AO SIBERIAN OIL COMPANY

CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 1997 AND 1996
TOGETHER WITH
REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders of AO Siberian Oil Company:

We have audited the accompanying consolidated balance sheets of AO Siberian Oil Company, a Russian open joint stock company, and subsidiaries as of December 31, 1997 and 1996, and the related consolidated statements of operations, changes in shareholders' capital and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as discussed in the following paragraph, we conducted our audits in accordance with generally accepted auditing standards in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As of the date of issuance of this report, an independent evaluation of the Company's oil and gas reserves ("reserve report"), as of December 31, 1997, had not been completed. Accordingly, we were unable to obtain sufficient evidence to form an opinion regarding the basis on which oil and gas properties and the related provision for depreciation, depletion and amortization are stated as of and for the year ended December 31, 1997.

In our opinion, except for the effects on the financial statements for 1997 of such adjustments, if any, as might have been disclosed with respect to oil and gas properties and the related provision for depreciation, depletion and amortization had an independent reserve report been available, as discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of AO Siberian Oil Company and subsidiaries as of December 31, 1997 and 1996, and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles in the United States.

As explained in Note 3 to the financial statements, the Company has given retroactive effect to the change in accounting for future site restoration costs.

Without qualifying our opinion, we draw attention to Notes 2 and 14 to the financial statements. Note 2 discusses the possible effect of future movements in exchange rates on realization of non-monetary assets in US dollar terms. Note 14 discusses the current status of negotiations with Federal tax authorities on the tax arrears of a subsidiary of the Company.

ARTHUR ANDERSEN ZAO　　　　UNICON M/S CONSULTING GROUP

Moscow, Russia
April 28, 1998 (except for certain matters discussed in Note 22, as to which the date is May 27, 1998)

1. The Company

Description of Business

AO Siberian Oil Company (the "Company" or "Sibneft") is a vertically integrated Russian oil company. Its principal activities concern oil and gas exploration, production, refining and marketing.

The Company was created by Presidential Decree Number 872 dated August 24, 1995. On September 29, 1995 Sibneft's charter was approved when the Government of the Russian Federation issued Resolution Number 972. The Omsk Registration Chamber officially registered Sibneft on October 6, 1995. For the purpose of these financial statements, the date of inception of Sibneft is considered to be September 30, 1995.

Under the terms of the Presidential Decree, Sibneft received 51 percent of the voting common shares (38 percent of the charter capital) belonging to the Russian Federation in four companies: Noyabrskneftegaz ("Noyabrsk"), Omsk Refinery ("OR"), Noyabrskneftegasgeophysica ("Geofizika") and Omsknefteprodukt ("Nefteprodukt").

Noyabrsk is primarily engaged in the exploration, production and development of oil and gas from its fields in the south Yamalo-Nentsk autonomous region and the northern part of the Khanti-Mansisk autonomous region. OR's principal activity is the production of refined petroleum products at its refinery in Omsk, Western Siberia. Nefteprodukt carries out marketing operations through its retail outlets in the Omsk region. Geofizika provides exploration and technical services in the Noyabrsk region. Historically, Noyabrsk had close business relationships with both Geofizika and OR, while OR had close business links not only with Noyabrsk but also Nefteprodukt. The consolidation of these companies under Sibneft's control has had a significant impact on the method of operation of each of the companies.

Acquisition of Additional Shares in Subsidiaries

During 1997, Noyabrsk and Geofizika issued additional shares, which were acquired by the Company. As a result, the Company's ownership percentage of voting common shares in Noyabrsk and Geofizika increased to 78.5 percent and 68 percent, respectively, as of December 31, 1997 (65.5 percent and 51 percent, respectively, of total charter capital). The Company acquired the additional shares in the two subsidiaries for a consideration of US$ 318 million. The 'negative goodwill' arising from this transaction has been set-off, in consolidation, against oil and gas properties (see Note 9).

Russian Environment

Over recent years, Russia has undergone substantial political, economic and social change. As an emerging market, Russia does not possess a well-developed business and regulatory infrastructure that would generally exist in a more mature free market economy. As a result, operations carried out in Russia involve significant risks that are not typically associated with those in developed markets. Instability in market reform could subject the Company to unpredictable changes in the basic business infrastructure under which it currently carries out its operations. Uncertainties regarding the political, legal, tax or regulatory environment, including the potential for adverse changes in any of these factors could significantly affect the Company's ability to operate commercially. Management is unable to estimate what changes may occur or the resulting effect of any such changes on the Company's financial condition or future results of operations.

Establishment of Prices

Prior to 1995, the Russian government determined the domestic price for the sale of crude oil that was significantly lower than the price for which the same crude could be sold on the world market. During

1995, the government withdrew its price control of domestic crude allowing the price to increase. The price of domestic crude has increased through 1995 to date, however, the price remains below the price received for crude that is exported. As of December 31, 1997, the domestic crude price was approximately 75% percent of the world market price for equivalent crude. In addition, the amount of oil that Noyabrsk is allowed to export is also limited by government restrictions.

2. Summary of Significant Accounting Policies

Form and Content of the Consolidated Financial Statements

The Company and its subsidiaries maintain their books and records in accordance with accounting principles and practices mandated by Russian Accounting Regulations (RAR). These regulations are principally structured for the preparation of information for taxation reporting. Accordingly, tax considerations embodied within the regulations result in significant departures from generally accepted accounting principles in the United States (US GAAP).

