

Bashneft Group

**Interim Condensed
Consolidated Financial Statements
for the three and the nine months ended
30 September 2014 (unaudited)**

BASHNEFT GROUP

TABLE OF CONTENTS

	Page
STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014	1
INDEPENDENT AUDITORS' REPORT ON REVIEW OF THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS	2
INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014:	
Interim condensed consolidated statement of profit or loss and other comprehensive income	3
Interim condensed consolidated statement of financial position	4
Interim condensed consolidated statement of cash flows	5-6
Interim condensed consolidated statement of changes in equity	7
Notes to the interim condensed consolidated financial statements	8-27

BASHNEFT GROUP

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014

The following statement, which should be read in conjunction with the independent auditors' report on review of the interim condensed consolidated financial statements set out on page 2, is made with a view to distinguish the respective responsibilities of management and those of the independent auditors in relation to the interim condensed consolidated financial statements of Joint Stock Oil Company Bashneft (the "Company"), its subsidiaries and its structured entities (the "Group").

Management is responsible for the preparation of the interim condensed consolidated financial statements that present fairly in all material respects the consolidated financial position of the Group at 30 September 2014, its financial performance for the three and the nine months then ended, cash flows and changes in equity for the nine months then ended, in accordance with International Accounting Standard 34 *Interim Financial Reporting* ("IAS 34").

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

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IFRS are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's consolidated financial position and financial performance;
- Making judgements and estimates that are reasonable and prudent;
- Stating whether IAS 34 has been followed, subject to any material departures disclosed and explained in the interim condensed consolidated financial statements; and
- Making an assessment of the Group's ability to continue as a going concern.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the consolidated financial position of the Group, and which enable them to ensure that the interim condensed consolidated financial statements of the Group comply with IAS 34;
- Maintaining statutory accounting records in compliance with legislation and accounting standards in the Russian Federation;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The interim condensed consolidated financial statements for the three and the nine months ended 30 September 2014 were approved by:



A.L. Kovsik
President

Ufa, Russian Federation
21 November 2014



A.Y. Lisovenko
Chief Accountant

INDEPENDENT AUDITORS' REPORT ON REVIEW OF THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

To the shareholders and Board of Directors of Joint Stock Oil Company Bashneft:

Introduction

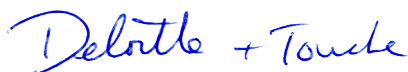
We have reviewed the accompanying interim condensed consolidated statement of financial position of Joint Stock Oil Company Bashneft and its subsidiaries (the "Group") as of 30 September 2014 and the related interim condensed consolidated statements of profit or loss and other comprehensive income for the three and the nine months then ended, changes in equity and cash flows for the nine months then ended, and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and presentation of this interim condensed consolidated financial information in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting*. Our responsibility is to express a conclusion on this interim condensed consolidated financial information based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial information is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting*.



Moscow, Russian Federation
21 November 2014

BASHNEFT GROUP

INTERIM CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles, except for earnings per share data

	Notes	Three months ended 30 September		Nine months ended 30 September	
		2014	2013	2014	2013
Revenue	7	162,861	156,571	472,705	417,054
Export tariffs and excise		(47,866)	(42,303)	(141,008)	(117,438)
Cost of purchased crude oil, gas and petroleum products		(34,929)	(36,658)	(104,083)	(95,059)
Taxes other than income tax	8	(19,527)	(18,812)	(58,188)	(52,129)
Production and operating expenses		(18,674)	(14,970)	(50,249)	(42,730)
Transportation expenses		(7,276)	(6,973)	(22,404)	(21,284)
Depletion and depreciation		(5,886)	(5,082)	(16,671)	(14,217)
Selling, general and administrative expenses		(4,291)	(4,015)	(11,480)	(11,433)
Other operating expenses, net		(313)	(624)	(1,956)	(812)
Operating profit		24,099	27,134	66,666	61,952
Impairment of investment in associate		-	(15,752)	-	(15,752)
Finance income	9	676	1,308	3,193	3,635
Finance costs	9	(3,800)	(2,206)	(9,075)	(7,462)
Foreign exchange (loss)/gain, net		(603)	(148)	(2,778)	451
Share of (loss)/profit of associate and joint ventures, net of income tax		(1)	(328)	58	(185)
Profit before income tax		20,371	10,008	58,064	42,639
Income tax	10	(4,578)	(2,496)	(12,459)	(9,837)
Profit for the period and total comprehensive income		15,793	7,512	45,605	32,802
Attributable to:					
Owners of the Company		15,611	7,388	45,425	32,542
Non-controlling interests		182	124	180	260
		15,793	7,512	45,605	32,802
EARNINGS PER SHARE					
Weighted average number of ordinary shares in issue during the period		144,417,602	157,085,505	149,991,906	157,085,505
Basic and diluted earnings per share attributable to shareholders of the parent company (Russian roubles per share)		92.19	38.73	254.78	170.61

BASHNEFT GROUP

INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION AT 30 SEPTEMBER 2014 (UNAUDITED) *Millions of Russian roubles*

	Notes	30 September 2014	31 December 2013
ASSETS			
Non-current assets			
Property, plant and equipment	11	364,207	277,369
Advances paid for acquisition of property, plant and equipment		973	805
Intangible assets		2,547	1,981
Financial assets	13	3,513	4,019
Investments in joint ventures	12	5,480	18,848
Long-term inventories		2,980	3,022
Other non-current assets		549	380
		380,249	306,424
Current assets			
Inventories		29,532	21,450
Financial assets	13	5,106	5,066
Trade and other receivables		28,254	27,317
Advances to suppliers and prepaid expenses		6,574	5,906
Income tax prepaid		317	289
Other taxes receivable		28,176	25,990
Cash and cash equivalents		37,620	16,395
		135,579	102,413
Assets classified as held for sale	5	-	38,962
TOTAL ASSETS		515,828	447,799
EQUITY AND LIABILITIES			
Capital and reserves			
Share capital	14	1,984	2,501
Treasury shares	5	(18,122)	(38,147)
Additional paid-in capital		81,409	72,682
Retained earnings		132,798	199,131
Equity attributable to owners of the Company		198,069	236,167
Non-controlling interests		8,139	155
		206,208	236,322
Non-current liabilities			
Loans and borrowings	15	139,209	78,902
Decommissioning provision		6,603	6,145
Deferred tax liabilities		43,370	33,489
Prepayment on oil products supply agreement	16	17,347	-
Other non-current liabilities	17	1,544	6,164
		208,073	124,700
Current liabilities			
Loans and borrowings	15	27,227	11,914
Trade and other payables		42,649	50,372
Dividends payable	14	408	275
Advances received		16,003	12,066
Provisions		490	895
Income tax payable		1,863	32
Other taxes payable		12,907	10,340
		101,547	85,894
Liabilities directly associated with assets classified as held for sale	5	-	883
TOTAL LIABILITIES		309,620	211,477
TOTAL EQUITY AND LIABILITIES		515,828	447,799

