TRANSNEFT

CONSOLIDATED FINANCIAL STATEMENTS
PREPARED IN ACCORDANCE WITH
INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)
AND INDEPENDENT AUDITORS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2017

2017 YEAR OF ECOLOGY

CONTENT

Independent Auditors' Report

To the Shareholders and Board of Directors of Transneft

Opinion

We have audited the consolidated financial statements of Transneft (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the independence requirements that are relevant to our audit of the consolidated financial statements in the Russian Federation and with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the requirements in the Russian Federation and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Audited entity: Transneft

Entered in the United State Register of Legal Entities No 1027700049486.

Moscow, Russia

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

Entered in the Unified State Register of Legal Entities, Registration No. 1027700125628.

Member of the Self-regulated organization of auditors "Russian Union of auditors" (Association). The Principal Registration Number of the Entry in the Register of Auditors and Audit Organisations: No. 11603053203.

Valuation of investments in associates and jointly controlled entities

Please refer to the Note 7 in the consolidated financial statements.

The key audit matter	How the matter was addressed in our audit
As of the reporting date the Group has significant investments in PJSC "NCSP" and OOO "NMT", which are accounted for by the equity method. These investments have been tested for impairment. Due to the inherent uncertainty involved in forecasting and discounting future cash flows, which form the basis of the assessment of recoverable amount, this is one of the key judgmental areas that our audit is concentrated on.	Our audit procedures included analysing the investees' budgets upon which the forecasts are based and testing the accuracy of the data used in the discounted cash flow model (including comparison of forecast and actual goods turnovers). We used our own internal valuation specialists who: — analyzed methodology used by the Group when preparing the model; — compared assumptions used by the Group to externally derived data (inflation, exchange rates and tax rate) as well as to our own assessments in relation to key inputs (terminal growth rate, expenses growth due to inflation and discount rate). We compared the recoverable amount of Group's investment to investee's market capitalization (where investee shares are publicly traded). We have also considered appropriateness and completeness of the disclosures in the consolidated financial statements regarding the assumptions used in the recoverable amount assessment.

Classification and accounting of the investment in closed combined mutual investment fund "Gazprombank – Finansoviy"

Please refer to the Note 7 in the consolidated financial statements.

The key audit matter	How the matter was addressed in our audit
In the reporting period the Group made a significant investment in closed combined mutual investment fund "Gazprombank – Finansoviy" (hereinafter – the "Fund"). The investment was classified as a jointly controlled entity, which is accounted for using the equity method. Due to significant professional judgment applied in determination	Our audit procedures included: — analysis of the Group's strategy in relation to the Fund, planned investment structure and transactions performed by the Fund in the reporting period; — joint control analysis, including: — analysis of the ownership structure of the Fund;

of classification and accounting method for this investment, this is one of the key judgmental areas that our audit is concentrated on.	— analysis of foundation documents and management structure of the Fund to understand the decision making principles. We have also considered appropriateness and completeness of the disclosures in the consolidated financial statements regarding this investment.

Assessment of recoverable amount of property, plant and equipment

Please refer to the Note 6 in the consolidated financial statements.

The key audit matter	**How the matter was addressed in our audit**
As of the reporting date the Group has significant amount of property, plant and equipment which is accounted for at historical cost and which has been tested for impairment due to identification of triggers for potential impairment. Due to the inherent uncertainty involved in forecasting and discounting future cash flows, which form the basis of the assessment of the recoverable amount, this is one of the key judgmental areas that our audit is concentrated on.	Our audit procedures included: — analysis of the appropriateness of the cash generating unit identification; — analysis of the budget upon which the forecasts are based and testing the accuracy of the data used in the discounted cash flow model (including comparison of forecast and actual oil turnovers); — analysis of the model sensitivity due to changes of key assumptions. We used our own internal valuation specialists who: — analyzed methodology used by the Group when preparing the model; — compared assumptions used by the Group to externally derived data (inflation, exchange rates and tax rate) as well as to our own assessments in relation to key inputs (expenses growth due to inflation, discount rate, etc.) We have also considered appropriateness and completeness of the disclosures in the consolidated financial statements regarding this matter.

Other Information

Management is responsible for the other information. The other information comprises the *Management's discussion and analysis of the Group's financial position and results of its operations,* but does not include the consolidated financial statements and our auditors' report thereon, which we obtained prior to the date of this auditors' report, and the *Annual report for 2017*, which is expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we have obtained prior to the date of this auditors' report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

— Identify and assess the risks of material misstatement of the (consolidated) financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the (consolidated) financial statements, including the disclosures, and whether the (consolidated) financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditors' report is:

Kim A. A.

JSC "KPMG"
Moscow, Russia

29 March 2018

АКЦИОНЕРНОЕ ОБЩЕСТВО ОГРН 1027700125628 КПМГ KPMG МОСКВА

TRANSNEFT
CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2017
(in millions of Russian roubles, if not stated otherwise)

ASSETS			
Non-current assets	**Notes**	**31 December 2017**	**31 December 2016**
Intangible assets		8,966	8,987
Property, plant and equipment	6	2,268,663	2,146,419
Available-for-sale financial assets		251	252
Investments in associates and jointly controlled entities	7	126,769	41,299
Receivables and prepayments, VAT assets	12	2,083	1,443
Other financial assets	10	23,096	32,738
Total non-current assets		**2,429,828**	**2,231,138**
Current assets			
Inventories	11	30,662	30,930
Receivables and prepayments	12	42,400	36,162
VAT assets		35,316	37,725
Current income tax prepayments		5,697	3,493
Financial assets at fair value through profit or loss	8	58,859	44,302
Other financial assets	10	208,768	308,409
Cash and cash equivalents	13	76,162	74,586
Total current assets		**457,864**	**535,607**
Total assets		**2,887,692**	**2,766,745**
EQUITY AND LIABILITIES			
Equity			
Share capital	14	308	308
Share premium reserve	14	58,544	52,553
Merger reserve	14	(13,080)	(13,080)
Prepaid share reserve	14	-	5,991
Retained earnings		1,803,206	1,668,788
Attributable to the shareholders of Transneft		**1,848,978**	**1,714,560**
Non-controlling interests		1,776	1,795
Total equity		**1,850,754**	**1,716,355**
Non-current liabilities			
Loans and borrowings	15	579,180	592,505
Deferred income tax liabilities	16	47,120	46,416
Provisions for liabilities and charges	17	126,725	115,541
Trade and other payables	18	3,458	2,464
Total non-current liabilities		**756,483**	**756,926**
Current liabilities			
Loans and borrowings	15	109,730	109,047
Provisions for liabilities and charges	17	41,468	35,182
Trade and other payables	18	129,021	148,664
Current income tax payable		236	571
Total current liabilities		**280,455**	**293,464**
Total liabilities		**1,036,938**	**1,050,390**
Total equity and liabilities		**2,887,692**	**2,766,745**

Approved on 29 March 2018 by:

N.P. Tokarev President

ПУБЛИЧНОЕ АКЦИОНЕРНОЕ ОБЩЕСТВО «ТРАНСНЕФТЬ» РОССИЙСКАЯ ФЕДЕРАЦИЯ г. МОСКВА

The accompanying notes set out on pages 12 to 54 are an integral part of these consolidated financial statements

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

	Notes	Year ended 31 December 2017	Year ended 31 December 2016
Revenue	19	884,337	848,134
Operating expenses net of amortisation and depreciation	20	(476,062)	(439,917)
Operating profit before amortisation and depreciation		**408,275**	**408,217**
Amortisation and depreciation		(152,637)	(128,523)
Operating profit		**255,638**	**279,694**
Other expenses		(13,686)	(7,456)
Share of profit from associates and jointly controlled entities	7	15,847	19,519
Profit before income tax and finance income/(costs)		**257,799**	**291,757**
Finance income	21	109,177	290,908
Finance costs	21	(124,809)	(281,243)
Profit before income tax		**242,167**	**301,422**
Income tax expense	16	(50,362)	(68,515)
Profit for the reporting year		**191,805**	**232,907**
Other comprehensive income, net of income tax			
Items that may be reclassified to profit or loss			
Currency translation differences, net of income tax		41	(110)
Total items that may be reclassified to profit or loss, net of income tax		*41*	*(110)*
Items that will not be reclassified to profit or loss			
Remeasurement of net defined benefit plan obligation, net of income tax	17	537	2,431
Total items that will not be reclassified to profit or loss, net of income tax		*537*	*2,431*
Total other comprehensive income for the reporting year, net of income tax		**578**	**2,321**
Total comprehensive income for the reporting year		**192,383**	**235,228**
Profit attributable to			
Shareholders of Transneft		191,971	232,856
Non-controlling interests		(166)	51
Total comprehensive income attributable to			
Shareholders of Transneft		192,549	235,177
Non-controlling interests		(166)	51

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

	Notes	Year ended 31 December 2017	Year ended 31 December 2016
Cash flows from operating activities			
Cash receipts from customers		948,360	894,316
Cash paid to suppliers and employees, and taxes other than income tax		(606,686)	(583,057)
Interest paid		(46,220)	(46,246)
Income tax paid		(52,391)	(49,078)
Income tax refund		403	597
VAT and other taxes refund		87,559	105,582
Other cash flows used in operating activities		(3,924)	(4,544)
Net cash from operating activities		**327,101**	**317,570**
Cash flows from investing activities			
Purchase of property, plant and equipment		(306,880)	(321,603)
Proceeds from sale of property, plant and equipment		681	1,645
Interest received		22,429	22,147
Purchase of debt securities and placement of funds on deposit accounts		(416,364)	(562,015)
Proceeds from sale of debt securities and closure of deposit accounts		500,300	623,954
Acquisition of shares of associates and jointly controlled entities	7	(98,310)	(12,497)
Dividends received and other cash proceeds from associates and jointly controlled entities		28,485	2,031
Issuance and repayment of loans		(4,260)	(6,568)
Cash inflows as a result of disposal of entities	9	-	2,636
Other cash flows used in investing activities		(253)	(438)
Net cash used in investing activities		**(274,172)**	**(250,708)**
Cash flows from financing activities			
Repayment of loans and borrowings		(190,059)	(129,358)
Proceeds from loans and borrowings		197,020	79,207
Purchase of treasury shares	14	(1,106)	-
Sale of treasury shares	14	1,134	-
Dividends paid out	14	(58,159)	(12,801)
Acquisition of non-controlling interest		-	(19)
Other cash received from financing activities		22	61
Other cash used in financing activities		(35)	(9,600)
Net cash used in financing activities		**(51,183)**	**(72,510)**
Effects of exchange rate changes on cash and cash equivalents		**(170)**	**(12,479)**
Net increase / (decrease) in cash and cash equivalents		**1,576**	**(18,127)**
Cash and cash equivalents at the beginning of the year	13	**74,586**	**92,713**
Cash and cash equivalents at the end of the year	13	**76,162**	**74,586**

The accompanying notes set out on pages 12 to 54 are an integral part of these consolidated financial statements

TRANSNEFT
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2017
(in millions of Russian roubles, if not stated otherwise)

