

**MANAGEMENT REPORT  
OAO GAZPROM  
2012**

## CONTENTS

<b>The Gazprom Group</b> .....	<b>3</b>
OAO Gazprom's mission.....	3
OAO Gazprom's strategic goal.....	3
Principles of OAO Gazprom's operations.....	3
Competitive advantages of OAO Gazprom.....	3
The Group's position in global energy industry.....	4
<b>Operating results</b> .....	<b>5</b>
Reserves, exploration and production of hydrocarbons.....	5
Transportation of gas.....	13
Underground gas storage.....	15
Gas distribution.....	17
Refining.....	20
Electric power.....	23
<b>Innovative development</b> .....	<b>26</b>
Research and Development.....	26
Improved management of innovative activities.....	28
International cooperation in R&D.....	28
<b>Environment protection</b> .....	<b>30</b>
<b>Employees</b> .....	<b>32</b>
<b>Analysis of financial results of operations</b> .....	<b>34</b>
Results of operations.....	34
Liquidity and capital recourses.....	42
Capital expenditures.....	44
Debt obligations.....	45
<b>Shareholder structure and stock market of OAO Gazprom</b> .....	<b>47</b>
<b>Management structure of OAO Gazprom</b> .....	<b>49</b>
<b>Risk management</b> .....	<b>56</b>
Development of risk management system.....	56
Key risk factors.....	56
<b>Branches and representative offices of OAO Gazprom</b> .....	<b>68</b>
<b>Conversion Table</b> .....	<b>69</b>
<b>Glossary of major terms and abbreviations</b> .....	<b>70</b>
<b>Addresses and contacts</b> .....	<b>73</b>

*Notes:*

In the present Management Report some of operating and economic parameters have been determined in accordance with International Financial Reporting Standards (IFRS) principles and for the Gazprom Group's entities consolidated in the IFRS consolidated financial statements of OAO Gazprom for the year ended 31 December 2012, therefore they can differ from similar parameters in reports of OAO Gazprom prepared under Russian statutory requirements.

Moreover, some operating parameters of OAO Gazprom and its subsidiaries are determined in accordance with principles underlying management reporting.

Analysis of financial results should be read in conjunction with the audited annual consolidated financial statements of OAO Gazprom for the year ended 31 December 2012, prepared in accordance with IFRS.

Among other things the report discloses information on the future production and economic activities of the Gazprom Group, based on the forecasts and estimations of the management, on the basis reasoning from the current situation. Actual performance results may differ from forecasts and estimations under the influence of various objective factors.

## **THE GAZPROM GROUP**

The Gazprom Group (OAO Gazprom and its subsidiaries, hereafter - Gazprom, the Group) is one of the world's largest vertically-integrated energy companies.

### **OAO Gazprom's mission**

Gazprom views its mission in reliable, efficient and balanced supply of natural gas, other energy resources and their derivatives to consumers.

### **OAO Gazprom's strategic goal**

Gazprom pursues the strategic objective of establishing itself as a leader among global energy companies through markets diversification, ensuring reliable supplies, efficiencies and using scientific research and technology potential.

### **Principles of OAO Gazprom's operations**

- constant raising of operating efficiency by using experience and scientific research and technology potential;
- efficient management of available resources (natural, human, financial, technological and innovative);
- diversifying through high-performance projects to create commodities with high added value;
- increasing capitalization and credit ratings;
- meeting the interests of all OAO Gazprom's shareholders;
- improving corporate governance;
- improving transparency of financial and business activities;
- establishing personal responsibility in its leadership for managerial decision-making;
- minimizing specific adverse technological environmental impact

### **Competitive advantages of OAO Gazprom**

- rich raw material and production bases of the Group;
- unique Russian Unified gas transportation system, which ensures fast response to changes in any of its components including gas, gas condensate and oil and gas condensate fields in use, major pipelines equipped with compressor stations, underground gas storages, gas production plants and distribution stations, which enable assured gas supplies to customers in the Russian Federation and abroad;
- profound vertical integration of the Group;
- beneficial geographic location between Europe and Asia;
- years of experience with foreign partners and reputation as a reliable supplier;
- portfolio of long-term contracts of gas supplies to European customers;
- large potential for success in production, scientific research and projects.

## The Group's position in global energy industry

Gazprom is a global leader in terms of reserves (approximately 18%) and natural gas production volumes (approximately 14%). In Russia, Gazprom provides for above 70% of gas production and approximately 9% of oil and gas condensate production.

The Group owns the world's largest gas transportation network located in Russia with length more than 170 thousands kilometers, which ensures distribution of natural gas to customers within Russia and access of natural gas to European markets.

Half of gas processing and 19% of oil and stable gas condensate refining in Russia is attributable to Gazprom.

Gazprom is the dominant gas supplier to Russian consumers (Gazprom's share in the Russian gas market is above 70%) and to former Soviet Union (FSU) countries. Besides the Group is the major supplier of natural gas to Europe (Gazprom's share on the European market is 25.4%). The Group has branched network more than 1,600 of fuel stations in Russia, FSU and on Balkans.

The Group also owns electricity generating assets, which provide for approximately 17% of the electricity generation in Russia.

Major operational and financial parameters of the Gazprom Group for 2012 and 2011 are presented in the table below:

	As of and for the year ended		Change
	31 December 2012	2011	
<b>Reserves of hydrocarbons under PRMS Standards</b>			
Proved and probable gas reserves, tcm	23.4	22.8	2.6%
Proved and probable crude oil and gas condensate reserves, million tons	2,046.4	1,973.9	3.7%
Proved and probable reserves of hydrocarbons, bboe	153.3	149.7	2.4%
<b>Operating indicators</b>			
Gas production, bcm	487.0	513.2	-5.1%
Crude oil and gas condensate production, million tons	46.1	44.4	3.8%
Hydrocarbon production, million boe	3,217.2	3,358.5	-4.2%
Natural and associated gas refining, bcm	32.7	33.2	-1.5%
Oil and gas condensate refining, million tons	61.4	53.5	14.8%
Electricity generation, billion kilowatt-hour (kWh)	162.2	173.2	-2.9%
<b>Statement of Comprehensive Income highlights (RUB million)</b>			
Sales	4,764,411	4,637,090	2.7%
Operating profit	1,289,176	1,656,843	-22.2%
Profit for the year attributable to owners of OAO Gazprom	1,182,625	1,307,018	-9.5%
Adjusted EBITDA	1,572,806	1,930,533	-18.5%
<b>Balance Sheet highlights (RUB million)</b>			
Cash and cash equivalents	419,536	501,344	-16.3%
Total debt	1,504,741	1,540,162	-2.3%
Net debt	1,081,547	1,034,941	4.5%
Equity, including non-controlling interest	8,701,094	7,760,991	12.1%
<b>Ratios</b>			
Net earnings per share for profit attributable to owners of OAO Gazprom, RUB	51.53	56.95	-9.5%
Total debt to equity, including non-controlling interest	0.17	0.20	-15.0%
Adjusted EBITDA to interest expense	42.52	60.33	-29.5%
Return on average capital employed	12.6%	16.1%	-21.7%

## OPERATING RESULTS

### Reserves, exploration and production of hydrocarbons

The Gazprom Group keeps a leading position in terms of industrial gas reserves among global oil and gas companies owning 18% of global and 72% of Russian reserves. Prospected gas reserves located abroad are less than 1% as of 31 December 2012.

The table below presents assets and volumes of capital expenditures in the Production of Gas and Production of Oil and Gas Condensate segments:

	As of 31 December	
	2012	2011
<b>Gas production</b>		
Assets, RUB million	1,875,535	1,725,762
Share in total assets of the Group	15.4%	15.0%
<b>Oil and gas condensate production</b>		
Assets, RUB million	1,385,095	1,272,339
Share in total assets of the Group	11.3%	11.0%
<b>Year ended 31 December</b>		
<b>2012</b>		
<b>2011</b>		
<b>Gas production</b>		
Capital additions, RUB million	232,705	246,635
Share in capital additions of the Group	19.1%	18.3%
<b>Oil and gas condensate production</b>		
Capital additions, RUB million	108,683	79,102
Share in capital additions of the Group	8.9%	5.9%

### Reserves

According to the audit of the Gazprom Group's hydrocarbon reserves under PRMS Standards performed by DeGolyer and MacNaughton, as of 31 December 2012 proved and probable reserves of the Group's hydrocarbons were 153.3 bboe. Net present value of the Gazprom Group's hydrocarbon reserves is assessed at USD 279.6 billion (as of 31 December 2011 – USD 299.2 billion). The valuation covered 94% of natural gas, 89% of gas condensate and 88% of crude oil under the ABC1 classification accepted in Russia.

The following table shows proved and probable reserves of the Gazprom Group under PRMS Standards:

		As of 31 December	
		2012	2011
<b>Gas</b>			
Share of ABC <sub>1</sub> reserves covered by the assessment under PRMS Standards <sup>(1)</sup>		94%	90%
Proved			
	tcm	19.1	19.2
	tcf	674.5	678.1
Probable			
	tcm	4.3	3.6
	tcf	151.9	127.1
Proved and probable			
	tcm	23.4	22.8
	tcf	826.4	805.2
<b>Condensate</b>			
Share of ABC <sub>1</sub> reserves covered by the assessment under PRMS Standards <sup>(1)</sup>		89%	83%

		As of 31 December	
		2012	2011
Proved	million tons	633.8	605.2
	billion barrels	5.2	5.0
Probable	million tons	174.9	152.6
	billion barrels	1.4	1.2
Proved and probable	million tons	808.7	757.8
	billion barrels	6.6	6.2
<b>Oil</b>			
Share of ABC <sub>1</sub> reserves covered by the assessment under PRMS Standards <sup>(1)</sup>		88%	89%
Proved	million tons	713.9	723.9
	billion barrels	5.2	5.3
Probable	million tons	523.8	492.2
	billion barrels	3.9	3.6
Proved and probable	million tons	1,237.7	1,216.1
	billion barrels	9.1	8.9
<b>Total</b>			
Share of ABC <sub>1</sub> reserves covered by the assessment under PRMS Standards <sup>(1)</sup>		93%	90%
Proved	billion tons of fuel equivalent	24.0	24.1
	bboe	123.0	123.4
Probable	billion tons of fuel equivalent	5.9	5.1
	bboe	30.3	26.3
Proved and probable	billion tons of fuel equivalent	29.9	29.2
	bboe	153.3	149.7

Note.

- (1) The ABC<sub>1</sub> classification accepted in Russia is based on analysis of geological parameters of reserves and evaluates the actual hydrocarbon reserves. PRMS Standards take into account not only the probability of hydrocarbon deposition in geological formations but also the economic feasibility of reserves extraction, determined based on exploration and drilling costs, operating expenses for production and transportation, taxes, hydrocarbon selling prices and other factors.

Compared to the assessment made as of 31 December 2011, proved and probable reserves of Gazprom increased by 3.6 bboe, mainly due to inclusion of a new field – Koviktinskoe. Decrease of net present value of the Group's reserves is primarily due to increase of minerals extraction tax for gas and gas condensate, as well as deferral of Shtokman filed development.

As of 31 December 2012 the Group had licenses for ABC<sub>1</sub> hydrocarbon reserves development in the following volumes: 35,143.5 bcm of natural gas, 1,382.9 million tons of gas condensate and 1,778.1 million tons of crude oil, for a total of 231.3 bboe.

As of 31 December 2012 the Group's share in the ABC<sub>1</sub> reserves of the associated companies was 758.5 bcm of natural gas, 65.2 million tons of gas condensate and 732.2 million tons of crude oil, or 10.4 bboe.

The following table sets forth changes to the Group's ABC1 reserves of natural gas, gas condensate and oil in the licensed areas in the Russian Federation in 2012:

	Natural gas bcm	Gas condensate million tons	Crude oil, million tons	Total, million boe
<b>Reserves as of 31 December 2011</b>	<b>35,046.9</b>	<b>1,395.5</b>	<b>1,767.3</b>	<b>230,795.7</b>
<b>including share of non-controlling     shareholders</b>	<b>595.9</b>	<b>0.3</b>	<b>53.4</b>	<b>3,903.8</b>
Additions to reserves as a result of exploration	573.0	21.5	55.2	3,955.5
Transfer of reserves discovered in 2012 to the Undistributed Subsoil Fund of Russia <sup>(1)</sup> , acquisition from other companies	(4.6)	(0.4)	(4.3)	(61.9)
Receipt of licenses	201.0	4.3	7.0	1,270.4
including based on discovery	17.2	1.5	7.0	164.9
Return of licenses	(1.4)	(0.1)	-	(9.0)
Acquisition of assets	-	-	0.4	2.9
Disposal of assets	-	-	(13.1)	(96.0)
Revaluation	(185.8)	(28.6)	(1.4)	(1,338.6)
Production (including losses)	(485.6) <sup>(2)</sup>	(9.3) <sup>(3)</sup>	(33.0)	(3,178.2)
<b>Reserves as of 31 December 2012</b>	<b>35,143.5</b>	<b>1,382.9</b>	<b>1,778.1</b>	<b>231,340.8</b>
<b>including share of non-controlling     shareholders</b>	<b>587.6</b>	<b>1.0</b>	<b>63.1</b>	<b>3,931.7</b>

Notes.

- (1) Under the law of the Russian Federation, the subsoil user does not have any vested right to develop reserves discovered in areas covered by exploration licenses or beyond the licensed areas. Such reserves shall be transferred to the Undistributed Subsoil Fund of the Russian Federation. Subsequently the subsoil user has a preference right to receive a license for their development.
- (2) Except for dissolved gas.
- (3) Any changes in gas condensate reserves due to production are recognized as converted into stable gas condensate (C5+). The production volume of unstable gas condensate of the Gazprom Group in 2012 was 12.8 million tons.

### Exploration

In 2012 exploration was carried out in all oil and gas provinces of Russia: West and East Siberia, Far East, the Orenburg Region, the Krasnodar Territory, the Republic of Komi, offshore areas of the Kara Sea and the Sea of Okhotsk.

In compliance with corresponding contractual obligations the Gazprom Group continued to carry out exploration projects abroad.

The following table shows summary information on exploration work at licensed areas of the Gazprom Group:

	Year ended 31 December 2012	
	In Russia	Abroad
Total financing of exploration, RUB billion	31.9	8.9
Exploration drilling, thousand meters	126.4	24.0
Completed exploration wells, units	54	7
including successful wells	46	1
Seismic exploration 2D, thousand line km	1.9	0.7
Seismic exploration 3D, thousand km <sup>2</sup>	8.4	0.4

The exploration work in Russia resulted in the increase of reserves by 573.0 bcm of natural gas and 76.7 million tons of crude oil and gas condensate. Recovery of natural gas reserves was 1.18,

of gas condensate – 2.31, and of oil - 1.67. In 2012 efficiency of exploration was 6,099.7 tons of fuel equivalent per 1 meter drilled.

In 2012 five new fields were discovered: two gas condensate fields in the Krasnoyarsk Territory - Ilbokichskoye and Novo-Yudokonskoye; as well as three oil fields - Severo-Romanovskoye in YaNAO, Yuzhno-Shinginskoye in the Tomsk region and Novaya Nadezhda in Dagestan. In addition 49 deposits were discovered in Chikansky, Yuzhno-Parusovsky, Severo-Parusovsky, Yubileyny, Yety-Purovsky, Vyngapurovsky and other fields.

The main increase of gas reserves in the amount of 273 bcm relates to fields of the Tambeyskoye group: Severo-Tambeyskoye and Tasijskoye located in the Yamal Peninsular, as well as Chayandinskoye in the Republic of Sakha (Yakutia) - 75 bcm.

In 2012 exploration work abroad on the Group's licensed sites was concentrated in Vietnam, Algeria and Tadzhikistan and seismological study were carried out in Serbia, Hungary. Due to the force-majeur mode that was introduced in February 2011 for PSA projects at blocks No.19 and No.64 in Libya, operations on these sites were limited.

Also, prospecting and exploratory drilling activities were performed in the territory of foreign states in the reporting year as part of joint efforts in which Gazprom Neft Group is involved, namely: in Iraq (Badra) – 9.3 thousand m, Venezuela (Hunin-6) – 2.3 thousand m, Cuba – 4.7 thousand m.

In August 2012 Gazprom Neft completed the first stage of exploration operations under two Product Sharing Agreements in Equatorial Guinea. No commercial hydrocarbon reserves have been identified and the agreements have been terminated.

The first exploration well Catoche-1 drilled in the offshore area of Cuba has not discovered any commercial reserves of hydrocarbons either. The project is implemented by the Gazprom Neft Group together with the Malaysian company - operator Petronas.

Gazprom continues its expansion on global oil markets striving to strengthen its positions. In 2012 the Group became participant of new projects in Vietnam and Iraq, it laid the ground for expanding its presence in Libya.

### Licensing

As of 31 December 2012 the Gazprom Group held 255 subsoil licenses for prospecting, exploration and production of hydrocarbons and geological survey of deposits. The size of this subsoil area was 315.3 thousand sq. km, including 62.4 thousand sq. km of offshore sites.

In 2012 by order of the Russian Government the Gazprom Group received licenses for exploration and production at the following sites: by the order of the Russian Government a subsoil site of federal importance that includes the Western part of Shtokman field with category C1 gas reserves of 183.8 bcm and gas condensate reserves of 2.8 million tons; licenses for the oil and gas condensate South – Padinskoye field and West – Yubileynoye and Filatovskoye oil fields were received as a result of new discoveries. A license for prospecting, exploration and production at the West-Chatylsky section was received as a result of the tender.

Costs of licensed sites acquisition totalled RUB 1.9 million.

In 2012 12 licenses for subsoil use in Russia were returned: 10 licenses - due to expiry, 2 licenses were terminated early due to inexpediency of any work continuation. Also licenses for two sites in Tadzhikistan (Sargazon and Rengan) were returned due to identification of high geological, technical and economical risks associated with their development.

### Transactions with assets that changed controlled reserves and production capacities, revaluation

The Gazprom Neft Group acquired 100% of OOO Zhivoy Istok. The Company owns subsoil licenses for exploration and extraction of hydrocarbons on Baleykinsky field and geological exploration on Uransky section.

The hydrocarbon reserves have been revalued due to changes in variables used to estimate reserves of Zapolyarnoye oil and gas condensate field.

### Production

In oil and gas sector Gazprom's operations are based on advanced technologies of hydrocarbon production and modern enhanced oil recovery methods. This will allow producing oil and gas in volumes that will be of demand on the market.

The following table contains information on the volumes of natural gas and liquid hydrocarbons produced by the Group and associated companies in Russia:

	<b>Natural and associated gas, bcm</b>	<b>Unstable condensate, million tons</b>	<b>Crude oil, million tons</b>	<b>Total million boe</b>
<b>Year ended 31 December 2012</b>				
Production of the Gazprom Group	487.0	12.8	33.3	3,217.2
Share of the Gazprom Group in the production of associated companies	12.8	1.1	19.7	228.8
<b>Year ended 31 December 2011</b>				
Production of the Gazprom Group	513.2	12.1	32.3	3,358.5
Share of the Gazprom Group in the production of associated companies	11.3	1.0	20.5	225.0

In 2012 the Gazprom Group produced 487.0 bcm of gas (in 2011 - 513.2 bcm). The gas production decline that is explained by a sharp slump in demand, has not affected the ability to ensure maximum daily production of gas in the periods of peak demand. In autumn-winter 2012/2013 the maximum daily gas production was 1,658 million cm which is 50 million cm more than in prior year autumn-winter period.

In 2012 the Bovanenkovskoye field, the largest field in the Yamal peninsular, was put into operation. The field is expected to reach the designed capacity of 115 bcm p.a. in 2019 -2021.

Gazprom continued to develop Kirinsky field in the offshore zone of the Okhotsk Sea eastward of the Sakhalin Island. Gazprom has started to drill production wells. For the first time in Russia the production will be executed using underwater extraction systems.

In Zapolyarnoye field Gazprom built the second unit of the complex gas treatment facility for gas from the Valanginian deposits (UKPG-1V) with the annual capacity of 9.74 bcm, and 75 new wells. In addition gas production capacities from the Cenomanian deposits have been increased as a result of putting into operation 12 new wells. As a result the field producing annually 130 bcm of hydrocarbons, has become the most productive in Russia.

The Zapolyarnaya main compressor station with the capacity of 354 MW is one of the most powerful compressor stations in Russia. It has modern gas pumping facilities with centrifugal rotor boosters suspended magnetically. The devices are equipped with a remote control and self-diagnostics system. This allows to significantly reduce the time of routine maintenance. Moreover, gas pumping facilities are more environmental friendly as emissions of nitrogen oxide and carbon have been minimized.

Oil business development is one of Gazprom's strategic priorities. The oil production in the Gazprom Group is concentrated in the Gazprom Neft Group. In 2012 production of gas condensate was 12.8 million tons (0.8 million tons more than in 2011), of crude oil –

33.3 million of tons (1.1 million tons more than in 2011). The Group's share in the production of the associated companies totalled 1.1 million tons of gas condensate and 19.7 million tons of crude oil. In the reporting year test oil production started at East Messoyakhsky field; first oil was extracted at Novoportovskiy field. The oil production sector has continued to be developed in the Orenburg region: ZAO Gazprom Neft Orenburg, a Group entity, launched implementation of the second pilot drilling project in the east part of Orenburgskiy oil and gas condensate field.

