TATNEFT

CONSOLIDATED FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2003

ERNST & YOUNG

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of OJSC Tatneft

We have audited the accompanying consolidated balance sheet of OJSC Tatneft and its subsidiaries (jointly referred to as the "Company") as of December 31, 2003 and the related consolidated statements of operations and comprehensive income, shareholders' equity, and cash flows for the year ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of OJSC Tatneft and its subsidiaries at December 31, 2003 and the consolidated results of their operations and their cash flows for the year ended December 31, 2003 in conformity with U.S. generally accepted accounting principles.

As discussed in Notes 3 and 11 to the consolidated financial statements, in 2003 the Company adopted Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations, effective January 1, 2003.

Ernst & Young (CIS) Limited

Moscow, Russia

July 2, 2005

TATNEFT
Consolidated Balance Sheets
(in millions of Russian Roubles)

	Notes	At December 31, 2003	At December 31, 2002
Assets			**(restated)**
Cash and cash equivalents	5	8,450	7,070
Restricted cash	5	300	40
Accounts receivable, net	6	13,297	13,657
Due from related parties	19	6,631	4,105
Short-term investments	7	3,223	3,477
Current portion of loans receivable and advances, net	10	14,042	9,652
Inventories, net	8	10,051	9,962
Prepaid expenses and other current assets	9	17,506	16,940
Total current assets		**73,500**	**64,903**
Restricted cash	5	1,742	1,756
Long-term loans receivable and advances, net	10	6,746	2,978
Long-term investments	7	3,721	4,203
Property, plant and equipment, net	11	177,008	152,448
Total assets		**262,717**	**226,288**
Liabilities and shareholders' equity			
Short-term debt and current portion of long-term debt	12	13,213	16,618
Notes payable	13	6,948	3,482
Banking customer deposits	13	16,665	11,408
Trade accounts payable		2,948	6,370
Due to related parties	19	1,034	762
Other accounts payable and accrued liabilities	14	5,427	5,571
Current deferred tax liability	15	196	170
Capital lease obligations to related parties	11,19	643	-
Taxes payable		7,159	3,759
Total current liabilities		**54,233**	**48,140**
Long-term debt, net of current portion	12	12,796	14,622
Notes payable	13	1,485	866
Banking customer deposits	13	1,337	1,152
Asset retirement obligations, net of current portion	11	16,955	-
Deferred tax liability	15	21,271	21,287
Capital lease obligations to related parties, net of current portion	11,19	359	-
Total liabilities		**108,436**	**86,067**
Minority interest		**5,101**	**5,069**
Shareholders' equity			
Preferred shares (authorized and issued at December 31, 2003 and 2002 – 147,508,500 shares; nominal value at December 31, 2003 and 2002 - RR1.00)	16	148	148
Common shares (authorized and issued at December 31, 2003 and 2002 - 2,178,690,700 shares; nominal value at December 31, 2003 and 2002 - RR1.00)	16	2,179	2,179
Additional paid-in capital	16	89,516	88,863
Accumulated other comprehensive income		189	176
Retained earnings		62,291	47,776
Less: Common shares held in treasury, at cost (191,430,258 shares and 200,288,083 shares at December 31, 2003 and 2002, respectively)		(5,143)	(3,990)
Total shareholders' equity		**149,180**	**135,152**
Total liabilities and shareholders' equity		**262,717**	**226,288**

(in millions of Russian Roubles)

	Notes	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
			(restated)	(restated)
Sales and other operating revenues	18	**155,818**	**146,328**	**156,861**
Costs and other deductions				
Operating		31,799	36,389	31,297
Purchased oil and refined products		28,997	28,372	34,104
Exploration		812	463	839
Transportation		7,635	5,683	5,183
Selling, general and administrative		15,499	16,031	17,282
Bad debt charges and credits, net		(262)	(261)	1,027
Depreciation, depletion and amortization	18	8,850	7,541	6,139
Loss on disposals of property, plant and equipment and impairment of investments	10,11	2,325	851	2,502
Taxes other than income taxes	15	43,378	31,988	33,373
Maintenance of social infrastructure	11	279	199	491
Transfer of social assets	11	2,162	1,293	593
Total costs and other deductions		**141,474**	**128,549**	**132,830**
Other income (expenses)				
Earnings from equity investments	7	101	148	501
Foreign exchange loss		(225)	(1,042)	(851)
Monetary gain	2	-	871	1,764
Interest income		303	804	1,517
Interest expense		(1,827)	(2,855)	(2,875)
Other income, net		1,961	3,599	511
Total other income		**313**	**1,525**	**567**
Income before income taxes, minority interest and cumulative effect of change in accounting principle		**14,657**	**19,304**	**24,598**
Income taxes				
Current		(6,070)	(4,743)	(7,072)
Deferred benefit / (expense)		1,488	(620)	8,316
Total income tax (expense) / benefit	15	**(4,582)**	**(5,363)**	**1,244**
Income before minority interest and cumulative effect of change in accounting principle		**10,075**	**13,941**	**25,842**
Minority interest benefit / (expense)		63	(471)	(1,698)
Income before cumulative effect of change in accounting principle		**10,138**	**13,470**	**24,144**
Cumulative effect of change in accounting principle, net of RR 1,498 million tax	11	4,742	-	-
Net income		**14,880**	**13,470**	**24,144**
Foreign currency translation adjustments		3	(20)	163
Unrealized holding gains on available-for-sale securities, net of tax		43	33	2,329
Less: transfer of realized gains included in net income, net of tax		(33)	(2,981)	(622)
Comprehensive income		**14,893**	**10,502**	**26,014**

(in millions of Russian Roubles, except per share information)

	Notes	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
			(restated)	(restated)
Basic net income per share before cumulative effect of changes in accounting principle (RR)	16			
Common		4.70	6.24	10.94
Preferred		5.59	7.12	11.05
Cumulative effect of changes in accounting principle (RR)				
Common		2.23	-	-
Preferred		2.23	-	-
Basic net income per share (RR)				
Common		6.93	6.24	10.94
Preferred		7.82	7.12	11.05
Diluted net income per share before cumulative effect of changes in accounting principle (RR)	16			
Common		4.68	6.23	10.92
Preferred		5.58	7.11	11.02
Cumulative effect of changes in accounting principle (RR)				
Common		2.22	-	-
Preferred		2.22	-	-
Diluted net income per share (RR)				
Common		6.90	6.23	10.92
Preferred		7.80	7.11	11.02
Weighted average common shares outstanding (millions of shares)	16			
Basic		1,983	1,991	2,057
Diluted		1,988	1,993	2,062
Weighted average preferred shares outstanding (millions of shares)	16			
Basic		148	148	148
Diluted		148	148	148

TATNEFT
Consolidated Statements of Cash Flows
(in millions of Russian Roubles)

	Notes	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
			(restated)	(restated)
Operating activities				
Net income		14,880	13,470	24,144
Adjustments:				
Cumulative effect of change in accounting principle		(4,742)	-	-
Minority interest		(63)	471	1,698
Depreciation, depletion and amortization	18	8,850	7,541	6,139
Net barter settlements	5	(1,126)	(2,425)	(4,227)
Deferred income tax expense (benefit)		(1,488)	620	(8,316)
Disposals and impairments		2,325	851	2,502
Net realized (gain)/loss on available-for-sale securities		10	(3,408)	(1,003)
Effects of foreign exchange		(1,527)	869	1,638
Monetary gain		-	(871)	(1,764)
Undistributed earnings of equity investments		(71)	(121)	(381)
Transfer of social assets		2,162	1,293	593
Other		(1,014)	(383)	460
Changes in operational working capital, excluding cash:				
Accounts receivable		(3,623)	6,021	(1,497)
Inventories		212	1,946	1,338
Prepaid expenses and other current assets		(996)	(1,686)	(4,010)
Trading securities		(193)	100	(1,867)
Loans receivable		(8,143)	(5,615)	(6,406)
Notes receivable		1,093	(4,425)	(472)
Trade accounts payable		(3,576)	(2,662)	1,052
Other accounts payable and accrued liabilities		10,079	664	7,418
Taxes payable		3,372	(2,097)	(1,780)
Net cash provided by operating activities		**16,421**	**10,153**	**15,259**
Investing activities				
Additions to property, plant and equipment		(12,679)	(13,100)	(20,583)
Proceeds from disposals of property, plant and equipment		1,147	109	142
Proceeds from disposal/ maturity of investments		1,943	6,272	2,805
Purchase of investments		(779)	(1,681)	(636)
Change in restricted cash		(246)	398	760
Net cash used for investing activities		**(10,614)**	**(8,002)**	**(17,512)**

