Транснефть

OIL TRANSPORTING
JOINT STOCK COMPANY
"TRANSNEFT"

CONSOLIDATED FINANCIAL STATEMENTS
PREPARED IN ACCORDANCE WITH INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)
AND AUDITORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2014

WE TRANSPORT OIL,
SO IT SETS THE WORLD IN MOTION

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STATEMENT OF DIRECTORS' RESPONSIBILITIES

To the Shareholders of OAO AK Transneft

1. We have prepared the consolidated financial statements for year ended 31 December 2014 which give a true and fair view of the financial position of the OAO AK Transneft (the "Company") and its subsidiaries (the "Group") at the end of the year and of the results of its operations and cash flows for the year then ended. Management of the Group is responsible for ensuring that the Group entities keep accounting records which disclose with reasonable accuracy the financial position of each entity and which enable them to ensure that the consolidated financial statements comply with International Financial Reporting Standards and that their statutory accounting reports comply with Russian laws and regulations. Management also has a general responsibility for taking such steps as are reasonably available to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

2. Management believes that, in preparing the consolidated financial statements set out on pages 6 to 49 the Group has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that appropriate International Financial Reporting Standards have been followed.

3. The consolidated financial statements, which are based on the statutory consolidated accounting reports for the year ended 31 December 2014, approved by management in March 2015, have been converted in accordance with International Financial Reporting Standards.

M.S. Grishanin
First Vice-President
7 April 2015

ОТКРЫТОЕ АКЦИОНЕРНОЕ ОБЩЕСТВО «Акционерная компания по транспорту нефти» «ТРАНСНЕФТЬ» МОСКВА

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Russian Federation

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Auditors' Report

To the Shareholders and Board of Directors OAO AK Transneft

We have audited the accompanying consolidated financial statements of OAO AK Transneft (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2014, and the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for 2014, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on the fair presentation of these consolidated financial statements based on our audit. We conducted our audit in accordance with Russian Federal Auditing Standards and International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to express an opinion on the fair presentation of these consolidated financial statements.

Audited entity: OAO AK Transneft

Registered by Moscow Registration Chamber on 26 august 1993, Registration No. 026.800

Registered in the Unified State Register of Legal Entities/Entered in the Unified State Register of Legal Entities on 24 July 2002 by Department of Ministry of Taxes and Duties, Registration No. 1027700049486, Certificate series 77 No. 007893052.

119180, Moscow, ul. Bolshaya Polyanka, 57

Independent auditor: JSC "KPMG", a company incorporated under the Laws of the Russian Federation, a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

Registered by the Moscow Registration Chamber on 25 May 1992, Registration No. 011.585.

Entered in the Unified State Register of Legal Entities on 13 August 2002 by the Moscow Inter-Regional Tax Inspectorate No.39 of the Ministry for Taxes and Duties of the Russian Federation, Registration No. 1027700125628, Certificate series 77 No. 005721432.

Member of the Non-commercial Partnership "Chamber of Auditors of Russia". The Principal Registration Number of the Entry in the State Register of Auditors and Audit Organisations: No.10301000804.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2014, and its financial performance and its cash flows for 2014 in accordance with International Financial Reporting Standards.

Kim A.A.

Director, (power of attorney dated 16 March 2015 No. 11/15)

JSC "KPMG"

7 April 2015

Moscow, Russian Federation

(in millions of Russian roubles, if not stated otherwise)

	Notes	31 December 2014	31 December 2013
ASSETS			
Non-current assets			
Intangible assets		4,535	3,624
Property, plant and equipment	6	1,706,368	1,527,720
Available-for-sale financial assets		231	217
Investments in associates and jointly controlled entities	7	19,517	31,583
Receivables and prepayments	11	3,360	2,136
Other financial assets	9	42,823	19,297
Total non-current assets		**1,776,834**	**1,584,577**
Current assets			
Inventories	10	29,973	27,883
Receivables and prepayments	11	45,563	44,634
VAT assets	11	55,147	52,170
Current income tax prepayments		14,467	1,587
Financial assets at fair value through profit or loss	8	33,482	90
Other financial assets	9	405,802	300,911
Cash and cash equivalents	12	113,060	104,742
Total current assets		**697,494**	**532,017**
Total assets		**2,474,328**	**2,116,594**
EQUITY AND LIABILITIES			
Equity			
Share capital	13	308	308
Share premium reserve	13	52,553	52,553
Merger reserve	13	(13,080)	(13,080)
Retained earnings		1,302,605	1,249,863
Attributable to the shareholders of OAO AK Transneft		**1,342,386**	**1,289,644**
Non-controlling interests	15	26,477	25,395
Total equity		**1,368,863**	**1,315,039**
Non-current liabilities			
Loans and borrowings	16	577,272	484,593
Deferred income tax liabilities	17	55,252	45,304
Provisions for liabilities and charges	18	75,522	43,737
Trade and other payables, including derivatives	19	13,700	1,836
Total non-current liabilities		**721,746**	**575,470**
Current liabilities			
Trade and other payables, including derivatives	19	201,349	126,522
Current income tax payable		450	3,598
Loans and borrowings	16	181,920	95,965
Total current liabilities		**383,719**	**226,085**
Total liabilities		**1,105,465**	**801,555**
Total equity and liabilities		**2,474,328**	**2,116,594**

Approved on 2 April 2015 by:

M.S. Grishanin — First Vice-President

M.V. Russkikh — General director of OOO Transneft Finance, a specialized organization, which performs the accounting function for OAO AK Transneft

ОТКРЫТОЕ АКЦИОНЕРНОЕ ОБЩЕСТО
Акционерная компания по транспорту нефти
«ТРАНСНЕФТЬ»
МОСКВА

The accompanying notes set out on pages 10 to 49 are an integral part of these consolidated financial statements

OAO AK TRANSNEFT
CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2014
(in millions of Russian roubles, if not stated otherwise)

	Notes	Year ended 31 December 2014	Year ended 31 December 2013
Revenue	20	774,380	749,617
Operating expenses	21	(541,053)	(499,134)
Operating profit		**233,327**	**250,483**
Finance income		303,676	88,999
Finance costs		(438,570)	(115,300)
Total net financial items	22	**(134,894)**	**(26,301)**
Changes in the Group's structure	14	8,796	2,848
Share of loss from associates and jointly controlled entities	7	(10,786)	(15,018)
Profit before income tax		**96,443**	**212,012**
Current income tax expense		(27,164)	(48,055)
Deferred tax expense		(9,779)	(5,940)
Income tax expense	17	**(36,943)**	**(53,995)**
Profit for the year		**59,500**	**158,017**
Other comprehensive income			
Items that may be reclassified to profit and loss			
Currency translation differences, net of tax		351	137
Total items that may be reclassified to profit and loss, net of tax		*351*	*137*
Items that will not be reclassified to profit and loss			
Remeasurement of net defined benefit plan obligation	18	1,580	1,245
Total items that will not be reclassified to profit and loss, net of tax		*1,580*	*1,245*
Total other comprehensive income for the year, net of tax		**1,931**	**1,382**
Total comprehensive income		**61,431**	**159,399**
Profit attributable to:			
Shareholders of OAO AK Transneft		58,767	152,917
Non-controlling interests		733	5,100
Total comprehensive income attributable to:			
Shareholders of OAO AK Transneft		60,643	154,275
Non-controlling interests		788	5,124

Approved on 2 April 2015 by:

M.S. Grishanin — First Vice-President

M.V. Russkikh — General director of OOO Transneft Finance, a specialized organization, which performs the accounting function for OAO AK Transneft

(in millions of Russian roubles, if not stated otherwise)

	Notes	Year ended 31 December 2014	Year ended 31 December 2013
Cash flows from operating activities			
Cash receipts from customers		832,209	800,382
Cash paid to suppliers and employees, and taxes other than income tax		(563,559)	(514,979)
Interest paid		(33,699)	(34,887)
Income tax paid		(44,122)	(41,361)
Income tax refund		575	9,037
VAT and taxes other than income tax refunds		83,035	107,633
Other cash used in operating activities		(1,229)	(3,049)
Net cash from operating activities		**273,210**	**322,776**
Cash flows used in investing activities			
Purchase of property, plant and equipment		(312,020)	(223,015)
Proceeds from sales of property, plant and equipment		794	391
Interest and dividends received		20,527	17,491
Purchase of notes and placement of funds on deposit accounts		(344,029)	(310,566)
Proceeds from sale of notes and close of deposit accounts		415,922	258,175
Purchase of shares in associates and jointly-controlled entities		-	(8,104)
Cash inflow/ (outflow) from changes in the Group's structure		6,803	(2,796)
Provision of loans		(18)	-
Other cash from/ (used in) investing activities		266	(521)
Net cash used in investing activities		**(211,755)**	**(268,945)**
Cash flows from financing activities			
Proceeds from long-term loans and borrowings		14,998	620
Repayment of short-term loans and borrowings		(96,998)	(19,859)
Dividends paid		(7,897)	(4,738)
Purchase of non-controlling interests		-	(12,550)
Other cash from/ (used in) financing activities		2	(266)
Net cash used in financing activities		**(89,895)**	**(36,793)**
Effects of exchange rate changes on cash and cash equivalents		**36,758**	**3,187**
Net increase in cash and cash equivalents		**8,318**	**20,225**
Cash and cash equivalents at the beginning of the year	12	104,742	84,517
Cash and cash equivalents at the end of the year	**12**	**113,060**	**104,742**

Approved on 6 April 2015 by:

M.S. Grishanin — First Vice-President

M.V. Russkikh — General director of OOO Transneft Finance, a specialized organization, which performs the accounting function for OAO AK Transneft

(in millions of Russian roubles, if not stated otherwise)

	Attributable to the owners of OAO AK Transneft						
	Share capital	Share premium	Merger reserve	Retained earnings	Total	Non-controlling interest	Total equity
Balance at 1 January 2013	**308**	**52,553**	**(13,080)**	**1,096,088**	**1,135,869**	**37,186**	**1,173,055**
Profit for the year	-	-	-	152,917	152,917	5,100	158,017
Defined benefit plan actuarial gains	-	-	-	1,221	1,221	24	1,245
Currency translation differences, net of tax	-	-	-	137	137	-	137
Total comprehensive income for the year	**-**	**-**	**-**	**154,275**	**154,275**	**5,124**	**159,399**
Purchase of non-controlling interests (Note 15)	-	-	-	4,365	4,365	(16,915)	(12,550)
Dividends (Note 13)							
- ordinary shares	-	-	-	(3,800)	(3,800)	-	(3,800)
- preferred shares	-	-	-	(1,065)	(1,065)	-	(1,065)
Balance at 31 December 2013	**308**	**52,553**	**(13,080)**	**1,249,863**	**1,289,644**	**25,395**	**1,315,039**
Balance at 1 January 2014	**308**	**52,553**	**(13,080)**	**1,249,863**	**1,289,644**	**25,395**	**1,315,039**
Profit for the reporting year	-	-	-	58,767	**58,767**	733	**59,500**
Defined benefit plan actuarial gains	-	-	-	1,525	**1,525**	55	**1,580**
Currency translation differences, net of tax	-	-	-	351	**351**	-	**351**
Total comprehensive income for the year	**-**	**-**	**-**	60,643	**60,643**	**788**	**61,431**
Acquisition of subsidiary with NCI(Note 15)	-	-	-	-	-	294	**294**
Dividends (Note 13)							
- ordinary shares	-	-	-	(6,775)	**(6,775)**	-	**(6,775)**
- preferred shares	-	-	-	(1,126)	**(1,126)**	-	**(1,126)**
Balance at 31 December 2014	**308**	**52,553**	**(13,080)**	**1,302,605**	**1,342,386**	**26,477**	**1,368,863**

Approved on 7 April 2015 by:

M.S. Grishanin — First Vice-President

M.V. Russkikh — General director of OOO Transneft Finance, a specialized organization, which performs the accounting function for OAO AK Transneft

ОТКРЫТОЕ АКЦИОНЕРНОЕ ОБЩЕСТВО «Акционерная компания по транспорту нефти «ТРАНСНЕФТЬ» МОСКВА

1 NATURE OF OPERATIONS

OAO AK Transneft (hereinafter OAO AK Transneft or the "Company") was established as an open joint stock company and incorporated on 14 August 1993 by the Russian Government Resolution No. 810 under Presidential Decree No. 1403 dated 17 November 1992. The Company's registered office is at 119180 Moscow, ul. Bolshaya Polyanka, 57, Russian Federation.

The Company and its subsidiaries (the "Group") operate the oil pipeline system in the Russian Federation totalling 53,256 km at 31 December 2014 and the oil products pipeline system in the Russian Federation and in the Republics of Belarus and Ukraine totalling 18,839 km as at 31 December 2014. Its associate OOO LatRosTrans operates an interconnected system in the Latvian Republic.

During the year ended 31 December 2014, the Group transported 478 million tonnes of crude oil to domestic and export markets (year ended 31 December 2013 – 481 million tonnes), which represents a substantial majority of the crude oil produced in the territory of the Russian Federation during that period, and 31.2 million tonnes of oil products (31.0 million tonnes for year ended 31 December 2013).

2 ECONOMIC ENVIRONMENT IN THE RUSSIAN FEDERATION

The Group's operations are primarily located in the Russian Federation. Consequently, the Group is exposed to the economic and financial markets of the Russian Federation which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in the Russian Federation.

The ongoing conflict in Ukraine and related events has increased the perceived risks of doing business in the Russian Federation. The imposition of economic sanctions on Russian individuals and legal entities including the Company by the European Union, the United States of America, Japan, Canada, Australia and others, as well as retaliatory sanctions imposed by the Russian government, has resulted in increased economic uncertainty including more volatile equity markets, a depreciation of the Russian Ruble, a reduction in both local and foreign direct investment inflows and a significant tightening in the availability of credit. In particular, some Russian entities may be experiencing difficulties in accessing international equity and debt markets and may become increasingly dependent on Russian state banks to finance their operations. The longer term effects of recently implemented sanctions are difficult to determine.