The financial statements presented herein have been reformatted for international presentation from the Russian statutory financial statements of the Company and its subsidiaries for the years ended December 31, 1997 and 1996 and adjusted to comply with US GAAP.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiary companies, Noyabrsk, OR, Geofizika, and Nefteprodukt (together referred to as “the Group”), in which the Company owns more than 50 percent of the voting common stock. All significant intercompany balances and transactions have been eliminated. Acquisitions of additional shares in subsidiaries are accounted for by the purchase method for business combinations. As a result of this accounting treatment, the Company’s consolidated value in net oil and gas properties has been reduced in 1997, as discussed in Note 9.

On June 10, 1997, the Company purchased 100% of OOO Kapital and 89% of OOO Vklad for an amount of $53.7 million and $24.6 million, respectively. The activity of these companies is to invest in various investment funds. Subsequent to year-end, management has entered into discussions to sell these companies at a value at least equivalent to the amount paid on purchase. These companies are disclosed as long-term investments and are not consolidated due to the immaterial impact on the classification of assets and liabilities.

As further discussed in Note 8, the Company has interests in various Russian legal entities ranging from less than 5% to 24%. The Company accounts for these investments using the cost method due to their insignificance to the Company’s operations.

Common Stock

The Presidential Decree establishing Sibneft stated that the charter capital of the Company would be equal to 38 percent of the aggregate of the charter capitals of its four subsidiaries. The 38 percent of the aggregate of the Charter capitals of the four subsidiaries also gave Sibneft 51 percent of the voting common stock in each of the subsidiaries and represented the Government’s ownership in these companies. This consolidation of the Government’s ownership into one company established the share capital of Sibneft at 4,516,396,250 shares of 1.6 Russian Rubles (“rubles”) each. For the purposes of these financial statements, the ruble value of the shares has been translated into US Dollars (“US$”) at the exchange rate prevailing at that date.

Reserves and Retained Earnings (Accumulated Deficit)

The audited financial statements for the year ended December 31, 1996 contained, for comparison purposes, an unaudited consolidated statement of operations for the year ended December 31, 1995 based on the assumption that Sibneft came into being with effect from January 1, 1995. Subsequent to the date of issuance of the audited financial statements for the year ended December 31, 1996 the financial statements of the Company for the period from inception (September 30, 1995) to December 31, 1995 have been audited by Arthur Andersen and Unicon M/S Consulting Group. In order to present the Company's reserves and retained earnings (accumulated deficit) from the date of inception, the statement of shareholders equity has been adjusted to incorporate the results of the audit for the period September 30, 1995 to December 31, 1995.

Management Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities in the balance sheet as well as the revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Foreign Currency Translation

Translation (remeasurement) of the Company's ruble denominated financial statements into US$ has been performed in accordance with the provisions of Statement of Financial Accounting Standards ("SFAS") No. 52, "Foreign Currency Translation", as they relate to hyperinflationary economies. The objective of this remeasurement process is to produce the same results that would have been reported if the accounting records had been kept in US$. In 1997, 1996 and 1995, Russia experienced cumulative inflation in excess of 100 percent over a three-year period, as determined by government statistics.

Monetary assets and liabilities have been translated at the rate prevailing at each balance sheet date. Non-monetary assets (other than oil and gas properties and property, plant and equipment - See "Property, Plant and Equipment" below) and liabilities have been translated at historical rates. Revenues, expenses and cash flows have been translated at quarterly average rates. Translation differences resulting from the use of these rates have been accounted for in currency translation gains and losses in the accompanying consolidated statements of operations.

The Group's principal future operating cash flows (revenues, production costs and general and administrative expenses) will be generated in rubles. As a result, future movements in the exchange rate between the ruble and the US$ will affect the carrying value of the Company's monetary assets and liabilities. Such changes may also affect the Company's ability to realize non-monetary assets as represented in terms of US$ in the accompanying financial statements.

The exchange rate for 1 US$ ranged from 4,640 to 5,560 rubles during 1996 and from 5,560 to 5,960 rubles during 1997. The year-end exchange rates equaled 5,960 rubles as of December 31, 1997 and 5,560 rubles as of December 31, 1996. Effective January 1, 1998, the Russian government redenominated the ruble by dividing by 1,000 and issued new currency. As an example, the December 31, 1997 exchange rate of 5,960 rubles to 1 US$ became 5.96 rubles to 1 US$ on January 1, 1998. The exchange rate as of April 1, 1998 (in redenominated rubles) was 6.108 rubles to 1 US$.

Cash and Cash Equivalents

Cash represents cash on hand and in the Group's bank accounts and cash equivalents represent deposits with original maturity dates of three months or less. Foreign currency deposits are translated at year-end exchange rates.

Inventories

Inventories, consisting primarily of crude oil, petroleum products and materials and supplies, are stated at the lower of average cost or market. A general reserve is established against slow moving and obsolete material and supplies.

Oil and Gas Properties

Oil and gas properties are accounted for under the full cost method of accounting. Accordingly, all costs associated with acquisition, exploration, and development of oil and gas reserves, including directly related overhead costs, are capitalized.

Investments in unproved properties and major development projects are not amortized until proved reserves associated with the projects can be determined or until impairment occurs. If the results of an assessment indicate that the properties are impaired, the amount of the impairment is added to the capitalized costs to be amortized.