(in millions of Russian Roubles)

	Notes	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
			(restated)	(restated)
Financing activities				
Proceeds from issuance of debt		39,468	40,840	25,019
Repayment of debt		(42,788)	(39,698)	(19,215)
Repayment of capital lease obligations		(1,221)	-	-
Dividends paid		(354)	(401)	(690)
Purchase of treasury shares		(5,425)	(1,523)	(2,119)
Proceeds from sale of treasury shares		5,495	1,107	345
Proceeds from issuance of shares by subsidiaries		401	-	684
Net cash provided by (used in) financing activities		**(4,424)**	**325**	**4,024**
Effect of foreign exchange on cash and cash equivalents		(3)	10	(37)
Effect of inflation accounting		-	(288)	(393)
Net change in cash and cash equivalents		**1,380**	**2,198**	**1,341**
Cash and cash equivalents at beginning of period		7,070	4,872	3,531
Cash and cash equivalents at end of period		**8,450**	**7,070**	**4,872**

TATNEFT
Consolidated Statements of Shareholders' Equity
(in millions of Russian Roubles)

	2003		2002		2001	
	Shares	Amount	Shares	Amount	Shares	Amount
				(restated)		(restated)
Preferred shares:						
Balance at January 1 and December 31 (shares in thousands)	147,509	148	147,509	148	147,509	148
Common shares:						
Balance at January 1 and December 31 (shares in thousands)	2,178,691	2,179	2,178,691	2,179	2,178,691	2,179
Treasury shares, at cost:						
Balance at January 1	200,288	(3,990)	176,133	(2,511)	66,575	(787)
Purchases	196,452	(5,995)	195,659	(5,083)	131,889	(2,119)
Sales	(205,310)	4,842	(171,504)	3,604	(22,331)	395
Balance at December 31 (shares in thousands)	191,430	(5,143)	200,288	(3,990)	176,133	(2,511)
Additional paid-in capital						
Balance at January 1		88,863		89,026		88,863
Stock-based compensation		-		-		163
Stock-options redeemed		-		(163)		-
Treasury share transactions		653		-		-
Balance at December 31		89,516		88,863		89,026
Accumulated other comprehensive income						
Balance at January 1		176		3,144		1,274
Foreign currency translation adjustments		3		(20)		163
Unrealized holding gains on available-for-sale securities, net of tax		43		33		2,329
Transfer of realized gains included in net income, net of tax		(33)		(2,981)		(622)
Balance at December 31		189		176		3,144
Retained earnings						
Balance at January 1		**51,002**		**36,098**		**12,104**
The cumulative effect on prior years of prior year adjustments (see Note 4)		(3,226)		(903)		(697)
Balance at January 1, as adjusted		**47,776**		**35,195**		**11,407**
Net income, as adjusted (see Note 4)		14,880		13,470		24,144
Dividends		(365)		(387)		(306)
Treasury share transactions		-		(502)		(50)
Balance at December 31		**62,291**		**47,776**		**35,195**
Total shareholders' equity at December 31		**149,180**		**135,152**		**127,181**

Note 1: Organization

OAO Tatneft (the "Company") and its subsidiaries (jointly referred to as "the Group") are engaged in crude oil exploration, development and production principally in the Republic of Tatarstan ("Tatarstan"), an autonomous republic within the Russian Federation. The Group also engages in refining and marketing of crude oil and refined products and petrochemical and banking activities, as further described in Note 18. The Group's banking activities comprise the operations of Zenit Bank and Devon Credit Bank.

The Company was incorporated as an open joint stock company effective January 1, 1994 (the "privatization date") pursuant to the approval of the State Property Management Committee of the Republic of Tatarstan (the "Government"). All assets and liabilities previously managed by the production association Tatneft, Bugulminsky Mechanical Plant, Menzelinsky Exploratory Drilling Department and Bavlinsky Drilling Department were transferred to the Company at their book value at the privatization date in accordance with Decree No. 1403 on Privatization and Restructuring of Enterprises and Corporations into Joint-Stock Companies. Such transfers are considered transfers between entities under common control at the privatization date, and have been recorded at book value.

At December 31, 2003, the Government held 33% of the common shares of the Company. As further described in Note 16, the Government owns one "Golden Share" which carries the right to veto certain decisions taken at meetings of the shareholders and the Board of Directors. The Government of Tatarstan is able to exercise significant influence through its ownership interest in the Company, its legislative, taxation and regulatory powers, its representation on the Board of Directors and informal influence. The Government has used its influence in the past to facilitate actions that may not maximize shareholder value, such as maintaining employment levels, increasing expenditure on social assets, selling oil to certain customers, transferring exploration or production licenses to small Tatarstan oil companies (including companies not affiliated with the Group), acquiring specified companies or taking actions to raise funds for the benefit of Tatarstan (see Notes 9, 10, 11, 15, 16, 19, 21 and 22).

The Government of Tatarstan controls a number of the Group's suppliers, such as OAO Tatenergo, the supplier of electricity to the Group, and a number of the Group's ultimate customers, such as OAO Nizhnekamskneftekhim ("Nizhnekamskneftekhim"), the principal petrochemical company in Tatarstan. Consequently, the Group may be subject to pressures to enter into transactions that we might not otherwise contemplate with suppliers and contractors controlled by the Government. Related party transactions are further disclosed in Note 19.

Note 2: Basis of Presentation

The Group maintains its accounting records and prepares its statutory financial statements principally in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR"). The accompanying financial statements have been prepared from these accounting records and adjusted as necessary to comply with accounting principles generally accepted in the United States of America ("US GAAP"). The principal differences between RAR and US GAAP relate to: (1) revenue recognition; (2) valuation and depreciation of property, plant and equipment; (3) foreign currency translation; (4) deferred income taxes; (5) valuation allowances for unrecoverable assets; (6) capital leases; (7) stock option transactions; and (8) consolidation and accounting for subsidiaries and equity investees.

Use of estimates in the preparation of financial statements. The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosures of contingent assets and liabilities. While management uses its best estimates and judgments, actual results could differ from those estimates and assumption used. Among the estimates made by the management are: assets valuation allowances, depreciable lives, oil and gas reserves, dismantling costs and income taxes.

Foreign currency transactions and translation. The functional currency of the Group except for subsidiaries located outside of the Russian Federation is the Russian Rouble because the majority of its revenues, costs, property and equipment purchased, debt and trade liabilities are either priced, incurred, payable or otherwise measured in Russian Roubles. Accordingly, transactions and balances not already measured in Russian Roubles (primarily US Dollars) have been re-measured into Russian Roubles in accordance with the relevant provisions of US Statement of Financial Accounting Standards ("SFAS") No. 52, *"Foreign Currency Translation"*.

Under SFAS No. 52, revenues, costs, capital and non-monetary assets and liabilities are translated at historical exchange rates prevailing on the transaction dates. Monetary assets and liabilities are translated at exchange rates prevailing on the balance sheet date. Exchange gains and losses arising from re-measurement of monetary assets and liabilities that are not denominated in Russian Roubles are credited or charged to operations.

Note 2: Basis of Presentation (continued)

For operations of the subsidiaries located outside of the Russian Federation, that use primarily US Dollars as the functional currency, adjustments resulting from translating foreign functional currency assets and liabilities into Russian Roubles are recorded in a separate component of shareholders' equity entitled accumulated other comprehensive income. Gains or losses resulting from transactions in other than the functional currency are reflected in net income.