The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

3 BASIS OF PRESENTATION

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

The principal accounting policies have been consistently applied in the preparation of these consolidated financial statements to all periods presented are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated (see Note 4). The consolidated financial statements of the Group are prepared under the historical cost convention except as described in Notes 4 and 5.

Certain comparative amounts have been corrected to confirm with the current year's presentation.

The functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The functional currency of the Company and its principal subsidiaries including ChUP Zapad-Transnefteproduct and DP Prikarpatzapadtrans, and the Group's presentation currency, is the national currency of the Russian Federation, Russian Rouble ("RUB"). The official US dollar ("USD") to Russian Rouble ("RUB") exchange rates as determined by the Central Bank of the Russian Federation ("CBR") was 56.2584 and 32.7292 as at 31 December 2014 and 31 December 2013, respectively. The official euro ("EUR") to Russian Rouble ("RUB") exchange rates as determined by the Central Bank of the Russian Federation was 68.3427 and 44.9699 as at 31 December 2014 and 31 December 2013, respectively.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

Subsidiaries are those companies in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has the power to govern the financial and operating policies of the subsidiary. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases.

Non-controlling interests at the reporting date represent the non-controlling shareholders' portion of the identifiable assets and liabilities of the subsidiary at the acquisition date, and the non-controlling interests' portion of movements in equity since the date of the acquisition.

Acquisitions of non-controlling interests are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognised as a result. Adjustments to non-controlling interests arising from transactions that do not involve the loss of control are based on a proportionate amount of the net assets of the subsidiary.

Investments in associates and jointly controlled entities

Associates are undertakings over which the Group has significant influence, but not control, over the financial and operating policies. Significant influence occurred when the Group has the power to participate in the financial and operational policy decisions of the entity but has no control or joint control over those policies.

Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity.

Joint control entities are companies, financial or operating policies of which are controlled by the Group as well as other members of these companies.

Investments in associates and jointly controlled entities are accounted under equity method and are recognised initially at cost. The cost of the investment includes transaction costs. The consolidated financial statements include the Group’s share of the profit or loss and other comprehensive income of equity accounted investees, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases.

Business combination under common control

Business combinations under common control are accounted for using the predecessor values method from the date of combination. Under this method the acquired entities results are included into the acquirer's financial statements from the date the transaction occurred. The assets and liabilities of the subsidiary transferred under common control are recorded at the predecessor entity’s carrying amounts. The predecessor entity is considered to be the highest reporting entity in which the subsidiary’s IFRS financial information was consolidated. Related goodwill inherent in the predecessor entity’s original acquisitions is also recorded in consolidated financial statements. Any difference between the carrying amount of net assets, including the predecessor entity's goodwill, and the consideration for the acquisition is accounted for in these consolidated financial statements as an adjustment to merger reserve within equity.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of the Group’s interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items in a foreign currency that are measured based on historical cost are translated using the exchange rate at the date of the transaction. Foreign currency differences arising in retranslation are recognised in profit or loss, except for differences arising on the retranslation of available-for-sale equity instruments which are recognised in other comprehensive income.

Property, plant and equipment

Property, plant and equipment are carried at initial historical cost, including, where appropriate, the net present value of the estimated dismantlement or removal cost of the asset at the end of its estimated useful life, less accumulated depreciation. Assets under construction are carried at historical cost and depreciated from the time the asset is available for use. Depreciation is calculated on the straight-line basis to write down the cost of each asset to its estimated residual value over its estimated useful life as follows:

	Years
Buildings and facilities	8-50
Crude oil pipelines and tanks	20-33
Oil product pipelines	50
Other plant and equipment	5-25

Management approves specific plans for prospective dismantlement or decommissioning of sections of pipeline and related facilities on an annual basis and, at that time, the estimated useful life of the related asset is revised and the annual depreciation charge is amended if applicable.

Renewals and improvements are capitalised and the assets replaced are retired. Maintenance, repairs, and minor renewals are expensed as incurred. Gains and losses arising from the retirements or other disposals of property, plant and equipment are included in profit for the period in the consolidated statement of profit or loss and other comprehensive income.

Crude oil and oil products used for technical operation of the pipeline network ("linefill") owned by the Group is treated as a separate component of the pipeline class of asset and is not depreciated as its residual value exceeds its carrying amount.

Any additions to linefill over the period are recognised at cost, and any disposals are written off at weighted average carrying value of linefill.

Oil surpluses arising from operations are recognised at market value and are recorded in inventory with a correspondent credit to oil surplus, a component of net other operating income, in profit and loss netted by expenses on charity, made from income received.

Disposals of oil surpluses are accounted for as revenues and included in sales in the consolidated statement of profit or loss and other comprehensive income.

The prepayments which relate to property, plant and equipment and inventory for construction are included in the category Assets under construction including prepayments.

Leased assets

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Plant and equipment acquired by way of finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at the inception of the lease, less accumulated depreciation and impairment losses. Each lease payment is allocated between the liability and finance charges so as to achieve a constant effective interest rate on the finance balance outstanding. The leased assets are depreciated from the time the asset is available for use. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life.

Other lease agreements are classified as operating leases and corresponding leased assets are not recognized in the Group's consolidated statement of financial position.

Inventories

Inventories are valued at the lower of weighted average cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Non-derivative financial instruments

Financial assets and liabilities

Financial assets and liabilities include cash and cash equivalents, available-for-sale financial assets, receivables, borrowings, and trade and other payables and other financial assets. These items are initially recognised at fair value adjusted for transaction costs on the date when the Group becomes a party to the contractual provisions of the instrument. Financial assets are de-recognised only when the rights to the appropriate benefits under the relevant contract are settled, lost, surrendered, or have expired. Financial liabilities are partially or fully de-recognised only when the obligation specified in the relevant contract is discharged, cancelled, or has expired.

Financial assets at fair value through profit or loss and available-for-sale financial assets are re-measured to fair value at each subsequent reporting date, other financial assets and financial liabilities are carried at amortised cost.

The fair values of financial assets and liabilities with a maturity date less than year from the reporting date, including trade and other receivables and payables, are assumed to approximate their carrying amounts unless there is an indication of impairment at the reporting date. The fair value of all other financial assets and liabilities is based on the amount receivable or payable at the expected settlement date, discounted to net present value using a rate considered appropriate for the asset or liability.

A financial asset not carried at fair value through profit or loss, including an interest in an equity-accounted investee, is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Besides, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment. The Group considers a decline of 20% to be significant and a period of twelve months to be prolonged.

Impairment of an equity-accounted investee are disclosed in the consolidated statement of profit or loss and other comprehensive income.

Available-for-sale financial assets

Fair value of available-for-sale securities is determined using the quoted prices on active market. Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months after the reporting date.

Gains and losses arising from changes in the fair value of the investments classified as available-for-sale are recognised in other comprehensive income. When the investments classified as available-for-sale are sold or impaired, the fair value adjustments accumulated in other comprehensive income are included in the consolidated statement of profit or loss and other comprehensive income as a reclassification adjustment as gains and losses from the investments.

Financial assets at fair value through profit or loss

A financial asset is classified at fair value through profit or loss -category if it is classified as held for trading or is designated as such upon initial recognition. Financial assets at fair value through profit or loss if the Group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Group's documented risk management or investment strategy. Directly attributable transaction costs are recognised in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss for the period.

Interest income on financial assets at fair value through profit and loss calculated based on effective interest method as well as gains or losses on derecognition of these financial assets is recognized in the statement of profit or loss and other comprehensive income in the profit from operations with securities at fair value through profit and loss. Dividend income is recognized in profit or loss for the period when the Group's right to receive payment is established. Changes in fair value are recognized in the profit or loss from operations with securities at fair value through profit or loss in the period when changes occurred.

Accounts receivable

Accounts receivable are carried at original invoice amount inclusive of value added taxes less provision made for impairment.

A provision for impairment is established when there is an objective evidence that Group will not be able to collect all amounts due according to the original terms of the contract. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the market rate of interest for the similar borrowers at the date of origination of the receivables.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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

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

Prepayments

Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition.

Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying value of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss in the consolidated statement of profit or loss and other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents consist of cash, bank balances, and highly liquid investments, and which have original maturities of three months or less.

VAT assets

VAT assets relate to VAT incurred on capital construction, operating and export activities, including oil transportation to russian oil-processing plants. VAT is included in current assets if the amount is expected to be recovered within 12 months after the reporting date.

Loans and borrowings

Borrowings are recognised initially at the fair value which is determined using the prevailing market rate of interest for a similar instrument, if significantly different from the transaction price, net of transaction costs incurred. In subsequent periods, borrowings are carried at amortised cost, using the effective interest rate method; any difference between the fair value (net of transaction costs) and the redemption amount is recognised as interest expense over the period of the borrowings.

Derivatives

The Group has certain derivatives in the form of options which were acquired for hedging and as held for trading. Derivatives are initially recognised at fair value, relevant expenses are recognised in the statement of profit or loss and other comprehensive income. Following initial recognition derivatives are re-measured at fair value with appropriate changes recognised directly in profit or loss for the period.

The best evidence of fair value of a financial instrument at initial recognition is the transaction price (ie the fair value of the consideration given or received). If the Group determines that the fair value on initial recognition differs from the transaction price, the difference between the fair value at initial recognition and the transaction price is taken into account as follows:

(a) in profit or loss if the fair value of the quoted price is confirmed for identical assets or liabilities in an active market (accounted for Level 1) or based on a valuation method, which uses only data from observable markets.

(b) as deferred income or loss to defer recognition of the difference between the fair value at initial recognition and the transaction price. After initial recognition, the Group recognizes the difference as the deferred gain or loss over the life of the financial instrument, but not later than the time when the estimate of its fair value can be made on fully observable market data, or the date of termination.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The Group has established a system of control in relation to the fair value measurement. Within this framework, the Group regularly checks significant unobservable inputs and valuation adjustments. In estimating the fair value of the asset or liability Group applies as possible, observable market data. Fair value estimates are different levels of the fair value hierarchy depending on the input data used in the relevant assessment methods:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the initial data used to estimate the fair value of the asset or liability can be attributed to different levels of the fair value hierarchy, the fair value generally refers to the level of the hierarchy, which corresponds to the original data of the lowest level, are essential for the entire evaluation.

The Group recognizes transfers between levels of the fair value hierarchy at the end of the reporting period in which the change occurred.

Income tax

Income tax has been provided for in the consolidated financial statements in accordance with legislation enacted or substantively enacted by the reporting date. The income tax charge comprises current tax and deferred tax and is recognised in the profit or loss in the statement of profit or loss and other comprehensive income except if it is recognised directly in equity or comprehensive income because it relates to transactions that are also recognised, in the same or a different period, directly in equity or comprehensive income.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax balances are measured at tax rates enacted or substantively enacted at the reporting date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised.

Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Provisions

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

Provisions are estimated and remeasured at each reporting date, and are included in the consolidated financial statements at their expected net present values using the discount rate appropriate to the liability in the economic environment of the Russian Federation.

Changes in provisions resulting from the passage of time are reflected as financial items in the consolidated financial statement of profit or loss and other comprehensive income. Changes in provisions resulting from changes in the discount rate and other changes in provisions, related to a change in the expected pattern or estimated cost of settlement of the obligation, are treated as a change in an accounting estimate in the period of the change by adjusting the corresponding asset or expense.

Pension activities

State pension fund

The Group makes contributions to the State pension fund. Contribuitions to the State pension fund are recognized as expenses when accrued.

Pension liabilities

In addition to contributions to State pension fund, the Group sponsors defined benefit plans for the majority of its employees.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and any unrecognised past service costs and the fair value of any plan assets are deducted. The discount rate is the yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations and that are denominated in the same currency in which the benefits are expected to be paid.

The calculation is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a potential asset for the Group, the recognised asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. In order to calculate the present value of economic benefits, consideration is given to any minimum funding requirements that apply to any plan in the Group. An economic benefit is available to the Group if it is realisable during the life of the plan, or on settlement of the plan liabilities.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in OCI. The Group determines the net interest expense (income) on the net defined benefit liability (asset) for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability (asset), taking into account any changes in the net defined benefit liability (asset) during the period as a result of contributions and benefit payments. Net interest expense and other expenses related to defined benefit plans are recognised in profit or loss.

When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognised immediately in profit or loss. The Group recognises gains and losses on the settlement of a defined benefit plan when the settlement occurs.

The Group operates its pension obligations (non-state pension provision (hereinafter - NPO), compulsory pension insurance (hereinafter - OPS)) through its subsidiary NPF Transneft.

Insurance contracts

NPF Transneft assigns to insurance contracts agreements for provision of NPO in accordance with current pension plans (pension schemes) and agreement for provision of OPS when significant insurance risk is transferred to NPF Transneft. NPF Transneft does not apply for additional financing of NPO to employers-investors and for additional insurance contributions to previous insurer in case of unfavorable events such as decline in investments and increase in longevity. NPF Transneft defines insurance contracts in accordance with IFRS 4 Insurance contracts as a contract under which one party (the insurer or NPF Transneft) accepts significant insurance risk from another party entered into agreement for pension provision when this risk arises from uncertainty connected with payment of pension and deviation of actual repayments from forecasted mortality tables.

Investment contracts

NPF Transneft recognizes as investment contracts agreements for provision of NPO in accordance with current pension plans (pension schemes) when these contracts contain financial risk without significant insurance risk. All investment contracts contain discretionary participation feature and NPF Transneft recognizes them in accordance with IFRS 4 Insurance contracts.