In addition, the first stage of Samburgskiy oil and gas condensate field has been put into commercial operation, the corresponding subsoil license is held by OAO Arkticgaz, a subsidiary of OOO SeverEnergiya (in which the Group's effective interest is 25.5%).

Prirazlomnoye field development is an important part of Gazprom Group's oil business development strategy. The key development target of the oil field - the Prirazlomnaya sea stationary ice-strengthened platform - was installed in the field in the waters of the Pechora Sea. In 2012 the Gazprom Group completed the construction and installation works and a significant scope of electric installation as well as performed the first stage of in-plant equipment tests. A group project has been designed for the construction of operating (production and pressure) wells. The drilling of these wells is planned to commence in the second quarter 2013.

The Gazprom Group also participates in hydrocarbon production projects abroad. In 2012 the Group's Serbian concern NIS produced 1.2 million tons of oil and 0.6 bcm of gas.

Gazprom participates in joint projects in Iraq, Libya, Venezuela and the UK.

Gazprom owns a 20% interest in the project related to the development of Wingate field in the North Sea (blocks 44/24b and 44/19f). In 2012 production volumes attributable to the Group's share amounted to 150 million cm of gas and 900 tons of condensate. Volume of oil produced in Kurdistan (Iraq) totaled 4.6 thousand tons.

In Libya Wintershall AG (the operator), the Group's associate, continues to develop nine fields in the framework of oil concessions C96 and C97. The Gazprom Group's share in the 2012 hydrocarbon production amounted to 2.1 million tons of oil and 0.3 bcm of gas.

In parallel with the exploration work, oil production was commenced at Hunin-6 block located in the Orinoko river basin in Venezuela. Russian oil companies participate in the project via OOO National Oil Consortium in which Gazprom Neft has a 20% share.

The following table sets forth information on the number of developed producing fields and production wells of the Gazprom Group:

	As of 31 December 2012	
	In Russia	Abroad
Developed producing fields	127	50
Gas production wells	7,717	234
including active	7,226	111
Oil production wells	7,296	903
including active	6,738	623

#### Main areas of capital investments

Main investments in the Group's gas production segment in 2012 were allocated to the infrastructure development of Bovankovskoye, Kirinskoye and Zapolyarnoye fields, maintenance of current production levels at Yamburgskoye, Urengoyevskoye, Medvezhiye, Yubileynoye, Yamsoveyskoye, Vyngapurovskoye, West-Tarkosalinskoye, Komsomolskoye oil and gas condensate fields, Vyngayakhinskoye gas and oil field, Orenburgskoye oil and gas condensate field, Astrakhanskoye gas condensate field and fields of OOO Gazprom Dobycha Krasnodar.

In 2012 the following facilities were put into operation:

- 2 boosting compressor stations in Bovanenkovskoye and Medvezhiye fields with the capacity of 250 MW and 24 MW respectively;
- 2 gas treatment facilities: with the annual capacity of 60.0 bcm at Bovanenkovskoye oil and gas condensate field and of 9.74 bcm at Zapolyarnoye field;
- 298 gas production wells.

Capacity of boosting compressor stations at Komsomolskoye gas field and at UKPG-4 (complex gas treatment facility) of Yamburgskoye oil and gas condensate field have been increased by 32 MW each.

The Group's capital investments in exploration and production of oil and gas condensate were primarily used for infrastructure development at Prirazlomnoye field and development of the Eastern part of Orenburgskoye and Novoportovskoye fields, implementation of Messoyakhinsky project, implementation of drilling program on Priobskoye and other fields of YaNAO and KhMAO as well as implementation of projects in Iraq including the Badra field development and acquisition of the share in the development of Garmian and Shakal blocks located in the South of Kurdistan in the framework of concluded contracts on division of production.

In total in 2012 the Group put into operation 726 new oil production wells in Russia.

#### Sale of oil and gas condensate

In 2012 the Gazprom Group sold 20.8 million tons of oil and gas condensate.

Volumes of oil and gas condensate sold on domestic and external markets were as follows:

(million tons)	Year ended 31 December		Changes
	2012 <sup>(1)</sup>	2011 <sup>(1)</sup>	
Russia	3.5	4.1	-14.6%
including the Gazprom Neft Group	0.6	0.1	
FSU	2.5	3.0	-16.6%
including the Gazprom Neft Group	2.5	3.0	
Europe and other countries	14.8	13.5	9.6%
including the Gazprom Neft Group	14.2	13.1	
<b>Total</b>	<b>20.8</b>	<b>20.6</b>	<b>1.0%</b>

Note.

- (1) The volumes of oil and gas condensate sold to indicated markets do not include intra-group sales. The total volume of hydrocarbon sold by the Gazprom Group is included, both own production and purchased from third parties.

Production capacities need to be utilized in accordance with the approved oil refinery and export programs, therefore free oil sales (exclusively of replacement deliveries) in Russia were not significant.

The Group's operations are significantly affected by the prevailing price of crude oil, both in domestic and international oil markets. Regardless of minor fluctuations in 2012 the price for Brent crude oil was retained at a relatively high level of about USD 111 per barrel which is similar to the 2011 level. The only period when the price dropped to USD 90 per barrel was not long.

Oil grade	January	February	March	April	May	June
	USD per barrel					
BRENT <sup>(1)</sup>	110.58	119.56	125.33	119.54	110.20	94.84
URALS <sup>(2)</sup>	109.92	118.49	122.17	117.14	108.70	93.56
Spread URALS to BRENT	-0.66	-1.06	-3.16	-2.40	-1.50	-1.28
Oil grade	July	August	September	October	November	December
	USD per barrel					
BRENT <sup>(1)</sup>	102.59	113.37	112.86	111.60	109.11	109.35
URALS <sup>(2)</sup>	102.47	112.90	111.60	110.15	108.11	107.97
Spread URALS to BRENT	-0.12	-0.47	-1.26	-1.45	-1.00	-1.38

## Notes:

- (1) Based on daily average of BRENT quotes, calculated as an average between daily maximum and minimum quotes.
- (2) Based on average quotes of URALS Mediterranean and URALS Rotterdam, calculated as an average between daily maximum and minimum quotes.

Reporting year and subsequent events

On 14 November 2012 OAO Gazprom and Wintershall Holding GmbH signed a Basic Agreement setting out the terms of asset exchange. As a result of the transaction, Wintershall Holding GmbH will receive 25% + 1 share in the project for the development of areas 4A and 5A of Achimov deposits on the Urengoykoe oil and gas condensate field. In its turn, OAO Gazprom will increase its shares in WIEH, Wingas, WIEE, European gas trade and storage companies, from 50% to 100%. In addition, OAO Gazprom will receive a 50% share in Wintershall Nordzee involved in the exploration and development of oil and gas fields in the southern part of the North Sea (Netherlands, the United Kingdom, Denmark).

In September 2012, the Gazprom Group acquired Statoil's share of 24% in Shtokman Development AG – a special purpose entity created by OAO Gazprom, Total and Statoil for designing, financing, construction and operation of equipment of the first stage of the Shtokman field development. As a result, as of 31 December 2012 the Group's share of Shtokman Development AG is 75%, Total - 25%. In April 2012, an agreement on entering the project for the joint development of licensed blocks 05.2 and 05.3 in the offshore areas of Vietnam in the South China Sea water zone was signed with Petrovietnam. The document stipulates receipt of a 49% interest in Product Sharing Agreements based on the terms of this project.

In December 2012, OAO Gazprom Neft sent a notification to the Italian company ENI on its intent to exercise its option to acquire 33.3% in the consortium of companies developing the Elephant oil field in Libya. OAO Gazprom Neft is planning to become an eligible participant of the project during 2013, provided that the Libyan authorities grant their permission.

Development plans for the Production of Gas and Production of Crude Oil and Gas Condensate segments

Gas reserves on conventional hydrocarbon fields secure long-term gas supplies (at least 70 years) to the domestic and foreign markets. In these circumstances, one of Gazprom's key production goals is to develop the unique and large fields of the Yamal Peninsula in northern offshore areas to maintain and increase the level of hydrocarbon production volume.

It is expected to secure required gas production levels in the mid-term through further infrastructure development on the existing fields and commissioning of new fields in the Nadym-Pur-Tozovsky Region of the Yamal Peninsula, as well as Sakhalin-3 fields.

In the long-term, strategic gas production regions include the Yamal Peninsula, water zones of northern seas and Far East seas of Russia, the fields of East Siberia and Far East. Participation in foreign projects is aimed at the expansion of Gazprom's resource base outside of Russia in order to strengthen its position on foreign oil and gas markets.

From the point of view of oil business development huge hydrocarbon production potential in Russia is concentrated in the northern areas of the Yamal-Nenetsky Autonomous District (Novoportovskoe oil and gas condensate field, fields of OOO SeverEnergia subsidiaries, Messoyakha project), water zone of the Pechora Sea (Prirazlomnoye and Dolginskoe oil fields) and Orenburg Region (eastern part of the Orenburgskoe oil and gas condensate field and new areas).

In addition, East Siberia fields, such as Kuyumbinskoe and Chonskoe, are expected to contribute to the achievement of production targets.

The following are the long-term strategic goals: strengthening Gazprom's positions in the Arctic offshore area, development of non-licensed areas in the Gydan and Yamal peninsulas, participation in the development of non-conventional reserves of West Siberia as well as growth of foreign projects portfolio. Gazprom actively develops its portfolio of foreign assets involved in liquid hydrocarbon production.

A long-term goal is to expand to the following regions: Middle East, the Balkans, West and North Africa, Latin America.

## Transportation of gas

The following table contains information on assets and volumes of capital investments in the Transportation segment:

	As of 31 December	
	2012	2011
Assets, RUB million	5,279,904	4,972,244
Share in total assets of the Group	43.3%	43.2%
	<b>Year ended 31 December</b>	
	<b>2012</b>	<b>2011</b>
Capital additions, RUB million	563,822	740,910
Share in the Group's total capital additions	46.2%	54.8%

### Gas transportation system

As of the end of 2012, the total length of trunk pipelines and branch pipes owned by OAO Gazprom and its gas transportation subsidiaries in Russia was 168.3 thousand km. The Gas Transportation System includes 222 compressor stations with 3,738 gas compressor units with the total capacity of 43.87 thousand MW.

In addition, gas is transferred to gas compressor units via gas pipelines of gas producers, refinery subsidiaries and underground storage entities, with the total length of 4.1 thousand km.

The age of the gas trunk pipelines in Russia is shown in the table below:

Age of trunk pipelines	As of 31 December 2012	
	Length, km	Share
Up to 10 years	22.2	13.2%
11 – 20	20.4	12.1%
21 – 30	61.7	36.6%
31 – 40	36.8	21.9%
41 – 50	18.8	11.2%
Over 50	8.4	5.0%
<b>Total</b>	<b>168.3</b>	<b>100.0%</b>

For the purpose of higher security of gas supplies, technical and environmental safety and efficient gas transportation, Gazprom annually performs capital repairs and scheduled preventive maintenance of the Gas Transportation System. In 2012, there were 16 technical failures at trunk gas pipelines, i.e. 0.091 of failure per 1,000 km.

Volume of gas pumped into Gazprom's GTS in Russia in 2012 totalled 666.2 bcm, which was 2.5% lower than the level of 2011 due to the complex impact of two factors: lower gas sales of the Gazprom Group in the domestic market with the increased share of gas from non-Group entities pumped into the GTS to 95.8 bcm (in 2011 – 81.5 bcm).

Volumes of natural gas used for own technical needs of the GTS and UGSF were 40.9 bcm of natural gas in 2012 (45.8 bcm of natural gas in 2011). The Group assesses the level of gas losses as low and the level of gas consumed as fuel as satisfactory.

The Group's key foreign gas transportation asset is OAO Beltransgaz. The total length of gas pipelines operated by the company is 8.1 thousand km, a half of which was built less than 20 years ago. In 2012, 64.5 bcm of natural gas were pumped into the GTS operated by OAO Beltransgaz, including 44.3 bcm of gas transported through the Belarus territory.

Also, Gazprom owns the GTS in the Republic of Armenia which includes trunk pipelines with the total length of 1.9 thousand km and 76 gas distribution stations.

In foreign states, Gazprom's gas transit is ensured by the Group's associated and jointly controlled gas transportation companies: Nord Stream AG, SGT EuRoPol GAZ S.A, Blue Stream Pipeline Company B.V., AO Moldovagaz, AO Lietuvos Dujos, AO Latvijas Gāze, AO Eesti Gaas.

The Nord Stream project is operated by an associated company Nord Stream AG. The total gas transportation volume in 2012 was 11.8 bcm.

#### Main areas of long-term capital investments

Key capital investments are aimed at the construction of the Bovanenkov-Ukhta (the linear part of the first line with two compressor sections with the total capacity of 224 MW is complete) and Ukhta-Torzhok trunk pipeline systems, as well as the Gryazovets-Vyborg trunk gas pipeline (the linear part of the second line with four compressor sections with the total capacity of 345 MW is complete).

In addition, the construction of SRTO-Torzhok gas pipeline (the last three compressor stations with the total capacity of 240 MW are complete) and Pochinki-Gryazovets gas pipeline (Vyaznikovskaya compressor station with the capacity of 64 MW is complete, which will secure the estimated level of gas transportation up to 2020) is finished.

In 2012 3.2 thousand km of trunk grid pipelines and branch connections, and nine compressor stations at gas pipelines with the total capacity of 1,249 MW were commissioned as part of gas transportation projects. At the end of 2012 Gazprom started the expansion and renovation of the UGSS in order to secure gas supplies to the offshore section of the South Stream gas pipeline.

Along with the construction of new gas transportation capacities, Gazprom is involved in the reconstruction and re-equipment of gas transportation facilities. There were 131.8 km of trunk pipelines reconstructed in 2012.

Main areas of long-term investments in 2012 were related to OAO Gazprom's involvement in the construction of the Nord Stream and South Stream pipelines. In October 2012, the second line of the Nord Stream pipeline was commissioned.

#### Reporting year and subsequent events

In the course of implementation of the offshore part of the South Stream project in November 2012, OAO Gazprom, ENI, EDF and Wintershall put into effect their joint resolution to change the jurisdiction of South Stream Transport AG from Switzerland to Netherlands. As a result, a new project entity South Stream Transport B.V. was incorporated.

In the same period, under the South Stream Transport B.V. Shareholders' Agreement and in accordance with the target offshore part of the South Stream project schedule, a final project investment decision was made.

In the course of implementation of the onshore part of the South Stream project in Europe in 2012, final positive investment decisions were made together with the states of Bulgaria, Serbia, Hungary and Slovenia. In September, Gazprom and its Slovenian partner in the Plinovodi d.o.o. project incorporated a joint project entity South Stream Slovenia LLC to implement the project in the territory of Slovenia.

In April 2013, OAO Gazprom and OAO Rosneftegaz signed a contract for the purchase and sale of shares of 72 gas distribution stations owned by OAO Rosneftegaz.

#### Development plans for the Transportation of Gas segment

The key gas transportation projects in Russia are the construction of the Bovanenkovo-Ukhta and Ukhta-Torzhok trunk pipeline systems, the Gryazovets-Vyborg pipeline, as well as the project of UGSS expansion to insure gas supply to the South Stream pipeline.

OAO Gazprom's long-term objectives include the development of gas infrastructure in East Siberia and Far East as part of the Eastern gas project.

In 2013 it is planned to put into operation a pipeline from the onshore technological complex at Kirinsky field to the Sakhalin key compressor station with the aim to connect fields of Sakhalin-3 project to the Sakhalin-Khabarovsk-Vladivostok pipeline.

Activities aimed at the development of the Sakhalin-Khabarovsk-Vladivostok trunk pipeline are designed. R&D activities are performed as part of the Power of Siberia Trunk Pipeline project for gas transportation from Yakutsk and Irkutsk production centres.

South Stream and Nord Stream gas transportation projects are implemented in foreign countries, and potential participation in the construction of gas pipelines to the Asian-Pacific Region is under consideration.

Reconstruction and re-equipment of gas transportation facilities is also a key area of focus. The Complex Program for Reconstruction and Re-equipment of Gas Transportation Facilities in 2011-2015 is being implemented in the territory of Russia. The Program is implemented in order to:

- achieve target gas transportation volumes;
- secure gas transportation and supplies to customers of all levels;
- ensure industrial and environmental safety of gas transportation facilities;
- increase the economic efficiency of gas transportation, including resource and energy efficiency.

### **Underground gas storage**

The following table contains information on assets and volumes of capital investments in the Gas Storage segment:

	<b>As of 31 December</b>	
	<b>2012</b>	<b>2011</b>
Assets, RUB million	220,581	206,126
Share in total assets of the Group	1.8%	1.8%
	<b>Year ended 31 December</b>	
	<b>2012</b>	<b>2011</b>
Capital additions, RUB million	18,247	19,978
Share in the Group's total capital additions	1.5%	1,5%

The development of the underground gas storage system is one of Gazprom's strategic goals. Underground gas storage facilities help control seasonal differences in gas consumption, reduce maximum load, ensure flexible and secure gas supplies.

#### Underground gas storages in Russia and abroad

The Group operates 21 UGSFs in 25 storage facilities in Russia. As of 31 December 2012, the total volume of active gas in UGSFs reached 68.16 bcm. In 2012, 44.3 bcm of gas were withdrawn from UGSF in Russia, and 44.1 bcm of gas were pumped into UGSF, including 100 million cm of buffer gas (Nevskoe UGSF). Maximum daily capacity as of 20 December

2012 was 670.7 million cm per day. Potential daily capacity increased by 23.4 million cm as compared to 2011.

During the period of peak load, the network of underground storages ensures about 20% of gas supply to Russian consumers and outside Russia, and in the days of quick freeze this figure reaches 30%. During maximum gas withdrawal season in 2012/2013 the share of gas supplies from UGSF in Russia reached 38.3%.

By the start of the withdrawal season of 2012 – 2013, the volume of the operating gas reserve in Russian UGSFs reached 66.28 bcm, which is 1.03 bcm higher than in the previous season.

To increase the security of export gas supplies, Gazprom uses UGSF capacities in foreign countries.

In Europe the Group has access to active UGSF capacities in Austria (Haidach), UK (Humbly Grove), Germany (Reden, Katarina, UGSFs of VNG and Vitol), Serbia (Banatsky Dvor). In the reporting year, 5.4 bcm of gas were pumped into European UGSFs, and total gas withdrawal was 1.6 bcm.

Gazprom also uses underground gas storage facilities in the FSU countries.

- In Latvia, Gazprom uses the capacities of the Inchukalnskoe UGSF.
- In Belarus, Gazprom owns three underground gas storage facilities – Pributskoe, Osipovichskoe and Mozyrskoe UGSFs with the total active capacity of 993 million cm.
- In Armenia, Gazprom owns the Abovianskaya underground gas storage station with the active capacity of 135 million cm.

Overall, the Group pumped 2.7 bcm into UGSFs in FSU countries and withdrew 2.5 bcm of gas from those UGSFs.

#### Main areas of capital investments

The main area of capital expenditure on underground gas storage system in 2012 was channeled to reconstruction of Sovkhoznoe UGSF, gasfield facilities of Stepnovskoe and Peschano-Umetskoe UGSF, reconstruction and development of Kasymovskoe UGSF as well as construction of Bednodemyanovskoe and Volgogradskoe UGSFs.

In 2012, activities aimed at the increase of underground gas storage capacities in Russia were carried out at the Kanchurinsko-Musinskoe UGSF (active capacity increased by 0.3 bcm), Sovkhoznoe UGSF (active capacity increased by 0.7 bcm), Severo-Stavropolskoe UGSF (active capacity increased by 0.196 bcm, 6 production wells were connected), Krasnodarskoe UGSF (active capacity increased by 0.25 bcm), and Peschano-Umetskoe UGSF (2 production wells were connected).

In 2012, the second cavern of the Katarina UGSF in Germany was commissioned, and the active capacity increased to 115 million cm.

Activities at the Haidach UGSF in Austria and Banatsky Dvor in Serbia continued.

#### Reporting year and subsequent events

In March 2013, OAO Gazprom and MND Group signed an agreement on the construction of a new UGSF in Dambořice (Czech Republic). The construction is planned for 2014, and the commissioning is scheduled for 2016. The UGSF will have the active gas volume of 448 million cm and will become one of the largest among the similar facilities in Czech Republic. The companies will make equal investments in the construction of the UGSF in the amount of USD 128 million.

### Development plans for the Gas Storage segment

The tasks of long-term development of the underground gas storage system in Russia are set in the General Gas Industry Development Scheme up to 2030 and are aimed at the increase of the daily withdrawal capacity of UGSFs and reserve gas volumes. Gazprom's strategy tasks include technical re-equipment, reconstruction and expansion of existing storage facilities as well as development of new UGSFs. By the withdrawal season of 2015-2016, it is planned to increase maximum daily capacity up to 819.6 million cm.