BASHNEFT GROUP

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED) *Millions of Russian roubles*

	Notes	Nine months ended 30 September	
		2014	2013
OPERATING ACTIVITIES			
Profit before income tax		58,064	42,639
Adjustments for:			
Depletion and depreciation		16,671	14,217
Loss on disposal of property, plant and equipment		741	457
Finance income		(3,193)	(3,635)
Finance costs		9,075	7,462
Impairment/(reversal of impairment) of property, plant and equipment	11	44	(12)
Share of (profit)/loss of associate and joint ventures		(58)	185
Impairment of investment in associate		-	15,752
Loss on disposal of subsidiaries		-	24
Foreign exchange loss/(gain), net		4,068	(370)
Change in provisions and allowances, net		198	1,221
Other, net		(1,092)	109
Operating cash flows before working capital changes		84,518	78,049
Movements in working capital:			
Inventories		(4,363)	(2,686)
Trade and other receivables		(5,856)	(8,977)
Advances to suppliers and prepaid expenses		402	171
Other taxes receivable		1,216	497
Trade and other payables		731	9,204
Advances received		3,296	(4,805)
Prepayment on oil products supply agreement	16	17,347	-
Other taxes payable		(292)	4,349
Cash generated from operations		96,999	75,802
Interest paid		(8,539)	(6,447)
Income tax paid		(10,763)	(10,423)
NET CASH GENERATED FROM OPERATING ACTIVITIES		77,697	58,932
INVESTING ACTIVITIES			
Payments for acquisition of property, plant and equipment		(31,643)	(22,989)
Proceeds from disposal of property, plant and equipment		3	1,042
Contributions to joint ventures		(2,961)	(8,966)
Repayment of contributions from joint venture	12	3,133	-
Acquisition of subsidiaries, net of cash acquired	4	(40,219)	-
Disposal of structured entities and subsidiaries		(24)	(5,810)
Payments for acquisition of intangible assets		(585)	(304)
Proceeds from disposal of investment in associate		-	6,469
Payments for acquisition of financial assets		(346)	(13,213)
Proceeds from disposal of financial assets		2,476	14,271
Interest received		1,610	2,545
Dividends received		-	115
NET CASH USED IN INVESTING ACTIVITIES		(68,556)	(26,840)

BASHNEFT GROUP

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED) FOR THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED) *Millions of Russian roubles*

	Notes	Nine months ended 30 September	
		2014	2013
FINANCING ACTIVITIES			
Payments for acquisition of non-controlling interests		-	(528)
Purchase of treasury shares	5	(17,869)	-
Proceeds from loans and borrowings		95,833	31,450
Repayments of loans and borrowings		(31,573)	(62,556)
Dividends paid by the Company		(35,597)	(4,650)
Dividends paid by subsidiaries		-	(5)
		<u>-</u>	<u>(5)</u>
NET CASH GENERATED FROM/(USED IN) FINANCING ACTIVITIES		10,794	(36,289)
Net increase/(decrease) in cash and cash equivalents		19,935	(4,197)
Cash and cash equivalents at beginning of the period		16,395	20,104
Effect of exchange rate changes on the balance of cash and cash equivalents held in foreign currencies		1,290	81
		<u>1,290</u>	<u>81</u>
Cash and cash equivalents at end of the period		37,620	15,988

BASHNEFT GROUP

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

	Notes	Share capital	Treasury shares	Additional paid-in capital	Retained earnings	Equity attributable to owners of the Company	Non-controlling interests	Total
Balance at 1 January 2013		2,501	(38,147)	83,651	194,975	242,980	4,928	247,908
Profit for the period		-	-	-	32,542	32,542	260	32,802
Total comprehensive income for the period		-	-	-	32,542	32,542	260	32,802
Dividends	14	-	-	-	(4,573)	(4,573)	(5)	(4,578)
Transactions with the Controlling shareholder		-	-	(10,455)	-	(10,455)	(5,004)	(15,459)
Acquisition of additional interests in subsidiaries		-	-	-	490	490	(1,017)	(527)
Other equity transactions		-	-	(514)	(51)	(565)	499	(66)
Balance at 30 September 2013		2,501	(38,147)	72,682	223,383	260,419	(339)	260,080
Balance at 1 January 2014		2,501	(38,147)	72,682	199,131	236,167	155	236,322
Profit for the period		-	-	-	45,425	45,425	180	45,605
Total comprehensive income for the period		-	-	-	45,425	45,425	180	45,605
Dividends	14	-	-	-	(35,730)	(35,730)	-	(35,730)
Transactions with the Controlling shareholder	4	-	-	7,575	-	7,575	4,205	11,780
Effect of reorganisation of CJSC Sistema-Invest and the Group	5	(517)	20,025	-	(76,028)	(56,520)	-	(56,520)
Non-controlling interests arising on change of control over LLC Bashneft-Polyus	4	-	-	-	-	-	27	27
Transfer of license on Trebs and Titov deposit to Bashneft-Polyus	17	-	-	1,152	-	1,152	3,616	4,768
Other equity transactions		-	-	-	-	-	(44)	(44)
Balance at 30 September 2014		1,984	(18,122)	81,409	132,798	198,069	8,139	206,208

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

1. GENERAL INFORMATION

Organisation and operations

Joint Stock Oil Company Bashneft (the “Company” or “Bashneft”), its subsidiaries and structured entities (together referred to as the “Group” or the “Bashneft Group”) are primarily involved in oil production, refining, marketing and distribution of petroleum products in the Russian Federation. The Group’s oil production, refining, marketing and distribution base includes oil and gas fields, refineries and petrol stations. Bashneft is the parent company of a vertically integrated group of oil and gas companies.

The Company was incorporated in the Russian Federation as an open joint stock company on 13 January 1995, following the privatisation of Bashneft production association. The Company’s registered office is located at 30, bldg.1, Karl Marx Street, the City of Ufa, the Republic of Bashkortostan, 450077, Russian Federation.