		Attributable to the owners of Transneft								
	Note	Share capital	Share premium reserve	Merger reserve	Treasury shares	Prepaid share reserve	Retained earnings	Total	Non-controlling interests	Total equity
Balance at 1 January 2016		308	52,553	(13,080)	-	-	1,446,470	1,486,251	1,705	1,487,956
Profit for the reporting year		-	-	-	-	-	232,856	232,856	51	232,907
Remeasurement of net defined benefit plan obligation, net of income tax	17	-	-	-	-	-	2,431	2,431	-	2,431
Currency translation differences, net of income tax		-	-	-	-	-	(110)	(110)	-	(110)
Total comprehensive income for the reporting year		-	-	-	-	-	235,177	235,177	51	235,228
Transactions with owners of the Company					-					
Distributions and contributions										
Prepayment for shares	14	-	-	-	-	5,991	-	5,991	-	5,991
Dividends : ordinary shares	14	-	-	-	-	-	(11,521)	(11,521)	-	(11,521)
preferred shares	14	-	-	-	-	-	(1,280)	(1,280)	-	(1,280)
Total distributions		-	-	-	-	5,991	(12,801)	(6,810)	-	(6,810)
Changes in ownership interests										
Acquisition of non-controlling interests without a change in control		-	-	-	-	-	(58)	(58)	39	(19)
Total changes in ownership interests		-	-	-	-	-	(58)	(58)	39	(19)
Total transactions with owners of the Company		-	-	-	-	5,991	(12,859)	(6,868)	39	(6,829)
Balance at 31 December 2016		308	52,553	(13,080)	-	5,991	1,668,788	1,714,560	1,795	1,716,355
Balance at 1 January 2017		308	52,553	(13,080)	-	5,991	1,668,788	1,714,560	1,795	1,716,355
Profit for the reporting year		-	-	-	-	-	191,971	191,971	(166)	191,805
Remeasurement of net defined benefit plan obligation, net of income tax	17	-	-	-	-	-	537	537	-	537
Currency translation differences, net of income tax		-	-	-	-	-	41	41	-	41
Total comprehensive income for the reporting year		-	-	-	-	-	192,549	192,549	(166)	192,383
Transactions with owners of the Company										
Distributions and contributions										
Placement of ordinary certified non-documentary shares	14	-	5,991	-	-	(5,991)	-	-	-	-
Purchase of treasury shares	14	-	-	-	(1,106)	-	-	(1,106)	-	(1,106)
Sale of treasury shares	14	-	-	-	1,106	-	28	1,134	-	1,134
Dividends : ordinary shares	14	-	-	-	-	-	(45,508)	(45,508)	-	(45,508)
preferred shares	14	-	-	-	-	-	(12,651)	(12,651)	-	(12,651)
Total distributions and contributions		-	5,991	-	-	(5,991)	(58,131)	(58,131)	-	(58,131)
Changes in ownership interests										
Disposal of subsidiary		-	-	-	-	-	-	-	147	147
Total changes in ownership interests		-	-	-	-	-	-	-	147	147
Total transactions with owners of the Company		-	5,991	-	-	(5,991)	(58,131)	(58,131)	147	(57,984)
Balance at 31 December 2017		308	58,544	(13,080)	-	-	1,803,206	1,848,978	1,776	1,850,754

The accompanying notes set out on pages 12 to 54 are an integral part of these consolidated financial statements

1 NATURE OF OPERATIONS

Public Joint Stock Company “Transneft” (hereinafter named the “Company”) was incorporated by the Resolution of the Council of Ministers - Russian Government dated 14.08.1993 № 810. The Company's registered office is located in Moscow, Russian Federation.

In July 2016 according to amendments made to the Civil Code of the Russian Federation, to the Unified state register of legal entities the name of the Company has been changed to Public Joint Stock Company “Transneft” (Transneft).

The Company and its subsidiaries (hereinafter - the "Group") as at 31 December 2017 operate the trunk oil pipeline system in the Russian Federation totalling 51,489 km and the oil products pipeline system in the Russian Federation, the Republic of Belarus and the Republic of Kazakhstan totalling 16,885 km. Its associate OOO LatRosTrans operates an oil products pipeline system in the Republic of Latvia interconnected with the general system.

During the year ended 31 December 2017, the Group transported 478 million tonnes of crude oil to domestic and export markets (as for the year ended 31 December 2016 – 483 million tonnes), which represents a substantial majority of the crude oil produced in the territory of the Russian Federation during that period, and 33.1 million tonnes of oil products (33.1 million tonnes as for the year ended 31 December 2016).

2 ECONOMIC ENVIRONMENT IN THE RUSSIAN FEDERATION

The Group’s operations are primarily located in the Russian Federation. Consequently, the Group is exposed to the economic and financial markets of the Russian Federation which display characteristics of an emerging market. Because the legal, tax and regulatory frameworks continue to develop and change the risk of ambiguous interpretations of their requirements exists.

The imposition of economic sanctions on Russian individuals and legal entities including the Company by the European Union, the United States of America and other countries, as well as, retaliatory sanctions imposed by the Russian government, has resulted in more volatile equity markets, and a significant tightening in the availability of credit. In particular, some Russian entities may be experiencing difficulties in accessing international equity and debt markets and may become increasingly dependent on Russian state banks to finance their operations. The longer term effects of recently implemented sanctions are difficult to determine.

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

3 BASIS OF PRESENTATION

The consolidated financial statements are prepared in accordance with, and comply with, International Financial Reporting Standards (“IFRS”).

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

During the year ended 31 December 2016 the Group changed the disclosure of the consolidated statement of profit or loss and other comprehensive income for more appropriate and clear presentation of results of its operations. As a result of this change Amortisation and depreciation and Other expenses are presented separately from Operating expenses. Other expenses include provisions not related to operating activity, result from disposal of subsidiaries, associates and jointly controlled entities, income from oil and oil products surplus, charity contributions, impairment provision of property, plant and equipment and other expenses.

Certain comparative amounts have been adjusted to conform with the current year's presentation.

The functional currency of each of the Group’s consolidated entities is the currency of the primary economic environment in which the entity operates. The functional currency of the Company and its principal subsidiaries including UP Zapad-Transnefteproduct, and the Group’s presentation currency, is the national currency of the Russian Federation - Russian Rouble (“RUB”).

The official US dollar (“USD”) to Russian Rouble (“RUB”) exchange rate as determined by the Central Bank of the Russian Federation (“CBR”) was 57.6002 and 60.6569 as at 31 December 2017 and 31 December 2016, respectively.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

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

Acquisitions of non-controlling interests are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognised as a result. Adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary.

Business combination under common control

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

Loss of control

When control of subsidiary is lost the Group ceases recognition of its assets and liabilities, as well as, relating to subsidiary non-controlling interests and other components of equity. If the Group retain part of the investment in the former subsidiary then such investment is recognised at fair value when control ceases. Subsequently, the investment is accounted for as associate (using the equity method) or as financial asset available for sale depending on the Group's influence on the entity.

Investments in associates and jointly controlled entities

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

Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity, either directly or indirectly, unless lack of ability to exercise significant influence can be demonstrated clearly.

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

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

Transactions eliminated on consolidation

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

Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items in a foreign currency that are measured based on historical cost are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising in translation are recognised in profit or loss, except for differences arising on the translation of available-for-sale equity instruments which are recognised in other comprehensive income.

Property, plant and equipment

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

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

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

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

Crude oil and oil products used for technical operation of the pipeline network (“linefill”) owned by the Group are treated as a separate component of the pipeline class of asset and are not depreciated as their residual values exceed carrying amounts.

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

Oil surpluses arising from stocktaking are recognised at market value and are recorded in inventory in the consolidated statement of financial position, and income from oil surplus is netted with other expenses which include charity expenses, made from the above specified income received, and recognised in Other expenses in the consolidated statement of profit or loss and other comprehensive income.

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

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

Leased assets

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Plant and equipment acquired by way of finance lease are stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at the inception of the lease, less accumulated depreciation and impairment losses. Each lease payment is allocated between the liability and finance charges so as to achieve a constant effective interest rate on the finance balance outstanding. The leased assets which assume the transfer of ownership are depreciated over their useful lives. Other leased assets are depreciated over the shorter of its useful life and the lease term.

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

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventories

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

Non-derivative financial instruments

Financial assets and liabilities

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

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

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

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

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

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

Available-for-sale financial assets

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

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

Held-to-maturity financial assets

If the Group has the positive intent and ability to hold to maturity debt securities that are quoted in an active market, then such financial assets are classified to held-to-maturity category. Held-to-maturity financial assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition they are measured at amortised cost using the effective interest method, less any impairment losses.

The Group is not permitted to classify any financial assets as held to maturity during the following two financial years and reclassifies the assets of this category as available-for-sale if the Group during the current financial year has sold or reclassified more than an insignificant amount of held-to-maturity investments before maturity other than sales or reclassifications that:

- are close to maturity or the financial asset's call date;
- occur after the Group has collected substantially all of the financial asset's original principal through scheduled payments or prepayments; or
- are attributable to an isolated event that is beyond the Group's control, is non-recurring and could not have been reasonable anticipated by the Group.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets measured at fair value through profit or loss

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

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

Loans and receivable

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Those assets are initially measured at fair value plus directly attributable transaction costs. After initial measurement loans and receivables are measured at amortised cost which is calculated based on the effective interest method less provision made for impairment.

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

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

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

Cash and cash equivalents

Cash and cash equivalents consist of cash in hand, call bank deposits, and highly liquid investments, which have original maturities of three months or less at the date of acquisition and which are subject to insignificant risk of fair value change.

Prepayments

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

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

VAT assets

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

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Loans and borrowings

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

Derivatives

Derivatives are initially recognised at fair value, relevant transaction expenses are recognised as profit or loss when incurred. Following initial recognition derivatives are measured at fair value with appropriate changes recognised directly in profit or loss for the period.

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

(a) in profit or loss if the fair value of the quoted price is confirmed for identical assets or liabilities in an active market (accounted for Level 1) or based on a valuation method, which uses only data from observable markets;
(b) as deferred loss or income to defer recognition of the difference between the fair value at initial recognition and the transaction price. After initial recognition, the Group recognizes the difference as the deferred gain or loss over the life of the financial instrument, but not later than the time when the estimate of its fair value can be made on fully observable market data, or the date of termination.

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

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

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

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

Income tax

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

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

Deferred income tax is provided for using the balance sheet liability method and is recognised for tax loss carried forward and temporary differences arising between the tax base of assets and liabilities and their carrying amounts in the consolidated financial statements.

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

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

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Provisions (including dismantlement provision)

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

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

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

Pension activities

State pension fund

The Group makes contributions to the State pension fund. Contributions to the State pension fund are recognised as expenses when accrued.

Pension liabilities

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

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

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

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

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

The Group operates its pension obligations, which are non-state pension provision (hereinafter - NPO), compulsory pension insurance (hereinafter - OPS), through its subsidiary JSC “NPF “TRANSNEFT”.

Insurance contracts

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

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investment contracts

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

Recognition and measurement of pension liabilities

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

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

Asset management agreements

For the investments into financial instruments made by the Group via the asset management agreements, there is no transfer of risk and benefits related to change in fair value of the investments. Thus, these financial instruments are recognised by the Group.

Site restoration provision

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

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

Revenue recognition

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

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

Revenue and costs under the construction contract are recognised as revenue and costs, respectively, to the extent the stages under the contract are completed as at the end of the reporting period. The percentage of completion is measured by comparing costs under the contract incurred to fulfil work as at the specific date against the aggregate costs under the contract.

Revenue represents the fair value of consideration received or receivable for the sale of goods and services in the normal course of business, net of discounts and value-added tax. Customs duties are reported separately as income and expenses in the consolidated financial statements.

Capitalisation of borrowing costs

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

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

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Capitalisation of borrowing costs includes capitalising foreign exchange differences relating to borrowings to the extent that they are regarded as an adjustment to interest costs. The exchange differences are capitalised as part of qualifying assets to the extent of the interest rate difference between borrowing costs that would be incurred if the entity borrowed funds in Russian roubles, and borrowing costs actually incurred on foreign currency borrowings.

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

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

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

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

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

Share capital and dividends

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

Dividends are recognised as a liability and deducted from other comprehensive income on the date on which they are approved at the annual general shareholders meeting. Dividends proposed at any time, and those approved between the reporting date and the date of issuing the consolidated financial statements, are disclosed in the consolidated financial statements.

New accounting standards

A number of new Standards, amendments to Standards and Interpretations become effective for annual periods from 1 January 2018, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the Group’s operations. The Group plans to adopt these pronouncements when they become effective.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 11 *Construction Contracts,* IAS 18 *Revenue* and IFRIC 13 *Customer Loyalty Programmes*.

At present the Group provides the following services: oil transportation, oil products transportation and export sales of crude oil. As per the Group preliminary assessment, the adoption of requirements of IFRS 15 would not have a material impact on recognition of revenue for these services.

The Group also renders services for technological connection to the trunk pipeline system and expansion of the throughput capacity of the trunk pipelines. These services are provided in accordance with contracts for technological connection and agreements for setting of long-term (agreed) tariffs for oil transportation via active parts of oil pipelines. Oil transport facilities constructed under such contracts become property of the Group and are further used for transportation of oil and oil products.

When financing is received through specific long-term (agreed) tariffs in accordance with IAS 18 *Revenue* revenue is recognised when transportation services are provided as revenue from transportation of oil and oil products. When financing is received by way of down payments in terms of agreements for connection to the trunk pipelines in accordance with effective IFRIC 18 *Transfer of Assets from Customers* revenue is recognised as assets construction costs are incurred as revenue for provision of services for connecting facilities to the trunk pipeline system, which is then included in other revenue.