Gazprom actively participates in prospective projects of gas storage in Netherlands, Czech Republic, Turkey; a feasibility study of potential cooperation in underground gas storage with the United Kingdom, France and Germany is performed.

Gazprom plans to increase own gas storage capacities in Europe and reach the level of 5 bcm of active gas by 2015.

### **Gas distribution**

The following table contains information on assets and volumes of capital investments in the Gas Distribution segment:

	As of 31 December	
	2012	2011
Assets, RUB million	1,217,828	1,223,035
Share in total assets of the Group	10.0%	10.6%

  

	Year ended 31 December	
	2012	2011
Capital additions, RUB million	47,166	48,802
Share in the Group's total capital additions	3.9%	3.6%

The Group is the largest exporter of gas in the world. The following table sets out natural gas sales volumes by geographical segments:

(bcm)	Year ended 31 December		Change
	2012	2011	
Russia	264.9	280.7	-5.6%
FSU <sup>(1)</sup>	66.1	81.7	-19.1%
Europe and other countries <sup>(1)</sup>	151.0	156.6	-3.6%
<b>Total</b>	<b>482.0</b>	<b>519.0</b>	<b>-7.1%</b>

Note.

- (1) The sales to FSU countries and Europe and other countries include both export from Russian Federation, and sales of gas purchased by the Group outside Russian Federation. According to the law "On Gas Export" dated 18 July 2006 No.117-FZ, OAO Gazprom as the owner of the UGSS or its 100% owned subsidiaries have the exclusive right to export gas or liquefied natural gas (LNG) produced in any hydrocarbon field within Russia.

In 2012, gas consumption in Russia totaled 465.4 bcm which is a 1.6% decrease as compared to 2011.

Main customers are electric-power industry, metallurgy and agricultural chemistry. Their consumption is 50% of total gas volumes. High level of gas consumption attributes to utilities and population. The Gazprom Group is the largest supplier on the domestic market and accounts for 70% of total gas supplies.

According to preliminary estimates, gas consumption in Europe decreased by 13.1 bcm to 542.9 bcm (or by 2.4%).

In 2012, the overall sales of gas to far abroad countries under long-term contracts were 138.8 bcm that is by 7.5% lower than in 2011. More than 8% of the above volume were

transported by Nord Stream pipeline. To date, the largest buyers of the Russian gas include Germany, Turkey and Italy.

The sales of gas by the Gazprom Group's subsidiaries to final customers in the United Kingdom, France, the Netherlands, Czech Republic and Slovakia totalled 4.0 bcm. The Group's associated companies and joint ventures also supplied gas to the final customers in Bulgaria, Germany, Italy, Romania, Serbia, Turkey, Croatia and Finland.

In 2012, the Gazprom Group sold 22 batches of LNG with the volume of 68.7 trillion BTU (1.44 million tons or 1.92 bcm) including 4 batches of LNG which were supplied under the contract with Indian company GSPC.

#### The price of natural gas in FSU, Europe and other countries

In 2012, just like in prior years, export prices for gas in the export contracts of OAO Gazprom primarily depended on changes in global prices for liquid fuel. In 2012, price for BRENT crude oil and European prices for oil products that compete with gas, remained at the level of 2011.

In 2012, the average price for gas amounted to USD 385.1/1,000 cm against USD 383/1,000 cm in 2011.

Currently, the European gas market is characterised by a hybrid two-level pricing system. Despite limited application of trading floors (hubs) prices in certain long-term contracts, OAO Gazprom has no plans to refuse oil indexation.

For maintaining competitiveness of the Russian gas on European markets OAO Gazprom regularly holds negotiations on contractual prices modification with its partners. In 2012, agreements on adaptation of price conditions were reached with E.ON Ruhrgas, Shell Energy Europe, WIEH, WINGAS (Germany), ENI, EGL (Italy), EconGas, Centrex, GWH (Austria), GasTerra (the Netherlands), DONG (Denmark), PGNiG (Poland), Bulgargaz EAD (Bulgaria), WIEE (Rumania), Conef Energy (Rumania).

Due to the changes in OAO Gazprom's long-term contracts, retrospective payments resulting from the post factum revision of the supply price become an increasingly pressing issue. This issue is the subject of extended negotiations with partners to agree the volumes and terms of payments.

As of 31 December 2012 Gazprom Group's liabilities associated with revision of price conditions of gas supplies amounted to RUB 115.3 billion. Actual payments made in 2012 had minimal impact on export revenue and as a result, in 2012 the average export price was much higher than expected.

The following table shows the average prices of natural gas sales to FSU, Europe and other countries in 2012 and 2011:

	<b>Year ended 31 December</b>	
	<b>2012</b>	<b>2011</b>
	<b>(including customs duties)</b>	
Natural gas sales to Europe and other countries <sup>(1)</sup>		
USD / thousand cm <sup>(2)</sup>	385.1	383.0
USD / thousand cf <sup>(2)</sup>	10.8	10.7
RUB / thousand cm	11,969.8	11,259.1
Natural gas sales to FSU <sup>(1)</sup>		
USD / thousand cm <sup>(2)</sup>	305.3	289.5
USD / thousand cf <sup>(2)</sup>	8.5	8.1
RUB / thousand cm	9,489.5	8,509.3

Note.

(1) VAT is not charged on sales to Europe and Former Soviet Union countries.

(2) Calculated based on annual average currency exchange rate between RUB and USD.

Increase in the average price of natural gas sales to FSU as compared to the prior period mainly related to the fact that Gazprom started providing FSU customers with contractual prices the earning capacity of which is similar to the European prices.

#### Domestic natural gas prices

In 2012, as a consequence of the governmental gas pricing policy the wholesale prices for the Russian customers increased by 8% as compared to 2011.

The following table shows the average prices for natural gas sold in domestic market:

	Year ended 31 December	
	2012	2011
	(net of VAT)	
RUB per thousand cm	2,871.4	2,631.7
RUB per thousand cf	80.4	74.5
USD per thousand cm <sup>(1)</sup>	92.4	89.6
USD per thousand cf <sup>(1)</sup>	2.6	2.5

Note:

(1) Calculated based on annual average currency exchange rate between RUB and USD.

#### Main areas of capital investments

A significant portion of capital expenditures in Gas Distribution segment includes the Group's investments in gasification of the Russian Federation regions. In 2012 the construction of 235 gasification facilities with total length of 3.4 thousand km was completed. It provided gas supply to 429 centres of population in 40 territorial subjects of the Russian Federation.

#### Reporting year and subsequent events

In 2012 OAO Gazprom and the Agency for Natural Resources and Energy of Japan signed the Memorandum on Vladivostok-LNG project. In February 2013 the Management Committee of OAO Gazprom approved Substantiation of investments in construction of LNG plant in the district of Vladivostok. The project involves construction of an LNG plant with a capacity of 10 million tons per year expandable to 15 million tons a year on the Lomonosov peninsula. Putting into operation of the first phase is planned for 2018.

In the reporting year OAO Gazprom signed the contracts for supplying LNG with the following companies:

- Kogas (Republic of Korea) for supplying 16 batches of LNG (1.33 bcm) in 2013-2014;
- Osaka Gas (Japan) for supplying 4 batches (0.34 bcm) in 2014;
- GAIL (India) supplying for 2.5 million tons during 20 years.

The contract with ENEL for purchasing 6 batches (about 0.5 bcm) of LNG in Nigeria was concluded.

In December 2012, the world's first transportation of LNG by Northern Sea Route was performed.

#### Development plans for Gas Distribution segment

In the Russian market Gazprom will try to keep its current positions as to the volumes of gas delivery, provided stability of supplies, including in autumn and winter is ensured.

A comprehensive system of organised gas trading in the domestic market (including the spot segment) is being developed. The Company continues working with federal executive bodies in order to receive a permission for OAO Gazprom to sell gas through trading systems (e-trading floors), as well as on stock exchanges. The Company's principled position is that these two forms of gas trading are complementary and are both necessary for the development of the gas market

in Russia. Currently, OAO Gazprom specialists cooperate with the Russian Ministry of Energy to develop the procedure for launching gas sales on stock exchanges and via electronic trading.

The Group's key objectives in the European market are to maintain the market-leading position, provide for reliable gas supply, and increase the efficiency of our marketing activities. The Group plans to achieve these objectives by developing relationships with traditional customers on a long-term contractual basis and using new forms of trade based on short-term and medium-term sales, as well as gas exchange and one-time transactions. The Group intends to increase its ownership in companies engaged in the sale of gas and electricity to end-users.

The key components of Gazprom's strategy in the FSU countries are to maintain the attractiveness of the Russian gas and expand access to the end-consumers.

To ensure the flexibility in determining the development stages of fields in the new gas producing regions in Russia, the Group develops the cooperation with Central Asian and other countries in developing gas reserves and purchase of gas.

Marketing strategy of Gazprom Group provides for diversification of the export sales geography by expanding presence in prospective gas markets. In particular, the Group's priorities include increasing LNG volumes in the Group's export portfolio and, within geographical diversification – access to the markets in NEA countries and other countries of Asia-Pacific Region.

## Refining

Assets and volumes of capital investments in Refining segment are presented in the table below:

	As of 31 December	
	2012	2011
Assets, RUB million	1,048,925	1,086,188
Share in total assets of the Group	8.6%	9.4%
<hr/>		
	As of 31 December	
	2012	2011
Capital additions, RUB million	134,163	115,642
Share in total capital additions of the Group	11.0%	8.6%

### Processing of hydrocarbons and production of refined products

Gazprom Group processing capacities include gas and gas condensate processing plants, oil refining capacities of Gazprom Neft and OOO Sibmetakhim that owns metanol production plant in Tomsk.

In 2012, due to obtaining the control over OAO Gazprom neftekhim Salavat the processing capacities increased for the company's refining and petrochemical assets.

The Group's total processing and refining capacity was 53.4 bcm of natural gas and 92.5 million tons of unstable gas condensate and crude oil per year.

The following table sets forth the volumes of the Group's hydrocarbon processing for the periods indicated:

	Year ended 31 December			
	2012 <sup>(1)</sup>		2011 <sup>(1)</sup>	
	Total	including abroad	Total	including abroad
Natural and petroleum gas, bcm	32.7	–	33.2	–
including OAO Gazprom neftekhim Salavat	0.5	–	–	–
Crude oil and unstable gas condensate, million tons	61.4	4.1	53.5	2.4
including				
the Gazprom Neft Group	43.3	4.1	40.5	2.4
OAO Gazprom neftekhim Salavat	4.1	–	–	–

Notes:

(1) The data in tables do not include raw materials supplied by customers.

The following table sets out production volumes of major refined products for the periods indicated:

	Year ended 31 December			
	2012 <sup>(1)</sup>		2011 <sup>(1)</sup>	
	Total	including abroad	Total	including abroad
Dry gas, bcm	25.0	–	25.7	–
Liquefied oil gas, million tons	3.1	0.1	3.0	0.1
including the Gazprom Neft Group	0.8	0.1	0.7	0.1
Broad fractions of light hydrocarbons, million tons	1.0	–	0.7	–
Stable gas condensate and crude oil, million tons	4.7	–	4.6	–
Oil products, million tons	49.7	3.7	42.6	2.1
including				
the Gazprom Neft Group	40.1	3.7	37.5	2.1
OAO Gazprom neftekhim Salavat	3.9	–	–	–
Helium, million cm	4.9	–	3.5	–
Sulphur, million tons	5.3	0.003	5.4	0.003
including the Gazprom Neft Group	0.1	0.003	0.1	0.003

Notes:

(1) The data in tables do not include raw materials supplied by customers.

The decrease in gas processing and dry stripped gas production in 2012 as compared with 2011 is explained by the decreased gas production at Orenburgskoe and Vuktylsky oil and gas condensate fields being the raw material bases for Orenburgsky and Sosnogorsky refineries. Helium refining at Orenburg helium refinery was recovered up to the prior year level.

The increase in unstable gas condensate processing volumes is explained by the increased production of liquid hydrocarbons in Western Siberia.

The increase in oil refining volumes is explained by consolidation of the data of OAO Gazprom neftekhim Salavat starting from 1 June 2012 due to the control established by the Gazprom Group, increased demand for oil products. Due to modernisation of production capacities, gasoline (classes 4 and 5) and diesel fuel (class 5) production volumes increased.

### Sales of refined products

There was a general price increase in the reporting year as compared to the year ended 31 December 2011. The All key products prices exceeded prior year level. One of the few exceptions was sulphur – in average the price was twice as low as in the year ended 31 December 2011, which is due to global market conditions for sulphur and its mineral fertilizers derivatives.

The following table sets out the sales of refined and petrochemical products by the Gazprom Group:

(million tons)	<b>Year ended 31 December</b>		<b>Change</b>
	<b>2012<sup>(1, 2)</sup></b>	<b>2011<sup>(1, 2)</sup></b>	
Russia	36.1	32.7	10.4%
including the Gazprom Neft Group	25.0	24.2	
FSU	5.2	4.4	18.2%
including the Gazprom Neft Group	4.2	4.0	
Europe and other countries	22.6	18.6	21.5%
including the Gazprom Neft Group	14.7	13.1	
<b>Total</b>	<b>63.9</b>	<b>55.7</b>	<b>14.7%</b>

Notes:

(1) The volumes of refined products and petrochemicals sold to the consumers of the corresponding sales markets are presented net of intercompany sales. The data include sales volumes of refined products produced by the Gazprom Group and purchased from third parties.

(2) The volumes do not include helium.

The increase of refined and petrochemical products sales of the Gazprom Group is mainly driven by inclusion of OAO Gazprom neftekhim Salavat and its subsidiaries into the scope of the consolidated financial statements as well as by increase of the volume of liquid hydrocarbons refining by OAO Gazprom Neft and at the gas processing plants of the Group.

In the year ended 31 December 2012 around 13% of the total volume of refined and petrochemical products sales of the Group were sold via the network of fuel stations of the Gazprom Neft Group. As at the end of the reporting year the number of operating fuel stations of the Gazprom Neft Group was 1,609 (including 549 fuel stations that represent the Group's foreign assets). In 2012 sales of the Group's oil products via the network of fuel stations of the Gazprom Neft Group reached 8.1 million tons (in 2011 - 6.2 million tons). The increase in sales is explained by modernisation and optimisation of own network of fuel stations and increased operational efficiency of each fuel station.

In 2012, the Group started selling liquid helium produced during processing at ZAO Krior capacities that was subsequently sold on external markets. Total sales of gaseous helium amounted to 2.7 million cm, sales of liquid helium amounted to 3.0 million litres.

### Main areas of capital investments

The major portion of capital expenditure on refining in 2012 was channeled to construction of Novourengoijsky gas chemical facility, modernization and reconstruction of capacities at Astrakhansky and Orenburgsky gas processing plants, Syrgutsky condensate stabilization plant, to construction of isomerization facilities for light gasoline fractions, for cat-cracked gasoline hydrotreatment and reconstruction of diesel fuel oil hydrotreatment at the Moscovsky NPZ; for cat-cracked gasoline hydrotreatment and reconstruction of diesel fuel oil hydrotreatment at the Omsky NPZ as well as to atmospheric-and-vacuum distillation facilities at the NPZ of OAO Gazprom neftekhim Salavat. The Group also continued constructing the incomplete area of the second line of Urengoy- Surgut condensate pipeline (508 km – 588 km).

### Reporting year and subsequent events

In May 2012, the Group completed acquisition of 18.48% shares of OAO Gazprom neftekhim Salavat and increased its ownership interest to 87.51%. As a result of this transaction Gazprom obtained control over OAO Gazprom neftekhim Salavat. In the second half of 2012, the Group acquired additional 10.33% of OAO Gazprom neftekhim Salavat shares increasing its ownership interest to 97.84%.

### Development plans for the Refining segment

The main objectives of the Gazprom Group's development in gas processing and gas chemistry include increasing the rate of extraction of valuable components of natural gas and their effective use for further refining to marketable products with high added value; modernisation and upgrading of gas condensate processing facilities for production of motor fuels of class 5 and creating new gas processing and gas chemistry centres on the basis of fields located in Eastern Siberia and Far East.

To ensure refining of the prospective liquid hydrocarbon stock obtained in the process of gas production in gas condensate fields of Western Siberia, it is planned to expand and reconstruct Urengoy plant on condensate treatment for transportation, build treatment and transportation facilities for gas condensate and oil from the Achimov formation; finalize construction of the condensate pipeline Urengoy – Surgut; increase the capacities on stabilization of oil and gas condensate blended product at Surgut stable condensate plant, expand and reconstruct the plant.

To improve the quality of the produced motor fuels it is planned to commission a pentane-hexane fraction isomerisation unit at Astrakhansky refinery and Surgutsky condensate stabilization plant in 2013 and 2015, respectively. In addition, feasibility studies of other projects on gas processing and gas chemistry in UGSS operating area (TransValGaz project) and in Eastern Siberia (GPP and helium plant in Amur region, GPP in Irkutsk region) are being performed.

Strategic goals set by Gazprom in refinery include production of goods that comply with the technical regulations, i.e. class 5, increase the yield of light fractions. In addition, one of the key goals is upgrading the production to existing and projected standards of safety.

## **Electric power**

The following table shows assets and capital investments related Electricity and Heat Generation and Sale segment:

	<b>As of 31 December</b>	
	<b>2012</b>	<b>2011</b>
Assets, RUB million	592,251	560,182
Share in total assets of the Group	4.9%	4.9%
	<b>Year ended 31 December</b>	
	<b>2012</b>	<b>2011</b>
Capital expenditures, RUB million	54,851	69,447
Share in the Group's total capital additions	4.5%	5.1%

The Gazprom Group keeps the leading position in the Russian electricity market being the largest owner of power generating assets. Gazprom's share in electricity generation in Russia is approximately 17%, heat generation - 8%.

Information on the Group's key generating assets in Russia and abroad is presented in the table below:

<b>Generating companies</b>	<b>Generating capacities as of 31 December 2012, GW</b>	<b>Power generation, year ended 31 December 2012, billion kW/h</b>	<b>Heat capacity as of 31 December 2012, thousand Gcal/h</b>	<b>Heat production, year ended 31 December 2012, million Gcal</b>
OAo Mosenergo	12.3	61.3	35.0	68.4
OAo WGC-2	18.4	75.2	4.5	6.0
OAo TGC-1	6.9	30.4	14.5	26.7
<b>Total<sup>(1)</sup></b>	<b>37.6</b>	<b>166.9</b>	<b>54.0</b>	<b>101.1</b>

Note:

(1) Totals may not add up due to rounding.

As of 31 December 2012 the Group included ZAO Kaunasskaya TES that owns Kaunassky thermal power plant in Lithuania.

In 2006-2012 the Group's entity, ZAO ArmRosgasprom implemented Razdan-5 project in Armenia. Based on the 2012 results the Group's electricity generation in Russia was 166.9 billion kWh that is 3.4% lower than in 2011; heat generation - 101.1 million Gcal that is 2.3% higher than in 2011. The decrease in electricity generation is explained by the decline in prices in the wholesale electricity market during the first half of 2012 and commissioning new nuclear capacities in Moscow generation centre (Kalininsky NPP).

In 2012 Kaunassky TPP (Lithuania) generated 0.3 billion kW/h of electricity and 1.4 million Gcal of heat.

In 2012 the 5th power generating unit of Razdansky TPP operating under the testing regime generated about 1 billion kW/h of electricity.

In 2012 electricity generated by Gazprom Group totalled 168.2 billion kW/h and heat - 102.5 million Gcal.

All electricity generated by the Russian generating companies of the Group is sold on the wholesale market of electricity and capacity and also exported to Finland.

The Group's subsidiary, OAO Mezhregionenergosbyt is one of the leaders in the Russian power trading market. Its consumers include more than 700 large and middle electricity consumers in 47 territorial subjects of the Russian Federation. The Company is also an active participant of the wholesale and retail electricity markets. OAO Mezhregionenergosbyt provides for above 85% of electricity consumption of Gazprom Group subsidiaries.

The Gazprom Group also carried out trading operations with electricity in European trading floors. Total electricity trading volume amounted to 272 TW/h. In addition, in 2012 the Gazprom Group supplied electricity of 2.1 TW/h to final consumers in United Kingdom and Germany.

#### Main areas of capital investments

The main investments in electric power in 2012 were allocated to construction of the second phase of the Cherepovets SDPP, power-generating units of Serovsky SDPP, Troitsky SDPP and Pravoberejny TPP-5, Adlersky TPP, as well as construction and modernization of power generating units at TPP OAO Mosenergo.

In 2012 the Group launched 2.2 GW of new power capacity in Russia. Power generating unit of Combined Cycle Plant-800 MW at Kirishskaya GRES (OAo WGC-2), new power generating unit of Combined Cycle Plant-450 MW at Praviberezhny TPP (OAo TGC-1), power generating unit at Novocherkassaya GRES (OAo WGC-2) with replacement of major equipment and hydro turbine unit No. 3 at Lesogorsky HPP (OAo TGC-1) were commissioned.