Russian financial information is maintained in historic ruble terms. However, the US$ carrying value of oil and gas properties in the accompanying balance sheet was obtained using the same methodology applied to property, plant and equipment, as discussed below in "Property, Plant and Equipment". In addition, the net capitalized oil and gas costs are subject to a "ceiling test", which basically limits such costs to the aggregate of the "estimated present value" (future net revenues from proved reserves, discounted at a 10 percent interest rate based on current economic and operating conditions) plus the lower of cost or fair market value of unproved properties. For the year ended December 31, 1996, the independent reserve engineering firm, Miller and Lents, Ltd., prepared a report on the evaluation of the Company's oil and gas reserves (reserve report). As a result of this evaluation, no writedown was required for the year ended December 31, 1996. As at the date of issuance of these financial statements, the independent reserve engineering firm had not completed their evaluation of the Company's oil and gas reserves as at December 31, 1997. Accordingly, the Company has used the reserve report for the year ended December 31, 1996 (adjusted for 1997 activity) to calculate the depreciation, depletion and amortization, relating to oil and gas properties, for the year ended December 31, 1997.

Sales and abandonments of proved and unproved properties are accounted for as adjustments of capitalized costs with no gain or loss recognized, unless such adjustments would significantly alter the relationship between capitalized costs and proved reserves of oil and gas, in which case the gain or loss is recognized in income.

Property, Plant and Equipment

As discussed above, Russian financial information is maintained in historic ruble terms. In years prior to 1992, exchange rates were fixed by the government and did not necessarily correspond to the real market value of the ruble. In addition, certain purchases were made through central purchasing authorities and values transferred to receiving organizations were determined by the government. During 1992, fixed assets were revalued in accordance with Government Decree Number 595 dated August 14, 1992. Similar revaluations took place as of January 1, 1994, January 1, 1996 and January 1, 1998. Indexes used for these revaluations did not necessarily reflect the changes in the ruble's value, nor did they result in the value of the underlying fixed assets to which they were applied being revalued to a current market value.

As a result, it was not possible to determine from the statutory accounting records an appropriate carrying value of property, plant and equipment for US GAAP reporting purposes. Accordingly, an independent appraisal company, American Appraisal (AAR) Inc., was engaged to perform an historic cost valuation of property, plant and equipment, together with related accumulated depreciation as of

December 31, 1996. Disposals of property, plant and equipment have been accounted for at their historic cost while additions to property, plant and equipment have been recorded at cost using exchange rates as of the transaction dates.

In performing a valuation of property, plant and equipment, the independent appraisal company employed appraisal techniques to determine both the historic cost and fair market value (in-use) for the appraised property in US$ terms. The first step in estimating the historic cost and fair market value of the fixed assets entailed estimating the cost new, which is either cost of reproduction new (CRN) or, where CRN data was not available due to technical and/or design changes, the cost of replacement (COR). The CRN reflects the cost to reproduce the existing property in like kind while the COR reflects the cost to replace the existing property using current technology and materials. Cost data from both Russian and foreign producers of equipment was taken into account.

To arrive at an appropriate estimate of original historic cost, the CRN/COR was back-trended according to the actual age of the asset using historic western inflation adjustments. The historic cost of the assets was then depreciated using estimates of economic useful lives as outlined in "Depreciation, Depletion and Amortization" below.

The results of this work have been used to determine the carrying values of property, plant and equipment for US GAAP purposes in the accompanying balance sheets as of December 31, 1996.

The cost of maintenance, repairs, and replacement of minor items of property is charged to maintenance expense. Renewals and betterments of assets are capitalized. Upon sale or retirement of property, plant and equipment, the cost and related accumulated depreciation are eliminated from the accounts. Any resulting gains or losses are included in the determination of net income.

Depreciation, Depletion and Amortization

Depreciation, depletion and amortization of oil and gas properties, including the estimated future costs to develop proved reserves, is provided on the unit-of-production method based on the ratio of current year production to total estimated future production from proved reserves.

The provision for depreciation and amortization with respect to operations other than oil and gas producing activities is computed using the straight-line method based on estimated economic lives. Composite depreciation rates are applied to similar types of buildings and equipment having similar economic characteristics, as shown below:

Asset Group	Average Life
Buildings and land improvements	15-45 years
Machinery and Equipment (including refinery assets)	20-30 years
Vehicles and other	3-10 years

Capitalized Interest

Interest is capitalized on expenditures made in connection with capital projects (exclusive of oil and gas properties) that, theoretically, could have been avoided if expenditures for the assets had not been made. Interest is only capitalized for the period that activities are in progress to bring these projects to their intended use. During 1997, US$ 14.6 million in interest costs were capitalized (no material interest costs were capitalized during 1996).

Minority Interest in Subsidiary Companies

Minority interest in the consolidated balance sheets reflects minority owners' percent share of shareholders' capital in subsidiaries. The minority interest is calculated based on the shareholders' equity of each subsidiary as determine under US GAAP. The actual ruble denominated balance attributable to minority interests may differ from this amount. Minority owners' interest in the Company's subsidiaries, is as follows:

	December 31, 1997		December 31, 1996	
	Voting	Total	Voting	Total
Noyabrsk	21.5%	34.5%	49.0%	62.0%
OR	49.0%	62.0%	49.0%	62.0%
Geofizika	32.0%	49.0%	49.0%	62.0%
Nefteprodukt	49.0%	62.0%	49.0%	62.0%

Income Taxes

The Company is not subject to taxation on a consolidated basis. Current income taxes are provided on the accounting profit as determined under RAR at a rate of 35 percent, for the periods ended December 31, 1997 and 1996, after adjustments for certain items which are not deductible for taxation purposes, and after consideration of capital investment tax credits.

