC 10, *Interim Financial Reporting and Impairment* (effective for annual periods beginning on or after 1 November 2006).

Management believes that the adoption of these standards and interpretations will not have a significant impact on the Group's financial statements.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 5 Business Combinations

***Acquisition of New Leasing Company.*** In February 2007, the Group completed the acquisition of a 100 percent interest in New Leasing Company ("NLK"), a company providing production equipment under lease agreements to certain companies of the Group, for total consideration of $3,646,000. No transaction costs were incurred on the acquisition. NLK is included within the Group's formation evaluation segment. The Group recognized a gain, in the amount of $91,000, as a result of the excess of management's preliminary assessment of the fair value of net assets acquired over the actual purchase price. It is not practicable to disclose NLK's carrying value of its assets, liabilities and contingent liabilities immediately before the acquisition, as NLK had not previously prepared its financial statements in accordance with IFRS. From the acquisition date to 30 June 2007, NLK contributed $193,000 of net profits to the Group.

***Fair values of NLK at date of acquisition.*** Below is a summary of the purchase accounting allocation for the acquisition of NLK at the date of acquisition. Amounts for the acquisition are based upon management's preliminary estimates of the fair values.

| | **Total** |
|---|---|
| Cash and cash equivalents | 41 |
| Trade and other receivables | 2,349 |
| Property, plant and equipment | 1,828 |
| Short-term borrowings | (38) |
| Deferred tax liability | (443) |
| Less: minority interest not acquired | - |
| Share in net assets (liabilities) acquired | 3,737 |
| Purchase consideration | 3,646 |
| **Excess of fair value of net assets acquired over purchase price** | **91** |

***Summary combined financial information (unaudited).*** The following table sets forth summary combined financial information for the six months ended 30 June 2007 and is presented to provide information to evaluate the financial effects of the acquisition of NLK, as if it had occurred on 1 January 2007. Adjustments have been made to eliminate post-acquisition results for the acquisition that are included both in the Group's and in NLK's results, inter-company transactions and to adjust depreciation and amortization expense to reflect adjusted carrying values of property, plant and equipment and intangibles assets following fair value adjustments and the associated income tax effects.

| | **Total revenues** | **Profit (loss)** |
|---|---|---|
| Group | 487,892 | (51,542) |
| ***Subsidiaries acquired prior to 30 June 2007*** | | |
| NLK | 662 | 431 |
| Adjustments and eliminations | (217) | (193) |
| **Summary combined** | **488,337** | **(51,304)** |

The summary combined financial information should not be construed to represent consolidated financial information. Specifically, no adjustments have been made for financing transactions or any other arrangements associated with the NLK acquisition. The profit adjustment of $193,000 represents elimination of post-acquisition results that were included in both the Group and NLK totals. The revenue adjustment of $217,000 represents elimination of post-acquisition revenues that were included in both the Group and NLK totals.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 5 Business Combinations (Continued)

***Acquisition of additional interest in Yamalgeophyzika.*** In February 2007, the Group purchased an additional 2.15 percent interest in YGF for $1,758,000, which brought the Group's total cost of investment in YGF to $79,806,000, representing 52.89 percent of effective ownership of YGF's shares. The Group has been consolidating YGF since the date of acquisition of control of a 50.74 percent interest in YGF in August 2006. The acquisition of the additional 2.15 interest in YGF resulted in a gain of $506,000 from the excess of the carrying value of net assets acquired over the purchase price, which is recognized in the Group consolidated statement of income for the six months ended 30 June 2007.

## 6 Segment Information

The Group organizes its operational activities into the following three reportable segments: drilling, workover and integrated project management ("IPM"), manufacturing and formation evaluation. The Group's drilling, workover and integrated project management segment manufactures drilling tools and provides a wide variety of services including rig up work, mud system services, rig and drill bit management, well cementing and completing, maintenance and capital workovers, chemical treatment, well preparation and completion work. The formation evaluation segment provides both well and field geophysical services including logging, perforation and 2D and 3D seismic data acquisition, processing and interpretation. The manufacturing segment comprises URBO, which was acquired in September 2005, and Strommachina and manufactures heavy oil and gas drilling rigs and other equipment. Corporate assets, liabilities and expenses such as certain administrative assets, general and administrative expenses and borrowings represent activities that cannot be directly allocated to the Group's primary operating segments. At 30 June 2007 and 31 December 2006, the Group operated substantially within one geographical segment which is the Russian Federation and CIS.

Segment information for the six months ended 30 June 2007 and 2006 was as follows:

| Six months ended 30 June 2007: | Drilling, workover and IPM | Formation evaluation | Manufacturing | Other | Total |
|---|---|---|---|---|---|
| Sales | 270,103 | 143,981 | 94,506 | (20,698) | 487,892 |
| Cost of sales | (228,047) | (120,320) | (73,619) | 21,287 | (400,699) |
| **Gross profit** | **42,056** | **23,661** | **20,887** | **589** | **87,193** |
| Selling, general and administrative expenses | (36,470) | (19,684) | (15,405) | (23,860) | (95,419) |
| Other operating incomes (expenses) | 377 | 418 | (3) | 61 | 853 |
| **Operating profit (loss)** | **5,963** | **4,395** | **5,479** | **(23,210)** | **(7,373)** |
| Interest expense, net | (10,873) | (4,715) | (912) | (18,519) | (35,019) |
| Other incomes (expenses) | 144 | 1,293 | 29 | (1,010) | 456 |
| **(Loss) profit before taxation** | **(4,766)** | **973** | **4,596** | **(42,739)** | **(41,936)** |
| Total tax expense | (5,952) | (510) | (1,452) | (1,692) | (9,606) |
| **(Loss) profit for the period** | **(10,718)** | **463** | **3,144** | **(44,431)** | **(51,542)** |

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 6 Segment Information (Continued)

| **Six months ended 30 June 2006:** | **Drilling, workover and IPM** | **Formation evaluation** | **Manufacturing** | **Other** | **Total** |
|---|---|---|---|---|---|
| Sales | 99,165 | 44,426 | 34,532 | (1,723) | 176,400 |
| Cost of sales | (77,795) | (39,173) | (24,018) | 1,917 | (139,069) |
| **Gross profit** | **21,370** | **5,253** | **10,514** | **194** | **37,331** |
| Selling, general and administrative expenses | (12,747) | (4,310) | (2,650) | (11,895) | (31,602) |
| Gain on disposal of subsidiaries | 225 | - | - | - | 225 |
| **Operating profit (loss)** | **8,848** | **943** | **7,864** | **(11,701)** | **5,954** |
| Interest (expense) income, net | (3,737) | (896) | (168) | (10,880) | (15,681) |
| Other incomes | 123 | 776 | 186 | 6,539 | 7,624 |
| **Profit (loss) before taxation** | **5,234** | **823** | **7,882** | **(16,042)** | **(2,103)** |
| Total tax (expense) benefit | (1,441) | (309) | (1,933) | 1,196 | (2,487) |
| **Profit (loss) for the period** | **3,793** | **514** | **5,949** | **(14,846)** | **(4,590)** |