In January 2012, the 5th power generating unit of Razdansky TPP was put into test production. The project's objective was creation of a combined cycle gas turbine with the capacity of

460 MW based on the steam power plant with the capacity of 300 MW uncompleted in 1980 and new combined cycle gas turbine of Alstom.

#### Reporting year and subsequent events

In accordance with the decision of the Board of Directors made in 2011 on sale of shares of ZAO Kaunasskaya power station, a sales contract was signed in October 2012. The transaction was consummated in March 2013.

#### Development plans for electric and heat energy generation and sales segment

Implementation of the investment program under capacity supply contracts is also a priority in the development of the Group's energy companies. The Group's companies shall put into operation around 9GW of new capacities in Russia by 2016.

From 2007 to 2011, the electricity market was fully liberalised. As for the free gas market, it is still at the development stage, therefore, income from electricity sales is higher.

During the reform, a capacity payment scheme was launched which helps cover semi-fixed costs of generating companies. Starting from 2012, the competitive capacity selection procedure was launched which regulated the price depending on bids submitted by a generating company and capacity demand. Launch of the long-term capacity market and market liberalisation will guarantee that new power generation units commissioned under capacity supply contracts will pay off.

Gazprom targets to increase operating efficiency of the Group's generating entities by modernization of existing capacities and construction of new effective combined steamgas capacities that will increase production of electric power and heat. Gazprom Group is carrying out activities to improve operating efficiency, implements the cost optimization programs and measures to improve financial results to ensure the increase in the electricity assets' value.

The decisions made by the companies' boards of directors provide for the continuation of these activities. In 2013-2015 the full-scale implementation of Lean Production programme and programs on enhancing value in OAO WGC-2 and OAO TGC-1 is expected to produce the major effect.

The Group is considering potential electric power projects in a number of European and Northern-East Asian countries. Based on the analysis of the European electric power market in 2012, OAO Gazprom identified four regions which are the most promising for developing its activities in electric power segment: Germany, United Kingdom, Turkey and the Balkans. The implementation of decisions promoting investment in gas electrogeneration, in particular the "payment for capacity" tool, in the EU and certain European countries, is a crucial condition for OAO Gazprom's participation in the European power sector, especially projects for building generating capacity.

## **INNOVATIVE DEVELOPMENT**

Unique climate and geological conditions of new production regions that Gazprom plans to develop require the development and implementation of new technology, equipment, and materials. The long-term objective of the innovation activities is to continuously enhance the level of technology that would support the Company's leadership in the global energy business.

The Group's innovation activities are based on the Program of OAO Gazprom's Innovative Development for the period up to 2020 (hereinafter – the Program of Innovative Development) approved by the Company's Board of Directors.

The Program of Innovative Development covers a set of interdependent actions aimed at the development and implementation of new technologies, innovative products and services of the global level, as well as creation of favourable conditions for the development of innovative activity in OAO Gazprom and adjacent industries of the Russian Federation. The document highlights basic directions of technology improvement or technology priorities in gas, oil and electric power businesses. Investments into these areas will allow Gazprom to obtain the maximum economic benefit.

### **Research and Development**

Gazprom significantly invests in research and development. In 2012 research and development costs financed by the Gazprom Group totalled RUB 7.7 billion (in 2011, RUB 7.9 billion). In this area the Group is the leader among Russian energy companies and is among the top ten global energy companies.

With regard to each resulting intellectual property decision is made on the optimal form of its legal protection, expediency of patenting or selection of security system. As of 31 December 2012 entities of the Gazprom Group held 1,828 patents for patent rights subjects (207 patents were obtained in the reporting year). In 2012, 328 patent rights subjects were used in the business and corresponding economic benefit amounted to RUB 1.1 billion. More than 10% of patents held by the Group entities were obtained in 2012.

#### Exploration

For the purposes of improving the accuracy of forecasting the hydrocarbon deposits development the Company:

- has developed the geological model, including the structure and oil&gas bearing capacity, of the sedimentary cover in the south block of the Siberian platform; has substantiated the prospectivity of oil and gas plays in the junction zone of the Russkaya platform and the Urals for the purposes of licensing the most prospective subsoil blocks;
- has assessed resources and oil and gas potential of the West African offshore licensed blocks for the purposes of developing an efficient investment policy of OAO Gazprom in West and South-West Africa;
- continues to explore coal bed characteristics at the science base in the Kuznetsk Basin for the purpose of increasing well production rates.

Preparation is under way to commence advanced projects of developing Cenonian and Turonian gas deposits in the north of West Siberia, non-conventional resources of gas (gas hydrates, shale and coal gases, tight gas), hydrocarbon fields in the north-east offshore area of the Sakhalin island.

### Development and production

To improve efficiency of field development including development of new gas production regions and offshore areas of northern seas, the Group:

- has developed technical solutions supporting creation of national subglacial gas production equipment and technology in the process of developing field infrastructure in the Russian offshore areas (as exemplified by the Rusanovsky and Leningradsky fields of the Kara Sea);
- has been developing technical requirements and technical solutions for the creation of equipment for the subglacial gas production facility that would promote development of gas condensate fields in sea ice hazardous regions of the north-east offshore area of the Barents sea;
- has developed and tested at pilot sites solutions for technical and biological rehabilitation with the use of biologies, bio-polymers, drilling waste and granulated seeding of disturbed and contaminated lands of the Bovanenkovo group of fields;
- has been implementing automated systems of remote control and management of wells in electrified and non-electrified clusters, as well as systems managing vital infrastructure of gas fields on the principles of minimal manned technology.

The work is continued in the following areas:

- expediency consideration of pumping carbon dioxide into the productive strata of the Astrakhansky gas condensate field for the purpose of increasing condensate recovery;
- creation of the scientific basis for and technology of wave action on the productive strata for the purposes of increasing hydrocarbon recovery and well productivity.

### Gas transportation and underground storage

To ensure reliability and safety of gas transportation and storage as well as to improve efficiency of gas pumping equipment, the Company has been developing and implementing:

- a system that will manage technical condition and integrity of the linear part of the trunk pipelines and compressor stations of the UGSS;
- smart pigging tools of the new generation that are based on magneto-electric acoustical method of control, diagnostic tools for gas pipelines with internal anti-friction coating designed for the pressure of above 10 MPa;
- optimal solutions in the area of forecasting geological risks associated with building up underground storage facilities for gas, oil and refinery products in rock-salt deposits in the Russian Federation, including East Siberia regions where helium-rich gas fields are developed.

### Processing of hydrocarbon feedstock and manufacturing of petrochemical products

In the area of gas processing the Company continues to implement projects related to creating technologies of synthetic liquid fuel (SLF) production from natural gas:

- the Fischer–Tropsch process based technology of large-scale SLF production (over 100 thousand tons);
- the small scale SLF production technology based on the use of dual function catalysts aimed at production of high-octane gasoline directly at gas production sites (depleted and low pressure wells).

Commercial realisation of the new technologies is planned upon completion of the corresponding research and development work after 2015.

In the framework of helium-rich gas fields development the Company has been designing a process of an integrated feedstock processing that would result in obtaining LNG and helium, as well as a process of and technical solutions for helium transportation and storage. In particular, the Company has been developing a pilot industrial two-stage membrane unit for extracting helium from high pressure natural gas for Kovykta and Irkutsk gas production centres. The unit will be tested at a processing facility of the Kovykta field.

### Electric power

In the reporting year generating companies of Gazprom Group implemented the following projects:

- TPP-16 of OAO Mosenergo: construction of an innovative CCGT unit with the capacity of 420 MW on the basis of a GTP unit with the capacity of 280 MW;
- Troitskaya SDPP (OAO WGC-2): construction of a new carbon block with the capacity of 660 MW;
- construction of a carbon block with CFB-330 at Novocherkassaya SDPP is under way; it will allow to use several different types of coal including those of low quality for boiler equipment operation.

The short-term development plans also include: an upgrade of GTP-160 turbines for CCGT-450 units; building up of a unit CCGT-500 MW or more; development of technical solutions for the reconstruction of blocks T-250/300-240.

In the process of developing the framework for an integrated development of the Yamalo-Nenetsky Autonomous Region energy supply system, the Company has substantiated circuitry and priority processes for the implementation of non-conventional and renewable power sources (wind farms, small scale hydro power plants, thermal pumps, solar energy collectors, solid and bio-waste recycling technologies) to ensure supply of energy to remote communities of the region.

In the area of small-scale power generation the Company continues to develop power supply plants based on solid polymer fuel cells (with the capacity of up to 10 kW) that are intended to be used for autonomous supply of power to cathodic control stations, communication hubs, telemechanics and other users in hard-to-reach areas, and as emergency (backup) sources of electrical power.

### **Improved management of innovative activities**

To fulfil the task of innovative activities control that is defined in the Program of Innovative Development, in the reporting year the Company took actions to improve the system controlling a number of research entities and the corporate R&D management system.

To promote innovative activities the Group entities have approved standard organisational structures for gas transportation and gas producing subsidiaries of OAO Gazprom. These structures envisage creation of innovative activities support divisions that will implement the Program of Innovative Development.

### **International cooperation in R&D**

Gazprom's interaction with foreign partners is not limited to business. Business relations are generally accompanied by mutually beneficial cooperation in R&D carried out on the basis of underlying agreements and joint programs.

In Europe Gazprom's partners in research and development projects are well known German companies E.ON Ruhrgas AG BASF / Wintershall Holding, Verbundnetz Gas AG, Siemens AG,

Europipe, as well as Nederlandse Gasunie, a Dutch company; GDF SUEZ, a French company; ENI, an Italian company, and Statoil ASA, a Norwegian company.

In the Asian-Pacific Region the science and technology cooperation is being actively developed with the Korean gas corporation KOGAS, the Oil and Gas Corporation of Vietnam, the Chinese corporation CNPC, the Agency for Natural Resources and Energy under the Japanese Ministry of Economy, Trade and Industry.

This cooperation facilitates an exchange of best operating practices, an exchange of information on prospects and priorities of global technical development of the gas industry, identification of topical science and technology issues the joint solution of which creates a foundation for new international knowledge and technology.

Given positive results of their cooperation OAO Gazprom and its partners plan to continue their interaction in R&D areas that are of mutual interest to them, including:

- technologies of helium extraction in field conditions of East Siberia and Far East;
- technologies of distributed compressing to increase operational efficiency of fields in their closing stage;
- using gas as a motor fuel;
- harmonization of gas industry national standards and norms, including those related to the quality of supplied gas;
- environmental protection, energy saving and energy efficiency.

## ENVIRONMENT PROTECTION

Efficient usage of mineral resources and preservation of the environment for future generations is the key principle of the Company's Ecological Policy. Being one of the largest user of natural resources in Russia the Gazprom Group strictly complies with rules of international and Russian environmental legislation and voluntary commitments in this area.

The Ecological Policy is the basis of Environmental Management System (EMS). In October 2011, the Board of Directors approved OAO Gazprom's Environmental Policy and recommended that Gazprom Group's entities should use this document.

In 2011, EMS of OAO Gazprom was successfully certified and in 2012, it was subject to the compliance audit that confirmed EMS compliance with International Standard ISO 14001:2004.

In 2012, as a results of 256 governmental inspections in Gazprom Group's entities 207 violations of the Russian environmental legislation were identified. Penalties paid amounted to RUB 6.0 million.

The main indicators of Gazprom Group impact on environment are presented below:

Main indicators	Year ended 31 December		Change
	2012	2011	
Pollutant emissions into the air, thousand tons	3,410.9	3,124.2	9.2%
carbonic oxide	1,031.9	687.2	50.2%
nitrogen oxide	378.3	372.6	1.5%
sulfur dioxide	310.0	260.9	18.8%
hydrocarbons (methane)	1,606.6	1,491.1	7.7%
Discharge of waste water, million cm	4,931.2	5,300.7	-7.0%
including in surface-water bodies	4,893.0	5,257.7	-6.9%
including clean and cleaned as per standard norms	4,691.6	5,096.2	-7.9%
Generation of waste, thousand tons	5,226.6	4,973.8	5.1%
Recultivated lands, thousand ha	9.7	11.6	-16.2%

Gross pollutant emissions made by stationary sources of ambient air contamination of Gazprom Group increased by 286.7 thousand tons or 9% as compared with prior year. Gazprom Neft Group's contribution was the largest and its emissions increased by 276.4 thousand tons. The most significant volume of emissions (84%) of Gazprom Neft Group falls for emissions from associated gas burning.

Increase in waste products as compared with prior year is explained by inclusion of the merged asset, OAO Gazprom neftekhim Salavat, in the financial statements.

In 2012 the Group reduced the volume of water disposed into surface water bodies by means of reducing the water consumption volume, including for technical needs. Power companies of the Group account for 98% of consumed and almost 99% of disposed water volumes. 96.4% of waste water disposed to surface water was filtered and met standard quality requirements.

Gazprom Group's environmental costs are disclosed below:

(RUB million)	Year ended 31 December		Change
	2012	2011	
Current costs	18,354.68	11,232.70	63.4%
Costs of capital repairs of fixed assets used for environmental protection	2,444.61	2,571.76	-4.9%
Pollution charges	1,563.12	1,017.24	53.7%
Capital environmental costs	12,885.76	9,785.71	31.7%
<b>Total</b>	<b>35,248.17</b>	<b>24,607.41</b>	<b>43.2%</b>

In 2012 the Group paid RUB 1.56 billion to the budgets of different levels for negative impact on the environment. Out of that amount RUB 0.61 billion were paid for negative impact within the established limits and RUB 0.95 billion were paid for negative impact in excess of the established limits. A 54% increase as compared to 2011 is explained by the increased payments for negative impact on the environment in Gazprom Neft Group due to applying multiplying coefficients of 4.5 and 5 to the established payments for pollutant emissions. This is explained by the fact that Gazprom Neft did not complete the works allowing to reach 95% APG utilization level by 2012 in accordance with the Resolution of the Russian Government of 8 January 2009 No.7 “On measures for promoting the reduction of air pollution caused by APG products combusted at flare facilities”.

OAO Gazprom's environmental initiatives and actions are carried out based on the Russian Energy Strategy up to 2030, Environmental Protection for 2012-2020 State Program of the Russian Federation and Environmental Doctrine of the Russian Federation. The main components of Gazprom's policy for environmental protection are: participation in international organisations' activities, development of environmental standards in accordance with the international agreements, research of greenhouse gas emissions, and implementation of target projects to reduce greenhouse gas emissions, and the efficient usage of associated gases.

In 2012, CO<sub>2</sub> and CH<sub>4</sub> emissions of OAO Gazprom's main upstream, downstream and underground storage subsidiaries were 123.8 million tons of CO<sub>2</sub> equivalent, which is 9.6 million tons (7%) less than in 2011. Reduction of greenhouse gas emissions resulted from decreased consumption of natural gas for compression purposes due to lower volumes of gas production and transportation, and fewer scheduled preventive repairs at gas producing entities, as well as certain activities performed as part of OAO Gazprom's Energy Efficiency Program for 2011–2013.

## EMPLOYEES

In its operations, the Group complies with all requirements of the conventions of International Labour Organization ratified by the Russian Federation. Guided thereby, the Group complies with international standards related to freedom of associations, salary, duration of the working day and labour conditions, employees' compensation for their work, social security, provision of paid vacation, labour safety, etc.

As of 31 December 2012 the number of employees in Gazprom Group's subsidiaries was 431.2 thousand people, including 27.4 thousand employees of Gazprom Group's entities registered abroad.

Increased number of employees as compared with the number as of 31 December 2011 is explained by the inclusion of OOO Gazprom Neftekhim Salavat and its subsidiaries into the Gazprom Group.

The structure of Gazprom Group's employees as of 31 December 2012 is provided in the following table:

(share)	<u>As of 31 December 2012</u>
Managers	13%
Specialists	26%
Workers	57%
Other employees	4%

The age composition of the Group's personnel is well balanced: employees aged up to 30 years account for 19.2%, aged 50 years and older - 25.2%.

The table below shows the age structure of the Gazprom Group's personnel as of 31 December 2012.

(share)	<u>As of 31 December 2012</u>
up to 30 years	19.2%
30 – 40 years	27.8%
40 – 50 years	27.8%
50 years and older	25.2%

The system of continuing house professional education of OAO Gazprom's personnel is based on the corporate training institutions. Its aim is to support and improve the professional level of the Group's employees. Gazprom's approaches to staff training and retraining make it possible to ensure efficient management of staff knowledge and to form a talent pool capable of realising the task of innovative development. In 2012 178.9 thousand employees took advanced and professional training courses.

OAO Gazprom pays special attention to young professionals. The Company takes individual approach to training and development of this staff category. In 2012 the Gazprom Group recruited over 2.1 thousand young professionals who graduated higher and secondary vocational educational establishments. Training costs of young professionals amounted to 68 million roubles.

Existing remuneration systems include a salary attached to the position and tariff rates adjusted for competency and business qualities, current bonuses based on employee's operational performance, additional payments and allowances depending on labour conditions and scope of work performed, annual performance bonuses and spot bonuses (for putting into operation production capacities and construction units, implementing new technologies, energy saving and discovering new hydrocarbon deposits etc.).

In the framework of developing standard corporate approaches to labor remuneration, in the reporting year the Company drafted new Standard provisions on remuneration of Gazprom entities' employees. This document specifies remuneration of employees who work in entities

involved in the development of offshore oil and gas fields as well as defines remuneration conditions of employees working in scientific organisations, catering divisions and internal audit services.

OAO Gazprom and its major gas production, transportation, underground storage, processing and sale subsidiaries have set up an incentive system for top management that comprises such elements as the annual bonus system and the stock option plan.

The social policy of OAO Gazprom is targeted at ensuring social security of employees and at motivating employees to work in the Company efficiently and for a long-time. This policy is realized through provision of allowances, guarantees, compensations, health care services and health resort treatment, various types of personal insurance, creation of comfort and safe labour conditions, provision of additional retirement benefits.

The housing program based on such market tools as bank mortgage lending is designed to solve housing problems. With the help of this tool over 9 thousand employees and pensioners participating in the general collective contract improved their living conditions in the reporting year.

## ANALYSIS OF FINANCIAL RESULTS OF OPERATIONS

### Results of operations

(RUB million)

	Year ended 31 December	
	2012	2011
Sales	4,764,411	4,637,090
Net gain from trading activity	2,821	2,791
Operating expenses	(3,481,264)	(2,942,181)
Reversal of (charge for) impairment and other provisions, net	3,208	(40,857)
<b>Operating profit</b>	<b>1,289,176</b>	<b>1,656,843</b>
Finance income	307,871	190,488
Finance expense	(247,138)	(267,823)
Share of net income of associated undertakings and jointly controlled entities	161,500	99,049
Gains on disposal of available-for-sale financial assets	546	1,379
<b>Profit before profit tax</b>	<b>1,511,955</b>	<b>1,679,936</b>
Current profit tax expense	(276,045)	(279,216)
Deferred profit tax expense	(25,344)	(58,278)
Profit tax expense	(301,389)	(337,494)
<b>Profit for the year</b>	<b>1,210,566</b>	<b>1,342,442</b>
<b>Other comprehensive income</b>		
Losses arising from change in fair value of available-for-sale financial assets, net of tax	(17,499)	(7,669)
Share of other comprehensive gain (loss) of associated undertakings and jointly controlled entities	1,885	(19,302)
Translation differences	(32,366)	19,342
Gains from cash flow hedges, net of tax	806	-
<b>Other comprehensive loss for the year, net of tax</b>	<b>(47,174)</b>	<b>(7,629)</b>
<b>Total comprehensive income for the year</b>	<b>1,163,392</b>	<b>1,334,813</b>
<b>Profit attributable to:</b>		
owners of OAO Gazprom	1,182,625	1,307,018
non-controlling interest	27,941	35,424
	<b>1,210,566</b>	<b>1,342,442</b>
<b>Total comprehensive income attributable to:</b>		
owners of OAO Gazprom	1,137,257	1,297,891
non-controlling interest	26,135	36,922
	<b>1,163,392</b>	<b>1,334,813</b>

## Sales

The following table sets out our volumes and realized prices:

(RUB million unless indicated otherwise)	Year ended 31 December	
	2012	2011
Sales of gas		
<i>Europe and other countries</i>		
Gross sales <sup>(1)</sup>	1,806,947	1,763,716
Custom duties	(337,492)	(324,647)
Net sales	1,469,455	1,439,069
Volumes in bcm	151.0	156.6
Gross average price, USD per mcm (including customs duties) <sup>(2)</sup>	385.1	383.0
Gross average price, RUB per mcm (including customs duties)	11,969.8	11,259.1
<i>FSU (Former Soviet Union)</i>		
Gross sales <sup>(1)</sup>	626,820	694,937
Custom duties	(97,304)	(57,759)
Net sales	529,516	637,178
Volumes in bcm	66.1	81.7
Gross average price, USD per mcm (including customs duties) <sup>(2)</sup>	305.3	289.5
Gross average price, RUB per mcm (including customs duties)	9,489.5	8,509.3
<i>Russian Federation</i>		
Gross sales (net of VAT)	760,696	738,601
Net sales	760,696	738,601
Volumes in bcm	264.9	280.7
Average price, RUB per mcm (net of VAT)	2,871.4	2,631.7
<i>Total sales of gas</i>		
Gross sales (net of VAT)	3,194,463	3,197,254
Customs duties	(434,796)	(382,406)
Effect of retroactive gas price adjustments	(102,749)	-
Net sales	2,656,918	2,814,848
Volumes in bcm	482.0	519.0
Net sales of refined products (net of excise tax, VAT and customs duties)	1,208,153	973,026
Net sales of electric and heat energy (net of VAT)	343,509	344,551
Net sales of crude oil and gas condensate (net of VAT and customs duties)	275,307	235,432
Gas transportation net sales (net of VAT)	125,386	112,995
Other revenues (net of VAT)	155,138	156,238
<b>Total sales (net of excise tax, VAT and customs duties)</b>	<b>4,764,411</b>	<b>4,637,090</b>

Notes:

(1) VAT is not charged on sales to Europe and Former Soviet Union countries.

