

**KAZANORGSINTEZ GROUP**

**International Financial Reporting Standards**

**Consolidated Financial Statements  
for the year ended 31 December 2008**

**Independent Auditor's Report**

# KAZANORGSINTEZ GROUP

## IFRS CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

---

### CONTENTS

Statement of Management responsibilities for the preparation and approval of the Consolidated financial statements for the year ended 31 December 2008

Independent Auditor's report

### CONSOLIDATED FINANCIAL STATEMENTS

Consolidated income statement	1
Consolidated balance sheet	2
Consolidated statement of changes in shareholders' equity	3
Consolidated cash flow statement	4
Notes to the consolidated financial statements	5 - 40

## **STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008**

---

The following statement, which should be read in conjunction with the independent auditor's responsibilities stated in the independent auditor's report, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditor in relation to the consolidated financial statements of Open Joint Stock Company "Kazanorgsintez" and its subsidiaries (the "Group").

Management is responsible for the preparation of consolidated financial statements that present fairly the financial position of the Group at 31 December 2008, and the consolidated results of its operations, changes in shareholders' equity and cash flows for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

In preparing the consolidated financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether IFRS have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- Preparing the consolidated financial statements on a going concern basis, unless it is inappropriate to presume that the Group will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective system of internal controls throughout the Group;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking steps to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2008 were approved on 28 May 2009 in Kazan, Republic of Tatarstan, Russian Federation, by:



---

L.S. Alekhin  
General Director



---

N.F. Gaynullina  
Chief Financial Officer

**INDEPENDENT AUDITOR'S REPORT**

To the Shareholders and Board of Directors of Open Joint Stock Company "Kazanorgsintez":

- 1 We have audited the accompanying consolidated financial statements of Open Joint Stock Company "Kazanorgsintez" and its subsidiaries (the "Group") which comprise the consolidated balance sheet as at 31 December 2008 and the consolidated income statement, consolidated statement of changes in shareholders' equity and consolidated cash flow statement 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 of 31 December 2008, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

*Emphasis of Matter*

- 7 Without qualifying our opinion, we draw attention to Note 5 to the financial statements, which indicate that the Group has significant indebtedness which is contractually due in the next 12 months and was not in compliance with certain debt covenants as of 31 December 2008. These conditions raise substantial doubt about the Group's ability to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments that may result from the outcome of this material uncertainty.

*ZAO PricewaterhouseCoopers Audit*

# KAZANORGSINTEZ GROUP

## CONSOLIDATED INCOME STATEMENT

(in thousands of Russian roubles)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Sales	6	23,004,806	21,194,194
Cost of sales	7	(18,886,604)	(15,174,159)
<b>Gross profit</b>		<b>4,118,202</b>	<b>6,020,035</b>
Selling, general and administrative expenses	8	(3,082,410)	(2,529,681)
Loss from other sales, net	9	(135,337)	(168,806)
Finance costs	10	(1,226,935)	(339,024)
(Loss)/income from investments, net	11	(78)	58,261
Share of (loss)/profit of associates	12	(44,727)	119
Foreign exchange (loss)/gain, net		(2,982,189)	542,681
Other expenses, net	13	(418,917)	(195,927)
<b>(Loss)/profit before income tax</b>		<b>(3,772,391)</b>	<b>3,387,658</b>
Income tax credit/(expense)	14	816,899	(833,749)
<b>(Loss) /profit for the period</b>		<b>(2,955,492)</b>	<b>2,553,909</b>
Attributable to:			
Shareholders of the parent company		(2,955,417)	2,552,980
Minority interest		(75)	929
		<b>(2,955,492)</b>	<b>2,553,909</b>
<b>(LOSS)/EARNINGS PER SHARE (RUR)</b>			
Basic and diluted	31	(1.67)	1.42

The accompanying notes on pages 5 to 40 are an integral part of these consolidated financial statements.

# KAZANORGSINTEZ GROUP

## CONSOLIDATED BALANCE SHEET

(in thousands of Russian roubles)

	Notes	As at 31 December 2008	As at 31 December 2007
<b>ASSETS</b>			
NON-CURRENT ASSETS:			
Property, plant and equipment	15	40,150,036	34,840,461
Intangible assets	16	919,665	23,866
Other financial assets	17	52,675	52,100
Investments in associates	18	2,560	24,789
Advances paid for licenses	19	417,253	1,039,946
		<u>41,542,189</u>	<u>35,981,162</u>
CURRENT ASSETS:			
Inventories	20	3,904,388	3,073,991
Trade and other receivables	21	1,071,313	1,343,919
Income tax prepaid		70,527	56,533
Other prepaid and recoverable taxes	22	370,091	1,009,304
Cash and cash equivalents	23	324,630	455,205
		<u>5,740,949</u>	<u>5,938,952</u>
<b>TOTAL ASSETS</b>		<b><u>47,283,138</u></b>	<b><u>41,920,114</u></b>
<b>EQUITY AND LIABILITIES</b>			
EQUITY AND RESERVES:			
Share capital	24	1,904,710	1,904,710
Treasury shares	24	-	(7,712)
Additional paid-in capital	24	1,515,015	1,515,015
Retained earnings		7,955,434	11,691,746
Equity attributable to shareholders of the parent company		<u>11,375,159</u>	<u>15,103,759</u>
Minority interest		7,983	32,253
		<u>11,383,142</u>	<u>15,136,012</u>
NON-CURRENT LIABILITIES:			
Long-term borrowings	25	948,349	11,747,017
Deferred tax liabilities	14	678,692	1,498,196
Obligations under finance leases	26	551,577	91,359
		<u>2,178,618</u>	<u>13,336,572</u>
CURRENT LIABILITIES:			
Short-term borrowings	27	27,941,132	9,341,818
Trade payables	28	4,027,523	2,020,485
Other payables and accrued liabilities	29	1,347,708	1,078,559
Advances received from customers		292,524	855,078
Other taxes payable	30	112,491	151,590
		<u>33,721,378</u>	<u>13,447,530</u>
<b>TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES</b>		<b><u>47,283,138</u></b>	<b><u>41,920,114</u></b>

The accompanying notes on pages 5 to 40 are an integral part of these consolidated financial statements.

## KAZANORGSINTEZ GROUP

### CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(in thousands of Russian roubles)

	Equity attributable to shareholders of the parent company							Minority interest	Total equity
	Notes	Share capital	Additional paid-in capital	Treasury Shares	Retained earnings	Total	Total		
<b>Balance at 31 December 2006</b>		1,904,710	1,515,015	(46,251)	9,801,397	13,174,871	31,324	13,206,195	
Profit for the year		-	-	-	2,552,980	2,552,980	929	2,553,909	
Dividends	32	-	-	-	(662,631)	(662,631)	-	(662,631)	
Acquisition of treasury shares		-	-	(9,359)	-	(9,359)	-	(9,359)	
Disposition of treasury shares		-	-	47,898	-	47,898	-	47,898	
<b>Balance at 31 December 2007</b>		1,904,710	1,515,015	(7,712)	11,691,746	15,103,759	32,253	15,136,012	
Loss for the year		-	-	-	(2,955,417)	(2,955,417)	(75)	(2,955,492)	
Disposal of subsidiaries		-	-	-	(780,895)	(780,895)	(24,195)	(24,195)	
Dividends	32	-	-	(758)	-	(758)	-	(780,895)	
Acquisition of treasury shares		-	-	8,470	-	8,470	-	(758)	
Disposition of treasury shares		-	-	-	-	-	-	8,470	
<b>Balance at 31 December 2008</b>		1,904,710	1,515,015	-	7,955,434	11,375,159	7,983	11,383,142	

The accompanying notes on pages 5 to 40 are an integral part of these consolidated financial statements.

# KAZANORGSINTEZ GROUP

## IFRS CONSOLIDATED CASH FLOW STATEMENT

(in thousands of Russian roubles)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
<b>OPERATING ACTIVITIES:</b>			
Cash flows from operations	33	3,271,193	2,578,855
Income tax paid		(100,159)	(458,725)
Interest paid		(2,042,398)	(1,338,430)
<b>Net cash from operating activities</b>		<b>1,128,636</b>	<b>781,700</b>
<b>INVESTING ACTIVITIES:</b>			
Purchase of property, plant and equipment		(5,327,280)	(10,066,527)
Proceeds on disposal of property, plant and equipment		9,595	55,448
Proceeds on disposal of equity investments		75	19,392
Payments for the licenses		(297,927)	-
Interest received		4,795	8,217
Dividends received		1,682	15
<b>Net cash used in investing activities</b>		<b>(5,609,060)</b>	<b>(9,983,455)</b>
<b>FINANCING ACTIVITIES:</b>			
Proceeds from short-term borrowings		14,674,641	7,125,123
Repayments of short-term borrowings		(13,486,584)	(4,310,297)
Proceeds from long-term borrowings		5,196,287	8,519,279
Repayments of long-term borrowings		(1,049,673)	(1,983,814)
Dividends paid		(603,340)	(359,828)
Re-acquisition of issued shares		(758)	(9,359)
Proceeds on re-issuance of ordinary shares from treasury shares		8,470	47,898
Repayment of obligations under finance lease		(336,506)	(180,851)
<b>Net cash generated from financing activities</b>		<b>4,402,537</b>	<b>8,848,151</b>
<b>Net decrease in cash and cash equivalents</b>		<b>(77,887)</b>	<b>(353,604)</b>
<b>Cash and cash equivalents at beginning of the period</b>		<b>455,205</b>	<b>784,163</b>
Effect of exchange rate changes on cash held in foreign currencies		(52,688)	24,646
<b>Cash and cash equivalents at end of the period</b>		<b>324,630</b>	<b>455,205</b>

The accompanying notes on pages 5 to 40 are an integral part of these consolidated financial statements.



# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

*(in thousands of Russian roubles)*

---

### 1. GENERAL

#### Organisation

Open Joint Stock Company "Kazanorgsintez" (the "Company") was incorporated in Kazan, Republic of Tatarstan, Russian Federation on 1 September 1993. The principal activity of the Company and its subsidiaries (the "Group") is production of chemical products and derivatives thereof (mainly polyethylene) which are marketed and sold primarily in the Russian Federation.

Major production facilities of the Group are located in Kazan, Republic of Tatarstan, Russian Federation. The registered office of the Company is located at the following address: 101, Belomorskaya street, 420051, Kazan, Republic of Tatarstan, Russian Federation.

Details of the Company's subsidiaries are in Note 37.

