OAO NOVATEK

IFRS CONSOLIDATED FINANCIAL STATEMENTS

AND INDEPENDENT AUDITOR’S REPORT

FOR THE YEARS ENDED 31 DECEMBER 2008 AND 2007

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INDEPENDENT AUDITOR'S REPORT

To the shareholders and directors of OAO NOVATEK

1 We have audited the accompanying consolidated financial statements of OAO NOVATEK and its subsidiaries (the "Group") set out on pages 4 to 53 which comprise the consolidated balance sheet as at 31 December 2008 and the consolidated statement of income, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

2 Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Opinion

6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2008, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation
17 March 2009

Consolidated Balance Sheet

(in millions of Russian roubles)

	Notes	At 31 December: 2008	2007
ASSETS			
Non-current assets			
Property, plant and equipment	6	108,714	82,669
Investments in associates		1,416	1,125
Long-term loans and receivables		736	681
Other non-current assets		2,712	2,462
Total non-current assets		**113,578**	**86,937**
Current assets			
Inventories	7	2,156	1,794
Current income tax prepayments		1,765	335
Trade and other receivables	8	2,485	3,267
Prepayments and other current assets	9	8,030	7,660
Cash and cash equivalents	10	10,992	3,982
Total current assets		**25,428**	**17,038**
Assets classified as held for sale	22	**901**	**-**
Total assets		**139,907**	**103,975**
LIABILITIES AND EQUITY			
Non-current liabilities			
Long-term debt	11	19,935	42
Deferred income tax liabilities	21	6,720	8,083
Other non-current liabilities		593	905
Asset retirement obligations		1,515	1,058
Total non-current liabilities		**28,763**	**10,088**
Current liabilities			
Short-term debt and current portion of long-term debt	13	6,342	6,560
Trade payables and accrued liabilities	14	6,223	3,599
Current income tax payable		231	645
Other taxes payable		1,373	1,271
Total current liabilities		**14,169**	**12,075**
Liabilities associated with assets held for sale	22	**335**	**-**
Total liabilities		**43,267**	**22,163**
Equity attributable to OAO NOVATEK shareholders			
Ordinary share capital		393	393
Treasury shares		(599)	-
Additional paid-in capital		30,433	30,257
Currency translation differences		(91)	-
Asset revaluation surplus on acquisitions		5,617	5,617
Retained earnings		60,316	45,068
Total equity attributable to OAO NOVATEK shareholders	15	**96,069**	**81,335**
Minority interest		**571**	**477**
Total equity		**96,640**	**81,812**
Total liabilities and equity		**139,907**	**103,975**

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

Approved for issue and signed on behalf of the Board of Directors on 17 March 2009:

L. Mikhelson
General Director

M. Gyetvay
Financial Director

OAO NOVATEK
Consolidated Statement of Income
(in millions of Russian roubles, except for share and per share amounts)

	Notes	Year ended 31 December: 2008	2007
Revenues			
Oil and gas sales	16	76,076	60,406
Sales of polymer and insulation tape		2,098	1,602
Other revenues		1,098	362
Total revenues		**79,272**	**62,370**
Net gain (loss) on disposal of interest in subsidiaries		8	95
Other income (loss)		(244)	15
Total revenues and other income		**79,036**	**62,480**
Operating expenses			
Transportation expenses	17	(18,153)	(14,421)
Taxes other than income tax	18	(7,186)	(6,379)
Materials, services and other	19	(6,332)	(4,924)
General and administrative expenses	20	(5,064)	(3,873)
Purchases of oil, gas condensate and natural gas		(4,665)	(3,242)
Depreciation, depletion and amortization	6	(4,478)	(3,668)
Exploration expenses		(1,117)	(486)
Net impairment expense		(105)	(153)
Change in natural gas, liquid hydrocarbons, and polymer products and work-in-progress		184	31
Total operating expenses		**(46,916)**	**(37,115)**
Profit from operations		**32,120**	**25,365**
Finance income (expense)			
Interest expense		(222)	(263)
Interest income		407	376
Foreign exchange gain (loss)		(3,569)	11
Total finance income (expense)		**(3,384)**	**124**
Share of profit (loss) of associates, net of income tax		(147)	-
Profit before income tax		**28,589**	**25,489**
Income tax expense			
Current income tax expense		(6,892)	(7,301)
Net deferred income tax benefit		1,230	540
Total income tax expense	21	**(5,662)**	**(6,761)**
Profit for the year		**22,927**	**18,728**
Profit (loss) attributable to:			
Minority interest		28	(8)
Shareholders of OAO NOVATEK		**22,899**	**18,736**
Basic and diluted earnings per share (in Russian roubles)		7.54	6.17
Weighted average number of shares outstanding (in thousands)		*3,035,279*	*3,036,306*

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

(in millions of Russian roubles)

	Notes	Year ended 31 December: 2008	2007
Profit before income tax		**28,589**	**25,489**
Adjustments to profit before income tax:			
Depreciation, depletion and amortization		4,581	3,734
Net impairment expense		105	153
Net foreign exchange loss (gain)		3,569	(11)
Net loss (gain) on disposal of assets		315	(93)
Share-based compensation	26	176	176
Interest expense		222	263
Interest income		(407)	(376)
Share of loss (profit) in associates, net of income tax		147	-
Net change in other non-current assets		467	(178)
Other adjustments		26	24
Working capital changes			
Decrease (increase) in trade and other receivables, prepayments and other current assets		430	(4,048)
Decrease (increase) in inventories		(421)	(94)
Increase (decrease) in trade payables and accrued liabilities, excluding interest and dividends		2,406	1,856
Increase (decrease) in other taxes payable		100	587
Total effect of working capital changes		**2,515**	**(1,699)**
Income taxes paid		(8,791)	(6,099)
Net cash provided by operating activities		**31,514**	**21,383**
Cash flows from investing activities			
Purchases of property, plant and equipment		(30,455)	(19,043)
Purchases of inventories intended for construction		(1,141)	(623)
Additional capital contribution, acquisition of subsidiaries, associates and minority interests, net of cash acquired		(457)	(989)
Proceeds from disposals of assets, subsidiaries, associates and minority interests, net of cash disposed		264	5
Interest paid and capitalized		(474)	(139)
Loans provided		(445)	(423)
Repayments of loans provided		442	83
Interest received		380	382
Net cash (used for) provided by investing activities		**(31,886)**	**(20,747)**
Cash flows from financing activities			
Proceeds from long-term debt		19,308	-
Proceeds from short-term debt		6,618	5,448
Repayments of long-term debt		(279)	(2,293)
Repayments of short-term debt		(9,134)	(862)
Interest paid		(119)	(111)
Purchase of treasury shares	15	(599)	-
Dividends paid	15	(7,652)	(5,860)
Net cash (used for) provided by financing activities		**8,143**	**(3,678)**
Net effect of exchange rate changes on cash, cash equivalents and bank overdrafts		635	(12)
Net increase (decrease) in cash, cash equivalents and bank overdrafts		**8,406**	**(3,054)**
Cash and cash equivalents at beginning of the year		2,614	5,668
Cash and cash equivalents reclassified as assets classified as held for sale		(29)	-
Cash, cash equivalents and bank overdrafts at end of the year		**10,991**	**2,614**

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

OAO NOVATEK
Consolidated Statement of Changes in Equity
(in millions of Russian roubles, except for number of shares)

	Number of ordinary shares (in thousands)	**Ordinary share capital**	**Treasury shares**	**Additional paid in capital**	**Asset revaluation surplus on acquisitions**	**Currency translation differences**	**Retained earnings**	**Equity attributable to OAO NOVATEK shareholders**	**Minority interest**	**Total equity**
At 31 December 2006	***3,036,306***	**393**	**-**	**30,081**	**5,617**	**-**	**32,229**	**68,320**	**356**	**68,676**
Dividends (Note 15)	-	-	-	-	-	-	(5,860)	(5,860)	-	(5,860)
Purchase of minority interest	-	-	-	-	-	-	(37)	(37)	(111)	(148)
Impact of additional shares subscription in subsidiaries on minority interest	-	-	-	-	-	-	-	-	240	240
Share-based compensation funded by shareholders	-	-	-	176	-	-	-	176	-	176
Profit (loss) for the year	-	-	-	-	-	-	18,736	18,736	(8)	18,728
At 31 December 2007	***3,036,306***	**393**	**-**	**30,257**	**5,617**	**-**	**45,068**	**81,335**	**477**	**81,812**
Dividends (Note 15)	-	-	-	-	-	-	(7,651)	(7,651)	-	(7,651)
Purchase of treasury shares (Note 15)	*(4,192)*	-	(599)	-	-	-	-	(599)	-	(599)
Impact of additional shares subscription in subsidiaries on minority interest	-	-	-	-	-	-	-	-	108	108
Disposal of subsidiaries	-	-	-	-	-	-	-	-	(42)	(42)
Share-based compensation funded by shareholders	-	-	-	176	-	-	-	176	-	176
Currency translation differences	-	-	-	-	-	(91)	-	(91)	-	(91)
Profit (loss) for the year	-	-	-	-	-	-	22,899	22,899	28	22,927
At 31 December 2008	***3,032,114***	**393**	**(599)**	**30,433**	**5,617**	**(91)**	**60,316**	**96,069**	**571**	**96,640**

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

1 ORGANISATION AND PRINCIPAL ACTIVITIES

OAO NOVATEK (hereinafter referred to as "NOVATEK") and its subsidiaries (hereinafter jointly referred to as the "Group") is an independent oil and gas company engaged in the acquisition, exploration, development, production and processing of hydrocarbons with its core operations of oil and gas properties located and incorporated in the Yamal-Nenets Autonomous Region ("YNAO") of the Russian Federation.

The Group sells its natural gas on the Russian domestic market at both regulated and unregulated market prices; however, the majority of natural gas sold on the domestic market is sold at prices regulated by the Federal Tariff Service, a governmental agency. The Group's stable gas condensate and crude oil sales are sold on both the Russian domestic and international markets, and are subject to fluctuations in benchmark crude oil prices. Additionally, the Group's natural gas sales fluctuate on a seasonal basis due mostly to Russian weather conditions, with sales peaking in the winter months of December and January and decreasing in the summer months of July and August. The Group's liquids sales volumes comprising stable gas condensate, crude oil and oil products remain relatively stable from period to period.

2 BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). In the absence of specific IFRS guidance for oil and gas producing companies, the Group has developed accounting policies in accordance with other generally accepted accounting principles for oil and gas producing companies, mainly US GAAP, insofar as they do not conflict with IFRS principles. The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

Most of the Group entities maintained their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR"). The Group's consolidated financial statements are based on the statutory records with adjustments and reclassifications recorded in the consolidated financial statements for the fair presentation in accordance with IFRS. The principal adjustments primarily relate to (1) depreciation, depletion and amortization, and valuation of property, plant and equipment, (2) consolidation of subsidiaries, (3) business combinations, (4) accounting for income taxes, and (5) valuation of unrecoverable assets, expense recognition and other provisions.

The consolidated financial statements have been prepared under the historical cost convention and are presented in Russian roubles, the Group's reporting currency and the functional currency of the majority of entities. The assets and liabilities of the Group entities whose functional currency is not the Russian rouble are translated into Russian roubles at the exchange rate at the balance sheet date. The financial results of these entities are translated into Russian roubles using average exchange rates for the reporting periods. Exchange adjustments arising on the opening net assets and the profits for the reporting period are taken to a separate component of equity and reported in the consolidated statement of changes in equity.

Exchange rates, restrictions and controls. The official rate of exchange of the Russian rouble to the US dollar ("USD") at 31 December 2008 and 2007 was 29.38 and 24.55 Russian roubles to USD 1.00, respectively. The official rate of exchange of the Russian rouble to the Euro at 31 December 2008 and 2007 was 41.44 and 35.93 Russian roubles to 1.00 Euro, respectively. Any re-measurement of Russian rouble amounts to US dollars or any other currency should not be construed as a representation that such Russian rouble amounts have been, could be, or will in the future be converted into other currencies at these exchange rates.

Reclassifications. The following reclassification has been made to the comparative figures to conform to the current period presentation. Commencing January 2008, crude oil sales on the domestic market are presented gross of rail transportation costs. Accordingly, crude oil sales on the domestic market and crude oil transportation to customers for the year ended 31 December 2007 were increased by RR 49 million.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation. The accompanying consolidated financial statements include the operations of all controlled companies in which NOVATEK directly or indirectly owns more than 50 percent of the voting stock or otherwise has the power to govern the financial and operating policies. Subsidiaries are consolidated from the date on which control is obtained unless the acquisition occurred between entities under common control, which are accounted for from the beginning of the earliest period presented. Subsidiaries are no longer consolidated from the date that control ceases. Except for the acquisition of entities under common control, the purchase method of accounting is used to account for the acquisition of subsidiaries.

Upon achieving a controlling interest in an entity in which the Group previously held a non-controlling interest, the acquiree's identifiable assets, liabilities and contingent liabilities are restated to their fair values as at the date of achieving control. The effect of revaluing previously held interests to current fair values is recorded within asset revaluation surplus in the consolidated statement of changes in equity.

Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

All intercompany transactions, balances and unrealized gains on transactions between the Group entities are eliminated. Unrealized losses are also eliminated upon consolidation, but in the case where an asset is transferred with a loss amongst the Group entities, this event is considered by management as an impairment indicator for that asset.