The accompanying consolidated financial statements reflect deferred income taxes of the Company and its subsidiaries using the liability method, which requires that deferred tax assets and liabilities be recorded for the expected future tax consequences of existing differences between financial reporting and tax reporting bases of assets and liabilities, and loss or tax credit carryforwards (see Note 19).

Accounting for Contingencies

Certain conditions may exist as of the date these financial statements are issued, which may result in a loss to the Company, but which will only be resolved when one or more future events occur or fail to occur. The Company's management and legal counsel assess such contingent liabilities. The assessment of loss contingencies necessarily involves an exercise of judgment and is a matter of opinion. In assessing loss contingencies related to legal proceedings that are pending against the Company or unasserted claims that may result in such proceedings, the Company's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

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

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

Revenue

Noyabrsk follows the policy of recognizing sales at the point its produced oil enters the transportation network.

Petroleum product sales are recognized when finished products are shipped to customers.

Retirement and Other Benefit Obligations

The Company and its subsidiaries do not have any substantial pension arrangements separate from the State pension scheme of the Russian Federation, which requires current contributions by the employer calculated as a percentage of current gross salary payments; such contributions are charged to expense as incurred. In addition, the Company has no post-retirement benefits or significant other compensated benefits requiring accrual.

Cash Flow Statement

A significant portion of the Company's accounts are settled by non-cash transactions and are included in the accompanying consolidated financial statements on the same basis as cash transactions. These transactions are generally either in the form of direct settlement by goods or services to the final customer or through a chain of non-cash transactions involving several companies. In such cases, both sales and purchases are recorded as a result of the non-cash transaction. Non-cash transactions have been recorded in the financial statements at the market value of the goods or services provided.

During 1997, a significant proportion, approximately US$ 1.5 billion (US$ 1.4 billion during 1996), of the Company's operations were settled through non-cash transactions.

3. Change in Accounting Policy

During in 1997, the Company adopted the policy of providing for future site restoration costs. Such policy has been applied retroactively in the accompanying financial statements. These costs represent the estimated future cost to abandon wells and production facilities. Total site restoration costs are accrued on a unit-of-production basis.

As of December 31, 1997, estimated total future site restoration costs related to existing oil and gas properties are estimated to be approximately US$ 343 million. During 1997 and 1996, the Company has included US$ 11.5 million and US$ 10 million (US$ 3.8 million net of minority interest effects), respectively, of such costs as a component of the depreciation, depletion and amortization expense. The cumulative effect of the accounting change resulted in a charge to opening reserves of US $122.5 million (US$ 46.6 million net of minority interest effects) and to opening retained earnings of US$ 2.5 million (US$ 950 thousand net of minority interest effects), as of December 31, 1995.

The Company has estimated its liability based on current site restoration costs incurred during 1997 and will continue to update its estimates in the future. However, Russian environmental regulations and their enforcement can have a significant impact on these costs and, as governmental authorities are continually considering such regulations, the future costs associated with these liabilities may differ from the recorded amounts.

4. Cash and Cash Equivalents

Cash and cash equivalents as of December 31, comprise the following (in US$ thousands):

	1997	1996
Cash in bank – rubles	69,847	2,920

Cash in bank – hard currency	32,725	2,053
Cash equivalents – deposits of less than 3 months	3,569	9,947
Cash on hand	2,553	3,876
Total cash and cash equivalents	108,694	18,796

The Company has ruble and hard currency accounts in related banks, Obedineny Bank, Neftechimbank and Noyabrskneftecombank. As of December 31, 1997, the Company's share in the capital of Obedineny Bank, Neftechimbank and Noyabrskneftecombank were 19%, 10% and 12%, respectively. The balances in these accounts, as of December 31, 1997, amounted to US$ 68.6 million, US$ 128 thousand and US$ 14 thousand, respectively.

5. Short-Term Investments

Short-term investments include promissory notes, received in settlement of trade accounts receivable, and time deposits. As of December 31, 1997 and 1996, the most significant investments were time deposits of US$ 1.4 million and US$ 82 million, respectively, with major Russian banks.

6. Accounts Receivable

The composition of accounts receivable is as follows as of December 31, (in US$ thousands):

	1997	1996
Trade receivables	266,244	410,411
Advances paid to suppliers	86,226	33,996
Value Added Tax receivable	85,362	66,447
Other	50,567	64,817
Less allowance for doubtful accounts	(65,611)	(72,268)
Total	422,788	503,403

In prior years, and due to government involvement in the subsidiaries, organizations in certain sectors of the economy were supplied with product irrespective of their ability to make repayments. Significant market reforms within Russia have reduced the availability of budgetary funds to many governmental and recently privatized enterprises. These budget deficits have further hindered the ability of large industrial and governmental organizations to make payment to suppliers on a timely basis.

For many industrial customers, amounts due can be offset against payables for services received. In order to further reduce a portion of the risk associated with customer non-payments, in certain circumstances, arrangements have been negotiated whereby payment is made in goods and services which are utilized in core business activities, promissory notes and government securities.

Management has provided a general allowance on amounts due from commercial and industrial customers principally based on the overall delinquency in customer payments.