### 2. OPERATING ENVIRONMENT OF THE GROUP

#### Russian Federation

The Russian Federation displays certain characteristics of an emerging market, including relatively high inflation. Despite strong economic growth in recent years, the financial situation in the Russian market significantly deteriorated during 2008, particularly in the fourth quarter. As a result of global volatility in financial and commodity markets, among other factors, there has been a significant decline in the Russian stock market since mid-2008. Since September 2008, there has been increased volatility in currency markets and the Russian Rouble (RR) has depreciated significantly against some major currencies.

The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and 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.

Management is unable to predict all developments in the economic environment which could have an impact on the Group's operations and consequently what effect, if any, they could have on the financial position of the Group.

#### Impact of the ongoing global financial and economic crisis

The ongoing global financial and economic crisis that emerged out of the severe reduction in global liquidity which commenced in the middle of 2007 (often referred to as the "Credit Crunch") has resulted in, among other things, a lower level of capital market funding, lower liquidity levels across the banking sector and wider economy, and, at times, higher interbank lending rates and very high volatility in stock and currency markets. The uncertainties in the global financial markets have also led to failures of banks and other corporates, and to bank rescues in the United States of America, Western Europe, Russia and elsewhere. The full extent of the impact of the ongoing financial crisis is proving to be difficult to anticipate or completely guard against.

#### *Impact on liquidity:*

The availability of external funding in financial markets has significantly reduced since August 2007. This has affected the ability of the Group to obtain new borrowings and refinance its existing borrowings at terms and conditions similar to those applied to earlier transactions.

#### *Impact on customers:*

Debtors of the Group may be adversely affected by the financial and economic environment, which could in turn impact their ability to repay the amounts owed. Deteriorating economic conditions for customers 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 properly reflected revised estimates of expected future cash flows in its impairment assessments.

Management is unable to reliably determine the effects on the Group's future financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and development of the Group's business in the current circumstances.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 3. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

In the current year, the Group has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the "IASB") and the International Financial Reporting Interpretations Committee (the "IFRIC") of the IASB that are relevant to its operations and effective for annual reporting periods beginning on 1 January 2008. The adoption of *IFRIC 14, IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction, IFRIC 11 IFRS 2 – Group and treasury share transaction and IFRIC 12 Service Concession Arrangements* did not have any significant impact on the consolidated financial statements of the Group.

**Reclassification of Financial Assets – Amendments to IAS 39, Financial Instruments: Recognition and Measurement, and IFRS 7, Financial Instruments: Disclosures and a subsequent amendment, Reclassification of Financial Assets: Effective Date and Transition.** The amendments allow entities the options (a) to reclassify a financial asset out of the held for 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 before 1 November 2008; the reclassifications allowed by the amendments may not be applied before 1 July 2008 and retrospective reclassifications are only allowed if made prior to 1 November 2008. Any reclassification of a financial asset made on or after 1 November 2008 takes effect only from the date when the reclassification is made. These optional reclassifications are not applicable to the Group.

#### New Accounting Pronouncements

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2009 or later periods and which the Group has not early adopted:

**IFRS 8, Operating Segments** (effective for annual periods beginning on or after 1 January 2009). The standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments, 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.

**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.

**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. The Group does not expect the amended standard to have a material effect on its financial statements.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 3. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (continued)

#### 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 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. The Group does not expect the amendments to have any material effect on its financial statements.

**Improving Disclosures about Financial Instruments – Amendment to IFRS 7, Financial Instruments: Disclosures** (issued in March 2009; effective for annual periods beginning on or after 1 January 2009). The amendment requires enhanced disclosures about fair value measurements and liquidity risk. The entity will be required to disclose an analysis of financial instruments using a three-level fair value measurement hierarchy. The amendment (a) clarifies that the maturity analysis of liabilities should include issued financial guarantee contracts at the maximum amount of the guarantee in the earliest period in which the guarantee could be called; and (b) requires disclosure of remaining contractual maturities of financial derivatives if the contractual maturities are essential for an understanding of the timing of the cash flows. An entity will further have to disclose a maturity analysis of financial assets it holds for managing liquidity risk, if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk. The Group is currently assessing the impact of the amendment on disclosures in its financial statements.

**Improvements to International Financial Reporting Standards** (issued in April 2009; amendments to IFRS 2, IAS 38, IFRIC 9 and IFRIC 16 are effective for annual periods beginning on or after 1 July 2009; amendments to IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36 and IAS 39 are effective for annual periods beginning on or after 1 January 2010). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: clarification that contributions of businesses in common control transactions and formation of joint ventures are not within the scope of IFRS 2; clarification of disclosure requirements set by IFRS 5 and other standards for non-current assets (or disposal groups) classified as held for sale or discontinued operations; requiring to report a measure of total assets and liabilities for each reportable segment under IFRS 8 only if such amounts are regularly provided to the chief operating decision maker; amending IAS 1 to allow classification of certain liabilities settled by entity's own equity instruments as non-current; changing IAS 7 such that only expenditures that result in a recognised asset are eligible for classification as investing activities; allowing classification of certain long-term land leases as finance leases under IAS 17 even without transfer of ownership of the land at the end of the lease; providing additional guidance in IAS 18 for determining whether an entity acts as a principal or an agent; clarification in IAS 36 that a cash generating unit shall not be larger than an operating segment before aggregation; supplementing IAS 38 regarding measurement of fair value of intangible assets acquired in a business combination; amending IAS 39 (i) to include in its scope option contracts that could result in business combinations, (ii) to clarify the period of reclassifying gains or losses on cash flow hedging instruments from equity to profit or loss and (iii) to state that a prepayment option is closely related to the host contract if upon exercise the borrower reimburses economic loss of the lender; amending IFRIC 9 to state that embedded derivatives in contracts acquired in common control transactions and formation of joint ventures are not within its scope; and removing the restriction in IFRIC 16 that hedging instruments may not be held by the foreign operation that itself is being hedged. The Group does not expect the amendments to have any material effect on its financial statements.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 3. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (continued)

#### Standards and Interpretations in issue not yet adopted

At the date of authorisation of these consolidated financial statements, the following Standards and Interpretations were in issue but not yet effective:

<b>Standards and interpretations</b>	<b>Effective for annual periods beginning on or after</b>
<i>Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate – IFRS 1 and IAS 27 Amendment (issued in May 2008)</i>	1 January 2009
<i>IAS 23, Borrowing Costs (revised March 2007)</i>	1 January 2009
<i>Eligible Hedged Items – Amendment to IAS 39, Financial Instruments: Recognition and Measurement (effective with retrospective application)</i>	1 July 2009
<i>Puttable Financial Instruments and Obligations Arising on Liquidation – IAS 32 and IAS 1 Amendment</i>	1 January 2009
<i>IFRS 1, First-time Adoption of International Financial Reporting Standards</i>	1 July 2009
<i>Vesting Conditions and Cancellations – Amendment to IFRS 2, Share-based Payment (issued in January 2008)</i>	1 January 2009
<i>IFRS 3, Business Combinations (revised January 2008)</i>	1 July 2009
<i>Embedded Derivatives – Amendments to IFRIC 9 and IAS 39</i>	30 June 2009
<i>IFRIC 13, Customer Loyalty Programmes</i>	1 July 2008
<i>IFRIC 15, Agreements for the Construction of Real Estate</i>	1 January 2009
<i>IFRIC 16, Hedges of a Net Investment in a Foreign Operation</i>	1 October 2008
<i>IFRIC 17, Distribution of Non-Cash Assets to Owners</i>	1 July 2009
<i>IFRIC 18, Transfers of Assets from Customers</i>	1 July 2009

Management anticipates that the adoption of these Standards and Interpretations in the preparation of the consolidated financial statements in future periods will have no material impact on the consolidated financial statements of the Group.

### 4. SIGNIFICANT ACCOUNTING POLICIES

#### Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards.

#### Basis of preparation

The financial statements have been prepared on the historical cost basis except for the valuation of certain financial instruments. The principal accounting policies are set out below.

#### Subsidiaries

Subsidiaries are those companies and other entities (including special purpose entities) in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain benefits. The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Subsidiaries (continued)

The excess of the cost of acquisition over the acquirer's share of the fair value of the net assets of the acquiree at each exchange transaction is recorded as goodwill. The excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost ("negative goodwill") is recognised immediately in profit or loss.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any minority interest

#### Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries (including special purpose entities) controlled by the Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-Group transactions, balances, income and expenses are eliminated in full on consolidation.

Minority interests in the net assets (excluding goodwill) of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination (see below) and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

#### Purchases and sales of minority interests

The Group applies the parent company model to account for transactions with minority shareholders. Any difference between the purchase consideration and the carrying amount of minority interest acquired is recorded as goodwill or negative goodwill. The Group recognises the difference between sales consideration and carrying amount of minority interest sold as a gain or loss in the income statement.

#### Business combinations

Acquisitions of subsidiaries and businesses are accounted for using the purchase method. The cost of the business combination is measured as the aggregate of the fair values of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 *Business Combinations* are recognised at their fair values at the acquisition date, except for non-current assets that are classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Investments in associates

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

The results and assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate) are not recognised, unless the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

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

Where a Group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

#### Special purpose entities

Special purpose entities ("SPEs") are those undertakings that are created to satisfy specific business needs of the Group and the Group has the right to the majority of the benefits of the SPE, or exposed to risks associated with activities of the SPE.

SPEs are consolidated in the same manner as subsidiaries when the substance of the relationship indicates that the SPE is controlled by the Group.

#### Goodwill

Goodwill arising on the acquisition of a subsidiary represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary recognised at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

The Group's policy for goodwill arising on the acquisition of an associate is described under 'Investments in associates' above.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable net of VAT and discounts.

#### Sale of goods

Revenue from the sale of goods is recognised when all the following conditions are satisfied:

- The Group has transferred to the buyer the significant risks and rewards of ownership of the goods, which is typically at the date of loading to third party for transportation;
- The Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the entity; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

#### Dividend, interest and other revenue

Dividend revenue from investments is recognised when the Group's right to receive payment has been established.

Interest revenue is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

The income from other sales includes revenues from sale of ancillary items, net of cost of sales. Other sales primarily consist of sales of electricity, water and heat.

#### Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs (see below). Contingent rentals are recognised as expenses in the periods in which they are incurred.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

#### Foreign currencies

The functional currency of the Company and all its subsidiaries, which reflects the economic substance of their operations, and presentation currency of the consolidated financial statements of the Group, is the Russian rouble ("RUR").