Minority interest is that part of the net results and of the net assets of a subsidiary, including the fair value adjustments, which is attributable to interests which are not owned, directly or indirectly, by NOVATEK. Minority interest forms a separate component of the Group's equity.

Acquisition of minority interests. For accounting of acquisitions of non-controlling minority stakes, the difference between the purchase consideration and the carrying amount of minority interests acquired is recognized within equity.

Investments in associates. Associated companies are entities over which the Group has significant influence, but which it does not control. Generally, significant influence exists when the Group has between 20 and 50 percent of voting rights. On acquisition of the associated company the difference between the cost of an acquisition and the share of the fair value of the associate's identifiable net assets represents goodwill. Associated companies are accounted for using the equity method and are initially recognized at cost. After the date of acquisition the carrying amount of the investment is increased or decreased to recognize the Group's share of the profit or loss of the investee. The carrying amount of associates includes goodwill identified on acquisition less accumulated impairment losses, if any. The Group's share of the post-acquisition profits or losses of associates is recorded in the consolidated statement of income, and its share of post-acquisition movements in reserves is recognized in the consolidated statement of changes in equity. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealized gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Non-current assets held for sale. Non-current assets classified as held for sale are measured at the lower of carrying amount and fair value less costs of sell. Non-current assets are classified as held for sale if their carrying amounts will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Property, plant and equipment once classified as held for sale are not depreciated.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment. Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation, depletion, amortization and impairment.

The Group follows the successful efforts method of accounting for its oil and gas properties and equipment whereby property acquisitions, successful exploratory wells, all development costs and support equipment and facilities are capitalized. Unsuccessful exploratory wells are charged to expense at the time the wells are determined to be non-productive. Production costs, overheads and all exploration costs other than exploratory drilling are charged to expense as incurred. Acquisition costs of unproved properties are evaluated periodically and any impairment assessed is charged to expense.

The Group's principal oil and gas reserves have been independently estimated by internationally recognized petroleum engineers whereas other oil and gas reserves of the Group have been determined based on estimates of mineral reserves prepared by management in accordance with internationally recognized definitions. The present value of the estimated costs of dismantling oil and gas production facilities, including abandonment and site restoration costs, are recognized when the obligation is incurred and are included within the carrying value of property, plant and equipment, subject to depletion using the unit-of-production method.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components that extend the life of property, plant and equipment items are capitalized and depreciated over the estimated remaining life of the major part or component.

The cost of self-constructed assets includes the cost of direct materials, direct employee related costs, a pro-rata portion of depreciation of assets used for construction and an allocation of the Group's overhead costs.

At each reporting date management assesses whether there is any indication of impairment in respect of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognized in the consolidated statement of income. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. Gains and losses are recognized in the consolidated statement of income.

Exploration costs. Exploration costs (geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity), excluding exploratory drilling expenditures and license acquisition costs, are charged to the consolidated statement of income as incurred. License acquisition costs and exploratory drilling costs are recognized as assets until it is determined whether proved reserves justifying their commercial development have been found. If no proved reserves are found, the capitalized drilling costs are charged to the consolidated statement of income. License acquisition costs and exploratory drilling costs recognized as assets are reviewed for impairment on an annual basis.

Depreciation. Depreciation, depletion and amortization of oil and gas properties and equipment (except for processing facilities) is calculated using the unit-of-production method for each field based upon proved developed reserves for development costs, and total proved reserves for costs associated with acquisitions of proved properties. A portion of the reserves used for depreciation, depletion and amortization calculations include reserves expected to be produced beyond license expiry dates. Management believes that there is requisite legislation and past results (or experience) to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the current license expiry dates.

Property, plant and equipment, other than oil and gas properties and equipment, are depreciated on a straight-line basis over their estimated useful lives. Land and assets under construction are not depreciated.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The estimated useful lives of the Group's property, plant and equipment, other than oil and gas properties and equipment, are as follows:

	Years
Machinery and equipment	5-15
Processing facilities	20-30
Buildings	25-50

Derivative instruments. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognizing the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either:

a) hedges of the fair value of recognized assets or liabilities or a firm commitment (fair value hedge);
b) hedges of a particular risk associated with a recognized asset or liability or a highly probable forecast transaction (cash flow hedge).

At inception, the Group documents the relationship between the hedging instruments and the items hedged, as well as the Group's risk management objectives and strategy for undertaking various hedging activities. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

There were no derivative instruments used or in place as at 31 December 2008, therefore, there were no derivative instruments related impacts in the consolidated financial statements of the Group.

(a) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the consolidated statement of income, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The Group only applies fair value hedge accounting for hedging fixed interest risk on borrowings. The gain or loss relating to the effective portion of interest rate swaps hedging fixed rate borrowings is recognized in the consolidated statement of income within finance income (expenses). The gain or loss relating to the ineffective portion is recognized in the consolidated statement of income within other income (loss). Changes in the fair value of the hedge fixed rate borrowings attributable to interest rate risk are recognized in the consolidated statement of income within finance income (expenses).

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortized to profit or loss over the period to maturity. There were no fair value hedges used throughout 2007 or 2008 or in place at 31 December 2008.

(b) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognized in consolidated statement of changes in equity. The gain or loss relating to the ineffective portion is recognized immediately in the consolidated statement of income within other income (loss).

Amounts accumulated in equity are recycled in the consolidated statement of income in the periods when the hedged item affects profit or loss (for example, when the forecast sale that is hedged takes place). The gain or loss relating to the effective portion of interest rate swaps hedging variable rate borrowings is recognized in the consolidated statement of income within finance income (expenses). The gain or loss relating to the ineffective portion is recognized in the consolidated statement of income within other income (loss). However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory or fixed assets), the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset. The deferred amounts are ultimately recognized in cost of goods sold in case of inventory or in depreciation in the case of fixed assets.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognized when the forecast transaction is ultimately recognized in the consolidated statement of income. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the consolidated statement of income within other income (loss). There were no cash flow hedges used throughout 2007 or 2008 or in place at 31 December 2008.

(c) Derivatives at fair value through profit or loss and accounted for at fair value through profit or loss

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any these derivative instruments are recognized immediately in the consolidated statement of income within other income (loss). There were no net derivative instruments recorded at fair value through profit or loss throughout 2007 or 2008 or in place at 31 December 2008.

Effective interest method. The effective interest method is a method of calculating the carrying value of a financial asset or a financial liability held at amortized costs and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts future cash payments and receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying value of the financial asset or financial liability.

Financial assets. The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, held-to-maturity, loans and receivables, and available-for-sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition. Subsequent reclassification of financial assets is made only as a result of a change in intention or ability of management to hold the financial assets. Financial assets are recognized initially at fair value, normally being the transaction price plus, in the case of financial assets not at fair value through profit or loss, directly attributable transaction costs. The subsequent measurement of financial assets depends on their classification.

(a) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term. Derivative instruments are also categorized as held for trading unless they are designated as hedges. Financial assets carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the consolidated statement of income. Gains or losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are presented in the consolidated statement of income within other income (loss) in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognized in the consolidated statement of income as part of other income when the Group's right to receive payments is established.

Financial assets at fair value through profit or loss are classified as current assets. There were no financial assets designated at fair value through profit or loss held by the Group at the reporting dates.

(b) Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities and are classified as held-to-maturity when the Group has the positive intention and ability to hold these investments to maturity. After initial measurement, the held-to-maturity investments are measured at amortized cost using the effective interest method. Gains and losses are recognized in the consolidated statement of income when the investments are derecognized or impaired, as well as through the amortization process.

Held-to-maturity investments are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. There were no such investments held by the Group at the reporting dates.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Financial assets classified as loans and receivables are carried at amortized cost using the effective interest method. Gains and losses are recognized in the consolidated statement of income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Loans and receivables are included in current assets, except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets.

(d) Available-for-sale financial assets

Financial assets classified as available-for-sale are non-derivatives financial assets that are either specially designated in this category or are not classified in any of the other categories. After initial recognition, financial assets classified as available-for-sale are measured at fair value, with gains and losses recognized directly in the consolidated statement of changes in equity until the investment is derecognized or determined to be impaired, at which time the cumulative gain or loss previously recorded in equity is recognized in profit or loss.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale financial assets are analyzed between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the security. The translation differences on monetary securities are recognized in profit or loss, while translation differences on non-monetary securities are recognized in equity. Changes in the fair value of monetary and non-monetary securities classified as available-for-sale are recognized in equity. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognized in equity are included in the consolidated statement of income as profit or loss on sales of available-for-sale investments.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss) is removed from equity and recognized in the consolidated statement of income. Impairment losses recognized in the consolidated statement of income on equity instruments are not reversed. There were no available-for-sale investments held by the Group at the reporting dates.

Financial liabilities. Financial liabilities are classified at initial recognition as either financial liabilities at fair value through profit or loss, derivative instruments designated as hedging instruments in an effective hedge or as financial liabilities measured at amortized cost. The measurement of financial liabilities depends on their classification, as follows:

(a) Financial liabilities at fair value through profit or loss

Derivative instruments, other than those designated as effective hedging instruments, are classified as held for trading and are included in this category. These financial liabilities are carried on the balance sheet at fair value with gains or losses recognized in the consolidated statement of income. There were no financial liabilities designated at fair value through profit or loss held by the Group at the reporting dates.

(b) Financial liabilities measured at amortized cost

All other financial liabilities are included in this category and initially recognized at fair value. For interest-bearing debt, the fair value of the liability is the fair value of the proceeds received net of associated issue costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method. This category of financial liabilities includes trade and other payables and debt.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income taxes. Income taxes have been provided for in the consolidated financial statements in accordance with Russian legislation enacted or substantively enacted as of end of the reporting period. The income tax charge or benefit comprises current tax and deferred tax and is recognized in the consolidated statement of income unless it relates to transactions that are recognized, in the same or a different period, directly in equity.

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

Deferred tax assets and liabilities are recognized in full for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or when the tax loss carry forwards will be utilized. Deferred tax assets and liabilities are netted only with respect to 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 utilized.

Deferred income tax is provided on post acquisition retained earnings of subsidiaries, except where the Group controls the subsidiary’s dividend policy and it is probable that the difference will not reverse through dividends or otherwise in the foreseeable future.

Inventories. Natural gas, gas condensate, crude oil and related products inventories are valued at the lower of cost or net realizable value. The cost of inventories includes applicable purchase costs of raw materials, direct operating costs, and related production overhead expenses and is recorded on a first-in-first-out (FIFO) basis. Net realizable value is the estimate of the selling price in the ordinary course of business, less selling expenses.

Materials and supplies inventories are carried at amounts which do not exceed their respective recoverable amounts in the normal course of business.

Trade and other receivables. Trade receivables are represented by amounts due from regular customers in the ordinary course of business (production and marketing of natural gas, gas condensate, crude oil and related products; production and marketing of polymer and insulation tape products). Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method and include value-added taxes. Trade receivables are analyzed for impairment on a debtor by debtor basis. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset’s carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of the provision is recognized in the consolidated statement of income within operating expenses. Subsequent recoveries of amounts previously written off are credited against the amount of the provision in the consolidated statement of income.

Cash and cash equivalents. Cash and cash equivalents comprises cash on hand, cash deposits held with banks, investments which are readily convertible to known amounts of cash and which are not subject to significant risk of change in value and have an original maturity of three months or less. For purposes of the presentation of the statement of cash flows, bank overdrafts are deducted from cash and cash equivalents. Bank overdrafts are shown within short-term debt in current liabilities on the consolidated balance sheet.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Treasury shares. Where any Group company purchases NOVATEK's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to OAO NOVATEK shareholders until the shares are cancelled or reissued. Where such shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to OAO NOVATEK shareholders. Treasury shares are recorded at weighted average cost. Gains or losses resulting from subsequent sales of shares are recorded in the consolidated statement of changes in equity, net of associated costs including taxation.

Dividends. Dividends are recognized as a liability and deducted from shareholders' equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the consolidated financial statements are authorized for issue.

Value added tax (VAT). Output VAT related to sales is payable to the tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT related to purchases is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases which is not settled or recovered at the balance sheet date (VAT payable and VAT recoverable) is recognized on a gross basis and disclosed separately within current assets and current liabilities. Where a provision has been made for the impairment of receivables, the impairment loss is recorded for the gross amount of the debtor, including VAT.

Borrowings. Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the consolidated statement of income over the period of the borrowings using the effective interest method.

Interest costs on borrowings to finance the construction of property, plant and equipment are capitalized during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

Trade and other payables. Trade payables are accrued when the counterparty performed its obligations under the contract. Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

Provisions for liabilities and charges. Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events; when 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.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be low.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. Provisions are reassessed at each reporting date and changes in the provisions resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset retirement obligations. An asset retirement obligation is recognized when the Group has a present legal or constructive obligation to dismantle, remove and restore items of property, plant and equipment. The amount of the obligation is the present value of the estimated expenditures expected to be required to settle the obligation, determined using discount rates reflecting adjustments for risks specific to the obligation. Changes in the obligation resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Changes in the obligation, reassessed at each balance sheet date, related to a change in the expected pattern of settlement of the obligation, or in the estimated amount of the obligation or in the discount rates, are treated as a change in an accounting estimate in the period. Such changes are reflected as adjustments to the carrying value of property, plant and equipment and the corresponding liability.

Foreign currency transactions. Transactions denominated in foreign currencies are converted into the functional currency of each entity of the Group at the exchange rates prevailing on the date of transactions. Exchange gains and losses resulting from foreign currency remeasurement into the functional currencies are included in the determination of profit for the reporting period.

Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency of each entity of the Group by applying the year end exchange rate and the effect is stated in the consolidated statement of income. Non-monetary assets and liabilities denominated in foreign currencies valued at cost are converted into the functional currency of each entity of the Group at the initial exchange rate. Non-monetary assets that are remeasured to fair value, recoverable amount or realizable value, are translated at the exchange rate applicable to the date of remeasurement.

Revenue recognition. 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, value-added tax and export duties.

Revenues from oil and gas sales and sales of polymer and insulation tape are recognized when such products are shipped or delivered to customers in accordance to the contract terms and the title has transferred. Services are recognized in the period in which the services are rendered.

Interest income is recognized as the interest accrues as related to the net carrying amount of the financial asset.

General and administrative expenses. General and administrative expenses represent overall corporate management and other expenses related to the general management and administration of the business unit as a whole. They include management and administrative compensation, certain legal and other advisory expenses, insurance of properties, social expenses and other expenses necessary for the administration of the Group.

Employee benefits. Wages and salaries, bonuses, voluntary medical insurance, paid annual and sick leaves are accrued in the period in which the associated services are rendered by the employees of the Group. Compensation at dismissals, vocational support payments, and other allowances are expensed when incurred.

The Group contributes to the Russian Federation State social insurance fund and State pension plan on behalf of its employees. Mandatory contributions to the State social insurance fund and the State pension plan, which is a defined contribution plan, are expensed when incurred and are included in payroll expenses.

The Group also incurs employee costs related to the provision of benefits such as health and social infrastructure and services, employees meals, transportation, and other services. These amounts principally represent an implicit cost of employing production workers and, accordingly, are charged to payroll expenses in the consolidated statement of income.

Share based compensation. The Group accounts for share-based compensation in accordance with IFRS 2, *Share-based Payment* ("IFRS 2"). The fair value of the employee services received in exchange for the grant of the equity instruments is recognized as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the instruments granted measured at the grant date. For share-based compensation made to employees by shareholders, an increase to additional paid in capital is recorded equal to the associated compensation expense each period.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Pension obligations. The Group operates a non-contributory post-employment defined benefit plan based on employees' years of service and average salary (Note 12).

The liability recognized in the consolidated balance sheet in respect of the defined benefit pension plan is the present value of the defined benefit obligations at the balance sheet date, together with adjustments for unrecognized past service costs. The present value of the pension obligations are determined by discounting the estimated future cash outflows. The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method. The discount rate was determined by reference to Russian rouble denominated bonds issued by the Government of the Russian Federation chosen to match the duration of the post-employment benefit obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are recorded to the consolidated statement of income in the period in which they arise. Past-service costs are amortized on a straight-line basis over the vesting period.

Earnings per share. Earnings per share are determined by dividing the profit or loss attributable to OAO NOVATEK shareholders by the weighted average number of shares outstanding during the reporting period.

Segment reporting. A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment) or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. Segments with a majority of revenues earned from sales to external customers and whose revenues, results or assets are ten percent or more of all the segments are reported separately.

The Group's primary format for reporting segment information is business segments and the secondary format is geographical segments. The risks and returns of the Group's operations are primarily determined by the nature of the different activities that the Group engages in, rather than the geographical location of these operations. This is reflected by the Group's organizational structure.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Consolidated financial statements prepared in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period.

Management reviews these estimates and assumptions on a continuous basis, by reference to past experiences and other factors considered as reasonable which form the basis for assessing the book values of assets and liabilities. Adjustments to accounting estimates are recognized in the period in which the estimate is revised if the change affects only that period or in the period of the revision and subsequent periods, if both periods are affected. Management also makes certain judgments, apart from those involving estimations, in the process of applying the Group's accounting policies. Actual results may differ from such estimates if different assumptions or circumstances apply.

Judgments and estimates that have the most significant effect on the amounts reported in these consolidated financial statements and have a risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are described below.

Useful lives of property, plant and equipment. Management assesses the useful life of an asset by considering the expected usage, estimated technical obsolescence, residual value, physical wear and tear and the operating environment in which the asset is located. Differences between such estimates and actual results may have a material impact on the amount of the carrying values of the property, plant and equipment and may result in adjustments to future depreciation rates and expenses for the period.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Fair values of financial assets and liabilities. The fair value of financial assets and liabilities, other than financial instruments that are traded in an active market, is determined by applying various valuation methodologies. Management uses its judgment to make assumptions based on market conditions existing at each balance sheet date. Discounted cash flow analysis is used for various loans and receivables as well as debt instruments that are not traded in active markets. The effective interest rate is determined by reference to the interest rates of instruments available to the Group in active markets. In the absence of such instruments, the effective interest rate is determined by reference to the interest rates of active market instruments available adjusted for the Group's specific risk premium estimated by management.

Deferred income tax asset recognition. Management assesses deferred income tax assets at each balance sheet date and determines the amount recorded to the extent that realization of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimations based on prior years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

Estimation of oil and gas reserves. Engineering estimates of oil and gas reserves are inherently uncertain and are subject to future revisions. The Group estimates its oil and gas reserves in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves. Accounting measures such as depreciation, depletion and amortization charges, impairment assessments and asset retirement obligations that are based on the estimates of proved reserves are subject to change based on future changes to estimates of oil and gas reserves.

Proved reserves are estimated by reference to available reservoir and well information, including production and pressure trends for producing reservoirs. Furthermore, estimates of proved reserves only include volumes for which access to market is assured with reasonable certainty. All proved reserves estimates are subject to revision, either upward or downward, based on new information, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As those fields are further developed, new information may lead to further revisions in reserve estimates.

Oil and gas reserves have a direct impact on certain amounts reported in the consolidated financial statements, most notably depreciation, depletion and amortization as well as impairment expenses. Depreciation rates on oil and gas assets using the units-of-production method for each field are based on proved developed reserves for development costs, and total proved reserves for costs associated with the acquisition of proved properties. Assuming all variables are held constant, an increase in proved developed reserves for each field decreases depreciation, depletion and amortization expenses. Conversely, a decrease in the estimated proved developed reserves increases depreciation, depletion and amortization expenses. Moreover, estimated proved reserves are used to calculate future cash flows from oil and gas properties, which serve as an indicator in determining whether or not property impairment is present.

Although the possibility exists for changes or revisions in estimated reserves to have a critical effect on depreciation, depletion and amortization charges and, therefore, reported net profit for the year, it is expected that in the normal course of business the diversity of the Group's asset portfolio will mitigate the likelihood of this occurring.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Impairment of non-financial assets. Management assesses whether there are any indicators of possible impairment of all non-financial assets at each reporting date based on events or circumstances that indicate the carrying value of assets may not be recoverable. Such indicators include changes in the Group's business plans, changes in commodity prices leading to unprofitable performances, changes in product mixes, and for oil and gas properties, significant downward revisions of estimated proved reserves. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable.

When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows.

Impairment provision for trade receivables. The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the receivable is potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates.

When there is no expectation of recovering additional cash for an amount receivable, the expected amount receivable is written off against the associated provision.

Future cash flows of trade receivables that are evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Pension obligations. The cost of defined benefit pension plans and related current service costs are determined using actuarial valuations. The actuarial valuations involve making demographic assumptions (mortality rates, age of retirement, employee turnover and disability) as well as financial assumptions (discount rates, expected rates of return on assets, inflation forecasts, future salary and pension increases). Due to the long term nature of these plans, such estimates are subject to significant uncertainty.

Asset retirement obligations. Management makes provision for the future costs of decommissioning oil and gas production facilities, pipelines and related support equipment based on the best estimates of future cost and economic lives of those assets. Estimating future asset retirement obligations is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future. Changes in the measurement of existing obligations can result from changes in estimated timing, future costs or discount rates used in valuation.

The Group also assesses its liabilities for site restoration at each balance sheet period in accordance with the guidelines of IFRIC 1, *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. The amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the balance sheet date based on current legislation where the Group's respective operating assets are located, and is also subject to change because of modifications, revisions and changes in laws and regulations and their interpretation thereof. As a result of the subjectivity of these provisions there is uncertainty regarding both the amount and estimated timing of incurring such costs.

5 ACQUISITIONS AND DISPOSALS

In December 2008, the Group disposed of its non-core subsidiary, OOO "Purovsky Terminal", to third parties for RR 235 million payable in equal monthly installments through July 2009**.** The Group recognized a loss on the sale of RR 18 million, net of associated income tax of RR 11 million. The Group included balances and results of the operations of the disposed subsidiary within "other" in the Group's segment information.

In November 2007, the Group disposed of its non-core subsidiary, OAO "Geolog Yamala", to third parties for RR 175 million payable in three equal annual installments, recognizing a gain on sale of RR 85 million, net of associated income tax of RR 10 million. The Group included balances and results of the operations of the disposed subsidiary within "other" in the Group's segment information.

In September 2007, the Group acquired a 50 percent working interest in the Concession Agreement for Gas and Crude Oil Exploration and Exploitation in El Arish Offshore Area (hereinafter referred to as the "Concession Agreement") in the Arab Republic of Egypt. The remaining working interest is held by Tharwa Petroleum S.A.E. Pursuant to the Concession Agreement the Group is committed to spend a minimum of USD 40 million on exploration operations during the initial exploration period of four years. At 31 December 2008, amounts spent under the terms of the Concession Agreement aggregated approximately USD 20 million.

In July 2007, the Group acquired 25 percent participation interests in OOO Oiltechproduct-Invest, OOO Petra Invest-M and OOO Tailiksneftegas. These entities hold exploration licenses for the Sredniy Chaselskiy, Severo Russkiy, Yuzhno-Zapolyarniy, Zapadno-Tazovskiy, Anomalniy and Severo-Yamsoveskiy license area which expire in 2010 and 2011. The Group intends to extend the license terms for these exploration licenses based on the activities performed to date. The cost of these participation interests was RR 1,125 million, of which RR 108 million were payable at 31 December 2008. The Group has an option to purchase an additional 25 percent participation interests in the aforementioned companies after they are granted production licenses and if the license areas are deemed economically viable. Purchase prices for these entities approximated their fair value. The financial and operational activities of the acquirees were not material to the Group's assets, liabilities, revenues and results of operations as at and for the years ended 31 December 2008 and 2007.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

6 PROPERTY, PLANT AND EQUIPMENT

Movements in property, plant and equipment, for the years ended 31 December 2008 and 2007 are as follows:

	Oil and gas properties and equipment	Assets under construction	Other	Total
Cost	66,555	4,517	3,643	74,715
Accumulated depreciation, depletion and amortization	(7,529)	-	(452)	(7,981)
Net book value at 1 January 2007	**59,026**	**4,517**	**3,191**	**66,734**
Acquisition of subsidiaries	-	-	254	254
Additions	2,136	17,324	6	19,466
Transfers	2,716	(2,999)	283	-
Depreciation, depletion and amortization	(3,478)	-	(260)	(3,738)
Disposal of subsidiaries, net	-	-	(18)	(18)
Disposals, net	(2)	-	(27)	(29)
Cost	71,404	18,842	4,098	94,344
Accumulated depreciation, depletion and amortization	(11,006)	-	(669)	(11,675)
Net book value at 31 December 2007	**60,398**	**18,842**	**3,429**	**82,669**
Additions	3,077	28,723	10	31,810
Transfers	21,517	(22,338)	821	-
Depreciation, depletion and amortization	(4,291)	-	(318)	(4,609)
Disposal of subsidiaries, net	(81)	(77)	(17)	(175)
Reclassified as assets classified as held for sale	(437)	(257)	(2)	(696)
Disposals, net	(107)	(122)	(56)	(285)
Cost	95,242	24,771	4,787	124,800
Accumulated depreciation, depletion and amortization	(15,166)	-	(920)	(16,086)
Net book value at 31 December 2008	**80,076**	**24,771**	**3,867**	**108,714**

Included within the oil and gas properties and equipment balance at 31 December 2008 and 2007 are proved properties of RR 26,755 million and RR 28,222 million, net of accumulated depreciation, depletion and amortization of RR 6,470 million and RR 4,908 million, respectively.

During 2008, the transfers and additions to oil and gas property and equipment included the completion of the second phase of development at the Yurkharovskoye field in the amount of RR 13,492 million, which consisted of a natural gas separation unit, a condensate preparation unit, and 87 kilometers of natural gas pipeline connected to the Unified Gas Supply System. The Group also launched the second phase of the Purovsky Gas Condensate Plant for RR 3,468 million, which increased processing capacity of the plant by an additional 3 million tons to 5 million tons per annum as well as plant storage facilities.

Included in additions to property, plant and equipment for the years ending 31 December 2008 and 2007 is capitalized interest of RR 622 million and RR 139 million, respectively. The interest capitalization rates for 2008 and 2007 used for additions were 4.0 percent and 6.0 percent, respectively.

Depreciation, depletion and amortization for the year ended 31 December 2008 comprises charge of RR 4,478 million included in operating expenses, RR 103 million of depreciation of administrative buildings included in general and administrative expenses (see Note 20), and RR 28 million of depreciation capitalized in the course of intragroup construction services. Depreciation, depletion and amortization for the year ended 31 December 2007 comprises charge of RR 3,668 million included in operating expenses, RR 66 million of depreciation of administrative buildings included in general and administrative expenses (see Note 20), and RR 4 million of depreciation capitalized in the course of intragroup construction services.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Asset retirement obligations. Estimated costs of dismantling oil and gas production facilities, pipelines and related processing facilities, including abandonment and site restoration costs, amounting to RR 1,284 million and RR 618 million at 31 December 2008 and 2007, respectively, are included in the cost of oil and gas properties and equipment. The Group has estimated its liability based on current legislation using estimated costs and timing of when the expenses are expected to be incurred between the end of the reporting period and 2051. Governmental authorities are continually reviewing regulations and their enforcement. Consequently, the Group's ultimate liabilities may differ from the recorded amounts.