Exchange rates, restrictions and controls. At present, the Russian Rouble is not a fully convertible currency outside of the Russian Federation and, further, the Company is required to sell up to 50% (25% from July 9, 2003) of its hard currency earnings for Russian Roubles. Within the Russian Federation, official exchange rates are determined daily by the Central Bank of Russia ("CBR"). Market rates may differ from the official rates but the differences are, generally, within narrow parameters monitored by the CBR. Accordingly, the translation of foreign currency denominated assets and liabilities into Russian Roubles does not indicate that the Group could realize or settle, in Russian Roubles, the reported values of these assets and liabilities. The official rate of exchange of the Russian Rouble ("RR") to the US Dollar ("US $") at December 31, 2003 and 2002 was RR 29.45 and RR 31.78 to US $1.00, respectively.

Inflation accounting. Prior to January 1, 2003 the adjustments and reclassifications made to statutory records for the purpose of US GAAP presentation included the restatement of balances and transactions for the changes in the general purchasing power of the RR in accordance with Accounting Principles Board Statement No. 3, "*Financial Statements Restated for General Price-Level Changes"* ("APB 3").

Corresponding figures for the year ended December 31, 2002, were restated for the changes in the general purchasing power of the RR at December 31, 2002. The restatement was calculated using the conversion factors derived from the Russian Federation Consumer Price Index, a historical price index published by the Russian State Committee on Statistics ("Goskomstat" prior to October 1999 and "Russian Statistics Agency" since October 1999), and from indices obtained from other sources for years prior to 1992.

The main guidelines followed in restating the corresponding figures were:

- All corresponding amounts were stated in terms of the measuring unit current at December 31, 2002;
- Monetary assets and liabilities held at December 31, 2002 were not restated because they were already expressed in terms of the monetary unit current at December 31, 2002.
- Non-monetary assets and liabilities (those balance sheet items that were not expressed in terms of the monetary unit current at December 31, 2002) and components of shareholders' equity were restated from their historical cost by applying the change in the general price index from the date the non-monetary item originated to December 31, 2002;
- All items in the statement of operations and cash flows were restated by applying the change in the general price index from the dates when the items were initially transacted to December 31, 2002.
- Gains or losses that arose as a result of holding monetary assets and liabilities for the reporting year ended December 31, 2002 were included in the statement of operations as a monetary gain or loss.

On November 25, 2002, the International Practices Task Force of the American Institute of Certified Public Accountants concluded that the Russian Federation would no longer be considered highly inflationary effective January 1, 2003. Accordingly, no restatement was made in the consolidated financial statements of the Group for the years subsequent to January 1, 2003 and the amounts expressed in the measuring unit at December 31, 2002 are treated as the basis for the carrying amounts in these financial statements.

Barter transactions. Transactions settled by barter are included in the accompanying consolidated balance sheets and statements of operations on the same basis as cash transactions.

Barter transactions relate to sales of crude oil and refined products and are generally either in the form of direct settlement by crude oil and refined products to the final customer, or through a chain of non-cash transactions involving several companies. In such cases, both sales and purchases are recorded as a result of the barter transaction. Barter sales are recognized at the fair value as disclosed in Note 3 "Non-monetary transactions".

Reclassifications. Certain reclassifications in the consolidated financial statements as of and for the years ended December 31, 2002 and 2001 have been made to conform with the current year's presentation; such reclassifications have no effect on net income or shareholders' equity.

Amounts due to and from related parties were disclosed separately in the consolidated balance sheet. Certain restricted cash balances were reclassified from non-current assets to current assets. Certain prepaid expenses and other current assets were reclassified to long-term loans receivable and advances.

Note 2: Basis of Presentation (continued)

Net banking interest income previously included within other income in the consolidated statement of operations and comprehensive income was reclassified to sales and other operating revenues. Bad debt charges and write-offs previously included within selling, general and administrative expenses were disclosed separately in the consolidated statement of operations and comprehensive income.

Principles of consolidation and long-term investments. The accompanying consolidated financial statements include the operations of all entities that the Group controls through direct or indirect ownership of the voting stock (generally more than 50 percent of the voting stock). Joint ventures and affiliates in which the Group has significant influence but not control (generally 20 percent to 50 percent of the voting stock) are accounted for using the equity method. Intercompany transactions and accounts are eliminated on consolidation. Other long-term investments are carried at cost and adjusted for estimated impairment. The Group reviews equity method investments for impairment whenever events or changes in circumstances indicate that an other than temporary decline in value has occurred. The amount of the impairment is based on quoted market prices, where available, or other valuation techniques, including discounted cash flows.

Note 3: Summary of Significant Accounting Policies

Cash equivalents. Cash equivalents are highly liquid short-term investments that are readily convertible to known amounts of cash and have original maturities within three months from their date of purchase. They are carried at cost plus accrued interest, which approximate fair value.

Inventories. Inventories of crude oil, refined oil products, materials and supplies, and finished goods are valued at the lower of cost or net realizable value. For inventories valued at cost, the Group uses the weighted-average-cost method. Costs include both direct and indirect expenditures incurred in bringing an item or product to its existing condition and location, but not unusual/non-recurring costs or research and development costs.

Short-term investments. Short-term investments consist of debt and equity securities classified as available-for-sale or trading. Securities are classified as available-for-sale when, in management's judgment, they may be sold in response to or in anticipation of changes in market conditions. Available-for-sale securities are carried at estimated fair values on the consolidated balance sheet. Unrealized gains and losses on available-for-sale securities are reported net as increases or decreases to accumulated other comprehensive income. The specific identification method is used to determine realized gains and losses on available-for-sale securities.

Securities classified as trading are bought and held principally for the purpose of selling them in the near term. Trading securities are carried at fair value on the consolidated balance sheet. In determining fair value, trading securities are valued at the last trade price if quoted on an exchange or, if traded over-the-counter, at the last bid price. Unrealized and realized gains and losses on trading securities are included in other income of the consolidated statements of operations and comprehensive income.

If the decline in fair value of an investment below accounting basis is other-than-temporary, the carrying value of the securities is reduced and a loss in the amount of any such decline is recorded. No such reductions have been required during the past three years.

Sale and repurchase agreements and lending of securities. Sale and repurchase agreements are treated as secured financing transactions. Securities sold under sale and repurchase agreements are included in trading securities. The corresponding liability is presented within short-term and long-term debt as well as banking customer deposits. Securities purchased under agreements to resell ("reverse repurchase") are recorded as loans receivable and advances. The difference between the sale and repurchase prices is treated as interest and recognized over the life of the repurchase agreements using the effective interest method.

Securities lent to counterparts are retained in the consolidated financial statements. Securities borrowed are not recognized in the consolidated financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded within gains less losses arising from trading securities in the consolidated statement of operations and comprehensive income. The obligation to return them is recorded at fair value as a trading liability.

Trade accounts receivable and allowances for bad debts. Trade accounts receivable are stated at their principal amounts outstanding net of allowances for bad debts. Specific allowances are recorded against trade receivables whose recovery or collection has been identified as doubtful. An estimated allowance is recorded against trade receivables which are inherent in the portfolio but which at the date of preparing the financial statements have not been specifically identified, as doubtful. Estimates of allowances require the exercise of judgment and the use of assumptions.

Note 3: Summary of Significant Accounting Policies (continued)

Loans receivable and allowances for impairment. Loans originated by the Group by providing money directly to the borrower or to a sub-participation agent at draw down are carried at amortized cost less allowance for loan impairment. Loans are recognized when cash is advanced to borrowers.

The allowance is equal to the difference between the carrying amount and estimated recoverable amount, calculated as the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted based on the loan's interest rate at inception.

The allowance for loan impairment also covers losses where there is objective evidence that probable losses are present in components of the loan portfolio at the balance sheet date. These have been estimated based upon historical patterns of losses in each component and the credit ratings assigned to the borrowers, and reflect the current economic environment in which the borrowers operate.

When a loan is uncollectible, it is written off against the related allowance for loan impairment. Such loans are written off after the necessary legal procedures have been completed and the amount of the loss has been determined. Recoveries of amounts previously written off are credited to the related allowance for impairment.