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in profit or loss in the period in which they arise.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

#### Income taxes

Income taxes have been provided for in the financial statements in accordance with legislation enacted or substantively enacted by the balance sheet date. The income tax charge or credit comprises current tax and deferred tax and is recognised in the income statement except if it is recognised directly in equity because it relates to transactions that are also recognised, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes other than on income are recorded within operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. 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 the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

The Group controls reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains at their disposal. The Group does not recognise deferred tax liabilities on such temporary differences except to the extent that Management expects the temporary differences to reverse in the foreseeable future.

The Group's uncertain tax positions are reassessed by management at every balance sheet date. Liabilities are recorded for income tax positions that are determined by management as more likely than not to result in additional taxes being levied if the positions were to be challenged by the tax authorities. The assessment is based on the interpretation of tax laws that have been enacted or substantively enacted by the balance sheet date and any known court or other rulings on such issues. Liabilities for penalties, interest and taxes other than on income are recognised based on management's best estimate of the expenditure required to settle the obligations at the balance sheet date.

#### Property, plant and equipment

Property, plant and equipment held for use in the production or supply of goods or services, or for administrative purposes, are stated in the balance sheet at their cost less any accumulated depreciation and accumulated impairment losses.

Capitalised cost includes acquisition cost and major expenditures for improvements and replacements that extend the useful lives of the assets or increase their revenue generating capacity. Repair and maintenance expenditures that do not meet the foregoing criteria for capitalisation are charged to the income statement as incurred.

Depreciation is computed under the straight-line method utilizing the estimated useful lives of the assets, which are:

Buildings	20-80 years
Machinery and equipment	5-30 years
Other	3-10 years

Land occupied by the Group's facilities is owned by the Group. Land is not depreciated and is included in property, plant and equipment.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as similar owned assets or, where shorter, the term of the relevant lease.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the income statement.



# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Construction in progress

Construction in progress comprises costs directly related to construction of property, plant and equipment including an appropriate allocation of directly attributable variable overheads that are incurred in construction. Depreciation of constructed assets commences when the assets are put into operation.

#### Intangible assets

Intangible assets acquired separately are reported at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged on a straight-line basis over their estimated useful lives.

The Group has purchased various licenses for the use of technologies used in the production of Bisphenol-A, polycarbonate and high density polyethylene. The cost of acquiring these licenses are initially recorded as advances paid for licenses. The terms of the licenses are 10 years from the commencement of commercial production as defined in the respective agreements. Upon commencement of commercial production, these licenses are reclassified to intangible assets and amortized on a straight line basis over the term of the license.

The estimated useful life and amortisation method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Software costs incurred for the development, implementation and enhancement of the operating systems, are capitalised and amortised over the expected useful life of the system. Software costs relating to the maintenance of the operating system are recognised as an expense in the period in which they occur.

#### Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

#### Impairment of financial assets carried at amortised cost

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. The primary factors that the Group considers in determining whether a financial asset is impaired are its overdue status and realisability of related collateral, if any. The following other principal criteria are also used to determine whether there is objective evidence that an impairment loss has occurred:

- any portion or instalment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- the counterparty experiences a significant financial difficulty as evidenced by its financial information that the Group obtains;

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

- the counterparty considers bankruptcy or a financial reorganisation;
- there is adverse change in the payment status of the counterparty as a result of changes in the national or local economic conditions that impact the counterparty; or
- the value of collateral, if any, significantly decreases as a result of deteriorating market conditions.

If the terms of an impaired financial asset held at amortised cost are renegotiated or otherwise modified because of financial difficulties of the counterparty, impairment is measured using the original effective interest rate before the modification of terms.

Impairment losses are always recognised through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account through profit or loss.

Uncollectible assets are written off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to impairment loss account in the income statement.

#### **Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour, transportation, handling costs and those overhead costs that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method. Net realisable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Work in progress and semi-finished products are valued at the net unit cost of production allocated to the estimated stage of completion.

#### **Provisions**

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

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

#### **Cash and cash equivalents**

Cash and cash equivalents include cash on hand, cash with banks, deposits and marketable securities with original maturity of three months or less.

#### **Prepayments**

Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group. Other prepayments are written off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying value of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Financial assets

Financial assets, except for cash and cash equivalents and financial assets out of scope of IAS 39 (Revised), *Financial Instruments: Recognition and Measurement*, are classified into the following specified categories: financial assets as "held-to-maturity" ("HTM") investments, "available-for-sale" ("AFS") financial assets and "loans and receivables". The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

#### Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial asset, or, where appropriate, a shorter period.

#### HTM investments

Debt securities with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity are classified as HTM investments. HTM investments are recorded at amortised cost using the effective interest method less impairment, with income recognised on an effective yield basis.

#### AFS financial assets

AFS financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition AFS financial assets are measured at fair value with gains and losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the income statement.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the closing of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques.

Dividends on AFS equity instruments are recognised in the consolidated income statement when the Group's right to receive payments is established.

#### Loans and receivables

Loans and receivables include trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market and are measured at amortised cost using the effective interest method less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

#### Impairment of financial assets

Financial assets are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortised cost, the amount of the impairment 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 carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in the income statement.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognised impairment loss is reversed through the consolidated income statement to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognised. Any increase in fair value of AFS equity securities subsequent to an impairment loss is recognised directly in equity.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Financial liabilities and equity instruments issued by the Group

##### Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

##### Financial liabilities

Financial liabilities, including borrowings, trade and other payables are initially measured at fair value, net of transaction costs, and subsequently measured at amortised cost using the effective interest method.

##### Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recorded at the proceeds received, net of direct issue costs.

#### Earnings per share

Earnings per share is determined by dividing the profit or loss attributable to equity holders of the Group less amount of dividends on preferred shares by the weighted average number of participating shares in issue outstanding during the reporting year.

#### Employee benefit obligations

Remuneration to employees in respect of services rendered during a reporting period is recognised as expenses in that period.

The Group's Russian subsidiaries are legally obliged to make defined contributions to the Russian Federation State Pension Fund. These contributions are recognised in the income statement as incurred.

In the Russian Federation all obligatory social contributions, including contributions to the Russian Federation State Pension Fund, are collected through a unified social tax ("UST") calculated by the application of a regressive rate from 26% to 2% of the annual gross remuneration of each employee. UST is allocated to three state social funds, including the Russian Federation State Pension Fund at the rates varying from 20% to 2% of the annual gross remuneration of each employee. UST is recognised as an expense when employees have rendered service entitling them to the contributions.

#### Segment reporting

The majority of the Group's business operations are located in the Russian Federation and relate primarily to the production and marketing of chemical products and derivatives thereof (mainly ethylene and polyethylene). Therefore, business activities are subject to the same risks and returns and are addressed in the consolidated financial statements of the Group as one reportable segment.

#### Dividends declared

Dividends and related taxation thereon are recognised as a liability in the period in which they have been declared and become legally payable.

Accumulated profit legally distributable by the Company is based on the amounts available for distribution in accordance with the applicable legislation and as reflected in the statutory financial statements of the individual entities of the Group. These amounts may differ significantly from the amounts calculated on the basis of IFRS.

#### Treasury shares

When Group companies purchase the Company's equity share capital, the consideration paid including any attributable transaction costs is deducted from total equity as treasury shares until they are re-sold. When such shares are subsequently sold, any consideration received is included, net of associated income tax in equity. Treasury shares are recorded at cost as determined on a weighted average basis. The gains (losses) arising from treasury share transactions are recognized as a movement in the consolidated statement of changes in shareholders' equity.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 4. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Value-added taxes

Value-added taxes ("VAT") related to sales are payable to the tax authorities on an accrual basis based upon invoices issued to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales.

### 5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTIES

#### Going concern assumption

Management prepared these financial statements on a going concern basis. In making this judgment management considered the Group's financial position, current intentions, profitability of operations and access to financial resources, and analysed the impact of the recent financial crisis on future operations of the Group. As of 31 December 2008 the Group borrowings totaled RUR 28,889,481 thousand. Of this amount, RUR 4,745,474 thousand (2007: RUR 3,188,059 thousand) is contractually due in the next twelve months and RUR 16,542,604 thousand has been reclassified to short-term as the Group was not in compliance with certain debt covenants at 31 December 2008 (2007: RUR 4,987,447 thousand) and as a consequence of the default event described in Note 38. As a result of this reclassification, and the performance of the Group for the year, the Group is in a net current liability position of RUR 27,980,429 thousand (2007: RUR 7,508,578 thousand). The Group has appointed an international financial advisor and is currently in negotiations with its lenders to refinance or restructure its current obligations and obtain a waiver and amend its covenants. Absent such refinancing, and waiver or amendment, this condition raises substantial doubt about the Group's ability to continue as a going concern. Management believes that these negotiations will be successful. The accompanying consolidated financial statements do not include any adjustments that may result from the outcome of this uncertainty.

In the application of the Group's accounting policies management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may significantly differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

#### Critical judgments in applying accounting policies

The following are the critical judgments, apart from those involving estimations, that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognised in financial statements.

#### Taxation

Judgments are required in determining current income tax liabilities. The Group recognises liabilities for taxes based on estimates of whether additional taxes will be due. Where the final outcome of various tax matters is different from the amounts that were initially recorded, such differences will impact income tax and deferred tax provisions in the period in which such determination is made.

The Group has not recognised a deferred tax liability in respect of temporary differences associated with investments in subsidiaries. The Group controls the timing of the reversal of those temporary differences and does not expect their reversal in the foreseeable future.

The recognised deferred tax asset represents income taxes recoverable through future deductions from taxable profits and is recorded on the balance sheet. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. The future taxable profits and the amount of tax benefits that are probable in the future are based on medium term business plan prepared by management and extrapolated results thereafter. The business plan is based on management expectations that are believed to be reasonable under the circumstances. Key assumptions in the business plan are obtaining refinance, sales volumes, sales prices and raw materials prices.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

*(in thousands of Russian roubles)*

---

### 5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTIES (continued)

#### Critical judgments in applying accounting policies (continued)

##### Environmental obligations

The Group's activities are subject to various laws and regulations governing the protection of the environment. The Group pays fees to the regulatory authorities for the right to discharge within legal norms. Management believes this fee covers all environmental obligations, and this fee is recorded as an expense in the period incurred. No other provisions for environmental obligations are recorded.

##### **Key sources of estimation uncertainty**

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

##### Useful economic lives of property, plant and equipment

Management assesses the useful economic lives of property, plant and equipment considering the current technical condition of assets and potential changes in technology and demand. Any changes of these conditions could affect prospective depreciation of property, plant and equipment and their carrying value.

