OAO AK TRANSNEFT
IAS CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2000

CONTENTS

	Page
Statement of Directors' Responsibilities	3 – 4
Auditors' Report	5
Consolidated Balance Sheet	6
Consolidated Statements of Income	7
Consolidated Statements of Cash Flows	8
Consolidated Statements of Changes in Shareholders' Equity	9
Notes to the Consolidated Financial Statements	10 – 31

STATEMENT OF DIRECTORS' RESPONSIBILITIES
To the Shareholders of OAO AK Transneft

1. We have prepared consolidated financial statements for the year ended 31 December 2000 which give a true and fair view of the financial position of the Group at the end of the period and of the results of operations and cash flows for the period then ended. Management is responsible for ensuring that the Group entities keep accounting records which disclose with reasonable accuracy the financial position of each entity and which enable them to ensure that the consolidated financial statements comply with International Accounting Standards and that their statutory accounting reports comply with Russian laws and regulations. Management also has a general responsibility for taking such steps as are reasonably available to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

2. Management considers that, in preparing the consolidated financial statements set out on pages 6 to 31, the Group has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that appropriate International Accounting Standards have been followed.

3. The names of the directors during the year ended 31 December 2000, and their other positions in Group companies or government were as follows:

Name	Position in Group companies or Government
Current Board Members	
Alexandrov V.N.	General Director of OAO Verkhnevolzhskye MN
Danilov-Danialian A.V.	Chief of Economics Department in the Presidential Administration
Gref G.O.	First Deputy Minister of the State Property Committee of the Russian Federation
Kutovoi G.P.	Deputy Chairman of the Federal Energy Commission
Morozov E.S.	Deputy Minister of Energy
Nabiev R.R.	General Director of OAO Uralsibnefteprovod
Rybak O.P.	Chief of Department in the State Property Committee
Shamraev N.G.	Deputy Minister of Economics
Stanev V.S.	Deputy Minister of Energy of the Russian Federation, Chairman of the Board of Directors of the Company
Toropov S.V.	Chief of Department in the State Property Committee
Tsyganov A.G.	Deputy Minister of the State Anti-Monopoly Policy and Business Support
Vainstock S.M.	President OAO AK Transneft
Vorobiev V.A.	Chief of Department in the Ministry of Energy
Retired during the period	
Arakelian E.M.	Deputy Chief of Department in the Ministry of Energy
Zhirov A.I.	General Director of OAO Chernomortransneft MN

(continued on page 4)

STATEMENT OF DIRECTORS' RESPONSIBILITIES
To the Shareholders of OAO AK Transneft (continuation)

4. None of the directors held any shares in Group companies during the year ended 31 December 2000.

5. The consolidated financial statements, which are based on the statutory consolidated accounting reports approved by the Board of Directors in May 2001, have been restated in accordance with International Accounting Standards.

____
S.M. Vainstock
President
25 May 2001

OAO AK Transneft
109180 Moscow
ul. Bolshaya Polyanka 57
Russian Federation

PRICEWATERHOUSECOOPERS

ZAO PricewaterhouseCoopers Audit
Kosmodamianskaya Nab. 52, Bld. 5
113054 Moscow
Russia
Telephone +7 (095) 967 6000
Facsimile +7 (095) 967 6001

AUDITORS' REPORT
To the Shareholders and Board of Directors of OAO AK Transneft

1. We have audited the accompanying consolidated balance sheet of OAO AK Transneft (the "Company") and its subsidiaries (the "Group") as at 31 December 2000 and the related consolidated statements of income, of cash flows and of changes in shareholders' equity for the year then ended. These consolidated financial statements set out on pages 6 to 31 are the responsibility of the Group's management. Our responsibility is to express an opinion on the consolidated financial statements based on our audit.

2. We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

3. In our opinion, the accompanying consolidated financial statements give a true and fair view of the financial position of the Group as at 31 December 2000 and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards.

4. Without qualifying our opinion, we draw your attention to Note 19.1 to the consolidated financial statements. The changes in the dividend rights of the preferred shares, approved in a resolution of the Annual General Meeting held on 25 June 1999, have been nullified by a decision of the Federal Arbitration Court of the Moscow Region dated 21 January 2001. The Company has submitted the case for review by the Supreme Arbitration Court.

   As a result of the above mentioned decision of the Court, the number of shares participating in earnings has been revised to include preferred shares for the year ended 31 December 2000.

PricewaterhouseCoopers

Moscow, Russia
25 May 2001

(in millions of Russian roubles)

Consolidated Balance Sheet

	Notes	31 December 2000	31 December 1999
ASSETS			
Non-current assets			
Intangible assets		65	88
Property, plant and equipment	4	135,631	130,962
Investments and other long-term assets	5	600	551
Total non-current assets		**136,296**	**131,601**
Current assets			
Inventories	6	4,498	2,951
Receivables and prepayments	7	5,563	6,626
Profit tax assets		421	1,747
Other current assets	8	40	2,494
Cash and cash equivalents	9	5,496	2,573
Total current assets		**16,018**	**16,391**
Total assets		**152,314**	**147,992**
EQUITY AND LIABILITIES			
Shareholders' equity			
Share capital	10	225	225
Retained earnings	10	107,582	103,061
Total shareholders' equity		**107,807**	**103,286**
Minority interests	11	**5,352**	**5,478**
Non-current liabilities			
Borrowings	12	87	161
Deferred taxes	13	28,736	23,898
Provisions for liabilities and charges	14	1,539	1,525
Total non-current liabilities		**30,362**	**25,584**
Current liabilities			
Trade and other payables	15	7,397	12,442
Profit tax liabilities		265	482
Borrowings	12	1,131	720
Total current liabilities		**8,793**	**13,644**
Total liabilities		**39,155**	**39,228**
Total shareholders' equity, minority Interests and liabilities		**152,314**	**147,992**

S.M. Vainstock President

E.I. Astafiev Vice-President, Finance

The accounting policies and the accompanying notes set out on pages 10 to 31 are an integral part of these financial statements. See Auditors' Report on page 5.

(in millions of Russian roubles except amounts per share)

Consolidated Statements of Income

	Notes	Year ended 31 December 2000	Year ended 31 December 1999
Sales	16	54,122	41,801
Operating expenses	17	(35,615)	(31,784)
Net other operating income/(expense)	17	(132)	(1,353)
Operating income		**18,375**	**8,664**
Financial items (net):			
Exchange gains		281	887
Monetary loss		(2,399)	(3,177)
Interest income / (expense)	12	(377)	493
Total financial items		**(2,495)**	**(1,797)**
Income before profit tax		15,880	6,867
Profit tax expense	13	(11,485)	(2,837)
Income after profit tax and before minority interest		4,395	4,030
Minority interests	11	126	(69)
Net income		**4,521**	**3,961**
Basic and diluted earnings per participating share	10	727	849

The accounting policies and the accompanying notes set out on pages 10 to 31 are an integral part of these financial statements. See Auditors' Report on page 5.