(2) Calculated on the basis of annual average currency exchange rate between RUB and USD.

Total sales (net of excise tax, VAT, and customs duties) increased by RUB 127,321 million, or 3%, to RUB 4,764,411 million in the year ended 31 December 2012 compared to the prior year.

Sales of gas accounted for 56% and 61% of total net sales in the years ended 31 December 2012 and 2011, respectively.

Net sales of gas decreased from RUB 2,814,848 million in the year ended 31 December 2011 to RUB 2,656,918 million in the year ended 31 December 2012 or by 6%.

Net sales of gas to Europe and other countries increased in the year ended 31 December 2012 compared to the year ended 31 December 2011, by RUB 30,386 million, or 2%, to RUB 1,469,455 million. The overall increase in net sales of gas to Europe and other countries was primarily driven by the increase in average prices. The gross average RUB price (including customs duties) increased by 6% in the year ended 31 December 2012, compared to the year

ended 31 December 2011. Volume of gas sold in the year ended 31 December 2012 decreased by 4% compared to the prior year.

During the year ended 31 December 2012 the Group recognized the effect of renegotiated prices for long-term gas supply contracts related to gas deliveries in the years ended 31 December 2010 and 2011. Retroactive gas price adjustments were recognized in the financial statements as a decrease of sales in the amount of RUB 102,749 million. In the Q4 2012 the Group revised the amount of retroactive gas price adjustments downwards.

Net sales of gas to FSU countries decreased in the year ended 31 December 2012 compared to the year ended 31 December 2011, by RUB 107,662 million, or 17%, to RUB 529,516 million. This decrease was mainly due to the decrease in volumes of gas sold to FSU countries by 19% in the year ended 31 December 2012 compared to the year ended 31 December 2011. The gross average RUB price (including customs duties) increased by 12% in the year ended 31 December 2012, compared to the prior year.

Net sales of gas in the Russian Federation increased in the year ended 31 December 2012 compared to the same period of the prior year by RUB 22,095 million, or 3%, to RUB 760,696 million. The change was due to the increase in the gross average price for domestic gas sales by 9% in the year ended 31 December 2012 compared to the prior year and decrease of gas volume sold in the year ended 31 December 2012 compared to the prior year by 6%.

Net sales of refined products (net of excise tax, VAT and customs duties) increased by RUB 235,127 million, or 24%, to RUB 1,208,153 million in the year ended 31 December 2012 in comparison with the same period of the prior year. The increase is mainly driven by increase of prices and volumes sold by Gazprom нефт group to customers in the Russian Federation and inclusion of OAO Gazprom neftekhim Salavat sales, due to the fact that in 2012 the Group obtained control over the operating and financial activities of the company. In the years ended 31 December 2012 and 2011 the Gazprom нефт Group's sales comprised 77% and 84% of the total amount of our net sales of refined products, respectively.

Net sales of electric and heat energy (net of VAT) insignificantly decreased in the year ended 31 December 2012 compared to the prior year and amounted to RUB 343,509 million. The decrease is mainly caused by decline in revenues from electric and heat energy sales due to reduction of electricity prices at the day-ahead market and decrease in sales volumes of electric and heat energy.

Net sales of crude oil and gas condensate (net of VAT and customs duties) increased by RUB 39,875 million, or 17%, to RUB 275,307 million in the year ended 31 December 2012 compared to RUB 235,432 million in the year ended 31 December 2011. The increase was mainly caused by the increase in oil and gas condensate prices and volumes sold in the year ended 31 December 2012 compared to the prior year. Sales of crude oil included in net sales of crude oil and gas condensate (net of VAT and customs duties), amounted to RUB 234,217 million and RUB 189,945 million in the years ended 31 December 2012 and 2011, respectively.

Gas transportation net sales (net of VAT) increased by RUB 12,391 million, or 11%, to RUB 125,386 million in the year ended 31 December 2012 from RUB 112,995 million in the year ended 31 December 2011. The growth was mainly caused by the increase of transportation volumes for independent gas suppliers in the year ended 31 December 2011 compared to the same period of the prior year, as well as by increase of gas transportation tariffs for independent suppliers.

Other revenues decreased by RUB 1,100 million, or 1%, to RUB 155,138 million in the year ended 31 December 2012 compared to RUB 156,238 million in the year ended 31 December 2011.

Net gain from trading activity increased insignificantly and totaled RUB 2,821 million in the year ended 31 December 2012 in comparison with RUB 2,791 million in the year ended 31 December 2011.

### Operating expenses

Operating expenses increased by 18% in the year ended 31 December 2012 to RUB 3,481,264 million from RUB 2,942,181 million in the year ended 31 December 2011. Operating expenses as a percentage of sales increased from 63% in the year ended 31 December 2011 to 73% in the year ended 31 December 2012. The table below presents a breakdown of operating expenses in each year:

(RUB million)	Year ended 31 December	
	2012	2011
Purchased oil and gas	910,560	828,551
Taxes other than on income	578,617	418,134
Staff costs	447,954	374,731
Depreciation	334,162	275,184
Transit of gas, oil and refined products	319,963	280,770
Repairs and maintenance	216,676	189,865
Materials	183,792	104,349
Cost of goods for resale, including refined products	129,812	125,520
Electricity and heating expenses	74,572	70,356
Transportation services	37,782	33,753
Social expenses	31,736	18,811
Rental expenses	23,237	26,787
Insurance expenses	22,321	20,384
Research and development expenses	19,766	29,489
Heat transmission	19,647	26,465
Processing services	14,228	10,935
Exchange rate differences on operating items	13,752	(6,386)
Losses (profit) from derivatives financial instruments in the operating activities	8,802	(4,613)
Other	181,150	183,509
	<b><u>3,568,529</u></b>	<b><u>3,006,594</u></b>
Changes in inventories of finished goods, work in progress and other effects	<u>(87,265)</u>	<u>(64,413)</u>
<b>Total operating expenses</b>	<b><u>3,481,264</u></b>	<b><u>2,942,181</u></b>

### *Purchased gas and oil*

Cost of purchased gas and oil increased by 10% to RUB 910,560 million in 2012 from RUB 828,551 million in 2011. Cost of purchased gas decreased by RUB 21,824 million, or 4% and amounted to RUB 556,182 million. This decrease relates to the decrease in volumes of gas purchased from third parties abroad. The cost of purchased oil included in the cost of purchased gas and oil increased by RUB 103,833 million, or 41%, and amounted to RUB 354,378 million in 2012 in comparison to RUB 250,545 million in 2011 due to the increase in oil prices.

*Taxes other than on income*

Taxes other than on income consist of:

(RUB million)	Year ended 31 December	
	2012	2011
Natural resources production tax	413,181	265,742
Excise tax	98,780	95,752
Property tax	54,149	46,699
Other taxes	<u>12,507</u>	<u>9,941</u>
<b>Taxes other than on income</b>	<b>578,617</b>	<b>418,134</b>

The natural resources production tax increased by 55% to RUB 413,181 million in 2012 from RUB 265,742 million in 2011. The increase of natural resources production tax on gas extraction results from growth of tax rate for gas from RUB 237 to RUB 509 per thousand cubic meters since 1 January 2012. The increase of natural resources production tax on oil extraction results from growth of base tax rate for oil from RUB 419 to RUB 446 per ton, as well as from the increase of average world oil prices.

*Staff costs*

Staff costs increased by 20% to RUB 447,954 million in 2012 from RUB 374,731 million in 2011. Staff costs includes pension expenses, which were RUB 67,694 million in 2012 and RUB 35,471 million in 2011. The increase of staff costs (excluding pension liabilities expenses) mainly resulted from the average salary indexation. Increase of pension expenses relates to reconsideration of actuarial assumptions for 2012.

*Depreciation*

Depreciation increased by 21%, or RUB 58,978 million, to RUB 334,162 million in 2012 from RUB 275,184 million in 2011. The increase primarily relates to the growth in the fixed asset base.

*Transit of gas, oil and refined products*

Transit of gas, oil and refined products increased by 14% to RUB 319,963 million in 2012 from RUB 280,770 million in 2011. This increase is mainly driven by increase of gas transportation cost to Western Europe via the Nord Stream pipeline.

*Repairs and maintenance*

Expenditure on repairs and maintenance increased by 14% to RUB 216,676 million in 2012 from RUB 189,865 million in 2011. This increase was caused by the increase of volume of repair services rendered by third parties to the Group in 2012.

*Materials*

Cost of materials increased by 76% to RUB 183,792 million in 2012 from RUB 104,349 million in 2011. The growth mainly relates to increase of the scope of the Gazprom Group consolidation - inclusion of OAO Gazprom neftekhim Salavat into the consolidated financial statements from June 2012 as well as to increase of materials purchase prices.

*Cost of goods for resale, including refined products*

Cost of goods for resale, including refined products increased by 3% to RUB 129,812 million in 2012 from RUB 125,520 million in 2011. The increase in cost of goods for resale, including refined products, mainly results from the increase in volumes of refined products purchased by the Gazprom neft Group and the increase in refined products prices.

*Electricity and heating expenses*

Electricity and heating expenses increased by 6% to RUB 74,572 million in 2012 from RUB 70,356 million in 2011. The increase mainly resulted from the increase in consumption of electricity and increase in electricity tariffs.

*Exchange rate differences on operating items*

Exchange rate differences on operating items in 2012 amounted to a net loss of RUB 13,752 million and net gain of RUB 6,386 million in 2011. The change was primarily driven by depreciation of USD and EURO against RUB by 6% and 4% in 2012, respectively, compared to appreciation of USD and EURO against RUB by 6% and 3% in 2011, respectively.

*Other operating expenses*

Other operating expenses decreased by 1% to RUB 181,150 million in 2012 from RUB 183,509 million in 2011. Other expenses include bank charges, security services, legal and consulting services, software services, charity, finance aid and advertising services.

*Changes in inventories of finished goods, work in progress and other effects*

Changes in inventories of finished goods, work in progress and other effects increased by 35% to RUB 87,265 million in 2012. This increase relates mainly to the increase in the balance of finished goods as of 31 December 2012 in comparison to the balance as of 31 December 2011.

Reversal of (charge for) impairment and other provisions, net

The net release in 2012 was primarily due to the release of impairment for construction in progress more than charge for new bad debt provisions.

In October 2012, upon completion of the first phase of infrastructure development and commencement of operations of the Bovanenkovo field, the Group reversed the previously created impairment provision for assets under construction related to Bovanenkovo and Kharosaveyskoe fields and the Obskaya – Bovanenkovo railroad. Total amount of the impairment provision reversal amounted to RUB 47,574 million.

Charges for provisions for short-term and long-term accounts receivable were RUB 47,238 million and RUB 42,351 million related to 2012 and 2011, respectively.

Operating profit

As a result of the factors discussed above, our operating profit decreased by RUB 367,667 million, or 22%, to RUB 1,289,176 million in the year ended 31 December 2012 from RUB 1,656,843 million in the year ended 31 December 2011. Operating profit margin decreased from 36% in the year ended 31 December 2011 to 27% in the year ended 31 December 2012.

Finance income (expense)

(RUB million)	Year ended 31 December ,	
	2012	2011
Exchange gains	281,379	171,570
Exchange losses	<u>(210,146)</u>	<u>(235,825)</u>
Net exchange gain (loss)	71,233	(64,255)
Interest income	26,492	18,918
Interest expense	<u>(36,992)</u>	<u>(31,998)</u>
<b>Net finance income (expense)</b>	<b>60,733</b>	<b>(77,335)</b>

The net exchange gain of RUB 71,233 million in the year ended 31 December 2012 in comparison with net exchange loss of RUB 64,255 million the year ended 31 December 2011 is explained by depreciation of USD and Euro against RUB in the year ended 31 December 2012 in comparison with the prior year. This decreased liabilities of the Group denominated in foreign currency.

Interest income increased by 40% to RUB 26,492 million in the year ended 31 December 2012 from RUB 18,918 million in the year ended 31 December 2011, mainly due to increase of interest accrued on Group's cash held with banks and consolidation of new companies.

Interest expense increased by 16% to RUB 36,992 million in the year ended 31 December 2012 from RUB 31,998 million in the year ended 31 December 2011, mainly due to increase in average borrowings balance during the year ended 31 December 2012 in comparison with the prior year.

Share of net income of associated undertakings and jointly controlled entities

Share of net income of associated undertakings and jointly controlled entities increased by RUB 62,451 million, or 63%, to RUB 161,500 million in the year ended 31 December 2012 compared to RUB 99,049 million in the year ended 31 December 2011.

The increase of the Group's share of net income of associated undertakings and jointly controlled entities in the year ended 31 December 2012 relates mainly to recognition of share in net income of RosUkrEnergo AG for 2011 in the amount of RUB 17,017 million triggered by the receipt of dividends in July 2012, increase in net income of Sakhalin Energy Investment Company Ltd. by RUB 12,799 million due to increase in sales of hydrocarbons, and increase in net income of Salym Petroleum Development N.V., OAO Tomskneft VNK and its subsidiaries and OAO NGK Slavneft and its subsidiaries in the total amount of RUB 21,570 million caused by the growth of oil prices.

Profit tax

Total profit tax expense decreased by RUB 36,105 million, or 11%, to RUB 301,389 million for the year ended 31 December 2012 compared to RUB 337,494 million for the year ended 31 December 2011. The effective profit tax rate was 19.9% and 20.1% in the years ended 31 December 2012 and 2011, respectively.

Profit for the period attributable to owners of OAO Gazprom

As a result of the factors discussed above, our profit for the period attributable to owners of OAO Gazprom decreased by RUB 124,393 million, or 10%, from RUB 1,307,018 million in the year ended 31 December 2011 to RUB 1,182,625 million in the year ended 31 December 2012.

Profit for the period attributable to non-controlling interest

Profit for the period attributable to non-controlling interest decreased by RUB 7,483 million, or 21%, to RUB 27,941 million in the year ended 31 December 2012 compared to RUB 35,424 million in the year ended 31 December 2011.

## Liquidity and capital recourses

The following table summarizes our statement of cash flows:

(RUB million)	Year ended 31 December,	
	2012	2011
Net cash provided by operating activities	1,445,617	1,637,450
Net cash used for investing activities	(1,267,310)	(1,605,245)
Net cash (used for) provided by financing activities	(249,381)	31,814

### Net cash provided by operating activities

Net cash provided by operating activities decreased by RUB 191,833 million, or 12%, and amounted to RUB 1,445,617 million in the year ended 31 December 2012 compared to RUB 1,637,450 million in the year ended 31 December 2011. The decrease was primarily due to the decrease in profit before profit tax caused by increase in share of operating expenses in total sales in the year ended 31 December 2012 in comparison with the year ended 31 December 2011.

### Net cash used for investing activities

Net cash used for investing activities decreased by RUB 337,935 million, or 21%, to RUB 1,267,310 million in the year ended 31 December 2012 compared to RUB 1,605,245 million in the year ended 31 December 2011. The decrease relates mainly to the decrease in cash used for capital expenditures in development of fields and transport infrastructure, as well as, decrease in cash used for acquisition of subsidiaries. This influence was partly offset by increase in proceeds from associated undertakings and jointly controlled entities in the year ended 31 December 2012 in comparison with the year ended 31 December 2011.

### Net cash (used for) provided by financing activities

Net cash used for financing activities amounted to RUB 249,381 million in the year ended 31 December 2012 compared to net cash provided by financing activities in the amount of RUB 31,814 million in the year ended 31 December 2011. This change was primarily due to increase of dividends paid in the year ended 31 December 2012 compared to the year ended 31 December 2011 and due to change from net proceeds from long term loans and borrowings in 2011 to net repayment in 2012.

### Working capital

The working capital surplus (current assets less current liabilities) was RUB 918,929 million as of 31 December 2012 and RUB 931,038 million as of 31 December 2011. The decrease in our working capital by RUB 12,109 million in the year ended 31 December 2012 was primarily due to increase of accounts payable balance and decrease in cash and cash equivalents. These effects were partially offset by an increase of accounts receivable balance, increase in VAT recoverable and decrease in short-term borrowings and current portion of long-term borrowings.

The increase in accounts payable amounting to RUB 235,630 million was caused mainly by increase in trade payables related to investment construction and gas price adjustments recognition in respect of gas supplied in 2010 – 2012 arising from the claims made by foreign customers based on the contracts turns.

The increase in short-term accounts receivable amounting to RUB 156,053 million was caused by increase in debt for gas in all geographical segments.

The increase in VAT recoverable in the amount of RUB 91,796 million was caused by completion of constructions under the investment agreement.

The decrease in short-term borrowings and current portion of long-term borrowings in the amount of RUB 40,061 million was caused by redemption of loans.

Management of OAO Gazprom believes that the Group has sufficient working capital to meet the Group's obligations for at least the next twelve months. However, the Group is dependent on the short-term credit markets to finance its working capital. The Group is also dependent on a regular access to the domestic debt capital markets to meet a significant portion of its financing requirements in Russian rubles.

## Capital expenditures

Total capital expenditures (excluding the effect of acquisitions of subsidiaries) by segment for the years ended 31 December 2012 and 2011 is presented in the table below:

	Year ended 31 December	
	2012 <sup>(1)</sup>	2011 <sup>(1)</sup>
(RUB million)		
Transport	706,414	905,010
Production of gas	285,925	288,409
Refining	170,860	139,670
Production of crude oil and gas condensate	139,296	97,359
Electric and heat energy generation and sales	70,440	85,463
Distribution	61,266	51,270
Gas storage	23,031	24,585
All other segments	<u>78,695</u>	<u>36,343</u>
<b>Total</b>	<b><u>1,535,927</u></b>	<b><u>1,628,109</u></b>

Note:

- (1) The capital expenditures in the present analysis differs from the capital additions disclosed within the Group's business segments in IFRS consolidated financial statements of OAO Gazprom primarily due to VAT.

Total capital expenditures (excluding the effect of acquisitions of subsidiaries) decreased by RUB 92,182 million, or 6%, from RUB 1,628,109 million in the year ended 31 December 2011 to RUB 1,535,927 million in the year ended 31 December 2012.

The decrease of our capital expenditures in the Transport segment was primarily due to assets that were put into operation, including of Pipeline Bovanenkovo-Ukhta, Pipeline Ukhta-Torzhok and launching of Bovanenkovo field.

The increase of our capital expenditures in the Refining segment was primarily due to increased capital expenditures of OAO Gazprom neftekhim Salavat and OOO Novourengovsky GCC.

The increase of our capital expenditures in the segment of Production of crude oil and gas condensate was due to capital expenditures of the Gazprom Neft Group.

The decrease of our capital expenditures in the Electric and heat energy generation and sales segment was primarily due to decrease of capital expenditures of OOO Gazprom Investproekt in connection with the completion of the Adlerskaya HPP.

The increase of capital investment in other segments was mainly due to construction in the scope of the Program of Construction of Olympic Venues and the Development of Sochi as a Mountain Climate Resort.

## Debt obligations

Net debt balance (defined as the sum of short-term borrowings, current portion of long-term borrowings, short-term promissory notes payable, long-term borrowings, long-term promissory notes payable, net of cash and cash equivalents and balances of cash and cash equivalents restricted as to withdrawal under the terms of certain borrowings and other contractual obligations) increased by RUB 46,606 million, or 4.5%, from RUB 1,034,941 million as of 31 December 2011 to RUB 1,081,547 million as of 31 December 2012. This growth resulted from the decrease of cash and cash equivalents.