##### Impairment of assets

The Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets are impaired. In making the assessment for impairment, assets that do not generate independent cash flows are allocated to an appropriate cash generating unit. Management necessarily applies its judgment in allocating assets that do not generate independent cash flows to appropriate cash generating units, and also in estimating the timing and value of underlying cash flows within the value in use calculation. Key assumptions in Management's analysis relate to obtaining refinance, sales volumes, sales prices and raw materials prices. Subsequent changes to the cash generating unit allocation or to the timing of cash flows could impact the carrying value of the respective assets.

##### Allowances for doubtful debts

The Group creates allowances for doubtful debts to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful debts, management bases its estimates on the current overall economic conditions, the aging of accounts receivable balances, historical write-off experience, customer creditworthiness and changes in payment terms.

Changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful debts recorded in the consolidated financial statements.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 6. SALES

	Year ended 31 December 2008	Year ended 31 December 2007
<b>By geographic region:</b>		
Domestic sales	16,951,040	15,356,486
Export sales	6,053,766	5,837,708
<b>Total</b>	<b>23,004,806</b>	<b>21,194,194</b>
<b>By products:</b>		
High density polyethylene	8,962,848	8,076,085
Low density polyethylene	5,700,159	5,467,782
Organic products	2,289,939	1,967,281
Plastic goods	1,814,415	1,724,995
Bisphenol A	1,647,151	83,936
Products produced by Ethylene plant	1,213,450	2,861,947
Polycarbonate	13,081	-
Tolling services	1,363,763	1,012,168
<b>Total</b>	<b>23,004,806</b>	<b>21,194,194</b>

### 7. COST OF SALES

	Year ended 31 December 2008	Year ended 31 December 2007
Raw materials	11,365,881	9,980,577
Energy and water	2,791,625	1,928,621
Labour costs	1,785,138	1,536,374
Depreciation	1,571,182	1,036,569
Auxiliary materials	904,506	557,615
Inventory obsolescence provision charged/(released)	284,694	(13,401)
Services	279,031	357,395
Other	354,598	50,921
	<b>19,336,655</b>	<b>15,434,671</b>
Increase in work in progress and finished goods	(450,051)	(260,512)
<b>Total</b>	<b>18,886,604</b>	<b>15,174,159</b>

### 8. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December 2008	Year ended 31 December 2007
Labour costs	1,027,581	822,509
Taxes, other than income tax	322,834	304,438
Transportation, storage and export duties	321,006	285,043
Insurance expenses	297,434	193,544
Material costs (energy, materials, etc.)	297,150	268,097
Services	254,169	231,718
Depreciation and amortization	154,397	117,813
Bank charges	79,239	46,847
Other	328,600	259,672
<b>Total</b>	<b>3,082,410</b>	<b>2,529,681</b>

The 2007 Group financial statements disclosed general and administrative expenses of RUR 1,567,734 thousand and selling expenses of RUR 492,849 thousand by function. The table above contains these amounts broken down by nature.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 9. LOSS FROM OTHER SALES, NET

	Year ended 31 December 2008	Year ended 31 December 2007
Other revenue	506,038	606,278
Cost of other sales	(641,375)	(775,084)
<b>Total</b>	<b>(135,337)</b>	<b>(168,806)</b>

Revenue and costs from other sales comprise revenue and the corresponding costs from sales of products of subsidiary units and auxiliary shops.

### 10. FINANCE COSTS

	Year ended 31 December 2008	Year ended 31 December 2007
Interest expense on loans and borrowings	2,011,431	1,357,835
Interest expense on obligations under finance leases	51,247	29,154
Other expenses	-	1,287
Less: amount included in the cost of qualifying assets	(835,743)	(1,049,252)
<b>Total</b>	<b>1,226,935</b>	<b>339,024</b>

### 11. (LOSS)/ INCOME FROM INVESTMENTS, NET

	Year ended 31 December 2008	Year ended 31 December 2007
(Loss)/Income from disposal of subsidiaries (refer to Note 37)	(6,555)	35,244
Income from disposal of associate	-	14,785
Interest income	4,795	8,217
Dividends received	1,682	15
<b>Total</b>	<b>(78)</b>	<b>58,261</b>

### 12. SHARE OF (LOSS)/ PROFIT OF ASSOCIATES

	Year ended 31 December 2008	Year ended 31 December 2007
LLC TAIF Invest	(24,159)	119
LLC Kolos-Sintez	(20,568)	-
<b>Total</b>	<b>(44,727)</b>	<b>119</b>

### 13. OTHER EXPENSES, NET

	Year ended 31 December 2008	Year ended 31 December 2007
Rent of land	223,744	203,877
Service divisions	84,999	95,117
Maintenance of social infrastructure	45,173	24,474
Loss on disposal of property, plant and equipment	27,540	27,600
Income from disposal of materials	(17,745)	(36,654)
Other expenses/(income)	55,206	(118,487)
<b>Total</b>	<b>418,917</b>	<b>195,927</b>

Maintenance of social infrastructure comprises primarily operating costs of facilities such as hotel, dormitory and other sports facilities.

Expenses for rent of land relate to rent of an idle plot of land in the remote region of Tatarstan Republic, the agreement was concluded at the request of the local tax authorities.



# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 14. INCOME TAX

The Group's provision for income tax is as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Current income tax	2,605	549,678
Deferred tax (credit)/charge	(819,504)	284,071
<b>Total</b>	<b>(816,899)</b>	<b>833,749</b>

The following presents a reconciliation of theoretical income tax calculated at the rate effective in the Russian Federation (24%) to the amount of actual income tax expense recorded in the income statement:

	Year ended 31 December 2008	Year ended 31 December 2007
(Loss)/profit before income tax	(3,772,391)	3,387,658
Theoretical income tax (credit)/expense at 24%	(905,374)	813,038
Effect of non-deductible expenses and other permanent differences, net	224,213	20,711
Effect of reduction in tax rate to 20% enacted in 2008 with effect from 1 January 2009	(135,738)	-
<b>Income tax (credit)/expense</b>	<b>(816,899)</b>	<b>833,749</b>

On 26 November 2008, the Russian Federation reduced the standard corporate income tax rate from 24% to 20% with effect with 1 January 2009. The impact of the change in tax rate presented above represents the effect of applying the reduced 20% tax rate to deferred tax balances at 31 December 2008.

Temporary differences between the Russian statutory tax accounts and these financial statements give rise to the following deferred tax liabilities. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rate of 20% (2007: 24%)

	Year ended 31 December 2008	Year ended 31 December 2007
Property, plant and equipment	1,610,084	1,526,117
Provision for doubtful debts	(654)	(5,082)
Accrued income	(11,088)	(22,839)
Tax losses carried forward	(919,650)	-
<b>Deferred tax liabilities, net</b>	<b>678,692</b>	<b>1,498,196</b>

The movements in the Group's deferred tax position were as follows:

	Year ended 31 December 2008	Year ended 31 December 2007
Balance at beginning of period	1,498,196	1,214,125
(Credit)/charge to income statement	(819,504)	284,071
<b>Balance at end of the period</b>	<b>678,692</b>	<b>1,498,196</b>

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Russian roubles)

### 15. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings	Machinery and equipment	Other assets	Construction In progress	Total
<b>Cost</b>					
At 1 January 2007	8,729,856	12,992,889	1,353,557	13,892,456	36,968,758
Additions	48,582	252,459	22,322	10,962,695	11,286,058
Disposals	(44,057)	(140,248)	(15,627)	(13,884)	(213,816)
Transfers	1,890,998	3,788,312	461,083	(6,140,393)	-
<b>At 31 December 2007</b>	<b>10,625,379</b>	<b>16,893,412</b>	<b>1,821,335</b>	<b>18,700,874</b>	<b>48,041,000</b>
Additions	2,642	706,639	10,641	6,577,915	7,297,837
Disposals	(53,898)	(191,719)	(37,412)	(91,827)	(374,856)
Transfers	166,191	5,507,356	259,398	(5,932,945)	-
<b>At 31 December 2008</b>	<b>10,740,314</b>	<b>22,915,688</b>	<b>2,053,962</b>	<b>19,254,017</b>	<b>54,963,981</b>
<b>Accumulated depreciation</b>					
At 1 January 2007	(4,417,796)	(7,191,803)	(485,255)	-	(12,094,854)
Charge for the year	(196,973)	(895,435)	(144,045)	-	(1,236,453)
Eliminated on disposals	8,689	111,932	10,147	-	130,768
<b>At 31 December 2007</b>	<b>(4,606,080)</b>	<b>(7,975,306)</b>	<b>(619,153)</b>	<b>-</b>	<b>(13,200,539)</b>
Charge for the period	(257,176)	(1,322,772)	(213,710)	-	(1,793,658)
Eliminated on disposals	16,367	157,261	6,624	-	180,252
<b>At 31 December 2008</b>	<b>(4,846,889)</b>	<b>(9,140,817)</b>	<b>(826,239)</b>	<b>-</b>	<b>(14,813,945)</b>
<b>Net book value</b>					
At 31 December 2007	<u>6,019,299</u>	<u>8,918,106</u>	<u>1,202,182</u>	<u>18,700,874</u>	<u>34,840,461</u>
At 31 December 2008	<u>5,893,425</u>	<u>13,774,871</u>	<u>1,227,723</u>	<u>19,254,017</u>	<u>40,150,036</u>

The Group's plant sites presently occupy approximately 479.8 hectares of land for which the Group holds the title.

At 31 December 2008 property, plant and equipment with the carrying value of RUR 7,012,245 thousand (2007: RUR 2,379,222 thousand) were pledged to secure certain short-term and long-term loans granted to the Group (refer to Note 25 and 27).

During the year ended 31 December 2008 interest of RUR 835,743 thousand has been capitalized in property, plant and equipment (2007: RUR 1,049,252 thousand) refer to Note 10. The average interest capitalisation rates for 2008 and 2007 were 8.33 percent and 7.28 percent, respectively.

At 31 December 2008, property, plant and equipment include assets held under a number of finance lease agreements (refer to Note 26). At the end of the lease term the Group takes automatic ownership of these assets. The carrying value of such assets was RUR 1,170,660 thousands: RUR 1,030,907 thousands of equipment, and RUR 139,753 thousands of construction in progress (2007: RUR 703,805 thousand: RUR 638,387 thousands of equipment, and RUR 65,418 thousands of construction in progress).

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 16. INTANGIBLE ASSETS

Intangible assets at 31 December 2007 primarily comprise costs incurred in connection with acquisition and implementation of our management information system SAP R/3 and are amortised over a period of thirteen years. In addition, as commercial Bisphenol A and Polycarbonates productions have commenced in the current period the licence costs associated with the production technology has been reclassified from advances paid for licenses to Intangible assets and are being amortised over the ten year term of the licenses.