The Group's trade receivables are denominated primarily in rubles and are short-term in nature. However, in US$ terms, due to significant delays in collection, the Company is subject to the economic risk of currency movements between the time of billing and the receipt of payment. Since July 1996, the value of the ruble against the US$ has been maintained within a pre-set range (the "Ruble Corridor") by the Central Bank of the Russian Federation. The Central Bank set the Ruble Corridor from 5,500 to 6,100 rubles to the US$, at January 1, 1997. In December 1997, the Central Bank announced that the Ruble Corridor was to be from 5,750 to 6,350 rubles to the 1 US$, effective December 31, 1997.

7. Inventories

The following are the major components of inventory as of December 31, (in US$ thousands):

	1997	1996
Crude oil	12,206	21,304
Petroleum products	108,511	107,444
Materials and supplies	215,835	239,562
Other	81,394	28,644
Less reserve for materials and supplies	(19,370)	(54,519)
Total	398,576	342,435

8. Long-Term Investments

The Group owns equity interests in various Russian entities. These investments have been accounted for at cost, less any provisions for permanent diminution in value, regardless of ownership interest. US GAAP requires that investments in entities not controlled by the holding company, but in which the holding company's ownership percentage is greater than 20 percent, be accounted for using the equity method and that investments in entities controlled by the holding company be consolidated. The impact of this departure from US GAAP is not significant to the overall financial presentation.

None of the companies listed below are traded on the Russian Stock Exchange and due to the nature of the financial markets it is not possible to obtain a current market price for these investments, however, management believes that the costs of these investments approximate their fair value. The significant equity and other long-term investments in Russian companies are summarized below as of December 31, 1997 and 1996 (in US$ thousands):

Name	Nature of Business	Ownership Percentage at December 31, 1997	1997	Ownership Percentage at December 31, 1996	1996
OOO Kapital	Investment	100%	53,727	-	-
OOO Vklad	Investment	89%	24,563	-	-
Neftechimbank	Bank	10%	10,000	10%	10,000
Mosnefteproduct	Marketing	15%	9,223	15%	9,718
KOPF Bank	Bank	-	2,100	-	-
OOO Stolichnye Ivestitsii	Investment	24%	5,192	-	-
Vnesheconombank (bonds)	Bank	-	4,974	-	4,974
Eastern Siberian Oil Co.	Oil & Gas	15%	2,915	-	-
Noyabrskneftecombank	Bank	12%	1,580	97%	2,261
Tokobank	Bank	-	-	2%	5,004
Other			3,745		1,677
Total			118,019		33,634

Investments purchased in 1997 included, OOO Kapital, OOO Vklad, OOO Stolichnye Ivestitsii on June 10, KOPF Bank on June 4 and Eastern Siberian Oil Co. on June 26.

9. Oil and Gas Properties

Oil and gas properties as of December 31, are as follows (in US$ thousands):

	1997	1996
Oil and gas properties	7,454,315	8,156,481
Depreciation, depletion and amortization	(3,437,814)	(3,141,438)
Net oil and gas properties	4,016,501	5,015,043

In connection with the increase in the Company's ownership percentage in Noyabrsk's charter capital, a reduction in net oil and gas properties of US$ 1,277 million has been made during 1997 for consolidation purposes (see Note 1).

10. Property, Plant and Equipment

Property, plant and equipment as of December 31, is as follows (in US$ thousands):

	1997	1996
Buildings	1,182,616	1,324,702
Machinery and Equipment	1,544,162	1,509,488
Vehicles and other Equipment	140,843	84,416
	2,867,621	2,918,606
Less: Accumulated Depreciation	(1,561,014)	(1,584,867)
Property, Plant and Equipment, net	1,306,607	1,333,739

11. Construction in Progress

Construction in progress includes various construction projects and machinery and equipment delivered but not yet installed. As of December 31, 1997, detail of construction in progress is as follows (in US$ thousands):

	Construction Work in Progress	Machinery/ Equipment to be Installed	Total
Buildings	80,983	-	80,983
Plant and machinery	46,482	57,935	104,417
Vehicles and other equipment	18,862	3,081	21,943
Total	146,327	61,016	207,343
Comparative balance at December 31, 1996	176,256	88,223	264,479

12. Short-term Loans

Short-term loans are comprised of (1) export financing loan facilities in US$ from major Western banks and their affiliates, secured by Noyabrsk crude production and (2) unsecured loans from Russian banks, denominated in rubles with fixed terms of repayment. As of December 31, the Group had outstanding loans as follows (in US$ thousands):

	1997	1996
Banks	296,503	93,810
Banks – related party	27,674	25,906
Other	-	270
Total	324,177	119,986

Related party loans consist of various loan amounts received from Noyabrskneftcombank and Neftechembank in the amounts of US$ 14,492 and US$ 13,182, respectively, for 1997 and US$ 18,150 and US$ 7,756, respectively, for 1996. The interest rates on these loans ranged from 24% to 31% for 1997 and 20% to 160% for 1996.

In general, short-term loans are used for the provision of working capital needs. As of December 31, 1997 approximately 80 percent of loans were provided in hard currency. The largest bank loans outstanding as of December 31, 1997 are loans from "Credit Lyonnais Russie" and "Raiffeisen Zentralbank". Sibneft has a short-term syndicated loan from "Credit Lyonnais Russie" with US$ 16 million outstanding at December 31, 1997. This loan is secured by crude oil production of Noyabrsk, bears interest at an annual rate of US LIBOR plus 3% and is repayable from export proceeds on a month-to-month basis. Sibneft also has a line of credit of US$ 114 million and other loans of US$ 66 million outstanding from "Credit Lyonnais Russie" under the same terms. In addition, the Company has unsecured loans of US$ 20 million from "Raiffeisen Zentralbank." These loans bear floating interest at rates from London Interbank rate plus 4-5%. The remaining balances of loans outstanding, at December 31, 1997, are denominated in rubles.