(RUB million)

	<b>As of 31 December,</b>	
	<b>2012</b>	<b>2011</b>
<b>Long-term borrowings</b>		
Fixed interest rate borrowings	1,164,841	1,191,984
Weighted average interest rates for fixed rate borrowings	7.12%	7.38%
Variable interest rate borrowings	268,997	283,252
Weighted average interest rates for variable rate borrowings	<u>3.02%</u>	<u>2.91%</u>
<b>Total long-term borrowings</b>	<b>1,433,838</b>	<b>1,475,236</b>
RUB denominated borrowings	207,953	203,742
Foreign currency denominated borrowings	<u>1,225,885</u>	<u>1,271,494</u>
<b>Total long-term borrowings</b>	<b>1,433,838</b>	<b>1,475,236</b>
Less: current portion of long-term borrowings	(255,945)	(301,942)
Add: long-term promissory notes	<u>41</u>	<u>-</u>
<b>Total long-term debt obligations</b>	<b>1,177,934</b>	<b>1,173,294</b>
<b>Short-term debt borrowings</b>		
Fixed interest rate borrowings	60,482	54,098
Weighted average interest rates for fixed rate borrowings	5.00%	5.11%
Variable interest rate borrowings	10,372	10,777
Weighted average interest rates for variable rate borrowings	<u>1.94%</u>	<u>6.25%</u>
<b>Total short-term borrowings</b>	<b>70,854</b>	<b>64,875</b>
RUB denominated borrowings	27,958	28,465
Foreign currency denominated borrowings	<u>42,896</u>	<u>36,410</u>
<b>Total short-term borrowings</b>	<b>70,854</b>	<b>64,875</b>
Plus: Current portion of long-term borrowings	255,945	301,942
Short-term promissory notes	<u>8</u>	<u>51</u>
<b>Total short-term debt obligations</b>	<b>326,807</b>	<b>366,868</b>
<b>Total borrowings</b>	<b>1,504,741</b>	<b>1,540,162</b>

The following table presents our actual foreign currency denominated long-term borrowings (expressed in millions of USD) as of 31 December 2012 and 2011 as well as the same balances expressed in RUB:

	<b>As of 31 December,</b>	
	<b>2012</b>	<b>2011</b>
USD denominated (expressed in USD million)	28,562	28,708
Euro denominated (expressed in USD million) <sup>(1)</sup>	11,787	10,498
Other currencies denominated (expressed in USD million)	12	286
<b>Total long-term foreign currency denominated borrowings expressed in USD million</b>	<b>40,361</b>	<b>39,492</b>
<b>Total long-term foreign currency denominated borrowings expressed in RUB million</b> <sup>(2)</sup>	<b>1,225,885</b>	<b>1,271,494</b>

Notes:

(1) Converted at Euro to U.S.\$ exchange rate of 1.32 and 1.29 as of 31 December 2012 and 2011, respectively.

(2) Converted at the exchange rate as of period-end.

A portion of our long-term borrowings denominated in convertible currencies is collateralized by revenue under certain of the Group's export contracts. As of 31 December 2012 and 2011, borrowings of RUB 12,509 million and RUB 18,838 million, respectively, inclusive of current portion of long-term borrowings, were secured by revenues from export supplies of gas to Western Europe.

As of 31 December 2012 and 31 December 2011 according to the project facility agreement, signed within the framework of the development project of Yuzhno-Russkoe oil and gas field with the group of international financial institutions with UniCredit Bank AG acting as a facility agent, ordinary shares of OAO Severneftegazprom with the pledge value of RUB 16,968 million and fixed assets with the pledge value of RUB 25,656 million were pledged to ING Bank N.V. (London branch) up to the date of full redemption of the liabilities on this agreement. Management of the Group does not expect any substantial consequences to occur which relate to respective pledge agreement.

The following table presents the schedule of repayments for long-term borrowings (excluding long-term promissory notes) as of 31 December 2012 and 2011:

(RUB million)	As of 31 December,	
	2012	2011
Between one and two years	278,726	264,547
Between two and five years	502,399	586,574
After five years	396,768	322,173
<b>Total</b>	<b>1,177,893</b>	<b>1,173,294</b>

## SHAREHOLDER STRUCTURE AND STOCK MARKET OF OAO GAZPROM

OAO Gazprom's charter capital amounts to RUB 118,367,564,500, consisting of 23,673,512,900 ordinary registered shares with a nominal value of RUB 5 each. There are no preference shares.

During 2012 the equity holding structure changed insignificantly.

The following table summarises shareholder structure of OAO Gazprom:

	As of 31 December	
	2012	2011
Interest controlled by the Russian Federation, total, including:	50.002%	50.002%
Russian Federation represented by the Federal Agency For State Property Management	38.373%	38.373%
OAO Rosneftegaz	10.740%	10.740%
OAO Rosgazifikatsiya	0.889%	0.889%
The Bank of New York Mellon (bank emitting ADR issued against OAO Gazprom's ordinary shares)	26.955%	28.350 %
Other entities	23.043%	21.648 %

The Russian Federation is the major shareholder of OAO Gazprom with a controlling interest exceeding 50%.

Ordinary shares of OAO Gazprom are traded on Moscow Interbank Currency Exchange, established in December 2011 as a result of Moscow Interbank Currency Exchange and The Russian Trading System merger. OAO Gazprom's shares are among the most liquid shares on the Russian stock market: they are accounted for MICEX and RTS indexes computation.

American Depositary Receipts of OAO Gazprom are freely tradable on the London Stock Exchange, the Berlin-Bremen Stock Exchange and the Frankfurt Stock Exchange with majority of transactions being registered on the London Stock Exchange.

The majority of OAO Gazprom's ADR is traded on the over-the-counter stock market in the United States among qualified institutional investors.

	As of 31 December		Changes
	2012	2011	
<b>MICEX</b>			
Closing price for share, RUB			
Year end	143.91	171.37	-16.0%
Minimum	137.18	143.03	-4.1%
Maximum	199.69	243.93	-18.1%
Average daily trading volume, million shares	39.4	74.6	-47.2%
Average daily trading volume, RUB billion	6.4	14.3	-55.2%
<b>LSE</b>			
Closing price for ADR <sup>(1)</sup> , USD			
Year end	9.46	10.66	-11.3%
Minimum	8.70	8.74	-0.5%
Maximum	13.53	17.40	-22.2%
Average daily trading volume, million shares	32.1	43.9	-26.9%
Average daily trading volume, USD million	340,6	577,3	-41,0%

Note:

- (1) Before April 2011 onwards 1 ADR provided a right for 4 ordinary shares of OAO Gazprom. Since April 2011 onwards 1 ADR provides a right for 2 ordinary shares of OAO Gazprom. The 2010 comparatives have been restated accordingly.

As of 31 December 2012 market capitalization of OAO Gazprom totaled USD 111.6 billion decreasing by 9% during 2012. In 2012 the average market capitalization of OAO Gazprom decreased by 20% as compared to 2011 and totaled USD 124.2 billion.

Dividends paid in 2012 based on OAO Gazprom performance results for 2011 as of 31 December 2012 are as follows:

	<b>As of 31 December 2012</b>			
	<b>Accrued, RUB thousand</b>	<b>Paid, RUB thousand</b>	<b>Unpaid dividends, RUB thousand<sup>(1)</sup></b>	<b>Proportion of unpaid and accrued dividends</b>
Total	212,351,411	212,156,122	195,289	0.09%
including dividends on shares:				
owned by the state	81,485,926	81,485,926	-	-
owned by state-controlled legal entities: OAO Rosneftegaz and OAO Rosgazifikatsiya	24,693,590	24,693,590	-	-
owned by individuals and legal entities (apart from state- controlled)	106,166,520	105,976,606	189,914	0.18%
owned by undefined holders	5,375	-	5,375	100%

Note:

- (1) Dividends are not paid to shareholders (legal entities and individuals) that did not provide data required for dividend payments as per para 5, Art. 44 of Federal Law No. 208-FZ "On Joint Stock Companies" dated 26 December, 1995. Dividends accrued on shares of undefined holders shall be paid upon establishment of the shareholders' rights for securities.

## MANAGEMENT STRUCTURE OF OAO GAZPROM

The rights of OAO Gazprom shareholders and regulation of OAO Gazprom management activity are determined by and carried out in accordance with the legislation of the Russian Federation and may differ from the regulating practice in companies registered in Great Britain. In accordance with the Federal Law "On Joint Stock Companies" and OAO Gazprom's Charter, OAO Gazprom's operations are governed by OAO Gazprom's General Meeting of Shareholders, Board of Directors, Management Committee and the Chairman of Management Committee. The General Meeting of Shareholders is OAO Gazprom's top governing body and, among other things, elects OAO Gazprom's Board of Directors. The Board of Directors exercises general governance of the OAO Gazprom's activities, with the exception of decisions on the issues that in compliance with the Federal Law "On Joint-Stock Companies" pertain to the authority of the General Shareholders Meeting. The Management Committee Chairman is the sole executive body and the Management Committee is the collective executive body. The Management Committee and the Management Committee Chairman are responsible for day-to-day management of the activities in such a way that ensures both payments of dividends to the shareholders and development opportunities for OAO Gazprom. In order to achieve these goals the executive bodies primarily solve problems related to realization of goals, strategy, policy of OAO Gazprom and implement the decisions of the Board of Directors and the Annual shareholders meeting faithfully, efficiently and on time.

### Board of Directors and Management Committee

Information on members of the Board of Directors as of 31 December 2012:

Name	Year of Birth	Position
Viktor A. Zubkov	1941	Chairman of OAO Gazprom's Board of Directors Russian Special Presidential Representative for Cooperation with Gas Exporting Countries Forum, Management Committee Chairman of OOO Gazprom gazomotornoe toplivo
Alexey B. Miller	1962	Deputy Chairman of OAO Gazprom's Board of Directors and Chairman of OAO Gazprom's Management Committee
Andrey I. Akimov	1953	Chairman of OAO Gazprombank's Management Committee (open joint stock company)
Farit R. Gazizullin	1946	Member of OAO Gazprom's Board of Directors
Elena E. Karpel	1944	Head of the Economic Appraisal and Pricing Department of OAO Gazprom
Timur A. Kulibayev	1966	Chairman of the Presidium of the Legal Entities Association National Economic Chamber of Kazakhstan (Atameken Union)
Vitaly A. Markelov	1963	Deputy Chairman of OAO Gazprom's Management Committee
Vladimir A. Mau	1959	Rector of the Russian Presidential Academy of National Economy and Public Administration
Valery A. Musin	1939	Head of Department for Civil Process of Legal Faculty, St. Petersburg State University, senior partner of the Russian-British company Musin & partners
Mikhail L. Sereda	1970	Deputy Chairman of OAO Gazprom's Management Committee and Head of Administration of OAO Gazprom's Management Committee
Igor H. Yusufov	1956	Member of OAO Gazprom's Board of Directors

## Changes in the Board of Directors:

Name	Changes
Vitaly A. Markelov	elected on 29 June 2012
Alexander G. Ananenko	termination of powers on 29 June 2012

In 2012, 87 sessions of the Board of Directors of OAO Gazprom (12 – in person, 75 - vote in absentia) were held, 197 decisions were made (47- in person, 150 – vote in absentia).

Name of a member of the Board of Directors	Participation in the Board of Directors meetings <i>(out of the total number of meetings a member of the Board of Directors could participate)</i>
Andrey I. Akimov	49 out of 87
Alexander G. Ananenko <sup>(1)</sup>	37 out of 51
Farit R. Gazizullin	86 out of 87
Viktor A. Zubkov	87 out of 87
Elena E. Karpel	85 out of 87
Timur A. Kulibayev	85 out of 87
Vitaly A. Markelov <sup>(2)</sup>	35 out of 36
Vladimir A. Mau	86 out of 87
Alexey B. Miller	82 out of 87
Valery A. Musin	85 out of 87
Mikhail L. Sereda	83 out of 87
Igor H. Yusufov	87 out of 87

Note:

(1) Ananenko was a member of the Board of Directors of OAO Gazprom till 29 June 2012.

(2) Markelov has been a member of the Board of Directors of OAO Gazprom since 29 June 2012.

## Information on members of the Management Committee as of 31 December 2012:

Name	Year of Birth	Position
Alexey B. Miller	1962	Chairman of OAO Gazprom's Management Committee
Elena A. Vasilieva	1959	Deputy Chairman of OAO Gazprom's Management Committee and OAO Gazprom's Chief Accountant
Valery A. Golubev	1952	Deputy Chairman of OAO Gazprom's Management Committee
Alexander N. Kozlov	1952	Deputy Chairman of OAO Gazprom's Management Committee
Andrey V. Kruglov	1969	Deputy Chairman of OAO Gazprom's Management Committee and Head of the Finance and Economics Department of OAO Gazprom
Vitaly A. Markelov	1963	Deputy Chairman of OAO Gazprom's Management Committee
Alexander I. Medvedev	1955	Deputy Chairman of OAO Gazprom's Management Committee and General Director of OOO Gazprom Export
Sergei F. Khomyakov	1953	Deputy Chairman of OAO Gazprom's Management Committee and General Director of OAO Gazprom's Corporate Security Service Branch in Moscow
Oleg E. Aksyutin	1967	Head of the Gas Transportation, Underground Storage and Utilization Department of OAO Gazprom
Yaroslav Ya. Golko	1961	Head of the Department of Investment and Construction of OAO Gazprom

<b>Name</b>	<b>Year of Birth</b>	<b>Position</b>
Nikolay N. Dubik	1971	Head of the Legal Department of OAO Gazprom
Vladimir K. Markov	1955	Head of the Department for Relations with the Russian Federation Authorities of OAO Gazprom
Elena V. Mikhailova	1977	Head of the Asset Management and Corporate Relations Department of OAO Gazprom
Vlada V. Rusakova	1953	Member of the Management Committee of OAO Gazprom
Kirill G. Seleznev	1974	Head of the Gas and Liquid Hydrocarbons Processing and Marketing Department of OAO Gazprom and General Director of OOO Gazprom mezhregiongaz
Igor Y. Fedorov	1965	General Director of OOO Gazprom komplektatsiya
Vsevolod V. Cherepanov	1966	Head of the Gas, Gas Condensate and Oil Production Department of OAO Gazprom

#### Changes in the Management Committee:

<b>Name</b>	<b>Changes</b>
Vitaly A. Markelov	elected on 23 January 2012
Vladimir K. Markov	elected on 23 January 2012
Elena V. Mikhailova	elected on 23 January 2012
Victor V. Ilyushin	termination of powers on 23 January 2012
Olga P. Pavlova	termination of powers on 23 January 2012

#### Remuneration of the members of the Board of Directors and Management Committee

Key management personnel (the members of the Board of Directors and Management Committee of OAO Gazprom) short-term compensation, including salary, bonuses and remuneration for serving on the management bodies of Group companies, amounted to approximately RUB 2,130 million and RUB 1,795 million for the years ended 31 December 2012 and 2011 respectively. Such amounts include personal income tax and Insurance contributions to non-budget funds. Government officials, who are directors, do not receive remuneration from the Group. The remuneration for serving on the Boards of Directors of Group companies is subject to approval by the General Meeting of Shareholders of each Group company. Compensation of key management personnel (other than remuneration for serving as directors of Group companies) is determined by the terms of the employment contracts. Key management personnel also receive certain short-term benefits related to healthcare.

According to Russian legislation, the Group makes contributions to the Russian Federation State pension fund for all of its employees including key management personnel. Key management personnel also participate in certain post-retirement benefit programs. The programs include pension benefits provided by the non-governmental pension fund, NPF Gazfund, and a one-time payment from the Group at their retirement date. The employees of the majority of the Group companies are eligible for such benefits after retirement.

The Group provided medical insurance and liability insurance for key management personnel.

#### Liability insurance for the members of the Board of Directors and Management Committee.

Within the framework of insurance coverage the Gazprom Group provides the liability insurance for the members of the Board of Directors (including independent directors but excluding those who are state officials) and Management Committee that ensures the compensation of damage to

the shareholders, creditors and other persons incurred as a result of indeliberate erroneous actions (failure to act) of the insured persons when performing management functions.

Liability insurance for key personnel is a generally accepted practice for international companies which can face extraordinary expenses due to third parties' claims, court proceedings that in their turn can have an adverse impact on the financial performance indicators, damage the company's business reputation and image.

Relevance of the above insurance for OAO Gazprom is associated with the existing probability of claims that can be made against OAO Gazprom, members of the Board of Directors and Management Committee under the conditions of increasing integration of the company into the global economy, liberalization of OAO Gazprom stock market, existence of ADR program, changes in the Russian and international laws and corporate governance. Insurance contract with a single limit of insurer's liability provides for insurance coverage of risks associated with the following:

- risk of the third parties' claims against members of the Board of Directors and Management Board for compensation of losses as a result of indeliberate erroneous actions (failure to act) of the insured persons when performing management functions.
- risk of the third parties' claims against OAO Gazprom for compensation of losses as a result of indeliberate erroneous actions of members of the Board of Directors and Management Board when performing management functions.

The insurance contract provides for a single limit of insurer's liability that consists of two parts. The first part provides for insurance under applicable law other than the law of the Russian Federation, extends its validity on a global level and provides for the most favorable conditions for OAO Gazprom and members of the Board of Directors and Management Board; the second part provides for insurance that complies with the law of the Russian Federation and is maximally close (to the extent it is possible under the Russian legal framework) to the insurance terms of the first part.

Based on risk appraisal made by western reinsurers for OAO Gazprom the premium under the insurance contract concluded in 2012, was maintained at the 2011 level and amounted to USD 1.57 million at insured amount of USD 100 million.

Insurance coverage under the liability insurance contract for the members of the Board of Directors and Management Committee of OAO Gazprom complies with the international standards of insurance in terms of the insured risks and indemnity limits.

#### Shares of the members of the Board of Directors and the Management Committee

As of 31 December 2012 the total share of the members of the Board of Directors and the Management Committee in OAO Gazprom equity was 0.01003325%.

#### Corporate governance

Basic corporate governance principles are set out in the Corporate Governance (Conduct) Charter of OAO Gazprom approved by the General Shareholders' Meeting of OAO Gazprom on 28 June 2002 and comply with the generally accepted global standards.

Corporate governance of the Company is primarily aimed at strict observance of rights of all shareholders of OAO Gazprom. The key documents of OAO Gazprom related to corporate governance are based on fair treatment of shareholders, protection of their rights and interests irrespective the number of shares owned.

The key documents of OAO Gazprom that ensure observance of the shareholders' rights include:

- Charter of OAO Gazprom;
- Regulation on OAO Gazprom's General Meeting of Shareholders;

- Regulation on OAO Gazprom's Board of Directors;
- Regulation on OAO Gazprom's Management Committee;
- Regulation on the Chairman of OAO Gazprom's Management Committee;
- Regulation on OAO Gazprom's Audit Commission;
- Corporate Governance (Conduct) Charter of OAO Gazprom;
- OAO Gazprom's dividend policy;
- Procedure for documenting the shareholders' proposals and requirements related to the calling of OAO Gazprom's General Meeting of Shareholders;
- OAO Gazprom's regulation on information disclosures;
- Procedure for informing shareholders on OAO Gazprom;
- Code of Corporate Ethics of OAO Gazprom.

All the above documents and OAO Gazprom's Charter can be found on OAO Gazprom's official web-site [www.gazprom.ru](http://www.gazprom.ru) or in the shareholders' affairs division the contacts of which are included in the Addresses and Contacts section of the Report.

OAO Gazprom makes on-going efforts to improve its corporate governance. During the reporting year the significant changes that were highly appreciated by shareholders and investment professionals were implemented:

- The Corporate Governance (Conduct) Charter of OAO Gazprom was adopted based on the Board of Directors' decision of 30 July 2012, No2038; it is being implemented in the Group's subsidiaries and associates. The Corporate Governance (Conduct) Charter confirms the company's corporate values, provides for the course of actions applied in conflict of interests and announces intolerance to corruption conduct. To minimize the conflict of interests the Corporate Governance (Conduct) Charter specifies limitations including those related to joint work of relatives, employees' participation interest in competitors, elective state bodies, acceptance of gifts, use of the Company's resources by employees including property and information for personal purposes. The Corporate Governance (Conduct) Charter is mandatory for OAO Gazprom and its controlled legal entities; for legal entities with the participation of OAO Gazprom but which are not controlled by OAO Gazprom the Corporate Governance (Conduct) Charter is recommended for observance.
- The procedure for accessing the insider information and its confidentiality protection rules were approved. Measures aimed at protecting the insider information will ensure the control over information which has impact on the cost of OAO Gazprom securities.
- Regarding the preparation for OAO Gazprom's General Meeting of Shareholders the period of providing shareholders with the materials for the General Meeting of Shareholders was extended - from 20 days to 30 days. It will allow time for the shareholders to take the balanced decisions on the issues brought up for vote.
- The corporate Report on the activities related to sustainable development experienced fundamental changes: its coverage was extended by oil and electric power segments of business. In November 2012, the Board of Directors of OAO Gazprom approved the Company's non-financial reporting practice and entrusted the Management Board with ensuring the publication of corporate reports on sustainable development activities on an ongoing basis.
- The Company's key documents that ensure the observance of the shareholders' rights were translated into English and placed on OAO Gazprom web-site ([www.gazprom.com](http://www.gazprom.com)).

In 2013, it is planned to approve the Regulation on the Corporate Ethics Commission of OAO Gazprom by the order of OAO Gazprom and implement the codes of corporate ethics in the Company's controlled legal entities, develop the procedure for dividends payments; the ability to use the IFRS consolidated profit of the Group as the basis for dividends calculation is being considered.

The activities related to cooperation with shareholders and investors, the planning system based on strategic target values and optimization of asset ownership structure will be further continued.

#### Internal controls system

The internal control system in place in OAO Gazprom is a combination of internal control bodies and internal control procedures (methods), standards of employees' conduct and actions to achieve the Company's goals. Internal control system is an important component of the shareholders and investors' interests protection.