(in millions of Russian roubles)

Consolidated Statements of Cash Flows

	Notes	Year ended 31 December 2000	Year ended 31 December 1999
Cash flows from operating activities			
Cash receipts from customers	16	61,627	47,425
Cash paid to suppliers and employees, and taxes other than profit tax		(38,819)	(31,856)
Interest paid		(581)	(226)
Profit tax paid		(5,611)	(5,785)
Net cash from operating activities		**16,616**	**9,558**
Cash flows from investing activities			
Purchase of property, plant and equipment		(13,458)	(9,895)
Interest received		45	169
Acquisition of subsidiaries		-	(699)
Net cash used in investing activities		**(13,413)**	**(10,425)**
Cash flows from financing activities			
Proceeds from long and short-term borrowings		6,280	12,211
Repayment of long and short-term borrowings		(5,838)	(11,875)
Dividends paid		(126)	(178)
Net cash used in financing activities		**316**	**158**
Effects of exchange rate changes on cash and cash equivalents		**172**	**620**
Effect of inflation on holding cash		**(768)**	**(1,061)**
Net increase / (decrease) in cash and cash equivalents		**2,923**	**(1,150)**
Cash and cash equivalents at the beginning of the period	9	2,573	3,723
Cash and cash equivalents at the end of the period	**9**	**5,496**	**2,573**

The accounting policies and the accompanying notes set out on pages 10 to 31 are an integral part of these financial statements. See Auditors' Report on page 5.

(in millions of Russian roubles)

Consolidated Statements of Changes in Shareholders' Equity

	Notes	Share capital	Retained earnings	Total shareholders' equity
Balance at 1 January		**225**	**99,287**	**99,512**
Net income for the year			3,961	3,961
Dividends - preferred	10		(2)	(2)
- ordinary	10		(185)	(185)
Balance at 31 December 1999		**225**	**103,061**	**103,286**
Net income for the year			4,521	4,521
Dividends - preferred	10		-	-
- ordinary	10		-	-
Balance at 31 December 2000		**225**	**107,582**	**107,807**

The accounting policies and the accompanying notes set out on pages 10 to 31 are an integral part of these financial statements. See Auditors' Report on page 5.

.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 NATURE OF OPERATIONS

OAO AK Transneft (the "Company") was established as an open joint stock company and incorporated on 14 August 1993 in the Russian Federation by the Russian Government Resolution No. 810 under Presidential Decree No. 1403 dated 17 November 1992. The Company's registered office is at 109180 Moscow, ul. Bolshaya Polyanka 57, Russian Federation.

The Company and its subsidiaries (the "Group") operate the largest crude oil pipeline system in the world totalling approximately 47,900 km (31 December 1999 – 46,700 km) and are responsible for transportation to refineries and export markets of substantially all the crude oil produced in the territory of the Russian Federation, which amounted to 312.5 million tonnes in the year ended 31 December 2000 (year ended 31 December 1999 – 299 million tonnes).

The Group, which had 56,832 employees as at 31 December 2000 (31 December 1999 – 54,795 employees), is considered by management to have a single main activity and all its activities comprise one industry and geographic segment. Other sales and cost of sales are shown separately in the relevant footnotes, but these activities do not result in significant assets and liabilities and do not constitute a reportable segment as defined by IAS 14 "Segment Reporting".

2 BASIS OF PRESENTATION

Those Group companies incorporated in Russia maintain their statutory accounting records and prepare statutory financial reports in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR") and their measurement currency is the Russian rouble ("RR"). Group companies incorporated in other countries maintain their statutory accounting records in accordance with relevant legislation and in the appropriate measurement currency. The accompanying consolidated financial statements are based on the statutory accounting records, which are maintained under the historical cost convention, with adjustments and reclassifications for the purpose of presentation in accordance with International Accounting Standards ("IAS") issued by the International Accounting Standards Committee ("IASC").

The Group companies were all incorporated at approximately the same time and the consolidated financial statements have been prepared on the basis that there were no acquisitions of shares at the time of incorporation of the Group companies in the context of IAS 22, “Business Combinations”. Subsequent acquisitions have been accounted for in accordance with the relevant accounting policy.

The adjustments and reclassifications made to the statutory accounts for IAS presentation include the restatement for changes in the general purchasing power of the Russian rouble based on IAS 29, "Financial Reporting in Hyperinflationary Economies". IAS 29 requires that financial statements in the currency of a hyperinflationary economy are stated in terms of the measuring unit current at the latest balance sheet date. The restatement was calculated from the conversion factors derived from the Russian Federation Consumer Price Index, published by the Russian State Committee on Statistics, and from indices obtained from other sources for years prior to 1992, which management believes represent the most appropriate measure of inflation in the economy. The rates of inflation for the years ended 31 December 2000 and 1999 were approximately 36% and 20%, respectively.

The indices and the respective conversion factors used to restate the consolidated financial statements, based on 1988 prices (1988=100) for the five years ended 31 December 2000, are:

(in millions of Russian roubles except amounts per share)

Year	Index	Conversion Factors
1996	594,110	3,4
1997	659,403	3,0
1998	1,216,400	1,7
1999	1,661,481	1,2
2000	1,995,937	1,0

The significant guidelines followed in restating the consolidated financial statements are:

- all amounts including corresponding figures are stated in terms of the measuring unit current at the latest balance sheet date;
- monetary assets and liabilities are not restated because they are already expressed in terms of the monetary unit current at the latest balance sheet date;
- non-monetary assets and liabilities (items which are not expressed in the monetary unit current at the balance sheet date) and components of shareholders' equity are restated by applying a conversion factor based on the origination date of the underlying asset, liability or component of shareholders' equity;
- most items in the consolidated statements of income and cash flows are restated by applying the conversion factors for the period between the approximate date of the transaction and the balance sheet date. Depreciation, amortisation, and loss on disposal of property, plant and equipment are restated based on the restated balances of property, plant and equipment at each balance sheet date. Bad and doubtful debts expense represents the movement between the opening and closing provisions adjusted for amounts written off during the period at historic cost, indexed at the average inflation rate for the period. The cash flow statement contains an adjustment to reflect the effect of inflation on holding cash; and
- the effect of inflation on the Group's net monetary position is included in the consolidated statement of income as a net monetary gain or loss.

In December 1998, the IASC issued IAS 39, "Financial Instruments – Recognition and Measurement". IAS 39 is effective for accounting periods beginning on or after 1 January 2001. Management is satisfied that its adoption will not have any significant impact on the Group's consolidated financial statements.