The following principal subsidiaries incorporated in the Russian Federation were included in the scope of consolidation at 30 September 2014 and 31 December 2013:

Company	Principal activities	Group’s effective interest	
		30 September 2014	31 December 2013
LLC Bashneft-Dobycha	Production of crude oil and gas	100%	100%
LLC Bashneft-Retail Sales (former LLC Bashneft-Udmurtia)	Petroleum products trading	100%	100%
LLC Burneftegaz ⁽¹⁾	Exploration and production of crude oil	100%	not applicable
LLC Bashneft-Polyus ⁽²⁾	Exploration and production of crude oil	74.9%	not applicable

⁽¹⁾ In March 2014 the Group acquired a 100% interest in LLC Burneftegaz (“Burneftegaz”), which is engaged in exploration and production of crude oil in the Tyumen District (refer to note 4).

⁽²⁾ In May 2014 the Company and OAO LUKOIL signed an amended agreement that transferred effective control over the operational and financial activities of LLC Bashneft-Polyus (“Bashneft-Polyus”) to the Company (refer to note 4).

At 30 September 2014, the Group had five structured entities (31 December 2013: six structured entities) which were established to provide supporting services to the Group and which are engaged in the supporting of production and refining of crude oil. Such structured entities have been consolidated.

Controlling shareholder

JSFC Sistema (“Sistema”) is the controlling shareholder of Bashneft. The controlling shareholder of Sistema and the ultimate controlling party of Bashneft Group is Mr. Vladimir P. Evtushenkov.

On 30 October 2014, the Moscow Commercial Court upheld the claim of the Prosecutor General’s Office of the Russian Federation for the recovery of JSOC Bashneft’s shares owned by JSFC Sistema and CJSC Sistema-Invest in favor of the Russian Federation. This ruling has not come into force and under the Russian legislation an appeal against it may be filed within a one-month period ending on 8 December 2014. On 12 November 2014, Sistema’s Board of Directors issued a statement indicating that the decision of the Moscow Commercial Court will not be appealed. Should no appeal be launched within the permitted time, the controlling block of shares owned by Sistema will revert to the Russian Federation.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Going concern

In assessing its going concern status, the Group has taken into account its financial position, anticipated future trading performance, its borrowings and other facilities and its capital expenditure commitments and plans, together with other risks facing the Group. After making appropriate enquires, the Group considers that it has adequate resources to continue in operational existence for at least the next 12 months from the date of issuance of these interim condensed consolidated financial statements. Consequently, the Group has determined that it is appropriate to adopt the going concern basis in the preparation of these interim condensed consolidated financial statements.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

These interim condensed consolidated financial statements for the three and the nine months ended 30 September 2014 have been prepared in accordance with IAS 34. These interim condensed consolidated financial statements do not include all the information and disclosure required in the annual consolidated financial statements and should be read in conjunction with the Group's annual consolidated financial statements for the years ended 31 December 2013, 2012 and 2011, which have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

The same accounting policies and methods of computation have been followed in these interim condensed consolidated financial statements as were applied in the preparation of the Group's consolidated financial statements for the years ended 31 December 2013, 2012 and 2011 except for amendments, related to application of new standards or interpretations described below.

Standards and interpretations effective in the current period

Several amendments including amended IAS 32 *Financial Instruments: Presentation*, IFRS 10 *Consolidated Financial Statements*, IFRS 12 *Disclosure of Interests in Other Entities*, IAS 27 *Separate Financial Statement*, IAS 36 *Impairment of assets*, IAS 39 *Financial instruments: Recognition and Measurement* and IFRIC 21 *Levies* were applied for the first time in these interim condensed consolidated financial statements. The application of these amendments did not result in significant changes to the Group's financial position or results of operations.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

The critical accounting judgements, estimates and assumptions made by management of the Group and applied in these interim condensed consolidated financial statements for the three and the nine months ended 30 September 2014 are consistent with those applied in the preparation of annual consolidated financial statements of the Group for the years ended 31 December 2013, 2012 and 2011.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

4. BUSINESS COMBINATIONS

LLC Burneftegaz

On 26 March 2014 the Group acquired a 100% interest in the outstanding charter capital of Burneftegaz, which is engaged in exploration and production of crude oil in the Tyumen District of the Russian Federation for total cash consideration of RUB 35,953 million. The acquisition of Burneftegaz followed the Group's strategy for the upstream segment growth, which involved the expansion of the resource base of the Group by acquiring assets with considerable production potential.

The accounting for the acquisition of Burneftegaz has been provisionally determined at 26 March 2014. The valuation of the fair values of identifiable assets and liabilities was not completed at the reporting date.

At the date of acquisition, the provisional fair values of identifiable assets and liabilities of Burneftegaz were as follows:

	Provisional fair value at the acquisition date
ASSETS	
Property, plant and equipment	41,784
Advances paid for acquisition of property, plant and equipment	526
Inventories	293
Trade and other receivables	142
Advances to suppliers and prepaid expenses	110
Other taxes receivable	107
Cash and cash equivalents	208
Other assets	42
	43,212
LIABILITIES	
Deferred tax liabilities	(5,516)
Trade and other payables	(691)
Advances received	(185)
Other taxes payable	(478)
Borrowings	(363)
Other liabilities	(26)
	(7,259)
Fair value of net assets acquired	35,953
Cash consideration	35,953
Excess of the cost of acquisition over the Group's share in the fair value of net assets acquired	-
Net cash outflow arising on acquisition	
Consideration paid	35,953
Cash and cash equivalents acquired	(208)
Net cash outflow on acquisition	35,745

Burneftegaz contributed RUB 5,065 million of revenue, RUB 296 million of profit before tax and RUB 192 million of profit from the date of acquisition to 30 September 2014.

The Group's financial results if the combination had taken place at the beginning of the nine months ended 30 September 2014 are not disclosed as Burneftegaz did not prepare financial statements in accordance with IFRS before the acquisition.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

LLC Bashneft-Polyus

Until 23 May 2014 Bashneft-Polyus was a joint venture between the Company and OAO LUKOIL established for the development of Trebs and Titov oil deposits. The Company holds 74.9% interest in the charter capital of Bashneft-Polyus.

On 23 May 2014 the Company and OAO LUKOIL agreed to change their participation agreement which substantially altered effective control over the operational and financial activities of Bashneft-Polyus in favour of the Company.