Under IFRS 15 the Group has one separately identifiable performance obligation: provision of services for transportation of oil and oil products, thus revenue would be recognised only from these services. Revenue from technological connection to the trunk pipelines is not recognised as it is not a separate performance obligation provided to customers, but is a part of performance obligation for provision of services for transportation of oil and oil products.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Based on the Group's preliminary assessment, the impact of changes in accounting policies for contracts for technological connection to the trunk pipelines and for expansion of the throughput capacity of the trunk pipelines on equity as at 1 January 2018 would not be material. The actual impact of adopting the standard at 1 January 2018 may change because the new accounting policies are subject to change until the Group presents its first financial statements that include the date of initial application.

The Group intends to adopt IFRS 15 only to agreements which are not yet completed as at 1 January 2018. In relation to agreements already completed at this date exemption provided by the standard would be applied allowing not to recalculate such agreements. IFRS 15 would be adopted retrospectively recognising the combined effect of the first adoption at the date of initial application (i.e. from 1 January 2018). Thus, starting from interim financial statements for 2018, the Group would not adopt the IFRS 15 requirements to comparative period which would be presented in the statements.

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement.

Classification - Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). The standard eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale.

Based on the Group's preliminary assessment, the adoption of new classification requirements would not have a material impact on its accounting for trade receivables, loans, investments in debt securities and investments in equity securities. As at 31 December 2017, the Group had equity investments classified as available-for-sale, based on preliminary estimation their fair value does not significantly differ from their carrying value, and in accordance with IFRS 9, the Group would classify these investments as measured at fair value through profit or loss. Consequently, all fair value gains and losses will be reported in profit or loss.

Impairment - Financial assets and contract assets

In relation to impairment IFRS 9 introduces a new forward-looking 'expected credit loss' model which replaces the 'incurred loss' model in IAS 39.

In accordance with the Group's preliminary assessment it is unlikely that impairment losses would increase and become more volatile in the scope of the IFRS 9 impairment model.

Trade and other receivables, including contract assets

The estimated expected credit losses will be calculated based on actual credit loss experience and the Group's view of economic conditions over the expected lives of the receivables using the matrix approach.

The Group preliminary expects the application of IFRS 9 impairment requirements from January 1, 2018 would not result in significant increase of impairment loss recognised in accordance with IAS 39.

Debt securities

The Group controls changes in credit risk by tracking published external credit ratings.

To determine whether there has been a significant increase in credit risk at 1 January 2018 that has not been reflected in published ratings, the Group also reviews all quantitative and qualitative information available for the Group including changes in bond yields and, where available, CDS prices together with available press and regulatory information about issuers, as well as, additionally performs analysis based on historic experience and internal expert assessment of credit risk.

Default probabilities during 12 months after the reporting date and during the term of financial instruments are based on historical data supplied by Standard & Poors for each credit rating and are checked taking into account current bond yields and current CDS prices. Loss given default applied by the Group is determined based on presumed recovery rate. With the exception when a security is credit-impaired, in which case the estimate of loss is based on the instrument's current market price and original effective interest rate.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

On preliminary estimation of the Group the application of IFRS 9 impairment requirements as at 1 January 2018 would not have a material impact on the consolidated financial statements.

Deposits, cash and cash equivalents

As at 31 December 2017 deposits and cash and cash equivalents were mainly held with largest bank which have external credit ratings supplied by rating agency Moody's and other rating agencies and adjusted to the Moody's rating scale from Ba1 to Ba2.

The estimated impairment on deposits and cash and cash equivalents was calculated based on the 12-month expected loss basis and reflects the short maturities of the exposures. The Group considers that its deposits, cash and cash equivalents have low credit risk based on the external credit ratings of the counterparties, and application of IFRS 9 impairment requirements would not have a material impact on the consolidated financial statements.

The Group used a similar approach for assessment of ECLs for deposits, cash and cash equivalents to those used for debt securities.

Classification - Financial liabilities

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

The Group's assessment did not indicate any material impact regarding the classification of financial liabilities at 1 January 2018.

Disclosures

IFRS 9 will require extensive new disclosures, in particular about hedge accounting, credit risk and expected credit losses. The Group's assessment included an analysis to identify data gaps against current processes and the Group is in the process of implementing the system and controls changes that it believes will be necessary to capture the required data.

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 will generally be applied retrospectively, except as described below.

The Group plans to take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 generally will be recognised in retained earnings and reserves as at 1 January 2018.

IFRS 16 Lease

IFRS 16 introduces a single, on-balance lease sheet accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

IFRS 16 replaces existing leases guidance including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases—Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

The standard is effective for annual periods beginning on or after 1 January 2019. Early adoption is permitted for entities that apply IFRS 15 Revenue from Contracts with Customers at or before the date of initial application of IFRS 16.

The Group has not yet completed a detailed assessment of the potential impact of adopting IFRS 16 on its consolidated financial statements. The actual impact of applying IFRS 16 on the financial statements in the period of initial application will depend on future economic conditions, including the Group's borrowing rate at 1 January 2019, the composition of the Group's lease portfolio at that date, the Group's latest assessment of whether it will exercise any lease renewal options and the extent to which the Group chooses to use practical expedients and recognition exemptions.

The adoption of IFRS 16 is expected to have a significant effect on the consolidated financial statements of the Group relating to recognition of assets and liabilities for its operating leases of land and other production properties (Note 23).

In addition, the nature of expenses related to those leases will now change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities.

4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Transition

As a lessee, the Group can either apply the standard using a:

- retrospective approach; or
- modified retrospective approach with optional practical expedients.

The lessee applies the election consistently to all of its leases.

The Group plans to apply IFRS 16 initially on 1 January 2019, using the modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

When applying the modified retrospective approach to leases previously classified as operating leases under IAS 17, the lessee can elect, on a lease-by-lease basis, whether to apply a number of practical expedients on transition. The Group is assessing the potential impact of using these practical expedients.

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

- Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28;
- Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2);
- Transfers of Investment Property (Amendments to IAS 40);
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28);
- IFRIC 22 Foreign Currency Transactions and Advance Consideration;
- IFRIC 23 Uncertainty over Income Tax Treatments.

5 CRITICAL ESTIMATES IN APPLYING ACCOUNTING POLICIES

The preparation of consolidated financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the following notes:

Useful lives of property, plant and equipment

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

Should the useful life of the crude oil and oil product pipelines increase by 10 years, the profit for the year ended 31 December 2017 would be RUB 8,480 higher as a result of decrease of depreciation expense.

Impairment testing of investment in associates and jointly controlled entities

Further information is disclosed in Note 7.

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

6 PROPERTY, PLANT AND EQUIPMENT

	Buildings and facilities	Pipelines and tanks	Other plant and equipment	Linefill	Assets under construction including prepayments	Total
At 1 January 2017						
Cost	196,539	1,339,231	1,136,478	121,354	406,560	3,200,162
Accumulated depreciation and impairment	(53,465)	(476,208)	(524,070)	-	-	(1,053,743)
Net book value at 1 January 2017	**143,074**	**863,023**	**612,408**	**121,354**	**406,560**	**2,146,419**
Depreciation	(7,323)	(48,084)	(96,297)	-	-	(151,704)
Additions (including prepayments)	-	-	-	5,972	293,832	299,804
Transfers from assets under construction	28,731	105,720	202,483	-	(336,934)	-
Change in impairment provision	(1,784)	(8,638)	(13,111)	-	-	(23,533)
Net change in dismantlement provision (Note 17)	-	95	-	-	-	95
Disposals: cost	(607)	(22,683)	(10,798)	(489)	-	(34,577)
Disposals: accumulated depreciation and impairment	275	22,027	9,857	-	-	32,159
Net book value at 31 December 2017	162,366	911,460	704,542	126,837	363,458	2,268,663
At 31 December 2017						
Cost	222,879	1,413,725	1,315,052	126,837	363,458	3,441,951
Accumulated depreciation and impairment	(60,513)	(502,265)	(610,510)	-	-	(1,173,288)
Net book value at 31 December 2017	162,366	911,460	704,542	126,837	363,458	2,268,663

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

6 PROPERTY, PLANT AND EQUIPMENT (continued)

	Buildings and facilities	Pipelines and tanks	Other plant and equipment	Linefill	Assets under construction including prepayments	Total
At 1 January 2016						
Cost	170,115	1,146,055	920,949	115,586	511,636	2,864,341
Accumulated depreciation and impairment	(48,102)	(438,636)	(454,137)	-	-	(940,875)
Net book value at 1 January 2016	**122,013**	**707,419**	**466,812**	**115,586**	**511,636**	**1,923,466**
Depreciation	(6,012)	(39,755)	(81,163)	-	-	(126,930)
Additions (including prepayments)	-	-	-	6,492	349,055	355,547
Transfers from assets under construction	27,277	198,282	228,572	-	(454,131)	-
Change in impairment provision	61	(1,000)	(244)	-	-	(1,183)
Net change in dismantlement provision (Note 17)	-	(686)	-	-	-	(686)
Disposals: cost	(914)	(3,420)	(12,799)	(724)	-	(17,857)
Disposals: accumulated depreciation and impairment	649	2,183	11,230	-	-	14,062
Net book value at 31 December 2016	**143,074**	**863,023**	**612,408**	**121,354**	**406,560**	**2,146,419**
At 31 December 2016						
Cost	196,539	1,339,231	1,136,478	121,354	406,560	3,200,162
Accumulated depreciation and impairment	(53,465)	(476,208)	(524,070)	-	-	(1,053,743)
Net book value at 31 December 2016	**143,074**	**863,023**	**612,408**	**121,354**	**406,560**	**2,146,419**

Property, plant and equipment and assets under construction are shown net of impairment provision amounting to RUB 26,889 as at 31 December 2017 (RUB 3,356 as at 31 December 2016).

Linefill represents RUB 102,506 of crude oil and RUB 24,331 of oil products as at 31 December 2017 (as at 31 December 2016 – RUB 100,717 of crude oil and RUB 20,637 of oil products).

During the year ended 31 December 2017, borrowing costs in the amount of RUB 3,459 were capitalised as part of cost of assets under construction (for the year ended 31 December 2016 – RUB 2,341) including interests to be capitalised in the amount of RUB 3,755 (for the year ended 31 December 2016 – RUB 3,437) less amount to be excluded from capitalised borrowing costs in the amount of RUB 296 (for the year ended 31 December 2016 – RUB 1,305) as disclosed in Note 21.

Due to a decline in 2017 of oil transportation turnover the Group tested for impairment its assets relating to the oil transportation segment as separate cash generating unit (CGU). As a result of the test the Group recognised impairment loss of CGU in the amount of RUB 25,569. The recoverable value of the CGU amounting to RUB 2,071,404 was determined as value in use equal to present value of future cash flows. For calculation of value in use the following assumptions were made – the forecast period of 5 years, discount rate of 12%.

Should the oil transportation turnover change for +0.5%/-0.5% the recoverable value of the CGU for would change in the amount of RUB +25,604 and -25,604 accordingly.

Impairment loss was recognised in Other expenses in the consolidated statement of profit or loss and other comprehensive income.

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

7 INVESTMENTS IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES

In December 2017 the Group acquired 25% share in share capitals of AO Ust-Luga Oil and Sandmark Operations Limited for a total consideration of RUB 38,160. Taking into account the key decision making process the Group classified these investments as jointly controlled entities and accounts for them using the equity method in the financial statements. AO Ust-Luga and Sandmark Operations Limited present a common business for transhipment of oil products in Ust-Luga port where AO Ust-Luga is the owner of production complex and capacities for transhipment of oil products and carries out operating activities, and Sandmark Operations Limited acts as a counterparty for contracts with clients and accompanies them receiving agent commission.

Summarised financial information of AO Ust-Luga Oil and Sandmark Operations Limited as well as its reconciliation with the carrying value of the Group's investment is presented below:

	At acquisition date
Current assets	3,940
incl. cash and cash equivalents	*929*
Non-current assets	42,390
Current liabilities	6,440
incl. current financial liabilities	*4,630*
Non-current liabilities	617
incl. non-current financial liabilities	-
Net assets	39,273
Share of net assets	**9,818**
Goodwill	28,342
Carrying value of the investment	**38,160**

In March 2017 the Group acquired 57.41% share in the closed combined mutual investment fund Gazprombank - Finansoviy (hereinafter - the "Fund") for a total consideration of RUB 60 billion. Given the structure of the Fund's ownership and the decision-making procedure for key issues, as well as, existence of a co-investor with a significant share the Group classified the Fund as a jointly controlled entity and accounts for it using the equity method. The main purpose of the Fund is to receive income from investing the assets constituting the Fund.