Recognition and measurement of pension liabilities

NPF Transneft uses IAS 37 Provisions, Contingent Liabilities and Contingent Assets to measure its obligations under insurance contracts for NPO and investment contracts with discretionary participation feature. In accordance with IAS 37 the amount of provision recognized is the best estimate of expenditure required to settle the present obligation at the end of the reporting period. The provision in accoradance with IAS 37 is adjusted to risk and uncertainty. This also responds to IFRS 4 Insurance contracts requirements.

In accordance with IFRS 4 Insurance contracts NPF Transneft reviews the relevance of liabilities to estimate whether there is enough pension assets to fulfill NPF Transneft's liabilities under insurance contracts for OPS. The relevance check is based on assumptions for mortality, discount rate in the period of payments and investment returns rate which are the best estimate as at the end of the reporting period.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Deed of Trust agreements

For the investments made by the Group via the Deed of Trust agreements, there is no transfer of risk and benefits related to change in fair value of the investments. Thus the investments are recognised by the Group.

Site restoration provision

The Group periodically evaluates its obligations under environmental regulations, including as discussed below for the remediation of oil spillage. As obligations are determined, they are recognised as expenses immediately unless they mitigate or prevent future environmental contamination, in which case they are capitalised.

At the date of spillage the Group recognises separately the estimated cost of crude oil spillages, including the cost of the obligation to restore the environment. The Group recognises the estimated recoveries under applicable insurance policies, when it is virtually certain that reimbursement will be received.

Revenue recognition

Revenues from transportation services are recognised when the services are provided as evidenced by the delivery of crude oil or oil products to the owner or the owner's customer in accordance with the contract.

Revenues from oil and oil products sales are recognised upon shipment of goods to the customer, when the goods cease to be under physical control of the Group and risks of ownership have been transferred to the buyer.

Revenue and costs under the construction contract are recognised as revenue and costs, respectively, to the extent the stages under the contract are completed as of the end of the reporting period.

The percentage of completion is measured by comparing costs under the contract incurred to fulfil work as of the specific date against the aggregate costs under the contract.

Revenues represent the fair value of consideration received or receivable for the sale of goods and services in the normal course of business, net of discounts and value-added tax. Customs duties are reported as income and expenses in the consolidated statement of profit or loss and other comprehensive income.

Capitalisation of borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of assets that necessarily take a substantial time to get ready for intended use or sale (qualifying assets) are capitalised as part of the costs of those assets.

The Group capitalises borrowing costs that could have been avoided if it had not made capital expenditure on qualifying assets. Borrowing costs capitalised are calculated at the group's average funding cost (the weighted average interest cost is applied to the expenditures on the qualifying assets), except to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset. Where this occurs, actual borrowing costs incurred less any investment income on the temporary investment of those borrowings are capitalised.

Capitalisation of borrowing costs includes capitalising foreign exchange differences relating to borrowings to the extent that they are regarded as an adjustment to interest costs. The gains and losses that are an adjustment to interest costs include the interest rate differential between borrowing costs that would be incurred if the entity borrowed funds in its functional currency, and borrowing costs actually incurred on foreign currency borrowings.

The portion of the foreign exchange movements is estimated based on interest rates on similar borrowing in the Group's functional currency. The foreign exchange gains and losses eligible for capitalisation are assessed on a cumulative basis.

Capitalisation of borrowing costs continues up to the date when the assets are substantially ready for their use or sale.

The portion of the foreign exchange movements on the USD loan eligible for capitalisation is estimated based on the interest rates of the coupon yield for the first period on the RUB nonconvertible interest bearing documentary bonds placed by the Group in the period of June to October 2009.

The foreign exchange gain on these borrowing is not attributable to the interest rate differentials and therefore is not capitalised.

Foreign currency gains and losses are reported on a gross-up basis as "Finance income" or "Finance costs" in the consolidated statement of profit or loss and other comprehensive income.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Share capital and dividends

Ordinary shares and non-redeemable preferred shares with the right to receive discretionary annual fixed dividends are both classified as equity.

Dividends are recognised as a liability and deducted from shareholders' equity on the date on which they are approved. Dividends proposed at any time, and those approved between the reporting date and the date of issuing the consolidated financial statements, are disclosed.

New accounting standards

New amendments to current Standards and a new comment which become effective for annual periods starting 1 January 2014 did not have significant influence on the Groups' consolidated financial statements.

A number of new Standards, amendments to Standards and Interpretations have been issued that are not yet effective as at 31 December 2014, and have not been applied in preparing these consolidated financial statements. The Group plans to adopt these pronouncements when they become effective.

IFRS 9 Financial Instruments. IFRS 9, published in July 2014, replaces the existing guidance in IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39. IFRS 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 9.

IFRS 15 Revenue from Contracts with Customers. IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty Programmes*. The core principle of the new standard is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new standard results in enhanced disclosures about revenue, provides guidance for transactions that were not previously addressed comprehensively and improves guidance for multiple-element arrangements. IFRS 15 is effective for annual reporting periods beginning on or after 1 January 2017, with early adoption permitted. The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 15.

The following new or amended standards are not expected to have a significant impact of the Group's consolidated financial statements.

- IFRS 14 Regulatory Deferral Accounts.
- Accounting for Acquisitions of Interests in Joint Operations (Amendments to IFRS 11).
- Clarification of Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38).
- Defined Benefit Plans: Employee Contributions (Amendments to IAS 19).
- Annual Improvements to IFRSs 2010–2012 Cycle.
- Annual Improvements to IFRSs 2011–2013 Cycle.

5 CRITICAL ESTIMATES IN APPLYING ACCOUNTING POLICIES

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates and judgments 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. Actual results could differ from these estimates and judgments. Management also makes certain judgments, apart from those involving estimations, 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 within the next financial year include:

Useful lives of property, plant and equipment

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

Should the useful life of the oil pipeline increase by 10 years, the profit for the year ended 31 December 2014 would be RUB 11,291 higher (the year ended 31 December 2013: RUB 9,716) as a result of decrease of depreciation expenses.

Dismantlement provision

As at 31 December 2014 the Group revised the assumption used to calculate the provision for dismantlement of the existing network of oil pipelines and oil product pipelines, according to which it was previously assumed that the whole length of oil and oil products pipeline network would be dismantled in the end of its useful life. The pipeline network is under regular diagnostics, maintained properly, periodically upgraded and reconstructed, which leads to the extension of its useful life. Also, as at the reporting date the Group has no plans for removal and as a consequence for dismantling the existing network of oil pipelines and oil product pipelines. Thus, the estimation of the dismantlement period of oil and oil products pipelines can not be made by the Group with sufficient reliability which makes it impossible to calculate dismantlement provision reliably.

Changes in these assumptions as at 31 December 2014 resulted in derecognition of dismantlement provision accrued before in the amount of RUB 29,461. From 2014 the Group recognises dismantlement provision only for the pipelines and period when necessary and sufficient information concerning recognition of provision, terms and amount of retirement obligation becomes available.

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

(in millions of Russian roubles, if not stated otherwise)

6 PROPERTY, PLANT AND EQUIPMENT

	Buildings and facilities	Pipelines and tanks	Other plant and equipment	Linefill	Assets under construction including prepayments	Total
At 1 January 2014						
Cost	148,479	1,038,640	725,591	102,262	230,474	2,245,446
Accumulated depreciation and impairment	(38,966)	(353,232)	(325,528)	-	-	(717,726)
Net book value at 1 January 2014	**109,513**	**685,408**	**400,063**	**102,262**	**230,474**	**1,527,720**
Depreciation	(4,949)	(45,654)	(66,957)	-	-	(117,560)
Additions (including prepayments)	27	84	3,193	10,289	313,762	327,355
Transfers from assets under construction	12,207	72,387	96,289	-	(180,883)	-
Change in provision for impairement of property, plant and equipment	-	(721)	-	-	-	(721)
Net change in dismantlement provision (see Note 18)	-	(28,936)	-	-	77	(28,859)
Disposals at cost	(1,045)	(4,046)	(4,087)	(745)	-	(9,923)
Accumulated depreciation on disposals and impairment	458	3,935	3,963	-	-	8,356
Net book value at 31 December 2014	**116,211**	**682,457**	**432,464**	**111,806**	**363,430**	**1,706,368**
At 31 December 2014						
Cost	159,668	1,078,408	820,986	111,806	363,430	2,533,988
Accumulated depreciation and impairment	(43,457)	(394,951)	(388,522)	-	-	(826,930)
Net book value at 31 December 2014	**116,211**	**682,457**	**432,464**	**111,806**	**363,430**	**1,706,368**

(in millions of Russian roubles, if not stated otherwise)

6 PROPERTY, PLANT AND EQUIPMENT (continued)

	Buildings and facilities	Pipelines and tanks	Other plant and equipment	Linefill	Assets under construction including prepayments	Total
At 1 January 2013						
Cost	157,566	1,037,518	654,543	100,647	124,206	2,074,480
Accumulated depreciation and impairment	(40,355)	(313,166)	(266,812)	-	-	(620,333)
Net book value at 1 January 2013	**117,211**	**724,352**	**387,731**	**100,647**	**124,206**	**1,454,147**
Depreciation	(4,659)	(42,225)	(58,599)	-	-	(105,483)
Additions (including prepayments)	3,482	-	-	2,153	228,039	233,674
Transfers from assets under construction	9,319	52,680	59,795	-	(121,794)	-
Additional impairment provision	-	(40)	(153)	-	-	(193)
Net change in dismantlement provision (see Note 18)	-	(52,707)	-	-	41	(52,666)
Reclassifications at cost	(21,026)	6,479	14,547	-	-	-
Reclassifications of accumulated depreciation	5,655	(2,148)	(3,507)	-	-	-
Disposals at cost	(862)	(5,290)	(3,141)	(538)	(18)	(9,849)
Accumulated depreciation on disposals and impairment	393	4,307	3,390	-	-	8,090
Net book value at 31 December 2013	**109,513**	**685,408**	**400,063**	**102,262**	**230,474**	**1,527,720**
At 31 December 2013						
Cost	148,479	1,038,640	725,591	102,262	230,474	2,245,446
Accumulated depreciation and impairment	(38,966)	(353,232)	(325,528)	-	-	(717,726)
Net book value at 31 December 2013	**109,513**	**685,408**	**400,063**	**102,262**	**230,474**	**1,527,720**

Property, plant and equipment and assets under construction as at 31 December 2014 are presented net of impairment provision of RUB 5,427 (as at 31 December 2013 – net of impairment provision of RUB 4,706), against specific pipeline assets and machinery and equipment.

Losses from disposal of fixed assets in the amount of RUB 1,567 and RUB 1,759 for the years ended 31 December 2014 and 31 December 2013 respectively, are included in other expenses in the consolidated statement of profit or loss and other comprehensive income.

Linefill represents RUB 95,847 of crude oil and RUB 15,959 of oil products as at 31 December 2014 (as at 31 December 2013 – RUB 94,765 of crude oil and RUB 7,497 of oil products).

During the year ended 31 December 2014 borrowing costs in the amount of RUB 3,487 were capitalised as part of cost of assets under construction (for the year ended 31 December 2013 – RUB 2,389) including interests to be capitalised in the amount of RUB 2,071 less interest income on the temporary investment of borrowings in the amount of RUB 839 as disclosed in Note 22.

(in millions of Russian roubles, if not stated otherwise)

7 INVESTMENTS IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES

Carrying amount of investment in associates and jointly controlled entities in amount of RUB 19,517 as at 31 December 2014 (RUB 31,583 - at 31 December 2013) is shown net of impairment provision of RUB 16,884 as at 31 December 2014 (RUB 15,898 - at 31 December 2013), including the amount of provision of EUR 42,301 thousand as 31 December 2014 and LVL 29,729 thousand at 31 December 2013.

Summarised financial information of associates and jointly controlled entities was as follows:

	31 December 2014	31 December 2013
Current assets	32,218	24,755
including cash and cash equivalents	23,301	18,793
Non-current assets	171,132	164,475
Current liabilities	(110,221)	(19,732)
including current financial liabilities	(102,939)	(15,309)
Non-current liabilities	(34,431)	(82,062)
including non-current financial liabilities	(25,789)	(73,087)
Total net assets	58,698	87,436
Share in net assets	**35,002**	**31,583**
Carrying value of investment	**19,517**	**31,583**

	Year ended 31 December 2014	Year ended 31 December 2013
Revenue	80,861	74,323
Interest expense	4,587	4,135
Current income tax (income)/expense	(3,089)	1,616
Loss	(17,302)	(63,618)
Other comprehensive loss	(8,492)	(631)
Total comprehensive loss	(25,794)	(64,249)
Share of comprehensive loss	**(10,786)**	**(15,018)**
Dividends received	**(1,338)**	**(536)**

The most significant share in the net assets (more than 90% as at 31 December 2014 and as at 31 December 2013), revenue (about 40% as at 31 December 2014 and as at 31 December 2013) and loss (about 100% as at 31 December 2014 and as at 31 December 2013) is attributable to NCSP (Omirico Ltd.). The estimated effective share of the Group in NCSP based on share price at MICEX amounted to RUB 7,947 (RUB 19,388 – as at 31 December 2013). The main operating activities of NCSP and its subsidiaries are the provision of stevedore and supporting services of the port as well as servicing of sea ships.

As a result of significant decline in the share market price of NCSP as at 31 December 2013 and its continuing decline after 31 December 2013 the Group recognised impairment loss of the equity-accounted investee in the amount of RUB 13,993. The estimation of the recoverable amount of investment was based on assessment of its value in use, and the following assumptions were used – the forecast period of 5 years, the discount rate of 10.5%, growth rate after the forecast period of 2%.

The results as for 2013 were restated to show the effect of impairment distribution of NCSP as at 31 December 2013.

(in millions of Russian roubles, if not stated otherwise)

8 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	31 December 2014	31 December 2013
Corporate bonds	26,204	-
Municipal bonds	5,956	-
Government bonds (OFZ)	567	-
Corporate Eurobonds	186	-
Securities	6	-
Derivatives	563	90
	33,482	90

Financial assets at fair value through profit or loss are financial instruments assigned for trading. Financial assets at fair value through profit or loss are neither overdue nor impaired. Financial assets at fair value through profit or loss were recognised in the consolidated financial statements because of consolidation of NPF Transneft (Note 14).