At the date of acquisition of control, the fair values of identifiable assets and liabilities of Bashneft-Polyus were as follows:

	Fair value at the acquisition date
ASSETS	
Property, plant and equipment	11,644
Advances paid for acquisition of property, plant and equipment	46
Inventories	846
Trade and other receivables	15,436
Advances to suppliers and prepaid expenses	412
Other taxes receivable	2,351
Cash and cash equivalents	11
Other assets	2
	30,748
LIABILITIES	
Trade and other payables	(4,606)
Advances received	(17)
Other taxes payable	(2,232)
Borrowings from OAO LUKOIL and JSOC Bashneft	(23,334)
Deferred tax liabilities	(386)
Other liabilities	(67)
	(30,642)
Fair value of net assets obtained	106
Fair value of previously held share of investment in joint venture, net of loans from the Group treated as additional contribution to the joint venture	451
Non-controlling interests' share in fair value of net assets	27
Excess of the cost of acquisition over the Group's share in the fair value of net assets acquired, recognised in Other operating expenses, net	372
Net cash inflow arising on acquisition	
Cash and cash equivalents acquired	11
Net cash inflow on acquisition	11

Following the consolidation of Bashneft-Polyus, loans issued by the Group to Bashneft-Polyus in the amount of RUB 17,380 million at the date of acquisition, which were previously presented as an additional contribution to the joint venture, were eliminated in full as intra-group balances.

Bashneft-Polyus contributed RUB 5,261 million of revenue, RUB 969 million of profit before tax and RUB 998 million of profit from the date of acquisition to 30 September 2014.

If the acquisition of control had taken place at the beginning of the nine months ended 30 September 2014, the Group's revenue would have been RUB 474,318 million, profit for the nine months would have been RUB 45,640 million.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

Optan group

In July and August 2014 Bashneft through a series of transactions acquired 100% stakes in five legal entities which own a network of 91 petrol stations operated under the “Optan” brand (“Optan group”) and 11 land plots located in 12 regions of the Russian Federation for a total cash consideration of RUB 7,715 million. The acquisition of the Optan group is part of Bashneft’s strategy to expand its own retail network. Optan Group’s petrol stations are in high-priority regions in geographical proximity to the Group’s refining complex in Ufa.

At the date of acquisition, the fair values of identifiable assets and liabilities of Optan group were as follows:

	<u>Fair value at the acquisition date</u>
ASSETS	
Property, plant and equipment	10,210
Intangible assets	277
Other assets	105
	<u>10,592</u>
LIABILITIES	
Deferred tax liabilities	(1,848)
Borrowings	(949)
Other liabilities	(80)
	<u>(2,877)</u>
Fair value of net assets acquired	<u>7,715</u>
Cash consideration	<u>7,715</u>
Excess of the cost of acquisition over the Group’s share in the fair value of net assets acquired	<u>-</u>
Net cash outflow arising on acquisition	
Consideration paid	7,715
Cash and cash equivalents acquired	(8)
	<u>7,707</u>

The acquired petrol stations’ network is utilized by the Company for its retail activities and, therefore, revenue and profit contribution of Optan Group is insignificant to the Group.

The Group’s financial results if the combination had taken place at the beginning of the nine months ended 30 September 2014 are not disclosed as Optan group did not prepare financial statements in accordance with IFRS before the acquisition.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

OJSC United Petrochemical Company

On 17 September 2013 the Group entered into agreement to sell its 98% interest in OJSC United Petrochemical Company ("UPC") to Sistema for cash consideration of RUB 6,200 million payable in one year. UPC was the holding company of the petrochemical assets of the Group, including OJSC Ufaorgsintez ("Ufaorgsintez"). On 24 September 2014 this agreement was terminated and the Group re-obtained the control over UPC.

Both transactions were under common control so the assets and liabilities are recorded at their historical carrying values. As a result of the termination of the sale agreement the Group recognised a gain on acquisition of RUB 7,575 million, net of related income taxes in the amount of RUB 831 million, within additional paid-in capital in the interim condensed consolidated statement of changes in equity being the result of the transaction with the Group's controlling shareholder.

The result of transaction is set out below:

	Carrying value at the acquisition date
ASSETS	
Property, plant and equipment	13,441
Intangible assets	207
Investments in joint venture	506
Inventories	1,973
Trade and other receivables	666
Advances to suppliers and prepaid expenses	542
Taxes receivable	1,079
Financial assets	1,240
Cash and cash equivalents	3,572
Other assets	88
	23,314
LIABILITIES	
Deferred tax liabilities	(1,468)
Trade and other payables	(2,361)
Advances received	(438)
Other liabilities	(236)
	(4,503)
Net assets acquired	18,811
Non-controlling interests	(4,205)
	14,606
Income tax expense recognised on acquisition of UPC	(831)
Consideration receivable on disposal of UPC	(6,200)
Gain on acquisition of UPC	7,575
Net cash inflow arising on acquisition	
Cash and cash equivalents acquired	3,572
Net cash inflow on acquisition	3,572

UPC contributed RUB 796 million of revenue, RUB 127 million of profit before tax and RUB 96 million of profit from the date of acquisition to 30 September 2014.

If the acquisition of control had taken place at the beginning of the nine months ended 30 September 2014, the Group's revenue would have been RUB 492,935 million and profit for the nine months would have been RUB 46,541 million.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

Other acquisition

During the nine months ended 30 September 2014 the Group also acquired a subsidiary in the Downstream segment for a total cash consideration of RUB 350 million. The fair value of the net assets acquired approximated the consideration paid.

5. REORGANISATION OF CJSC SISTEMA-INVEST AND THE GROUP

On 3 February 2014 at an Extraordinary General Shareholders' Meeting of the Company, a reorganisation programme was approved involving establishment of CJSC Bashneft-Invest ("Bashneft-invest") through a spinoff from CJSC Sistema-Invest ("Sistema-invest") and its consolidation with Bashneft.

In April 2014 as part of the reorganisation of the Group, the Company acquired 2,724,173 of its own ordinary shares and 8,885,866 of its own preferred shares for total cash consideration of RUB 17,869 million.

Bashneft-invest was created on 5 May 2014 as a wholly owned subsidiary of the Company through a spinoff from Sistema-invest. Sistema-invest is a legal entity controlled by Sistema that owned equity interests in the Company, Ufaorgsintez and OJSC Bashkirian Power Grid Company. Bashneft's effective interest of 49.41% in the assets and liabilities of Sistema-invest were accounted for as held for sale from 31 December 2013. On the date of the spinoff Bashneft-invest effectively obtained 9,943,730 ordinary shares of the Company and acquired direct ownership of 28,196,195 ordinary shares previously recognised as assets effectively owned, but held by Sistema-invest. Those shares were accounted for as treasury shares in the financial statements of the Group at the date of the transaction. Additionally, Bashneft-invest assumed the liabilities that existed under the loan payable by Sistema-invest to the Company.