7 INVENTORIES

	At 31 December:	
	2008	**2007**
Materials and supplies at net realizable value (net of provisions of RR 32 million and RR 45 million at 31 December 2008 and 2007, respectively)	418	280
Materials and supplies at cost	508	438
Natural gas and hydrocarbon liquids at cost	856	799
Polymer and insulation tape products (net of provisions of RR 4 million and RR 10 million at 31 December 2008 and 2007, respectively)	253	177
Other inventories	121	100
Total inventories	**2,156**	**1,794**

The Group recorded an expense of RR 25 million and RR 101 million during the years ended 31 December 2008 and 2007, respectively, to write-down the carrying value of inventory due to obsolescence.

8 TRADE AND OTHER RECEIVABLES

	At 31 December:	
	2008	**2007**
Trade receivables (net of provision of RR 9 million and RR 8 million at 31 December 2008 and 2007, respectively)	1,819	2,947
Interest on loans receivable	-	3
Other receivables (net of provision of RR 25 million and RR 47 million at 31 December 2008 and 2007, respectively)	666	317
Total trade and other receivables	**2,485**	**3,267**

The carrying values of trade and other receivables approximate their fair value. The related exposure to credit risk at the balance sheet date is the carrying value of each class of receivables mentioned above. The Group does not hold any collateral as security for trade and other receivables (see Note 23 for credit risk disclosures).

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

8 TRADE AND OTHER RECEIVABLES (CONTINUED)

Trade and other receivables that are less than three months past due are generally not considered for impairment unless other indicators of impairment exist. Trade and other receivables of RR 162 million and RR 81 million at 31 December 2008 and 2007, respectively were past due but not impaired. These relate to a number of independent customers for whom there is no recent history of default. The ageing analysis of these past due but not impaired trade and other receivables are as follows:

	At 31 December:	
	2008	2007
Up to 90 days past-due	84	19
91 to 360 days past-due	67	55
Over 360 days past-due	11	7
Total past due but not impaired	**162**	**81**
Not past due and not impaired	2,323	3,186
Total trade and other receivables	**2,485**	**3,267**

Movements on the Group provision for impairment of trade and other receivables are as follows:

	Year ended 31 December:	
	2008	2007
At 1 January	**55**	**75**
Additional provision recorded	67	23
Receivables written off as uncollectible	(84)	(43)
Provision amount reversed into income	(4)	-
At 31 December	**34**	**55**

The provision for impaired trade and other receivables has been included in the consolidated statement of income in net impairment expense.

9 PREPAYMENTS AND OTHER CURRENT ASSETS

	At 31 December:	
	2008	2007
Financial assets		
Short-term loans receivable	3	36
Short-term bank deposits	5	-
Non-financial assets		
Recoverable value-added tax	1,174	2,668
Prepayments and advances to suppliers (net of provision of RR 4 million and RR 4 million at 31 December 2008 and 2007)	2,808	2,413
Deferred export duties for stable gas condensate	299	1,069
Prepaid taxes other than income tax	3,004	974
Deferred transportation expense for stable gas condensate	318	334
Deferred transportation expense for natural gas	351	55
Other current assets	68	111
Total prepayments and other current assets	**8,030**	**7,660**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

10 CASH AND CASH EQUIVALENTS

	At 31 December:	
	2008	2007
Cash in bank accounts	5,304	1,787
Interest bearing bank deposits	5,614	2,195
Other deposits	74	-
Total cash and cash equivalents per the consolidated balance sheet	**10,992**	**3,982**
Less: bank overdrafts (Note 13)	(1)	(1,368)
Cash, cash equivalents and bank overdrafts per the consolidated statement of cash flows	**10,991**	**2,614**

All deposits have original maturities of less than three months (see Note 23 for credit risk disclosures).

11 LONG-TERM DEBT

	At 31 December:	
	2008	2007
US dollar denominated loans	23,293	54
Euro denominated loans	45	270
Total	**23,338**	**324**
Less: current portion of long-term debt	(3,403)	(282)
Total long-term debt	**19,935**	**42**

At 31 December 2008 and 2007, the Group's long-term debt by facility is as follows:

	At 31 December:	
	2008	2007
Syndicated term loan facility	23,293	-
Other loans	45	324
Total	**23,338**	**324**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

11 LONG-TERM DEBT (CONTINUED)

Syndicated term loan facility. On 21 April 2008, the Group obtained a USD 800 million unsecured syndicated term loan facility for general corporate purposes including funding capital expenditure programs. The facility has a three year tenure with payments to begin 18 months after 21 April 2008 and is to be repaid in quarterly installments thereafter. The facility pays an initial interest of LIBOR plus 1.25 percent per annum for the first 18 months and rising to 1.50 percent per annum thereafter (3.42 percent at 31 December 2008). The facility terms include the maintenance of certain restrictive financial covenants. At 31 December 2008, RR 23,293 million (USD 793 million), net of transaction costs of RR 216 million, had been drawn down under this facility agreement.

Other loans. At 31 December 2007, other loans included US dollar denominated loans totaling RR 54 million (USD 2.2 million), with a weighted average interest rate of 10.8 percent. These loans matured between 2007 and 2008 and have been fully repaid. At 31 December 2008 and 2007, other loans also included Euro denominated loans totaling RR 45 million (Euro 1.1 million) and RR 270 million (Euro 7.5 million), respectively, with a weighted average effective interest rate of 13.6 percent and 13.6 percent, respectively. These loans mature during 2009.

The carrying values of long-term debt approximate their fair value.

Scheduled maturities of long-term debt at 31 December 2008 were as follows:

Twelve months ended 31 December:	
2010	13,242
2011	6,693
Total long-term debt	**19,935**

12 PENSION OBLIGATIONS

In February 2007, the Group announced the implementation of a post-employment benefit program. Under the pension program, employees who are employed by the Group for more than three years and retire from the Group on or after the statutory retirement age will receive monthly payments from NOVATEK for life unless they are actively employed. The amount of payments to be disbursed depends on the average salary, duration and location of employment. The program is effective from 1 January 2007 and applies to employees who retire after that date.

The program represents an unfunded defined benefit plan and is accounted for as such under provisions of IAS 19, *Employee Benefits*. The impact of the program on the consolidated financial statements is disclosed below.

The amounts recognized in the consolidated balance sheet and included in other non-current liabilities are determined as follows:

	At 31 December:	
	2008	**2007**
Present value of the defined benefit obligations	468	492
Unrecognized past service cost	(256)	(276)
Defined benefit plan liability recognized in the consolidated balance sheet	**212**	**216**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

12 PENSION OBLIGATIONS (CONTINUED)

The movements in the present value of the defined benefit obligations are as follows:

	Year ended 31 December:	
	2008	2007
At 1 January	**492**	**-**
Past service cost	-	293
Interest cost	24	18
Benefits paid	(2)	-
Current service cost	67	60
Actuarial (gain) loss	(113)	121
At 31 December	**468**	**492**

The amounts recognized in the consolidated statement of income are as follows:

	Year ended 31 December:	
	2008	2007
Current service cost	67	60
Interest cost	24	18
Actuarial (gain) loss	(113)	121
Amortization of past service cost	18	17
Defined benefit plan (benefits) costs recognized in operating expenses	**(4)**	**216**
of which the following amounts were included as employee compensation in:		
Materials, services and other	(2)	106
General and administrative expenses	(2)	110

The Group recognized a loss of RR 27 million and RR 77 million as a result of experience adjustments on plan liabilities during the years ended 31 December 2008 and 2007, respectively, included in actuarial (gain) loss.

The principal actuarial assumptions used at 31 December 2008 and 2007 are as follows:

	At 31 December:	
	2008	2007
Weighted average discount rate	9.6%	6.4%
Projected annual increase in employee compensation	10%	10%
Expected increases to pension benefits	6.7%	10%

The assumed average salary and pension payment increases for Group employees have been calculated on the basis of inflation forecasts, analysis of increases of past salaries and the general salary policy of the Group. Inflation forecasts have been estimated to reduce from 12 percent for 2009 to 8 percent in 2013 and on average equal to 6 percent thereafter.

Mortality assumptions are based on the Russian mortality tables published by the State Statistics Committee from the years 1986 to 1987, which management believes are the most conservative and prudent Russian whole-population mortality tables available.

Management has assessed that reasonable changes in the most significant actuarial assumptions will not have a significant impact on the consolidated statement of income or the liability recognized in the consolidated balance sheet.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

13 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT

	At 31 December: 2008	2007
US dollar denominated loans	2,938	4,910
US dollar denominated bank overdrafts	1	1,368
Total	2,939	6,278
Add: current portion of long-term debt	3,403	282
Total short-term debt and current portion of long-term debt	**6,342**	**6,560**

US dollar denominated loans. At 31 December 2008, the US dollar denominated loans included a loan from BNP PARIBAS in the amount of RR 2,938 million (USD 100 million). The loan bears annual interest of 6.27 percent and is repayable in equal parts in August and September 2009.

At 31 December 2007, the US dollar denominated loans included a loan from BNP PARIBAS in the amount of RR 2,455 million (USD 100 million). The loan was repaid in September 2008.

At 31 December 2007, the US dollar denominated loans included loans from CALYON S.A. and CALYON RUSBANK Corporate and Investment Bank in the total amount of RR 2,455 million (USD 100 million). The loans were repaid in May 2008.

The carrying value of the short-term debt approximates their fair value.

Available credit facilities and bank overdrafts. At 31 December 2008 and 2007, the Group used RR 1 million and RR 1,368 million of its credit facilities as bank overdrafts, respectively. Available funds under these short-term credit lines with various international banks totaled RR 4,407 million (USD 150 million) and RR 4,148 million (USD 169 million) at 31 December 2008 and 2007, respectively, on either fixed or variable interest rates subject to the specific type of credit facility.

In addition, the Group has available funds up to the maximum amount of RR 2,938 million (USD 100 million) under a two year credit line facility starting from November 2007 with UniCredit Bank with interest rates negotiated on each withdrawal date.

14 TRADE PAYABLES AND ACCRUED LIABILITIES

	At 31 December: 2008	2007
Financial liabilities		
Trade payables	3,863	1,327
Other payables	450	375
Interest payable	92	9
Non-financial liabilities		
Advances from customers	1,192	1,535
Salary payables	626	352
Other payables	-	1
Trade payables and accrued liabilities	**6,223**	**3,599**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

15 SHAREHOLDERS' EQUITY

Ordinary share capital. Share capital issued and paid in consisted of 3,036,306,000 ordinary shares at 31 December 2008 and 2007 with a par value of RR 0.1 each. The total authorized number of ordinary shares was 10,593,682,000 shares at both dates.

Treasury shares. During 2008, and in accordance with the share buyback program authorized by the Board of Directors on 11 February 2008, the Group has periodically purchased ordinary shares of OAO NOVATEK in the form of Global Depository Receipts (GDRs) on the London Stock Exchange through the use of independent brokers.

At 31 December 2008, a Group wholly-owned subsidiary, Novatek Equity (Cyprus) Limited, held 419,233 GDRs (4,192 thousand ordinary shares) at total cost of RR 599 million. The Group has decided that these shares do not vote.

Dividends. Dividends declared and paid were as follows:

	Year ended 31 December:	
	2008	**2007**
Dividends payable at 1 January	1	1
Total dividends declared	7,651	5,860
Dividends paid	(7,652)	(5,860)
Dividends payable at 31 December	**-**	**1**
Dividends per share declared during the year (in Russian roubles)	2.52	1.93
Dividends per GDR declared during the year (in Russian roubles)	25.2	19.3

The Group declares and pays dividends in Russian roubles. Dividends declared in 2008 and 2007 were as follows:

Final for 2007: RR 1.52 per share or RR 15.2 per GDR declared in May 2008	4,615
Interim for 2008: RR 1.00 per share or RR 10.0 per GDR declared in October 2008	3,036
Total dividends declared in 2008	**7,651**
Final for 2006: RR 1.10 per share or RR 11.0 per GDR declared in May 2007	3,340
Interim for 2007: RR 0.83 per share or RR 8.30 per GDR declared in October 2007	2,520
Total dividends declared in 2007	**5,860**

Share-based compensation. In 2005, certain shareholders provided share-based compensation to key members of the Group's management team. The fair value of the awards of RR 879 million is being recognized as compensation expense evenly over their five year vesting period beginning the second quarter of 2005. A corresponding increase is recorded to additional paid in capital as expense is recognized to reflect the shareholders contribution in providing the award. The fair value of the awards was determined by reference to the fair value of the limited liability company's net assets estimated by its owners.