If the required allowance for loan impairment subsequently decreases due to an event occurring after the write-down, the release of the allowance is credited to other income line in the consolidated statements of operations and comprehensive income.

Oil and gas exploration and development cost. Oil and gas exploration and production activities are accounted for using the successful efforts method whereby costs of acquiring unproved and proved oil and gas property as well as costs of drilling and equipping productive wells, including development dry holes, and related production facilities are capitalized. Exploration expenses, including geological and geophysical expenses and the costs of carrying and retaining undeveloped properties, are expensed as incurred. The costs of exploratory wells that find oil and gas reserves are capitalized pending determination of whether proved reserves have been found. If proved reserves are not found exploratory well costs are expensed. In an area requiring a major capital expenditure before production can begin, an exploratory well remains capitalized if sufficient reserves are discovered to justify its completion as a production well, and additional exploration drilling is underway or firmly planned. The Group does not capitalize the costs of other exploratory wells for more than one year unless proved reserves are found.

Impairment of long-lived assets. Long-lived assets, including proved oil and gas properties at a field level, are assessed for possible impairment in accordance with SFAS No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets"*. Properties, plant and equipment used in operations are assessed for impairment whenever events or changes in circumstances indicate that the carrying amounts may not be recovered. If the carrying amounts are not expected to be recovered by undiscounted pretax future cash flows, the assets are impaired and an impairment loss is recorded through additional amortization or depreciation provisions in the periods in which the determination of impairment is made. The amount of impairment is determined based on the estimated fair value of the assets determined by discounting anticipated future net cash flows or based on quoted market prices in active markets, if available. In the case of oil and gas fields, the net present value of future cash flows is based on management's best estimate of future prices, which is determined with reference to recent historical prices and published forward prices, applied to projected production volumes of individual fields and discounted at a rate commensurate with the risks involved. The projected production volumes represent reserves, including risk-adjusted probable reserves, expected to be produced based on a stipulated amount of capital expenditures. The production volumes, prices and timing of production are consistent with internal projections and other externally reported information. The price and cost outlook assumptions used in impairment reviews differ from the assumptions used in the Standardized Measure of Discounted Future Net Cash Flows Relating to Proved Oil and Gas Reserve Quantities. In that disclosure, SFAS No. 69, *"Disclosures about Oil and Gas Producing Activities"* requires the use of prices and costs at the balance sheet date, with no projection of future changes in those assumptions.

Individual assets are grouped for impairment purposes at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets - generally on a field-by-field basis for exploration and production assets, at an entire complex level for refining assets or at a site level for service stations. Long-lived assets committed by management for disposal within one year are accounted for at the lower of amortized cost or fair value, less cost to sell. Acquisition costs of unproved oil and gas properties are evaluated periodically and any impairment assessed is charged to expense.

(in millions of Russian Roubles)

Note 3: Summary of Significant Accounting Policies (continued)

Depreciation, depletion and amortization. The Group calculates depletion expense for acquisition costs of proved properties using the unit of production method over proved oil and gas reserves. Depreciation and depletion expense for oil and gas production equipment and wells is calculated using the unit of production method for each field over proved developed oil and gas reserves (see Note 11). Depreciation of all other plant and equipment is determined on the straight-line method based on estimated useful lives which are as follows:

	Years
Buildings and constructions	25 - 33
Machinery and equipment	5 - 15

Maintenance and repair. Maintenance and repairs, which are not significant improvements, are expensed when incurred.

Capitalized interest. Interest from external borrowings is capitalized on major projects with an expected total cost exceeding RR 100 million each and an expected construction period of one year or longer. Capitalized interest is added to the cost of the underlying asset and is amortized over the useful lives of the assets in the same manner as the underlying assets. Since there were no projects which qualified for interest capitalization, no interest was capitalized during the year ended December 31, 2003, 2002 or 2001.

Change in accounting principle of recognition and measurement of asset retirement obligations. Effective January 1, 2003, the Group adopted SFAS No. 143, "*Accounting for Asset Retirement Obligations*" ("SFAS 143"). This new statement applies to legal obligations associated with the retirement and removal of tangible long-lived assets. Following the requirements of SFAS 143 the Group recognizes a liability for the fair value of legally required asset retirement obligations associated with long-lived assets in the period in which the retirement obligations are incurred (typically when the asset is installed at the production location). The Group capitalizes the associated asset retirement costs as part of the carrying amount of the long-lived assets in accordance with SFAS 143. Legal obligations, if any, to retire refining and marketing, distribution and banking assets are generally not recognized because of the indeterminable settlement date of these obligations.

Through December 31, 2002, in accordance with SFAS No. 19, "*Financial Accounting and Reporting by Oil and Gas Producing Companies*" ("SFAS 19") the estimated undiscounted costs of dismantling and removing major oil and gas production and transportation facilities, including necessary site restoration, were accrued using the unit-of-production method. The change in accounting of asset retirement obligations was accounted for as a change in accounting principle. See Note 11 for additional information.

Property dispositions. When complete units of depreciable property are retired or sold, the asset cost and related accumulated depreciation are eliminated, with any gain or loss reflected in the consolidated statements of operations and comprehensive income. When less than complete units of depreciable property are disposed of or retired, the difference between asset cost and salvage value is charged or credited to accumulated depreciation.

Capital leases. Capital leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the interest charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liabilities. Interest charges are charged directly to the consolidated statements of operation and comprehensive income.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term unless the leased assets are capitalized by virtue of the terms of the lease agreement granting the Group with ownership rights over the leased assets by the end of the lease term or containing a bargain purchase option. In this case, capitalized assets are depreciated over the estimated useful life of the asset regardless of the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the assets are classified as operating leases. Operating lease payments are recognized as an expense in the consolidated statements of operation and comprehensive income on a straight-line basis over the lease term.

Environmental expenditures. Environmental expenditures are expensed or capitalized, depending upon their future economic benefit. Expenditures that relate to an existing condition caused by past operations, and do not have a future economic benefit, are expensed. Liabilities for these expenditures are recorded on an undiscounted basis when environmental assessments or cleanups are probable and the costs can be reasonably estimated.

Note 3: Summary of Significant Accounting Policies (continued)

Pension and post-employment benefits. The Group's mandatory contributions to the governmental and discretionary non-governmental defined contribution pension schemes are expensed when incurred. The amount of contributions, frequency of payments and other conditions of non-governmental pension plans are regulated by the "Statement of National non-governmental pension fund of OAO "Tatneft" and the contracts concluded between the Company or its subsidiaries and non-profit organization "National non-governmental pension fund". In accordance with these contracts the Group is committed to make certain contributions which are determined solely at the discretion of the Group's or its subsidiary's management but not less than the minimum annual payment regulated by current Russian legislation. In accordance with the provisions of collective agreements concluded on an annual basis between the Company or its subsidiaries and their employees the Group is obligated to pay certain post-employment benefits the amounts of which are either fixed or depend on the governmental pension amount or at the full discretion of the Group's management. In 2003, 2002 and 2001 the contributions to non-governmental pension plans and post-employment benefit payments were not material.

Revenue recognition. Revenues from the production and sale of crude oil, petroleum and chemical products and all other products are recognized when deliveries of products to final customers are made, title passes to the customer, collection is reasonably assured and sales price to final customers is fixed or determinable. Revenues include the sales portion of contracts involving purchases and sales necessary to reposition supply to address location or quality or grade requirements (e.g., when the Group repositions crude by entering into a contract with a counter party to sell crude in one location and purchase it in a different location) and sales related to purchase for resale activity.

Bank interest income and expense are recognized on an accrual basis calculated using the effective interest method. The recognition of contractual interest income is suspended when loans become overdue by more than ninety days or when management believes that interest is not collectible. When interest accruals are suspended, interest accrued in a prior year is charged against the allowance for loan impairment while interest accrued in the current year but unpaid is reversed and charged against interest income. Loans are returned to accrual status when, in management's judgment, the borrower's ability to make periodic interest and principal payments has improved and payments are made timely over an approximate six month period. Until the loan is returned to accrual status, payments by borrower are applied to loan principal. Bank interest is included on a net basis in sales and other operating revenues in the consolidated statement of operations and comprehensive income since management believes that the activities of the banks are one of the core activities of the Group.