As a result of the reorganisation the Company no longer owns any shares in Sistema-invest.

The result from the reorganisation of Sistema-invest is presented below:

	<u>5 May 2014</u>
Decrease in assets classified as held for sale	(39,483)
Decrease in liabilities directly associated with assets classified as held for sale	<u>832</u>
Increase in treasury shares	<u><u>38,651</u></u>

On 6 May 2014 Bashneft-invest was legally merged with the Company. The reorganisation of the Group was completed on the date of the merger when the Company cancelled 38,139,925 ordinary shares and 8,885,866 preferred shares which were obtained through reorganisation of Sistema-invest and buy back transactions, respectively.

The result from the cancellation of treasury shares is presented below:

	<u>6 May 2014</u>
Decrease in treasury shares	(76,545)
Decrease in share capital	<u>517</u>
Decrease in retained earnings	<u><u>(76,028)</u></u>

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

6. SEGMENT INFORMATION

The Board of Directors (the "Board") is the Group's chief operating decision maker. Operating segments have been determined based on the information reviewed by the Board for the purposes of assessing performance.

The Board considers financial and operational results based on the stages of the production process and the marketing of associated products. The Group's reportable segments under IFRS 8 *Operating Segments* are, therefore, as follows:

- Upstream: this segment comprises subsidiaries and business units of the Company engaged in the exploration and production of crude oil; and
- Downstream: this segment comprises subsidiaries and business units of the Company engaged in processing and sale of crude oil, oil products and petrochemicals on export and domestic markets.

The information about other subsidiaries and business units of the Company engaged in non-core activities, none of which meet the criteria for separate reporting, is presented as All other segments.

During the three and the nine months ended 30 September 2013 the operations of UPC and its subsidiaries were included in the Reconciling item column below as the information about their operations was not included in the reports provided to the Board. Starting from 24 September 2014 the operations of UPC and its subsidiaries are included in the Downstream segment as the information about their operations is included in the reports provided to the Board.

There are varying levels of integration between the Group's operating segments. Inter-segment revenues of the Upstream segment represent oil transfer to the Downstream segment for the purpose of refining and crude oil sales and measured with a reference to market prices for crude oil. Inter-segment revenues of the Downstream segment and All other segments represent oil products deliveries and services provided. Inter-segment pricing is estimated to represent an arm's length basis.

Information regarding the results of each reportable segment is reviewed by the Board. Segment EBITDA is used to measure segment performance, as management believes that such information is the most relevant in evaluating the results of segments relative to other entities that operate within these industries. Segment EBITDA is determined as summation of Operating profit and Depletion and depreciation. Since Segment EBITDA is not a standard IFRS measure, the Group's definition of Segment EBITDA may differ from that of other companies. The significant accounting policies of the reportable and other segments are the same as the Group's accounting policies.

Information about the Group's reportable segments for the three months ended 30 September 2014 is presented below:

	<u>Upstream</u>	<u>Downstream</u>	<u>All other segments</u>	<u>Eliminations</u>	<u>Consolidated</u>
External revenues	976	161,669	216	-	162,861
Inter-segment revenues	<u>47,242</u>	<u>48</u>	<u>1,384</u>	<u>(48,674)</u>	<u>-</u>
External expenses	(34,451)	(102,792)	(1,519)	-	(138,762)
Inter-segment expenses	<u>(1,203)</u>	<u>(47,843)</u>	<u>(67)</u>	<u>49,113</u>	<u>-</u>
Segment EBITDA	<u>15,206</u>	<u>14,141</u>	<u>199</u>	<u>439</u>	29,985
Depletion and depreciation					(5,886)
Finance income					676
Finance costs					(3,800)
Foreign exchange loss, net					(603)
Share of loss of joint ventures, net of income tax					<u>(1)</u>
Profit before income tax					<u>20,371</u>
Income tax expense					<u>(4,578)</u>
Profit for the period					<u>15,793</u>

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

Information about the Group's reportable segments for the three months ended 30 September 2013 is presented below:

	<u>Upstream</u>	<u>Down- stream</u>	<u>All other segments</u>	<u>Recon- ciling item</u>	<u>Elimi- nations</u>	<u>Consoli- dated</u>
External revenues	236	149,322	1,517	5,496	-	156,571
Inter-segment revenues	48,534	2,505	7,067	191	(58,297)	-
External expenses	(27,259)	(94,779)	(4,344)	(3,055)	-	(129,437)
Inter-segment expenses	(4,732)	(48,557)	(3,343)	(2,567)	59,199	-
Segment EBITDA	18,558	10,934	1,319	503	902	32,216
Depletion and depreciation						(5,082)
Impairment of investment in associate						(15,752)
Finance income						1,308
Finance costs						(2,206)
Foreign exchange loss, net						(148)
Share of loss of associate and joint venture, net of income tax						(328)
Profit before income tax						10,008
Income tax expense						(2,496)
Profit for the period						7,512

Information about the Group's reportable segments for the nine months ended 30 September 2014 is presented below:

	<u>Upstream</u>	<u>Downstream</u>	<u>All other segments</u>	<u>Eliminations</u>	<u>Consoli- dated</u>
External revenues	3,387	468,501	817	-	472,705
Inter-segment revenues	145,707	1,399	3,677	(150,783)	-
External expenses	(101,284)	(300,550)	(4,205)	-	(406,039)
Inter-segment expenses	(2,221)	(148,396)	(166)	150,783	-
Segment EBITDA	52,886	29,774	677	-	83,337
Depletion and depreciation					(16,671)
Finance income					3,193
Finance costs					(9,075)
Foreign exchange loss, net					(2,778)
Share of profit of joint ventures, net of income tax					58
Profit before income tax					58,064
Income tax expense					(12,459)
Profit for the period					45,605

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

Information about the Group's reportable segments for the nine months ended 30 September 2013 is presented below:

	Upstream	Down-stream	All other segments	Recon-ciling item	Elimi-nations	Consoli-dated
External revenues	941	397,467	4,940	13,706	-	417,054
Inter-segment revenues	125,545	7,494	17,551	2,317	(152,907)	-
External expenses	(73,928)	(259,732)	(13,338)	(8,104)	-	(355,102)
Inter-segment expenses	(11,782)	(126,094)	(8,149)	(6,894)	152,919	-
Segment EBITDA	45,520	26,045	2,309	2,283	12	76,169
Depletion and depreciation						(14,217)
Impairment of investment in associate						(15,752)
Finance income						3,635
Finance costs						(7,462)
Foreign exchange gain, net						451
Share of loss of associate and joint venture, net of income tax						(185)
Profit before income tax						42,639
Income tax expense						(9,837)
Profit for the period						32,802

Substantially all of the Group's operations are conducted in the Russian Federation. Therefore, the Group has not presented any geographical disclosure about its non-current assets by geographical area, as amounts not pertaining to the Russian Federation are immaterial.