Distributable retained earnings. In accordance with Russian legislation, NOVATEK distributes profits as dividends or transfers them to reserves (fund accounts) on the basis of financial statements prepared in accordance with Russian Accounting Rules. Russian legislation identifies the net profit as basis of distribution. As of the date of preparation of these consolidated financial statements the statutory net profit of NOVATEK as determined under Russian Accounting Rules has not been finalized. For 2007, net statutory profit of NOVATEK as reported in the published annual statutory reporting forms was RR 16,242 million and the closing balance of the accumulated profit including the current year net statutory profit totaled RR 41,213 million.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

16 OIL AND GAS SALES

	Year ended 31 December:	
	2008	2007
Natural gas	45,650	35,605
Stable gas condensate	19,374	17,106
Liquefied petroleum gas	6,376	4,926
Oil products	2,633	967
Crude oil	2,043	1,802
Total oil and gas sales	**76,076**	**60,406**

17 TRANSPORTATION EXPENSES

	Year ended 31 December:	
	2008	2007
Natural gas transportation to customers	11,080	9,077
Stable gas condensate and liquefied petroleum gas transportation by rail	4,384	3,376
Stable gas condensate transportation by tankers	2,168	1,690
Unstable gas condensate transportation from the fields to the processing facilities through third party pipelines	232	115
Crude oil transportation to customers	123	127
Insurance expense	10	7
Other	156	29
Total transportation expenses	**18,153**	**14,421**

18 TAXES OTHER THAN INCOME TAX

The Group is subject to a number of taxes other than income tax, which are detailed as follows:

	Year ended 31 December:	
	2008	2007
Unified natural resources production tax	6,424	5,703
Property tax	670	544
Excise tax	8	36
Other taxes	84	96
Total taxes other than income tax	**7,186**	**6,379**

In 2008 and 2007, the unified natural resources production tax for natural gas production was fixed at a rate of RR 147 per thousand cubic meters.

The unified natural resources production tax rate for gas condensate is set at 17.5 percent of gas condensate revenues recognized by the producing entities.

Under the Tax Code of the Russian Federation, the tax rate for the unified natural resources production tax for crude oil is calculated by reference to an average price for Urals blend and an average exchange rate over the relevant tax period. Beginning 1 January 2005, the base rate was set at RR 419 per metric ton of crude oil.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

19 MATERIALS, SERVICES AND OTHER

	Year ended 31 December:	
	2008	**2007**
Employee compensation	2,169	1,897
Materials and supplies	1,766	1,521
Third party services (under operator contracts)	721	68
Repair and maintenance services	405	367
Processing fees	341	213
Electricity and fuel	308	216
Fire safety and security expense	168	263
Other	454	379
Total materials, services and other	**6,332**	**4,924**

20 GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December:	
	2008	**2007**
Employee compensation	3,053	1,961
Maintenance of social infrastructure and charitable contributions	499	559
Legal, audit, and consulting services	319	404
Business trips expense	216	199
Rent expense	184	146
Depreciation – administrative buildings	103	66
Insurance expense	90	117
Other	600	421
Total general and administrative expenses	**5,064**	**3,873**

Auditors' fees and services. ZAO PricewaterhouseCoopers Audit has served as the Group's independent external auditors for each of the reported financial years. The independent external auditors are subject to re-appointment at the Annual General Meeting of shareholders based on the recommendations from the Board of Directors. The following table presents the aggregate fees for professional services and other services rendered by ZAO PricewaterhouseCoopers Audit to the Group included within legal, audit, and consulting services:

	Year ended 31 December:	
	2008	**2007**
Audit services fee (audit of the Group's consolidated financial statements and the statutory audit of the parent company)	33	28
Non-audit services (tax services and other)	2	3
Total auditors' fees and services	**35**	**31**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

21 INCOME TAX

Reconciliation of income tax. The table below reconciles actual income tax expense and theoretical income tax, determined by applying the statutory tax rate to profit before income tax and share of income in associates.

	Year ended 31 December:	
	2008	2007
Profit before income tax (excluding share of profit (loss) of associates, net of income tax)	28,736	25,489
Theoretical income tax expense at statutory rate of 24 percent	6,896	6,117
Increase (decrease) due to:		
Non-deductible expenses	509	364
Foreign entities' taxation at lower income tax rate	(99)	(107)
Withholding tax on dividends distributed between parent and subsidiaries	-	193
Change in Russian statutory income tax rate	(1,289)	-
Other non-temporary differences	(355)	194
Total income tax expense	**5,662**	**6,761**

Effective income tax rate. The Group's Russian statutory income tax rate in 2008 and 2007 was 24.0 percent. For the years ended 31 December 2008 and 2007, the Group's effective income tax rate was 19.7 percent and 26.5 percent, respectively.

On the 20 November 2008, the Russian Federation government enacted legislation reducing the statutory income tax rate from 24 percent to 20 percent. Since this reduction in the statutory income tax rate was enacted prior to 31 December 2008, the effect of the change reduced net deferred liability by RR 1,289 million, which has been recognized in these consolidated financial statements. The Group's effective income tax rate for 2008 was 24.2 percent without applying the effect of the reduction in the statutory tax rate.

Deferred income tax. Differences between IFRS and Russian statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes.

Deferred income tax balances are presented in the consolidated balance sheets as follows:

	At 31 December:	
	2008	2007
Long-term deferred income tax asset (other non-current assets)	328	532
Long-term deferred income tax liability	(6,720)	(8,083)
Net deferred income tax liability	**(6,392)**	**(7,551)**

Deferred income tax assets expected to be realized within twelve months of 31 December 2008 and 2007 were RR 81 million and RR 608 million, respectively. Deferred tax liabilities expected to be reversed within twelve months of 31 December 2008 and 2007 were RR 86 million and RR 348 million, respectively.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

21 INCOME TAX (CONTINUED)

Movements in deferred income tax assets and liabilities during the years ended 31 December 2008 and 2007 are as follows:

	At 31 December 2008	Reclassification to the (assets) liabilities classified as held for sale	Statement of Income effect	At 31 December 2007	Statement of Income effect	At 31 December 2006
Liabilities						
Property, plant and equipment	(7,473)	70	1,177	(8,720)	226	(8,946)
Inventories	(56)	7	(20)	(43)	(3)	(40)
Other current assets	(10)	-	302	(312)	17	(329)
Trade payables and accrued liabilities	(25)	-	(22)	(3)	13	(16)
Total deferred income tax liabilities	(7,564)	77	1,437	(9,078)	253	(9,331)
Assets						
Inventories	430	(19)	(112)	561	170	391
Trade and other receivables	45	-	21	24	1	23
Trade payables and accrued liabilities	389	(93)	(103)	585	69	516
Tax losses carried forward	226	(11)	(82)	319	81	238
Other	82	(25)	69	38	(34)	72
Total deferred income tax assets	1,172	(148)	(207)	1,527	287	1,240
Net deferred income tax liabilities	**(6,392)**	**(71)**	**1,230**	**(7,551)**	**540**	**(8,091)**

At 31 December 2008, the Group had recognized deferred income tax assets of RR 226 million (31 December 2007: RR 319 million) in respect of unused tax loss carry forwards of RR 1,130 million (31 December 2007: RR 1,329 million). Tax losses can be carried forward for relief against taxable profits for 10 years after they are incurred, subject to certain limitations. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments including expectations regarding the Group’s ability to generate sufficient future taxable income and the projected time period over which deferred tax benefits will be realized.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 ASSETS HELD FOR SALE

The assets and liabilities related to OOO "Purneft", a Group's wholly owned subsidiary, engaged primarily in crude oil production at the Ust-Purpeyskoye field, have been reported as held for sale following the decision of management in December 2008 to dispose the subsidiary. The entity is included within "exploration and production" in the Group's segment information. The asset has not been disposed as of the date of these financial statements; however, management believes that this transaction will be completed during 2009. Further production from this field was considered economically not viable for the Group.

Non-current assets classified as held for sale are stated at the lower of their carrying amount and fair value less costs to sell. No impairment of the assets was necessary as a result of the decision to sell this subsidiary.

Below is a breakdown of major classes of assets and liabilities for assets classified as held for sale:

	At 31 December 2008
Property, plant and equipment	696
Deferred tax assets	71
Inventory	34
Other assets	100
Total assets classified as held for sale	**901**
Asset retirement obligations	321
Other liabilities	14
Total liabilities associated with assets held for sale	**335**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS

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

	Loans and receivables	
Financial assets	**At 31 December:**	
	2008	**2007**
Non-current		
Long-term loans receivable	413	412
Trade and other receivables	323	269
Long-term deposits and letters of credit	52	175
Current		
Short-term loans receivable	3	36
Trade and other receivables	2,485	3,267
Short-term bank deposits	5	-
Cash and cash equivalents	10,992	3,982
Total carrying amount	**14,273**	**8,141**

	Measured at amortized cost	
Financial liabilities	**At 31 December:**	
	2008	**2007**
Non-current		
Long-term debt	19,935	42
Current		
Current portion of long-term debt	3,403	282
Short-term debt	2,939	6,278
Trade and other payables	4,405	1,711
Total carrying amount	**30,682**	**8,313**

Financial risk management objectives and policies. In the ordinary course of business, the Group is exposed to market risks from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on the degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial results. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position.

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

Market risk. Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Group's financial results or the value of its holdings of financial instruments. The primary objective of mitigating these market risks is to manage and control market risk exposures, while optimizing the return on risk.

The Group is exposed to market price movements relating to changes in commodity prices such as crude oil, gas condensate, liquefied petroleum products and natural gas (commodity price risk), foreign currency exchange rates, interest rates, equity prices and other indices that could adversely affect the value of the Group's financial assets, liabilities or expected future cash flows.

(a) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to the US dollar and the Euro. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble or the US dollar. Foreign currency derivative instruments may be utilized to manage the risk exposures associated with fluctuations on certain firm commitments for sales and purchases, debt instruments and other transactions that are denominated in currencies other than the Russian rouble, and certain non-Russian rouble assets and liabilities.

The carrying amounts of the Group's financial instruments are denominated in the following currencies:

At 31 December 2008	Russian rouble	US dollar	Euro	Other	Total
Financial assets					
Non-current					
Long-term loans receivable	413	-	-	-	413
Trade and other receivables	323	-	-	-	323
Long-term deposits and letters of credit	49	1	-	2	52
Current					
Short-term loans receivable	3	-	-	-	3
Trade and other receivables	1,860	602	-	23	2,485
Short-term bank deposits	-	-	5	-	5
Cash and cash equivalents	3,748	7,162	74	8	10,992
Financial liabilities					
Non-current					
Long-term debt	-	(19,935)	-	-	(19,935)
Current					
Current portion of long-term debt	-	(3,358)	(45)	-	(3,403)
Short-term debt	-	(2,939)	-	-	(2,939)
Trade and other payables	(4,162)	(152)	(87)	(4)	(4,405)
Net exposure at 31 December 2008	**2,234**	**(18,619)**	**(53)**	**29**	**(16,409)**

At 31 December 2007	Russian rouble	US dollar	Euro	Other	Total
Financial assets					
Non-current					
Long-term loans receivable	412	-	-	-	412
Trade and other receivables	269	-	-	-	269
Long-term deposits and letters of credit	169	-	6	-	175
Current					
Short-term loans receivable	36	-	-	-	36
Trade and other receivables	1,913	1,350	-	4	3,267
Cash and cash equivalents	3,763	189	7	23	3,982
Financial liabilities					
Non-current					
Long-term debt	-	(4)	(38)	-	(42)
Current					
Current portion of long-term debt	-	(50)	(232)	-	(282)
Short-term debt	-	(6,278)	-		(6,278)
Trade and other payables	(1,657)	(31)	(16)	(7)	(1,711)
Net exposure at 31 December 2007	**4,905**	**(4,824)**	**(273)**	**20**	**(172)**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The Group has chosen to provide information about market risk and potential exposure to hypothetical loss from its use of financial instruments through sensitivity analysis disclosures in accordance with IFRS requirements.

The sensitivity analysis depicted in the table below reflects the hypothetical loss that would occur assuming a 30 percent change in exchange rates and no changes in the portfolio of instruments and other variables at 31 December 2008 and 2007, respectively.

		At 31 December:	
Effect on pre-tax profit	**Increase in exchange rate**	**2008**	**2007**
RUR / USD	30%	(5,586)	(1,446)
RUR / EUR	30%	(16)	(81)

The effect of a corresponding 30 percent decrease in exchange rate is approximately equal and opposite.

(b) Commodity price risk

The Group's overall commercial trading strategy in natural gas, stable gas condensate and crude oil and related products is centrally managed. Changes in commodity prices could negatively or positively affect the Group's results of operations. The Group manages the exposure to commodity price risk by optimizing its core activities to achieve stable price margins.

Natural gas. As an independent natural gas producer, the Group is not subject to the Russian Government's regulation of natural gas prices. Nevertheless, the Group's prices are strongly influenced by the prices regulated by the Federal Tariffs Service (FTS), a governmental agency. In November 2006, the FTS approved and published a plan to liberalize the price of natural gas sold on the Russian domestic market by the year 2011. Effective from 1 January 2008, the FTS increased the regulated price for 2008 by 25 percent. The FTS also announced a further increase of 5 percent in the regulated price effective 1 January 2009 for the first quarter 2009. As part of the program, the FTS announced its plans to further increase the regulated price at the beginning of the each remaining quarter throughout 2009 by 7 percent, 7 percent and 6.2 percent, respectively. Management believes it has limited downside commodity price risk for natural gas and does not use commodity derivative instruments for trading purposes. However, to effectively manage the margins achieved through its natural gas trading activities, management has established targets for volumes sold to wholesale traders, end-customers and the natural gas exchange.