The summarised financial information about the Fund and its reconciliation with the carrying value of the Group's investment is presented below:

	Date of acquisition
Current assets	104,515
incl. cash and cash equivalents	*104,515*
Current liabilities	-
Non-current liabilities	-
incl. financial liabilities	-
Total net assets	104,515
Share of net assets	**60,000**
Carrying value of the share	**60,000**

In February 2016 the Group acquired 50% share in the share capital of OOO NMT. The consideration amounted to USD 159 mln (RUB 12,497 at Bank of Russia exchange rate as at the date of payment). The difference between the amount of payment under agreement and value of the investment at the date of valuation was recognised in the consolidated statement of profit or loss and other comprehensive income. The Group's effective share of OOO NMT reached 67.79% as a result of the transaction. Taking into account the holding structure and key decision making process, this investment was classified as a jointly controlled entity. OOO NMT is a fuel oil terminal operating in Novorossiysk with maximum capacity of 4 mln tons per year.

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

7 INVESTMENTS IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES (continued)

The summarised financial information of OOO NMT as well as its reconciliation with the carrying value of the Group's investment is presented below:

	At acquisition date
Current assets	2,473
incl. cash and cash equivalents	*2,269*
Non-current assets	6,294
Current liabilities	1,659
incl. current financial liabilities	*1,227*
Non-current liabilities	3,344
incl. non-current financial liabilities	*3,172*
Net assets	3,764
Share of net assets	**1,882**
Goodwill	8,639
Carrying value of the investment	**10,521**

The summarised information concerning financial results and financial position of associates and jointly controlled entities is presented below:

	Country of opeartions	Share		Carrying value	
		31 December 2017	31 December 2016	31 December 2017	31 December 2016
Jointly controlled entities:					
PJSC NCSP (Omirico Limited)	Russia	35.57%	35.57%	34,073	26,191
OOO NMT*	Russia	50%	50%	2,411	11,890
Gazprombank-Finansoviy	Russia	57.41%	-	48,657	-
AO Ust-Luga Oil and Sandmark Operations Limited	Russia	25%	-	38,160	-
OOO NTK	Russia	26%	26%	1,511	1,702
Other associates and jointly controlled entities	Misc.	Misc.	Misc.	1,957	1,516
Total				**126,769**	**41,299**

* direct share

The carrying amount of investment in associates and jointly controlled entities in amount of RUB 126,769 as at 31 December 2017 (RUB 41,299 - at 31 December 2016) is shown net of impairment provision of RUB 23,456 as at 31 December 2017 (RUB 16,353 - at 31 December 2016).

As at 31 December 2017 the value of the Group's direct share in PJSC NCSP (10.52%) calculated based on MICEX market quotes amounted to RUB 15,905 (as at 31 December 2016 – RUB 13,342). The main operating activities of PJSC NCSP and its subsidiaries are the provision of stevedore and supporting services of the port as well as servicing of sea ships.

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

7 INVESTMENTS IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES (continued)

The summarised information about financial results and financial performance of associates and jointly controlled entities is presented below:

31 December 2017	PJSC NCSP (Omirico Limited), OOO NMT	AO Ust-Luga Oil and Sandmark Operations Limited, OOO NTK	Gazprombank-Finansoviy	Other	Total
Current assets	24,041	6,709	147,405*	16,889	195,044
incl. cash and cash equivalents	7,626	1,954	-	4,084	13,664
Non-current assets	200,126	57,382	-	15,674	273,632
Current liabilities	(14,941)	(7,066)	(2,031)	(14,292)	(38,330)
incl. current financial liabilities	(11,853)	5,067	-	(10,773)	(17,559)
Non-current liabilities	(90,239)	(638)	(60,618)	(13,613)	(165,108)
incl. non-current financial liabilities	(57,058)	-	-	(13,166)	(70,224)
Net assets	118,987	56,837	84,756	4,658	265,238
Share of net assets	**37,308**	**11,329**	**48,657**	**1,957**	**99,251**
Goodwill	8,639	28,342	-	-	36,981
Impairment	(9,463)	-	-	-	(9,463)
Carrying value of the investment	**36,484**	**39,671**	**48,657**	**1,957**	**126,769**

* mainly presented by financial instruments

31 December 2016	PJSC NCSP (Omirico Limited), OOO NMT	Other	Total
Current assets	27,193	20,114	47,307
incl. cash and cash equivalents	*15,813*	*6,528*	*22,341*
Non-current assets	197,050	11,126	208,176
Current liabilities	(15,860)	(13,249)	(29,109)
incl. current financial liabilities	*(12,137)*	*(550)*	*(12,687)*
Non-current liabilities	(108,185)	(9,073)	(117,258)
incl. non-current financial liabilities	*(72,965)*	*(8,906)*	*(81,871)*
Net assets	100,198	8,918	109,116
Share of net assets	**29,442**	**3,218**	**32,660**
Goodwill	8,639	-	8,639
Carrying value of the investment	**38,081**	**3,218**	**41,299**

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

7 INVESTMENTS IN ASSOCIATES AND JOINTLY CONTROLLED ENTITIES (continued)

The summarised information about the Group's share in the profit and other comprehensive income of associates and jointly controlled entities is presented below:

Year ended 31 December 2017	PJSC NCSP (Omirico Limited), OOO NMT	AO Ust-Luga Oil and Sandmark Operations Limited, OOO NTK	Gazprombank-Finansoviy	Other	Total
Revenue	54,848	4,996	-	55,442	115,286
Interest expense	(4,230)	(36)	(3,973)	(127)	(8,366)
Current income tax loss	(6,834)	(793)	-	(312)	(7,939)
Profit	20,495	3,519	24,778	1,331	50,123
Total comprehensive income	20,495	3,519	24,778	1,331	50,123
Share of comprehensive income	9,744	915	14,224	427	25,310
Impairment loss	(9,463)	-	-	-	(9,463)
Share of profit from associates and jointly controlled entities	**281**	**915**	**14,224**	**427**	**15,847**
Cash proceeds including dividends received	**(1,878)**	**(1,107)**	**(25,567)**	**(306)**	**(28,858)**

Year ended 31 December 2016	PJSC NCSP (Omirico Limited), OOO NMT	Other	Total
Revenue	63,257	46,302	109,559
Interest expense	(6,377)	(98)	(6,475)
Current income tax loss	(11,230)	(1,050)	(12,280)
Profit	32,656	5,382	38,038
Total comprehensive income	32,656	5,382	38,038
Share of profit from associates and jointly controlled entities	**18,092**	**1,427**	**19,519**
Cash proceeds including dividends received	**(1,051)**	**(1,263)**	**(2,314)**

A significant share of investments in associates and jointly controlled entities is the investment in PJSC "NCSP" (Omirico Limited). In March 2017 the Federal Antimonopoly Service (hereinafter – FAS) of Russia found PJSC "NCSP" guilty for breaking the Federal Law 135 – FZ "On Protection of Competition" because of its dominant position which resulted in setting and maintaining high monopoly prices for the transshipment of certain cargos in the port of Novorossiysk. The FAS of Russia issued an order to transfer to the federal budget the income received from monopolistic activities in the amount of RUB 9.7 billion. PJSC "NCSP" disagreed with the decision and the order, and appealed them in due course. In July 2017 the arbitration court invalidated this decision and the order of the FAS of Russia, and in October 2017 and in February 2018 the higher court left the decision unchanged. The carrying value of the investment in PJSC "NCSP" was not adjusted in these consolidated financial statements because of this fact.

Because of the significant revenue decline of OOO NMT during 2017 as compared to the prior year mainly caused by significant decline of cargo turnover and tariffs, the Group tested for impairment its investment in OOO NMT accounted for using equity method, and recognised impairment loss amounting to RUB 9,463 which was included in Share of profit from associates and jointly controlled entities in the consolidated statement of profit or loss and other comprehensive income. The estimate of investment's recoverable amount of RUB 2,387 was calculated using its value in use with the following assumptions – forecast period of 4 years, industry specific discount rate of 11.2%, terminal growth rate after forecast period of 1.9%.

As at 31 December 2017 the Group held the impairment test of its investment if PJSC NCSP. The recoverable amount of the investment in PJSC NCSP exceeded its carrying amount and thus no impairment loss was recognised. The estimate of investment's recoverable amount was calculated using its value in use with the following assumptions – forecast period of 9 years, industry specific discount rate of 12.3%, terminal growth rate after forecast period of 3.4%.

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

8 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

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

Financial instrument	31 December 2017	31 December 2016
Corporate bonds	31,455	23,557
Municipal bonds	342	1,308
Federal government bonds (OFZ)	26,392	18,342
Corporate Eurobonds	637	989
Securities	33	106
	58,859	**44,302**

Financial assets at fair value through profit or loss are financial instruments assigned for trading purposes.

Financial assets at fair value through profit or loss are neither overdue nor impaired.

The bond issuers were mainly presented by companies controlled by or under significant influence of the state as at 31 December 2017 and 31 December 2016 (88% and 77% accordingly).

Interest rates of the bonds as at 31 December 2017 were in range from 2.0% to 12.7% (as at 31 December 2016 – from 2.0% to 13.9%). Interest rates of the bonds issued by companies which were under control or significant influence of the state as at 31 December 2017 were in range from 2.0% to 12.7% (as at 31 December 2016 – from 2.0% to 13.3%).

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

Financial instrument	12 months and less	1 to 2 years	2 to 5 years	Over 5 years	Without maturity	Total
Corporate bonds	21,595	5,335	4,360	165	-	31,455
Municipal bonds	4	27	56	255	-	342
Government bonds (OFZ)	9,652	6,012	8,318	2,410	-	26,392
Corporate Eurobonds	92	-	545	-	-	637
Securities	-	-	-	-	33	33
	31,344	**11,374**	**13,279**	**2,829**	**33**	**58,859**

9 DISPOSAL OF SUBSIDIARIES

In February 2016 the Group completed the sale of AO Yugo-Zapad transnefteproduct which owned 100% of share capital of DP PrikarpatZapadtrans which assets were located on the territory of Ukraine. The amount of excess of consideration received over the carrying value of net assets disposed of amounted to RUB 998 and was recognised as Other expenses in the consolidated statement of profit or loss and other comprehensive income.

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

10 OTHER FINANCIAL ASSETS

As at 31 December 2017:

Type of asset	Maturity	Currency	Amount at the issue (purchase) date	Carrying amount
Long-term financial assets				
Loans granted to related parties	February 2019 – May 2029	USD	13,452	17,842
	December 2021 – March 2027	RUB	5,133	5,252
Other financial assets	-	RUB	2	2
			18,587	**23,096**
Short-term financial assets				
Loans granted to related parties	During the year after the reporting date	USD	-	1,788
		RUB	-	492
Eurobonds	During the year after the reporting date	USD	14,722	13,638
Deposits	During the year after the reporting date	USD	161,576	161,107
		RUB	31,215	31,735
Other financial assets	During the year after the reporting date	RUB	8	8
			207,521	**208,768**

As at 31 December 2016:

Type of asset	Maturity	Currency	Amount at the issue (purchase) date	Carrying amount
Long-term financial assets				
Loans granted to related parties	May 2029	USD	9,713	14,783
	December 2021, December 2025	RUB	3,900	3,900
Eurobonds	February 2017 – July 2018	USD	14,595	14,050
Other financial assets	-	RUB, USD	4	5
			28,212	**32,738**
Short-term financial assets				
Loans granted to related parties	During the year after the reporting date	USD	516	3,023
		RUB	-	43
Eurobonds	During the year after the reporting date	USD	5,234	7,067
Deposits	During the year after the reporting date	USD	278,343	269,996
		RUB	27,658	28,270
Other financial assets	During the year after the reporting date	RUB	10	10
			311,761	**308,409**

As at 31 December 2017 and 31 December 2016 the significant amount of deposits (80% and 93% respectively) were placed with banks which were under control or significant influence of the state.

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

10 OTHER FINANCIAL ASSETS (continued)

Interest rates of the deposits denominated in the US Dollars and Russian roubles as at 31 December 2017 were in the range from 1.0% to 8.1% (as at 31 December 2016 – from 0.8% to 11.0%). As for the deposits placed with banks controlled by or under significant influence of the state interest rates ranged from 1.0% to 8.1% as at 31 December 2017 (from 0.8% to 11.0% as at 31 December 2016).

Most of issuers of afore-mentioned notes and bonds as at 31 December 2017 and 31 December 2016 were organisations which were controlled or significantly influenced by the state (75% and 83% respectively).