The Group classified these financial assets as current assets due to its ability to sell the assets before maturity

Maturity table for financial assets at fair value through profit or loss as at 31 December 2014 was as follows:

Financial instrument	12 months and less	From 1 to 2 years	From 2 to 5 years	More than 5 years	Without maturity date	Total
Corporate bonds	4,157	4,540	6,156	11,351	-	26,204
Municipal bonds	327	608	3,641	1,380	-	5,956
Government bonds (OFZ)	81	5	100	381	-	567
Corporate Eurobonds	-	186	-	-	-	186
Securities	-	-	-	-	6	6
Derivatives	563	-	-	-	-	563
	5,128	5,339	9,897	13,112	6	33,482

The fair value hierarchy of the financial assets at fair value through profit or loss as at 31 December 2014 is presented below:

Financial instrument	Level 1	Level 2	Level 3
Corporate bonds	26,204	-	-
Municipal bonds	5,956	-	-
Government bonds (OFZ)	567	-	-
Corporate Eurobonds	-	186	-
Securities	6	-	-
Derivatives	-	-	563
	32,733	186	563

(in millions of Russian roubles, if not stated otherwise)

9 OTHER FINANCIAL ASSETS

As at 31 December 2014:

Type of asset	Maturity	Currency	Amount at the purchase date	Carrying amount
Long-term financial assets				
Loan to Omirico Ltd*	January 2016	USD	5,221	9,764
Bonds	May 2016 – May 2018	USD	3,338	4,672
	October, November 2016, December 2017	USD	17,854	25,376
Deposits	January 2016 – December 2016	RUB	2,998	3,009
Other financial assets	-	USD	2	2
			29,413	**42,823**
Short-term financial assets				
	January 2015 – July 2015	USD	101,304	166,276
	April 2015 – September 2015	USD	12,581	20,084
Interest-bearing notes	May 2015	RUB	2,500	2,667
Bonds	During the year after the reporting date	USD	234	365
	During the year after the reporting date	USD	148,672	179,839
		RUB	36,349	36,508
Deposits		Other	50	50
Other financial assets	-	RUB	13	13
			301,703	**405,802**

As at 31 December 2013:

Type of asset	Maturity	Currency	Amount at the purchase date	Carrying amount
Long-term financial assets				
Loan to Omirico Ltd*	January 2016	USD	5,221	5,679
Discounted promissory notes (on demand)	June 2015	USD	13,257	13,055
Derivatives	-	-	-	563
			18,478	**19,297**
Short-term financial assets				
Discounted promissory notes	January - November 2014	USD	184,020	192,455
(on demand)	December 2014	RUB	34,000	36,298
	January - October 2014	USD	19,892	20,737
Interest-bearing notes	May 2014	RUB	2,500	2,500
		RUB	126	126
	During 2014	USD	48,939	48,770
Deposits		Other	27	25
			289,504	**300,911**

*Loan with an 5.27% interest rate is repayable in 5 years. The amount of the loan and interest are repayable at the repayment date.

As at 31 December 2014 and 31 December 2013 the significant amount of deposits (62% and 84% respectively) was allocated among banks under control or significant influence of the state.

The afore-mentioned notes and bonds in significant part were issued by organisations under control or significant influence of the state.

According to IAS 39 Financial Instruments: Recognition and Measurement these notes were classified as loans and receivables and bonds as investments held till maturity and the Group does not intend to dispose these notes prior to the maturity date.

(in millions of Russian roubles, if not stated otherwise)

10 INVENTORIES

	31 December 2014	31 December 2013
Materials and supplies	22,688	18,618
Sundry goods for resale	7,285	9,265
	29,973	**27,883**

Materials and supplies are presented net of provisions for obsolescence of RUB 135 as at 31 December 2014 (as at 31 December 2013 – RUB 143). Materials are primarily used for repairment and maintenance of pipeline equipment.

Sundry goods for resale, including oil and oil products, were not impaired as at 31 December 2014 (as at 31 December 2013 the impairment amounted to RUB 2).

11 RECEIVABLES AND PREPAYMENTS AND VAT ASSETS

Receivables and prepayments

	31 December 2014	31 December 2013
Financial assets		
Other long-term receivables	3,312	2,084
Non-financial assets		
Long-term VAT	48	52
Total long-term receivables	**3,360**	**2,136**

	31 December 2014	31 December 2013
Short-term receivables		
Financial assets		
Trade receivables	24,030	20,233
Other receivables	9,241	15,077
less: provision for doubtful debts	(1,760)	(3,335)
Total financial assets in short-term receivables	**31,511**	**31,975**
Non-financial assets		
Prepayments and advances and other non-financial receivables	14,052	12,659
Total receivables	**45,563**	**44,634**

As at 31 December 2014 and 31 December 2013 other accounts receivable include interest receivable related to temporarily available cash balances with banks and receivables related to insurance.

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

	2014		2013	
	Trade receivables	Other receivables	Trade receivables	Other receivables
As at 1 January	**100**	**3,235**	**13**	**3,117**
Impairment loss	18	1,040	94	359
Amounts written off in trade and other receivables	-	(2,494)	-	-
Reversal of provision	(79)	(60)	(7)	(241)
As at 31 December	**39**	**1,721**	**100**	**3,235**

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

(in millions of Russian roubles, if not stated otherwise)

11 RECEIVABLES AND PREPAYMENTS AND VAT ASSETS (continued)

According to the analysis of accounts receivable in respect to the payment dates the Group has the following overdue balances not included in the provision for accounts receivable as at 31 December 2014 and 2013:

Outstanding period	31 December 2014		31 December 2013	
	Trade receivables	Other receivables	Trade receivables	Other receivables
Less than 90 days	153	284	58	156
More than 90 days but less than 365 days	116	424	24	38
Over 365 days	64	217	50	52
	333	**925**	**132**	**246**

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

Breakdown of accounts receivable by currency is presented in the tables below:

Currency	31 December 2014			31 December 2013		
	Trade receivables	Other receivables	Total receivables	Trade receivables	Other receivables	Total receivables
Russian roubles	9,641	4,923	14,564	6,036	11,504	17,540
USD	14,341	2,487	16,828	14,080	281	14,361
Other	9	110	119	17	57	74
	23,991	**7,520**	**31,511**	**20,133**	**11,842**	**31,975**

VAT assets

	31 December 2014	31 December 2013
Recoverable VAT related to construction projects	5,741	4,689
Recoverable VAT related to ordinary activity	49,454	47,533
Total VAT assets	**55,195**	**52,222**
Less: short-term VAT	(55,147)	(52,170)
Long-term VAT	**48**	**52**

12 CASH AND CASH EQUIVALENTS

	31 December 2014	31 December 2013
Balances in Russian roubles	47,306	36,129
Balances in US dollars	64,785	67,655
Balances in Euro	892	809
Balances in other currencies	77	149
	113,060	**104,742**

In accordance with Russian legislation, the Group selects financial institutions via holding tenders based on certain established qualifications required by law. As at 31 December 2014 and 31 December 2013, a significant portion of cash was placed with banks, which are under common control or significant influence of the state (49% and 34% correspondingly).

(in millions of Russian roubles, if not stated otherwise)

13 SHARE CAPITAL, RETAINED EARNINGS AND DIVIDENDS

Share capital	31 December 2014			31 December 2013		
	Number of shares	Historical cost	Inflated cost	Number of shares	Historical cost	Inflated cost
Authorised, issued and fully paid shares with par value RUB 1 each						
Ordinary:	5,546,847	5.6	231	5,546,847	5.6	231
Preferred:	1,554,875	1.5	77	1,554,875	1.5	77
	7,101,722	7.1	308	7,101,722	7.1	308

The carrying value of the share capital as at 31 December 2014 and as at 31 December 2013 differs from historical cost due to the effect of hyperinflation in the Russian Federation prior to 31 December 2002.

The difference of RUB 13,080,359 thousand between the historic IFRS book value of the Company's share in Transnefteproduct Group net assets (amounting to RUB 39,473,636 thousands) and the nominal value of the ordinary shares issued and the share premium (RUB 52,553,995 thousands including share premium of RUB 52,553,113 thousand), has been recorded as merger reserve within equity.

The Russian Federation, through the Federal Agency for the Management of State Property, holds 100% of the ordinary shares of the Company.

Rights attributable to preferred shares

Holders of preferred shares shall receive dividends pursuant to the authorization of dividend payments at the general meeting of shareholders. The amount of dividends to be paid on preferred shares is established as 10 percent of the net profits of the Company prepared in accordance with Russian Accounting Standards (RAS) for the most recent financial year.

Dividends on the preferred shares are not cumulative.

Shareholders that hold preferred shares in the Company shall be entitled to participate in the general meeting of shareholders with the right to vote on the following issues:

- on the reorganization and liquidation of the Company;
- on the introduction of amendments and addenda to the Charter of the Company which limit the rights of shareholders that hold preferred shares, including the determination or increase in the amount of dividends and/or determination or liquidation cost to be paid on preferred shares of the previous level of priority;
- on all issues within the competence of the general meeting of shareholders, after an annual general meeting of shareholders where no decision on payment of dividends was adopted or a decision was adopted on partial payment of dividends on preferred shares. This right is terminated from the time of the first full payment of dividends on the indicated shares;
- in other cases provided for by acting legislation of the Russian Federation.

Dividends

In June 2014 the following dividends were approved at the general shareholders meeting for the year ended 31 December 2013:

	Russian roubles per share	Total
Ordinary shares	1,221.38	6,775
Preferred shares	724.21	1,126
		7,901

Dividends were repaid in full in July-August 2014.

In June 2013 the following dividends were approved at the general shareholders meeting for the year ended 31 December 2012:

	Russian roubles per share	Total
Ordinary shares	685.10	3,800
Preferred shares	685.10	1,065
		4,865

The whole amount of dividends was paid in August 2013.

Distributable profits

The statutory accounting reports of the Company are the basis for their respective profit distribution and other appropriations. The statutory profit of the Company was RUB 11,784 for the year ended 31 December 2014 (RUB 11,260 for the year ended 31 December 2013).

(in millions of Russian roubles, if not stated otherwise)

14 ACQUISITION AND SALE OF SUBSIDIARIES

In October 2014 the Group acquired additional interest (shares) in share capitals of associates amounting to 75%, 50% and 50% of OOO Sigma Telecom, OOO Tikhoretsk-Nafta and ZAO PROMSFERA respectively. As a result the Group consolidated 100% of control in the mentioned companies. The amount of total consideration was RUB 2,221 (including consideration for OOO Sigma Telecom amounting to RUB 1,619). The main activity of OOO Sigma Telecom is telecommunication services, the main activities of OOO Tikhoretsk-Nafta and ZAO PROMSFERA are loading and shipment services. Information concerning assets and liabilities of the acquired companies as at the date of acquisition is presented below:

	2014
Non-current assets	
Property, plant and equipment	3,380
Deferred tax assets	33
Current assets	
Receivables and prepayments	446
Cash and cash equivalents	325
inventories	131
Current liabilities	
Trade and other payables including derivatives	(650)
Loans and borrowings	(302)
Total identifiable net assets	**3,363**
Consideration transferred	2,221
Payables due	(33)
Cash acquired	(325)
Cash outflow	1,863

The Company is the only founder of non-state pension fund “Transneft” (hereinafter – NPF Transneft), which was classified as unconsolidated structured entity untill 31 December 2014. Due to a decision to privatise NPF Transnfet in favour of OAO AK Transneft in conformity with Russian legislation, starting from 31 December 2014 NPF Transneft is included in the consolidated financial statements. As at the date of consolidation NPF Transneft’s assets amounted to RUB 63,838 including securities at fair value through profit or loss in the amount of RUB 32,919; its liabilities amounted to RUB 55,475 including RUB 55,360 of pension liabilities. As a result of these changes the Group recognised profit in the amount of RUB 8,364. The initial investment of the Company in the share capital of NPF Transneft amounted to RUB 50 (31 December 2013 – RUB 50). The main activity of NPF Transneft is non-state pension benefit provision for employees of the Group.

In September 2013 the Group acquired 100% share of OOO Avesta and Co for USD 110 (RUB 3,510 at the CBR exchange rate at acquisition date). The main asset of Avesta and Co is the office building which is intended to be used by the Group. The Group classified the acquisition as purchase of an asset and attributed the purchase consideration to this asset.

In Septeber 2013 OAO AK Transneft held an open tender for sale of shares of ZAO SK Transneft. The winner of the tender for 98.9 per cent of the shares of ZAO SK Transneft offered RUB 9,396. The deal was closed in the 4th quarter of 2013. According to the agreement the significant part of consideration is to be received by the end of 2014. The consideration due was included in other receivables in the consolidated statement of financial position as at 31 December 2013. Due to the fact that ZAO SK Transneft does not represent a separate major line of business for the Group its results of operations are not presented as discontinued operations.