The Group adopted all other new and revised standards approved by the IASC in the preparation of its consolidated financial statements in advance of their mandatory implementation dates, and therefore no adjustments arise in the current reporting period. The Group also adopts all the interpretations approved by the Standing Interpretations Committee of the IASC up to each balance sheet date in its consolidated financial statements.

The preparation of consolidated financial statements in conformity with IAS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates. The most significant estimates relate to estimated useful lives and dismantlement liabilities associated with property, plant and equipment, deferred taxation, the outcome of legal disputes, recovery of receivables and investments, and the probable losses arising from guarantees.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies followed by the Group are set out below:

Consolidation

Those business undertakings in which the Group, directly or indirectly, has an interest of more than one-half of the voting rights or otherwise has power to exercise control over the operations are defined as subsidiary undertakings ("subsidiaries") and have been consolidated. Subsidiaries are consolidated from the date on which effective control is transferred to the Group and are no longer consolidated from the date when such control ceases.

All transactions, balances and unrealised surpluses and deficits on transactions within the Group have been eliminated on consolidation. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group. The financial statements of all subsidiaries are prepared as of 31 December for the purposes of consolidation.

For subsidiaries that are not wholly owned, the minority's interest is measured as the proportion of the fair value of the assets and liabilities of the subsidiary at the acquisition date, amended for the minority's share of subsequent dividends, profits and losses.

Goodwill and intangible assets

Goodwill represents the difference between the fair value of the purchase consideration and the fair value of the proportion of the net assets at the date of acquisition of the subsidiary.

Goodwill is amortised on a straight-line basis over a maximum period of twenty years.

The carrying amount of goodwill is reviewed at each balance sheet date and written down for impairment where necessary.

Intangible assets are amortised on a straight-line basis over their estimated useful life, which is usually a maximum of ten years.

Foreign currencies

The financial statements of foreign subsidiaries whose operations are integral to those of the Group are translated into the reporting currency as if the transactions had been undertaken directly by the Company.

Foreign currency transactions undertaken by Group companies are accounted for at the exchange rates prevailing at the dates of the transactions. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated statement of income. Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates prevailing at each balance sheet date.

Property, plant and equipment

All property, plant and equipment is initially recorded at historical cost, including, where appropriate, the net present value of the estimated dismantlement or removal cost of the asset at the end of its estimated useful life, less accumulated depreciation. Assets under construction are carried at historical cost and depreciated from the time the asset is brought into use.

Depreciation is calculated on the straight-line basis to write down the cost of each asset to its estimated residual value over its estimated useful life as follows:

	Years
Buildings	50
Pipelines	33
Plant and equipment	10 - 20

Crude oil held in storage and in the pipeline network ("linefill") owned by the Group is treated as a separate class of asset, which is not depreciated as it is not physically consumed in the process of providing services to customers.

Management approves specific plans for prospective dismantlement or decommissioning of sections of pipeline and related facilities on an annual basis, and at this time, the estimated useful life of the related asset is revised and the annual depreciation charge is amended accordingly. In the event that a decision is made to abandon a construction project in progress or to significantly postpone its planned completion date, or if there are other indications of potential impairment, the carrying value of the asset is reviewed.

At each balance sheet date an assessment is made as to whether there is any indication that the recoverable amount of the Group's property, plant and equipment is less than the carrying amount. When there is such an indication, an impairment provision is made which is charged in full to the results of operations in the period in which the impairment occurred. Linefill is assessed for impairment by reference to net realisable value, which is calculated based on the export price of Russian Urals Blend crude oil (FOB Novorossiysk) at each balance sheet date. The Group's pipeline network, associated buildings and plant and equipment are assessed by reference to their value in use, based on future cash flow forecasts from continuing use of the asset discounted to net present value. The discount rate used is that considered appropriate to the Group in the economic environment in the Russian Federation at each balance sheet date.

Major renewals and improvements are capitalised and the assets replaced are retired. Maintenance and repairs and minor renewals are expensed as incurred. Minor renewals include all expenditures which do not result in a technical enhancement of the asset beyond its original capability, or which represent the replacement of sections of pipeline which are less than ten kilometers in length and do not constitute phased replacements of a longer section of pipeline over an extended period. Gains and losses arising from the retirement or other disposal of property, plant and equipment are included in the consolidated statement of income.

Interest costs on borrowings to finance the construction of property, plant and equipment are expensed as incurred.

Social assets which were part of the assets transferred to the Group companies at the time of their privatisation have been excluded from these consolidated financial statements if the privatisation plan provided for them to be transferred to municipal authorities or other organisations without consideration.

Investments and other long-term assets

Long-term investments, excluding marketable securities, are stated at cost. Provision is made where, in the opinion of the Group's management, there is a diminution in value which is other than temporary and such provisions are recognised as an expense in the period in which they are identified.

Marketable securities are valued at the lower of cost and market value, and changes in carrying amount are charged or credited to the consolidated statement of income.

On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is charged or credited to the consolidated statement of income.

Accounts receivable

Accounts receivable are presented at net realisable value. An estimate is made for doubtful receivables based on a review of all outstanding amounts at each balance sheet date, and the movement in the estimate is charged or credited to the consolidated statement of income. Bad debts are written off in the period in which they are identified.

Inventories

Inventories are valued at the lower of weighted average cost and net realisable value.

Revenue recognition

Revenues are recognised for financial reporting purposes when transportation services have been provided as evidenced by delivery of crude oil to the owner or customer in accordance with the contract.

Value Added Tax

In the consolidated balance sheet and the consolidated statements of cash flows, transactions and balances are presented inclusive of the associated Value Added Tax ("VAT") applicable under the legislation of the relevant jurisdiction in which the transaction occurred. These taxes are excluded from the consolidated statement of income since the payment and collection of VAT generally has no effect on the results of operations.

Deferred taxes

Deferred taxes are calculated at currently enacted or substantially enacted rates, using the liability method, for all temporary differences between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. The principal temporary differences arise from the inflation of, and depreciation on, property, plant and equipment and income, provisions and expenses which are included in the consolidated statement of income before they become taxable or deductible for tax purposes.

Deferred tax liabilities are recognised in respect of all taxable temporary differences relating to investments in subsidiaries, unless the Company is able to control the timing of the reversal of the temporary difference and it is probable that the difference will not reverse in the foreseeable future.

Deferred tax assets attributable to temporary differences and to unutilised tax losses and credits are recognised only to the extent that it is probable that future taxable profit or temporary differences will be available against which they can be utilised.

Retirement benefit obligations and other employee benefits

The Group makes statutory contributions, which are calculated as a percentage of current gross salary payments, in respect of its employees to the State Pension Scheme of the Russian Federation and such expense is charged to the consolidated statement of income.