Shipping and handling costs. Shipping and handling costs are included in Transportation expenses caption in the consolidated statements of operation and comprehensive income.

Non-monetary transactions. In accordance with Accounting Principles Board Statement No. 29, *"The Accounting for Non-monetary Transactions"* ("APB 29") such transactions are recorded based on the fair values of the assets (or services) involved which is the same basis as that used in monetary transactions. Thus, the cost of a non-monetary asset acquired in exchange for another non-monetary asset is the fair value of the asset surrendered to obtain it, and a gain or loss is recognized on the exchange if the carrying amount of the asset surrendered differs from its fair value. The fair value of the asset received should be used to measure the cost if it is more clearly evident than the fair value of the asset surrendered.

(in millions of Russian Roubles)

Note 3: Summary of Significant Accounting Policies (continued)

Stock-based compensation. At December 31, 2003, the Group has one stock-based employee compensation plan, which is described more fully in Note 17. The Group accounts for this plan under the recognition and measurement principles of Accounting Principles Board Statement No. 25, *"Accounting for Stock Issued to Employees"* ("APB 25"), and related Interpretations. The following table illustrates the effect on net income and income per share as if the Group applied the fair value recognition provisions of SFAS No. 123, *"Accounting for Stock-Based Compensation*" (SFAS 123), to stock-based employee compensation. The Group records compensation expense for non-vested common stock awards ratably over the vesting period.

	Year ended December 31, 2003	**Year ended December 31, 2002**	**Year ended December 31, 2001**
Income before cumulative effect of change in accounting principle, as reported	10,138	13,470	24,144
Add: Stock-based employee compensation expense (APB 25) included in reported net income, net of taxes	179	120	163
Deduct: Total stock-based employee compensation expense (SFAS 123) determined under fair value based method, net of taxes	(269)	(177)	(190)
Common share dividends	(217)	(239)	(271)
Preferred share dividends	(148)	(148)	(35)
Pro forma net income available to common and preferred shareholders, net of dividends	9,683	13,026	23,811
Net income per common share:			
Basic – as reported	4.70	6.24	10.94
Basic – pro forma	4.65	6.21	10.93
Diluted – as reported	4.68	6.23	10.92
Diluted – pro forma	4.64	6.20	10.91
Net income per preferred share:			
Basic – as reported	5.59	7.12	11.05
Basic – pro forma	5.54	7.09	11.04
Diluted – as reported	5.58	7.11	11.02
Diluted – pro forma	5.53	7.08	11.01

Income taxes. Deferred income tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates in the periods in which these temporary differences are expected to reverse. Valuation allowances are provided for deferred income tax assets when management believes that it is unlikely that the assets will be realized.

Minority interest. Minority interest represents the minority shareholders' proportionate share of the equity of the Group's subsidiaries. This has been calculated based upon the minority interest ownership percentage of these subsidiaries. The Company does not own any preference shares in subsidiaries.

Net income per share. Basic income per share is calculated using the two class method of computing income per share. Under this method, net income is reduced by the amount of dividends declared in the current period for each class of shares, and the remaining income is allocated to common and preferred shares to the extent that each class may share in income if all income for the period had been distributed. Diluted income per share reflects the potential dilution arising from options granted to senior managers and the Directors of the Group.

Note 3: Summary of Significant Accounting Policies (continued)

Treasury shares. Common shares of the Company owned by the Group at the balance sheet date are designated as treasury shares and are recorded at cost using the weighted-average method. Gains on the resale of treasury shares are credited to additional paid in capital whereas losses are charged to additional paid in capital to the extent that previous net gains from resale are included therein or otherwise to retained earnings.

Accounting for guarantees. The Group recognizes a liability for the fair value of the obligation it assumes under the guarantee in accordance with the provisions of Financial Accounting Standard Board ("FASB") issued Interpretation No. 45, *"Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others"* (FIN 45). The adoption of the provisions of FIN 45 did not have a material impact on the Group's results of operations, financial position or cash flow.

Recent accounting pronouncements:

Consolidation of Variable Interest Entities. In January 2003, the FASB issued Interpretation No. 46, "*Consolidation of Variable Interest Entities",* ("FIN 46") to expand existing accounting guidance and to establish standards for determining under what circumstances a variable interest ("VIE") should be consolidated with its primary beneficiary. FIN 46 also requires disclosure about VIEs that are not required to be consolidated but in which the reporting entity has a significant variable interest or about any potential VIEs when a reporting entity is unable to obtain the information necessary to confirm if this entity is a VIE or determine if a reporting entity is the primary beneficiary. In December 2003, the FASB revised certain implementation provision of FIN 46. The revised interpretation ("FIN 46R") substantially retained the requirements of immediate application of FIN 46 to VIEs created after January 31, 2003 or created before that date but which had significant modifications in terms of contracts or nature of transactions with a reporting entity subsequent to that date. With respect of older VIEs, the consolidation requirements under FIN 46R apply not later than for the first financial year or interim period ending after December 15, 2003, if such a VIE is a special-purpose entity ("SPE"), and no later than for the first financial year or interim period ending after March 15, 2004, if such a VIE is not an SPE.

In general, a VIE is a corporation, partnership, trust, or any other legal structure used for business purposes that either (a) does not have equity investors with voting rights or (b) has equity investors that do not provide sufficient financial resources for the entity to support its activities. FIN 46 requires a VIE to be consolidated by reporting entity if that entity is subject to a majority of the risk of loss from the VIE's activities, is entitled to receive a majority of the VIE's residual returns, or both (the entity required to consolidate VIE's is called the primary beneficiary). It also requires deconsolidation of a VIE if an entity is not the primary beneficiary of the VIE.

The Group has completed its analysis of compliance with the provisions of FIN 46 as revised by FIN 46R in respect of the existence of VIEs created after January 31, 2003 or VIEs created before that date but which had significant modifications in terms of contracts or nature of transactions with the Group subsequent to that date or VIEs which are SPEs. This analysis did not identify any significant impact of FIN 46 as revised by FIN 46R on the Group's consolidated financial statements as of and for the year ended December 31, 2003. The Group is still assessing the impact that FIN 46 as revised by FIN 46R may have on its consolidated financial statements for the periods commencing January 1, 2004.

Postretirement Benefits. In December 2003, the FASB revised and reissued SFAS No. 132 (revised 2003), *"Employers' Disclosures about Pensions and Other Postretirement Benefits-an amendment of FASB Statements No. 87, 88, and 106,"* which revises and requires additional disclosures about pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans required by previous Financial Accounting Board Standards. The Group adopted the provisions of this standard. Certain provisions of this Standard regarding disclosure of information about foreign plans and disclosure of estimated future benefit payments are not required until 2004. The adoption of the provisions applicable to 2003 did not have a material impact on the Group's results of operations, financial position or cash flow, nor will the adoption of the additional provisions in 2004 have a material impact on the Group's results of operations, financial position or cash flow.

Amendment to SFAS No. 133 on Derivative Instruments and Hedging Activities. In April 2003, the FASB issued SFAS No. 149, *"Amendment to Statement 133 on Derivative Instruments and Hedging Activities"* ("SFAS 149"). This statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133 *"Accounting for Derivative Instruments and Hedging Activities".* It is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. All provisions of the statement should be applied prospectively, except as stated further. Provisions related to SFAS 133 Implementation Issues that have been effective for fiscal quarters beginning prior to June 15, 2003, should continue to be applied in accordance with their respective dates. Rules related to forward purchases or sales of when-issued securities or other similar securities, should be also applied to existing contracts. The adoption of the provisions of SFAS 149 did not have a material impact on the Group's results of operations, financial position or cash flow.