Liquid hydrocarbons. The Group sells all its crude oil and related products and gas condensate under spot contracts. Gas condensate volumes sold to the US and European markets are based on benchmark reference crude oil prices of WTI and Brent dated, respectively, plus a margin or discount, depending on current market situation. Crude oil sold internationally are based on benchmark reference crude oil prices of Brent dated, plus a discount and on a transaction-by-transaction basis for volumes sold domestically. As a result, the Group's revenues from the sales of liquid hydrocarbons are subject to commodity price volatility based on fluctuations or changes in the crude oil benchmark reference prices. The Group did not use commodity derivative instruments for trading purposes to mitigate price volatility as at 31 December 2008 or during 2008.

(c) Cash flow and fair value interest rate risk

The Group is subject to interest rate risk on financial liabilities with variable interest rates. To mitigate this risk, the Group's treasury function performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In cases where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favorable interest rate terms.

Changes in interest rates impact primarily debt by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new debts management uses its judgment to decide whether it believes that a fixed or variable rate would be more favorable over the expected period until maturity.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The interest rate profile of the Group's interest-bearing financial instruments at the reporting dates were as follows:

	At 31 December:	
	2008	**2007**
At variable rate	23,293	6,278
At fixed rate	2,984	324
Total debt	**26,277**	**6,602**

The Group centralizes the cash requirements and surpluses of controlled subsidiaries and the majority of their external financing requirements, and applies, on its consolidated net debt position, a funding policy to optimize its financing costs and manage the impact of interest-rate changes on its financial results in line with market conditions. In this way, the Group is able to ensure that the balance between the floating rate portion of its debt and its cash surpluses has a low level of exposure to any change in interest rates over the short term. This policy makes it possible to significantly limit the Group's sensitivity to interest-rate volatility.

The Group's financial results are sensitive to changes in interest rates on the floating rate portion of the Group's debt portfolio. If the interest rates applicable to floating rate debt were to increase by 100 basis points at the reporting dates, assuming all other variables remain constant, it is estimated that the Group's profit before taxation for 2008 would decrease by the amounts shown below.

The Group is examining various ways to manage its cash flow interest rate risk by using floating to fixed interest rate. No swaps or other similar instruments were in place as of 31 December 2008 or during 2008.

	At 31 December:	
Effect on pre-tax profit	**2008**	**2007**
Increase by 100 basis points	233	63

The effect of a corresponding 100 basis points decrease in exchange rate is approximately equal and opposite.

Credit risk. Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if a counterparty defaults on its contractual obligations.

Credit risk is managed on a Group level and arises from cash and cash equivalents, including short-term deposits with banks, as well as credit exposures to customers, including outstanding trade receivables and committed transactions. Cash and cash equivalents are deposited only with banks that are considered by the Group at the time of deposit to minimal risk of default.

The Group's trade and other receivables consist of a large number of customers, spread across diverse industries and geographical areas. Most of the Group's international liquid sales are made to customers with independent external ratings. All domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis. The Group also requires 100 percent prepayments from small customers for natural gas deliveries and partial advances from others. Although the Group does not require collateral in respect of trade and other receivables, it has developed standard credit payment terms and constantly monitors the status of trade receivables and the creditworthiness of the customers.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The table below highlights the Group's trade and other receivables to published credit ratings of its counterparties.

	At 31 December:	
Moody's and/or Fitch	**2008**	**2007**
Investment grade rating	1,088	499
Non-investment grade rating	51	1,071
No external rating	1,346	1,697
Total trade and other receivables	**2,485**	**3,267**

The table below highlights the Group's cash balances to published credit ratings of its banks.

	At 31 December:	
Moody's and/or Fitch	**2008**	**2007**
Investment grade rating	9,985	2,528
Non-investment grade rating	875	1,303
No external rating	132	151
Total cash and cash equivalents	**10,992**	**3,982**

Investment grade ratings classification referred to as Aaa to Baa3 for Moody's and as AAA to BBB- for Fitch, respectively.

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 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. In managing its liquidity risk, the Group maintains adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows and matches the maturity profiles of financial assets and liabilities.

The Group prepares various financial plans (monthly, quarterly and annually) which ensures that the Group has sufficient cash on demand to meet expected operational expenses, financial obligations and investing activities for a period of 30 days or more. The Group has entered into a number of short-term credit facilities. Such credit lines and overdraft facilities can be drawn down to meet short-term financing needs. To fund cash requirements of a more permanent nature, the Group will normally raise long-term debt in available international and domestic markets.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

All of the Group's financial liabilities represent non-derivative financial instruments. The following tables summarize the maturity profile of the Group's financial liabilities based on contractual undiscounted payments, including interest payments:

At 31 December 2008	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Debt at fixed rate				
Principal	2,984	-	-	2,984
Interest	2	-	-	2
Debt at variable rate				
Principal	3,358	13,242	6,693	23,293
Interest	785	477	61	1,323
Trade and other payables	4,405	-	-	4,405
Total financial liabilities	**11,534**	**13,719**	**6,754**	**32,007**

At 31 December 2007	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Debt at fixed rate				
Principal	282	42	-	324
Interest	41	2	-	43
Debt at variable rate				
Principal	6,278	-	-	6,278
Interest	157	-	-	157
Trade and other payables	1,711	-	-	1,711
Total financial liabilities	**8,469**	**44**	**-**	**8,513**

Capital management. The primary objectives of the Group's capital management policy is to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain investor, market and creditor confidence to support its business activities.

The Group presently has an investment grade credit rating of Baa3 (stable outlook) by Moody's Investor Services and is rated BB+ (stable) by Standard & Poors. To maintain its credit rating, the Group has established certain financial targets and coverage ratios that it monitors on a quarterly and annual basis.

The Group manages its liquidity on a corporate-wide basis to ensure adequate funding to sufficiently meet group operational requirements. All external debts are centralized at the Parent level, and all financing to Group entities is facilitated through inter-company loan arrangements.

The Group has a stated dividend policy that distributes at least 30 percent of its parent company non-consolidated statutory net profit determined according to Russian accounting standards. However, the dividend for a specific year is determined after taking into consideration future earnings, capital expenditure requirements, future business opportunities and the Group current financial position. Dividends are recommended by the Board of Directors and approved by the NOVATEK's shareholders.

The Group defines the term "capital" as equity attributable to OAO NOVATEK shareholders minus net debt (total debt less cash and cash equivalents). There were no changes to the Group's approach to capital management during the year.

24 CONTINGENCIES AND COMMITMENTS

Operating environment. The Russian Federation continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is in practice not convertible in most countries outside of the Russian Federation, and relatively high inflation. The tax, currency and customs legislation is subject to varying interpretations, frequent changes and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

The Group’s business operations are primarily located in the Russian Federation and are thus exposed to the economic and financial markets of the country.

Recent volatility in global and Russian financial markets. The global liquidity crisis which commenced in the middle of 2007 has resulted in numerous stresses to the capital market system, which among other things, has resulted in a lower level of capital market raising activities, a lower level of liquidity across the international and Russian banking sector, and higher interbank lending rates. The present uncertainties in the global financial market have also led to a series of bank failures and bank rescue measures in the United States, Western Europe and in the Russian Federation amongst other countries. Moreover, the US Federal Reserve and Treasury as well as primary Central Banks around the world, including the Central Bank of the Russian Federation have initiated efforts to stimulate the global financial markets. The full extent of the impact of the ongoing financial and economic crisis is difficult to predict or anticipate at this stage of the economic business cycle.

Under the present market situation, the Group’s ability to obtain new borrowings and/or re-finance its existing borrowings at terms and conditions similar to those applied to earlier transactions may be affected. Moreover, the amount of financing available on the market has been significantly reduced since the onset of the economic and financial crisis (often referred to as the “credit crunch”). The Group’s debtors may also be affected by the lower liquidity situation which could negatively impact their ability to repay their amounts owed. Deteriorating operating and financial conditions of debtors may also have an impact on Management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, Management has reflected revised estimates of expected future cash flows in its impairment assessments.

Management believes it is taking all the necessary measures to support the sustainability and growth of the Group’s business in the current market circumstances. The effectiveness of the measures are in the view of management, significantly enabled by the effectiveness of the financial policies and treasury management practices that the Group has employed in recent years. Specifically, the Group has maintained adequate cash and cash equivalent balance, used diversified funding sources, limited bank concentration of liquid funds, required prepayments for hydrocarbon sales and had adhered to strict liquidity and financial leverage ratios.

Despite these efforts, management acknowledges that there are present uncertainties over the direction and duration of the current market volatility and, consequently, is unable to predict the impact of any further deterioration in the global and Russian financial markets.

Impairment analysis. Management considered the global economic and liquidity crisis and the decline in commodity prices, particularly, crude oil, stable gas condensate, liquefied petroleum gas, and oil products, as indicators of possible impairment and, in accordance with IAS 36, *Impairment of Assets*, has performed an impairment analysis in respect of all its assets.

The impairment assessments performed did not result in any impairment of the Group’s assets as of and for the year ended 31 December 2008.

Commitments. At 31 December 2008, the Group had contractual capital expenditures commitments aggregating approximately RR 16,991 million (at 31 December 2007: RR 21,744 million) for phase two development of the Yurkharovskoye field (through 2011), development of the East-Tarkosalinskoye and Khancheyskoye fields (through 2009 and 2010, respectively) and for continuation of phase two construction of the Purovsky Gas Condensate Plant (through 2011) in accordance with duly signed agreements. In addition, the Group has minimum capital commitments for exploration activities under the El Arish Concession Agreement (see Note 5).

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

24 CONTINGENCIES AND COMMITMENTS (CONTINUED)

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

As at 31 December 2008, management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued.

Mineral licenses. The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its mineral licenses. Management cooperates with governmental authorities to agree on remedial actions necessary to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties or license limitation, suspension or revocation. The Group's management believes any issues of non-compliance will be resolved through negotiations or corrective actions without any material adverse effect on the Group's financial position, statement of income or of cash flows.

The Group's oil and gas fields and license areas are situated on land located in the Yamal-Nenets Autonomous Region. Licenses are issued by the Federal Agency for the Use of Natural Resources under the Ministry of Natural Resources and the Group pays unified natural resources production tax to produce oil and gas from these fields and contributions for exploration of license areas. The principal licenses of the Group and their expiry dates are:

Field	License holder	License expiry date
Yurkharovskoye	OOO NOVATEK-YURKHAROVNEFTEGAS	2034
East-Tarkosalinskoye	OOO NOVATEK-TARKOSALENEFTEGAS	2043
Khancheyskoye	OOO NOVATEK-TARKOSALENEFTEGAS	2019
Sterkhovoye (within the Olympinsky license area)	OOO PurNovaGas	2026
Termokarstovoye	OOO Terneftegas	2021

Management believes the Group has the right to extend its licenses beyond the initial expiration date under the existing legislation and intends to exercise this right on all of its fields. In December 2007, the Group was successful in extending the license for the East-Tarkosalinskoye field from 2018 to 2043. The Group has plans to submit the appropriate application with the respective Agency for the Use of Natural Resources for the extension of the terms of the licenses for Khancheyskoye field.

Environmental liabilities. The Group and its predecessor entities have operated in the oil and gas industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations and, as obligations are determined, they are recognized as an expense immediately if no future benefit is discernible. Potential liabilities which might arise as a result of a change in interpretation of existing regulations, civil litigation or changes in legislation cannot be estimated. Under existing legislation, management believes that there are no probable liabilities which will have a material adverse effect on the Group's financial position, statement of income or of cash flows.

Legal contingencies. The Group is subject of, or party to a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Group and which have not been accrued or disclosed in the consolidated financial statements.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

25 PRINCIPAL SUBSIDIARIES AND ASSOCIATES

The principal subsidiaries and associates of the Group and respective ownership in the ordinary share capital at 31 December 2008 are set out below.

	Ownership interest at 31 December 2008	Country of incorporation	Principal activities
Subsidiaries			
OOO NOVATEK-YURKHAROVNEFTEGAS	100.0%	Russia	Exploration and production
OOO NOVATEK-TARKOSALENEFTEGAS	100.0%	Russia	Exploration and production
OOO Terneftegaz	100.0%	Russia	Exploration and production
OOO NOVATEK-PUROVSKY ZPK	100.0%	Russia	Gas Condensate Plant
OOO NOVATEK-TRANSERVICE	100.0%	Russia	Transportation services
OOO NOVASIB	100.0%	Russia	Exploration activities
OOO NOVATEK-AZK	100.0%	Russia	Wholesale and retail trading
OOO NOVATEK Severo-Zapad	100.0%	Russia	Trading and marketing
OOO NOVATEK-Polymer	100.0%	Russia	Production of polymer and insulation tape
OOO PurNovaGaz	100.0%	Russia	Exploration and production
OOO Purneft	100.0%	Russia	Exploration and production
OOO NOVATEK-Ust-Luga	100.0%	Russia	Construction of sea terminal
OOO YARGEO	51.0%	Russia	Exploration activities
Novatek Overseas AG	100.0%	Switzerland	Holding company
Runitek GmbH	100.0%	Switzerland	Trading and marketing
Novatek Overseas Exploration & Production GmbH	100.0%	Switzerland (branch in Egypt)	Exploration activities
Novatek Equity (Cyprus) Limited	100.0%	Cyprus	Purchase of the Group's shares
Associates			
OOO Oiltechproduct-Invest	25.0%	Russia	Exploration activities
OOO Petra Invest-M	25.0%	Russia	Exploration activities
OOO Tailiksneftegas	25.0%	Russia	Exploration activities

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

26 RELATED PARTY TRANSACTIONS

For the purposes of these consolidated financial statements, parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial and operational decisions. Management has used reasonable judgments in considering each possible related party relationship with attention directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be affected on the same terms, conditions and amounts as transactions between unrelated parties. The Group enters into transactions with related parties based on market or regulated prices.