Segment information at 30 June 2007 and 31 December 2006 was as follows:

| | **Drilling, workover and IPM** | **Formation evaluation** | **Manufacturing** | **Other** | **Total** |
|---|---|---|---|---|---|
| **At 30 June 2007:** | | | | | |
| Total assets | 744,812 | 410,799 | 324,555 | 62,711 | 1,542,877 |
| Total liabilities | 515,113 | 159,925 | 220,777 | (183,555) | 712,260 |
| **Six months ended 30 June 2007:** | | | | | |
| Additions to non-current assets | 42,863 | 11,779 | 2,229 | - | 56,871 |
| Depreciation and amortization | 37,071 | 25,701 | 4,392 | 297 | 67,461 |

| | **Drilling, workover and IPM** | **Formation evaluation** | **Manufacturing** | **Other** | **Total** |
|---|---|---|---|---|---|
| **At 31 December 2006:** | | | | | |
| Total assets | 607,752 | 442,098 | 252,560 | (62,352) | 1,240,058 |
| Total liabilities | 381,422 | 195,483 | 144,989 | 241,350 | 963,244 |
| **Six months ended 30 June 2006:** | | | | | |
| Additions to non-current assets | 50,519 | 9,054 | 423 | - | 59,996 |
| Depreciation and amortization | 5,316 | 5,827 | 4,689 | 105 | 15,937 |

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 7 Cost of Sales

| | Six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| Materials and supplies | 102,906 | 48,735 |
| Employee costs (including mandatory social contributions of $17.1 million and $8.0 million for six months ended 30 June 2007 and 2006, respectively) | 120,617 | 39,224 |
| Depreciation and amortization | 63,784 | 15,601 |
| Services | 110,112 | 33,994 |
| Other | 3,280 | 1,515 |
| **Total cost of sales** | **400,699** | **139,069** |

## 8 Selling, General and Administrative Expenses

| | Six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| Employee costs (including unified social tax of $5.5 million and $0.3 million for the periods ended 30 June 2007 and 2006, respectively) | 38,677 | 14,694 |
| Services | 26,129 | 8,201 |
| Share options granted | 16,075 | 3,005 |
| Transportation expenses | 2,501 | 327 |
| Taxes other than income | 4,147 | 866 |
| Depreciation | 3,677 | 336 |
| Other | 4,213 | 4,173 |
| **Total selling, general and administrative expenses** | **95,419** | **31,602** |

## 9 Construction Contracts

The revenues and gross margins recognised on long-term construction contracts for the six months ended 30 June 2007 were as follows:

| | Six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| Construction revenues | 70,159 | 31,070 |
| Construction costs | (53,903) | (21,674) |
| **Gross profit** | **16,256** | **9,396** |

The aggregate amount of costs incurred on construction contracts that were in progress at 30 June 2007 and 31 December 2006 was $75,203,000 and $53,551,000, respectively. During six months ended 30 June 2007 and 2006, the Group recognised aggregate gross profits of $14,274,000 and $15,573,000, respectively less losses of $608,000 and nil, respectively, for contracts that were in progress at 30 June 2007 and 2006, respectively.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 10 Trade and Other Receivables

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Trade receivables (net of allowances for doubtful accounts of $2.0 million and $0.9 million at 30 June 2007 and 31 December 2006, respectively) | 173,017 | 120,882 |
| Amounts due from customers for contract work | 24,228 | 25,089 |
| VAT recoverable | 36,925 | 16,940 |
| Advances to suppliers | 66,204 | 31,424 |
| Prepaid expenses and other receivables | 45,914 | 41,442 |
| **Total trade and other receivables** | **346,288** | **235,777** |

At 30 June 2007, advances to suppliers includes prepayments in the amount of $20,787,000 made by the Group to third parties for supplies and services to fulfil the Group's obligation to construct drilling rigs for one of its major customers (Note 16).

## 11 Inventories

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Materials and supplies (net of allowances for obsolete materials of $3.2 million and $2.7 million at 30 June 2007 and 31 December 2006, respectively) | 98,124 | 65,978 |
| Work in progress | 13,230 | 14,493 |
| Finished goods | 19,893 | 19,713 |
| **Total inventories** | **131,247** | **100,184** |

At 30 June 2007 and 31 December 2006, inventories with carrying values of nil and $3,358,000, respectively, were pledged as collateral for the Group's borrowings.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 12 Goodwill and Other Intangible Assets

At 30 June 2007 and 31 December 2006, the net book value of goodwill and other intangible assets was as follows:

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Goodwill from acquisition of subsidiaries, including: | | |
| - PNBK | 85 | 84 |
| - Argillit | 217 | 213 |
| - STM | 5,546 | 5,437 |
| - PBN | 11,312 | 11,092 |
| - Smith Eurasia | 71,948 | 70,541 |
| - YGF | 24,218 | 23,745 |
| - Azimuth | 6,508 | 6,378 |
| - URBO | 8,394 | 8,230 |
| - BI | 10,541 | 10,335 |
| - Other | 474 | 471 |
| **Total goodwill** | **139,243** | **136,526** |
| Other intangible assets, including: | | |
| - Long-term customer/supplier relationships | 158,392 | 169,516 |
| - Trademarks | 11,274 | 12,342 |
| - Patents | 3,766 | 3,865 |
| - Software | 3,235 | 3,159 |
| - Order backlog | 8,695 | 13,790 |
| - Other | 764 | 804 |
| **Total other intangible assets** | **186,126** | **203,476** |
| **Total goodwill and other intangible assets** | **325,369** | **340,002** |

***Goodwill.*** The Group concluded that none of its assets are impaired at 30 June 2007 in accordance with IAS 36.

***Other intangible assets.*** All other intangible assets are assessed as having finite useful lives.

The intangible assets associated with long-term customer/supplier relationships amortized over the period which the Group expects the assets will generate economical benefits as follows:

| Entity | Long-term customer/supplier relationship | Remaining amortization period, years |
|---|---|---|
| PBN | 13,498 | 4.5 |
| PNBK | 8,689 | 5.5 |
| STM | 12,550 | 3.5 |
| Smith Eurasia | 62,456 | 5.5 |
| YGF | 58,998 | 9.5 |
| Azimuth | 2,201 | 3.5 |
| **Total long-term customer/supplier relationship** | **158,392** | |