Note 3: Summary of Significant Accounting Policies (continued)

Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity. In May 2003, the FASB issued SFAS No. 150, *"Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity"* ("SFAS 150"). This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). This statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. On November 7, 2003, the FASB issued FASB Staff Position No. FAS 150-3, which deferred certain provisions of SFAS 150. The adoption of the provisions of SFAS 150 and deferral of certain provisions did not have a material impact on the Group's results of operations, financial position or cash flow.

Stock-based compensation. On December 16, 2004, FASB issued SFAS No. 123 (revised 2004), *"Share Based Payment"* ("SFAS 123R"), which is a revision of SFAS 123. SFAS 123R supersedes APB 25 and amends Statement No. 95, "Statement of Cash Flows". SFAS 123R prescribes the accounting for a wide range of share-based compensation arrangements, including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans; pro forma disclosure is no longer permitted. The cost of the equity instruments is to be measured based on fair value of the instruments on the date they are granted (with certain exceptions) and is required to be recognized over the period during which the employees are required to provide services in exchange for the equity instruments. SFAS 123R is effective in the first interim or annual reporting period beginning after June 15, 2005.

SFAS 123R provides two alternatives for adoption: (1) a "modified prospective" method in which compensation cost is recognized for all awards granted subsequent to the effective date of this statement as well as for the unvested portion of awards outstanding as of the effective date and (2) a "modified retrospective" method which follows the approach in the "modified prospective" method, but also permits entities to restate prior periods to reflect compensation cost calculated under SFAS 123 for pro forma amounts disclosure. The Group plans to adopt SFAS 123R using the modified prospective method. The adoption of SFAS 123R is expected to have an impact on our results of operations. On March 30, 2005, the SEC released Staff Accounting Bulletin No. 107, "Share-Based Payment," ("SAB 107"), which expresses the views of the SEC staff regarding the application of SFAS 123R. The impact of adopting SFAS 123R and SAB 107 cannot be accurately estimated at this time, as it will depend on the amount of share based awards granted in future periods. However, had we adopted SFAS 123R and SAB 107 in a prior period, the impact would approximate the impact of SFAS 123 as described in the disclosure of pro forma net income and income per share in this Note to the consolidated financial statements.

Inventory costs. In November 2004, the FASB issued SFAS No. 151, "*Inventory Costs an amendment of ARB No. 43, Chapter 4"* ("SFAS 151"). SFAS 151 requires that items, such as idle facility expense, excessive spoilage, double freight, and re-handling costs, be recognized as a current-period charge. The provisions of SFAS 151 are effective for financial statements for fiscal years beginning after June 15, 2005. The Group is analyzing the provisions of this statement to determine the effects, if any, on the Group's results of operations, financial position or cash flow.

Nonmonetary exchanges of similar assets. In December 2004, the FASB issued SFAS No. 153, *"Exchanges of Nonmonetary Assets"* ("SFAS 153"). SFAS 153 addresses the measurement of exchanges of nonmonetary assets. The guidance in APB 29 is based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. The guidance in APB 29, however, included certain exceptions to that principle. SFAS 153 amends APB 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. A nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. The provisions of SFAS 153 are effective for financial statements for fiscal years beginning after June 15, 2005. The adoption of the provisions of SFAS 153 is not expected to have a material impact on the Group's results of operations, financial position or cash flow.

Note 3: Summary of Significant Accounting Policies (continued)

Accounting changes and error corrections. In May 2005, the FASB issued SFAS No. 154, *"Accounting changes and error corrections"* ("SFAS 154"). SFAS 154 replaces APB Opinion No. 20, *"Accounting Changes"* ("APB 20"), and SFAS No. 3, *"Reporting Changes in Interim Financial Statements"*, and changes the requirements for the accounting for and reporting of a change in accounting principle. SFAS 154 requires retrospective application to prior period's financial statements of all changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change, if a pronouncement which requires the change in accounting principle does not include specific transition provisions. SFAS 154 carries forward without change the guidance contained in APB 20 for reporting the correction of an error in previously issued financial statements and a change in accounting estimate. The adoption of the provisions of SFAS 154 is not expected to have a material impact on the Group's results of operations, financial position or cash flow.

Income per share calculation. In March 2004, the Emergency Issue Task Force ("EITF") reached a consensus on Issue 03-6, *"Participating Securities and the Two-Class Method under FASB Statement No. 128, Earnings per Share"*, that explained how to determine whether a security should be considered a "participating security" and how income should be allocated to a participating security when using the two-class method for computing basic income per share. The adoption of this standard which is effective for financial statements for fiscal periods beginning after March 31, 2004 is not expected to have a material impact on the Group's income per share calculation.

Discontinued operations. In November 2004, the EITF issued EITF No. 03-13, *"Applying the Conditions in Paragraph 42 of FASB Statement No. 144 in Determining Whether to Report Discontinued Operations"* ("EITF 03-13"). EITF 03-13 assists in the development of a model for evaluating (a) which cash flows are to be considered in determining whether cash flows have been or will be eliminated and (b) what types of continuing involvement constitute significant continuing involvement when determining whether the disposal or sale of a component of a business is to be accounted for as discontinued operations. The Group is analyzing the provisions of EITF 03-13 to determine the effects, if any, on the Group's results of operations, financial position or cash flow.

Conditional asset retirement obligations. In March 2005, the FASB issued Interpretation No. 47, *"Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143"* ("FIN 47"). This interpretation clarifies that an entity is required to recognize a liability for a legal obligation to perform asset retirement activities when the retirement is conditional on a future event if the liability's fair value can be reasonably estimated. The Group is analyzing the provisions of this interpretation to determine the effects, if any, on the Group's results of operations, financial position or cash flow.

Suspended well costs. In April 2005, the FASB issued FASB Staff Position FAS No. 19-1, *"Accounting for suspended well costs"* ("FSP FAS 19-1"). FSP FAS 19-1 amends SFAS 19 and applies to companies that follow the successful efforts method of accounting. FSP FAS 19-1 concludes that exploratory well costs should continue to be capitalized when the well has found a sufficient quantity of reserves to justify its completion as a producing well and an entity is making sufficient progress assessing the reserves and the economic and operating viability of the project. In addition FSP 19-1 requires certain disclosures to provide financial statement users information about management's evaluation of capitalized exploratory well costs. The provisions of FSP FAS 19-1 are effective for the first reporting period beginning after April 4, 2005 and should be applied prospectively to existing and newly capitalized exploratory well costs. The adoption of the provisions of FSP FAS 19-1 is not expected to have a material impact on the Group's results of operations, financial position or cash flow.

Implicit variable interest. In March 2005, the FASB issued FASB Staff Position FIN 46(R)-5, *"Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities*" ("FSP FIN 46(R)-5"). FSP FIN 46(R)-5 is applicable to both nonpublic and public reporting enterprises and addresses an issue that commonly arises in leasing arrangements among related parties, and in other types of arrangements involving related parties and unrelated parties. The Group is analyzing the provisions of this interpretation to determine the effects, if any, on the Group's results of operations, financial position or cash flow.

(in millions of Russian Roubles)

Note 4: Restatement of previously issued financial statements

The consolidated financial statements of the Group for the years ended December 31, 2002 and 2001 have been restated to reflect the effects of changes in calculation of deferred income taxes and depreciation, depletion and amortization as described below.

Deferred taxes

For the year ended December 31, 2002, as permitted by the legislation of the Russian Federation, the Group recorded a statutory revaluation of its property, plant and equipment tax base amounting to RR 11,893 million, and inappropriately recorded a decrease in its deferred tax liability of RR 2,854 million calculated on the entire amount of this statutory revaluation. Only a portion of this statutory revaluation, however, will be deductible in the future for tax purposes and as such the tax base of property, plant and equipment as of December 31, 2002 was overstated resulting in an understatement of deferred tax liabilities as of December 31, 2002 amounting to RR 2,158 million. Deferred tax liabilities as of December 31, 2002 and 2001 and the corresponding deferred tax expenses and benefits for the years then ended were also restated as a result of a restatement of property, plant and equipment, net of accumulated depreciation, depletion and amortization, as of December 31, 2002 and 2001 as discussed below in the amounts of RR 111 million and RR 50 million, respectively.