Short-term employee benefits, provided under the conditions of legal agreements with employees' organisations, expected to be paid within one year of the balance sheet date are included in expenses on the accruals basis.

Other expenditures for the benefit of employees, former employees and their dependants which are discretionary are expensed following management approval in the period to which they relate.

The Group's contractual liability for long-term employee benefits, such as lump sum payments at the point of retirement, is estimated at each balance sheet date and included in the consolidated financial statements at its expected net present value using the discount rate appropriate to the Group in the economic environment in the Russian Federation at each balance sheet date.

Provisions

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

Provisions are reassessed at each balance sheet date, and are included in the consolidated financial statements at their expected net present values using the discount rate appropriate to the Group in the economic environment in the Russian Federation at each balance sheet date.

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

The Group recognises the estimated cost of crude oil spillages, including the cost of the obligations to restore the environment (air, land, water and other resources) and the estimated recoveries under applicable insurance policies, at the date of the spillage.

The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised as expenses immediately, unless they extend the life of the related property or mitigate or prevent future environmental contamination, in which case they are capitalised.

Financial assets and liabilities

Financial assets and liabilities carried on the consolidated balance sheet include cash and cash equivalents, investments, receivables, borrowings and trade and other payables. The particular recognition methods adopted are disclosed in the individual accounting policies contained in these concolidated financial statements associated with each item.

Cash received as restricted purpose investment tariff is excluded from the consolidated statements of income and cashflow and is accumulated in current liabilities in the consolidated balance sheet until its disposition is clarified, and the restricted bank accounts representing those funds which have not yet been disbursed are classified as other current assets.

Cash and cash equivalents

Cash and cash equivalents consist of cash, bank balances and highly liquid investments with maturities of three months or less at the date of acquisition.

Earnings/(loss) per share

Earnings/(loss) per share is calculated by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding those held by entities within the Group.

(in millions of Russian roubles except amounts per share)

4 PROPERTY, PLANT AND EQUIPMENT

	Buildings	Pipelines	Plant and equipment	Linefill	Assets under construction including prepayments	Total
At 1 January 2000						
Cost	24,084	120,627	66,351	36,367	10,136	257,565
Accumulated depreciation	(9,333)	(82,043)	(35,227)	-	-	(126,603)
Net book value at 1 January 2000	14,751	38,584	31,124	36,367	10,136	130,962
Depreciation	(549)	(3,675)	(4,698)	-	-	(8,922)
Additions	-	-		311	14,081	14,392
Transfers from assets under construction to fixed assets	2,045	5,779	5,701	-	(13,525)	-
Disposals at cost	(410)	(196)	(1,701)	(285)	-	(2,592)
Accumulated depreciation on disposals	250	188	1,353	-	-	1,791
Net book value at 31 December 2000	16,087	40,680	31,779	36,393	10,692	135,631
At 31 December 2000						
Cost	25,719	126,210	70,351	36,393	10,692	269,364
Accumulated depreciation	(9,632)	(85,530)	(38,572)	-	-	(133,734)
Net book value	16,087	40,680	31,779	36,393	10,692	135,631

Linefill represents 26,285 thousand tonnes of crude oil (31 December 1999 – 26,383 thousand tonnes).

Assets under construction at 31 December 2000 are presented net of a provision of RR 144 million for projects which are unlikely to be completed (31 December 1999 – RR 502 million) .

Included in property, plant and equipment above are fully depreciated assets still in service whose cost is RR 35,086 million (31 December 1999 – RR 34,420 million), and temporarily idle assets whose net book value is RR 1,642 million (31 December 1999 – RR 1,313 million).

Property, plant and equipment pledged as security for borrowings totalled RR 19 million (31 December 1999 – RR 521 million).

5 INVESTMENTS AND OTHER LONG-TERM ASSETS

	31 December 2000	31 December 1999
Non-consolidated subsidiaries:		
Diana Insurance Company	72	72
Transneft Insurance Company	17	17
Other	16	24
Marketable securities	402	324
Investments in other Russian companies and banks	93	114
	600	551

(in millions of Russian roubles except amounts per share)

Subsidiaries whose total assets, net assets, revenues, costs and net income are not material, either individually or in the aggregate, are not consolidated but are included in investments.

Investments in other Russian companies and banks are carried net of provisions for diminution in value of RR 1,729 million (31 December 1999 – RR 1,688 million).

6 INVENTORIES

	31 December 2000	31 December 1999
Materials and supplies	4,002	2,057
Sundry goods for resale	298	817
Other items	198	77
	4,498	2,951

Inventories are presented net of provisions of RR 580 million (31 December 1999 – RR 452 million) for obsolescence and to reduce cost to net realisable value. A significant proportion of materials and supplies represents pipes that will eventually become part of property, plant and equipment.

7 RECEIVABLES AND PREPAYMENTS

	31 December 2000	31 December 1999
Trade receivables (net of a provision for doubtful accounts of RR 152 million at 31 December 2000 (31 December 1999 – RR 130 million)) (1)	2,486	2,489
VAT input tax recoverable	1,584	1,334
Other taxes recoverable	221	44
Prepayments and advances (net of a provision for doubtful accounts of RR 100 million at 31 December 2000 (31 December 1999 – RR 77 million))	816	770
Other receivables (net of a provision for doubtful accounts of RR 509 million at 31 December 2000 (31 December 1999 – RR 1,243 million))	456	1,067
Notes receivable (net of a provision for doubtful accounts of RR nil at 31 December 2000 (31 December 1999 – RR 117 million)) (2)	-	922
	5,563	6,626

(1) Notes receivable are generally unsecured, non-interest bearing and are due within six to twelve months from the date of issuance.

(in millions of Russian roubles except amounts per share)

8 OTHER CURRENT ASSETS

	31 December 2000	31 December 1999
Restricted bank balances	-	2,341
Other financial assets	40	153
	40	2,494

Restricted bank balances are funds collected from oil producers which were designated for the construction of the Baltic Pipeline System. The restrictions were lifted during the year ended 31 December 2000, and the funds were redesignated as cash and cash equivalents.