Assets and liabilities of ZAO SK Transneft as at disposal date are shown in the table below:

Fixed assets	48
Receivables and prepayments	1,317
Deposits	7,432
Cash and cash equivalents	5,792
Other assets	2,259
Payables	(683)
Accruals	(9,499)
Other liabilities	(20)
Total net assets	6,646

(in millions of Russian roubles, if not stated otherwise)

15 NON-CONTROLLING INTERESTS

The disclosure below presents information of the subsidiary with significant non-controling interest:

Company name	Type of activity	Country of incorporation	Non-controling interest 2014	2013
OAO SZMN	oil transportation	Russia	36%	36%

Aggregated financial information relating to OAO SZMN presented in accordance with IFRS including consolidation adjustments but without elimination of intercompany operations between companies of the Group was as following:

	2014	2013
Revenue	28,641	30,974
Profit	2,218	8,504
Profit of non-controlling interests	799	3,062
Other comprehensive income	55	66
Total recognised income	**2,273**	**8,570**
Total recognised income allocated to non-controlling interests	818	3,085
Assets	86,044	73,173
Liabilities	7,294	7,741
Net assets	**78,750**	**65,432**
Net assets allocated to non-controlling interests	28,350	23,556
Cash flows from operating activities	10,023	11,219
Cash flows used in investing activities	(9,984)	(11,379)
Cash flows (used in)/from financing activities	(46)	142
Net decrease in cash and cash equivalents	**(7)**	**(18)**
Dividends paid to non-controlling interests for the period	-	-

In December 2014 AO “Transneft neftyannie nasosy” (AO TNN) was established with the Group holding 51% share in the company. The main activity of this new company is production of pump equipment. The Group recognised addition to non-controlling interest in the amount of RUB 294 as a result of establishment of the new company.

In August 2013 the Group acquired further 24.5% and 13.8% shares of OAO Uralsibnefteprovod and OAO Uraltransnefteproduct for RUB 10,438 and RUB 2,112 accordingly, which were paid in cash. As a result the Group's interest in OAO Uralsibnefteprovod and OAO Uraltransnefteproduct increased from 75.5% and 86.2% accordingly to 100%. As at the date of acquisition the book value of net assets of these subsidiaries in the Group's consolidated financial statements amounted to RUB 72,763. The Group recognized a decrease in non-controlling interests in the amount of RUB 16,915 and an increase in retained earnings amounting to RUB 4,365.

Shares in other companies are disclosed in Note 23.

16 LOANS AND BORROWINGS

	31 December 2014	31 December 2013
Total loans and borrowings	759,192	580,558
Less: current loans and borrowings and current portion of non-current loans and borrowings	(181,920)	(95,965)
	577,272	**484,593**
Maturity of non-current loans and borrowings		
Between one and five years	224,094	257,307
After five years	353,178	227,286
	577,272	**484,593**

(in millions of Russian roubles, if not stated otherwise)

16 LOANS AND BORROWINGS (continued)

Terms and conditions of loans and borrowings were as follows:

Type of loans and borrowings	Date of issue	Years to maturity	Currency	Interest rate, %	Carrying amount 31 December 2014	Carrying amount 31 December 2013
Eurobonds	March 2007	7	USD	5.67	-	42,548
Eurobonds	August 2008	10	USD	8.70	59,071	34,366
Non-convertible interest-bearing documentary	June-October 2009	10*	RUB	Floating, depending on CBR's REPO rate	135,000	135,000
Non-convertible interest-bearing documentary	December 2012	3**	RUB	7.50 (1st - 4th coupons)	45	34,000
Non-convertible interest-bearing documentary	October 2014	10***	RUB	11	15,000	-
Loan agreement with China Development Bank Corporation	February 2009	20****	USD	Floating-LIBOR	540,706	327,292
Loan agreement with OOO Latrostrans	April 2013	2	USD	Floating-LIBOR	1,158	663

* earlier redemption possibility in 2015

** earlier redemption on offer in 2014

*** earlier redemption possibility in 2016

**** equal instalments during 5 years after attraction.

The proceeds from Eurobonds issues are used to finance investment projects or to refinance current portion of loans and borrowings to finance investment projects.

The loan proceeds from China Development Bank Corporation were used for the construction of crude oil pipeline infrastructure, including construction of the crude oil pipeline from Skovorodino to the border of the People's Republic of China and general corporate purposes.

Collateral

All borrowings and loans of the Group, except the loan from China Development Bank Corporation, are unsecured as at 31 December 2014 and 31 December 2013.

In February 2009 as collateral for the loan from China Development Bank Corporation the Company signed a contract for the term of 20 years for the annual supply of 6 mln. tons of crude oil to the People's Republic of China starting from 1 January 2011. For the fulfillment of this obligations, a contract was signed with OAO NK Rosneft in April 2009 for the supply of corresponding volumes of crude oil to the Company.

Fair value

Fair value of loan from China Development Bank Corporation was RUB 494,535 as at 31 December 2014 (fair values of loans did not differ significantly from carrying amounts as at 31 December 2013). The fair value of loan (Level 3) was determined as a result of discounting using estimated market interest rates for similar financing arrangements. These amounts include all future cash outflows assocated with the long-term debt repayments, including the current portion and interest. Market interest rates mean the rates of raising long-term debt by companies with a similar credit rating for similar maturities, repayment schedules and similar other main terms.

The fair value of bonds (Level 1) was determined based on market quotations as at 31 December 2014 and 2013, respectively.

Type of bonds	Interest rate	Currency	Carrying amounts 31 December 2014	Carrying amounts 31 December 2013	Fair value 31 December 2014	Fair value 31 December 2013
Non-convertible interest-bearing documentary	Floating	RUB	135,000	135,000	135,928	141,266
Non-convertible interest-bearing documentary	Fixed	RUB	45	34,000	45	34,085
Non-convertible interest-bearing documentary	Fixed	RUB	15,000	-	14,552	-
Eurobonds	Fixed	USD	59,071	76,914	61,152	84,959

(in millions of Russian roubles, if not stated otherwise)

17 DEFERRED TAX LIABILITIES AND INCOME TAX EXPENSE

Deferred tax liabilities and assets consist of the following:

	1 January 2014	(Charged)/ credited to profit or loss	Credited directly to other comprehensive income	Changes in the composition of the Group	31 December 2014
Deferred tax liabilities:					
Carrying value of property, plant and equipment in excess of tax base	(53,622)	(6,381)	-	-	(60,003)
Changes in the Group's structure	(4,014)	1,416	-	-	(2,598)
Other	(312)	(341)	(145)	(41)	(839)
	(57,948)	**(5,306)**	**(145)**	**(41)**	**(63,440)**
Deferred tax assets:					
Provisions against inventories, receivables and accruals	1,269	93	-	-	1,362
Tax loss carry-forwards	4,020	173	-	17	4,210
Provisions for dismantlement and other expenses	7,355	(4,739)	-	-	2,616
	12,644	**(4,473)**	**-**	**17**	**8,188**
Net deferred tax liability	**(45,304)**	**(9,779)**	**(145)**	**(24)**	**(55,252)**

	1 January 2013	(Charged)/ credited to profit or loss	Credited directly to other comprehensive income	Changes in the composition of the Group	31 December 2013
Deferred tax liabilities:					
Carrying value of property, plant and equipment in excess of tax base	(60,328)	6,706	-	-	(53,622)
Changes in the Group's structure	-	(4,014)	-	-	(4,014)
Other	(418)	170	(14)	(50)	(312)
	(60,746)	**2,862**	**(14)**	**(50)**	**(57,948)**
Deferred tax assets:					
Provisions against inventories, receivables and accruals	825	444	-	-	1,269
Tax loss carry-forwards	3,983	37	-	-	4,020
Provisions for dismantlement and other expenses	16,638	(9,283)	-	-	7,355
	21,446	**(8,802)**	**-**	**-**	**12,644**
Net deferred tax liability	**(39,300)**	**(5,940)**	**(14)**	**(50)**	**(45,304)**

Differences between the recognition criteria in Russian statutory taxation regulations and IFRS give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. The tax effect of the movement on these temporary differences is recorded at the statutory rate of 20% for year ended 31 December 2014 and 31 December 2013.

(in millions of Russian roubles, if not stated otherwise)

17 DEFERRED TAX LIABILITIES AND INCOME TAX EXPENSE (continued)

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

	Year ended 31 December 2014	Year ended 31 December 2013
Profit before income tax	**96,443**	**212,012**
Theoretical income tax expense at 20%	19,289	**42,402**
Increase due to:		
Changes in the Group's structure	1,417	7,812
Items not taxable for income tax purposes	(647)	(230)
Items not deductible for income tax	16,883	4,011
Actual income tax expense	**36,943**	**53,995**

The Group does not recognise a deferred tax liability in respect of RUB 372,749 as at 31 December 2014 (as at 31 December 2013 - RUB 196,309) of taxable temporary differences associated with its investments in subsidiaries as the Group is able to control the timing of their reversal and does not believe they will reverse in the foreseeable future.

As at 31 December 2014 the Group have not recognized deferred tax assets in the amount of RUB 15,020 because it is not probable that future taxable profit will be available against which the Group can utilise the benefits therefrom. According to current tax legislation deductible temporary differences do not expire.

Since 1 January 2012 OAO AK Transneft and almost all of its significant subsidiaries merged into the consolidated taxpayers' group for the purpose of calculation and payment of income tax.

18 PROVISIONS FOR LIABILITIES AND CHARGES

	31 December 2014	31 December 2013
Dismantlement provision	-	29,234
Pension provision	71,131	8,939
Other provisions	4,391	5,564
	75,522	**43,737**

Dismantlement provision

As at 31 December 2014 the Group revised the assumption used to calculate the provision for dismantlement of the existing network of oil pipelines and oil product pipelines, according to which it was previously assumed that the whole length of oil and oil products pipeline network would be dismantled in the end of its useful life. This assumption was changed because the pipeline network is under regular diagnostics, maintained properly, periodically upgraded and reconstructed, which leads to the extension of its useful life. As at the reporting date the Group had no plans for removal and as a consequence for dismantling the existing network of oil pipelines and oil product pipelines. Thus, the estimation of the period of the oil and oil products pipelines dismantlement as well as amount of dismantlement provision can not be measured by the Group with sufficient reliability.

	2014	2013
At 1 January	**29,234**	**78,266**
Provision on additions to property, plant and equipment	602	683
Changes in estimates adjusted against property, plant and equipment	(29,461)	(53,349)
Utilised in the period	(2,439)	(2,105)
Unwinding of the present value discount	2,329	5,777
Reversal of provision	(265)	(38)
At 31 December	**-**	**29,234**

As at 31 December 2013 the expected costs at the dates of dismantlement have been discounted to net present value using a nominal average rate of 7.90% per year).

Provision in accordance with IAS 19

In addition to contributions to State pension fund, the Group sponsors defined benefit plans for the majority of its employees which was classified as a defined contributions plan untill 31 December 2014. These plans assume a regular pension payments upon retirement for employees who have worked for

(in millions of Russian roubles, if not stated otherwise)

18 PROVISIONS FOR LIABILITIES AND CHARGES (continued)

more than five years based on years of service, salary and received awards during working. Simultaneously, these employees acquire the right to accumulate pensions with the Group's share. The change in classification of the plan increased the pension provision of the Group fro RUB 8,441. The pension plan's assets as well as payments of pension are managed by NPF Transneft.

Under collective agreements with Group's employees, an amount ranging from one to five months final salary is payable upon retirement to those who have worked for the Group for more than three years. Also under collective agreements with the employees the Group provides regular payments to those retired employees who have not entered in an agreement with the Non-state pension fund of the Group, and an amount ranging from one to five months minimal salary is payable to retired employees for anniversary milestones and to cover funeral costs.

Management has assessed the net present value of these obligations, following the guidelines set out in IAS 19 "Employee Benefits". For the calculation of obligations the projected unit method was applied.

Reconciliation of opening and closing present value of the defined benefit obligation is as follows:

Movement in defined benefit obligation	2014	2013
At 1 January	**8,939**	**10,153**
Interest cost	719	707
Service cost	277	327
Actuarial gain	(1,580)	(1,245)
Adjustments	8,441	-
NPF Transneft consolidation	7,383	-
Benefits paid	(1,025)	(1,003)
At 31 December	**23,154**	**8,939**

Service cost and adjustments amounting to RUB 8,718 and RUB 327 as for the years ended 31 December 2014 and 2013, respectively, are included in staff costs in the consolidated statement of profit or loss and other comprehensive income, interest expense in the amount of RUB 719 and RUB 707 for the year ended 31 December 2014 and 2013, respectively, are included in interest expenses.

Actuarial gains amounting to RUB 1,580 for the year ended 31 December 2014 (RUB 1,245 for the year ended 31 December 2013) are included in other comprehensive income and total actuarial losses amounted to RUB 1,534 as at 31 December 2014 (RUB 46 as at 31 December 2013).

Assumptions regarding future mortality are based on published statistics and mortality tables. Assumptions are based on mortality statistics in Russia for 2011. The retirement age in Russia is currently 60 years for men and 55 years for women.

The amounts associated with pension provision recognised in the statement of financial position are as follows:

	31 December 2014	31 December 2013
Pension provision for defined benefit plan recognised in Provisions for liabilities and charges	23,154	8,939

Principal actuarial assumptions used (expressed as weighted average):

	31 December 2014	31 December 2013
Average nominal discount rate	12.32%	8.04%
Future salary increases (nominal)	5.14%	3.90%
Expected long-term inflation rate	4.14%	2.90%

As at 31 December 2014, if the future estimated inflation rate had increased by 1%, the amount of the Group pension provisions would have been RUB 1,461 higher.

As at 31 December 2014, if the average nominal discount rate had decreased by 1%, the amount of the Group pension provisions would have been RUB 1,372 higher.

Pension liabilities through NPF Transneft's activity:

	31 December 2014
Pension liabilities – insurance contracts	29,138
Pension liabilities – investment contracts	18,839
	47,977

18 PROVISIONS FOR LIABILITIES AND CHARGES (continued)

Liabilities under insurance contracts

Liabilities under insurance contracts consist of liabilities under compulsory pension insurance (OPS) and liability under non-state pension provision (NPO).

Liaibilities under insurance contracts under OPS

Liabilities under OPS are considered insurance contracts. The assumption is based on NPF Transneft's obligation to make pension payments to the insured person during his life after post-employment.

During relevance check for the amount of liability under insurance contracts under OPS the following assumptions were made:

(a) Discount rate and pension indexation

The discount rate is the average yield at the reporting date on government bonds that have maturity dates approximating the terms of the Group's obligations taken as at 31 December 2014 and amounting to 11.96%.