Whereas the loans, at December 31, 1996, incurred relatively high interest rates, during 1997 these ruble debts have been renegotiated, with reduced interest rates. Weighted average interest rates related to the short-term loans outstanding as of December 31, 1997 for hard currency and ruble denominated loans equal 10 percent and 25 percent, respectively (57 percent weighted average for all loans outstanding at December 31, 1996). During the year ended December 31, 1997, the weighted average hard currency and ruble denominated short-term debt balances outstanding were US$ 122 million and US$ 108 million, respectively, with weighted average interest rates of 10 and 30 percent, respectively. During 1996, the weighted average of all short-term debt balances outstanding was US$ 82 million, with a weighted average period interest rate of 88 percent. As of December 31, 1997 and 1996, approximately US$ 22 million and US$ 33 million, respectively, of Noyabrsk's short-term loans are secured by proceeds from domestic crude sales.

13. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities as of December 31, comprise the following (in US$ thousands):

	1997	1996
Trade accounts payable	228,707	251,443
Other accounts payable	160,114	111,818

Accrued liabilities	18,788	99,443
Total	407,609	462,704

Included in trade accounts payable, as of December 31, 1997, is US$ 4,868 (US$ 57,152 for 1996) relating to taxes payable that the tax authorities have requested the Company to pay, in refined product, to a third party.

14. Income and Other Taxes

Income and other taxes payable comprise the following as of December 31, (in US$ thousands):

	1997	1996
Amounts falling due within one year		
Lubricant tax	159,433	33,096
VAT	84,596	180,236
Excise tax	84,461	117,046
Royalties	66,914	92,752
Road Users tax	63,818	32,633
Mineral Replenishment tax	18,079	43,681
Profits tax	17,003	38,802
Property tax	15,281	24,568
Other taxes payable	95,040	75,880
Fines, penalties and interest (see below)	136,000	87,000
Estimated income and other taxes payable	740,625	725,694
Amounts falling due after one year		
Long-term taxes payable (see below)	14,555	14,000

In 1996, Noyabrsk received a formal tax deferral approval under the terms of Presidential Decree 65 of January 19,1996. Under the terms of this deferral, accumulated tax arrears, fines and penalties owed to the federal budget from 1993 to 1996 were to be repaid over a number of years.

During 1997, Noyabrsk has not met several of the required conditions of this scheme. Ordinarily this would have lead to the entire amount subject to deferral being immediately payable. However, notwithstanding this failure, Noyabrsk has secured a further deferral scheme in the current year. Firstly, in a letter issued on December 31, 1997, the Prime Minister, in accordance with Decision No. 254 of March 5, 1997, granted Noyabrsk an approval for the deferral of the principal tax debt amounts owing to the federal budget. The total amount subject to the deferral is approximately US$ 152 million and it will become effective on registration of the arrangement. The deferral is made up of four separate decisions each relating to a quarter of the above sum. The decisions provide that deferral will be available for periods of six, twelve, eighteen and twenty four months. The basis for this deferral includes the issue of bonds by Noyabrsk to the Government of the Russian Federation for the total of the deferred amount. The terms of the bonds match the period of the deferrals. Interest is payable at one quarter of the prevailing Central Bank rate at the time of bond repayment. The deferral arrangements are supported by a guarantee from Sibneft.

Noyabrsk has also successfully negotiated an agreement with the local tax inspectorate. This agreement has two elements. Noyabrsk's total fines, penalties and interest outstanding to the federal budget as at January 1, 1997 continue to be subject to deferral over 10 years. Fines, penalties and interest accruing on this amount during 1997 have been waived. The total fines, penalties and interest amount subject to a 10 year deferral is approximately US$ 100 million.

Accordingly, an accrual of US$ 14.6 million, being the present value of the fines, penalties and interest subject to the above deferral, discounted at the Company's current effective borrowing rate, has been made in the financial statements. This accrual is represented within long-term taxes payable.

This agreement is subject to the continuing fulfillment of current tax obligations, and certain other obligations including the requirements of the deferral issued under Decision 254.

If any of the deferral schemes described above were withdrawn, the relevant sums together with a charge for penalties and interest arising as a result of the default would become payable immediately. There is also a mechanism in Decision 254 for taking recovery action through Proceedings on Insolvency against default in the terms of the bond issue.

Despite the conclusion of the agreements described above, the group companies continue in ongoing discussions with both Federal and local tax authorities on a range of issues arising from the continuing audit of the Group's records by the various tax inspectorates.

Consequently, the group maintains a number of provisions that are included within long-term taxes payable. These provisions represent management's best estimate of the outcome of their discussions with the tax authorities. If the tax authorities do not accept the group's representations in these discussions, a significantly higher liability may be imposed.

Although legal authority exists for the imposition of severe penalties for unpaid or delayed taxes, it should be noted that in the current Russian taxation environment, several Russian companies in similar circumstances have successfully negotiated reductions, deferrals or waivers in respect of fines and penalties with local and federal tax authorities.

Noyabrsk also has an agreement with the local and district tax authorities to make the payment of certain taxes through the delivery of refined product. Sibneft delivers the refined product and the value is agreed each quarter with the tax authorities and charged to Noyabrsk.