9 CASH AND CASH EQUIVALENTS

	31 December 2000	31 December 1999
State Savings Bank (Sberbank Russia)	470	1,036
Alef Bank (Russia)	615	94
Mezhprombank (Russia)	308	1,481
Barclays Bank (UK)	422	500
Alfa Bank (Russia)	1,464	630
MDM Bank (Russia)	906	602
Stroicredit Bank (Russia)	632	27
Vneshtorgbank (Russia)	20	0
SDM Bank (Russia)	95	62
Bank Vozrozhdenie (Russia)	292	0
Other Russian banks	272	482
	5,496	4,914
Restricted bank balances	-	(2,341)
	5,496	2,573

10 SHARE CAPITAL, RETAINED EARNINGS AND EARNINGS PER SHARE

	Nominal amounts	31 December 2000 and 1999
Authorised, issued and fully paid shares of par value RR 1 each		
Ordinary: 4,664,627 shares	5	169
Preferred: 1,554,875 shares	1	56
	6	225

As a result of the decision of the Federal Arbitration Court dated 21 January 2001, explained in more detail in Note 19.1, management's estimate of the number of shares entitled to participate in earnings has been revised for the year ended 31 December 2000 to include the preferred shares. Accordingly, the numbers of shares used in the calculation of earnings per share are as follows:

(in millions of Russian roubles except amounts per share)

	Year ended 31 December 2000	**Year ended 31 December 1999**
Ordinary shares	4,664,627	4,664,627
Preferred shares	1,554,875	-
Total	6,219,502	4,664,627

	Year ended 31 December 2000	**Year ended 31 December 1999**
Net income	4,521	3,961
Less dividends on preferred shares	-	(2)
Amounts available for ordinary shareholders	4,521	3,959
Basic and diluted earnings per ordinary share	727	849

The Group's largest shareholders are:

State Property Committee of the Russian Federation	100% of ordinary shares
OOO Benevent	43% of preferred shares
Smeralco Investment Ltd.	13% of preferred shares

Rights attributable to preferred shares

Preferred shareholders may only vote at meetings on the following issues:

- the amendment of their rights to income;
- the issue of additional shares with rights greater than or equal to their rights in terms of income or assets on liquidation; and
- the liquidation or reorganisation of the Group.

Holders of preferred shares acquire the same voting rights as holders of ordinary shares in the event that dividends are either not declared, or are declared but not paid.

In accordance with the Company's charter documents, preferred shares earned dividends amounting to 10% of the net income of the Company according to RAR for the year, if any, and the dividend per share on preferred shares was not permitted to be less than that paid on each ordinary share until these rights were amended based on a resolution of the Annual General Meeting dated 25 June 1999, after which the annual dividend on preferred shares was fixed at RR 0.5 per share. The necessary amendments to the charter document were registered on 30 August 1999. On liquidation, the preferred shareholders are entitled to receive distribution of net assets equal to the par value of the shares, prior to any distribution to ordinary shareholders.

As a result of the matter explained in more detail in note 19.1, as well as earlier legal actions now resolved, the preferred shares acquired voting rights equivalent to those attributable to ordinary shares during 1999, and this situation has not changed at the date of issuing these consolidated financial statements.

Dividends

Dividends of RR 253.11 (RR 85.91 in historic terms) on each preferred share were approved in the shareholders' annual general meeting held on 30 June 1998 in respect of the financial year 1997 and were paid in June 2000.

(in millions of Russian roubles except amounts per share)

Interim dividends of RR 34.07 (RR 27.02 in historic terms) on each ordinary share were approved in the Board of Directors' meeting held on 26 August 1999 in respect of the financial year ending 31 December 1999, and were paid in November 1999. Further interim dividends of RR 28.05 per ordinary share for the year ended 31 December 1999 were approved in the Board of Directors' meeting held on 8 February 2001 and paid in January 2001.

Dividends of RR 0.62 (RR 0.5 in historic terms) on each preferred share in respect of the year ended 31 December 1999 were approved in the meeting of the Board of Directors held on 26 August 1999. Payment of these dividends has been delayed pending resolution of the matter explained in more detail in note 19.1.

The Board of Directors has made the following proposals for dividends per share in respect of the years ended 31 December 1999 and 2000, which have not been included as liabilities in these consolidated financial statements, but will be considered by the shareholders in their Annual General Meeting in June 2001:

	Roubles per share	**Total RR million**
For the year ended 31 December 1999		
Preferred shares	207.50	322.6
Ordinary shares (including interim dividends paid in November 1999 and January 2001)	55.74	260.0
For the year ended 31 December 2000		
Preferred shares	nil	nil
Ordinary shares	nil	nil

Distributable retained earnings

The statutory accounting reports of the parent Company and each subsidiary are the basis for their respective profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the current period net profit. For the year ended 31 December 2000, the statutory profit for the Company as reported in the statutory reporting forms was RR 10,998 million (1999 – RR 3,963 million or RR 3,226 million in historic terms). However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation and accordingly management believes at present it would not be appropriate to disclose an amount as "distributable retained earnings" in these consolidated financial statements.

11 MINORITY INTERESTS

	Year ended 31 December 2000	**Year ended 31 December 1999**
At 1 January	5,478	6,185
Effect of acquisition	-	(776)
Share of net income for the year	(126)	69
Balance 31 December	5,352	5,478

Minority interests represent the shares in consolidated subsidiaries held by the Regional State Property Committees of the Republics of Tatarstan (36% of OAO Severo-Zapadny MN) and Bashkortostan through OAO Bashneft (24.5% of OAO Uralsibnefteprovod).

As a result of the acquisition by the Group of the minority interest in OAO Severniye MN during the year ended 31 December 1999, the minority interest in this subsidiary has been eliminated in the calculation of goodwill.

(in millions of Russian roubles except amounts per share)

12 BORROWINGS AND INTEREST INCOME/(EXPENSE)

	31 December 2000	31 December 1999
Total borrowings	1,218	881
Less: current portion of borrowings	(1,131)	(720)
	87	161
Maturity of non-current borrowings		
Due for repayment:		
Between one and two years	4	58
Between three and five years	47	54
After five years	36	49
	87	161

The majority of borrowings are in Russian roubles and bear variable market rates of interest which range from 10% to 28% annually. Typical security for these loans are crude oil in storage reservoirs and general charges on assets. The total value of property, plant and equipment pledged as security and general charges on assets was RR 67 million (31 December 1999 – RR 521 million).

	Year ended 31 December 2000	Year ended 31 December 1999
Interest income / (expense):		
Interest expense	(562)	(185)
Interest income	185	678
Net interest income / (expense)	(377)	493

13 PROFIT TAX AND DEFERRED TAXES

	Year ended 31 December 2000	Year ended 31 December 1999
Profit tax expense consists of:		
Current tax expense	6,646	4,493
Effect of change in tax rate on deferred tax liabilities and assets	4,105	(3,651)
Deferred tax expense	734	1,995
	11,485	2,837

(in millions of Russian roubles)

Deferred tax liabilities and assets consist of the following:

	31 December 2000	31 December 1999
Deferred tax liabilities:		
Revenue recognition	(130)	(196)
Carrying value of property, plant and equipment in excess of tax base	(29,412)	(24,448)
	(29,542)	(24,644)
Deferred tax assets:		
Provisions against inventories and receivables	213	207
Provisions for dismantlement and other expenses	593	539
	806	746
Net deferred tax liability	(28,736)	(23,898)

With effect from 1 April 1999, the standard rate of profit tax payable by companies in the Russian Federation was reduced from 35% to 30%. Therefore, the effective tax rate for 1999 was 31.25%.