The indexation rate is the discount rated adjusted for management companies' remuneration, special depositary remuneration as well as part of returns spent on managing of NPF Transneft.

(b) Mortality data

Mortality assumptions are based on historical experience regarding future improvents in mortality rated based on annuities. NPF Transneft's own mortality experience is regularly reassessed and analysed. NPF Transneft is using mortality data for Russian Federation population for 2011.

(c) Future contributions for adequacy test of amount of liability under insurance contracts under OPS.

To apply liability adequacy test for insurance contracts under OPS the annuity was calculated for men in 60 years old and women in 55 years old. These annuities are equal to 155 months and 238 months respectively. As a result the average annuity (including indexationa and discounting) is less than 228 months or 19 years which are used by Russian Federation Pension Fund for calculation of funded part of labour pension.

Liability under insurance contracts under NPO

Liabilities under insurance contracts are calculated by discounting future pension payments. The amount of future pension is the amount guaranteed under insurance contract, pension indexated from agreement date to the reporting date, as well as pension indexation forecast.

(a) Discount rate and pension indexation rate

According to the long-term investment policy of NPF Transneft fulfillment of obligations to participants and insured persons by NPF Transneft is to ensure the safety of funds.

To calculate obligations under insurance contracts under NPO NPF Transneft uses the inflation rate as a rate for pension indexation.

For discounting of pension liabilities NPF Transneft uses the discount rate equal to indexation rate. The effective discounting rate is equal to 0% p.a. accordingly.

(b) Mortality data

Mortality assumptions are based on historical experience regarding future improvents in mortality rated based on annuities. NPF Transneft's own mortality experience is regularly reassessed and analysed.

NPF Transneft uses mortality table for Russian Federation population for 2011 to calculate liabilities under insurance contracts under NPO for consolidated financial statements in accordance with IFRS.

Liabilities under investment contracts under NPO

Liabilities under investment contracts is the balance of participants' personal accounts as at the reporting date which is the amount of accumulated contributions, returns from investment of pension reserves less amount of benefits paid to the date.

(in millions of Russian roubles, if not stated otherwise)

19 TRADE AND OTHER PAYABLES, INCLUDING DERIVATIVES

	31 December 2014	31 December 2013
Trade payables	44,950	38,756
Other payables	85,339	9,999
Total financial payables	**130,289**	**48,755**
Less: Long-term portion of derivatives	(13,700)	(1,836)
Total current financial liabilities	**116,589**	**46,919**
Advances received for oil and oil product transportation services	48,481	42,013
Accrued expenses	24,627	26,026
VAT output tax payable	8,367	8,808
Other taxes payable	3,015	2,756
Total payables	**201,349**	**126,522**

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

Currency	31 December 2014			31 December 2013		
	Trade payables	Other payables	Total payables	Trade payables	Other payables	Total payables
Russian roubles	38,325	79,187	117,512	30,206	8,374	38,580
USD	6,625	2,363	8,988	8,523	1,154	9,677
Euro	-	1,407	1,407	-	441	441
Other	-	2,382	2,382	27	30	57
	44,950	**85,339**	**130,289**	**38,756**	**9,999**	**48,755**

Trade payables include payables for purchases of property, plant and equipment in amount RUB 30,734 as at 31 December 2014 and RUB 22,762 as at 31 December 2013.

Accrued expenses mainly include amounts of unused vacation allowance, provision for the annual bonus of the reporting year.

Derivatives

During the year ended 31 December 2014 in order to mitigate unfavourable consequences of the possible depreciation of US Dollar the Group in addition acquired put-options and sold call-options in the amount of USD 2,726.5 million with exercise dates in August – December 2014.

During 2013 in order to mitigate unfavourable consequences of the possible depreciation of US Dollar the Group had simultaneously acquired put-options and sold call-options in the amount of USD 4,247 million with exercise dates in May 2013 – October 2014. The carrying amount of a liability for these financial instruments was RUB 90 as at 31 December 2013 (Note 8).

The Group classified these contracts as derivatives at fair value through profit or loss.

Fair value measurement is based on Black-Scholes model, the inputs for which are observable in the market and the Group classified them to Level 2 in accordance with the fair value hierarchy.

In December 2013 the Group entered into the deal with the state-controlled bank and had simultaneously purchased barrier put-options with a delayed condition and sold barrier call-options with a delayed condition (hereinafter – barrier options) for the total amount of USD 1,999 million with the exercise date in September 2015 to reduce costs of servicing corporate bonds.

The Group classified this contract as a derivative recognised at fair value through profit and loss. Fair value measurement is based on Black-Scholes model, the inputs for which are observable in the market except for assumed volatility measure and the Group classified them to Level 3 in accordance with the fair value hierarchy.

At the date of transaction the excess of fair value of the liability of these derivatives over fair value of the premium receivable under the contract amounted to RUB 563 and was recognised as other financial asset (Note 8).

19 TRADE AND OTHER PAYABLES, INCLUDING DERIVAITES (continued)

In September-October 2014 the Group and the afore-mentioned bank entered into an interest rate swap transaction which assumes an exchange of one floating rate to another (float-to-float) based on an amortised nominal amount till 2029. In accordance with the deal the Group will make annual payments to the bank based on 6MLIBOR as at the dates of payment and the bank will make annual payments to the Group based on 6MLIBOR determined annually starting from the date of transaction; exchange of nominal amounts is absent. As part of the transaction the terms of the afore-mentioned transaction with barrier were revised and barrier level was increased, as well as new option contracts were entered into with exercise date in October-December 2014. The fair value of the interest rate swap transaction was estimated as the difference between present value of future net payments between the bank and the Group. Future payments were determined on the basis of 6MLIBOR forward rates provided by the Bloomberg.

The Group classified this transaction as a derivative at fair value with changes recognised in profit or loss. The Group classifies this interest-rate swap to Level 2 in accordance with the fair value hierarchy.

As at 31 December 2014 the carrying value of the liability of barrier options amounted to RUB 62,607 (RUB 1,836 as at 31 December 2013) and the carrying value of the liability for the interest rate swap amounted to RUB 13,779, both were recognized as other payables.

Implied volatility index which was used to estimate the fair value of the barrier options amounted to 45.2% as at 31 December 2014 (as at 31 December of 2013 - 9.3%).

Should the risk-free RUB rate increase / (decrease) by 3% while other input data remain constant the fair value of the liability would have increased / (decreased) by RUB 1,255 and RUB 1,283 respectively.

Should the exchange rate of the US dollar increase / (decrease) by 1 ruble while all other input data remain constant the fair value of the liability at the reporting date would have increased / (decreased) by RUB 1,997.

Should the floating 6MLIBOR interest rates increase / (decrease) by 10% the liability as at the reporting date would increase / (decrease) by RUB 1,471 and RUB 1,344 respectively.

(in millions of Russian roubles, if not stated otherwise)

20 REVENUE

	Year ended 31 December 2014	Year ended 31 December 2013
Revenues from crude oil transportation services		
Domestic tariff	224,450	216,074
Export tariff	275,388	290,610
Total revenues from crude oil transportation services	**499,838**	**506,684**
Revenues from oil products transportation services	48,186	42,580
Revenues from crude oil sales	193,147	165,326
Revenues from oil products sales	4,416	6,569
Revenues from oil compounding	4,633	5,310
Other revenues	24,160	23,148
	774,380	749,617

Revenues from crude oil sales for the year ended 31 December 2014 include, mostly, revenues from supplying of oil according to the agreement signed by the Company in February 2009. According to the agreement the oil will be supplied to China during 20 years since 1 January 2011 amounting to 6 million tons of oil per annum. The Group purchases the oil under the contract signed in April 2009 with OAO NK Rosneft (see Note 26).

The Group revenues from crude oil transportation services on the domestic pipeline network comprise:

- revenues for transportation of crude oil to destinations in the Russian Federation and the Custom Union countries, based on distance-related tariffs denominated and payable in RUB and revised periodically after approval by the Federal Tariff Agency (“domestic tariff”);
- revenues for transportation of crude oil which is destined for export (outside of the Russian Federation and the Custom Union countries), based on distance-related tariffs denominated in RUB and payable in RUB and revised periodically after approval by the Federal Tariff Agency (“export tariff”);
- revenues for transportation of transit crude oil from Azerbaijan to export destinations through the territory of the Russian Federation to the Novorossiysk’s port, based on fixed tariff approved by intergovernmental agreement (“export tariff”) and paid for in USD;
- revenues for transportation of transit crude oil from Kazakhstan, based on the tariffs which are set by the Federal Tariff Agency and paid for in RUB (“export tariff”).

Revenue from oil products transportation includes revenue from oil product transportation in the Russian Federation, in Belarus and in the Ukraine and Kazakhstan.

Revenue from domestic transportation of oil products is formed on the basis of tariffs which are set within limits imposed by government regulations and includes:

- revenue for oil products transportation services in the territory of the Russian Federation and countries of the Customs Union which is based on tariffs set and paid for in RUB;
- revenue for oil products transportation services for export outside the territory of the Russian Federation and countries of the Customs Union at tariffs set and paid for in RUB;

Revenue from oil product transportation in Belarus is formed on the basis of tariffs set in US Dollars by the relevant regulatory body of the Belarusian Republic in compliance with the Treaty between the governments of the Russian Federation and the Belarusian Republic on cooperation in operating oil product pipelines, located on the territory of the Belarusian Republic. These services are paid for in USD.

Revenue from oil product transportation services in the Ukraine is formed on the basis of tariffs set by OAO AK Transneft in US Dollars calculated using the amount of expenses needed for normal operation of oil product transporting companies. These services are paid for in USD.

Revenue from oil product transportation services in the Kazakhstan is formed on the basis of tariffs set by OAO AK Transneft in Kazakh tenge calculated using the amount of expenses needed for normal operation of oil product transporting companies. These services are paid for in RUB at the exchange rate set by CBR at the date of payment.

(in millions of Russian roubles, if not stated otherwise)

21 OPERATING EXPENSES

	Year ended 31 December 2014	Year ended 31 December 2013
Amortisation and depreciation	111,818	102,261
Salaries	90,704	88,724
Social Funds contributions	20,329	19,600
Social expenses	3,429	3,218
Energy	32,043	32,089
Transportation of oil using railways	2,404	6,515
Materials	22,999	22,009
Repairs and maintenance services	13,608	14,328
Cost of crude oil sold	106,369	89,244
Customs duties	79,812	74,422
Cost of oil products sold	4,107	6,205
Insurance expense	6,126	6,717
Net change in doubtful debt provision	919	205
Net change in impairment provision of property, plant and equipment	721	193
Business trip expense	5,740	5,996
Property tax and other taxes other than profit tax	12,309	10,153
Pension expenses	11,614	4,405
Other expenses	16,002	12,850
	541,053	499,134

Transportation of oil by using railways comprises transportation of oil by railway from Skovorodino to port Kozmino.

Other expenses comprise of income and expenses from disposal of fixed assets, the gain from oil surplus, expenses on charity, both received and paid penalties, and also other operating income and expenses.

22 NET FINANCE COSTS

	Year ended 31 December 2014	Year ended 31 December 2013
Interest income on cash and cash equivalents	4,275	5,380
Interest income from other financial assets	15,265	13,746
Other interest income	366	304
Total interest income	**19,906**	**19,430**
less interest income on the temporary investment of borrowings	(839)	(2,798)
Total interest income recognised in statement of profit or loss and other comprehensive income	**19,067**	**16,632**
Foreign exchange gains	284,609	72,367
Total finance income	**303,676**	**88,999**
Interest expense on borrowing cost	34,656	34,096
Provisions for asset retirement obligations: unwinding of the present value discount	2,329	5,777
Other interest expenses	1,589	1,132
Total interest expenses	**38,574**	**41,005**
Less capitalised finance costs	(2,071)	(3,911)
Total interest expenses recognised in the statement of profit or loss and other comprehensive income	**36,503**	**37,094**
Foreign exchange loss	326,778	78,154
Net loss from derivatives	75,289	52
Total finance costs	**438,570**	**115,300**
Total net finance costs	**134,894**	**26,301**

(in millions of Russian roubles, if not stated otherwise)

23 SUBSIDIARIES, ASSOCIATES AND JOINTLY CONTROLLED ENTITIES

The following are the principal subsidiaries which have been consolidated and associates and jointly controlled entities accounted for using equity method in these consolidated financial statements:

	Type of activity	Country of incorporation	Percentage (%) of ownership interest at 31 December 2014
Subsidiaries, associates and jointly controlled entities "Oil transportation" segment			
AO Transneft - Sibir	crude oil transportation	Russia	100.0
AO Chernomortransneft	crude oil transportation	Russia	100.0
AO Transneft - Druzhba	crude oil transportation	Russia	100.0
AO Transneft - Privolga	crude oil transportation	Russia	100.0
AO Transneft – Zapadnaya Sibir	crude oil and oil products transportation	Russia	100.0
AO Transneft – Verkhnyaya Volga	crude oil and oil products transportation	Russia	100.0
AO Transneft – Tsentralnaya Sibir	crude oil transportation	Russia	100.0
AO Transneft – Sever	crude oil transportation	Russia	100.0
OOO Transneft - Baltika	crude oil and oil products transportation	Russia	100.0
AO Transneft - Ural	crude oil and oil products transportation	Russia	100.0
OAO SZMN	crude oil transportation	Russia	64.0
OOO Transneft - Vostok	crude oil transportation	Russia	100.0
OOO Transneft – Dalniy Vostok	crude oil transportation	Russia	100.0
AO Giprotruboprovod	project and designed work for oil pipeline	Russia	100.0
AO Svyaztransneft	technological connection	Russia	100.0
AO Transneft - Diascan	diagnostics	Russia	100.0
AO Transneft - Podvodservice	diagnostics, repair and maintenance of underwater line	Russia	100.0
ZAO Tsentr MO	metrological support	Russia	100.0
OOO Transneft - Port Primorsk	loading and off-loading and oil and oil products transshipment	Russia	100.0
OOO Transneft – Media	press	Russia	100.0
OOO TsUP VSTO	constructor of ESPO	Russia	100.0
OOO Transneft Finance	accounting	Russia	100.0
OOO Transneft - Port Kozmino	loading of oil and oil products	Russia	100.0
OOO Transneftenergo	electric power transmission	Russia	100.0
OOO Transneft-Servis	port facilities	Russia	100.0
AO Transneft - Energoterminal	organisation of cargo	Russia	50.04
AO Transneftsvyazstroy	general contractor	Russia	100.0
OOO DSD	construction of ESPO-2	Russia	100.0
OOO Transneft - TSD	provision of general construction services	Russia	100.0
OOO Transneft – Port Ust-Luga	port facilities	Russia	100.0
OOO Transneft-Logistika	transportation of cargo	Russia	100.0
OOO Transneftstroy	general pipe contractor	Russia	100.0
OOO Transneftstroy–Bryansk	general construction works	Russia	100.0
OOO Transneftstroy–Omsk	general construction works	Russia	100.0
OOO Transneftstroy–Tyumen	general construction works	Russia	100.0
Fenti Development Limited	financial activity	Switzerland	100.0
OOO Transneft-Terminal	organization of transhipment of crude oil and oil prodructs	Russia	75.0