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 13 Property, Plant and Equipment

| | Rigs | Buildings | Plant and equipment | Motor vehicles | Other | Total |
|---|---|---|---|---|---|---|
| *Cost* | | | | | | |
| **Balance at 31 December 2006** | **73,339** | **103,371** | **245,576** | **46,867** | **17,424** | **486,577** |
| Additions | 13,540 | 1,488 | 30,604 | 6,307 | 4,932 | 56,871 |
| Acquisitions of subsidiaries | - | - | 1,828 | - | - | 1,828 |
| Disposals | (1,274) | (357) | (1,611) | (226) | (1,725) | (5,193) |
| Exchange differences | 1,408 | 2,302 | 5,207 | 969 | 414 | 10,300 |
| **Balance at 30 June 2007** | **87,013** | **106,804** | **281,604** | **53,917** | **21,045** | **550,383** |
| *Accumulated depreciation* | | | | | | |
| **Balance at 31 December 2006** | **(15,062)** | **(5,637)** | **(32,912)** | **(6,019)** | **(2,304)** | **(61,934)** |
| Depreciation | (9,152) | (3,328) | (24,023) | (5,583) | (2,984) | (45,070) |
| Disposals | 345 | 41 | 981 | 99 | 1,184 | 2,650 |
| Exchange differences | (247) | (93) | (520) | (87) | (43) | (990) |
| **Balance at 30 June 2007** | **(24,116)** | **(9,017)** | **(56,474)** | **(11,590)** | **(4,147)** | **(105,344)** |
| ***Net book value*** | | | | | | |
| Balance at 31 December 2006 | 58,277 | 97,734 | 212,664 | 40,848 | 15,120 | 424,643 |
| Balance at 30 June 2007 | 62,897 | 97,787 | 225,130 | 42,327 | 16,898 | 445,039 |

At 30 June 2007 and 31 December 2006, certain property, plant and equipment with a net book value of $34,791,000 and $108,718,000, respectively, were pledged as collateral for the Group's borrowings.

## 14 Investments in Associates

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| NNGF | 10,656 | 9,701 |
| SNGF | 3,319 | 2,644 |
| NGT-G | 2,428 | 2,381 |
| Yamal Fund | 592 | 649 |
| **Total investments in associates** | **16,995** | **15,375** |

***NNGF.*** The Group acquired its 25.4 percent interest in NNGF as part of its acquisition of RGK in May 2005.

***SNGF.*** The Group acquired its 6.22 percent interest in SNGF as part of its acquisition of RGK in May 2005. In May 2005, the Group purchased an additional 19.18 percent interest for $598,000, bringing its total stake to 25.4 percent.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 14 Investments in Associates (Continued)

*NGT-G.* In May 2005 the Group acquired its 12.95 percent of effective interest in NGT-G through its ownership of NNGF and its 49.0 percent of effective interest in NGT-G through its acquisition of GFS. In February 2006 the Group reduced its effective interest in NGT-G to 44.8 percent through its holding of GFS by transferring its 100 percent interest in GFS to YPGF in exchange for 91.4 percent interest in YPGF. The Group recognized a loss of $271,000 from the transaction within share of results of associates.

***Yamal Fund.*** The Group assumed its 32.5 percent interest in Yamal Fund on its acquisition of YGF in August 2006.

Movements in the carrying value of the Group's investments in associates are summarized in the table below.

| | **Six months ended 30 June:** | |
|---|---|---|
| | **2007** | **2006** |
| Carrying amount at the beginning of the period | 15,375 | 13,913 |
| Share of results of associates | 1,352 | 335 |
| Distributions received | - | (75) |
| Exchange differences | 268 | 958 |
| **Carrying amount at the end of the period** | **16,995** | **15,131** |

Summarized balance sheet information of the Group's associates is provided in the table below:

| | **30 June 2007** | **31 December 2006** |
|---|---|---|
| Total assets | 64,349 | 53,853 |
| Total liabilities | 18,197 | 14,430 |

Summarized income statement information of the Group's associates is provided in the table below:

| | **Six moths ended 30 June:** | |
|---|---|---|
| | **2007** | **2006** |
| Total revenues | 35,304 | 22,913 |
| Total operating expenses | (29,531) | (21,137) |
| Operating profit | 5,773 | 1,776 |
| Interest expense, net | (37) | (136) |
| Income tax expense | (1,634) | (470) |
| Minority share | 2 | - |
| **Profit for the period** | **4,104** | **1,170** |

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 15 Loans Provided and Other Assets

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Advances to third parties | 31,332 | 26,094 |
| Loans receivable (net of allowance for doubtful accounts of $0.9 million at 30 June 2007 and 31 December 2006, respectively) | 5,778 | 4,854 |
| Other assets | 7,895 | 3,383 |
| **Total loans provided and other assets** | **45,005** | **34,331** |

***Advances to third parties.*** The advances to third parties relate to purchase of minority interest share in the Group's subsidiaries as follows:

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| YGF | 27,469 | 23,843 |
| Other | 3,863 | 2,251 |
| **Total advances to third parties** | **31,332** | **26,094** |

***Advances to purchase YGF's minority interest.*** The advances were provided to third parties to assist in the identification and purchase of minority interests share in YGF not already owned by the Group. Some of the advances were provided in the form of short-term loans bearing interest at a rate of 14 percent per annum and maturing in December 2007. In February 2007, advances amounting to $1,758,000 were offset off by the third parties in exchange for shares representing the interest in YGF of 2.15 percent. In March 2007, the Group advanced a further $2,382,000 to third parties. At 30 June 2007 the total balance of outstanding advances of $27,469,000 includes interest of $3,002,000.

At 30 June 2007, the third parties represented that they controlled a 49.95 percent interest in YGF to a total of $29,494,000, comprised of $27,469,000 in outstanding advances and $2,025,000 of YGF shares pledged to the Group. The cost of the pledged shares is recognized as part of the Group's cost of acquisition of YGF.

***Loans receivable.*** Included within loans receivables are loans to employees of $1,353,000 and $1,020,000 at 30 June 2007 and 31 December 2006, respectively. The loans are further described in Note 22. Other loans have weighted average rates ranging from 11.0 to 14.5 percent per annum.