With effect from 1 January 2001, profit tax payable by companies in the Russian Federation can range from 30% to 35%, depending on the decision of regional and local tax authorities each year which can agree jointly on a supplementary amount of up to 5% above that set by the federal tax authorities. The rate used to compute the deferred tax assets and liabilities of the Group at 31 December 2000 is 35%, which reflects the fact that substantially all regional and local tax authorities in the regions where the Group operates had decided to assess the maximum supplementary amount in respect of the year 2001.

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

	Year ended 31 December 2000	Year ended 31 December 1999
Income before profit tax	15,880	6,867
Theoretical profit tax expense at 30% (1999: 31.25%)	4,764	2,146
Increase (reduction) due to:		
Allowance for capital expenditure	(1,021)	(1,395)
Expenses not deductible for profit tax purposes	407	1,474
Non-temporary elements of net monetary loss	7,196	13,625
Tax penalties and interest	38	32
Temporary difference on revaluation of tax base	-	(44)
Effect of changes in tax rates	4,105	(3,651)
Inflation effect on deferred tax balance at the beginning of the year	(4,004)	(9,350)
Actual profit tax expense	11,485	2,837

The maximum potential deferred tax liability, not provided in these consolidated financial statements, which would materialise in the event that the subsidiaries paid all available amounts as dividends is RR 8,426 million (31 December 1999 – RR 7,999 million).

(in millions of Russian roubles)

14 PROVISIONS FOR LIABILITIES AND CHARGES

	Dismantlement (1)	Preferred shares (2)	Employment benefits (3)	Total
At 1 January 2000	1,232	88	205	1,525
Additional provisions made/released	190	35	12	237
Amounts used	(163)	(25)	(35)	(223)
Balance 31 December 2000	1,259	98	182	1,539

(1) Dismantlement

A provision is established for the expected cost of dismantling the existing pipeline network based on the average current cost per kilometre of removal according to an estimated plan of replacement over the long term and discounted to net present value using a rate of 17.5% per year (1999 - 17.5% per year). The replacement program is expected to cover the same number of kilometres each year over the useful life of the network, and this plan could change over the course of time. The cost of dismantlement is added to the cost of property, plant and equipment and depreciated over the useful economic life of the pipeline network. Additional provisions are therefore made when the total length of the network increases, and reductions occur when sections of the pipeline are decommissioned. Other changes are made when the expected pattern or unit cost of dismantlement is changed.

(2) Preferred shares

Certain subsidiaries entered into contracts with the original holders of the preferred shares of the Company under which, in return for the holders selling their shares, those subsidiaries made commitments to pay annual amounts indefinitely based on a percentage of the profits of the subsidiary calculated in accordance with RAR. Payments are made in May and November each year based on the results of operations of the relevant subsidiaries for the six months ended on the previous 31 December and 30 June, respectively. A provision is made for the net present value of the estimated future payments under such contracts assuming that the relevant subsidiaries continue to make profits of the same average amount as in the last three most recently completed financial years. The net present value is calculated using a discount rate of 17.5% per year (1999 - 17.5% per year).

(3) Employment benefits

Under collective agreements with the employees, an amount ranging from one to ten months' final salary is payable upon retirement to those who have worked for the Group for more than five years. Management has carried out an exercise, following the guidelines set out in IAS 19, "Employee Benefits", to assess the net present value of these obligations. Under this method an assessment has been made of an employee's service period with the Group, and the expected salary and number of months' salary payable under these agreements having regard to staff turnover statistics, retirement age, and salaries at retirement. The expected liabilities at the date of retirement have been discounted to net present value using a rate of 17.5% per year (1999 – 17.5% per year).

In view of the relative insignificance of the overall liability, and of the expense recognised in the consolidated statement of income for the year, the additional disclosures required by IAS 19 have not been made.

(in millions of Russian roubles)

15 TRADE AND OTHER PAYABLES

	31 December 2000	31 December 1999
Trade payables	4,268	3,193
Notes payable	90	1,071
Accruals and deferred income	276	50
VAT output tax payable (including deferred amounts of RR 350 million (31 December 1999 – RR 603 million))	520	1,214
Advances received	881	2,040
Advances related to Baltic Pipeline System (Note 16)	-	2,851
Other taxes payable	631	731
Dividends payable (Note 10)	1	138
Other payables	730	1,154
	7,397	12,442

Notes payable are generally unsecured, non-interest bearing and are due within six months of the date of issuance.

VAT input and output taxes can only be offset under tax regulations to the extent that they relate to the same subsidiary; deferred VAT output tax liabilities become payable when the value of the underlying invoice has been received.

16 SALES

	Year ended 31 December 2000	Year ended 31 December 1999
Revenues from oil transportation services		
Domestic tariff	23,383	20,848
Export tariff	20,166	13,507
Investment tariff	2,851	-
Total revenues from oil transportation services	46,400	34,355
Net other revenues	7,722	7,446
Total sales	54,122	41,801

Tariff structure as at 31 December 2000:

The revenues of the Group for oil transportation services comprise:

- distance-related tariffs, denominated and payable in RR and revised periodically after approval by the Federal Energy Commission ("domestic tariff"), for transportation of crude oil on the domestic pipeline network. These are calculated based on total operating costs calculated in accordance with RAR (with certain exclusions) based on normal levels of activity and a monetary profit margin;

- a further distance-related tariff, denominated in US$ but payable in RR, and revised periodically after approved by the Federal Energy Commission for transportation on the domestic pipeline network of crude oil which is destined for export ("export tariff") which is designed to provide revenues for the reconstruction of the existing network;

(in millions of Russian roubles)

- a fixed tariff, denominated and payable in US$, under intergovernmental agreements for the transportation of crude oil from Azerbaijan, for export at Novorossiysk and other outlets; and

- a distance-related tariff, denominated and payable in US$, set by the Federal Energy Commission, for transit of Kazakhstan crude oil over the territory of the Russian Federation.

Baltic Pipeline System

The Group had invoiced RR 2,851 million of investment tariff in 1999 which was designated to provide funds for the construction of the Baltic Pipeline System, and these amounts had not previously been recognised as income or as cash receipts from customers since their eventual dispositon was uncertain. Management is satisfied that these uncertanties were materially eliminated during the year ended 31 December 2000, and therefore the entire amount has been recognised as income in that year in the consolidated statement of income and as cash receipts from customers in the consolidated statement of cash flows.