	Software	Licences and franchises	Other intangible assets	Total
<b>Cost</b>				
At 1 January 2007	109,351	-	-	109,351
Additions		411	51	462
Disposals	(849)	-	-	(849)
<b>At 31 December 2007</b>	<b>108,502</b>	<b>411</b>	<b>51</b>	<b>108,964</b>
Additions	-	920,498	198	920,696
Disposals	-	(77)	-	(77)
<b>At 31 December 2008</b>	<b>108,502</b>	<b>920,832</b>	<b>249</b>	<b>1,029,583</b>
<b>Accumulated amortisation</b>				
At 1 January 2007	(76,752)	-	-	(76,752)
Charge for the year	(8,346)	-	-	(8,346)
<b>At 31 December 2007</b>	<b>(85,098)</b>	<b>-</b>	<b>-</b>	<b>(85,098)</b>
Charge for the period	(8,346)	(16,450)	(24)	(24,820)
<b>At 31 December 2008</b>	<b>(93,444)</b>	<b>(16,450)</b>	<b>(24)</b>	<b>(109,918)</b>
<b>Net book value</b>				
At 31 December 2007	<u>23,404</u>	<u>411</u>	<u>51</u>	<u>23,866</u>
At 31 December 2008	<u>15,058</u>	<u>904,382</u>	<u>225</u>	<u>919,665</u>

### 17. OTHER FINANCIAL ASSETS

	As at 31 December 2008		As at 31 December 2007	
	% ownership	Amount	% ownership	Amount
OJSC "Tatneftekhiminvestholding"	7%	38,538	7%	38,537
National non-state pension fund	5%	10,557	5%	10,557
OJSC "Kazanskaya yarmarka"	2%	2,950	2%	2,950
LLC Taif-Invest	6.65%	630	-	-
Other	-	-	-	56
<b>Total</b>		<u>52,675</u>		<u>52,100</u>

Management was unable to determine fair value of unquoted shares using valuation techniques that are supported by publicly available market information. As a result, AFS investments are presented at cost, net of impairment provision. The company has no intention to dispose of these financial assets.

In December 2008 the Group has diluted its share of investment in associate company LLC Taif-Invest which resulted in reclassification of this investment into other financial assets (refer to Note 18).

The Group does not hold any collateral as security.

## KAZANORGSINTEZ GROUP

### NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

#### 18. INVESTMENTS IN ASSOCIATES

Name of associate	Principal activity	As at 31 December 2008		As at 31 December 2007	
		% ownership	Amount	% ownership	Amount
LLC Kolos-Sintez (refer to Note 37)	Agriculture Investing	49	2,560	-	-
LLC "Taif-Invest"	activity	-	-	40	24,789
LLC "Novomoskovsky trubny zavod"	Manufacturing	26	-	26	-
<b>Total</b>			<b>2,560</b>		<b>24,789</b>

In September 2008 the Group reclassified its share in subsidiary entity LLC "Kolos-Sintez" from Investments in subsidiaries to Investments in associates as a result of an additional subscription for shares in which the Group has not increased its investment (refer to Note 37).

	As at 31 December 2008	As at 31 December 2007
Total assets	275,392	148,903
Total liabilities	(309,557)	(144,740)
Net (liabilities)/assets	(34,165)	4,163

LLC "Novomoskovsky trubny zavod" is loss making. The Group has not recognized the losses beyond the value of the investment.

	As at 31 December 2008	As at 31 December 2007
Group's share of associates' net (liabilities)/assets	2,560	24,789
Total revenue	380,178	1,031,389
Total loss for the period	100,509	19,680
Unrecognised share of losses in an associate	-	6,316
Group's share of associates' (loss)/profit for the period	(44,727)	119

#### 19. ADVANCES PAID FOR LICENSES

Advances paid for licenses as at 31 December 2007 are comprised of prepaid amounts for licenses for polycarbonate plastic and high density polyethylene production technologies.

The costs of license for Bisphenol A and Polycarbonates production technology acquired during the previous periods were reclassified from advances paid for licenses to Intangible assets as commercial Bisphenol A and Polycarbonates production has commenced in the current period (refer to Note 16).

As of 31 December 2008 advances paid for a license related to polyethylene production. Commercial production is expected to be launched in 2009.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 20. INVENTORIES

	As at 31 December 2008	As at 31 December 2007
Stores and materials	2,823,443	2,158,403
Finished goods	894,012	549,908
Work in progress and semi-finished products	473,882	367,935
Less: provision for obsolescence	(286,949)	(2,255)
<b>Total</b>	<b>3,904,388</b>	<b>3,073,991</b>

One of the Group's subsidiaries as at 31 December 2007 was engaged in agricultural activity of breeding livestock intended for the production of meat and planting and harvesting of potato and other agricultural products. The aggregated biological assets of this subsidiary are not material to the accompanying Group's consolidated financial statements and are included in stores and materials. In September 2008 the Group reclassified its share in subsidiary entity from Investments in subsidiaries to Investments in associates due to partial disposal (refer to Note 18).

### 21. TRADE AND OTHER RECEIVABLES

	As at 31 December 2008	As at 31 December 2007
Trade receivables	772,069	604,926
Advances paid	227,779	606,841
Other receivables and prepaid expenses	109,568	175,715
Less: provision for doubtful debts	(38,103)	(43,563)
<b>Total</b>	<b>1,071,313</b>	<b>1,343,919</b>

The prevailing majority of sales of goods are contracted at prepayment basis. Post payment sales are used to promote new types of product to the markets and under sales of tolling services. The maximum credit period on post payment sales of goods is 30 days. In case of delay, interest is charged at 3% (2% for export contracts) per month on the outstanding balance. The Group has analyzed all receivables over 45 days for recoverability, because historical experience indicates that accounts receivable aged between 45 and 90 days are recovered by 50 percent and receivables over 90 days are generally not recoverable. Based on results of this analysis, and in the cases where the Group has no collateral and no counter liabilities, the Group identified specific accounts and provided fully for the receivables that are past due beyond 90 days and provided 50 percent for the receivables between 45 days and 90 days.

Before accepting any new customer, the Group uses an internal procedure to assess the potential customer's credit quality and defines credit limits by customer. Only customers, which have long-term relationship with the Company and good credit history, can have contracts with post sales payments. All new customers have to pass approving procedure, which includes: security check, check of set up documents, tax registration, feasibility analysis and credit history.

As of 31 December 2008, trade receivables of RUR 29,411 thousand (2007: RUR 37,523 thousand) 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 trade and other receivables is as follows:

	As at 31 December 2008	As at 31 December 2007
90-180 days	7,154	7,951
180-365 days	4,517	25,375
1 year – 3 years	17,740	4,197
<b>Total</b>	<b>29,411</b>	<b>37,523</b>

The maximum exposure to credit risk at the reporting date is the fair value of each class of trade and other accounts receivable mentioned above. The Group does not hold any collateral as security.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 21. TRADE AND OTHER RECEIVABLES (continued)

#### Movement in the provision for doubtful debts:

As of 31 December 2008, trade receivables of RUR 44,227 thousand (2007: RUR 45,468 thousand) were impaired and provided for. The amount of the provision was RUR 38,103 thousand at 31 December 2008 (2007: RUR 43,563 thousand). It was assessed that a portion of the receivables is expected to be recovered. Movements on the Group provision for impairment of these receivables are as follows:

	As at 31 December 2008	As at 31 December 2007
<b>Balance at beginning of the year</b>	<b>43,563</b>	<b>90,362</b>
Impairment losses recognised on receivables	19,997	9,267
Amounts written off as uncollectible	(16,762)	(49,548)
Amounts recovered during the year	(8,695)	(6,518)
<b>Balance at end of the year</b>	<b>38,103</b>	<b>43,563</b>

In determining the recoverability of a trade receivable, the Group considers any change in the credit quality of the trade receivable from the date credit was initially granted up to the reporting date. The concentration of credit risk is limited due to the customer base being large and unrelated. Accordingly, management believes that there is no further credit provision required in excess of the allowance for doubtful debts.

#### Ageing of impaired trade and other receivables:

	As at 31 December 2008	As at 31 December 2007
45-90 days	2,799	-
90-180 days	9,814	253
180-365 days	4,368	5,085
1 year – 3 years	2,524	21,231
Over 3 years	18,598	16,994
<b>Total</b>	<b>38,103</b>	<b>43,563</b>

### 22. OTHER PREPAID AND RECOVERABLE TAXES

	As at 31 December 2008	As at 31 December 2007
Value added tax, net of output VAT	370,091	1,009,304
<b>Total</b>	<b>370,091</b>	<b>1,009,304</b>

### 23. CASH AND CASH EQUIVALENTS

	As at 31 December 2008	As at 31 December 2007
Current accounts, including:		
RUR-denominated	61,117	82,086
USD-denominated	123,656	89,270
EUR-denominated	38,545	34,344
Letters of credit	-	241,854
Deposits RUR-denominated	70,000	-
Deposits EUR-denominated	30,252	-
Other cash and cash equivalents	1,060	7,651
<b>Total</b>	<b>324,630</b>	<b>455,205</b>

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 24. SHARE CAPITAL AND ADDITIONAL PAID IN CAPITAL

	As at 31 December 2008 '000 shares	As at 31 December 2007 '000 shares
<b>Authorised number of shares</b>		
Ordinary shares at par value of RUR 1 each	26,785,114	2,505,114
Preferred shares at par value of RUR 1 each	119,596	119,596
<b>Total authorised shares</b>	<b>26,904,710</b>	<b>2,624,710</b>
<b>Issued and fully paid number of shares</b>		
Ordinary shares at par value of RUR 1 each	1,785,114	1,785,114
Preferred shares at par value of RUR 1 each	119,596	119,596
<b>Total issued and fully paid shares</b>	<b>1,904,710</b>	<b>1,904,710</b>
<b>Treasury shares</b>		
At the beginning of the year	648	3,300
Re-acquired by the Group	64	748
Re-issued from treasury shares	(712)	(3,400)
<b>At the end of the year</b>	<b>-</b>	<b>648</b>

Treasury shares are recorded as a deduction from issued and fully paid share capital at 31 December 2008 in the amount of RUR nil thousand (2007: RUR 7,712 thousands).

Share capital balance was adjusted for the effects of inflation in accordance with IAS 29 "Financial Reporting in Hyperinflationary Economies". The effect of such adjustments was recorded as Additional paid-in capital. The adjustment was determined using the inflation rate index from 1 September 1993, the date the Company was established as a joint stock company, through 31 December 2002.

On 16 April 2008, the shareholders of the Company approved an increase in the authorised number of ordinary shares up to 24.28 billion shares with a par value of RUR 1 each.