## 16 Accounts Payable and Accrued Liabilities

| | 30 June 2007 | 31 December 2006 |
|---|---|---|
| Trade payables | 97,794 | 117,731 |
| Amounts due to customers for contract work | 15,178 | 13,463 |
| Accrued liabilities and other creditors | 50,803 | 83,271 |
| Advances from customers | 197,849 | 40,308 |
| **Total accounts payable and accrued liabilities** | **361,624** | **254,773** |

At 30 June 2007, advances from customers include prepayments made by one of the Group's major customers in the amount of $122,352,000 for construction of drilling rigs.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 17 Taxes

***Reconciliation of income taxes.*** The table below reconciles actual income tax expense and theoretical income tax, determined by applying the Russian statutory income tax rate to income before income tax and minority interest.

| | Six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| (Loss) profit before taxation | (41,936) | (2,103) |
| Theoretical tax benefit (charge) at Russian statutory income tax rate of 24 percent | 10,065 | 505 |
| Gain on disposal/acquisition of subsidiaries and minority interest in subsidiaries | 143 | 54 |
| Effect of income (loss) taxed at rates lower than 24 percent | 3,920 | 375 |
| Effect of income (loss) taxed at rates higher than 24 percent | (786) | - |
| Tax losses not expected to be utilized against future profits from overseas activities | (7,210) | (1,161) |
| Tax losses not expected to be utilized against future profits from domestic activities | (6,310) | (755) |
| Share-based compensation | (3,858) | (721) |
| Other non-tax deductible expenses | (5,512) | (850) |
| Other | (58) | 66 |
| **Total income tax expense** | **(9,606)** | **(2,487)** |

Taxes losses not expected to be utilized against future profits relate primarily to interest expense and other administrative expenses recorded in the Group's different holding entities where management does not anticipate sufficient taxable profits through which it may realize tax benefits for its expenses. The Group neither pays tax on income nor receives tax benefits for expenses incurred in its overseas subsidiaries. For expenses incurred in the Group's overseas entities, management does not anticipate sufficient taxable profits through which it may realize tax benefits for its expenses.

***Other taxes payable.*** Current taxes payable at 30 June 2007 and 31 December 2006 are detailed below.

| | **30 June 2007** | **31 December 2006** |
|---|---|---|
| Unified social tax | 3,277 | 3,041 |
| Personal income tax | 582 | 2,407 |
| Value-added tax | 17,916 | 13,867 |
| Property tax | 696 | 803 |
| Other taxes | 4,457 | 2,571 |
| **Total other taxes payable** | **26,928** | **22,689** |

Included within VAT payable $2,771,000 and $4,422,000 at 30 June 2007 and 31 December 2006, respectively, of VAT that is only payable to the tax authorities when the underlying receivable is recovered or written off.

Deferred tax assets for tax losses carried forward are recognized when management believes it is probable that the Group will be able to utilize the losses to offset future tax profits. At 30 June 2007 and 31 December 2006, deferred tax assets related to such tax losses were nil. Additionally, at 30 June 2007 and 31 December 2006, deferred tax assets, that do not have an expiration date, totalling $13,520,000 and $14,166,000 were not recognized. Such deferred tax assets were not recognised as management does not believe that the recoverability of such assets is probable based upon current forecasts of profitability for the appropriate entities.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 18 Financial Liabilities

***Short-term borrowings.*** Below are tables detailing short-term borrowings and the current portion of long-term borrowings at 30 June 2007 and 31 December 2006. Subsequent to 31 December 2006, the Group repaid its short-term borrowings from Renaissance Securities Trading Limited, Sberbank and Alba-Alliance.

| | Weighted average effective interest rate at: | | Balance at: | |
|---|---|---|---|---|
| | **30 June 2007** | **31 December 2006** | **30 June 2007** | **31 December 2006** |
| US Dollar-denominated borrowings | - | 10.2% - 13% | - | 79,100 |
| Russian Rouble-denominated borrowings | 10.5% | 9.25% - 15.4% | 8,751 | 115,129 |
| Other | 9.0% - 13% | 13% | 576 | 193 |
| Current portion of long-term borrowings | | | 15,708 | 145,999 |
| **Total short-term borrowings and current portion of long-term borrowings** | | | **25,035** | **340,421** |

| | **30 June 2007** | **31 December 2006** |
|---|---|---|
| Renaissance Securities Trading Limited ("Renaissance") | - | 75,000 |
| Alfa-Bank | 8,751 | 75,959 |
| Sberbank | - | 17,546 |
| Alba-Alliance | - | 16,052 |
| Other | 576 | 9,865 |
| Current portion of long-term borrowings | 15,708 | 145,999 |
| **Total short-term borrowings and current portion of long-term borrowings** | **25,035** | **340,421** |

***Renaissance Securities Trading Limited ("Renaissance").*** In August 2006, the Group obtained a loan in the amount of $75,000,000 from Renaissance as a bridge loan becoming immediately payable upon an initial public offering of the Group's shares. The bridge loan initially bore fixed interest of 10.2 percent per annum due on the loan repayment date.

From October 2006 through December 2006, the Group entered into several borrowing arrangements without obtaining the required consent from Renaissance. As a result of that and other violations, in December 2006, the Group received a notification of default from Renaissance. In January 2007, the Group obtained a waiver from Renaissance for the covenant violations. Under the terms of the waiver, the Group paid a fee of $2,000,000 to Renaissance and the interest rate on the original borrowings was increased to 12.0 percent per annum, with retrospective effect to 1 October 2006. Additionally, the Group agreed to pay to Renaissance an additional fee equal to 12.5 percent of the total of all outstanding principal and interest in the event of an initial public offering of its shares. Accordingly, in February 2007, the Group paid full amount of debt, along with an additional fee of $10,596,000 as a result of its initial public offering.

This restructuring comprises a significant modification of terms as defined in IAS 39. Accordingly, management estimated the fair value of the loan from Renaissance as $91,079,000, calculated applying as an effective interest rate of its external borrowing rate for similar instruments of 10.2 percent. The Group recognized a loss of $12,420,000 on the restructuring of its arrangement with Renaissance, which is recorded in the 2007 consolidated statement of income.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 18 Financial Liabilities (Continued)

***Alfa-Bank.*** Between February and July 2006, the Group entered into a series of Russian Rouble-denominated loan facility agreements with Alfa-Bank totalling RR 2,000 million ($76.0 million at 31 December 2006). The loans bore fixed interest rates ranging from 9.5 percent to 10.5 percent per annum, payable monthly. At 30 June 2007 the outstanding balance was RR 225.9 million ($8.8 million) which bore fixed interest rate of 10.5 percent per annum payable monthly and was collateralized by certain of the Group's property, plant and equipment with carrying value of $3,883,000. The loan matures in February 2008. At 31 December 2006, the loan balance was collateralized by certain of the Group's inventories and property, plant and equipment with carrying value of $1,792,000 and $7,071,000, respectively.

***Sberbank.*** During 2006, the Group entered into and assumed through an acquisition Russian Rouble-denominated loan agreements with Sberbank totalling RR 462 million ($17.5 million) at 31 December 2006. The loans bore interest ranging between 9.0 and 10.5 percent per annum, payable monthly. The loans outstanding at 31 December 2006 were repaid in full during the six months ended 30 June 2007.