Interest rates of the notes and bonds ranged from 3.4% to 8.1% as at 31 December 2017 (ranged from 3.4% to 8.1% as at 31 December 2016). As for the notes and bonds issued by companies which were controlled by or were under significant influence of the state interest rates ranged from 3.9% to 8.1% as at 31 December 2017 (ranged from 5.1% to 8.1% as at 31 December 2016).

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

11 INVENTORIES

	31 December 2017	31 December 2016
Materials and supplies	26,149	27,081
Sundry goods for resale	4,513	3,849
	30,662	**30,930**

Materials and supplies are presented net of provisions for obsolescence which amounted to RUB 692 as at 31 December 2017 (as at 31 December 2016 – RUB 24). Materials are primarily used for repairment and maintenance of pipeline equipment.

12 RECEIVABLES AND PREPAYMENTS, VAT ASSETS

Receivables and prepayments

	31 December 2017	31 December 2016
Long-term receivables		
Financial assets		
Other long-term receivables	2,080	1,439
Non-financial assets		
Long-term VAT	3	4
Total long-term receivables	**2,083**	**1,443**
Short-term receivables		
Financial assets		
Trade receivables	21,963	22,346
Other receivables	36,640	26,573
less: provision for impairment	(27,287)	(23,591)
Total financial assets in short-term receivables	**31,316**	**25,328**
Non-financial assets		
Prepayments, advances and other non-financial receivables	11,084	10,834
Total short-term receivables	**42,400**	**36,162**

As at 31 December 2017 other accounts receivable included interest receivable related to temporarily available cash balances with banks as well as receivables related to insurance, agency agreements, prepayment for taxes other than income tax and other receivables.

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

12 RECEIVABLES AND PREPAYMENTS, VAT ASSETS (continued)

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

	2017		2016	
	Trade receivables	Other receivables	Trade receivables	Other receivables
As at 1 January	**707**	**22,884**	**495**	**20,995**
Impairment loss	4,704	432	675	2,622
Amounts written off in trade and other receivables	(314)	(211)	(15)	(76)
Reversal of provision	(35)	(880)	(448)	(657)
As at 31 December	**5,062**	**22,225**	**707**	**22,884**

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

According to the analysis of accounts receivable in respect to the payment dates the Group has the following overdue balances not included in the provision for accounts receivable as at 31 December 2017 and 31 December 2016:

	31 December 2017		31 December 2016	
Outstanding period	Trade receivables	Other receivables	Trade receivables	Other receivables
Less than 90 days	107	61	800	465
More than 90 days but less than 365 days	72	98	138	176
Over 365 days	73	253	73	33
	252	**412**	**1,011**	**674**

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

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

	31 December 2017			31 December 2016		
Currency	Trade receivables	Other receivables	Total receivables	Trade receivables	Other receivables	Total receivables
RUB	1,218	14,233	15,451	8,330	3,531	11,861
USD	14,677	169	14,846	12,878	138	13,016
Other	1,006	13	1,019	431	20	451
	16,901	**14,415**	**31,316**	**21,639**	**3,689**	**25,328**

13 CASH AND CASH EQUIVALENTS

	31 December 2017	31 December 2016
Balances in RUB	60,584	71,388
Balances in USD	13,549	1,786
Balances in Euro	817	517
Balances in other currencies	1,212	895
	76,162	**74,586**

In accordance with Russian legislation, the Group selects financial institutions via holding tenders based on certain established qualifications required by law. As at 31 December 2017 and 31 December 2016, a significant portion of cash was placed with banks, which are under common control or significant influence of the state (92% and 72% correspondingly).

Information concerning the Group's exposure to interest risk and sensibility analysis relating to financial assets and liabilities are disclosed in Note 26.

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

14 SHARE CAPITAL, RETAINED EARNINGS AND DIVIDENDS

Share capital	31 December 2017			31 December 2016		
	Number of shares	Historical cost	Inflated cost	Number of shares	Historical cost	Inflated cost
Authorised, issued and fully paid shares with par value RUB 1 each						
Ordinary:	5,568,748	5.5	231	5,546,847	5.5	231
Preferred:	1,554,875	1.6	77	1,554,875	1.6	77
	7,123,623	**7.1**	**308**	**7,101,722**	**7.1**	**308**

The carrying value of the share capital as at 31 December 2017 and as at 31 December 2016 differs from historical cost due to the effect of hyperinflation in the Russian Federation prior to 31 December 2002.

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

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

In April 2017 changes to the charter of Transneft were registered according to which the share capital increased by 21,901 ordinary registered uncertified shares and constituted 7,123,623 shares with 1 RUB par value. The difference between par value of additional issue of shares and payment for the shares in the amount of RUB 5,991 was recognised as share premium.

Within the terms of the asset management agreement in the third quarter of 2017 the fiduciary manager acquired 6,178 of preferred shares of the Company which were sold in the fourth quarter of 2017. These operations were shown in the consolidated statement of changes in equity as purchase of treasury shares and sale of treasury shares.

In October 2017 the Board of directors of Transneft defined the offering price for one ordinary registered uncertified share of Transneft as 278,780 Russian roubles and recommended to the General meeting of shareholders to increase the share capital by 125,720 Russian roubles by issue of 125,720 ordinary registered uncertified shares with par value of 1 Rouble. The offering of shares will be held by private subscription in favor of the Russian Federation represented by the Federal Agency for the Management of State Property, the shares issued will be paid by 100% of ordinary shares of CPC Company and 100% of ordinary shares of CPC Investments Company which are owned by the Russian Federation (Note 25, 28).

Rights attributable to preferred shares

Holders of preferred shares are entitled to receive dividends pursuant to the authorization of dividend payment at the general meeting of shareholders of Transneft. The amount of dividends to be paid on preferred shares is established by the Company's Charter as 10 percent of net profits of the standalone (non-consolidated) financial statements of Transneft prepared in accordance with Russian Accounting Standards (RAS) for the most recent financial year. At the same time the amount of dividends paid for one preferred share cannot be lower than the dividend paid for an ordinary share.

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

- on the reorganization and liquidation of the Company;
- on the introduction of amendments and addenda to the Charter of the Company which limit the rights of shareholders that hold preferred shares and on the handling of application for delisting of the preferred shares.

In case where no decision on payment of dividends was adopted at an annual general meeting shareholders that hold preferred shares in the Company shall be entitled to participate in the general meeting of shareholders with the right to vote on any issues concerning its competences. This right of shareholders that hold preferred shares is terminated from the time of the first full payment of dividends on the indicated shares.

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

14 SHARE CAPITAL, RETAINED EARNINGS AND DIVIDENDS (continued)

Dividends

In June 2017 the following dividends were approved at the general shareholders meeting for the year ended 31 December 2016:

	Number of shares	RUB per share	Total
Ordinary shares	5,568,748	4,296.48	23,926
Preferred shares*	1,554,875	4,296.48	6,680
			30,606

* including treasury shares

Dividends were paid out in July - August 2017.

In August 2017 at the extraordinary general meeting of shareholders the payment of dividends based on the results of the first half of 2017 was approved:

	Number of shares	RUB per share	Total
Ordinary shares	5,568,748	3,875.49	21,582
Preferred shares*	1,554,875	3,875.49	6,026
			27,608

* including treasury shares

Dividends were paid out in October 2017.

In June 2016 the annual general meeting of shareholders of the Company approved the payment of dividends for the year ended 31 December 2015:

	Number of shares	RUB per share	Total
Ordinary shares	5,546,847	2,077.08	11,521
Preferred shares	1,554,875	823.31	1,280
			12,801

Dividends were paid out in July-August 2016.

Distributable profits

Standalone financial statements of the Company prepared in accordance with RAS form a basis for a profit distribution and other appropriations. Net profit of the Company based on the standalone RAS financial statements for the year ended 31 December 2017 amounted to RUB 58,844 (RUB 30,607 for the year ended 31 December 2016).

15 LOANS AND BORROWINGS

	31 December 2017	31 December 2016
Total loans and borrowings	688,910	701,552
Less: current loans and borrowings and current portion of non-current loans and borrowings	(109,730)	(109,047)
	579,810	**592,505**
Maturity of non-current loans and borrowings		
Between one and five years	311,275	301,116
After five years	267,905	291,389
	579,180	**592,505**

The amount of short-term loans and borrowings included non-convertible interest-bearing documentary bonds of RUB 12 with maturity date in May 2019 but with optional earlier redemption on demand of bond-holders or by issuer's intention in May of 2018.

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

15 LOANS AND BORROWINGS (continued)

Type of loans and borrowings	Mature in	Currency	Interest rate, %	31 December 2017		31 December 2016	
				Carrying value	Fair value	Carrying value	Fair value
Eurobonds	2018	USD	Fixed	62,585	65,001	65,906	72,139
Corporate bonds (unsecured)*	2018-2019	RUB	Fixed	60,663	64,644	96,573	98,393
Marketable bonds (unsecured)*	2021-2027	RUB	Fixed	205,465	214,987	107,040	107,896
Loan agreement with China Development Bank	2024	USD	Floating LIBOR	268,117	269,086	432,012	434,565
Other loans and borrowings	2018-2025	RUB	Fixed	92,080	92,080	21	21

* In accordance with the relevant prospectus, some bonds have an optional earlier redemption terms for the total amount of RUB 51,012 with maturity in May 2019, in April 2026, in August 2026 and in April 2027 but with with optional earlier redemption on demand of bond-holders or by issuer's intention in May of 2018, April 2021, September 2022, April 2024, respectively.

Proceeds from Eurobonds issues were used by the Group to finance investment projects or to refinance current portion of loans and borrowings to finance investment projects.

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

Cash proceeds from placement of marketable bonds and receipt of loans and borrowings during the reporting year were used for partial earlier repayment of the loan from China Development Bank Corporation and general corporate purposes.

In December 2017 the Group signed agreements for receipt of unsecured loans from banks under state control for the total amount of RUB 253 billion maturing in 2023-2028 of which RUB 213 billion had not been taken yet as at the reporting date. Loans received from these credit lines in December 2017 – January 2018 were used for partial earlier repayment of the loan from China Development Bank Corporation and general corporate purposes. On these credit lines, the difference between the calculated fair value determined using the discounted future cash flows method and nominal amounts of credit lines was recognized in Finance income in the consolidated statement of profit or loss and other comprehensive income.

Collateral

All borrowings and loans of the Group, except for the loan from China Development Bank Corporation, are unsecured as at 31 December 2017 and 31 December 2016.

In February 2009 as collateral for the loan from China Development Bank Corporation the Company signed a contract for the term of 20 years for the annual supply of 6 mln tons of crude oil to the People's Republic of China starting from 1 January 2011. For the fulfillment of this obligation, a contract was signed with Rosneft in April 2009 for the supply of corresponding volumes of crude oil to the Company (Note 25).

Fair value

Fair value of the loan from China Development Bank Corporation (Level 2) was determined as a result of discounting using estimated market interest rate for similar financing arrangements. These amounts include all future cash outflows associated with the long-term debt repayments, including the current portion and interest. Market interest rates mean the rates of raising long-term debt by companies with a similar credit rating for similar maturities, repayment schedules and similar other main terms.

The fair value of bonds (Level 1) was determined based on market quotations as at 31 December 2017 and 31 December 2016, respectively.

Changes in liabilities from financing activities were due to:

– cash flows from proceeds and repayment of loans and borrowings disclosed in the cash flows from financing activities in the Consolidated statement of cash flows;
– interest expense in the amount of RUB 48,712 including the amount of interest to be capitalised of RUB 3,755 (Note 21), payment of which was shown as cash flows from operating activities in the Consolidated statement of cash flows;
– negative changes in exchange rates in the amount of RUB 22,113.