The information provided above should be read in conjunction with the following comments in relation to the general Russian taxation environment. Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include value added tax, corporate income tax (profits tax), a number of turnover based taxes, and payroll (social) taxes, together with others. In addition, the subsidiaries of the group are also subject to various industry taxes including excise and mineral replenishment taxes. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies; therefore, implementing regulations are often unclear or nonexistent. Accordingly, few precedents with regard to issues have been established. Often, differing opinions regarding legal interpretation exist both among and within government ministries and organizations (like the State Tax Service and its various inspectorates); thus creating uncertainties and areas of conflict. Tax declarations, together with other legal compliance areas (as examples, customs and currency control matters) are subject to review and investigation by a number of authorities, who are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia substantially more significant than typically found in countries with more developed tax systems.

Generally, tax declarations remain open and subject to inspection for a period of six years. As of December 31, 1997, a substantial proportion of the tax declarations of the Company have been reviewed through to 1996. Management believes that the Company is in substantial compliance with the tax laws affecting its operations; however, the risk remains that the relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant. The fact that a year has been reviewed does not close that year, or any tax declaration applicable to that year, from further review during the six-year period.

15. Long-Term Debt

In August 1997, Sibneft issued US$ 150 million of Eurobonds, unconditionally guaranteed by the Company, Noyabrsk, OR, Geofizika, and Nefteprodukt. The Eurobonds bear interest from the date of issue (August 14, 1997) at a rate of 4% above the London Interbank Market rate for US$ deposits, payable quarterly, commencing on November 14, 1997. Interest is payable in US$. The maturity date of the notes is August 14, 2000.

Proceeds received by the Company totaled approximately US$ 147.8 million, which is net of original issue discount and fees and commissions associated with the placement of the notes.

16. Capitalization

The shareholders' capital account represents the authorized capital of the Company, as stated in its charter document. The common shareholders are allowed one vote per share. Dividends paid to shareholders are determined by the directors and approved at the annual shareholders' meeting.

The following comprises the share structure of the Company, as of December 31, 1997:

	Number of Shares (millions)	Ownership Percentage
Finansovaya Neftyanaya Korporatsiya	2,303	51.0%
SINS (Siberian Investors)	858	19.0%
Refine Oil	677	15.0%
Runicom S.A. (as nominee)	552	12.2%
Other Investors	126	2.8%
Total	4,516	100.0%

No companies or individuals, other than those listed above, hold more than five percent of the Company's shares as of December 31, 1997.

The following represents a reconciliation between total capitalization determined under RAR and US GAAP. For reconciliation purposes, the total capitalization in accordance with RAR, approximating 27,651 million rubles and 27,248 million rubles as of December 31, 1997 and 1996, respectively, were converted into US$ at the year end exchange rates (in US$ thousands).

	1997	1996
Russian Accounting Regulations	4,341,733	4,612,180
Increase/(decrease) due to effect of:		
Minority interest effects	(2,399,083)	(3,752,650)
Fixed assets valuation	866,675	1,829,443
Tax contingencies and other tax	(158,051)	(101,000)
Accrued site restoration	(146,500)	(135,000)
Allowance for bad debts	(65,611)	(72,268)
Inventory valuation	(19,370)	(54,519)
Investments valuation	(715)	(25,261)
Capitalized interest	14,571	-
Capitalized repair costs	4,087	-
Net other income and expense adjustments	(41,882)	(25,275)
Other	13,313	65,307
US GAAP	2,409,167	2,340,947

The significant difference between the years regarding fixed asset valuation is principally attributable to the use of year-end exchange rates to translate RAR equity and the use of historical rates in the financial statements.

The following represents a reconciliation between earnings determined under RAR and US GAAP. For reconciliation purpose, net statutory income for years 1997 and 1996 in accordance with RAR, approximating 1,121 million rubles and 1,108 million rubles, respectively, were converted into US$ at the year average exchange rates (in US$ thousands).

	1997	1996
Pre-tax income per the statutory financial Statements	191,383	216,529
Reconciling items:		
Revenue and operating expense accruals, net	(62,773)	(95,919)
Other income and expense adjustments, net	11,344	83,414
Statutory expenses recorded to equity	(41,995)	(55,031)
Differences in depreciation	(34,791)	(66,903)
Bad debt provision, net impact	6,657	(33,514)
Tax contingencies reserve, net impact	(71,050)	(93,000)
Capitalized interest	14,571	-
Capitalized repair expenditures	4,087	-
Equity investments written off	(28,037)	(32,597)
Inventory obsolescence reserve, net impact	35,169	(12,632)
Site restoration provision	(11,500)	(10,000)
Foreign currency gain	31,650	162,324
Effect of Minority Interest	72,571	41,316
Other differences	32,577	(38,234)
US GAAP pre-tax income	149,863	65,753

15. Dividends

In accordance with RAR, earnings available for dividends are limited to profits, retained earnings and other income, denominated in rubles, after certain deductions.

The Company to date has not declared any common stock dividends. Dividends declared by the subsidiaries in 1997, relating to 1996, on preferred shares included 10.6 billion rubles at Noyabrsk, 7.1 billion rubles at OR and 3.4 billion rubles at Nefteprodukt. Dividends declared in 1998, relating to 1997, included 6.0 million rubles at Noyabrsk and 3.0 billion rubles at OR. As of December 31, 1997, Noyabrsk had accumulated 700 billion rubles in earnings available for distribution.