The Group has re-assessed its approach in determining entities subject to the definition of a related party. Specifically, the subsidiaries of all entities considered to be a related party are also assumed to be related to the Group.

All natural gas producers and wholesalers operating in Russia transport their natural gas volumes through the Unified Gas Supply System (UGSS), which is owned and operated by OAO Gazprom, a State monopoly. As an independent natural gas producer, the Group utilizes the UGSS to transport natural gas to end-consumers at the tariff established by the Federal Tariff Service.

Transactions with OAO Gazprom, a shareholder of significant influence, from October 2006, and its subsidiaries are presented below.

	As at and for the year ended 31 December	
OAO Gazprom and its subsidiaries	2008	2007
Transactions		
Oil and gas sales	6,144	4,099
Purchases of natural gas and liquid hydrocarbons	1,549	1,446
Natural gas transportation to customers	11,544	9,140
Processing fees	342	213
Other operating expenses	33	27
Other income (loss)	221	(39)
Other revenue	3	-
Balances		
Cash	-	13
Trade and other receivables	232	413
Prepayments and other current assets	1,065	1,517
Trade and other payables	276	261

	As at and for the year ended 31 December	
Related parties – associates	2008	2007
Transactions		
Other revenues	805	22
Interest income	51	16
Balances		
Long-term loans receivable	410	409
Interest on long-term loans receivable	33	16
Trade payables and accrued liabilities	489	324

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

26 RELATED PARTY TRANSACTIONS (CONTINUED)

Related parties – parties under significant influence of key management personnel	**As at and for the year ended 31 December 2008**
Transactions	
Purchases of construction services (capitalized within property, plant and equipment)	6,980
Oil products sales	245
Polymer product sales	3
Other revenues	38
Finance income (expense)	42
Balances	
Prepayments and advances (for construction)	-
Prepayments and other current assets	21
Cash and cash equivalents	337
Trade payables and accrued liabilities	55

Transactions with related parties under significant influence of key management personnel occurred starting from January 2008.

Key management compensation. During 2008 and 2007, the Group paid to the key management personnel (the members of the Board of Directors and the Management Board, some of whom have also direct and indirect interests in the Group) short-term compensation, including salary, bonuses, excluding dividends the total of RR 817 million and RR 403 million in cash, respectively. Such amounts include personal income tax and are net of unified social tax. The remuneration for serving on the Board of Directors is subject to approval by the General Meeting of Shareholders. Key management personnel also receive certain short-term benefits related to healthcare. In addition, during 2008 and 2007, RR 176 million for each year, were recognized as part of the share-based compensation program (Note 15) and included in general and administrative expense.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

27 SEGMENT INFORMATION

The Group's primary format for reporting segment information is business segments and the secondary format is geographical segments.

Business Segments. The Group evaluates performance and makes investment and strategic decisions based upon a review of profitability for the Group as a whole. However, the Group's activities are considered by management to comprise the following business segments:

- Exploration and production – acquisitions, exploration, development, production, processing, marketing and transportation of natural gas, gas condensate, crude oil and related products;
- Corporate and other – other activities, including head-office, certain general and administrative services, polymer and tape insulation.

Segment information as at 31 December 2008 and 2007 is as follows:

At 31 December 2008	Exploration and production	Corporate and other	Total
Segment assets	117,592	7,212	124,804
Investment in associates	1,416	-	1,416
Unallocated assets:			
Current and deferred income tax			2,189
Long-term loans receivable			413
Trade and other receivables			2
Other non-current assets			52
Prepayments and other current assets			10
Cash and cash equivalents			11,021
Total assets			**139,907**
Segment liabilities	8,924	1,019	9,943
Unallocated liabilities:			
Current and deferred income tax			6,955
Long-term and short-term debt			26,277
Trade payable and accrued liabilities			92
Total liabilities			**43,267**

At 31 December 2007	Exploration and production	Corporate and other	Total
Segment assets	92,965	4,344	97,309
Investment in associates	1,125	-	1,125
Unallocated assets:			
Current and deferred income tax			868
Long-term loans receivable			412
Trade and other receivables			3
Other non-current assets			191
Prepayments and other current assets			85
Cash and cash equivalents			3,982
Total assets			**103,975**
Segment liabilities	6,728	94	6,822
Unallocated liabilities:			
Current and deferred income tax			8,728
Long-term and short-term debt			6,602
Trade payable and accrued liabilities			11
Total liabilities			**22,163**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

27 SEGMENT INFORMATION (CONTINUED)

Segment information for the years ended 31 December 2008 and 2007 is as follows:

Year ended 31 December 2008	Exploration and production	Corporate and other	Total
Segment revenues			
External revenues and other income	76,633	2,395	79,028
Inter-segment sales	13	134	147
Total segment revenues	**76,646**	**2,529**	**79,175**
Segment expenses			
External expenses	(41,228)	(5,688)	(46,916)
Inter-segment expenses	(19)	(13)	(32)
Total segment expenses	**(41,247)**	**(5,701)**	**(46,948)**
Segment result	**35,399**	**(3,172)**	**32,227**
Unallocated gains on sales of investments			8
Unrealized margin in segment assets			(115)
Profit from operations			**32,120**
Finance income (expense), net			(3,384)
Share of profit (loss) of associates, net of income tax			(147)
Profit before income tax			**28,589**
Income tax expense			(5,662)
Profit for the year			**22,927**
Capital expenditures	30,145	1,665	31,810
Depreciation, depletion and amortization	(4,412)	(169)	(4,581)
Impairment charges, net	(60)	(45)	(105)

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

27 SEGMENT INFORMATION (CONTINUED)

Year ended 31 December 2007	Exploration and production	Corporate and other	Total
Segment revenues			
External revenues and other income	60,527	1,858	62,385
Inter-segment sales	11	51	62
Total segment revenues	**60,538**	**1,909**	**62,447**
Segment expenses			
External expenses	(32,559)	(4,556)	(37,115)
Inter-segment expenses	(51)	(11)	(62)
Total segment expenses	**(32,610)**	**(4,567)**	**(37,177)**
Segment result	**27,928**	**(2,658)**	**25,270**
Unallocated gains on sales of investments			95
Profit from operations			**25,365**
Finance income (expense), net			124
Profit before income tax			**25,489**
Income tax expense			(6,761)
Profit for the year			**18,728**
Acquisition of subsidiaries	-	254	254
Capital expenditures	18,382	1,084	19,466
Depreciation, depletion and amortization	(3,516)	(218)	(3,734)
Impairment charges, net	(30)	(123)	(153)

Capital expenditures include purchases of property, plant, and equipment. Charges for impairment above include impairment provisions for accounts and loans receivable and inventories.

The inter-segment sales mainly consist of:

- Exploration and production – sale of gas and oil products to the other segments, for which prices are based on market prices; and
- Corporate and other – rendering rent services, transportation sales and sales of polymer to the other segments, for which prices are based on market prices.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

27 SEGMENT INFORMATION (CONTINUED)

Geographical segments. The Group's two business segments operate in three major geographical areas of the world. In the Russian Federation, its home country, the Group is mainly engaged in the exploration, development, extraction and sales of natural gas, crude oil, gas condensate and related products and sales of polymer and insulation tape. Activities outside the Russian Federation are conducted in the United States (sales of stable gas condensate), in Europe (sales of stable gas condensate, liquefied petroleum gas and crude oil) and other areas (sales of liquefied petroleum gas and sales of polymer and insulation tape). Information for the main geographical segments of the Group is set out below.

At 31 December 2008 and for the year then ended	Russia	Europe	USA	Other	Total
Total segment assets	123,873	74	840	17	124,804
Investment in associates	1,416				1,416
External revenues and other income	55,540	2,754	19,924	810	79,028
Unallocated loss on sales of investments					8
Total revenues and other income as per consolidated statement of income					**79,036**
Capital expenditures	31,729	5	-	76	31,810

At 31 December 2007 and for the year then ended	Russia	Europe	USA	Other	Total
Total segment assets	94,353	1,416	1,540	-	97,309
Investment in associates	1,125	-	-	-	1,125
External revenues and other income	42,250	5,693	13,377	1,065	62,385
Unallocated gain on sales of investments					95
Total revenues and other income as per consolidated statement of income					**62,480**
Acquisition of subsidiaries	254	-	-	-	254
Capital expenditures	19,440	-	-	26	19,466

Segment revenue from external customers is based on the geographical location of customers although all revenues are generated by assets in the Russian Federation. Segment assets are based on the geographical location of the assets. Capital expenditure is based on the geographical location of the Group's assets.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

28 EXPLORATION FOR AND EVALUATION OF MINERAL RESOURCES

The amounts included within the consolidated financial statements associated with the exploration for and evaluation of mineral resources for the years ended 31 December 2008 and 2007 is as follows:

	At 31 December and for the year then ended:	
	2008	**2007**
Assets	4,995	3,881
Liabilities	(22)	(12)
Expenses	(1,117)	(486)
Cash flows used for operating activities	(1,005)	(449)
Cash flows used for investing activities	(1,081)	(2,463)

Assets include uncompleted cost of drilling and equipping of exploratory wells on unproved reserves and participation payment for the rights to purchase oil and gas exploration and production licenses. Liabilities include unpaid obligations under the contracts for drilling and equipping exploratory wells. Exploration costs include geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity. Cash flows used for operating activities and for investing activities include cash paid for geological and geophysical studies performed and cash paid for drilling and equipping exploratory wells and acquiring the right for mineral recourses, respectively.

29 SUBSEQUENT EVENTS

On 29 January 2009, the Government of the Russian Federation announced the reduction of export duties on the shipment of liquefied petroleum gas to zero effective 1 January 2009. Subsequently, the government extended the zero tax rate through March 2009. The Group expects further prolongation of the zero tax rate on liquefied petroleum gas export deliveries for the most part of 2009.

On 20 February 2009, the FTS announced a planned reduction until the end of 2009 in the rail road transportation tariffs related to export deliveries of liquefied petroleum gas and stable gas condensate shipped from the Limbey station, located in close proximity to our Purovsky Plant. The planned reduction applies the following percentages to existing rail road tariffs:

- 35 percent – for liquefied petroleum gas after the first 90 thousand tons transported and if the distance is more than 3,500 kilometers;
- 72 percent – for stable gas condensate if the distance is more than 4,000 kilometers.

The reduction in tariffs will come into force after formal notification in accordance with Russian legislation.

The Group sells substantially all its stable gas condensate and a portion of its liquefied petroleum gas sales volumes on the international markets and anticipates that the reduction of the export duties and discounts on the transportation tariffs will enhance netback margin.

30 NEW ACCOUNTING PRONOUNCEMENTS

Beginning 1 January 2008, the Group has adopted the following interpretations:

- IFRIC 11, *IFRS 2 – Group and Treasury Share Transactions* (effective for annual periods beginning on or after 1 March 2007). IFRIC 11 addresses accounting for certain transactions an entity may enter into to satisfy rights to equity instruments previously granted to employees. Additionally it provides guidance on accounting for rights to equity instruments of a parent company granted for employees of a subsidiary in the subsidiary's separate financial statements;

- IFRIC 12, *Service Concession Arrangem*ents (effective for annual periods beginning on or after 1 January 2008). IFRIC 12 gives guidance on the accounting by operators for public-to-private service concession arrangements;

- IFRIC 13, *Customer Loyalty Programmes* (effective for annual periods beginning on or after 1 July 2008). IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values;

- IFRIC 14, IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* (effective for annual periods beginning on or after 1 January 2008). IFRIC 14 addresses the measurement of defined benefit plan assets and accounting for an obligation under a minimum funding requirement; and

- IFRIC 16, *Hedges of a Net Investment in a Foreign Operation* (effective for annual periods beginning on or after 1 October 2008). The interpretation explains which currency risk exposures are eligible for hedge accounting and states that translation from the functional currency to the presentation currency does not create an exposure to which hedge accounting could be applied. The IFRIC allows the hedging instrument to be held by any entity or entities within a group except the foreign operation that itself is being hedged. The interpretation also clarifies how the gain or loss recycled from the currency translation reserve to profit or loss is calculated on disposal of the hedged foreign operation. The Group will apply IAS 39 to discontinue hedge accounting prospectively when their hedges do not meet the criteria for hedge accounting in IFRIC 16.

The adoption of these interpretations, if applicable, had an insignificant effect on the Group's consolidated financial statements.