In accordance with Russian legislation, the Company distributes profits as dividends on the basis of financial statements prepared in accordance with Russian Accounting Rules. The statutory accounting reports of the Company are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit.

Group's ownership structure was as follows:

	% of ownership	
	As at 31 December 2008	As at 31 December 2007
OJSC "Svyazinvestneftekhim"	26.6%	26.6%
LLC "Telecom-Management"	50.2%	50.2%
Other legal entities and individuals	23.2%	23.2%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>

Common shareholders are allowed one vote per share. Preferred shares are non-voting. All common shares and preferred shares are eligible for distribution of earnings available in accordance with Russian statutory accounting regulations. Preferred shares holders are entitled to an annual payment of dividends in the amount equal to 25% of their par value. Shareholders of preferred shares have a preferred right to recover the par value of preferred shares in liquidation.

One share of the Company, held by the Government of Tatarstan, carries the right to veto certain decisions taken at shareholders' and Board of Directors' meetings. Decisions subject to veto include: increases and decreases in share capital, amendments to the Company's charter, liquidation or reorganization of the Group or any of its subsidiaries or branches and investments in other legal entities. This veto right is referred to as "Golden Share", and the term was extended indefinitely in 1998 by a decree of the President of Tatarstan and may be utilized by the Government of Tatarstan notwithstanding its voting rights are less than 25% of the Group.

The ultimate controlling party and ultimate parent is:

- OJSC "TAIF" ("TAIF"), which controls LLC "Telecom-Management".

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 25. LONG-TERM BORROWINGS

	As at 31 December 2008	As at 31 December 2007
Banks:		
USD denominated fixed rate	2,316,781	2,175,481
RUR denominated fixed rate	7,634,287	3,943,462
USD denominated floating rate	4,212,948	2,710,936
EUR denominated floating rate	3,455,833	3,486,116
RUR denominated floating rate	605,448	597,334
Non-convertible bonds (loan participation notes) fixed rate	5,918,710	4,987,447
<b>Total long-term borrowings</b>	<b>24,144,007</b>	<b>17,900,776</b>
Less: Current portion repayable within one year and shown under short-term borrowings (refer to Note 27)	(6,659,227)	(1,166,312)
Less: Non-convertible bonds (loan participation notes) with covenants breach (refer to Note 27)	(5,843,174)	(4,987,447)
Less: Obligations under agreements with covenants breach and cross-default event (refer to Notes 27 and 38)	(10,693,257)	-
<b>Net long-term borrowings</b>	<b>948,349</b>	<b>11,747,017</b>

The interest rates per annum on these long-term borrowings vary as follows:

	As at 31 December 2008	As at 31 December 2007
Banks:		
USD denominated fixed rate	6.36 to 7.83%	6.83% to 7.9%
RUR denominated fixed rate	8.5% to 13.5%	9.0% to 14%
	LIBOR plus 0.75% to	LIBOR
USD denominated floating rate	LIBOR plus 4.5%, Cost of Funds plus 2.5%	plus 0.75% to LIBOR plus 2.85%
	EURIBOR plus 0.4% to	EURIBOR
EUR denominated floating rate	EURIBOR plus 1.25%	plus 0.4% to EURIBOR plus 2.75%
	MOSPRIME plus	MOSPRIME plus
RUR denominated floating rate	2.0%	2.0%

As at 31 December 2008, long-term borrowings totalling RUR 9,297,566 thousand (2007: RUR 6,616,851 thousand) are secured by the pledge of equipment with the carrying value of RUR 4,653,606 thousand (2007: RUR 2,379,222 thousand), by the pledge of finished goods amounting RUR 200,585 thousand and by the pledge of contract revenue amounting RUR 1,220,000 thousand (2007: nil).

At 31 December 2008 the contractual undiscounted maturity profile for fixed rate borrowings is calculated using the applicable fixed interest rate and for variable rate borrowings is calculated using interest rates in effect at 31 December 2008 are as follows:

	Less than 1 year	Between 1 and 5 years	Over 5 years	Total
Banks:				
USD denominated fixed rate	-	-	-	-
RUR denominated fixed rate	-	899,913	-	899,913
USD denominated floating rate	-	195,281	-	195,281
EUR denominated floating rate	-	-	-	-
RUR denominated floating rate	-	-	-	-
Non-convertible bonds (loan participation notes)	-	-	-	-
	-	<b>1,095,194</b>	-	<b>1,095,194</b>



# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 25. LONG-TERM BORROWINGS (continued)

At 31 December 2007 the contractual undiscounted maturity profile for fixed rate borrowings is calculated using the applicable fixed interest rate and for variable rate borrowings is calculated using interest rates in effect at 31 December 2007 are as follows:

	Less than 1 year	Between 1 and 5 years	Over 5 years	Total
Banks:				
USD denominated fixed rate	-	1,541,455	1,023,313	2,564,768
RUR denominated fixed rate	-	3,883,975	1,348,524	5,232,499
USD denominated floating rate	-	2,547,614	19,944	2,567,558
EUR denominated floating rate	-	2,143,381	1,453,291	3,596,672
RUR denominated floating rate	-	716,422	-	716,422
	-	<b>10,832,847</b>	<b>3,845,072</b>	<b>14,677,919</b>

#### Breach of loan agreements

As of 31 December 2008 the Group had breached the financial ratio covenants contained in the Loan Participation Notes agreement and certain other Loan agreements. Due to the breach of these financial ratio covenants, the banks are contractually entitled to demand early repayment of the outstanding amount. Accordingly, the full amounts due under these agreements as of 31 December 2008 have been recorded as a current liability. As a result of the default event described in Note 38, other borrowings with cross-default terms have also been recorded as a current liability. The Group is currently in negotiations with its lenders to refinance or restructure its current obligations and obtain a waiver and amend its covenants. For details refer to Note 5.

### 26. OBLIGATIONS UNDER FINANCE LEASES

	As at 31 December 2008	As at 31 December 2007
<b>Minimum lease payments</b>		
Due within one year	339,255	180,275
Due later than one year and not later than five years	631,478	96,416
<b>Total future lease payments</b>	<b>970,733</b>	<b>276,691</b>
Less: future finance charges	(138,173)	(21,888)
<b>Present value of minimum lease payments</b>	<b>832,560</b>	<b>254,803</b>
Less: current portion of finance lease obligations (refer to Note 29)	(280,983)	(163,444)
<b>Non-current finance lease obligations</b>	<b>551,577</b>	<b>91,359</b>

The Group has no right to sell or sub-lease the assets under the lease arrangements until transfer of ownership.

### 27. SHORT-TERM BORROWINGS

	As at 31 December 2008	As at 31 December 2007
RUR denominated fixed rate	1,107,993	2,088,426
USD denominated fixed rate	715,413	-
USD denominated floating rate	1,820,291	974,647
EUR denominated floating rate	145,644	124,986
RUR denominated floating rate	956,133	-
Non-convertible bonds (loan participation notes) with covenants breach fixed rate	5,843,174	4,987,447
Obligation under agreements with covenants breach and cross-default event (refer to Note 38)	10,693,257	-
Current portion of long-term borrowings repayable within one year	6,659,227	1,166,312
<b>Total</b>	<b>27,941,132</b>	<b>9,341,818</b>

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Russian roubles)

### 27. SHORT-TERM BORROWINGS (continued)

Loan participation notes in the amount of USD 200,000 thousand, bearing interest at 9.25%, due on 30 October 2011 issued by Kazanorgsintez S.A., special purpose entity, on a limited recourse basis for the sole purpose of funding a loan to the Company. The notes are fully and unconditionally guaranteed by the Company. Interest payments on the notes are due semi-annually in April and October of each year.

The interest rates per annum on the borrowings vary as follows:

	As at 31 December 2008	As at 31 December 2007
RUR denominated fixed rate	6.5% to 19.0%	2% to 14%
USD denominated fixed rate	8.0% to 13.0%	-
USD denominated floating rate	LIBOR plus 1,5 % to LIBOR plus 2.25%, Cost of Funds plus 3%	LIBOR plus 1,5 % to LIBOR plus 2.25%
EUR denominated floating rate	Cost of Funds plus 2.25%	EURIBOR plus 2.75%
RUR denominated floating rate	Cost of Funds plus 2.5%	-
Non-convertible bonds	9.25%	9.25%

As at 31 December 2008, short-term borrowings totaling RUR 1,262,783 thousand (2007: nil) are secured by the pledge of equipment with the carrying value of RUR 2,358,639 thousand (2007: nil).

At 31 December 2008 the contractual undiscounted maturity profile for fixed rate borrowings is calculated using the applicable fixed interest rate and for variable rate borrowings is calculated using interest rates in effect at 31 December 2008 are as follows:

	Less than 1 month	1 to 3 months	3 month to 1 year	Total
Banks:				
RUR denominated fixed rate	124,280	126,561	916,898	1,167,739
USD denominated fixed rate	6,694	720,883	-	727,577
USD denominated floating rate	14,328	1,821,841	14,045	1,850,214
EUR denominated floating rate	1,637	96,725	48,774	147,136
RUR denominated floating rate	18,840	974,186	-	993,026
Non-convertible bonds fixed rate				5,843,174
Obligation under agreements with covenants breach and cross-default event (refer to Note 38)				10,693,257
Current portion of long-term borrowings	852,358	499,821	5,499,861	6,852,040
<b>Total</b>	<b>1,018,137</b>	<b>4,240,017</b>	<b>6,479,578</b>	<b>28,274,163</b>

At 31 December 2007 the contractual undiscounted maturity profile for fixed rate borrowings is calculated using the applicable fixed interest rate and for variable rate borrowings is calculated using interest rates in effect at 31 December 2007 are as follows:

	Less than 1 month	1 to 3 months	3 month to 1 year	Total
Banks:				
RUR denominated fixed rate	431,176	761,394	907,538	2,100,108
USD denominated floating rate	574	289,632	708,968	999,174
EUR denominated floating rate	443	83,550	44,896	128,889
Non-convertible bonds fixed rate				4,987,447
Current portion of long-term borrowings	144,253	107,423	914,636	1,166,312
<b>Total</b>	<b>576,446</b>	<b>1,241,999</b>	<b>2,576,038</b>	<b>9,381,930</b>

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Russian roubles)

### 28. TRADE PAYABLES

At 31 December 2008 trade accounts payable primarily denominated in RUR includes payables on purchases of raw materials, energy, maintenance services, spare parts and consumables. The fair value of trade accounts payable approximates their carrying amounts.