Depreciation, depletion and amortization calculation

The Group had been depleting oil and gas properties on a unit-of-production basis over total proved reserves, and not proved developed reserves, as required by US GAAP. The Group originally believed that the difference between the two classes of reserves was not material and that the impact on the calculation of depreciation, depletion and amortization would also not be material. As a result of a recalculation of depreciation, depletion and amortization using proved developed reserves, on a cumulative basis, the Group no longer believes that assumption to be appropriate. The cumulative effect of this adjustment to retain earnings as of December 31, 2000 was a decrease of RR 697 million.

The accompanying consolidated financial statements for the year ended December 31, 2002 and 2001 have been restated to adjust deferred income taxes for the non-deductible amount of the statutory revaluation and to adjust depreciation, depletion and amortization for the impact of using total proved reserves, instead of proved developed reserves as follows:

Year ended December 31, 2001	**As reported**	**As restated**
Deferred income tax benefit	8,205	8,316
Depreciation, depletion and amortization adjustments	(5,822)	(6,139)
Net income	24,350	24,144
Income per share:		
Basic		
Common	11.04	10.94
Preferred	11.14	11.05
Diluted		
Common	11.01	10.92
Preferred	11.11	11.02
Year ended December 31, 2002		
Deferred income tax benefit / (expenses)	1,488	(620)
Depreciation, depletion and amortization adjustments	(7,325)	(7,541)
Net income	15,793	13,470
Income per share:		
Basic		
Common	7.32	6.24
Preferred	8.20	7.12
Diluted		
Common	7.32	6.23
Preferred	8.20	7.11

(in millions of Russian Roubles)

Note 5: Cash and Cash Equivalents, Restricted Cash, and Cash Flow Information

The consolidated statements of cash flows provide information about changes in cash and cash equivalents. At December 31, 2003, 2002 and 2001, cash and cash equivalents of the Group include US Dollar denominated amounts of RR 2,888 million (US $98 million), RR 4,190 million (US $132 million) and RR 3,295 million (US $109 million), respectively. Short-term restricted cash is cash held in escrow accounts in the amount of RR 300 million and RR 40 million at December 31, 2003 and 2002, respectively. Long-term restricted cash primarily consists of mandatory deposits with the Central Bank of Russia and deposits with lending institutions. Deposits with lending institutions are held over the life of the respective loans. These deposits will unlikely become available to the Group in 2004.

Net cash provided by operating activities reflects payments of interest and income taxes as follows:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Interest paid	1,796	2,908	3,168
Income taxes paid	5,932	5,360	8,419

Non-cash sales. Non-cash sales for the years ended December 31, 2003, 2002 and 2001 totalled RR 4,188 million, RR 6,004 million and RR 8,560 million, respectively, which approximates 3%, 4% and 5% of sales and other operating revenues, respectively.

Non-cash sales, settled by purchases of property, plant and equipment, have been excluded from net cash provided by operating activities and from net cash used for investing activities in the accompanying statements of cash flows.

The following table shows the distribution of non-cash transactions included in the consolidated statements of operations and comprehensive income and as additions to property, plant and equipment:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Taxes other than income taxes	69	60	914
Additions to property plant and equipment	1,126	2,425	4,227
Operating and other expenditures	2,993	3,519	3,419
Total non-cash transactions	**4,188**	**6,004**	**8,560**

The majority of barter transactions represent transactions which have been settled through a chain of non-cash transactions involving several companies rather than transactions pursuant to standing barter arrangements or transactions originally intended to be settled through a contractual barter agreement.

In 2003 the Group capitalized leased assets in the amount of RR 2,223 million and paid only RR 1,221 million of this amount. Also the effect of adoption of SFAS 143 included an initial increase of property, plant and equipment of RR 9,912 million.

(in millions of Russian Roubles)

Note 6: Accounts Receivable

Accounts receivable are as follows:

	At December 31, 2003			At December 31, 2002		
	Total accounts receivable	**Accounts receivable from related parties**	**Accounts receivable, net**	**Total accounts receivable**	**Accounts receivable from related parties**	**Accounts receivable, net**
Trade – domestic	7,203	437	6,766	8,820	199	8,621
Trade – export (US $395 million and US $197 million at December 31, 2003 and 2002, respectively)	11,640	5,109	6,531	6,217	1,181	5,036
Total accounts receivable, net	**18,843**	**5,546**	**13,297**	**15,037**	**1,380**	**13,657**

Trade receivables are presented net of an allowance for doubtful accounts of RR 905 million and RR 1,073 million at December 31, 2003 and 2002, respectively.

Note 7: Short and Long-Term Investments

Short-term investments are classified as available-for-sale and trading securities as follows:

	At December 31, 2003	**At December 31, 2002**
Available-for-sale securities	379	944
Trading securities	2,844	2,533
Total short-term investments	**3,223**	**3,477**

Trading securities are held in the Group's banks and insurance company, which frequently buy and sell securities with the objective of earning profits on short-term differences in price. All other short-term investments in debt and equity securities are classified as available-for-sale and are as follows:

	Cost	**Gross unrealized gains**	**Fair value (carrying value)**
Equity securities	336	43	379
Total available-for-sale securities at December 31, 2003	**336**	**43**	**379**
Corporate debt securities	50	-	50
Equity securities	861	33	894
Total available-for-sale securities at December 31, 2002	**911**	**33**	**944**

(in millions of Russian Roubles)

Note 7: Short and Long-Term Investments (continued)

Short-term investments classified as trading securities are as follows:

	At December 31, 2003	At December 31, 2002
Bonds and other Russian government securities	647	1,110
Corporate debt securities	1,722	1,259
Equity securities	475	164
Total trading securities	**2,844**	**2,533**

Bonds and other Russian government securities at December 31, 2003 and 2002, include mainly Federal Currency Bonds (OVVZ) with a carrying value of RR 51 million and RR 712 million and Russian Federation Eurobonds with a carrying value of RR 334 million and RR 76 million, respectively.

At December 31, 2003, total debt securities with fair values totaling RR 692 million mature during 2004, and with fair values totaling RR 1,677 million mature between 2005 and 2030.

Net gains on trading and realized available-for-sale securities for the year ended December 31, 2003, 2002 and 2001 were RR 235 million, RR 3,583 million, RR 1,736 million, respectively, reported in the consolidated statements of operations and comprehensive income.

Long-term investments are as follows:

	Ownership percentage at	Net book value at		Income for the year ended December 31,		
	December 31, 2003	December 31, 2003	December 31, 2002	2003	2002	2001
Investments in and income from equity affiliates and joint ventures:						
ZAO Tatex	50	1,788	1,775	42	229	362
OAO Finansovaya Lizingovaya Kompania (“FLK”)	-	-	512	3	(82)	7
Other	20-50	241	246	56	1	132
Total investments in and income from equity affiliates and joint ventures		**2,029**	**2,533**	**101**	**148**	**501**
Long-term investments, at cost:						
ZAO Ukrtatnafta	9	504	504			
OAO AK Bars Bank	18	609	609			
Other	0-20	579	557			
Total long-term investments, at cost		**1,692**	**1,670**			
Total long-term investments		**3,721**	**4,203**			

At December 31, 2003, consolidated retained earnings included RR 1,755 million (2002 – RR 2,118 million) related to the undistributed earnings of 50% or less owned companies that are accounted for using the equity method. Summary financial information pertaining to these investments has not been presented as the investments are not material to the Group’s consolidated financial statements.

Long-term investments not designated as available-for-sale or trading securities are recorded at cost because they are not traded on the market and it is not practicable to determine their fair value.

At the beginning of 2003 the Group acquired 9% of the share capital of OAO Finansovaya Lizingovaya Kompania, a leasing company equity affiliated to the Group, for RR 263 million in addition to 12% previously owned by the Group. In June 2003 the entire interest in this company (21%) was sold for RR 676 million, resulting in a loss of RR 99 million.