(in millions of Russian roubles, if not stated otherwise)

23 SUBSIDIARIES, ASSOCIATES AND JOINTLY CONTROLLED ENTITIES

	Type of activity	Country of incorporation	Percentage (%) of ownership interest at 31 December 2014
Subsidiaries, associates and jointly controlled entities "Oil transportation" segment			
AO Transneft Neftyanniye Nasosy	production	Russia	51.0
OOO Rusenergoresurs *	wholesale of electric and heat power	Russia	25.0
OOO TK-BA *	designing and construction of "Burgas – Alexandroupolis" pipeline	Russia	33.34
ZAO PROMSFERA	rent	Russia	100.0
OOO Impex-Plus *	wholesale agent	Russia	50.0
OOO Tikhoretsk –Nafta	cargo handling	Russia	100.0
ZAO Transneft-Servis	crude oil sea and domestic water transportation	Russia	100.0
AO TNT	cargo handling	Russia	100.0
ZAO Omega	production of monitoring systems of pipe-lines	Russia	60.0
OOO NII Transneft	research	Russia	100.0
OOO TES	transmission of electricity	Russia	100.0
OOO TsRIVIS	development, tuning and implementation of automated management systems	Russia	100.0
OOO Transneft Nadzor	technical and building supervision and control	Russia	100.0
OOO Sigma Telecom	telecommunications	Russia	100.0
OOO Transneft – Okhrana	security services	Russia	100.0
OAO Novorossiysk Commercial Sea Port *	cargo handling	Russia	35.57
OOO PTP *	cargo handling	Russia	35.57
OOO Avesta and Co.	construction of buildings	Russia	100.0
Omirico Ltd. *	financial activity	Cyprus	50.0
Subsidiaries and associates, "Oil product transportation" segment			
OAO Mostransnefteproduct	oil product transportation	Russia	100.0
OAO Yugo-Zapad transnefteproduct	oil product transportation	Russia	100.0
OAO Sredne-VolzhskyTransnefteproduct	oil product transportation	Russia	100.0
Unitarnoye predpriyatiye Zapad-Transnefteproduct	oil product transportation	Belarus	100.0
DP PrikarpatZapadtrans	oil product transportation	Ukraine	100.0
OAO AK Transnefteproduct	oil product transportation	Russia	100.0
OOO ChOP STNP	security	Russia	100.0
OAO TD Transnefteproduct	integrated storage	Russia	100.0
OAO Telecomnefteproduct	communication services	Russia	100.0
DP Rovensky Tsekh Elektrosvyazi	communication services	Ukraine	100.0
Unitarnoye predpriyatiye Zapad-Telecomnefteproduct	communication services	Belarus	100.0
OOO LatRosTrans *	oil product transportation	Latvia	34.0

* equity accounted investees or jointly controlled entities

(in millions of Russian roubles, if not stated otherwise)

24 OPERATING LEASES

The Group leases a number of land plots, mainly, owned by local governments under operating lease. Land lease payments are determined by lease agreements and are as follows:

	31 December 2014	31 December 2013
Less than one year	1,067	987
Between one year and five years	4,267	3,946
After five years	48,004	44,397
Total	**53,338**	**49,330**

The land areas leased by the Group are the territories on which the Group the oil pipeline, the oil product pipeline and other assets are located. Most contracts for land lease are long term and concluded for duration up to 49 years with subsequent prolongation. In accordance with contracts for land lease the land title does not pass. After contract term expiration it can be terminated.

The rent paid to the landlord of the land is increased in accordance with the contractual terms at regular intervals, and the Group does not participate in the value of the land, it was determined that substantially all the risks and rewards of the land are with the landlord. As such, the Group determined that the leases are operating leases.

During the year ended 31 December 2014 RUB 569 (2013: RUB 535) was recognised in profit or loss in respect of operating lease.

25 CONTINGENT LIABILITIES, COMMITMENTS AND OTHER RISKS

Legal proceedings

During the year ended 31 December 2014 the Group was involved in a number of court proceedings arising in the ordinary course of business. In the opinion of the Group's management, there are no current legal proceedings or claims outstanding at 31 December 2014, which could have a material adverse effect on the results of operations or financial position of the Group.

Dismantlement provision

Usage by the Group of pipeline network results in accrual of contingent liability in connection with dismantlement of trunk pipelines as well as site restoration. It is not possible to reliably estimate the period of liquidation and thus measure the amount of dismantlement provision because the pipeline network is under regular diagnostics, maintained properly, periodically upgraded and reconstructed, which leads to the extension of its useful life. Starting from 2014 the Group recognizes dismantlement provision in the consolidated financial statements only in periods when necessary and sufficient information for estimating of dismantling liability, assessing of terms and amount of dismantling becomes available.

Cost of replacement of 1 km of trunk oil pipelines and oil products pipelines including site restoring costs significantly differs depending on the region and complexity of works.

26 RELATED PARTIES AND KEY MANAGEMENT PERSONNEL COMPENSATION

The Russian Federation, through the Federal Agency for the Management of Federal Property, owns 100% of the ordinary shares of the Company and controls its operations through Board members represented by the Ministry of Energy, other Federal bodies, and independent companies. The Government also appoints the members of the Federal Tariff Agency which sets the tariff rates.

As at 31 December 2014 and 31 December 2013 Company holds in trust on behalf of the Russian Government 100% of the shares of the CPC Investments Company, 100% of the shares of the CPC Company, 7% of the ordinary shares of the Caspian Pipeline Consortium-R and 7% of the ordinary shares of Caspian Pipeline Consortium–K and also 24% of the ordinary shares of the Caspian Pipeline Consortium-R and 24% of the ordinary shares of Caspian Pipeline Consortium–K. These interests are not recognised in these consolidated financial statements as the Company is acting as an agent on behalf of these Russian Government.

The Group's transactions with other state-controlled entities occur in the normal course of business and include, but are not limited to the following: purchase of electricity for production needs, transportation of oil produced by state-owned entities, and transactions with banks, which are under common control or significant influence of the state.

(in millions of Russian roubles, if not stated otherwise)

26 RELATED PARTIES AND KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

The Group had the following significant transactions with entities, which are under common control or significant influence of the state:

	Year ended 31 December 2014	Year ended 31 December 2013
Revenue from oil transportation services	246,872	231,149
OAO NK Rosneft and its subsidiaries	218,424	203,303
OAO Gazprom and its subsidiaries	27,994	27,354
Others	454	492
Revenue from oil products transportation services	20,999	18,843
OAO NK Rosneft and its subsidiaries	8,694	8,276
OAO Gazprom and its subsidiaries	12,305	10,567
Purchases of oil (OAO NK Rosneft)	83,243	78,417
Transportation of oil using railways and related services (OAO RZD and its subsidiaries)	2,641	7,270
Electricity expenses	384	426
Interest income from other financial assets	6,629	10,843
Transportation expenses	674	862

During the year ended 31 December 2014 and 31 December 2013, Group had following transactions with associates and jointly controlled entities:

	Year ended 31 December 2014	Year ended 31 December 2013
Revenue	2,444	2,128
Purchases of goods and services	29,590	31,387

At the 31 December 2014 and 31 December 2013, Group had following accounts with associates and jointly-controlled entities:

	31 December 2014	31 December 2013
Trade and other receivables	2,523	1,443
Trade and other payables	378	472
Loan issued	9,764	5,679
Loan received	1,158	663

Key management personnel compensation

Key management personnel (the members of the Board of Directors and Management Committee of the Company and general directors of subsidiaries) receive short-term compensations, including salary, bonuses, other payments and long-term and short-term interest-free loans. Short-term compensations payable to the key management personnel of the Company and subsidiaries consists of contractual remuneration for their services in full time executive positions. The remunerations for the members of the Boards of Directors of Company are subject to approval by the General Meeting of Shareholders.

According to Russian legislation, the Group makes contributions to the Russian Federation State pension fund for all of its employees including key management personnel. Key management personnel also participate in certain post-retirement compensation programs. The programs include pension benefits provided by the non-governmental pension fund, NPF Transneft, and one-time payments at the retirement date.

	Year ended 31 December 2014	Year ended 31 December 2013
Salaries and bonuses	1,528	1,414
Termination benefits	17	8
Other	21	11
	1,566	**1,433**

(in millions of Russian roubles, if not stated otherwise)

26 RELATED PARTIES AND KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

Amounts of loans issued to key management personnel were as follows:

	2014	2013
1 January	7	8
Repaid	(1)	(1)
31 December	6	7
due for repayment during 1 year	1	1
due for repayment after 1 year	5	6

During the year ended 31 December 2014 the Group contributed to NPF Transneft in favour of the key management personnel RUB 195 (for 2013 – RUB 58).

Contribution to the Pension Fund Transneft represent transfer to the fund of the present value of future pension values in connection with retirement in accordance with the terms of contracts for non-state pension benefits. These payments will be made when the right to receive the pensions in accordance with established rules of NPF Transneft vest.

Key management personnel for whom information was disclosed in the consolidated financial statements include members of the Board of Directors and the Board of OAO AK Transneft, as well as CEOs and their families (including change of management during the reporting periods) of subsidiaries that are considered as the most significant in the implementation of productive activities of the Group.

Total quantity of the persons who have received payments as the key management personnel as for the year ended 31 December 2014 constituted 64 persons (for the year ended 31 December 2013 – 62 persons).

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

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

	Loans and receivables	Financial assets at fair value through profit or loss	Available-for-sale financial assets
Assets as per balance sheet			
31 December 2014			
Cash and cash equivalents (Note 12)	113,060	-	-
Financial assets at fair value through profit or loss(Note 8)	-	33,482	-
Available-for-sale financial assets	-	-	231
Other non-current financial assets (Note 9)	42,823	-	-
Other current financial assets (Note 9)	405,802	-	-
Accounts receivable (trade and other) (Note 11)	31,511	-	-
	593,196	**33,482**	**231**
31 December 2013			
Cash and cash equivalents (Note 12)	104,742	-	-
Financial assets at fair value through profit or loss (Note 8)	-	90	-
Available-for-sale financial assets	-	-	217
Other non-current financial assets (Note 9)	19,297	-	-
Other current financial assets (Note 9)	300,911	-	-
Accounts receivable (trade and other) (Note 11)	31,975	-	-
	456,925	**90**	**217**

(in millions of Russian roubles, if not stated otherwise)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

	31 December 2014	31 December 2013
Liabilities as per balance sheet		
Accounts payable (trade and other) (Note 19)	130,289	48,755
Loans and borrowings (Note 16)	759,192	580,558
	889,481	629,313

The Group's activities expose it to a variety of financial risks: foreign exchange risk, interest rate risk, commodity price risks, credit risk and liquidity risk.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

Foreign exchange risk

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble, the US dollar or the Euro. The Group does not use foreign exchange or forward contracts. The Group's foreign exchange exposure mainly arises on USD and Euro-denominated borrowings, which the Group obtained in 2007-2010 (see Note 16) and USD and Euro-denominated cash balances. Assets and liabilities denominated in Ukrainian hryvna or the Belarusian rouble which give rise to foreign currency exchange exposure are insignificant.

As at 31 December 2014, if the USD had strengthened/weakened by 10% against the Russian rouble, with all other variables left constant, after tax profit and equity would have been RUB 9,944 lower/higher (for the year ended 31 December 2013 if the USD had strengthened/weakened by 10% against the Russian rouble, with all other variables held constant, after tax profit and equity would have been – RUB 4,320 lower/higher), mainly as a result of foreign exchange losses/(gains) on translation of USD-denominated borrowings and USD-denominated cash balances into Russian roubles.

As at 31 December 2014, if the Euro had strengthened/weakened by 10% against the Russian rouble, with all other variables left constant, after tax profit and equity would have been RUB 41 higher/lower (for the year ended 31 December 2013 if the Euro had strengthened/weakened by 10% against the Russian rouble, with all other variables held constant, after tax profit and equity would have been RUB 30 higher/lower) as a result of foreign exchange losses on translation of Euro-denominated borrowings and Euro-denominated cash balances into Russian roubles.

Interest rate risk

Management has a formal policy of determining how much the Group's exposure should be to fixed or variable rates. At the time of raising new loans or borrowings management uses its judgment, economic feasible and risk assessment to decide whether it believes that a fixed or variable rate would be more favorable to the Group over the expected period until maturity.

As the Group had no assets bearing significant interest, the Group's income and operating cash flows were substantially independent of changes in market interest rates on assets.