The Group's revenue from external customers by geographical location is presented below:

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Export outside the Customs Union	87,709	85,286	269,494	230,588
Russian Federation	70,303	67,055	190,699	173,075
Export to countries of the Customs Union	4,849	4,230	12,512	13,391
Total	162,861	156,571	472,705	417,054

7. REVENUE

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Petroleum products	119,302	123,847	348,477	327,003
Crude oil	42,022	29,948	118,750	81,747
Other revenue	1,537	2,776	5,478	8,304
Total	162,861	156,571	472,705	417,054

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

8. TAXES OTHER THAN INCOME TAX

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Mineral extraction tax	17,615	16,492	52,139	44,420
Contributions to Pension Fund of the Russian Federation	1,016	1,329	3,183	4,396
Property tax	372	393	1,164	1,196
Other social contributions	322	413	1,070	1,388
Other taxes	202	185	632	729
Total	19,527	18,812	58,188	52,129

9. FINANCE INCOME AND FINANCE COSTS

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Finance income				
Interest income on loans, promissory notes and bonds	132	868	1,759	2,245
Interest income on cash and deposits	544	440	1,434	1,272
Dividends income	-	-	-	118
Total	676	1,308	3,193	3,635
Finance costs				
Interest expense on loans and borrowings	3,625	1,997	8,547	6,836
Unwinding of discount	153	197	458	590
Other accretion expenses	22	12	70	36
Total	3,800	2,206	9,075	7,462

10. INCOME TAX

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Current period income tax expense	4,560	7,106	12,648	14,163
Adjustments relating to current income tax of prior years	(3)	37	11	35
Current income tax expense	4,557	7,143	12,659	14,198
Deferred tax expense/(benefit)	21	(4,647)	(200)	(4,361)
Income tax expense	4,578	2,496	12,459	9,837

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

11. PROPERTY, PLANT AND EQUIPMENT

	Nine months ended 30 September	
	2014	2013
Cost		
Balance at the beginning of the period	356,736	351,779
Acquisitions of subsidiaries	89,179	348
Disposal of structured entities and subsidiaries	(1)	(34,829)
Constructions and additions	31,658	30,733
Disposals	(2,511)	(2,069)
Contribution to LLC Vostok NAO Oil Company (refer to note 12)	(4,775)	-
Balance at the end of the period	470,286	345,962
Accumulated depletion, depreciation and impairment		
Balance at the beginning of the period	(79,367)	(74,630)
Acquisition of subsidiaries	(11,696)	-
Charge for the period	(16,739)	(14,047)
Disposal of structured entities and subsidiaries	-	13,676
Disposals	1,767	570
Impairment	(44)	12
Balance at the end of the period	(106,079)	(74,419)
Net book value		
At the beginning of the period	277,369	277,149
At the end of the period	364,207	271,543

12. INVESTMENTS IN JOINT VENTURES

	Nine months ended 30 September 2014
Balance at the beginning of the period	18,848
Establishment of LLC Vostok NAO Oil Company	4,975
Repayment of contributions from Bashneft-Polyus	(3,133)
Additional contributions to Bashneft-Polyus	2,012
Obtaining of control over Bashneft-Polyus (refer to note 4)	(17,831)
Group's share of gain eliminated on transaction with joint venture	45
Share of profit for the period	58
Acquired on acquisition of UPC (refer to note 4)	506
Balance at the end of the period	5,480

In May 2014 the Company and LLC Lukoil-Komi established a joint venture, LLC Vostok NAO Oil Company, to conduct geological exploration and prospecting and produce hydrocarbons in the Nenets Autonomous District. The Company and LLC Lukoil-Komi have equal 50.0% stake in this joint venture. In July 2014 the Group transferred licenses for geological exploration and prospecting and production of hydrocarbons in the Nenets Autonomous District in the amount of RUB 4,775 million to LLC Vostok NAO Oil Company.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

13. FINANCIAL ASSETS

	<u>30 September 2014</u>	<u>31 December 2013</u>
Non-current investments		
Loans given, at amortised cost	3,504	3,506
Deposits	9	-
Available-for-sale investment in Ufaorgsintez	-	423
Derivative financial instruments	-	90
Total	<u>3,513</u>	<u>4,019</u>
Current investments		
Loans given, at amortised cost	5,106	5,020
Deposits	-	46
Total	<u>5,106</u>	<u>5,066</u>

14. SHARE CAPITAL

Authorised, issued and fully paid share capital

	<u>30 September 2014</u>	<u>31 December 2013</u>
150,570,662 (31 December 2013: 188,710,587) ordinary shares with a par value of RUB 1.00	1,656	2,076
29,788,012 (31 December 2013: 38,673,878) preferred shares with a par value of RUB 1.00	328	425
Total	<u>1,984</u>	<u>2,501</u>

As a result of the Group reorganisation on 6 May 2014 (refer to note 5) the Company cancelled 38,139,925 ordinary and 8,885,866 preferred shares which were obtained through reorganisation of Sistema-invest and buy back transactions in 2014, respectively.

Treasury shares

At 30 September 2014 the number of treasury shares was 11,017,228 shares (31 December 2013: 36,647,659 shares). 4,864,168 shares out of these treasury shares were restricted for further sales at 30 September 2014.

Dividends

On 27 June 2013, the Company declared a dividend of RUB 24 per ordinary and preferred share amounting to RUB 5,324 million. A part of the dividend declared was attributable to the companies of the Group.