***Alba-Alliance loan.*** In December 2006, the Group entered into a Russian Rouble-denominated loan agreement with Alba Alliance bank totalling RR 423 million ($16.1 million) at 31 December 2006. The loan bore a fixed interest rate of 13.0 percent per annum, payable monthly. The loan was repaid in full in March 2007.

***Other.*** At 30 June 2007, other short-term borrowings of $0.6 million included Russian Rouble-denominated borrowings bearing fixed interest of ranging between 9.0 percent and 13.0 percent per annum. At 31 December 2006, other short-term borrowings of $9.9 million included US dollar-denominated borrowings of $0.2 million and Russian Rouble-denominated borrowings of RR 254 million ($9.7 million).

***Long-term borrowings.*** The Group's long-term borrowings at 30 June 2007 and 31 December 2006 are outlined below.

The fair values of the Group's long-term borrowings were estimated based upon rates available to the Group on similar instruments of similar maturities. At both 30 June 2007 and 31 December 2006, the carrying values of total long-term borrowings approximated their fair values.

During the six months ended 30 June 2007, the Group repaid in full the Senior Notes, the Restructured Senior Notes, the Facility Agreement, and its long-term borrowings from Sberbank, IMB and NOMOS-bank.

| | **30 June 2007** | **31 December 2006** |
|---|---|---|
| Senior Notes | - | 1,991 |
| Restructured Senior Notes | - | 15,472 |
| Facility Agreement | - | 96,748 |
| First Russian Rouble-denominated bonds | 77,471 | 75,484 |
| Second Russian Rouble-denominated bonds | 116,206 | 112,409 |
| Alfa-Bank | 15,708 | 40,796 |
| Sberbank | - | 14,345 |
| IMB | - | 11,644 |
| NOMOS-bank | - | 7,000 |
| Other | 12,957 | 11,029 |
| Subtotal | 222,342 | 386,918 |
| Less: current portion of long-term borrowings | (15,708) | (145,999) |
| **Total long-term borrowings** | **206,634** | **240,919** |
| Warrants | - | 5,170 |
| **Total long-term financial liabilities** | **206,634** | **246,089** |

## 18 Financial Liabilities (Continued)

***Senior Notes and Restructured Senior Notes.*** In May 2005, the Group issued unsecured Senior Notes to two investment funds totalling $14,500,000 and maturing in May 2008. The Senior Notes bore interest of 18.0 percent per annum due semi-annually on 31 May and 30 November.

In connection with the issuance of the Senior Notes, the Group issued 14,500 warrants to the holders to purchase 120,833 of the Group's Class A common shares for $20.00 per share. Management estimated the fair value of the warrants to be $136,000. This amount was recorded within equity in the Group's consolidated balance sheet, with a corresponding reduction in the carrying value of the Senior Notes. The difference between the carrying value and the par value of the Senior Notes was accreted over the term to maturity as interest expense at an effective interest rate of 18.0 percent.

In April 2006, the Group refinanced a portion of the Senior Notes with par values of $12,500,000. As a result of this refinancing, the new principal amount comprised of the initial principal amount of $12,500,000, an early prepayment premium amounting to $1,250,000, accrued interest amounting to $925,000 and additional cash provided by the holders of the Restructured Senior Notes amounting $325,000. Interest on the Restructured Senior Notes was due semi-annually on 30 April and 31 October.

The restructuring described above comprised a significant modification of terms as defined in IAS 39. Accordingly, management estimated the fair value of the Restructured Senior Notes and recorded a gain on extinguishment of liability of $676,000, included within interest income in the consolidated statement of income, by applying management's estimate of the Group's external borrowing rate for similar instruments, 13.0 percent. At 31 December 2006, the carrying value of the Restructured Senior Notes was $15,472,000. The difference between the carrying value and the face value of the Restructured Senior Notes was being accreted over the period to maturity at an effective interest rate of 13.0 percent.

Under the terms of both the Senior Notes and the Restructured Senior Notes, the Group was subject to certain covenants related to new borrowings and financial ratios. Additionally, the Restructured Senior Notes agreement contained cross-default provisions allowing holders of the Restructured Senior Notes to demand immediate payment in the event of a default in any of the Group's borrowings. As a result of the default with respect to the Group's borrowings from Renaissance described above, the entire balance of both the Senior Notes and the Restructured Senior Notes was classified within current liabilities in the Group's consolidated balance sheet at 31 December 2006. The Group did not incur any other consequences from the notes holders as a result of the default described above.

In March 2007, the Group repaid in full its debt on the Senior Notes and the Restructured Senior Notes. The total repayment amount of the Senior Notes of $2,269,000 included repayments of principal of $2,000,000, accrued interest of $99,000 and an early repayment fee of $170,000. The total repayment amount of the Restructured Senior Notes of $17,288,000 included principal of $15,856,000, accrued interest of $640,000 and an early repayment fee of $793,000.

***Facility Agreement.*** In September 2005, the Group entered into a $90,000,000 Facility Agreement with several different investment funds and financial institutions (collectively the "Lenders"). The Facility Agreement originally comprised of two separate $45.0 million tranches, Facility A and Facility B. Both Facility A and Facility B bore interest of 14.0 percent per annum payable semi-annually on 31 March and 30 September. Interest accrued on Facility B loan at the rate of 10.0 percent per annum was due in cash on each interest payment date. The balance of the 14.0 percent interest due on the Facility B loan and all of the 14.0 percent interest due on the Facility A loan may have been paid in cash or added to the outstanding balance of the respective loan at the option of the Group.

As part of its agreement with the Lenders under the Facility Agreement, the Group issued 90,000 warrants to the Lenders. Each warrant allowed its holder to purchase the Group's common shares in the event that the Group completes an initial public offering ("IPO") of its Class A shares, at a purchase price equal to a 25.0 percent discount to the listing price. Under the terms of the warrants, if exercised, the Group had the right to repurchase the warrants for a price per warrant which would aggregate to $5,250,000. As the number of shares to be issued upon exercise of the warrants was variable depending on the listing price, the estimated fair value of the warrants was recorded as a liability in the consolidated balance sheet and the carrying value of the Facility loans was reduced by a corresponding amount. In February 2007, the holders of 90,000 of the warrants exercised their rights and acquired 62,686 of the Group's Class A common shares for total proceeds of $15,750,000 (Note 19).

## 18 Financial Liabilities (Continued)

Under the Facility Agreement, the Group was subject to certain financial covenants and restrictions on borrowings as well as cross-default provisions allowing the lenders may have demanded immediate payment of all outstanding borrowings in the event of default in the Group's other borrowings. As a result of the default with respect to the Group's borrowings from Renaissance Securities Trading Limited described above, the entire balance of the Facility Agreement was classified within current liabilities in the Group's consolidated balance sheet at 31 December 2006 within the current portion of long-term borrowings. No other consequences occurred as a result of the default with respect to the Facility Agreement.