Borrowings received at fixed rates expose the Group to fair value interest rate risk. The Group obtains borrowings from banks at current market interest rates and does not use any hedging instruments to manage its exposure to changes in interest rates. The Group does not account for any of its fixed rate financial assets and liabilities at fair value through the profit and loss. Therefore, a change in interest rates at the reporting date would not affect profit or equity.

Loans and borrowings received by the Group under variable interest rate expose the Company to the risk of changes in the cash flows under loans and borrowings. As the Group received bank loans for financing its investment projects, the part of borrowing costs are capitalised. An increase of 1% in interest rates for the year ended 31 December 2014 would have decreased equity and profit for the period before income tax by RUB 4,910 (year ended 31 December 2013 – RUB 4,178). This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

Commodity price risk

The Group's principle activities include technical maintenance, replacement of the existing pipelines and construction of new pipelines. These require annual purchases of a significant number of metal pipes for replacement and construction of new pipelines.

The Group concluded framework agreements with pipes producers, under which the delivery price and delivery dates are not fixed at the moment of signing these agreements. In addition, the Group has no long-term contracts with oil producing companies (except agreement on crude oil delivery with OAO NK Rosneft) and refineries and does not use the additional contracts to manage the risks associated with changes in metal prices and prices for oil and oil product.

(in millions of Russian roubles, if not stated otherwise)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

Credit risk and compliance with contractual terms and obligations

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investments.

The Group has an approved policy in accordance with which it regularly assesses crediworthness of banks it deals with and reviews limit for allocation of cash.

The Group's policy is generally to transact with its customers on a prepayment basis. Its trade accounts receivable are unsecured. Being the subject of natural monopolies on the Russian transportation market the Group ensures equal access to the oil and oil product pipeline for all russian oil refining and oil products companies. The majority of the Group's customers are the major oil companies of the Russian Federation including those controlled by the State. The Group has no material concentrations of credit risk or any material past due accounts receivable.

Credit risk is managed on a Group basis. For certain customers there is no independent rating and therefore thtr Group assesses the credit quality of the customer, taking into account its financial position, past experience and other factors. The credit quality of financial assets that are neither past due nor impaired are assessed with the reference to historical information about counterparties, which are existing customers with no defaults in the past.

The Group's suppliers of assets and services are selected mainly through tenders. The criteria for the bidders include both technical and financial indicators (availability of production facilities, skilled personnel, relevant experience, cost of assets and services etc.) and reliability (financial position, professional and ethical image of the bidders, whether quality control of the assets and services is established). The tender approach is designed to ensure the selection of suppliers with a low risk of failure to discharge their contractual obligations.

An analysis cash and cash equivalents with reference to external credit ratings of credit quality of major banks in which the Group holds cash and cash equivalents is presented in the table below. The relevant credit ratings were published by Moody's Investor Service.

Credit rating	31 December 2014
External credit rating Baa1 – Baa3	19,776
External credit rating Ba1 – Ba3	60,185
External credit rating B1 – B3	32,205
	112,166

Financial assets at fair value through profit or loss are acquired from counterparties with the following Moody's credit ratings or other credit agencies ratings adjusted to Moody's rating scale.

Credit rating	31 December 2014
External credit rating Aaa	186
External credit rating Baa1 – Baa3	13,792
External credit rating Ba1 – Ba3	17,297
External credit rating B1 – B3	1,581
No credit rating assigned	626
	33,482

Information about credit quality of short-term financial assets (excluding equity securities) is presented in the table below with reference to external credit ratings of related counterparties or instruments (published by Moody's and other rating agencies). The table below uses Moody's rating classification.

Credit rating	31 December 2014
External credit rating Baa1-Baa3	995
External credit rating Ba1-Ba3	404,408
External credit rating B1-B3	30,332
No credit rating assigned	3,111
Total	**438,846**

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the consolidated statement of financial position.

Risks associated with securities under trust management

The Group is exposed to changes in equity price risk. Management companies which are entered into trust management agreements control operations with securities in accordance with approved investment declaration which sets the structure and ratio between debt and equity securities and cash levels which management companies must maintain. The specialized depositary also controls compliance with investment declarations on a daily basis.

(in millions of Russian roubles, if not stated otherwise)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

To manage other price risk the Group uses periodic estimation of potential losses which can be incurred because of negative market changes as well as sensitivity analysis of profit or loss for the year to changes in shares prices in accordance with a symmetrical increase or decrease scenario for a certain percentage points.

Sensitivity analysis of net profit to changes in price of shares (computed on positions open as at 31 December 2014 and simplified scenario for 10% decline or increase in all share prices) can be shown as follows:

	31 December 2014
	Profit (loss) before taxation
10% increase in securities' quotes	3,292
10% decline in securities' quotes	(3,292)

Insurance risk

For insurance contracts for payment of benefits under guaranteed pensions where insurance risk is the mortality risk the main factor is the improvement of medical services and social conditions which increase life expectancy.

Insurance risk management is performed by permanent observation of actual mortality of participans. Currently the actual mortality rate as well as its changes are consistent with expectations. To fulfill already taken obligations the part of investment returns from allocation of pension reserves including insurance reserve will be used.

The table below shows sensitivity analysis of insurance contract liabilities under non-state pension as at 1 January 2014:

Obligation under insurance contracts of NPO		31 December 2014
Change in obligation in relation to obligation as at reporting date		
Analysis of change in liability in case of change in discount rate	-1 p.p.	10.94%
	+1 p.p.	-9.23%
Analysis of change in liability in case of change in assumption of indexation of pensions	-1 p.p.	-9.31%
	+1 p.p.	10.83%
Analysis of change in liability in case of change in assumption of mortality	-10%	5.20%
	+10%	-4.58%

(*) p.p. – percentage point

Liability adequacy test for insurance contracts under OPS would not result in a deficit in all cases when indexation rate does not exceed discount rate. NPF Transneft estimated the minimal discount rate (with fixed indexation rate used in calculation as at the reporting date) equal to 9.85% and maximal indexation rate (with discount rate left unchanged at the reporting date) equal to 12.17% when the test will result in zero.

A decline in mortality probability by 44% will lead to a zero result in liability adequacy test relating to insurance contracts under OPS.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Prudent liquidity risk management includes maintaining sufficient cash and availability of funding from an adequate amount of committed credit facilities. Group maintains flexibility in funding by maintaining availability under committed credit lines.

Offseting and similar agreements

The Group may conclude agreements for purchase and sale with same counterparties in the ordinary course of business. Relevant amounts of receivables and payables are not always available for offsetting in the statement of financial position. This is due to the fact that the Group may not have currently legally enforceable right to offset the recognized amounts, since the right of set-off may be valid only when certain events occur in the future. In particular, in accordance with civil law in force in Russia, the obligation may be settled by offsetting uniform requirements, which are due either not specified or determined by the time on demand.

(in millions of Russian roubles, if not stated otherwise)

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

The following are the carrying values of recognised financial instruments under the afore-mentioned contracts:

	Trade and other receivables	Trade and other payables
31 December 2014		
Gross amounts	31,511	130,289
Net amounts shown in the consolidated statement of financial position	31,511	130,289
Amounts relating to recognised financial instruments which can not be offset	(8,831)	(8,831)
Net amount	**22,680**	**121,458**

	Trade and other receivables	Trade and other payables
31 December 2013		
Gross amounts	31,975	48,755
Net amounts shown in the consolidated statement of financial position	31,975	48,755
Amounts relating to recognised financial instruments which can not be offset	(5,798)	(5,798)
Net amount	**26,177**	**42,957**

The following are the contractual undiscounted cash flows of financial liabilities, including estimated interest payments:

31 December 2014:

	Carrying amount	Contractual cash flows				
		Total	12 months or less	1-2 years	2-5 years	More than 5 years
Loans and borrowings	759,192	933,004	218,440	75,898	224,547	414,119
Trade and other payables	130,289	130,289	130,289	-	-	-
	889,481	**1,063,293**	**348,729**	**75,898**	**224,547**	**414,119**

31 December 2013:

	Carrying amount	Contractual cash flows				
		Total	12 months or less	1-2 years	2-5 years	More than 5 years
Loans and borrowings	580,558	715,211	121,461	186,233	136,375	271,142
Trade and other payables	48,755	48,755	48,755	-	-	-
	629,313	**763,966**	**170,216**	**186,233**	**136,375**	**271,142**

Fair values

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. The fair value of the trade receivables and payables approximates their carrying amounts at 31 December 2014 and 31 December 2013. The fair values of loans, borrowings are disclosed in Note 16.

Capital management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. For this purpose, the Group's capital is considered to be equity attributable to the shareholders of the Company and the long-term and short-term debt (long-term and short term borrowings and trade and other payables). In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, issue new shares, attract new or repay existing loans and borrowings.

Within the framework of capital management for the purpose of maintaining major debt parameters at the optimal level, the Group's management monitors its key financial indicators, such as total debt/EBITDA, total debt/equity and cash from operating activities/total debt; that allows the Group at the maximum available for Russian companies level.

There were no changes in the Group's approach to capital management during the reporting period.

(in millions of Russian roubles, if not stated otherwise)

28 SEGMENT INFORMATION

Generally, Management of the Group analyses information by separate legal entities and operational segments are set by nature of its activity based on management accounting under Russian Accounting Standards (RAS). The following segments were allocated: Oil transportation services, Oil product transportation services and Sales of oil and oil products.

Adjusting entries used to reconcile this information with information in the consolidated financial statements primarily include adjustments and reclassifications resulting from differences between RAS and IFRS.

Segment information for the years ended 31 December 2014 and 31 December 2013 was as follows:

Year ended 31 December 2014	Oil transporta-tion services	Oil products transportation services	Trading operations for sale of oil and oil products	Adjust-ments	Total IFRS
Revenue					
Revenue from sales to third parties	524,272	49,828	197,068	3,212	774,380
Operating expenses	(339,496)	(29,598)	(191,213)	19,254	(541,053)
including depreciation	(132,173)	(5,068)		25,423	(111,818)
Operating profit	184,776	20,230	5,855	22,466	233,327
Finance income	-	-	-	-	303,676
Finance costs	-	-	-	-	(438,570)
Changes in the Group's structure	-	-	-	-	8,796
Share of loss from associates and jointly controlled entities					(10,786)
Profit before income tax	184,776	20,230	5,855	22,466	96,443
Income tax expense	-	-	-	-	(36,943)
Profit for the year	184,776	20,230	5,855	22,466	59,500

Year ended 31 December 2013	Oil transporta-tion services	Oil products transportation services	Trading operations for sale of oil and oil products	Adjust-ments	Total IFRS
Revenue					
Revenue from sales to third parties	532,718	44,647	171,821	431	749,617
Operating expenses	(320,603)	(25,077)	(171,417)	17,963	(499,134)
Including depreciation	(122,364)	(3,918)	-	24,021	(102,261)
Operating profit	212,115	19,570	404	18,394	250,483
Finance income	-	-	-	-	88,999
Finance costs	-	-	-	-	(115,300)
Changes in the Group's structure	-	-	-	-	2,848
Share of profit from associates and jointly controlled entities	-	-	-	-	(15,018)
Profit before income tax	212,115	19,570	404	18,394	212,012
Income tax expense	-	-	-	-	(53,995)
Profit for the year	212,115	19,570	404	18,394	158,017

(in millions of Russian roubles, if not stated otherwise)

28 SEGMENT INFORMATION (continued)

Adjusting items for segment's expenses in the amount of RUB 19,254 for the year ended 31 December 2014 and RUB 17,963 for the year ended 31 December 2013 include the following adjustments and reclassifications due to RAS and IFRS accounting differences:

	Year ended 31 December 2014	Year ended 31 December 2013
Dismantlement provision	(1,124)	1,007
Adjustment to Property plant and equipment to eliminate RAS revaluation effect and to record adjustment required under IAS 29 "Financial reporting in hyper-inflationary economies"	(23,947)	(19,994)
Pension liabilities	7,693	(676)
Deferred payment obligation	(1,913)	1,284
Others	37	416
Total adjusting items for segment's expenses	**(19,254)**	**(17,963)**

Geographical information. The Group's most part of assets attributable to reporting segments is primary located in the territory of the Russian Federation which results in the operating activity by each segment being carried out in the territory of the Russian Federation. Geographical information on revenue from external customers is presented based on the customers' country of incorporation; the majority of revenues are generated by assets located in the Russian Federation. The oil product transportation segment has certain assets located on the territory of Latvia, Ukraine and Belarus.

Information on revenue allocation by customers' country of incorporation is set out below:

	Year ended 31 December 2014	Year ended 31 December 2013
Russian Federation	583,728	569,791
China	168,515	153,688
Other countries	22,137	26,138
	774,380	**749,617**

Revenue from external customers in other countries mainly includes revenue from services provided to customers in Kazakhstan, Belarus and Ukraine.

Major customers. The Group's major customers are oil production companies which produce oil and transport it for export domestic sale or refining.

The information about largest customers of the Group is presented below:

	Year ended 31 December 2014	Year ended 31 December 2013
Companies under control of the state	267,871	249,992
China National United Oil Corporation	168,515	153,688
OAO Surgutneftegaz	92,299	87,872
OAO Lukoil	77,540	72,053
OAO TNK-BP Holding*	-	13,347
	606,225	**576,952**

* Revenue from OAO TNK-BP Holding is considered as revenue from the companies under control of the Russian Federation starting from the date when OAO TNK-BP Holding was acquired by OAO NK Rosneft.

Sales to the major customers are included in the results of the crude oil transportation, oil product transportation segments and trading operations for sales of oil and oil products.

29 EVENTS AFTER THE REPORTING DATE

In January 2015 the Group acquired from OAO Svyazinvestneftekhim non-controlling interest of 36% (251,956 ordinary shares with par value at RUB 1) of OAO SZMN. In accordance with the agreement the consideration is paid out in cash.

Bound, numbered and sealed on 49 *(forty nine)* pages.

Kim A.A.
Director AO KPMG