Objectives, tasks and components of internal control system, principle of its operation and OAO Gazprom governing bodies and persons responsible for internal control are specified in the Regulation on internal control system of OAO Gazprom approved by the Board of Directors' decision of 14 December 2012, No.2091 instead of the document version effective since 2009. The Regulation was developed in accordance with the Russian legislation, recommendations of the Federal Securities Commission's Code, Charter and internal regulatory document of OAO Gazprom considering the international standards of internal control and audit. Reference to the above international standards was included in a new version of the document for the first time.

For achieving the stated objective the internal control system was appropriately structured.

The Revision Commission in number of 9 persons is elected by the General Meeting of Shareholders. The competence of Revision Commission is specified by the Federal law "On joint-stock companies"; for the issues not specified by the law – by the Charter of OAO Gazprom.

Information on the persons elected to the Revision Commission at the General Meeting of Shareholders on 29 June 2012:

<b>Name</b>	<b>Year of Birth</b>	<b>Position as of 31 December 2012</b>
Mariya G. Tikhonova	1980	Chairman of the Audit Revision
Vadim K. Bikulov	1957	Head of Division of the Internal Audit Department of OAO Gazprom's Management Committee Administration, secretary of Revision Commission
Dmitry A. Arkhipov	1975	First Deputy Head of Management Committee Administration, Head of Internal Audit Department of OAO Gazprom
Alexei B. Mironov	1976	Head of Division for Innovative Corporate Technology and Industrial Complex Entities of the Federal Agency for State Property Management
Anna B. Nesterova	1982	Director in Charge of Property Department in the Russian Ministry for Economic Development
Georgy A. Nozadze	1979	Referent of the Presidential Experts Directorate in the Russian Federation
Yury S. Nosov	1963	Deputy Head of Management Committee Administration, Head of OAO Gazprom's Affairs Department
Karen I. Oganyan	1974	Head of Tax policy Department of OAO Gazprom
Alexander S. Yugov	1981	Head of Division for Infrastructure and Military Industrial Complex Entities of the Federal Agency for State Property Management

In 2012, the Audit Committee of Board of Directors of OAO Gazprom continued its activities.

The Audit Committee reports to the Board of Directors of OAO Gazprom and acts within the powers defined by the Regulation on the Audit Committee of the Board of Directors of OAO Gazprom approved by the Board of Directors' decision of 14 March 2006, No.819.

In 2012, the Audit Committee of the Board of Directors of OAO Gazprom included three members of the Board of Directors of OAO Gazprom: F.R. Gazizullin, V.A. Musin, M.L. Sereda.

V.A. Musin is the Chairman of the Audit Committee of the Board of Directors of OAO Gazprom.

During the reporting year the Audit Committee of the Board of Directors of OAO Gazprom held 4 meetings at which 9 issues were considered.

The Internal Audit Department carries out its activity in accordance with the International professional standards of internal audit.

The Department administratively reports to the Chairman of the Management Board of OAO Gazprom within Management Committee Administration and functionally – to the Audit Committee of Board of Directors. One of the key tasks of the Internal Audit Department is providing OAO Gazprom management with the information and proposals on improving the Company's operations based on the results of internal audits of OAO Gazprom business subdivisions and subsidiaries.

During 2012, the Internal Audit Department performed the audits of subsidiaries and organisations, business subdivisions of OAO Gazprom aimed at identifying risks and assessing the efficiency of significant business lines and business processes.

The results of the audits performed are quickly and efficiently communicated to the Chairman of the Management Board and on an annual basis - to the Management Board and the Audit Committee of the Board of Directors. The proposals aimed at improving the operations of OAO Gazprom and under which the Chairman of the Management Board entrusts business subdivisions, subsidiaries and organisations of OAO Gazprom with tasks are prepared based on the audit results. Internal Audit Department monitors the performance results.

On an annual basis OAO Gazprom selects its auditor based on the open tender results that is held in accordance with the Russian legislation. The Company's Board of Directors specifies the auditor's fees.

In 2012, ZAO PricewaterhouseCoopers was recognised as a winner of the open tender and was approved as the auditor at the General Meeting of Shareholders of OAO Gazprom on 29 June 2012.

The independence policy pursued by ZAO PricewaterhouseCoopers Audit provides for:

- use of independence monitoring system which includes annual independence confirmations from the auditor's employees;
- prohibition for all employees of the auditor to have any financial relationships with the audit clients;
- monitoring the existence of the employees' personal or family relationships with the management of the Gazprom Group at any level of its organizational structure.

## **RISK MANAGEMENT**

### **Development of risk management system**

Risk management within the framework of the unified corporate system is defined as continuous cycle of making and implementing management decisions about risks identification, risk response, control of efficiency and planning of risk management and monitoring. This cycle is an integral part of the Group's general management system and focuses on risk optimization that serves OAO Gazprom's interests in all areas of the Group's operations.

The Company's development towards vertical integration and diversification of its operations and improvement of global corporate governance practice require the appropriate development of the corporate risk management system.

These activities are focused on building major risks management system and implemented in the Gazprom Group in accordance with the plan of actions approved by the Chairman of the Management Board of OAO Gazprom. In 2011- 2012, unified approaches to organizing OAO Gazprom risk management system were developed.

In 2013-2014, the activities on improving the risk management system will be continued. It is expected to develop a methodological base for organising risk management in OAO Gazprom, develop the schemes of the Company's interaction with subsidiaries, associates and jointly-controlled companies and prepare a package of fundamental documents on major risks management in these companies. Draft normative documents are expected to be considered and approved at the level of executive management bodies of OAO Gazprom.

### **Key risk factors**

#### Strategic and country-specific risks

##### **Risks relating to the global credit crunch developments**

Despite the recent positive trends, there is still a wide spread uncertainty about how and at what rate the world economy will recover from the deep global recession.

Unfavourable economic conditions may have an adverse impact on the Group's operations.

#### *Management / influence on the risk level*

Gazprom pursues the policy that ensures financial stability, improvement of financial position and optimisation of debt portfolio that will enable to respond adequately if macroeconomic situation worsens.

##### **Risks relating to operations in the European gas market**

Gazprom is the largest natural gas supplier in Europe. EU countries are actively pursuing the policy of gas market liberalization that contributes in the competition and increase in spot sales. The aforementioned liberalization can entail the partial refusal from a long-term contract system.

Liberalization policy also provides for separation of gas production assets from transportation networks within EU. Lack of exemption from the above provision means that the Group is not able to own or exercise control over transport business that will impede the implementation of the investments projects in EU.

In addition, the EU energy sector strategy is focused on the diversification of sources of energy resources supplies, development of alternative energy sources.

Disparity of prices under long-term contracts and gas prices at spot markets represent a certain risk for Gazprom.

*Management / influence on the risk level*

Gazprom is maintaining the system of long-term contracts as the basis of its business which maximises its returns and provides guaranteed supplies to its customers. The Group is actively negotiating with its customers on finding mutually beneficial solutions depending on the market situation development. Refusal from the system of long-term contracts may disrupt the balance of demand and supply in the European gas market and result in unpredictable consequences, including threat to energy security of importing countries. For the purpose of diversifying its operations Gazprom considers the Asia-Pacific countries as key new markets.

**Risks associated with the development of renewable power sources**

A number of developed countries, firstly European countries pursue a policy of encouraging the use of renewable energy sources (wind power, solar power, biomass energy, distributed power generation, lower-grade heat) development including by means of the government grants for developing this industry.

Therefore, the above countries may experience growth of generating power from renewable sources that can result in displacing gas generation and reduction of gas consumption by major European customers.

*Management / influence on the risk level*

OAO Gazprom actively conducts an education campaign related to economic, technological and ecological advantages of gas use including for generating electricity. Generating electricity from renewable sources to ensure the reliability of supplies should be supplemented with its generation from other types of fuel having high requirements to maneuvering capabilities of equipment. From this viewpoint, natural gas is the most efficient type of fuel to support the generation of electricity from renewable energy sources.

At the same time, Gazprom continues implementing the projects aimed at diversification of types and areas of its activities.

**Risks of state regulation in the sector**

The Russian Federation controls 50.002% of OAO Gazprom's shares. The governmental representatives are the members of Gazprom's Board of Directors whose powers include the approval of the financial plan and the investment program; in this way the government exercises the control over financial flows of OAO Gazprom.

In accordance with the Federal Law "On natural monopolies" the Gazprom's gas transportation via pipelines is regulated as natural monopoly operations.

The government regulates the wholesale prices for gas which Gazprom applies to the major portion of domestic sales; tariffs for trunk pipeline transportation services provided to independent producers; tariffs for trunk pipeline transportation services via gas distribution networks; charges for procurement and sale services as well as retail prices for gas.

At the same time the government is interested in the Company's effective development because Gazprom is one of the largest Russian taxpayers and supplies a half of primary energy sources in the country.

*Management / influence on the risk level*

Gazprom's strategy is aimed at mutually beneficial cooperation with the government so as to ensure the energy security of the country and stable development of the company. The development strategy of OAO Gazprom has been designed and implemented in cooperation with governmental agencies and is an integral part of the Russian Energy Strategy.

In 2010, for improving the state's pricing policy in gas industry the Russian Government adopted the Resolution No1205 "On improving the state regulation of gas prices" under which the regulation of wholesale gas prices for industrial consumers in the mid-term perspective is based on the price formula that provides for a gradual achievement of equal profitability of gas supplies at export and domestic markets during the transition period considering the prices of alternative fuels sources. Timing of practical application of prices which provide for equal profitability of gas supplies on export and domestic markets will depend on the development of pricing environment on external gas markets and compliance with the dynamics of changes in the regulated prices for gas supplies on domestic market forecasted by the Russian Government.

OAo Gazprom is engaged in an active dialogue with the Russian Government with regard to improving its pricing policy.

### **Risks relating to natural gas transit**

Major volumes of natural gas sold in Europe transit FSU territories, in particular Ukraine, Belarus and Moldova. Gas transit through the territories of these countries is associated with a risk that they will fail to fulfill their transit obligations and this fact will result in the risks of inappropriate fulfillment of obligations by OAO Gazprom under the contracts for gas supplies to Europe.

#### *Management / influence on the risk level*

To mitigate its dependence on transit countries the Group:

- is gradually shifting to principles and procedures generally accepted in the global gas business for market pricing of gas imported by FSU and of related gas transit services;
- is implementing gas transportation projects aimed at diversification of export routes (the second thread of Nord Stream gas pipeline was put into operation; works under South Stream project are under way);
- is expanding the use of UGSF abroad;
- is developing the LNG trading.

### **Risks associated with entering new regions and new markets**

A key direction of the Gazprom Group's development strategy is the expansion of regions of its operations. Gazprom implements projects related to exploration and production of hydrocarbons in FSU countries, South America, South-East Asia, Africa and Middle East. Potential for entering gas markets of Asia, Africa, South and North America is being considered.

#### *Management / influence on the risk level*

Subsidiary undertakings and joint companies with foreign partners are established in the new regions for the purpose of obtaining the necessary business experience.

Gazprom's representative offices abroad are operating to enhance efficiency of Gazprom's interaction with governmental agencies, enterprises, companies and organizations of the respective countries and regions and provide information and analytical support to managing the international projects. As of 31 December 2012 twelve representative offices of OAO Gazprom are registered abroad, including Algeria, Belarus, Brazil, Iran, Kazakstan, Qatar, the People's Republic of China, Kyrgyzstan, Latvia, Moldova, Turkmenistan, and Ukraine.

### **Risks associated with the development of gas production from unconventional sources**

Higher prices of natural gas and the progress in science and technology in the last decades supported the increasing interest to unconventional resources of natural gas. In North American countries the share of gas produced from unconventional sources is expected to grow in the long-

term perspective. As a result, American gas market will be supplied with its own gas resources. The planned commencement of LNG production in the North America may result in increasing competition at global markets.

Projects on gas production from unconventional sources being implemented in various countries, in particular in China, may decrease the demand in imported gas in these countries.

*Management / influence on the risk level*

To support competitiveness of natural gas production and supply by applying the traditional methods, Gazprom:

- controls investment and running costs of production;
- improves and implements new technologies that enhance efficiency of traditional gas production.

Russia has large unconventional gas reserves and Gazprom develops technologies of their development.

At the same time perspectives of unconventional gas production are still uncertain as such a production is economically viable only when prices are consistently high and continued investments are required to maintain the formation productivity and it is also associated with significant environmental risks.

**Geographical and climatic risks**

Climate specifics and geographical location of principal regions where Gazprom operates significantly impact the Group's performance. Gazprom's production in West Siberia accounts for a substantial portion of the overall natural gas production and it is characterized by challenging environmental conditions and high costs. The fields in the Yamal Peninsula and resources of the Russian continental shelf will be developed in even more harsh climates.

Gazprom's gas sales and revenues may be affected by climatic conditions of short-term nature. Due to warm winters of recent years gas sales to Europe were decreasing. However, the influence of this factor of a probabilistic nature on Gazprom's gas sale volumes and revenues for the last several years is not significant as the alteration of cold and warm winters compensate the impact.

*Management / influence on the risk level*

The Group successfully implements the efficient technological processes developed for harsh climate conditions. The Group also develops and implements programs of improving efficiency of gas production and transportation, including efficiency of gas transportation network.

The Group also actively participates in the development and implementation of governmental programs aimed at improving the use of energy resources in Russia.

Risks relating to customs, foreign currency and tax regulation

**Risks associated with the changes in currency regulation and tax legislation in the Russian Federation**

Gazprom is involved in international transactions, it has foreign currency denominated assets and liabilities and foreign currency accounts opened with foreign banks. At the background of ongoing liberalization of foreign currency legislation, the Russian Government and Central Bank of Russia undertook measures to increase control over transactions denominated in foreign currency.

Tax legislation is the most flexible area of law which is often modified, supplemented and updated.

### **Significant changes in tax legislation in 2012**

- establishment of the consolidated taxpayers' group (from 1 January 2012);
- amendments to the Russian transfer pricing legislation which entitles taxpayers to justify their compliance with the arm's-length price rules as applied to controlled transactions through the preparation of documents to be used for tax control purposes (from 1 January 2012);
- increase in Mineral Extraction Tax rates as applied to natural gas from all types of hydrocarbon fields (from 1 January 2012 and from 1 January 2013) and gas condensate (from 1 January 2013);
- adding coal methane to the list of produced mineral resources for MET purposes and its recognition as an item not subjected to this tax (from 1 January 2013);
- cancellation of the property tax benefit for entities with gradual increase of maximum tax rates applied to trunk grid pipelines, power transmission lines and buildings being their integral technological part (from 1 January 2013).

During the reporting period, the Russian Government started considering a potential formula to calculate MET rates applied to natural gas. There is still a risk that MET payments for OAO Gazprom will increase from 2016. Given OAO Gazprom's responsibility to secure gas supplies as well as construction, operation, renovation and development of the Unified Gas Supply System, further growth of the fiscal burden can significantly impact OAO Gazprom's income and sources of financing capital expenditure, as well as overall security of gas supplies.

In addition, changes in regulatory framework related to pricing for tax purposes may result in additional risks associated with application of internal settlement prices between OAO Gazprom and the Gazprom Group's entities.

#### *Management / influence on the risk level*

OAO Gazprom activities are based on the principles of integrity and openness of information for tax authorities. Gazprom monitors changes in currency and tax legislation and makes every effort to comply with the requirements following the best law application practice and is also focused on mutually beneficial cooperation with the government so as to ensure the energy security of the country and stable development of the Group.

Building the effective tax risk management system in Gazprom Group as a whole is one of the key objectives for medium-term period. Centralised database in place and permanent monitoring of crucial risks in the Group's entities will enable to identify them timely at an early stage and minimize their adverse impact in advance.

In order to minimize tax risks associated with transfer pricing Gazprom Group established a consolidated group of taxpayers in 2013, where OAO Gazprom acts as a responsible participant, and has been implementing internal control procedures to ensure compliance with transfer pricing law.

To restrict further increase in MET rate OAO Gazprom continues to cooperate with governmental agencies to maintain the balance between fiscal burden and necessity of significant investments in the nearest future to ensure reliable gas supplies. In addition, in order to create the conditions for engaging complex field in remote locations, OAO Gazprom has prepared and sent to the Russian Federation Government economically feasible propositions to differentiate MET on natural gas with account of economic and geographic factors, the degree of reserves depletion, depth of formation and blend composition of natural gas.

## **Risks relating to changes in rules of customs control and payments in the Russian Federation**

Operations of the Group relating to export of hydrocarbons are subject to customs regulations. Some of key issues relating to export supply of natural gas are disputed by the Group and the customs agencies, in particular, approach to the procedure for paying export customs duty and its return, including the return arising out of customs value adjustment due to changes in the retroactive procedure of price parameters of the natural gas supplied to counterparties. A number of disputes were challenged by OAO Gazprom/OOO Gazprom Export in court. The actions of customs agencies were invalidated.

Due to the current practice of customs value adjustments due to the retroactive recalculation of the price of sold gas, which was supported by a number of positive court decisions in favour of OAO Gazprom, the necessity to recover excess amounts of paid export customs duty which covers a third of losses on recalculation was almost entirely eliminated. At the same time, tax authorities interpret this as a negative fact for the federal budget, and once again suggest replacing the ad valorem export customs duty for natural gas with the specific rate. OAO Gazprom believes that there are insufficient grounds for such changes.

Overall, the current procedure for the payment of the customs duty on exported natural gas before the transportation based on estimated supplies parameters has a risk of unpredictability related to the export customs duty to be paid upon supplies.

### *Management / influence on the risk level*

The Group makes every effort to comply with the customs legislation requirements, control and propose the respective amendments to the current customs clearance considering the gas industry interests; interacts with regulators regarding disputable issues, including the Russian Government.

As a result of performed work OAO Gazprom's argument against the specific export customs duty on natural gas were accepted by the Russian Ministry of Energy and Ministry of Economic Development which confirmed that the current procedure for calculating the export duty promotes flexible natural gas supplies, stable share of Russian gas in global markets and guaranteed stable proceeds from customs payment into the federal budget.

At the same time, there are certain complexities around the customs duty payment procedure which result from the necessity to pay it before actual supplies based on estimated price and volumes. As a result, it is necessary to continue the joint work with federal authorities aimed at the development of amendments to the Federal Law "On Customs Regulation in the Russian Federation" of 27 November 2010 to improve the customs duty payment procedure.

### Financial risks

#### **Foreign exchange risks, interest rate and inflation risks**

Gazprom's sales revenue is largely denominated in US dollars and Euro, while most of the costs are denominated in rubles.

A part of OAO Gazprom debt portfolio is represented by syndicated loans from Western banks. The interest rate on many of these loans is based on LIBOR/EURIBOR rates.

Therefore, changes in inflation rates and exchange rates significantly affect the Group's performance results.

### *Management / influence on the risk level*

OAO Gazprom is developing a methodology and contractual base for using hedging instruments in accordance with the requirements of the Russian legislation. Regulation on tax accounting

policies of OAO Gazprom for 2011 includes provisions related to tax accounting for transactions with financial instruments of forward-type deals (FIFD) including hedging currency and other risks. Natural hedging of risks associated with market changes in the foreign exchange rates and interest-bearing payments by:

- calculating net currency position of the Gazprom Group and balancing the cash flows of OAO Gazprom in terms of currency, volumes and period of receipt/payment;
- maintaining the currency balance in OAO Gazprom debt portfolio similar to the proportion of currency in revenue.

### **Credit and liquidity risks**

Untimely or partial fulfillment by some counterparties of their contractual obligations to the Company may have an adverse impact on Gazprom operations. In particular, the increase in gas prices in FSU with low solvency of final customers in the region entails a risk of partial and/or untimely payments under the contracts for the gas supplied.

Foreign counterparties' failure to perform their payment obligations for the gas supplied may result in a risk of bringing OAO Gazprom to administrative responsibility by the Russian currency regulation authorities for breaching currency legislation.

#### *Management / influence on the risk level*

The Group pursues a transparent policy requiring fulfillment of contractual obligations regarding payments for supplies and non-payers.

All counterparties engaged in gas supplies to far abroad countries are assigned with an internal credit rating (according to the adopted methodology of credit risks assessments). Based on assessment of the counterparties' creditworthiness and Monte Carlo modelling the credit risks are quantitatively assessed by applying CreditVaR method.

The basic tools to manage credit risks associated with gas supplies to far abroad countries include preparation of a list of authorized counterparties, with which the deals can be concluded and the requirement to provide the guarantees from the counterparties with low credit rating. The Group monitors the changes in the internal credit ratings of these counterparties on a daily basis and if they significantly decline, the respective contracts may be amended to mitigate non-payment risks.

The Gazprom Group cooperates with credit institutions based on credit risk limits established on a regular basis.

### **Market risks including risks associated with decrease in volumes and cost of gas sold at foreign markets**

Export sales of gas generate a major portion of the Group's revenue. Gas is exported under long-term contracts at prices linked to the world prices for major core products (oil products, coal, gas). Therefore, there arise risks of failure to receive the planned revenue (export price of commercial gas) or adverse change in the portfolio cost due to market factors effects. Price risks associated with fluctuations of prices for oil products and gas indices which are the basis for prices calculation under export contracts and risks of volume associated with the fact that the buyers are provided with certain flexibility in gas withdrawal are the basic factors of market risk.