The Group repaid both facilities in full in March 2007. The total repayment amount of $108,000,000 included repayment of the principal outstanding amount of Facility A and Facility B of $51,727,000 and $46,874,000, accrued interest on Facility A and Facility B of $3,379,000 and $3,062,000, and a prepayment fee of 3.0 percent of the principal amounts of $2,958,000.

***First Russian Rouble-denominated Bonds.*** In March 2006, the Group issued Russian Rouble-denominated bonds with a total nominal value of RR 2.0 billion ($77.5 million at 30 June 2007) (the "First Russian Rouble-denominated Bonds"). The First Russian Rouble-denominated Bonds bear fixed interest of 10.5 percent per annum, payable semi-annually, and mature in March 2009.

***Second Russian Rouble-denominated Bonds.*** In December 2006, the Group issued Russian Rouble-denominated bonds with a total nominal value of RR 3.0 billion ($116.2 million at 30 June 2007) (the "Second Russian Rouble-denominated Bonds"). The bonds bear a fixed interest of 10.7 percent per annum, payable semi-annually, and mature in November 2011.

***Alfa-Bank.*** In June and October 2006, the Group entered into a series of Russian Rouble-denominated loan agreements with Alfa-Bank totalling RR 1,074 million ($40.8 million at 31 December 2006). The loan facilities bore interest rates ranging from 10.5 to 10.9 percent per annum. At 30 June 2007 two loans were outstanding with the total amount of RR 405 million ($15.7 million), both loans bear fixed interest rate of 10.5 percent per annum payable monthly and mature in December 2007. The loans are collateralized by certain of the Group's property, plant and equipment with carrying value equivalent to $30,908,000 and $70,180,000 at 30 June 2007 and 31 December 2006, respectively.

Under the terms of the agreements, the Group is subject to certain covenants, including restrictions of incurrence of new debt without consent of the lender and maintaining certain minimum balances at designated bank accounts. At 30 June 2007 and 31 December 2006, the Group was in compliance with the covenants.

***Sberbank.*** During 2006, through acquisition, the Group assumed two Russian Rouble-denominated loan agreements with Sberbank. The loans bore fixed interest of 10.5 percent per annum payable monthly. At 31 December 2006, RR 377 million ($14.3 million) was outstanding under the agreements. All the loans were repaid in full during the six months ended 30 June 2007.

***IMB.*** In December 2005, the Group entered into a Euro-denominated loan facility with International Moscow Bank (IMB) totaling Euro 7.8 million ($10.3 million at 31 December 2006). The loan bore a floating interest rate of EURIBOR plus 5.5 percent per annum payable monthly. In March 2006, through acquisition the Group assumed a US Dollar-denominated loan agreement with IMB for a maximum amount of $4.0 million. The loan bore a floating interest rate of LIBOR plus 6.5 percent per annum, payable monthly and was scheduled to mature in September 2007. As of 31 December 2006, $1,333,000 was outstanding under the loan. The Group fully repaid the loans in March 2007.

***NOMOS-bank.*** In March 2006, the Group entered into a US Dollar-denominated loan agreement with NOMOS-bank for $7.0 million. The loan bore a fixed interest rate of 12.0 percent per annum payable monthly, maturing in March 2009. In March 2007 the Group fully repaid the loan.

(expressed in US Dollars (tabular amounts in thousands), except as indicated)

## 18 Financial Liabilities (Continued)

***Maturities of the long-term borrowings.*** Long-term borrowings outstanding at 30 June 2007 have scheduled maturities as follows:

| *Scheduled maturities during the periods ended 30 June:* | |
|---|---|
| 2009 | 84,381 |
| 2010 | 3,455 |
| 2011 | 1,296 |
| 2012 | 117,502 |
| **Total long-term borrowings** | **206,634** |

***Interest expense.*** Interest expense for the six months ended 30 June 2007 and 2006 comprised the following:

| | Six months ended 30 June: | |
|---|---|---|
| | 2007 | 2006 |
| ***Short-term borrowings*** | | |
| Renaissance Securities Trading Limited | 14,424 | - |
| Alfa-Bank | 1,839 | - |
| Sberbank | 483 | - |
| Alba-Alliance | 189 | - |
| Other | 3,927 | 1,255 |
| **Total interest expense on short-term borrowings** | **20,862** | **1,255** |
| ***Long-term borrowings*** | | |
| Senior Notes and Restructured Senior Notes | 2,064 | 2,487 |
| Facility Agreement | 4,746 | 8,175 |
| First Russian Rouble-denominated bonds | 6,203 | 1,157 |
| Second Russian Rouble-denominated bonds | 4,058 | - |
| Alfa Bank | 1,515 | 103 |
| Sberbank | 483 | 396 |
| NOMOS-bank | 226 | 247 |
| Other | 32 | 2,335 |
| **Total interest expense on long-term borrowings** | **19,327** | **14,900** |
| **Total interest expense** | **40,189** | **16,155** |

## 18 Financial Liabilities (Continued)

With the proceeds from the initial public offering completed in February 2007 (Note 19), the Group repaid its short-term borrowings from Renaissance, Sberbank and Alba-Alliance and long-term borrowings from Senior Notes, Restructured Senior Notes, Facility Agreement, Sberbank, IMB and NOMOS-bank. The interest expense incurred during the six months ended 30 June 2007 is segregated between the interest incurred on borrowings repaid from the IPO proceeds and interest on borrowings remaining after the IPO as follows:

| | Six months ended 30 June: | |
|---|---|---|
| | 2007 | 2006 |
| Interest on short-term borrowings repaid from the IPO proceeds | 15,096 | - |
| Interest on short-term borrowings remaining after the IPO | 5,766 | 1,255 |
| **Total interest expense on short-term borrowings** | **20,862** | **1,255** |
| Interest on long-term borrowings repaid from the IPO proceeds | 7,519 | 11,305 |
| Interest on long-term borrowings remaining after the IPO | 11,808 | 3,595 |
| **Total interest expense on long-term borrowings** | **19,327** | **14,900** |
| **Total interest expense** | **40,189** | **16,155** |

## 19 Shareholders' Equity

The following table summarizes share and share premium activity for the six months ended 30 June 2007 (share premium in thousands of US dollars).

| | Number of common shares: | | Number of preferred shares: | | Share Premium |
|---|---|---|---|---|---|
| | Class A | Class B | Series A | Series B | |
| **Balance at 31 December 2006** | **2,085,844** | **940,000** | **598,862** | **1,156,585** | **217,354** |
| Initial Public Offering | 1,791,676 | - | - | - | 559,260 |
| Issuance of Class A common shares from exercise of warrants connected with Senior Notes | 101,393 | - | - | - | 1,533 |
| Issuance of Class A common shares from exercise of warrants connected with Facility Agreement | 62,686 | - | - | - | 15,750 |
| Conversion of Series A and Series B preferred shares into Class A common shares | 1,755,447 | | (598,862) | (1,156,585) | - |
| Exercise of stock options | 61,160 | - | - | - | - |
| Share-based compensation (Note 20) | - | - | - | - | 16,075 |
| **Balance at 30 June 2007** | **5,858,206** | **940,000** | - | - | **809,972** |

***Initial public offering.*** In February 2007 the Group completed its Initial Public Offering ("IPO") of 1,492,537 Class A common shares at London Stock Exchange ("LSE") in the form of 29,850,740 Global Depository Receipts ("GDRs"), each with nominal value of 0.0001 20 GDRs representing an interest in one share. In addition, the Group issued 299,139 shares in the form of 5,982,780 GDRs to cover over allotments in offering. The offering was at price of $335.00 per share or $16.75 per one GDR. The over-allotment option was utilized in full at the offering.