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

16 DEFERRED TAX LIABILITIES AND INCOME TAX EXPENSE

The amounts recognised in the profit or loss

As for the year ended 31 December 2017 and the year ended 31 December 2016 the income tax included:

	Year ended 31 December 2017	Year ended 31 December 2016
Current income tax	49,911	55,838
Deferred income tax		
Origination and reversal of temporary differences	451	12,677
Deferred income tax loss	**451**	**12,677**
Total income tax expense	**50,362**	**68,515**

Deferred tax liabilities and assets consist of the following:

	1 January 2017	Credited/ (charged) to profit or loss	Credited directly to other comprehensive income	Disposal of subsidiary	31 December 2017
Deferred tax liabilities:					
Carrying value of property, plant and equipment in excess of tax base	(62,668)	(1,754)	-	10	(64,412)
Other	(638)	(687)	(153)	(28)	(1,506)
	(63,306)	**(2,441)**	**(153)**	**(18)**	**(65,918)**
Deferred tax assets:					
Provision for inventories, receivables and accruals	5,608	505	-	-	6,113
Tax loss carry-forwards	1,599	(279)	-	(81)	1,239
Provisions for dismantlement and other expenses	9,683	1,764	-	(1)	11,446
	16,890	**1,990**	**-**	**(82)**	**18,798**
Net deferred tax liabilities	**(46,416)**	**(451)**	**(153)**	**(100)**	**(47,120)**

	1 January 2016	Credited/ (charged) to profit or loss	Credited directly to other comprehensive income	31 December 2016
Deferred tax liabilities:				
Carrying value of property, plant and equipment in excess of tax base	(53,020)	(9,648)	-	(62,668)
Other	(353)	78	(363)	(638)
	(53,373)	**(9,570)**	**(363)**	**(63,306)**
Deferred tax assets:				
Provision for inventories, receivables and accruals	7,067	(1,459)	-	5,608
Tax loss carry-forwards	4,620	(3,021)	-	1,599
Provisions for dismantlement and other expenses	6,912	2,771	-	9,683
Trade and other payables	1,398	(1,398)		-
	19,997	**(3,107)**	**-**	**16,890**
Net deferred tax liabilities	**(33,376)**	**(12,677)**	**(363)**	**(46,416)**

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

16 DEFERRED TAX LIABILITIES AND INCOME TAX EXPENSE (continued)

Differences between the recognition criteria in Russian statutory taxation regulations and IFRS give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for profit tax purposes. The tax effect of the movement on these temporary differences is recorded at the statutory rate of 20% for year ended 31 December 2017 and 31 December 2016.

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

	Year ended 31 December 2017	Year ended 31 December 2016
Profit before income tax	**242,167**	**301,422**
Theoretical income tax expense at 20%	48,433	60,284
Increase/(decrease) due to:		
Changes in estimation of deferred tax assets	-	4,160
Changes in the Group's structure	-	111
Items not taxable for income tax purposes	(2,488)	(4,605)
Items not deductible for income tax purposes	4,417	8,565
Actual income tax expense	**50,362**	**68,515**

The Group did not recognise deferred tax liability in respect of RUB 335,753 as at 31 December 2017 (as at 31 December 2016 - RUB 369,634) of taxable temporary differences associated with its investments in subsidiaries as the Group is able to control the timing of their reversal and does not believe they will reverse in the foreseeable future.

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

17 PROVISIONS FOR LIABILITIES AND CHARGES

	31 December 2017	31 December 2016
Pension provision	107,995	97,414
Dismantlement provision	6,925	6,580
Other provisions	11,805	11,547
Total long-term provisions for liabilities and charges	**126,725**	**115,541**
Pension provision	4,605	2,079
Dismantlement provision	1,469	1,356
Other provisions	35,394	31,747
Total short-term provisions for liabilities and charges	**41,468**	**35,182**

Other provisions mainly include provision for unused vacations, accrued provision for annual performance benefit for the reporting year.

Provision in accordance with IAS 19

In addition to contributions to State pension fund, the Group sponsors defined benefit plans for the majority of its employees. These plans assume regular pension payments to participants during their lifetime for those who have worked for not less than five years based on years of service, salary and received awards during working. Also in accordance with collective agreements with employees the Group has a liability due to those who have worked not less than three years to pay a one-time benefit ranging from 1 to 5 salaries upon retirement, to cover funeral costs and to pay out benefits to pensioners to jubilees and holidays.

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

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

17 PROVISIONS FOR LIABILITIES AND CHARGES (continued)

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

Movement in defined benefit obligation	2017	2016
At 1 January	**32,786**	**31,537**
Interest cost	2,806	2,961
Service cost	3,194	2,969
Actuarial gain	(700)	(2,839)
Benefits paid	(2,765)	(1,842)
At 31 December	**35,321**	**32,786**

Service cost and adjustments amounting to RUB 3,194 and RUB 2,969 as for the years ended 31 December 2017 and 2016, respectively, are included in pension expenses in the consolidated statement of profit or loss and other comprehensive income, interest expense in the amount of RUB 2,806 and RUB 2,961 for the years ended 31 December 2017 and 2016, respectively, were included in interest expenses.

Actuarial gain amounting to RUB 700 for the year ended 31 December 2017 (actuarial gain amounting to RUB 2,839 for the year ended 31 December 2016) was included in other comprehensive income. As at 31 December 2017 accumulated actuarial loss amounted to RUB 1,197 (as at 31 December 2016 accumulated actuarial loss amounted to RUB 1,897).

Assumptions regarding future mortality are based on published statistics and mortality tables. Assumptions are based on mortality statistics in Russia for 2016. The retirement age in Russia is currently 60 years for men and 55 years for women.

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

	31 December 2017	31 December 2016
Pension provision for defined benefit plan	35,321	32,786

Principal actuarial assumptions used (expressed as weighted average):

	31 December 2017	31 December 2016
Average nominal discount rate	8.35%	8.56%
Future salary increases (nominal)	4.38%	4.52%
Expected long-term inflation rate	3.38%	3.52%

As at 31 December 2017, if the future estimated inflation rate had increased by 1%, the amount of the Group pension provisions would have been RUB 2,911 higher.

As at 31 December 2017, if the average nominal discount rate had decreased by 1%, the amount of the Group pension provisions would have been RUB 2,820 higher.

Pension liabilities through JSC "NPF "TRANSNEFT's" activity

Pension liabilities through JSC "NPF "TRANSNEFT's" activity include liabilities under insurance contracts and investment contracts.

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

Liabilities under investment contracts are amounts of the pension accounts balances of participants as at the reporting date, which are the amounts of accumulated contributions, accrued income from the placement of pension reserves less the amount of payments made to the reporting date.

	31 December 2017	31 December 2016
Pension liabilities – insurance contracts	52,799	44,682
Pension liabilities – investment contracts	24,480	22,025
	77,279	**66,707**

Increase in liabilities under insurance contracts were mainly caused by indexation of corporate non-state lifetime pensions from 1 March 2017 without additional funding by participants.

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

17 PROVISIONS FOR LIABILITIES AND CHARGES (continued)

Dismantlement provision

The Group uses the following assumption in relation to the provision for dismantlement of the existing network of oil and oil product pipelines. The operating oil and oil products pipeline network will be dismantled in the end of its useful life. The Group performs regular diagnostics, maintains periodic upgrades and reconstructions of oil and oil product pipelines, which leads to the extension of its useful life. Thus, the Group cannot make a reliable estimate of the period of the whole oil and oil products pipelines network dismantlement and consequently the amount of dismantlement provision. When the Group adopts a plan on liquidation and dismantlement of certain parts of network, the provision for dismantlement is recognised accordingly in the financial statements.

As at 31 December 2017 in relation to fixed assets included in the Programme for liquidation, adopted by the Group in accordance with established procedure, dismantlement provision was recognised in respect of future costs for liquidation of oil and oil product pipelines including site restoration expenses. The amount of provision is estimated by discounting future expenses at yield-to-maturity rates of federal bonds (OFZ) with relevant maturities; the rates amounted to 7.40% - 7.60% as at 31 December 2017 (8.74% - 8.84% as at 31 December 2016). Liquidation value of fixed assets in use is included in fixed assets and depreciated over the useful life of pipeline. Provision for liquidation of fixed assets, which are decommissioned, was recognised as operating expense. The carrying value of dismantlement provision amounted to RUB 8,394 as at 31 December 2017 (RUB 7,936 as at 31 December 2016) including short-term provision of RUB 1,469 (RUB 1,356 as at 31 December 2016), which is presented as current provisions for liabilities and charges.

18 TRADE AND OTHER PAYABLES

	31 December 2017	31 December 2016
Long-term payables		
Other payables	1,200	103
Total financial payables	**1,200**	**103**
Advances received	2,258	2,361
Total long-term payables	**3,458**	**2,464**
Short-term payables		
Trade payables	49,070	73,619
Other payables	10,189	12,101
Total financial payables	**59,259**	**85,720**
Advances received	51,423	47,061
VAT payable	9,881	9,296
Other taxes payable	8,458	6,587
Total short-term payables	**129,021**	**148,664**

Breakdown of accounts payable and other liabilities including derivatives by currency is presented in the table below:

Currency	31 December 2017			31 December 2016		
	Trade payables	Other payables	Total payables	Trade payables	Other payables	Total payables
RUB	48,950	8,983	57,933	73,432	10,343	83,775
USD	14	622	636	137	1,293	1,430
Euro	87	580	667	6	441	447
Other	19	4	23	44	24	68
	49,070	**10,189**	**59,259**	**73,619**	**12,101**	**85,720**

Trade payables include payables for purchases of property, plant and equipment in the amount of RUB 27,737 as at 31 December 2017 and RUB 51,332 as at 31 December 2016.

Information concerning the Group's exposure to currency risk and liquidity risk in relation to trade and other payables is disclosed in Note 26.

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

19 REVENUE

	Year ended 31 December 2017	Year ended 31 December 2016
Revenue from crude oil transportation services:		
Domestic tariff	257,307	245,562
Export tariff	374,152	368,577
Total revenue from crude oil transportation services	**631,459**	**614,139**
Revenue from crude oil sales	150,182	142,299
Revenue from oil products transportation services	66,035	64,485
Other revenue	36,661	27,211
	884,337	**848,134**

Revenue from crude oil sales for the year ended 31 December 2017 mainly include revenue from supplying of oil according to the agreement signed by the Company in February 2009. According to the agreement crude oil will be supplied to China during 20 years since 1 January 2011 amounting to 6 million tons of oil per annum. The Group purchases crude oil under the contract signed in April 2009 with Rosneft (see Note 25).

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

- revenue from transportation of crude oil to destinations in the Russian Federation and to the member-states of the Eurasian Economic Union, based on tariffs set by the Federal Antimonopoly Service and payable in RUB ("domestic tariff");
- revenue from transportation of crude oil which is destined for export outside of the Russian Federation and member-states of the Eurasian Economic Union, based on tariffs set by the Federal Antimonopoly Service and payable in RUB ("export tariff");
- revenue from transportation of transit crude oil from Azerbaijan to export destinations through the territory of the Russian Federation to the Novorossiysk's port in accordance with tariff set by the Federal Antimonopoly Service and payable in RUB ("export tariff");
- revenue from transportation of transit crude oil from Kazakhstan, based on the tariffs which are set by the Federal Antimonopoly Service and payable in RUB ("export tariff").

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

Revenue from domestic transportation of oil products is formed on the basis of tariffs which are set within limits imposed by tariffs approved by Federal Tariff Service and Federal Antimonopoly Service and includes:

- revenue from oil products transportation services in the territory of the Russian Federation and member-states of the Eurasian Economic Union at tariffs set and paid for in RUB;
- revenue from oil products transportation services for export outside the territory of the Russian Federation and member-states of the Eurasian Economic Union at tariffs set and paid for in RUB.

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

Revenue from oil product transportation services in the Republic of Kazakhstan is formed on the basis of tariffs set by Transneft in Kazakh tenge. These services are paid for in RUB at the exchange rate set by CBR at the date of payment.

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

20 OPERATING EXPENSES NET OF AMORTISATION AND DEPRECIATION

	Year ended 31 December 2017	Year ended 31 December 2016
Salaries	116,791	113,223
Social funds contributions	29,330	27,272
Social expenses	3,757	4,144
Cost of crude oil sold	119,260	111,166
Export custom duties	30,393	30,007
Energy	41,718	38,438
Materials	33,851	29,505
Repairs and maintenance services	17,790	15,746
Property tax and other taxes, except for income tax	28,494	21,362
Pension expenses	5,412	4,392
Insurance	6,070	7,059
Other expenses	43,196	37,603
Operating expenses net of amortisation and depreciation	**476,062**	**439,917**

Other expenses comprise of communication services, rent expenses, transportation expenses, business trip expenses, received and paid fines and penalties, as well as, other operating income and expenses.