16. Income Taxes

The Group's provision for income taxes as reported in the accompanying consolidated statements of operations is as follows (in US$ thousands):

	1997	1996
Current income taxes	81,643	71,899
Deferred income taxes	-	-
Total provision for income taxes	81,643	71,899

The provision for income taxes represents the total income tax expense for the Company and each of its subsidiaries. In all cases deferred income taxes were calculated for each as an asset. Due to the Russian environment described in Note 1 and the corresponding uncertainty of realization, all of these assets have been fully reserved.

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

	1997	1996
Income before income taxes	149,863	65,753
Statutory income tax rate	35%	35%
"Expected" income tax expense	52,452	23,014
Add (deduct) tax effect of:		
Minority interest effect on income	(25,400)	(14,461)
Dividends on preferred stock of subsidiaries	178	1,324
Temporary accounting differences, resulting in a net deferred tax asset which has been reserved	12,558	14,283
Permanent accounting differences	41,855	47,739
Income taxes	81,643	71,899
Effective tax rate	54%	109%

15. Commitments and Contingencies

Litigation

In connection with the increase in the Company's ownership percentage of Noyabrsk's charter capital during 1997 (Note 1), one of Noyabrsk's minority shareholders, Navaromco Limited ("the plaintiff") has filed a legal action against Noyabrsk in the Arbitration Court of the Yamalo-Nentsk autonomous region. The plaintiff has claimed that the issuance of shares made by Noyabrsk during 1997 was not performed in accordance with the charter requirements and Russian legislation. The plaintiff further contends that the offer price was significantly below the market price at the time of the offering. Company management is of the opinion that the Noyabrsk board of directors complied with all applicable procedural requirements as defined by both the Noyabrsk charter and Russian legislation.

Construction and Exploration Programs

The Group is engaged in continuous construction and exploration programs, currently estimated to total US$ 960 million over the next five years at Noyabrsk and US$ 48 million over the next two years for Omsk. The construction and exploration programs are subject to periodic reviews and actual expenditures may vary from the above estimates. At December 31, 1997, no significant purchase commitments were outstanding in connection with the construction programs.

Financing for all of the future costs has not yet been secured, and Sibneft is actively pursuing various financing opportunities. It is the opinion of management that the Company will be able to obtain all necessary financing to complete the construction programs.

Environmental Matters

Management is of the opinion that the Group has met the government's requirements concerning environmental matters, and therefore believes that the Group does not have any material current environmental liabilities.

Insurance Matters

The Group maintains only minimal levels of insurance on its existing asset base, or in certain cases self-insures, and as a result is subject to significant uninsured exposures in the event of loss or destruction of principal operating assets. In addition, Russian insurance providers do not offer business interruption insurance.

Social Assets

The Group possesses significant social assets for the use of employees. These assets were contributed by the State in years prior to the inception of the Company. In accordance with the Presidential Decree on privatization in Russia, the Group is required to transfer the social assets to the relevant local city administrations. Accordingly, as the Group does not have ownership of these assets, they are not recorded in these financial statements.

With respect to these social assets, the Group has incurred US$ 138 million and US$ 120 million in expenses for the years ended December 31, 1997 and 1996, respectively.

16. Related Party Transactions

During 1997, approximately 12% of sales (15% during 1996) were made to a shareholder, Runicom S.A. who principally exports refined product. These transactions were conducted at market prices. As of December 31, 1997, the Group had outstanding receivables from the shareholder totaling US$ 68 million (US$ 45 million as at December 31, 1996), representing amounts outstanding in connection with these export sales.

17. Subsequent Events

Potential merger with Yukos

In January 1998, the Company's controlling shareholders and AO Yukos' controlling shareholders signed a Memorandum of Understanding whereby they agreed to negotiate in good faith with the objective of proceeding towards concluding a transaction, whereby the controlling shareholders of AO Sibneft and controlling shareholders of AO Yukos exchange their shares for the shares of a new company AO Yuksi. This transaction has now been called off with both companies confirming they will continue to co-operate on certain operations and projects.

Receipt of short term loans

In March 1998, the Company issued six month discount Euronotes, unconditionally guaranteed by the Company, Noyabrsk, OR, Geofizika and Nefteprodukt. The Euronotes were issued at a discount with an issue price of 93.292% of the principal amount. The principal amount payable at maturity is US$ 200 million and bears interest at a weighted average rate of 13.3%. The maturity date of the Euronotes is September 18, 1998. Proceeds received by the Company totaled approximately US$ 186.6 million, which is net of original interest discount and fees associated with the placement of the Euronotes.

In April 1998, the Company obtained a Raiffeisen Zentral bank loan of US$ 51.5 million at LIBOR plus 5.5% with maturity in 176 days.

Potential investment from Elf Aquitaine

In April 1998, Elf Aquitaine (Elf), the Company and its controlling shareholders ("Sibneft Group") and AO Yukos and their controlling shareholders ("Yukos Group") signed a Heads of Agreement to enter into a long term strategic alliance on co-operation between the Parties in the Russian Federation relating to oil and gas upstream and downstream activities. Elf agreed to purchase 5% of Yuksi following the business combination of Yukos Group and Sibneft Group for a price of US$ 528 million and the participation on a fifty/fifty basis in the development of the Sugmut field located in Western Siberia (whose license is held by Noyabrsk) for US$ 57 million. However, due to the discontinuance of merger plans between Yukos Group and Sibneft Group, Elf will consider purchasing, for US$ 528 million, a yet to be agreed share in the Company and participating in the development of the Sugmut field for US$ 57 million.