From both IPO and over-allotment offering the Group raised $600,211,000 cash consideration, gross of $29,632,000 of fees charged at the offering. Additionally, the shareholders' equity is reduced by $11,319,000 of costs directly related to the preparation of the Group for the IPO. As a result, the Group's proceeds from IPO net of the directly attributable costs were $559,260,000 (Note 2).

## 19 Shareholders' Equity (Continued)

***Issuance of Class A common shares from exercise of warrants connected with Senior Notes.*** In connection with the issuance of the Senior Notes (Note 18), the Group issued 14,500 warrants to the holders to purchase 120,833 of the Group's Class A common shares for $20.00 per share. Management estimated the fair value of the warrants to be $136,000. This amount was recorded within equity in the Group's consolidated balance sheet, with a corresponding reduction in the carrying value of the Senior Notes. In April 2006, the warrants in the amount of 2,100 were exercised, resulting in issuance of 17,500 Class A common shares. In February 2007, after the initial public offering Class A common shares in the amount of 101,393 were issued in exchange for 8,500 warrants exercised into 70,833 shares for cash proceeds of $1,417,000 and 3,900 warrants exercised into 30,560 Class A common shares on a cash-less basis, under which 1,940 class A common shares were cancelled. The total cost of the issued Class A common shares of $1,533,000 consists of the initial value of the warrants of $116,000 and the value of the cash proceeds of $1,417,000 received upon the warrants exercise.

***Issuance of Class A common shares from exercise of warrants connected with Facility Agreement.*** In connection with entering into the $90,000,000 Facility Agreement (Note 18), the Group issued 90,000 warrants to the lenders. The number of shares each warrant entitled the holder to purchase equalled to 233.33 divided by the listing price of $335.00 of the Group's shares. After the initial public offering the warrant holders exercised in full their entitlement to exercise the 90,000 warrants into 62,686 Class A common shares at an exercise price of $251.25. The Group received proceeds of $15,750,000 from the exercise of these options in February 2007.

***Conversion of Series A and Series B preferred shares into Class A common shares.*** As a result of the IPO, all Series A and Series B preferred shares were converted into Class A common shares on a one-for-one basis in accordance with the terms of their respective certificates of designation.

***Exercise of stock options.*** In March and June 2007, the Group exercised 63,334 options into 61,160 Class A common shares. The options were exercised through a cash-less transaction under which 2,174 shares were cancelled as payment of the exercise price of the options.

## 20 Share-based Compensation

***2005 Stock Option Plan.*** In February 2007, the Group's Board of Directors authorized for issue additional 50,000 options, bringing the total of options authorized for grant to 1,200,000. In June 2007, the Group's Board of Directors authorized for issue additional 2,784 options under the 2005 Stock Option Plan, bringing the total of options authorized for grant to 1,202,784. At 30 June 2007, 8,000 options remained available for grant under the plan.

During the six months ended 30 June 2007, the Group granted options for the purchase of a further 112,600 shares of the Group's Class A common shares. Options granted vest over periods of up to four years and are exercisable for ten years from the grant date. Vesting provisions differ by award. The total grant date fair value of the stock options granted under the 2005 Plan during the six months ended 30 June 2007 was $18,071,000. This amount is being recognized over the vesting period. During the six months ended 30 June 2007, the total charge of the compensation expenses was $16,075,000, including $3,913,000 of compensation expense associated with awards granted during the six months ended 30 June 2007 and $12,162,000 of compensation expense associated with awards granted in earlier periods. The total amount of the compensation expense was recognized within selling, general and administrative expenses in the Group's consolidated condensed statement of income. The associated credit was recorded as share premium in the consolidated condensed statement of changes in the shareholders' equity.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 20 Share-based Compensation (Continued)

***Options outstanding.*** The following summarizes information about stock options activity, including Class B common shares, for the six months ended 30 June 2007.

| | Weighted average exercise price in $ per share | Options |
|---|---|---|
| **Options outstanding at 31 December 2006** | **$56.24** | **2,035,087** |
| Granted | $335.00 | 112,600 |
| Exercised | $12.63 | (63,334) |
| Forfeited | $16.00 | (26,666) |
| **Options outstanding at 30 June 2007** | **$74.04** | **2,057,687** |

| | Options outstanding | | | Options exercisable | |
|---|---|---|---|---|---|
| **Range of exercise prices (in US Dollars per share)** | **Number of options outstanding** | **Weighted-average remaining contractual life (years)** | **Weighted average exercise price ($)** | **Options exercisable at year end** | **Weighted average exercise price ($)** |
| $4.00 - $12.00 | 1,089,137 | 8.3 | $11.57 | 497,705 | $11.16 |
| $15.00 - $34.00 | 475,000 | 8.4 | $31.09 | 166,668 | $30.93 |
| $130.00 - $$275.00 | 380,950 | 9.2 | $225.39 | - | - |
| $335.00 - $375.00 | 112,600 | 9.7 | $347.32 | - | - |
| | **2,057,687** | **8.6** | **$74.04** | **664,373** | **$17.02** |

The Black-Scholes option valuation model is used for estimating the fair value of traded options that have no vesting restrictions and are fully transferable. Based on the assumptions below, the weighted average fair value of employee stock options granted during the six months ended 30 June 2007 was $160.49 per option. The significant inputs into the option valuation model were as follows.

| | Awards granted during the six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| Share price | $335.00 – 375.00 | $122.50 |
| Dividend yield | - | - |
| Expected volatility | 40.00% | 40.00% |
| Risk-free interest rate | 4.7 – 4.9% | 5.0-5.1% |
| Expected life | 5-7 years | 5-7 years |

Had the expected volatility been 25.0 percent, 50.0 percent or 75.0 percent, the weighted average fair value of employee stock options granted during the six months ended 30 June 2007 would have been $122.68, $184.78 or $238.41 per option, respectively.