21 FINANCE INCOME AND FINANCE COSTS

	Year ended 31 December 2017	Year ended 31 December 2016
Interest income from cash and cash equivalents	4,675	2,458
Interest income from other financial assets	14,315	17,701
Other interest income	11,763	793
Total interest income	**30,753**	**20,952**
Less interest income from the temporary investment of borrowings	(296)	(1,305)
Total interest income recognised in the consolidated statement of profit or loss and other comprehensive income	**30,457**	**19,647**
Foreign exchange gain	77,720	267,267
Gain from operations with derivatives	-	3,388
Net income from financial instruments through profit or loss	1,000	606
Total finance income	**109,177**	**290,908**
Interest expense on loans and borrowings	(48,712)	(46,883)
Distribution of pension income on pension liabilities	(6,744)	(6,747)
Other interest expenses	(4,023)	(5,044)
Total interest expenses	**(59,479)**	**(58,674)**
Less capitalised finance expenses	3,755	3,437
Total interest expenses recognised in the consolidated statement of profit or loss and other comprehensive income	**(55,724)**	**(55,237)**
Foreign exchange losses	(68,419)	(225,968)
Loss from operations with financial assets measured at fair value through profit or loss	(666)	(38)
Total finance costs	**(124,809)**	**(281,243)**
Net finance (costs) / income	**(15,632)**	**9,665**

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

22 SUBSIDIARIES, ASSOCIATES AND JOINTLY CONTROLLED ENTITIES

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

	Type of activity	Country of incorporation	Percentage (%) of ownership interest at 31 December 2017
AO Transneft - Sibir	crude oil and oil products transportation	Russia	100.0
AO Chernomortransneft	crude oil and oil products transportation	Russia	100.0
AO Transneft - Druzhba	crude oil and oil products transportation	Russia	100.0
AO Transneft - Privolga	crude oil and oil products transportation	Russia	100.0
AO Transneft – Zapadnaya Sibir	crude oil and oil products transportation	Russia	100.0
AO Transneft – Verkhnyaya Volga	crude oil and oil products transportation	Russia	100.0
AO Transneft – Tsentralnaya Sibir	crude oil transportation	Russia	100.0
AO Transneft – Sever	crude oil transportation	Russia	100.0
OOO Transneft - Baltika	crude oil and oil products transportation	Russia	100.0
AO Transneft - Ural	crude oil and oil products transportation	Russia	100.0
AO Transneft – Prikamye	crude oil transportation	Russia	100.0
OOO Transneft - Vostok	crude oil transportation	Russia	100.0
OOO Transneft – Dalniy Vostok	crude oil transportation	Russia	100.0
AO Transnefteproduct	wholesale of oil products	Russia	100.0
AO Mostransnefteproduct	oil products transportation	Russia	100.0
AO Sredne-Volzhsky Transnefteproduct	oil products transportation	Russia	100.0
Unitarnoye predpriyatiye Zapad-Transnefteproduct	oil products transportation	Belarus	100.0
AO Transnefteproduct-Zapad	holding of investment	Russia	100.0
OOO Transneft - Port Primorsk	transport processing of cargo	Russia	100.0
OOO Transneft - Port Kozmino	crude oil transportation	Russia	100.0
OOO Transneft – Port Ust-Luga	oil transshipment	Russia	100.0
AO Transneft - Podvodservice	diagnostics, repair of underwater line	Russia	100.0
AO Giprotruboprovod	development of engineering documentation	Russia	100.0
AO Svyaztransneft	technological connection	Russia	100.0
AO Transneft - Diascan	diagnostics of trunk pipelines	Russia	100.0
OOO Transneft Nadzor	technical and building supervision and control	Russia	100.0
OOO Transneft – TSD	provision of general construction services	Russia	100.0
OOO Transneft - Service	handling of cargo services	Russia	100.0
AO Transneft - Metrologia	metrological support of oil transportation	Russia	100.0
OOO NII Transneft	research activity	Russia	100.0
OOO IPTER	scientific research and development in the field of natural and technical sciences	Russia	100.0
OOO TsUP VSTO	construction services	Russia	100.0
OOO Transneft Finance	accounting services	Russia	100.0

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

22 SUBSIDIARIES, ASSOCIATES AND JOINTLY CONTROLLED ENTITIES (continued)

	Type of activity	Country of incorporation	Percentage (%) of ownership interest at 31 December 2017
OOO Transneftenergo	electricity sales	Russia	100.0
AO Transneft - Energoterminal	filling of oil into railway tank wagons	Russia	50.04
OOO Transneft-Logistika	transportation of cargo	Russia	100.0
OOO Transneftstroy	general building and machinery contractor	Russia	100.0
Fenti Development Ltd.	financial activity	Switzerland	100.0
OOO Transneft – Media	publishing activity	Russia	100.0
AO Telecomnefteproduct	communication services	Russia	100.0
DP Rovensky Tsekh Elektrosvyazi	communication services	Ukraine	100.0
Unitarnoye predpriyatiye Zapad-Telecomnefteproduct	communication services	Belarus	100.0
AO PROMSFERA	rent of property	Russia	100.0
OOO Tikhoretsk –Nafta	handling of cargo services	Russia	100.0
AO Transneft-Service	wholesale of oil products	Russia	100.0
AO TNT	crude oil and oil products transportation	Russia	100.0
OOO TES	transmission of electricity	Russia	100.0
OOO Transneft - Tekhnologii	maintenance of automation means, telemechanization systems and automated process control systems	Russia	100.0
OOO Transneft Telecom	telecommunication services	Russia	100.0
OOO Transneft – Okhrana	security services	Russia	100.0
JSC “NPF “TRANSNEFT”	non-state pension management	Russia	100.0
OOO UK TN Invest	trust management of non-state pension fund assets	Russia	100.0
Equity-accounted investments			
Omirico Limited	financial activity	Cyprus	50.0
PJSC NCSP	cargo handling and storage services	Russia	35.57
OOO NMT	cargo handling services	Russia	67.79
OOO PTP	technical / surveyor / shipchandler / agent servicing of sea vessels in seaports, cargo transportation by sea transport	Russia	35.57
OOO Nevskaya pipe company	handling of cargo services	Russia	26.0
AO OMEGA	production of monitoring systems of pipelines	Russia	50.0
OOO RUSENERGORESURS	wholesale of electric and heat power	Russia	25.0
AO Ust-Luga Oil	handling of cargo services	Russia	25.0
Sandmark Operations Limited	handling of cargo services	Cyprus	25.1
CMF Gazprombank-Finansoviy	financial activity	Russia	57.41
OOO TK-BA	designing and construction of “Burgas – Alexandroupolis” pipeline	Russia	33.34
AO TNN	development, production and sales of pumping equipment	Russia	51.0
AO RED	production of electric motors	Russia	51.0
OOO Transneft-Sintez	production of oil products	Russia	51.0
OOO Impex-Plus	production, holding and storage of crude oil and products of its processing	Russia	50.0
OOO LatRosTrans	oil products transportation	Latvia	34.0

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

23 OPERATING LEASES

The Group leases a number of land plots, mainly, owned by local governments under operating lease.

The future lease payments under lease agreements broken-down by period of payment were as follows:

	31 December 2017	31 December 2016
Less than one year	1,476	1,528
Between one year and five years	5,905	6,110
After five years	66,430	68,739
Total	**73,811**	**76,377**

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

The rent paid to the landlord of the land is increased in accordance with the contractual terms at regular intervals, it was determined that substantially all the risks and rewards of owning the land lie within the landlord. As such, the Group determined that the lease agreements are operating lease agreements.

During the year ended 31 December 2017 RUB 564 (31 December 2016: RUB 491) was recognised in profit or loss in respect of operating lease.

24 CONTINGENT LIABILITIES AND OTHER RISKS

Legal proceedings

During the year ended 31 December 2017 the Group was involved in a number of court proceedings arising in the ordinary course of business. In the opinion of the Group's management, there were no current legal proceedings or claims outstanding at 31 December 2017, which could have a material adverse effect on the results of operations or financial position of the Group.

25 RELATED PARTIES AND KEY MANAGEMENT PERSONNEL COMPENSATION

The Russian Federation represented by the Federal Agency for the Management of State Property owns 100% of the ordinary shares of the Company and conducts control via the Board of Directors that as at the 31 December 2017 was comprised of the State representatives (professional attorneys) and Independent Directors. The Government of the Russian Federation shall appoint the members of the Federal Antimonopoly Service to make decisions on tariff and their limits.

As at 31 December 2017 and 31 December 2016 the Company holds in trust on behalf of the Russian Federation 100% of the shares of the CPC Investments Company, 100% of the shares of the CPC Company (which owns 7% of the shares of CPC-R and 7% of the shares of CPC–K), 24% of the ordinary shares of the CPC-R and 24% of the ordinary shares of CPC–K. These interests are not recognised in these consolidated financial statements as the Company is acting as an agent in the shares of the above companies.

The Group's transactions with other entities which are controlled by the state occur in the normal course of business. These transactions include the following: purchase of electricity for production needs, transportation of oil produced by state-owned entities, and transactions with banks, which are under common control or significant influence of the state.

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

25 RELATED PARTIES AND KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

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

	Year ended 31 December 2017	Year ended 31 December 2016
Revenue from oil transportation services	336,760	327,605
Rosneft and its subsidiaries	272,889	265,898
PJSC “GAZPROM” and its subsidiaries	31,285	31,214
Others	32,586	30,493
Revenue from oil products transportation services	28,673	22,854
Rosneft and its subsidiaries	18,998	10,466
PJSC “GAZPROM” and its subsidiaries	9,675	12,388
Purchases of oil (Rosneft)	110,483	97,387
Transportation of oil using railways and related services (JSCo “RZD” and its subsidiaries)	-	768
Electricity expenses	914	736
Proceeds from loans from bank under state control	40,000	-
Finance income	17,028	10,691
Finance expense	145	-
Transportation expenses	33	1,724

During the year ended 31 December 2017 and 31 December 2016, Group had following transactions with associates and jointly controlled entities:

	Year ended 31 December 2017	Year ended 31 December 2016
Revenue from sales of goods and services	4,048	3,400
Purchases of goods and services	47,299	37,141

At 31 December 2017 and 31 December 2016 the Group had following accounts with associates and jointly controlled entities:

	31 December 2017	31 December 2016
Trade and other receivables	9,636	7,520
Trade and other payables	1,599	2,849
Borrowings granted	25,374	21,749
Borrowings received	59	20

Loans issued mainly include loan to Omirico Limited with 5.27% interest rate p.a. with principal amount and accrued interest to be paid before or at the date of loan repayment and the carrying value with interest accrued amounting to RUB 11,781 as at 31 December 2017 (RUB 13,057 as at 31 December 2016).

Key management personnel compensation

Key management personnel (the members of the Board of Directors and Management Committee of the Company and general directors of subsidiaries) receive short-term compensations, including salary, bonuses, other payments and long-term and short-term interest-free loans. Short-term compensations payable to the key management personnel of the Company and subsidiaries consist of contractual remuneration for their services in full time executive positions. The remunerations for the members of the Board of Directors of Company are subject to approval by the annual general meeting of shareholders. According to Russian legislation, the Group makes contributions to the pension fund of the Russian Federation to defined contributions plan for all of its employees including key management personnel. Key management personnel also participate in certain post-retirement compensation programs. The programs include pension benefits provided by the non-governmental pension fund, JSC "NPF "TRANSNEFT", and one-time payments programme at the retirement date.

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

25 RELATED PARTIES AND KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

	Year ended 31 December 2017	Year ended 31 December 2016
Salaries and bonuses	1,869	1,719
Termination benefits	8	28
Other	6	12
	1,883	**1,759**

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

	2017	2016
1 January	**22**	**5**
Granted	-	25
Repaid	(14)	(8)
31 December	**8**	**22**
due for repayment during 1 year	7	14
due for repayment after 1 year	1	8

During the year ended 31 December 2017 the Group contributed to JSC "NPF "TRANSNEFT" in favor of the key management personnel RUB 9 (for 2016 – RUB 48).

Contributions to the JSC "NPF "TRANSNEFT" represent transfer to the fund of the present value of future pension distributions in connection with retirement in accordance with the terms of contracts for non-state pension benefits. These distributions will be made when the right to receive the pension in accordance with established rules of JSC "NPF "TRANSNEFT" vest.

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

Total quantity of the persons who have received payments as the key management personnel as for the year ended 31 December 2017 constituted 62 persons (for the year ended 31 December 2016 – 64 persons).