Tariff increases in 2000 and 2001

	Domestic tariff	**Export tariff**
11 January 2000	17%	11%
1 April 2000	-	12%
14 July 2000	-	12%
10 August 2000	-	25%
1 November 2000	-	22%
11 January 2001	38%	-

A fixed tariff of US$ 8.06 per tonne was also established for crude oil transported through the Chechnya bypass on 14 July 2000.

17 OPERATING EXPENSES AND NET OTHER OPERATING INCOME/(EXPENSE)

	Year ended 31 December 2000	**Year ended 31 December 1999**
Operating expenses		
Depreciation	8,992	7,298
Staff costs	6,897	5,997
Electricity	2,680	2,655
Maintenance and repairs and minor renewals	3,570	3,186
Materials	3,440	3,337
Usage of oil	285	506
Taxes other than profit tax:		
Road users' and housing fund taxes	2,096	2,089
Property tax	338	318
Other taxes	427	344
Cost of goods for resale	3,897	2,757
Social expenditures and discretionary employee benefits	691	734
Research and development	204	380
Tax penalties and interest	127	139
Insurance expenses (Note 20.2)	345	179

(in millions of Russian roubles)

Communication expenses	142	109
Transport expenses	412	554
Administrative expenses	254	392
Other	888	810
Total operating expenses	35,615	31,784

Staff costs include RR 1,326 million (1999 - RR 1,289 million) of contributions to the State Pension Scheme of the Russian Federation.

Taxes included in operating expenses, which are calculated on figures prepared in accordance with RAR, are computed as follows:

- Road users' and housing fund taxes vary by region and locality but generally do not exceed 2.5% and 1.5%, respectively, of revenues invoiced in the respective region.

- Property tax is assessed at a maximum of 2.0% on the average annual net book value of fixed assets, intangible assets and inventory. Specific legislation provides for the exclusion of trunk pipelines from the taxable base.

The following items are included in net other operating income/(expenses):

	Year ended 31 December 2000	**Year ended 31 December 1999**
Amounts connected with related party transactions (Notes 20.1 and 20.4)	(55)	252
Recovery/(usage and losses) of linefill	203	(846)
Losses on disposal of property, plant and equipment and social assets	(106)	(1,099)
(Increase)/decrease in provisions against investments and doubtful debts	(16)	(115)
Other operating income/(expenses)	(158)	455
	(132)	(1,353)

18 CONSOLIDATED SUBSIDIARIES AND ACQUISITIONS

	Percent (%) of voting share capital held at 31 December 2000
Regional pipeline operators	
OAO Sibnefteprovod	100
OAO Chernomortransneft	100
OAO Druzhba	100
OAO Privolzhsknefteprovod	100
OAO Transsibneft	100
OAO Verkhnevolzhskiye MN	100
OAO Tsentrsib MN	100
OAO Severniye MN	100
OAO Uralsibnefteprovod	75.5
OAO Severo-Zapadniye MN	64
OOO Baltic MN	100
Other services	

OAO Giprotruboprovod	100
OAO Svyaztransneft	100
OAO Stroineft	100
OAO Technical Diagnostics Centre	100
OAO Volzhsky Podvodnik	100
OAO Metrological Ensuring Centre	100
Transneft UK Limited	100
OOO Trade House Transneft	100
OOO Transneftburservice (in liquidation)	100
OOO Transpress	100
Pension Fund Transneft	100
OOO Transneftservice	100

All of the consolidated subsidiaries are incorporated in the Russian Federation, with the exception of Transneft UK Limited, which is incorporated in the United Kingdom. There were no material changes in the structure of the Group during the year ended 31 December 2000 or 1999.

Changes in 1999

During the year ended 31 December 1999, the acquisition of the remaining 24.5% of the ordinary shares of OAO Severniye MN, previously held by the Regional State Committee of the Komi Republic, can be summarised as follows:

Purchase consideration	699
Fair value of net assets acquired	(776)
Negative goodwill arising on acquisition	(77)

The negative goodwill has been included in the results of the year ended 31 December 1999, as there was no economic reason for its deferral. The net assets acquired, stated in accordance with RAR, were adjusted for the most significant different accounting policies used in preparing financial statements in accordance with IAS to derive the above figure.

The acquisition of the shares in OAO Severniye MN had no significant effect on the Group's financial position or on its results of operations in the year ended 31 December 1999.

Changes in 2000 and 2001

In July 2000, Pension Fund Transneft was established and eventually will be responsible for funds contributed to a non-state pension scheme, the contributions and benefits of which have not yet been finalised.

OOO Transneftservice was incorporated in January 2001 to provide construction and maintenance services to Group companies, and OOO Transneftburservice is in the process of liquidation.

In October 2000, the Group acquired 65% of ZAO Black Sea Shipping, incorporated in the Russian Federation, which provides shipping services to exporters of crude oil and other products from the Black Sea Port of Novorossiysk (see note 20.3).

19 CONTINGENT LIABILITIES, COMMITMENTS AND OTHER RISKS

CONTINGENT LIABILITIES

Legal proceedings

19.1 The Group is a party to certain legal proceedings arising in the ordinary course of business. Also, the Group is subject to various environmental laws regarding handling, storage, and disposal of certain products and is subject to regulation by various governmental authorities. In the opinion of management, there are no current legal proceedings or other claims outstanding which could have a material adverse effect on the results of operations or financial position of the Group.

The dividend rights of the preferred shares (as described in note 10) were amended in a resolution of the Annual General Meeting held on 25 June 1999, and the necessary amendments to the charter document were registered on 30 August 1999. These amendments have been nullified by a decision of the Federal Arbitration Court of the Moscow Region dated 21 January 2001. The Company has submitted the case for review by the Supreme Arbitration Court.

As a result of the above mentioned decision of the Court, the number of shares participating in earnings has been revised to include preferred shares for the year ended 31 December 2000. In addition, these consolidated financial statements contain a liability included in trade and other payables for a dividend on preferred shares of approximately RR 0.78 million for the year ended 31 December 1999 calculated on the basis of the resolution of the Annual General Meeting dated 25 June 1999.

One of the Group's customers has initiated a claim in the Tyumen Region Court contending that the Government Order N476 dated 30 April 1999, which established the investment tariff (Note 16), was unlawful. The Tyumen Region Court upheld the customer's claim against the Government. Subsequently, the Government has appealed the decision of the court, stating that the claim is without merit. Management believes the claim will not result in any material loss to the Group, and therefore no provision has been made for any losses in these financial statements.

Taxation

19.2 Russian tax legislation is subject to varying interpretations and frequent changes. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activities of the Group may not coincide with that of management. As a result, transactions may be challenged by tax authorities and the Group may be assessed additional taxes, penalties and interest, which can be significant. The tax returns which have been submitted remain open for review by the tax and customs authorities for three years.