Recently, the International Accounting Standards Board published the following new standards and interpretations which have not been early adopted by the Group:

- IAS 1, *Presentation of Financial Statements* (revised September 2007); effective for annual periods beginning on or after 1 January 2009). The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which will also include all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities will be allowed to present two statements: a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The Group expects the revised IAS 1 to affect the presentation of its financial statements but to have no impact on the recognition or measurement of specific transactions and balances;

- IFRS 8, *Operating Segments*, (effective for annual periods beginning on or after 1 January 2009). IFRS 8 requires an entity to report financial and descriptive information about its operating segments, with segment information presented on a similar basis to that used for internal reporting purposes. Management is currently assessing what impact the standard will have on segment disclosures in the Group's financial statements;

30 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

- Amendment to IAS 32 and IAS 1, *Puttable financial instruments and obligations arising on liquidation* (effective from 1 January 2009). The amendment requires classification as equity of some financial instruments that meet the definition of a financial liability;

- IFRS 3, *Business Combinations* (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquirer's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, goodwill will be measured as the difference at acquisition date between the fair value of any investment in the business held before the acquisition, the consideration transferred and the net assets acquired. Acquisition-related costs will be accounted for separately from the business combination and therefore recognized as expenses rather than included in goodwill. An acquirer will have to recognize at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognized in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone;

- IAS 27, *Consolidated and Separate Financial Statements* (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value;

- Amendment to IFRS 2, *Share-based Payment* (issued in January 2008; effective for annual periods beginning on or after 1 January 2009). The amendment clarifies that only service conditions and performance conditions are vesting conditions. Other features of a share-based payment are not vesting conditions. The amendment specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment;

- IAS 23 (Revised), *Recognition of Borrowing Costs*. (revised March 2007). The main change to IAS 23 is the removal of the option of immediately recognizing as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. An entity is, therefore, required to capitalize such borrowing costs as part of the cost of the asset. The revised standard applies prospectively to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after 1 January 2009;

30 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

- *Improvements to International Financial Reporting Standards* (issued in May 2008). In 2007, the International Accounting Standards Board decided to initiate an annual improvements project as a method of making necessary, but non-urgent, amendments to IFRS. The amendments issued in May 2008 consist of a mixture of substantive changes, clarifications, and changes in terminology in various standards. The substantive changes relate to the following areas: classification as held for sale under IFRS 5 in case of a loss of control over a subsidiary; possibility of presentation of financial instruments held for trading as non-current under IAS 1; accounting for sale of IAS 16 assets which were previously held for rental and classification of the related cash flows under IAS 7 as cash flows from operating activities; clarification of definition of a curtailment under IAS 19; accounting for below market interest rate government loans in accordance with IAS 20; making the definition of borrowing costs in IAS 23 consistent with the effective interest method; clarification of accounting for subsidiaries held for sale under IAS 27 and IFRS 5; reduction in the disclosure requirements relating to associates and joint ventures under IAS 28 and IAS 31; enhancement of disclosures required by IAS 36; clarification of accounting for advertising costs under IAS 38; amending the definition of the fair value through profit or loss category to be consistent with hedge accounting under IAS 39; introduction of accounting for investment properties under construction in accordance with IAS 40; and reduction in restrictions over manner of determining fair value of biological assets under IAS 41. Further amendments made to IAS 8, 10, 18, 20, 29, 34, 40, 41 and to IFRS 7 represent terminology or editorial changes only, which the IASB believes have no or minimal effect on accounting;

- Amendment to IFRS 1 and IAS 27, *Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate* (revised May 2008; effective for annual periods beginning on or after 1 January 2009). The amendment allows first-time adopters of IFRS to measure investments in subsidiaries, jointly controlled entities or associates at fair value or at previous GAAP carrying value as deemed cost in the separate financial statements. The amendment also requires distributions from pre-acquisition net assets of investees to be recognized in profit or loss rather than as a recovery of the investment;

- Amendment to IAS 39, *Financial Instruments: Recognition and Measurement.* Entities are required to apply the amendment retrospectively for annual periods beginning on or after 1 July 2009, with earlier application permitted. The amendment clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations;

- Amendments to IAS 39, *Financial Instruments: Recognition and Measurement*, and IFRS 7, Financial *Instruments: Disclosures*. The amendments allow entities the options (a) to reclassify a financial asset out of the held to trading category if, in rare circumstances, the asset is no longer held for the purpose of selling or repurchasing it in the near term; and (b) to reclassify an available-for-sale asset or an asset held for trading to the loans and receivables category, if the entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity (subject to the asset otherwise meeting the definition of loans and receivables). The amendments may be applied with retrospective effect from 1 July 2008 for any reclassifications made in the periods beginning before 1 November 2008; the reclassifications allowed by the amendments may not be applied before 1 July 2008. Any reclassification of a financial asset made in periods beginning on or after 1 November 2008 takes effect only from the date when the reclassification is made;

- IFRIC 15, *Agreements for the Construction of Real Estate* (effective for annual periods beginning on or after 1 January 2009). The interpretation applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors, and provides guidance for determining whether agreements for the construction of real estate are within the scope of IAS 11 or IAS 18. It also provides criteria for determining when entities should recognize revenue on such transactions.

- IFRIC 17, *Distribution of Non-Cash Assets to Owners* (effective for annual periods beginning on or after 1 July 2009). The amendment clarifies when and how distribution of non-cash assets as dividends to the owners should be recognized. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets will be recognized in profit or loss when the entity settles the dividend payable. IFRIC 17 is not relevant to the Group’s operations because it does not distribute non-cash assets to owners; and

30 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

- IFRIC 18, *Transfers of Assets from Customers* (effective for annual periods beginning on or after 1 July 2009). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers.

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

On 31 December 2008, the Securities and Exchange Commission (SEC) issued its final rule on the Modernization of Oil and Gas Reporting (the "Final Rule"), which revises the disclosures required by oil and gas companies. Although these disclosure rules are voluntarily applied, the Group will adopt the revisions noted in the Final Rule as part of its overall oil and gas industry disclosures. The Final Rule details changes to the disclosure requirements for company and reserve information. In addition to changing the definition and disclosure requirements for oil and gas reserves, the Final Rule changes the requirements for determining quantities of oil and gas reserves to allow companies to report both proved and probable reserves. The new rules represent the first significant revisions in oil and gas disclosures requirements in more than 25 years, and are scheduled to be applied for fiscal years ended 31 December 2009. The new oil and gas reserve disclosure rules are not permitted for early adoption.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). In the absence of specific IFRS guidance, the Group has reverted to other relevant disclosure standards, mainly US GAAP, that are consistent with norms established for the oil and gas industry. While not required under IFRS, this section provides unaudited supplemental information on oil and gas exploration and production activities but excludes disclosures regarding the standardized measures of discounted cash flows related to oil and gas activities.

The Group's exploration and production activities are presently mainly within the Russian Federation; therefore, all of the information provided in this section pertains to this country. The Group operates through various oil and gas production subsidiaries. The Group also has an interest in oil and gas companies that are accounted for under the equity method. These associates have no proved reserves and immaterial capitalized costs.

Oil and Gas Exploration and Development Costs

The following tables set forth information regarding oil and gas acquisition, exploration and development activities. The amounts reported as costs incurred include both capitalized costs and costs charged to expense during the years ended 31 December 2008 and 2007 (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2008	2007
Costs incurred in exploration and development activities		
Acquisition cost	-	2,835
Exploration costs	2,119	1,605
Development costs	29,063	16,077
Total costs incurred in exploration and development activities	**31,182**	**20,517**

	At 31 December:	
	2008	2007
Capitalized costs relating to oil and gas producing activities		
Wells and related equipment and facilities	73,514	60,674
Support equipment and facilities	20,820	9,824
Uncompleted wells, equipment and facilities	23,835	18,312
Total capitalized costs relating to oil and gas producing activities	118,169	88,810
Less: accumulated depreciation, depletion and amortization	(15,015)	(10,909)
Net capitalized costs relating to oil and gas producing activities	**103,154**	**77,901**

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Results of Operations for Oil and Gas Producing Activities

The Group's results of operations for oil and gas producing activities are shown below. The results of operations for oil and gas producing activities do not include general corporate overhead or its associated tax effects. Income tax is based on statutory rates. In the following table both transportation and processing costs are included in Revenues from oil and gas sales (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2008	2007
Revenues from oil and gas sales	76,076	60,406
Lifting costs	(3,581)	(3,072)
Transportation expenses	(16,013)	(13,138)
Taxes other than income tax	(7,062)	(6,222)
Depreciation, depletion and amortization	(4,234)	(3,446)
Exploration expenses	(1,117)	(486)
Total production costs	**(32,007)**	**(26,364)**
Purchases of natural gas, gas condensate and crude oil	(4,665)	(3,242)
Transportation expenses related to purchases of natural gas, gas condensate and crude oil	(2,114)	(1,269)
Results of operations for oil and gas producing activities before income tax	37,290	29,531
Less: related income tax expense	(8,950)	(7,087)
Results of operations for oil and gas producing activities	**28,340**	**22,444**

Proved Oil and Gas Reserves

The Group's oil and gas reserves estimation and reporting process involves an annual independent third party reserve appraisal as well as internal technical appraisals of reserves. The Group maintains its own internal reserve estimates that are calculated by technical staff working directly with the oil and gas properties. The Group's technical staff periodically updates reserve estimates during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The Group estimates its oil and gas reserves in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves. The oil and gas reserve estimates reported below are determined by the Group's independent petroleum reservoir engineers, DeGolyer and MacNaughton ("D&M"), for the Group's fields – Yurkharovskoye, East-Tarkosalinskoye, Khancheyskoye, Sterkhovoye, Termokarstovoye, Urengoyskoe and North Khancheyskoye. The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for the reserve determination. The Group's and D&M's technical staffs meet to review and discuss the information provided, and upon completion of this process, senior management reviews and approves the final reserve estimates issued by D&M.

The following reserve estimates were prepared using standard geological and engineering methods generally accepted by the petroleum industry. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history.

The following information presents the quantities of proved oil and gas reserves and changes thereto as at and for the years ended 31 December 2008 and 2007.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Extensions of production licenses are assumed to be at the discretion of the Group. Management believes that proved reserves should include quantities which are expected to be produced after the expiry dates of the Group’s production licenses. The Group’s licenses expire between 2018 and 2043, with the most significant license, Yurkharovskoye field and East-Tarkosalinskoye field, expiring in 2034 and 2043, respectively. Management believes that there is requisite legislation to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the license expiry dates.

The Group has disclosed information on proved oil and gas reserve quantities for periods up to and past the license expiry dates separately.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

Proved developed reserves are those reserves which are expected to be recovered through existing wells with existing equipment and operating methods. Undeveloped reserves are those reserves which are expected to be recovered as a result of future investments to drill new wells, to re-complete existing wells and/or install facilities to collect and deliver the production.

Net reserves exclude quantities due to others when produced.

The reserve quantities below include 100 percent of the net proved reserve quantities attributable to the Group’s consolidated subsidiaries. A portion of the Group’s total proved reserves are classified as either developed non-producing or undeveloped. Of the non-producing reserves, a portion represents existing wells which are to be returned to production at a future date.

For convenience, volumes are provided both in English and metric units.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of natural gas are presented below.

	Net proved reserves of natural gas recoverable up to license expiry dates		Net proved reserves of natural gas recoverable past license expiry dates		Total net proved reserves of natural gas	
	Billions of cubic feet	*Billions of cubic meters*	*Billions of cubic feet*	*Billions of cubic meters*	*Billions of cubic feet*	*Billions of cubic meters*
Reserves at 31 December 2006	**18,984**	**538**	**4,006**	**113**	**22,990**	**651**
Changes attributable to:						
Revisions of previous estimates	(3,668)	(105)	4,109	117	441	12
Extension of license	7,521	213	(7,521)	(213)	-	-
Extension and discoveries	446	13	-	-	446	13
Additions	96	3	91	2	187	5
Production	(997)	(28)	-	-	(997)	(28)
Reserves at 31 December 2007	**22,382**	**634**	**685**	**19**	**23,067**	**653**
Changes attributable to:						
Revisions of previous estimates	211	5	82	3	293	8
Extension and discoveries	2,070	59	-	-	2,070	59
Production	(1,073)	(30)	-	-	(1,073)	(30)
Reserves at 31 December 2008	**23,590**	**668**	**767**	**22**	**24,357**	**690**
Net proved developed reserves (included above)						
At 31 December 2006	14,911	422	3,134	89	18,045	511
At 31 December 2007	19,290	546	106	3	19,396	549
At 31 December 2008	19,014	538	95	3	19,109	541

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of crude oil, gas condensate and natural gas liquids are presented below.

	Net proved reserves of crude oil, gas condensate and natural gas liquids recoverable up to license expiry dates		Net proved reserves of crude oil, gas condensate and natural gas liquids recoverable past license expiry dates		Total net proved reserves of crude oil, gas condensate and natural gas liquids	
	Millions of barrels	*Millions of metric tons*	*Millions of barrels*	*Millions of metric tons*	*Millions of barrels*	*Millions of metric tons*
Reserves at 31 December 2006	**337**	**41**	**70**	**9**	**407**	**50**
Changes attributable to:						
Revisions of previous estimates	(35)	(5)	35	5	-	-
Extension of license	97	13	(97)	(13)	-	-
Extension and discoveries	11	1	-	-	11	1
Additions	6	1	1	-	7	1
Production	(19)	(3)	-	-	(19)	(3)
Reserves at 31 December 2007	**397**	**48**	**9**	**1**	**406**	**49**
Changes attributable to:						
Revisions of previous estimates	4	-	2	1	6	1
Extension and discoveries	61	7	-	-	61	7
Production	(21)	(2)	-	-	(21)	(2)
Reserves at 31 December 2008	**441**	**53**	**11**	**2**	**452**	**55**
Net proved developed reserves (included above)						
At 31 December 2006	199	24	11	1	210	25
At 31 December 2007	259	31	4	1	263	32
At 31 December 2008	267	32	5	1	272	33

OAO NOVATEK was incorporated as a joint stock company in accordance with the Russian law and is domiciled in the Russian Federation.

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