On 10 June 2014, the Company declared a dividend of RUB 211 per ordinary and preferred share amounting to RUB 37,481 million. A part of the dividend declared was attributable to the companies of the Group. At 30 September 2014 dividends payable equaled RUB 408 million.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

15. LOANS AND BORROWINGS

	30 September 2014		31 December 2013	
	Rate, %	Outstanding balance	Rate, %	Outstanding balance
Non-current liabilities				
Unsecured fixed interest rate loans and borrowings	8.00%-10.55%	86,239	8.35%-8.85%	19,984
Unsecured non-convertible bonds issued in February 2013	8.65%-8.85%	29,967	8.65%-8.85%	29,960
Unsecured non-convertible bonds issued in May 2014	10.70%	10,000	-	-
Secured floating rate borrowings	Libor 1M+1.70%	7,730	Libor 1M+1.70%	13,697
Unsecured non-convertible bonds issued in December 2009	8.35%	5,273	8.35%	5,269
Unsecured non-convertible bonds issued in February 2012	-	-	9.0%	9,992
Total		139,209		78,902
Current liabilities				
Current portion of secured floating rate borrowings	Libor 1M+1.70%	11,769	Libor 1M+1.55%-1.70%	8,904
Unsecured non-convertible bonds issued in February 2012	9.00%	9,997	-	-
Unsecured non-convertible bonds issued in December 2011	0.10%	3,015	0.10%	3,010
Unsecured floating rate loan	MosPrime	1,683	-	-
Unsecured fixed interest rate loans and borrowings	8.25%	759	-	-
Secured fixed interest rate overdraft	12.75%	4	-	-
Total		27,227		11,914

As a result of the decision of Moscow Commercial Court on the recovery of JSOC Bashneft's shares owned by Sistema and Sistema-invest in favor of the Russian Federation (refer to note 1), some debt may become payable on demand due to covenants in respect of changes in control. The amount of such non-current debt at 30 September 2014 not covered by waivers as at the date of the approval of these interim condensed consolidated financial statements equaled to RUB 4,321 million.

Unsecured non-convertible bonds

In May 2014 the Group issued 10,000,000 non-convertible RUB-denominated bonds at a par value of RUB 1,000 and maturity in May 2024. These bonds have a coupon rate 10.7% per annum from the date of issuance to November 2018 payable semi-annually. Subsequent coupon rates are to be determined in November 2018 at which point the bondholders have the right to redeem the bonds at par value.

Unsecured fixed interest rate loans and borrowings

At 30 September 2014, unsecured fixed interest rate loans and borrowings were denominated in RUB and were obtained from a variety of lenders. The loans and borrowings mature from 2014 through 2019 (31 December 2013: denominated in RUB with maturity from 2016 through 2019).

16. PREPAYMENT ON OIL PRODUCTS SUPPLY AGREEMENT

In April 2014 the Company entered into a long-term oil products supply agreement and subsequently received an advance of US Dollar 500 million (RUB 17,347 million). The total minimum delivery volume approximates 3,150 thousand tons of oil products in the period from the date of the contract to July 2019.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

The agreements stipulate pricing calculated with reference to market quotes, and prepayments are settled through physical deliveries of oil products.

The prepayments will be reimbursed starting from 2016. The Group considers this agreement to be a regular way sale contract which was entered into for the purpose of the delivery of a non-financial item in accordance with the Company's expected sale requirements.

The outstanding balance is subject to interest at LIBOR + 1.5% per annum.

17. OTHER NON-CURRENT LIABILITIES

	<u>30 September 2014</u>	<u>31 December 2013</u>
Defined benefit obligation	1,348	1,216
Constructive obligation to OAO LUKOIL	-	4,768
Other non-current liabilities	<u>196</u>	<u>180</u>
Total	<u>1,544</u>	<u>6,164</u>

Constructive obligation to OAO LUKOIL

In 2012 as a result of the Federal Agency for Subsoil Use ("Rosnedra") order Trebs and Titov oilfield license was transferred to the Company from Bashneft-Polyus, which was a joint venture of the Company and OAO LUKOIL. As a result of that the license with a carrying value of RUB 18,490 million was recognised within Bashneft's property, plant and equipment with the corresponding decrease in the investment in Bashneft-Polyus. Cash consideration in the amount of RUB 4,768 million paid to the Company by OAO LUKOIL for 25.1% shares of Bashneft-Polyus was recognised in other non-current liabilities as a constructive obligation.

On 23 May 2014, as a result of the Rosnedra's order Trebs and Titov oilfield license was transferred from Bashneft to its subsidiary Bashneft-Polyus. This transaction resulted in an increase in non-controlling interests in the amount of RUB 3,616 million with the corresponding decrease in constructive obligation to OAO LUKOIL in the amount of RUB 4,768 million. As a result of this transaction the Group recognised a gain in the amount of RUB 1,152 million within Additional paid-in Capital in the interim condensed consolidated statement of changes in equity.

18. RELATED PARTIES

At 30 September 2014 and 31 December 2013, the Group had the following outstanding balances with related parties:

	<u>Amount owed by related parties</u>	
	<u>30 September 2014</u>	<u>31 December 2013</u>
Other Sistema Group companies	16,708	15,754
Sistema-invest	1,330	30,166
Joint ventures of the Group	<u>27</u>	<u>402</u>
Total	<u>18,065</u>	<u>46,322</u>

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

	Amount owed to related parties	
	30 September 2014	31 December 2013
Other Sistema Group companies	5,858	5,290
Joint ventures of the Group	1,683	16,922
Sistema-invest	-	655
Total	7,541	22,867

The amounts outstanding were unsecured and are expected to be settled in cash. The Group does not create an allowance for doubtful receivables in respect of outstanding balances of related parties. No balances owed by related parties were past due but not impaired.

No expense has been recognised in the current period for bad debts in respect of amounts owed by related parties.

The Group entered into the following transactions with related parties:

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Sistema-invest				
Dividends declared	-	-	4,061	702
Loans issued	-	-	-	10,024
Proceeds from repayment of loans issued	-	-	-	5,856
Dividends received	-	-	-	117
Interest income	-	284	519	786
Other Sistema Group companies and its affiliates				
Dividends declared	-	-	24,037	2,739
Sales of interests in subsidiaries	-	10,300	-	10,300
Cash placed on bank deposits	-	20	-	157
Proceeds from repayment of bank deposits	46	14	46	4,010
Proceeds from repayment of loans issued	51	-	51	-
Sale of goods and services	2,796	130	10,655	380
Purchase of goods and services	5,604	2,489	16,485	10,703
Purchase of property and construction services	3,495	561	7,147	660
Interest income	220	246	621	798
Proceeds from short-term borrowing	-	-	901	-
Repayment of short-term borrowing	-	-	901	-
Obtaining control over UPC (refer to note 4)	6,200	-	6,200	-
Dividends received	-	-	-	1
Associate and joint ventures of the Group				
Sale of goods and services	1	392	308	2,020
Purchase of property and construction services	-	1,300	2,903	9,330
Purchase of goods and services	-	860	1,174	1,669
Loans received from joint venture	1,484	-	1,683	-
Interest expense on loans	15	-	16	-
Interest income	-	343	565	777

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

Compensation of key management personnel

The remuneration of directors and other key management personnel was as follows:

	Three months ended 30 September		Nine months ended 30 September	
	2014	2013	2014	2013
Wages and salaries	179	215	523	636
Phantom shares granted	187	154	445	462
Termination bonuses	-	-	4	4
Total	366	369	972	1,102

At 30 September 2014, outstanding balances in respect of wages and salaries of key management personnel were RUB 278 million (31 December 2013: RUB 574 million).

19. FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of financial assets and liabilities is determined as follows:

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

At 30 September 2014 and 31 December 2013 management believes that the carrying values of all significant financial assets and financial liabilities recorded at amortised cost in the interim condensed consolidated financial statements approximated their fair values, except for the unsecured non-convertible bonds with carrying value of RUB 58,299 million and fair value RUB 55,745 million (31 December 2013: carrying value of RUB 48,299 million and fair value RUB 48,740 million) and unsecured fixed interest rate borrowings obtained in 2013 and earlier with carrying value of RUB 20,000 million and fair value RUB 19,117 million.

Management believes that the carrying value of financial assets and liabilities approximated their fair values due to (i) their short-term nature for current financial assets and liabilities, (ii) the fact that interest rates on loans receivable approximate current market rates for similar debt instruments, and (iii) the fact that the interest rates on long-term liabilities approximate the current market rates for similar instruments as the majority of loans and borrowings were obtained in 2014.

At 30 September 2014 assets and liabilities of the Group that are measured at fair value in accordance with the fair value hierarchy were as follows:

	Level 1	Level 2	Level 3	Total
Current liabilities				
Derivative financial instruments	-	(1,902)	-	(1,902)
Total	-	(1,902)	-	(1,902)

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

At 31 December 2013 assets and liabilities of the Group that are measured at fair value in accordance with the fair value hierarchy were as follows:

	Level 1	Level 2	Level 3	Total
Non-current assets				
Available-for-sale investment	-	-	423	423
Derivative financial instruments	-	90	-	90
Total	-	90	423	513

20. COMMITMENTS AND CONTINGENCIES

Capital commitments

At 30 September 2014, contractual capital commitments of the Group amounted to RUB 46,653 million (31 December 2013: RUB 8,601 million). Included in total capital commitments is RUB 27,705 million of capital commitments arisen in 2014 mainly in respect of drilling services based on the Group's capital construction programme, which is re-evaluated on an annual basis.

Operating leases: Group as a lessee

The Group leases certain production equipment, transport and office premises. The leases typically run for periods varying from 1 to 10 years with no renewal option at the end of the lease term. The Group's extraction, refining, marketing and distribution and other facilities are located on land under operating leases, which expire in various years through 2062.

The amount of rental expenses for the three months ended 30 September 2014 were RUB 285 million (for the three months ended 30 September 2013: RUB 401 million) and for the nine months ended 30 September 2014 were RUB 907 million (for the nine months ended 30 September 2013: RUB 1,209 million).

Future minimum rental expenses under non-cancellable operating leases are as follows:

	30 September 2014	31 December 2013
Due in one year	995	936
Due from one to five years	2,925	2,972
Thereafter	11,934	11,972
Total	15,854	15,880

Taxation contingencies in the Russian Federation

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

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

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

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

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

Legal contingencies

At 30 September 2014, unresolved legal claims against the Group amounted to RUB 180 million (31 December 2013: RUB 151 million). Management estimates the unfavourable outcome of these legal claims to be possible, and consequently no provision has been raised. The Group is rigorously defending itself in relation to such legal claims.

On 7 July 2014 Moscow's arbitration court received a claim from a minority shareholder of the Company, against the Company and Rosnedra, requesting that the decision of the Company's Board of Directors on reissuing the license from the Company to Bashneft-Polyus, as well as changes made by Rosnedra to license agreement, to be declared invalid. The hearing of this case is still ongoing and at this stage the Group is unable to evaluate the potential outcome.

Insurance

The Group does not have full coverage for property damage or loss, for business interruption and third party liabilities in respect of damage on the Group's property or relating to the Group's operations. Until the Group obtains adequate insurance coverage, there is a risk that losses relating to such matters could have an adverse effect on the Group's operations and financial position.

Management believes that the Group has adequate property damage coverage for its main production assets.

Russian Federation economic environment

Emerging markets such as Russian Federation are subject to different risks than more developed markets, including economic, political and social, and legal and legislative risks. As has happened in the past, actual or perceived financial problems or an increase in the perceived risks associated with investing in emerging economies could adversely affect the investment climate in Russian Federation and the country's economy in general.

Laws and regulations affecting businesses in the Russian Federation continue to change rapidly. Tax, currency and customs legislation within the country are subject to varying interpretations, and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in Russia. The future economic direction of the Russian Federation is heavily influenced by the economic, fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory, and political environment.

The global financial system continues to exhibit signs of deep stress and many economies around the world are experiencing lesser or no growth than in prior years. Additionally there is increased uncertainty about the creditworthiness of some sovereign states in the Eurozone and financial institutions with exposure to the sovereign debt of such states. These conditions could slow or disrupt Russia's economy, adversely affect the Group's access to capital and cost of capital for the Group and, more generally, its business, results of operations, financial condition and prospects.

Because the Russian Federation produces and exports large volumes of oil and gas, country's economy is particularly sensitive to the price of oil and gas on the world market.

BASHNEFT GROUP

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND THE NINE MONTHS ENDED 30 SEPTEMBER 2014 (UNAUDITED)

Millions of Russian roubles

Starting from March 2014, sanctions have been imposed in several packages by the U.S. and E.U. on certain Russian officials, businessmen and companies. In addition, in April 2014 credit agency Standard & Poor's downgraded Russia's long-term foreign currency sovereign rating from BBB to BBB- with a negative outlook. Previously, Fitch credit agency has also revised Russia's creditworthiness outlook from stable to negative. These events, including official sanctions, particularly if further extended, may adversely affect the Russian economy through reduced access of the Russian businesses to international capital and export markets, capital flight, weakening of the Ruble and other negative economic consequences. The impact of these developments on the operations and financial position of the Company is at this stage difficult to predict.

21. EVENTS SUBSEQUENT TO THE REPORTING PERIOD

On 30 October 2014, the Moscow Commercial Court upheld the claim of the Prosecutor General's Office of the Russian Federation for the recovery of JSOC Bashneft's shares owned by Sistema and Sistema-invest in favor of the Russian Federation. For details see Note 1.

On 20 November 2014 credit agency Moody's Investors Service confirmed Bashneft's corporate family rating (CFR) at Ba2 and probability of default rating (PDR) at Ba2-PD. According to credit agency Moody's Investors Service, the outlook for both ratings is positive.