**(expressed in US Dollars (tabular amounts in thousands), except as indicated)**

## 21 Loss per Share

The following table sets for the computation of basic and diluted loss per share.

| | Six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| ***Numerator*** | | |
| Loss attributable to shareholders of Integra Group for basic earnings per share | (50,296) | (5,550) |
| Loss attributable to shareholders of Integra Group for diluted earnings per share | (50,296) | (5,550) |
| ***Denominator*** | | |
| Weighted average number of common shares outstanding during the period - basic | 5,262,651 | 3,083,018 |
| Incremental common shares attributable to exercise of outstanding options | - | - |
| Incremental common shares attributable to exercise of warrants issued with Senior Notes | - | - |
| Denominator for diluted earnings per share | 5,262,651 | 3,083,018 |
| Basic and diluted loss per share (in US Dollars per share) | (9.56) | (1.80) |

## 22 Related Party Transactions

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24, *Related Party Disclosures*. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

The related parties with whom the Group had significant transactions with or significant balances outstanding as of and for the six months ended 30 June 2007 and 2006 are Brookline Partners LLC, a shareholder of Integra and the Group's associates (NNGF, NGT and SNGF).

Because of these relationships, it is possible that the Group may have entered transactions which unrelated parties might not and it is possible that the terms of these transactions are not the same as those that would have resulted from transactions with unrelated parties.

The table below discloses related party transactions as of 30 June 2007 and 31 December 2006 and for the six months ended 30 June 2007 and 2006 as follows:

| | Six months ended 30 June: | |
|---|---|---|
| | **2007** | **2006** |
| Sales of production evaluation services to related parties | 2,593 | 242 |
| Sales of management services by Integra Group to related parties | 331 | - |
| Purchase of management services by Integra Group from related parties | 150 | 323 |
| Purchase of materials by Integra Group | (24) | - |
| Purchase of transportation services by Integra Group | (326) | (778) |
| Purchase of formation evaluation services by Integra Group | (2,403) | (2,913) |
| Other income (expense) | 840 | (35) |

| | **30 June 2007** | **31 December 2006** |
|---|---|---|
| Trade receivables, net | 3,872 | 695 |
| Trade payables, current | 3,566 | 2,050 |
| Loans issued to employees | 1,353 | 1,020 |
| Long-term borrowings | 453 | 444 |

## 22 Related Party Transactions (Continued)

***Management compensation.*** The Group's senior management team comprised six individuals whose compensation totalled $9,453,000 and $3,460,000 for six months ended 30 June 2007 and 2006, respectively, including salary, bonuses and other benefits of $2,813,000 and $1,343,000 respectively, and share-based compensation of $6,640,000 and $2,117,000, respectively.

***Management and administrative services contracts.*** Prior to January 2007 the Group maintained a management services contract with Brookline Partners LLC, a significant shareholder and an affiliate of the Chairman of the Board. The Group incurred $323,000 under this contract for the six months ended 30 June 2006. In January 2007 the management services contract was terminated and replaced with an administrative services contract with another affiliate of the Chairman. During the six months ended 30 June 2007 under the administrative services contract the Group incurred $150,000.

***Loans issued to employees.*** From July 2006 till April 2007, the Group issued a number of Russian Rouble-denominated loans to its employees in the amount equivalent to $1,362,000. The loans bear interest rates ranging from nil to 10.0 percent per annum, payable upon repayment of the loans at their maturity. Initially the loans were repayable in June 2007. During the six months ended 30 June 2007 the maturity of the loans was extended till December 2007. At 30 June 2007 and 31 December 2006, the fair value of the outstanding loans was $1,353,000 and $1,020,000, respectively, and accrued interest was $112,000 and $40,000, respectively.

***Shareholder loans.*** There were no shareholder loans outstanding, issued or repaid during the six months year ended 30 June 2007 and 2006.

## 23 Contingencies, Commitments and Operating Risks

***Contractual commitments and guarantees.*** In the normal course of business, the Group entered into contracts for the purchase of property, plant and equipment. At 30 June 2007 and 31 December 2006, the Group had unpaid contracted amounts of $30,084,000 and $37,305,000, respectively.

***Environmental matters.*** The enforcement of environmental regulation in Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

***Taxation.*** Tax, currency and customs legislation of various jurisdictions in which the Group has its operations is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As of 30 June 2007, management believes that its interpretation of the relevant legislation is appropriate and that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued for in these financial statements.

***Insurance policies.*** The Group holds certain insurance policies in relation to its operations and assets including, but not limited to life insurance of employees, in respect of public liability and other insurable risks. The Group has Directors and Officers insurance policy in respect of its public liability.

## 23 Contingencies, Commitments and Operating Risks (Continued)

***Legal proceedings.*** At 30 June 2007, the Group was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding which could have a material adverse effect on the results of operations or financial position of the Group and which have not been accrued or disclosed in these consolidated interim condensed financial statements.

***Operating environment of the Group.*** The Russian Federation continues to display some characteristics of an emerging market economy. The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations, and changes, which can occur frequently. Whilst there have been improvements in economic trends, the future economic direction of the Russian Federation is largely dependant on the effectiveness of economic, financial and monetary measures undertaken by the government, together with tax, legal, regulatory and political developments.

## 24 Subsequent Events

***Acquisition of additional interest in Purgeophyzika.*** In August 2007, the Group purchased 42.83 percent interest of the PGF's total shares for $2,360,000, which resulted in the Group ownership of 100 percent interest in PGF. The Group has been consolidating PGF since the date of acquisition of its 57.17 percent interest in May 2005. The acquisition of the minority interest resulted in a loss of $2,315,000 from the excess of the purchase consideration over the carrying value of the net assets acquired which will be recognized in the Group's consolidated statements of income for the twelve months ended 31 December 2007.

***Acquisition of Geotechsystem.*** In August 2007, the Group purchased a 100 percent interest in Geotechsystem ("GTC"), a company providing seismic interpretation services to the petroleum industry in the Russian Federation and overseas for a total consideration of $11 million, including a contingent payment of up to $5 million based on GTC's operating results for 2007. GTC will be included within the Group's formation evaluation segment.

***Acquisition of Obnefteremont.*** On 6 September, 2007, the Group executed a purchase and sale agreement to acquire Obnefteremont ("ONR"), a company specializing in well workovers. The acquisition is subject to approval by Russian antimonopoly authorities in addition to the satisfaction of certain technical conditions precedent. The deal is expected to close in the near term and the final consideration paid will depend on completion of due diligence.

The Group's registered office in the Russian Federation is:

Integra Group
Smolenskaya-Sennaya square, bld. 27-29/1, block 6
119121 Moscow
Russian Federation

Telephone: +7 495 933 06 21
Email: reception@integragroup.ru