Financial guarantees

19.3 The Company had issued a guarantee valued at up to the equivalent of US$ 100 million in respect of the outstanding debt and interest obligations of FSUC All-Russian Television and Broadcasting Company which is valid until 31 December 2002.

19.4 Under a factoring agreement between one of the Group companies and OOO “Independent Development Bank”, the Group receives settlement of certain amount receivable from the Bank with recource. In the event that these receipts, amounting to RR 578 million at 31 December 2000 are not paid by the debtor to the Bank within the agreed period, the Group would have to repay this liability to the Bank and collect the outstanding amount from the debtor.

COMMITMENTS

19.4 In the normal course of business, the Group has entered into contracts for the purchase of property, plant and equipment and amounts contracted for but not reflected in the consolidated financial statements as at 31 December 2000 were approximately RR 8,353 million (31 December 1999 - RR 3,182 million). In addition to these contractual commitments, the Board of Directors of the Group has approved a capital expenditure budget of approximately RR 10,673 million for the year ending 31 December 2001 (year ended 31 December 2000 – RR 14,005 million).

OTHER RISKS

Government and tariffs

19.5 The Government of the Russian Federation, through the State Property Committee, owns 100% of the issued ordinary shares of the Company and controls most of its operations through the Ministry of Energy. The Government also appoints the members of the Federal Energy Commission, which is charged inter alia with the periodic review of tariff rates and structures which affect capital expenditure programs.

Operating environment of the Company

19.6 The economy of the Russian Federation continues to display characteristics of an emerging market. These characteristics include, but are not limited to, the existence of:

- a currency that is not freely convertible outside of the country;
- extensive currency controls;
- a low level of liquidity in the public and private debt and equity markets; and
- high inflation.

The prospects for future economic stability in the Russian Federation are largely dependent upon the effectiveness of economic measures undertaken by the government, together with legal, regulatory, and political developments.

Operations and environmental matters

19.7 Due to the capital intensive nature of the industry, the Group is subject to physical risks of various kinds. The nature and frequency of these developments and events associated with these risks as well as their effect on future operations and earnings are not predictable.

19.8 Potential liabilities which might arise as a result of stricter enforcement of existing environmental regulations, civil litigation or changes in legislation or regulation cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that all significant liabilities for environmental restoration have been accrued in the consolidated financial statements.

Insurance risks

19.9 The Group insures the majority of its fire and environmental risks with Russian reinsurers through its subsidiary, Transneft Insurance Company.

(in millions of Russian roubles)

20 RELATED PARTIES AND DIRECTORS' COMPENSATION

IAS 24 "Related Party Disclosures" specifically excludes government-controlled entities from the definition of related parties, and therefore transactions between, and balances due to or from, entities under government or other state control and the Group companies are not detailed in this note.

Related party transactions

The amounts included in the consolidated statement of income in respect of provisions against amounts due from and income or expenses attributable to transactions with related parties are as follows:

	Reference	Year ended 31 December 2000	Year ended 31 December 1999
Kemerovo Region Administration (included in other operating income/(expenses))	20.1	55	-
Transneft Insurance Company (included in operating expenses)	20.2	345	179
ZAO Black Sea Shipping (included in operating expenses)	20.3	32	-
International Industrial Company (included in net other operating income/(expenses))	20.4	-	(252)
		432	(73)

20.1 During the year ended 31 December 2000, the Company made a provision against an overdue advance of RR 55 million to the Kemerovo Region Administration.

20.2 The consolidated statement of income for the year ended 31 December 2000 includes insurance expense amounting to RR 345 million attributable to policies issued by Transneft Insurance Company which are priced at market rates (1999 – RR 179 million). This subsidiary is not consolidated on the basis that it is not material in the context of the Group.

20.3 In October 2000, the Group acquired a 65% interest in ZAO Black Sea Shipping, which provides shipping services to oil and other exporters at the port of Novorossiysk, including to OAO Chernomortransneft under a contract effective from 1 July 2000. This subsidiary is not consolidated on the basis that it is not material in the context of the Group. The amount received by ZAO Black Sea Shipping from the Group for such services in the year ended 31 December 2000 was RR 32 million.

20.4 An amount of RR 252 million due from one of the Group's main customers was assigned to International Industrial Company and this amount was provided for in full in the consolidated statement of income for the year ended 31 December 1998, but subsequently recovered and therefore reversed in 1999.

Directors' compensation

Compensation paid to directors and senior management for their services in full or part time executive management positions comprises a contractual salary, non-cash benefits, and a performance bonus depending on results for the year according to Russian statutory financial statements.

Total compensation of the above nature paid to directors for their services in the year ended 31 December 2000, included in staff costs in note 17, amounted to RR 82 million (1999 – RR 143 million).

21 FINANCIAL INSTRUMENTS

Foreign exchange

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble or the US dollar, and it does not use foreign exchange or forward contracts. At 31 December 2000, prepayments and advances paid for imported equipment and bank balances in US dollars amounted to RR 1,982 million (31 December 1999 – RR 4,793 million) and RR 1,471 million (31 December 1999 – RR 941 million), respectively, translated at the official rouble exchange rate used by Central Bank of Russian Federation.

Interest rates

The Group obtains borrowings from and deposits surpluses with banks at current market interest rates, and does not use any hedging instruments to manage its exposure to changes in interest rates.

Credit risk

The Group’s policy is to place cash and cash equivalents with banks in a manner which minimises the risk of default. The banks are listed in note 9.

The Group does not hold or issue financial instruments for trading purposes. Its trade accounts receivable are unsecured, and the largest single credit exposure (based on combined figures of accounts receivable, notes receivable and advances due from the same group of entities) at 31 December 2000 was RR 966 million (31 December 1999 – RR 3,379 million) advanced to an equipment manufacturer which is included in “assets under construction including prepayments” in property, plant and equipment.

Activities involving notes receivable and payable

The Group issued notes payable with a total value of RR 2,333 million during the year ended 31 December 2000 (year ended 31 December 1999 RR 16,369 million) to provide short-term working capital, usually in the form of cash, or in settlement of current liabilities. These notes were generally unsecured, non-interest bearing and were repayable six months from the date of issuance.

Included in the above figures are notes payable issued without receiving cash at the time of their issue, and which effectively represent loans to the beneficiaries supported by corresponding notes receivable. The corresponding notes receivable were generally unsecured, non-interest bearing and were due in twelve equal monthly instalments from the date of their issuance. The outstanding amounts of such notes receivable at 31 December 2000 was RR nil (31 December 1999 – RR 497 million).

Fair values of financial assets and liabilities

The fair values of the financial assets and liabilities at 31 December 2000 and 1999 were approximately equal to their carrying values.