The potential decrease in oil prices including due to the potential reduced volumes of oil imported by the United States because of development of own hydrocarbons production from unconventional sources also may result in the reduced revenues of OAO Gazprom.

The decrease in oil and oil products prices will result in improving the competitiveness of the Russian gas sold at export market under the contracts linked to oil prices that may increase the demand for gas in future.

Due to existence of contracts denominated in different payment currencies (mainly, US dollars and Euro) the currency risks associated with the adverse changes in exchange rates will also have impact on revenues.

*Management / influence on the risk level*

Price and volume risks represent key risks for OAO Gazprom.

The key method applied for quantitative assessment of price risks associated with gas sales to far abroad countries is Earnings at Risk (EaR) assessment that allows calculating the potential revenue deviation at a specific planning stage. For these purposes the probable scenarios of the portfolio are modelled considering the current contractual conditions and history of changes in risk factors related to prices, volumes and currency.

For considering new market risk factors and changes in the existing risk factors behaviour the methodology of risk assessment is improved.

The Group is taking measures to mitigate these risks, namely:

- As the pricing policy that is pursued by the state and aimed at transferring from the regulating the wholesale gas prices to the regulating the gas transportation tariffs improves, a share in the revenue from Gazprom supplies at the domestic market will increase mitigating the effects of export sales risks.
- Gazprom is entering new markets, including Asian-Pacific Region, LNG global market that will enable to mitigate the volume risk and, partially price risk.
- For the purposes of internal optimization the changes in the contractual conditions or conclusion of new contracts, identification of the affirmatively authorized deals and financial instruments and accordingly, counterparties with which these deals can be concluded, represent the main tool of the internal optimization. Currently, a major part of long-term contracts include “take-or-pay” conditions, which stipulate an advance payment against gas supply in subsequent period, even if the gas is not taken in the current year.

In addition, predominantly diverging trends in movements of prices for oil, oil products and Russian rouble exchange rate partially provide for natural hedging of Gazprom currency revenue denominated in roubles.

Operating risks

**Risks relating to non-extension of subsoil licenses**

The Group operates in compliance with subsoil licenses for exploration and production of hydrocarbons. Most licenses provide for an opportunity to suspend, amend or withdraw them if the requirements of license agreements are not complied with.

Licenses for production at major Group fields cover the period to 2012-2028. The Russian legislation provides for an opportunity to extend the licenses but do not provide the license holder with vested right of extension.

*Management / influence on the risk level*

Gazprom satisfies license requirements and takes all required steps to minimize the probability of license withdrawal, suspension or amendment.

### **Cost escalation risks**

During the pre-crisis years growth rates related to unit costs of capital construction in petroleum industry exceeded the inflation rates due to increase in prices of raw materials, component parts, services including prices of metals, gas-compressor plants, drilling costs, etc.

During the global crisis the costs of some items stabilized or even decreased but, as before, there is a probability of outrunning growth of costs in prospect.

*Management / influence on the risk level*

Gazprom organizes tenders to select suppliers and directly works with its suppliers.

### **Risks relating to exploitation of operating facilities**

AO Gazprom upstream, midstream and downstream operations are exposed to a wide range of technological, technical and natural and climatic character risks and risks associated with negative actions of personnel and third parties, including risks of employees' errors, thefts, terrorist attacks, subversive activities.

The above risks may have an adverse impact on the property interests of Gazprom Group and entail the decrease in production and economic indicators of Gazprom operations.

At that, liquidation of effects of natural and technogenic accidents and other adverse events requires significant financial costs.

When implementing the investment programs the priority is providing guarantees of completing the construction (reconstruction) of investee which, among other issues, is associated with the construction and assembly risks characterized by a high damage level.

*Management / influence on the risk level*

The unified gas supply system ensures the system reliability of gas supplies assuming that in case of a failure at one of its sections gas can be supplied via other routes by means of technological and intersystem shunt pipes.

Stability of the system operation is ensured by implementation of the advanced diagnostic technique, reconstruction and upgrading.

AO Gazprom has developed, approved and is implementing the policy on HSEA aimed at ensuring occupational safety, life and health safety of AO Gazprom's and its subsidiaries' employees and operational reliability of hazardous production facilities.

To ensure the sustainable operations of AO Gazprom and its subsidiaries and minimize the financial resources directed to mitigation of consequences resulting from natural and technogenic accidents and other unfavorable events (including terrorist attacks, subversive activities) the Group arranges a complex insurance coverage of the Group's companies including property insurance program (including off-shore facilities), insurance against production breaks at gas processing plants, insurance of hazardous facility operator's liability.

### **Risks associated with assessment of hydrocarbon reserves**

The Group's development plans are based on the amount and location of hydrocarbon reserves that are assessed in accordance with scientifically grounded and generally accepted standards.

Accuracy of reserves assessments depends on the quality of available information and technological and geological interpretation.

At the same time the regions where a significant part of the Group's reserves are located, are well explored that reduce these risks.

*Management / influence on the risk level*

The results of the Gazprom Group reserves assessment in accordance with the Russian classification of reserves are recorded on the balance sheet after annual consideration and approval by the State Reserves Commission.

OAo Gazprom has developed and is implementing the procedures for reserves assessment in accordance with international standards PRMS engaging an independent appraiser.

The accuracy of reserves assessment is based on a unique experience accumulated by Gazprom over many years of activities in this sphere.

### **Risks associated with vertical integration and diversification of operations**

Over recent years Gazprom significantly expanded oil business through acquisition of OAO Gazprom Neft, joined electricity generation and sales business. The Company also expands its activities on foreign markets of natural gas by applying new form of trading, develops business related to LNG production and sales.

Any failure in integration of past or future acquisitions may have an adverse impact on the Group's business, financial position and performance results.

#### *Management / influence on the risk level*

The Group improves the internal corporate governance structure for the purposes of breaking down the financial flows by types of activities and enhancing the efficiency of Gazprom as a vertically integrated company.

The Group also performs actions to bring the organizational structures of its subsidiaries engaged in gas production, transportation and processing into compliance with the corporate requirements of OAO Gazprom including the adopted standards of personnel number and corporate span of control.

The effective management procedures and projects on enhancing the efficiency of OAO Gazprom and its subsidiaries operations management, which are currently being implemented by the Group will also cover the Group's entities that exercise a significant influence on the Gazprom's performance results.

Gazprom has successfully developed, approved and is implementing the strategies in electric power and oil businesses aimed at increasing Gazprom's market value and establishing itself as a leader in electric power and oil businesses.

In accordance with the strategy on information system development the Group takes actions to create a unified information space. The above-noted work will enable to improve the transparency of corporate reporting preparation from the primary data sources to key performance indicators and risks.

### **Risks relating to registration of title to real estate and land plots of OAO Gazprom**

Under constant increase in property and land resources of OAO Gazprom the company may experience the claims made by the third parties, if the title to these assets is incorrectly or untimely registered.

Lack of registered title to the real estate items and land plots can have an adverse impact on attracting the investments in oil and gas industry.

Intensive development of town-planning activities in the Russian Federation regions identified the necessity to minimize the risk of violating the protected zones of UGSS and power supply network.

#### *Management / influence on the risk level*

The Gazprom Group is intensively and timely working over registering the title both to the land plots used to locate the production capacities and real estate items.

The Group is extensively applying all possible legal methods to defend the Group's interests including applications to the court regarding the confirmation and subsequent registration of title to the real estate items and land plots.

The Gazprom Group is extensively working over prevention and elimination of the protected zones violations by preparing the maps (plans) of protective zones and including the information about these protected zones in the State Immovable Property Cadastre.

OAo Gazprom also participates in the development of amendments to the civil legislation and draft laws regulating land relations. For these purpose the Company held the first international conference "Managing the corporations' real estate". Based on the conference results the resolution which initiates the creation of Corporate Owners' Club, an association aimed at formulating, structuring and promoting the interests of corporate owners related to real state management that will ensure an ongoing and efficient dialogue with government authorities and institutes for development, was approved.

### **Environmental risks**

The Gazprom Group production activity is associated with the use of natural resources and accordingly, involves a potential risk of environmental disruption.

Environmental damage or pollution may result in:

- legal consequence, including bringing to responsibility;
- finance costs associated with payments of fines and compensations of the incurred damage;
- damage to the business reputation.

#### *Management / influence on the risk level*

The Gazprom Group pursues a consistent environmental policy, implements programs and actions to reduce environmental effect, provides the financing for environmental activity, implements advanced resource-conservative and energy-conservative and other environmental protection technology.

Environmental Management System of OAO Gasprom was successfully certified for compliance with ISO 14001:2004. Gazprom Group continues improving its Environmental Management System. OAO Gasprom performs predesigned environmental researches, assessment of environmental effects of the planned operations, environmental assessments of projects. At all stages of construction, operation and decommissioning of assets the company exercises a control over compliance with legislation and corporate environmental standards. implements environmental monitoring, develops and implements environmental protection measures.

The key component of environmental risks management is the use of the best available technologies when designing, re-equipping and upgrading the production process.

Within the framework of comprehensive insurance coverage of the Group's entities the Group maintains liability insurance when constructing and operating dangerous production facilities that enables to compensate the damage incurred to environment and minimizes a risk of adverse financial consequences for the Group's subsidiaries. In 2012, OAO Gazprom made the decision on the necessity to maintain insurance for the liability of OAO Gazprom and its subsidiaries for environmental damage. The developed insurance terms will provide for coverage of life danger, harm to health, damage to other persons' property and environment as a result of land and offshore drilling and exploration works, production of hydrocarbons, their transportation, refining and storage, construction and other operations performed by OAO Gazprom, its

subsidiaries, associated companies and jointly-controlled companies. The commencement of insurance is planned for the second half of 2013.

The Gazprom Group maintains transparency of its ecological information.

In addition, 2013 was announced as the Ecology Year in OAO Gazprom. The Company plans to hold more than 1,200 activities including implementation of technical developments at gas production and transportation sites for mitigating the impact on environment, education events and providing assistance to specially protected natural areas.

## **BRANCHES AND REPRESENTATIVE OFFICES OF OAO GAZPROM**

Below is the information on branches and representations of OAO Gazprom based on its Charter:

<b>Name</b>	<b>Location</b>
Branch Avtopredpriyatie of OAO Gazprom	Moscow
Branch Corporate Premises Management of OAO Gazprom	Moscow
Branch Bogorodskoye Reception House	Moscow Region
Branch Souyz Holiday Hotel	Moscow Region
Branch Morozovka Holiday Hotel	Moscow Region
Branch Corporate Security Services of OAO Gazprom	Moscow
Central Interregional Security Division of OAO Gazprom	Moscow Region
North-Western Interregional Security Division of OAO Gazprom	St. Petersburg
Southern Interregional Security Division of OAO Gazprom	Krasnodar
Volga Interregional Security Division of OAO Gazprom	Samara
North Urals Interregional Security Division of OAO Gazprom	Novy Urengoi
South Urals Interregional Security Division of OAO Gazprom	Yekaterinburg
Siberian Interregional Security Division of OAO Gazprom	Tomsk
Far Eastern Interregional Security Division of OAO Gazprom	Khabarovsk
Representation in Ukraine	Kyiv
Representation in the Sakhalin Region	Yuzhno Sakhalinsk
Representation in the People's Democratic Republic of Algeria	Algiers
Representation in the Islamic Republic of Iran	Tehran
Representation in Republic of Turkey	Ankara
Representation in the People's Republic of China	Beijing
Representation in India	New Delhi
Representation in the Federative Republic of Brazil	Rio de Janeiro
Representation in Qatar	Doha
Representation in Turkmenistan	Ashgabat
Representation in Republic of Latvia	Riga
Representation in the Republic of Kazakhstan	Astana
Representation in Republic of Moldova	Kishinev
Representation in the Kyrgyz Republic	Bishkek
Representation in the Republic of Belarus	Minsk

**CONVERSION TABLE**

<b>Metric measure</b>	<b>U.S. measure</b>
1 bcm of natural gas	35.316 billion cubic feet (bcf) of natural gas
1 bcf of natural gas	0.028 bcm of natural gas
1 metric ton of crude oil	1,000 kilos, 2,204.6 pounds 7.33 barrels of crude oil, 8.18 barrels of gas condensate 1.43 ton of fuel equivalent
1 barrel of crude oil	0.1364 metric ton of crude oil
1 barrel of gas condensate	0.1222 metric ton of gas condensate
1 kilometer	Approximately 0.62 miles
1 ton of fuel equivalent	867 cm of natural gas, 0.7 ton of gas condensate, 0.7 ton of crude oil
1 mcm of natural gas	1.154 ton of fuel equivalent
1 barrel of gas condensate	1 barrel of oil equivalent (boe)
1 mcm of natural gas	5.89 barrels of oil equivalent (boe)
1 million tons of LNG	1.36 bcm of natural gas

## GLOSSARY OF MAJOR TERMS AND ABBREVIATIONS

Terms and abbreviations	Description
Adjusted EBITDA	Earnings before interest, taxes, depreciation, and amortization adjusted by changes in impairment provisions
ADR of OAO Gazprom	Before April 2011 onwards 1 ADR provided a right for four ordinary shares of OAO Gazprom. Since April 2011 onwards 1 ADR provides a right for two ordinary shares of OAO Gazprom
APG	Associated petroleum gas
APR	Asia-Pacific Region, which includes inland countries of Asia, America and Pacific Ocean Area
Associated undertaking	Associated undertaking is a company over which the Gazprom Group has significant influence – significant influence occurs when the Group has the power to participate in the financial and operating policy decisions of an entity but has no control or joint control over those policies
Baltic countries	Latvia, Lithuania, Estonia
bcm	Billion cubic meters
boe	Barrel of oil equivalent
bboe	Billion barrels of oil equivalent
Category ABC <sub>1</sub> hydrocarbon reserves	Explored reserves, according to the Russian reserves system. Gas reserves in categories ABC <sub>1</sub> are considered to be fully extractable. For reserves of crude oil and gas condensate, a predicted coefficient of extraction is calculated based on geological and technical factors.
Category C <sub>2</sub> hydrocarbon reserves	Category C <sub>2</sub> represents reserves of a deposit the crude oil or gas content of which is calculated on the basis of geological and geophysical data within the known gas areas. Category C <sub>2</sub> reserves are preliminary estimated reserves and represent a basis for exploration work at a particular field.
Central Asia	Kazakstan, Kyrgyzstan, Tadjikistan, Turkmenistan, Uzbekistan
Central Europe	Bulgaria, Bosnia-Herzegovina, Hungary, Macedonia, Poland, Romania, Serbia, Montenegro, Slovakia, Slovenia, Croatia, Czech Republic
cf	Cubic feet
CIS	Commonwealth of independent states – former Soviet Union republics except for Latvia, Lithuania and Estonia
cm	Cubic meter of natural gas measured under pressure of 1 bar at the temperature of 20°C
CS	Compressor station
EU	European Union
EURIBOR	Euro Interbank Offered Rate
Europe	For the purposes of the Report includes Western and Central Europe
Europe and other countries	Countries other than Russia and the FSU countries.
Far abroad	Foreign countries, except for FSU countries
FSU	Former Soviet Union republics, except for the Russian Federation
FTS of Russia	Federal Tariff Service
Fuel equivalent	Natural equivalent measuring unit used to compare different types of fuel. Recalculation of certain type of fuel to fuel equivalent is made by the ratio of enthalpy of that fuel (1 kg) to enthalpy of fuel equivalent (1 kg); the latter equals to 29.3076 Mega joule

<b>Terms and abbreviations</b>	<b>Description</b>
G&G	Geological exploration works
Gazprom Group, Group, Gazprom	An aggregate of entities which includes OAO Gazprom (Head Office) and its subsidiaries
Gazprom Neft Group	An aggregate of entities which includes OAO Gazprom Neft (Head Office) and its subsidiaries. Gazprom Group controls Gazprom Neft Group.
GCF	Gas Condensate Field
GPC	Gas Processing Complex
GTS	Gas Transportation System
IFRS	International Financial Reporting Standards accepted in EU
Jointly-controlled company	Jointly controlled company is an entities which is jointly controlled by two or more parties
kWh	Kilowatt-hour
LIBOR	London Interbank Offered Rate
LNG	Liquefied Natural Gas
LSE	London Stock Exchange
mboe	Million barrels of oil equivalent
mcm	Thousand cubic meters
MICEX	Moscow Interbank Currency Exchange
Net debt	The sum of short-term borrowings, current portion of long-term borrowings, short-term promissory notes payable, long-term borrowings, long-term promissory notes payable and restructured tax liabilities, net of cash and cash equivalents and balances of cash and cash equivalents restricted as to withdrawal under the terms of certain borrowings and other contractual obligations
NPZ	Refinery
OGCF	Oil and gas condensate field
PSC	Power supply contract
Return on capital employed	Calculated as operating and non-operating profit before interest, net of income tax to the average capital employed. Average capital employed is calculated as the average of total equity and total debt at the beginning and at the end of year.
RR	Russian Rouble
PRMS Standards	International classification and assessment of hydrocarbon reserves under PRMS (Petroleum Resources Management System). These standards do not only include the assessment of physical presence of hydrocarbons but also provide the economic viability of recovering the reserves and consider the period of commercial development of fields (term of development license).
SDPP	State district power plant
SRTO-Torzhok	Gas pipeline from Northern parts of Tyumen region to Torzhok
tcf	Trillion cubic feet
tcm	Trillion cubic meters
ton	Metric ton
Total debt	Long-term and short-term loans and borrowings, long-term and short-term promissory notes, restructured tax payable
TPP	Thermal Power Plant
UGSF	Underground Gas Storage Facility

<b>Terms and abbreviations</b>	<b>Description</b>
UGSS	Unified Gas Supply System of Russia
U.S.\$	The United States Dollars
VAT	Value Added Tax
Western Europe	Austria, Andorra, Belgium, Germany, Greenland, Greece, Denmark, Republic of Ireland, Iceland, Spain, Italy, Cyprus, Liechtenstein, Luxembourg, Malta, Monaco, The Netherlands, Norway, Portugal, San Marino, the United Kingdom and Republic of Ireland, Turkey, Finland, France, Switzerland, Sweden
YaNAO	Yamal-Nenets Autonomous District

**ADDRESSES AND CONTACTS****Full name:** Open Joint Stock Company Gazprom**Abbreviated name:** OAO Gazprom

Location: 16 Nametkina str., Moscow, Russian Federation

Mailing address: 16 Nametkina str., Moscow, GSP-7, 117997

Phone: +7 (495) 719-30-01 (information). Fax: +7 (495) 719-83-33

Web-site: [www.gazprom.ru](http://www.gazprom.ru) in the Russian language, [www.gazprom.com](http://www.gazprom.com) in the English languageE-mail: [gazprom@gazprom.ru](mailto:gazprom@gazprom.ru)

Certificate on entry in the Unified State Register of Legal Entities issued by the Interregional Inspectorate of the Russian Ministry of Taxes and Levies for the Moscow city on 2 August, 2002, OGRN - 1027700070518

Taxpayer's identification number (INN): 7736050003

**Department for Relations with Shareholders:** Olga Igorevna Borodina

Phone: +7 (495) 719-27-86, 719-26-01. Fax: +7 (495) 719-39-37

E-mail: [O.Borodina@adm.gazprom.ru](mailto:O.Borodina@adm.gazprom.ru)**Department for Relations with Investors:** Andrei Vitalievich Baranov

Phone: +7 (495) 719-25-89. Fax: +7 (495) 719-35-41

E-mail: [A.Baranov@adm.gazprom.ru](mailto:A.Baranov@adm.gazprom.ru)**Auditor of OAO Gazprom:** ZAO PricewaterhouseCoopers Audit

Member of non-profit partnership «Audit Chamber of Russia» (NP ACR) being a self-regulatory organization of auditors – registration number 870 in the register of NP ACR members

Major registration record number (ORNZ) in the register of auditors and audit organizations 102010003683

Location and mailing address: ZAO PricewaterhouseCoopers Audit (ZAO PwC Audit), White Square Office Center, 10 Butyrsky Val, Moscow 125047 Russian Federation

Phone: +7 (495) 967-60-00. Fax: +7 (495) 967-60-01

**Registrar:** Closed Joint Stock Company Specialized Registrar – Holder of the register of gas industry (ZAO SR-DRAG)

Location and mailing address: 71/32, Novocheryumushkinskaya str., Moscow 117420, Russian Federation

Phone: +7 (495) 719-39-29. Fax: +7 (495) 719-45-85

**Depository bank (ADR of OAO Gazprom):** The Bank of New York Mellon

Phone (the US only): 1-888-BNY-ADRS (1-888-269-2377). Phone (other countries): 201-680-6825

E-mail: [shrrelations@bnymellon.com](mailto:shrrelations@bnymellon.com)Web site: [www.bnymellon.com/shareowner](http://www.bnymellon.com/shareowner)