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

26 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

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

Assets as the reporting date	Held-to-maturity investments	Loans and receivables	Financial assets measured at fair value through profit or loss	Available-for-sale financial assets
31 December 2017				
Cash and cash equivalents (Note 13)	-	76,162	-	-
Financial assets measured at fair value through profit or loss (Note 8)	-	-	58,859	-
Available-for-sale financial assets	-	-	-	251
Other non-current financial assets (Note 10)	-	23,096	-	-
Other current financial assets (Note 10)	13,638	195,130	-	-
Receivables (trade and other) (Note 12)	-	31,316	-	-
	13,638	**325,704**	**58,859**	**251**
31 December 2016				
Cash and cash equivalents (Note 13)	-	74,586	-	-
Financial assets measured at fair value through profit or loss (Note 8)	-	-	44,302	-
Available-for-sale financial assets	-	-	-	252
Other non-current financial assets (Note 10)	14,050	18,688	-	-
Other current financial assets (Note 10)	-	308,409	-	-
Receivables (trade and other) (Note 12)	-	25,328	-	-
	14,050	**427,011**	**44,302**	**252**

Liabilities at the reporting date	31 December 2017	31 December 2016
Financial accounts payable (trade and other) (Note 18)	60,459	85,823
Loans and borrowings (Note 15)	688,910	701,552
	749,369	**787,375**

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

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

Foreign exchange risk

The Group's overall strategy is to mitigate currency risk which arises from use of currencies other than the Russian rouble - the US dollar. Moreover, the Group has an approved policy for managing currency risk as well as policy for management of currency risk arising from operations with derivatives. The Group's foreign exchange exposure mainly arises on USD-denominated loans and borrowings, which the Group obtained in 2007-2010 (Note 15) and translation of cash balances and other financial assets (Note 10) denominated in US Dollars and Euro. Assets and liabilities of the Group denominated in Euro and Belarusian rouble which give rise to foreign currency exchange exposure are insignificant.

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

26 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

As at 31 December 2017, if the US Dollar had strengthened/weakened by 10% against the Russian rouble, with all other variables left constant, after tax profit and equity would have been RUB 9,768 lower/higher (for the year ended 31 December 2016 if the US Dollar had strengthened/weakened by 10% against the Russian rouble, with all other variables held constant (excluding derivatives), after tax profit and equity would have been – RUB 14,050 lower/higher), mainly as a result of foreign exchange losses/(gains) on translation of USD-denominated borrowings and USD-denominated cash balances into Russian roubles.

Interest rate risk

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

Loans and borrowings received at fixed rates expose the Group to fair value interest rate risk. The Group obtains loans from banks at current market interest rates. The interest rate risk is constantly monitored and, if necessary, measures will be taken to decrease the Group's exposure to it. The Group does not account for any of its fixed rate financial assets and liabilities at fair value through profit or loss (except for the assets relating to JSC "NPF "TRANSNEFT"). Therefore, a change in interest rates for these loans and borrowings at the reporting date would not affect profit or equity.

Loans and borrowings received by the Group under variable interest rate expose the Group to the risk of changes in the cash flows under loans and borrowings. As the Group receives bank loans for financing its investment projects, the part of borrowing costs are capitalised. An increase/decrease of 1% in interest rates for the year ended 31 December 2017 would have decreased/increased after tax profit for the year and equity by RUB 2,496 (year ended 31 December 2016 – RUB 2,607). This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

To monitor changes in interest rate risk affecting assets of JSC "NPF "TRANSNEFT" the Group performs a sensitivity analysis of its comprehensive income to interest rates change based on the simplified scenario of the symmetric increase or decline in rates by certain amount of basic interest rate points.

Sensitivity analysis for profit or loss before tax and equity due to changes in value of financial instruments at fair value through profit and loss resulting from changes in interest rates (set up as at 31 December 2017 according to the simplified scenario of the parallel shift of the yield curve for 100 basis points increase or decline) may be presented as follows:

	Profit / (loss) before income tax	Net assets to execute liabilities towards participants and insured persons
	31 December 2017	
100 basic points interest rates increase	(820)	(820)
100 basic points interest rates decline	784	784

Commodity price risk

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

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

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

26 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

Credit risk and compliance with contractual terms and obligations

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

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

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

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

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

Financial assets had the following credit ratings assigned by Moody's and other credit agencies ratings adjusted to Moody's rating scale as at 31 December 2017:

Credit rating	Cash and cash equivalents	Financial assets at fair value through profit or loss	Other financial assets
External credit rating Baa1 – Baa3	-	637	-
External credit rating Ba1 – Ba2	71,505	53,150	206,129
Other	4,657	5,072	25,735
	76,162	**58,859**	**231,864**

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

Risks associated with securities under trust management

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

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

Sensitivity analysis of net profit to changes in price of shares (computed on positions open as at 31 December 2017 and simplified scenario for 10% decline or increase in all share prices) can be shown as follows:

	31 December 2017
	Profit (loss) before income tax
10% increase in securities' quotes	5,886
10% decline in securities' quotes	(5,886)

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

26 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

Insurance risk

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

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

The table below shows sensitivity analysis of insurance contract liabilities under non-state pension:

		31 December 2017
Change in obligation in relation to obligation as at reporting date		
Analysis of change in liability in case of change in discount rate	-1 p.p.*	11.1%
	+1 p.p.*	(9.3)%
Analysis of change in liability in case of change in assumption of indexation of pensions	-1 p.p.*	(9.4)%
	+1 p.p.*	11.0%
Analysis of change in liability in case of change in assumption of mortality	-10%	5.2%
	+10%	(4.6)%

(*) p.p. – percentage point

Liability adequacy test for insurance contracts under OPS would not result in a deficit in all cases when indexation rate does not exceed discount rate. JSC “NPF “TRANSNEFT” estimated the minimal discount rate (with fixed indexation rate used in calculation as at the reporting date) equal to 5.55% and maximal indexation rate (with discount rate left unchanged at the reporting date) equal to 5.48% when the test will result in zero.

A decline in mortality probability by 41.2% will lead to a zero result in liability adequacy test relating to insurance contracts under OPS.

Liquidity risk

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

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

Offsetting and similar agreements

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

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

26 FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

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

	Trade and other receivables	Trade and other payables
31 December 2017		
Gross amounts	31,316	59,259
Net amounts shown in the consolidated statement of financial position	31,316	59,259
Amounts relating to recognised financial instruments which cannot be offset	(1,386)	(1,386)
Net amount	**29,930**	**57,873**

	Trade and other receivables	Trade and other payables
31 December 2016		
Gross amounts	25,328	85,720
Net amounts shown in the consolidated statement of financial position	25,328	85,720
Amounts relating to recognised financial instruments which cannot be offset	(5,026)	(5,026)
Net amount	**20,302**	**80,694**

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

		Contractual cash flows				
	Carrying amount	Total	12 months or less	1-2 years	2-5 years	More than 5 years
31 December 2017						
Loans and borrowings	688,910	891,421	150,491	139,811	299,707	301,412
Trade and other payables	60,459	60,630	59,260	1,195	176	-
	749,369	**952,051**	**209,750**	**141,006**	**299,883**	**301,412**
31 December 2016						
Loans and borrowings	701,552	895,916	155,594	140,634	266,781	332,907
Trade and other payables	85,823	85,823	85,720	103	-	-
	787,272	**981,739**	**241,314**	**140,737**	**266,781**	**332,907**

Fair values

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. The fair value of the receivables and payables approximates their carrying amounts at 31 December 2017 and 31 December 2016. The fair values of loans and borrowings are disclosed in Note 15, of other financial assets in Note 10.

Capital management

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

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

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

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

27 SEGMENT INFORMATION

Generally, Management of the Group analyses information by separate legal entities and operational segments are set by nature of its activity based on management accounting under RAS. The following segments were allocated: Oil transportation services, Oil product transportation services and Trading operations for sale of oil and oil products.

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

Segment information for the year ended 31 December 2017 and 31 December 2016 was as follows:

Year ended 31 December 2017	Oil transportation services	Oil products transportation services	Trading operations for sale of oil and oil products	Adjustments	Total IFRS
Revenue	664,177	69,137	145,588	5,435	884,337
Operating expenses net of amortisation and depreciation	(293,363)	(35,818)	(145,465)	(1,416)	(476,062)
Operating profit net of amortisation and depreciation	**370,814**	**33,319**	**123**	**4,019**	**408,275**
Amortisation and depreciation	(189,906)	(15,421)	(9)	52,699	(152,637)
Operating profit	**180,908**	**17,898**	**114**	**56,718**	**255,638**
Other expenses	-	-	-	-	(13,686)
Share of profit from associates and jointly controlled entities	-	-	-	-	15,847
Profit before income tax and finance income/(costs)	**180,908**	**17,898**	**114**	**56,718**	**257,799**
Finance income	-	-	-	-	109,177
Finance costs	-	-	-	-	(124,809)
Profit before income tax	**180,908**	**17,898**	**114**	**56,718**	**242,167**
Income tax expense	-	-	-	-	(50,362)
Profit for the reporting year	**180,908**	**17,898**	**114**	**56,718**	**191,805**

Year ended 31 December 2016	Oil transportation services	Oil products transportation services	Trading operations for sale of oil and oil products	Adjustments	Total IFRS
Revenue	645,950	67,929	134,255	-	848,134
Operating expenses net of amortisation and depreciation	(277,847)	(31,433)	(134,113)	3,476	(439,917)
Operating profit net of amortisation and depreciation	**368,103**	**36,496**	**142**	**3,476**	**408,217**
Amortisation and depreciation	(168,759)	(11,987)	(29)	52,252	(128,523)
Operating profit	**199,344**	**24,509**	**113**	**55,728**	**279,694**
Other expenses	-	-	-	-	(7,456)
Share of profit from associates and jointly controlled entities	-	-	-	-	19,519
Profit before income tax and finance income/(costs)	**199,344**	**24,509**	**113**	**55,728**	**291,757**
Finance income	-	-	-	-	290,908
Finance costs	-	-	-	-	(281,243)
Profit before income tax	**199,344**	**24,509**	**113**	**55,728**	**301,422**
Income tax expense	-	-	-	-	(68,515)
Profit for the reporting year	**199,344**	**24,509**	**113**	**55,728**	**232,907**

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

27 SEGMENT INFORMATION (CONTINUED)

Adjusting items for segments' revenue in the amount of RUB 5,435 for the year ended 31 December 2017 include revenue for connection of facilities to the trunk oil pipeline system and relates to differences between RAS and IFRS.

Adjusting items for segments' expenses in the amount of RUB 51,283 for the year ended 31 December 2017 and RUB 55,728 for the year ended 31 December 2016 include the following adjustments and reclassifications due to RAP and IFRS accounting differences:

	Year ended 31 December 2017	Year ended 31 December 2016
Dismantlement provision	(2,101)	(2,101)
Adjustment to Property plant and equipment to eliminate RAR revaluation effect and to record adjustment required under IAS 29 "Financial reporting in hyper-inflationary economies"	(53,581)	(52,633)
Pension provision	3,235	4,088
Deferred payment obligation	281	5,680
Others	883	(10,762)
Total adjusting items for segment's expenses	**(51,283)**	**(55,728)**

Geographical information. The Group's most part of assets attributable to reporting segments is primary located in the territory of the Russian Federation which results in the operating activity by each segment being carried out in the territory of the Russian Federation. The Oil products transportation services segment has certain assets located in the territory of the Republic of Belarus and the Republic of Kazakhstan.

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

	Year ended 31 December 2017	Year ended 31 December 2016
Russian Federation	716,718	695,972
China	140,737	127,113
Other countries	26,882	25,049
Total	**884,337**	**848,134**

Revenue from external customers in other countries mainly includes revenue from services provided to customers in the Republic of Kazakhstan.

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

The information about largest customers of the Group in Group's revenue is presented below:

	Year ended 31 December 2017	Year ended 31 December 2016
Companies under control of the state	367,931	350,213
China National United Oil Corporation	140,737	127,113
OAO Surgutneftegaz	105,482	107,874
PJSC LUKOIL	87,770	83,902
Total	**701,920**	**669,102**

Sales to the major customers are included in the results of the Oil transportation services, Oil products transportation services and Trading operations for sale of oil and oil products segments.

28 EVENTS AFTER THE REPORTING DATE

In February 2018 through public offering Transneft issued non-convertible interest-bearing documentary bonds for the total amount of RUB 15 billion with a coupon rate of 7.15%. Cash proceeds from issue of bonds were used for general corporate purposes.

In March 2018 Transneft got the ownership of 100% of shares of CPC Company and CPC Investments Company which were received as a payment made by the Federal Agency for the Management of State Property for additional issue of Transneft's ordinary registered uncertified shares (Note 14).