The table below shows liabilities at 31 December 2008 by their remaining contractual maturity. The amounts disclosed in the maturity table are contractual undiscounted cash flows, including gross contract commitments. Foreign currency payments are translated using the spot exchange rate at the balance sheet date.

	As at 31 December 2008	As at 31 December 2007
Within 60 days	1,706,225	1,973,870
60-365 days	2,321,298	46,615
<b>Total</b>	<b>4,027,523</b>	<b>2,020,485</b>

### 29. OTHER PAYABLES AND ACCRUED LIABILITIES

	As at 31 December 2008	As at 31 December 2007
Dividends payable	780,515	603,014
Current portion of finance lease obligations (refer to Note 26)	280,983	163,444
Wages and salaries payable	255,976	248,006
Deferred income	4,259	5,758
Other payables and accrued liabilities	25,975	58,337
<b>Total</b>	<b>1,347,708</b>	<b>1,078,559</b>

Dividends payable are due for payment before 16 April 2009 (2007: dividends payable are due for payment before 15 June 2008).

### 30. OTHER TAXES PAYABLE

	As at 31 December 2008	As at 31 December 2007
Property tax	40,931	39,953
Land tax	40,033	39,200
Personal income tax	17,485	27,209
Unified social tax	8,449	29,768
Other taxes	5,593	15,460
<b>Total</b>	<b>112,491</b>	<b>151,590</b>

### 31. (LOSS)/EARNINGS PER SHARE

Basic earnings per share	2008	2007
Weighted average number of ordinary shares outstanding (thousands)	1,785,114	1,785,114
Adjusted for weighted average number of treasury shares (thousands)	(96)	(873)
Weighted average number of ordinary shares in issue (thousands)	1,785,018	1,784,241
(Loss)/profit for the year attributable to the Group's equity holders	(2,955,417)	2,552,980
Less: after-tax amount of preferred dividends	(29,899)	(29,899)
<b>Basic and diluted (loss)/earnings per share (RUR)</b>	<b>(1.67)</b>	<b>1.42</b>

The Group does not have shares with diluting effect.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Russian roubles)

### 32. DIVIDENDS

	As at 31 December 2008	As at 31 December 2007
Dividends declared in respect of the year ended 31 December 2006:		
- ordinary shares (RUR 0.3545 per share)	-	632,732
- preferred shares (RUR 0.25 per share)	-	29,899
Dividends declared in respect of the year ended 31 December 2007:		
- ordinary shares (RUR 0.4207 per share)	750,996	-
- preferred shares (RUR 0.25 per share)	29,899	-
<b>Total</b>	<b>780,895</b>	<b>662,631</b>

### 33. RECONCILIATION OF PROFIT BEFORE TAXATION TO CASH FLOWS FROM OPERATIONS

	2008	2007
<b>OPERATING ACTIVITIES:</b>		
<b>(Loss)/profit before income tax</b>	<b>(3,772,391)</b>	<b>3,387,658</b>
Adjustments for:		
Depreciation and amortisation	1,818,478	1,244,799
Loss/(income) from investments and associates, net	51,282	(58,380)
Change in provision for doubtful debts	11,302	2,749
Change in obsolescence provision	284,694	(13,401)
Loss on disposal of property, plant and equipment	27,540	27,600
Finance costs, net	1,226,935	339,024
Foreign exchange loss/(gain), net	2,982,189	(542,681)
<b>Operating cash flows before working capital changes</b>	<b>2,630,029</b>	<b>4,387,368</b>
Decrease in trade and other receivables	178,168	402,408
Decrease/(increase) in taxes recoverable and prepaid, other than income tax	625,107	(592,902)
Increase in inventories	(1,203,513)	(803,427)
Increase/(decrease) in trade payables	2,068,617	(193,375)
Decrease in advances received from customers	(562,554)	(525,246)
(Decrease)/Increase in other current liabilities	(425,592)	15,038
Decrease in other taxes payable	(39,069)	(111,009)
<b>Net cash inflow from operations</b>	<b>3,271,193</b>	<b>2,578,855</b>

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Russian roubles)

### 34. RELATED PARTIES

Related parties of the Group include two shareholders (OJSC "Svyazinvestneftekhim" and LLC "Telecom-Management"), associates, entities under common control and under members of key management personnel. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Transactions with shareholders, associates and other related parties are in the ordinary course of business with terms and conditions similar to transactions with third parties.

Included in financial statements are the following transactions and balances with shareholders:

	<u>2008</u>	<u>2007</u>
Sales of goods and services	1,544	63,813
TAIF OJSC	1,544	63,813
Purchase of goods and services	30,484	25,703
TAIF OJSC	30,484	25,703
Dividends paid including:	518,780	217,466
Telekom-Management LLC	338,956	140,605
Svyazinvestneftekhim JSC	179,824	76,861
Re-issuing of treasury shares	8,978	48,012
Telekom-Management LLC	8,978	48,012
	<u>As at</u>	<u>As at</u>
	<u>31 December</u>	<u>31 December</u>
	<u>2008</u>	<u>2007</u>
Trade accounts receivables and advances given	-	554
TAIF OJSC	-	554
Trade accounts payables and advances received	9,917	2,026
TAIF OJSC	9,917	2,026
Dividends payable including:	615,911	518,780
Telekom-Management LLC	402,526	338,956
Svyazinvestneftekhim JSC	213,385	179,824

Included in financial statements are the following transactions and balances with associated companies:

	<u>2008</u>	<u>2007</u>
Sales of goods and services	274	-
	<u>As at</u>	<u>As at</u>
	<u>31 December</u>	<u>31 December</u>
	<u>2008</u>	<u>2007</u>
Trade accounts receivables and advances given	2,289	-
Trade accounts payables and advances received	18	-

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 34. RELATED PARTIES (continued)

Included in financial statements are the following transactions and balances with other related parties which include entities under common control and under control of significantly influencing shareholders:

	<u>2008</u>	<u>2007</u>
Sales of goods and services including:	680,446	699,798
<i>Nizhnekamskneftekhim JSC</i>	261,869	6,425
<i>NKNKH-Service LLC</i>	165,935	558,589
<i>Karsar LLC</i>	165,722	67,326
<i>Neftekhimsevilen JSC</i>	40,363	45,731
<i>Other companies</i>	46,557	21,727
Purchase of goods and services including:	9,590,477	7,953,201
<i>Nizhnekamskneftekhim JSC</i>	4,251,159	3,261,072
<i>Tatenergo JSC</i>	3,159,962	2,215,597
<i>PSO Kazan LLC</i>	1,836,978	2,237,116
<i>Taif-NK JSC</i>	121,894	105,244
<i>Taif-ST LLC</i>	86,080	1,027
<i>Karsar LLC</i>	47,335	20,269
<i>NKNKH-Service LLC</i>	23,457	56,523
<i>MKB Avers LLC</i>	17,168	20,581
<i>Other companies</i>	46,444	35,772
Interest received	24	221
<i>MKB Avers LLC</i>	24	221
Interest accrued	7,375	790
<i>MKB Avers LLC</i>	7,375	790
Dividends paid	1	2
<i>Taif-Invest LLC</i>	1	2
Dividends received	1,624	-
<i>Taif-Invest LLC</i>	1,624	-
	<b>As at</b>	<b>As at</b>
	<b>31 December 2008</b>	<b>31 December 2007</b>
Cash and cash equivalents	1,060	83,955
<i>MKB Avers LLC</i>	1,060	83,955
Trade accounts receivables and advances given including:	52,491	287,975
<i>PSO Kazan LLC</i>	25,986	28
<i>Nizhnekamskneftekhim JSC</i>	7,493	182,245
<i>Neftekhimsevilen JSC</i>	7,368	7,967
<i>Tatenergo JSC</i>	2,655	39,095
<i>NKNKH-Service LLC</i>	392	48,310
<i>Other companies</i>	8,597	10,330
Trade accounts payables and advances received	1,813,654	332,510
<i>Nizhnekamskneftekhim JSC</i>	946,402	-
<i>PSO Kazan LLC</i>	731,061	282,408
<i>Taif-ST LLC</i>	99,650	187
<i>Taif-NK JSC</i>	20,765	18,971
<i>Other companies</i>	15,776	30,944
Loans and borrowings	107,501	15,720
<i>MKB Avers LLC</i>	107,501	15,720

Key management compensation for the year ended 31 December 2008 amounted to RUR 65,291 thousand (2007: RUR 55,494 thousand) and included salaries and bonuses to employees of the Group and remuneration to members of Board of Directors and related social security contributions.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 35. COMMITMENTS AND CONTINGENCIES

#### Capital commitments

The Group does not have any capital expenditures upon contracted obligations regarding construction or purchase of property or equipment as the investment programme has been interrupted due to the worldwide economic slowdown (2007: RUR 7.7 billion, including RUR 1.1 billion of contracted commitments).

#### Litigation

There is no unresolved tax litigation at 31 December 2008 (2007: RUR 74,131 thousand).

The Group has been and continues to be the subject of other legal proceedings and adjudications from time to time, none of which has had, individually or in the aggregate, a material adverse impact on the Group. Management believes that the resolution of any ongoing legal proceedings will not have a material impact on the Group's financial position or operating results.

#### Russian taxation contingencies

The taxation system in the Russian Federation is at a relatively early stage of development, and is characterised by numerous taxes, frequent changes and inconsistent enforcement at federal, regional and local levels.

The Government of the Russian Federation has commenced a revision of the Russian tax system and passed certain laws implementing tax reform. The new laws reduce the number of taxes and overall tax burden on businesses and simplify tax laws. However, these new tax laws continue to rely heavily on the interpretation of local tax officials and fail to address many existing problems. Many issues associated with the practical application of new legislation are unclear and complicate the Group's tax planning and related business decisions.

In terms of Russian tax legislation, authorities have a period of up to three years to re-open tax declarations for further inspection. Changes in the tax system that may be applied retrospectively by authorities could affect the Group's previously submitted and assessed tax declarations.

While management believes that it has adequately provided for tax liabilities based on its interpretation of current and previous legislation, the risk remains that tax authorities in the Russian Federation could take differing positions with regard to issues of interpretation. This uncertainty may expose the Group to additional taxation, fines and penalties that could be significant.

With regard to matters where practice concerning payment of taxes is unclear, management estimated possible tax exposures at 31 December 2008 to be approximately RUR 163,497 thousand (2007: RUR 73,389 thousand).

#### Russian Federation risk

As an emerging market, the Russian Federation does not possess a fully developed business and regulatory infrastructure including stable banking and judicial systems, which would generally exist in a more mature market economy. The economy of the Russian Federation is characterized by a currency that is not freely convertible outside of the country, currency controls, low liquidity levels for debt and equity markets, and continuing inflation. As a result, operations in the Russian Federation involve risks that are not typically associated with those in more developed markets.

Stability and success of Russian economy and the Group's business mainly depends on the effectiveness of economic measures undertaken by the government as well as the development of legal and political systems.

#### Environmental matters

The Group's management believes that it is in compliance with all current existing environmental laws and regulations of the Russian Federation. However, environmental laws and regulations continue to evolve. The Group is unable to predict the timing or extent to which those environmental laws and regulations may change. Such change, if it occurs, may require that the Group modernize technology to meet more stringent standards or start to provide for costs to rehabilitate the environment.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

---

### 35. COMMITMENTS AND CONTINGENCIES (continued)

#### Russian insurance environment

The Russian insurance industry is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available in Russia.

The Group maintains insurance cover for major production assets including insurance cover for damage related to explosion or environmental damage arising from accidents on the Group's property or related to the Group's operations. The Group does not have coverage for business interruption. Management believes that the existing level of insurance coverage addresses all major risks which could have a material effect on the Group's operations and financial position.

### 36. FINANCIAL RISK MANAGEMENT

#### Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and price risk), credit risk and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

Risk management is carried out by a central treasury department (Group treasury) under policies approved by the board of directors. Group treasury identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units.

#### Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. See Note 2 for further discussion of the impact of the current economic environment on the Group's capital structure.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The capital structure of the Group consists of debt which includes the borrowings disclosed in Notes 25 and 27, cash and cash equivalents in Note 23 and equity attributable to equity holders of the parent, comprising issued capital as disclosed in Note 24, reserves and retained earnings.

Consistent with others in the industry, the Group monitors capital on the basis of the debt to EBITDA ratio. This ratio is calculated as the ratio of debt as proportion of earnings before interest, taxes, depreciation and amortisation. The Group did not comply with externally imposed restrictions on the ratio of net debt to EBITDA. Refer to Note 5.

#### Major classes of financial instruments

The following table sets out the carrying amount of the Group's financial instruments per categories at the following dates:

	<u>As at</u> <u>31 December 2008</u>	<u>As at</u> <u>31 December 2007</u>
<b>Financial Assets</b>		
Cash and cash equivalents	324,630	455,205
Trade and other accounts receivable	864,305	754,526
Other financial assets	52,675	52,100
Investments in associates	2,560	24,789
<b>Total</b>	<b><u>1,244,170</u></b>	<b><u>1,286,620</u></b>



# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Russian roubles)

### 36. FINANCIAL RISK MANAGEMENT (continued)

#### Major classes of financial instruments (continued)

	As at 31 December 2008	As at 31 December 2007
<b>Financial Liabilities</b>		
Finance lease liabilities	832,560	254,803
Long-term borrowings	948,349	11,747,017
Short-term borrowings	27,941,132	9,341,818
Trade accounts payable	4,027,523	2,020,485
Other payables and accrued liabilities	806,490	661,351
<b>Total</b>	<b>34,556,054</b>	<b>24,025,474</b>

#### Liquidity risk management

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying businesses, Group treasury maintains flexibility in funding by maintaining availability under committed credit lines.

Liquidity risk is the risk that the Group will not be able to settle all liabilities as they are due. The Group manages its liquidity risk through a combination of short-term and long-term financing and self generated funds.

At 31 December 2008 the Group had credit facilities for the management of its day to day liquidity requirements available in the amount RUR 3,360,206 thousands (2007: RUR 2,894,958 thousands).

The summaries of maturity profile of the Group's financial liabilities at 31 December 2008 and 2007 on contractual payments are presented in Notes 25, 26 and 27.

#### Foreign currency risk management

Currency risk is the risk that the financial results of the Group will be adversely impacted by changes in exchange rates to which the Group is exposed. The Group undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise.

The Group is exposed to currency risk in that a significant portion of long and short term borrowings are denominated in foreign currencies. The Group management controls this risk by aligning the foreign currency borrowings with expected currency sales proceeds.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the reporting date are as follows:

	Liabilities		Assets	
	As at 31 December 2008	As at 31 December 2007	As at 31 December 2008	As at 31 December 2007
USD denominated	(15,380,793)	(11,210,974)	195,327	365,957
EUR denominated	(4,188,348)	(3,730,661)	129,223	41,630

#### Foreign currency sensitivity analysis

The Group is mainly exposed to USD and EUR.

The following table details the Group's sensitivity to a 33% (10% for 2007) increase and decrease in RUR against US dollar and 27% (10% for 2007) against Euro. The above estimates are based on development of exchange rates during 2008 and beginning of 2009. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a relevant change in foreign currency rates. A positive number below indicates an increase in profit and equity where RUR strengthens against the relevant currency. For a similar weakening of RUR against the relevant currency, there would be an equal and opposite impact on the profit, and the balances below would be negative.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 36. FINANCIAL RISK MANAGEMENT (continued)

#### Foreign currency risk management (continued)

##### Foreign currency sensitivity analysis (continued)

	USD Impact		EUR Impact	
	2008	2007	2008	2007
	33%	10%	27%	10%
Effect on profit and loss and equity	5,026,350	1,084,502	1,094,500	368,903

This is mainly attributable to the exposure outstanding on USD and EUR borrowings at year end in the Group.

The Group's sensitivity to foreign currency has increased during the current period mainly due to revaluation of USD denominated borrowings and increase volatility of the USD against the RUR.

#### Interest rate risk management

The Group is exposed to interest rate risk as entities in the Group borrow funds at both fixed and floating interest rates. The risk is managed by the Group by maintaining an appropriate mix between fixed and floating rate borrowings. The Group also has the possibility of early redemption of the contracts without significant costs.

##### Interest rate sensitivity analysis

The sensitivity analyses below have been determined based on the exposure to interest rates for non-derivative instruments at the balance sheet date. For floating rate liabilities, the analysis is prepared assuming the amount of liability outstanding at the balance sheet date was outstanding for the whole year. A 100 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

If interest rates had been 100 basis points higher/ lower and all other variables were held constant, the Group's profit before income tax for the year ended 31 December 2008 and equity at 31 December 2008 would decrease/ increase by RUR 110,446 thousand (2007 - decrease/ increase by RUR 77,591 thousand). This is mainly attributable to the Group's exposure to interest rates on its variable rate borrowings.

The Group's sensitivity to interest rates has increased during the current period mainly due to the increase in variable rate loans and borrowings.

#### Credit risk management

Credit risk refers to the risk that counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss from defaults. New customers are dealt only on 100% advances terms. The Group uses available financial information and its own trading records to rate its major customers. The Group's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties.

The Group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The Group defines counterparties as having similar characteristics if they are related entities. Concentration of credit risk did not exceed 5% of gross monetary assets at any time during the year.

Cash is placed in financial institutions, which are considered at the time of the deposit to have minimal risk of default.

Credit risk is managed on a Group basis. For wholesale customers there is no independent rating and therefore Group assesses the credit quality of the customer, taking into account its financial position, past experience and other factors. The following ratings have been assigned to Groups' financial assets:

Rating A – history of business relations more than one year, no creditworthiness difficulties;

Rating B – history of business relations more than one year, potential creditworthiness difficulties are anticipated and

Rating C – others, credit worthiness difficulties are anticipated.

# KAZANORGSINTEZ GROUP

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (in thousands of Russian roubles)

### 36. FINANCIAL RISK MANAGEMENT (continued)

#### Credit risk management (continued)

	Rating "A"	Rating "B"	Rating "C"
<b>At 31 December 2008</b>			
Cash and cash equivalents	324,630		
Trade accounts receivable and other receivables	858,182	6,123	
<b>At 31 December 2007</b>			
Cash and cash equivalents	455,205		
Trade accounts receivable and other receivables	752,621	1,905	

Management does not expect any losses from non-performance by these counterparties, other than those amounts already provided for.

The maximum exposure to credit risk comprises the carrying amount of trade and other receivables totalling RUR 864,305 thousand (2007: RUR 754,526 thousand) and cash and cash equivalents totalling RUR 324,630 thousand (2007: RUR 455,205 thousand).

#### Fair value of financial instruments

The fair values of financial assets and financial liabilities are determined as follows:

- The fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets is determined with reference to quoted market prices;
- The fair value of other financial assets and financial liabilities is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments.

Management believes that the carrying values of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate their fair values.

### 37. INVESTMENTS IN SUBSIDIARIES

The Company's ownership interest in consolidated entities is as follows:

Subsidiaries	Nature of business	% of ownership	
		As at 31 December 2008	As at 31 December 2007
<b>Incorporated in Russian Federation</b>			
OJSC "Spetsneftekhimmontazh"	Repair & Maintenance	-	100
LLC "Tatkhimremont"	Repair & Maintenance	100	100
LLC "Trade House Orgsintez"	Trading	-	70
LLC "Kolos-Sintez" (refer to Note 18)	Agriculture	-	51
LLC "DK Khimikov"	Entertainment	100	100
<b>Incorporated in Hungary</b>			
LLC "Elmer"	Trading	50	50
<b>Special purpose entity</b>			
<b>Incorporated in Luxembourg</b>			
Kazanorgsintez S.A.	Financing	-	-

## **KAZANORGSINTEZ GROUP**

### **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

*(in thousands of Russian roubles)*

---

#### **37. INVESTMENTS IN SUBSIDIARIES (continued)**

The Group does not own a majority of the voting shares of LLC Elmer. However, management believes that the Group has the power to govern the financial and operating policies of this entity so as to obtain benefits from their activities through significant operational influence and accordingly LLC Elmer is considered as a subsidiary and consolidated. The Group exercises control over LLC Elmer through supplying the majority of goods for resale to this entity.

In July 2008 the Group disposed of its share in subsidiary entity LLC "Trade House Orgsintez" resulted from its bankruptcy.

In September 2008 the Group disposed of its share in subsidiary entity OJSC "Spetsneftekhimmontazh" resulted from its bankruptcy.

In September 2008 the Group reclassified its share in subsidiary entity LLC "Kolos-Sintez" from subsidiaries to associates resulted from enlargement of its share capital (refer to Note 18).

#### **38. EVENTS AFTER THE BALANCE SHEET DATE**

The Group has been included in the list of Russian companies approved for assistance from the Russian Federal Government Commission on Sustainable Development of the Russian Economy.

In May 2009 the Group received a notice from one of its lenders demanding immediate repayment of loans totalling RUR 2,523,438 thousand, including interest payable. The lender was entitled to make the demand as it arose on a default that occurred on 12 May 2009. The Group did not make any payment and is working with all of its lenders collectively to restructure its borrowings.