In October 2003, the Group sold its 75% interest in the share capital of OAO Tatincom-T, a regional cellular telecommunications subsidiary, for RR 549 million, resulting in a gain of RR 681 million. Total assets of OAO Tatincom-T as of September 30, 2003 and December 31, 2002 were RR 442 million and RR 336 million, respectively, and total liabilities – RR 574 million and RR 515 million, respectively. Net results from disposal of OAO Finansovaya Lizingovaya Kompania and OAO Tatincom-T were included within other income of the consolidated statements of operations and comprehensive income for 2003.

(in millions of Russian Roubles)

Note 8: Inventories

Inventories are as follows:

	At December 31, 2003	At December 31, 2002
Materials and supplies	5,282	6,407
Crude oil	1,485	1,861
Refined oil products	2,641	799
Petrochemical supplies and finished goods	643	895
Total inventories	**10,051**	**9,962**

Note 9: Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets are as follows:

	At December 31, 2003	At December 31, 2002
VAT recoverable	6,391	5,908
Notes receivable	3,761	3,312
Receivable due from Tax Ministry	2,251	-
Advances	878	2,065
Prepaid export duties	694	1,011
Prepaid transportation expenses	504	252
Interest receivable	229	170
Prepaid profit tax	160	1,561
Other	2,638	2,661
Total prepaid expenses and other current assets	**17,506**	**16,940**

Receivable due from Ministry of Tax. On December 6, 2002, the Group filed a lawsuit in the Arbitration court of Tatarstan against the Tax Ministry of Tatarstan claiming a refund for mineral use tax (royalty tax) paid in the amount of RR 2,251 million. On January 17, 2003, the Arbitration court ruled in favor of the Group and permitted the Group to apply this amount against future tax payments. The Tax Ministry of Tatarstan appealed this decision to the Federal Arbitration court of Povolzhsky district which, on April 6, 2003, upheld the decision of the Arbitration court of Tatarstan. Accordingly, the Group recognized the gain of RR 2,251 million as well as a receivable due from the Tax Ministry in the same amount which will be legally offset against the Group's tax liabilities in 2004 (see Notes 1 and 22).

Note 10: Loans Receivable and Advances

	At December 31, 2003	At December 31, 2002
Banking loans and advances to customers, net	20,146	11,352
Long-term notes receivable	479	227
Other Russian Rouble denominated loans receivable	808	1,893
Total loans receivable and advances	**21,433**	**13,472**
Less: current portion of loans receivable and advances	(14,042)	(9,652)
Less: due from related parties	(645)	(842)
Total long-term loans receivable and advances	**6,746**	**2,978**

(in millions of Russian Roubles)

Note 10: Loans Receivable and Advances (continued)

Banking loans and advances to customers. Banking loans and advances to customers are presented net of allowance for losses of RR 741 million and RR 1,011 million as at December 31, 2003 and 2002, respectively.

At December 31, 2003 and 2002 the weighted average fixed interest rate on banking loans and advances was 14% and 18% on balances denominated in Russian Roubles and 12% and 14% on balances denominated in foreign currency, respectively. The fair values of banking loans and advances approximate the carrying values as interest rates typically adjust on a three months basis and the majority is short-term in nature.

Economic sector risk concentration within the loan portfolio is as follows:

	At December 31, 2003		At December 31, 2002	
	Amount	**%**	**Amount**	**%**
Commercial	14,443	72%	8,834	78%
Financial	2,988	15%	650	6%
Agricultural	1,454	7%	662	6%
Individuals	229	1%	124	1%
Other	1,032	5%	1,082	9%
	20,146		**11,352**	

Loans receivable and advances to customers reported as of December 31, 2003 in the amounts of RR 2,625 million, RR 1,057 million and RR 2,585 mature in 2005, 2006 and after 2007, respectively.

Aggregate non-performing loans on which contractual interest is not being recognized amounted to RR 394 million and RR 884 million as of December 31, 2003 and 2002, respectively. Unrecognized contractual interest related to such loans totaled RR 301 million and RR 228 million as of December 31, 2003 and 2002, respectively.

Included in current loans is RR 838 million and nil as of December 31, 2003 and 2002, respectively, which represents the amounts receivable from customers in connection with security repurchase transactions.

Promissory notes issued by "Nedoimka". In 2003 the Group purchased promissory notes issued by entity "Nedoimka", a unitary company controlled by Tatarstan government, in order to finance social expenditures planned under Tatarstan's budget at the request of Tatarstan government. Management of the Group believes that these notes are not recoverable and, accordingly, all notes in the amount of RR 1,197 million were written off and reported as a loss on disposals of property, plant and equipment and impairment of investments in the consolidated statements of operations and comprehensive income (see also Note 1).

Note 11: Property, Plant and Equipment

Effective January 1, 2003, the Group adopted SFAS 143. This new accounting standard applies to legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset. Subsequently, the liability is accreted for the passage of time and the related asset is depreciated over its estimated useful life. The adoption of SFAS 143 affected the accounting and reporting of the assets, liabilities and expenses related to these obligations.

Prior to the adoption of SFAS 143 costs related to asset retirement obligation were accrued ratably over the productive lives of the assets in accordance with SFAS 19. Under SFAS 19, asset retirement costs were accrued on a unit-of-production basis as the oil is produced and recorded as an increase of accumulated depreciation. The SFAS 19 method matched the accruals with the revenues generated from production and results in most of the costs being accrued early in field life, when production is at the highest level. Because SFAS 143 requires accretion of the liability as a result of the passage of time using an interest method of allocation, the majority of the costs will be accrued toward the end of field life, when production is at the lowest level. Accordingly, the cumulative income adjustment described below resulted from reversing the higher amount of depreciation accumulated under SFAS 19 in order to report a liability to the lower present value amount resulting from transition to SFAS 143. This amount being reversed in transition, which was previously charged to operating earnings under SFAS 19, will again be charged to those earnings under SFAS 143 in future years.

The Group has numerous asset removal obligations that it is required to perform under law or contract once an asset is permanently taken out of service. The Group’s field exploration, development, and production activities include assets related to: well bores and related equipment and operating sites, gathering and oil processing systems, oil storage facilities and pipelines to main transportation trunks. Generally, the Group’s licenses and other operating permits require certain actions to be taken by the Group in the abandonment of these operations. Such actions include well abandonment activities, equipment dismantlement and other reclamation activities. The Group’s estimates of future abandonment costs consider present regulatory or license requirements and are based upon management’s experience of the costs of and requirement for such activities. Most of these costs are not expected to be incurred until several years, or decades, in the future and will be funded from general Group resources at the time of removal. Legal or contractual obligations, if any, to retire or otherwise abandon petrochemical, refining and marketing, distribution and banking assets are generally not recognized because of limited history of such activities in these operating areas, absence of clear and definitive legal requirements and indeterminable lives of these assets. Inasmuch as the regulatory and legal environment in Russia continues to evolve, there could be future changes to the requirements and costs associated with abandoning long-lived assets.

SFAS 143 calls for measurements of asset retirement obligations to include, as a component of expected costs, an estimate of the price that a third party would demand, and could expect to receive, for bearing the uncertainties and unforeseeable circumstances inherent in the obligations, sometimes referred to as a market-risk premium. To date, the oil and gas industry has no examples of credit-worthy third parties who are willing to assume this type of risk, for a determinable price, on major oil and gas production facilities and pipelines. Therefore, because determining such a market-risk premium would be an arbitrary process, it has been excluded from the SFAS 143 estimates. As of January 1, 2003, the Group recorded a cumulative-effect adjustment resulting in an after-tax increase to net income of RR 4,742 million in relation to this change in accounting principle. The effect of adoption also included an initial increase of property, plant and equipment of RR 9,912 million, reduction of accumulated depreciation of RR 11,807 million and recognition of asset retirement obligation in the amount of RR 15,479 million as well as deferred tax liabilities of RR 1,498 million.

(in millions of Russian Roubles)

Note 11: Property, Plant and Equipment (continued)

The cumulative effect of the change on prior years resulted in a credit to income of RR 4,742 million (RR 2.23 per share), which is included in income for the year ended December 31, 2003. The pro forma effects of the application of SFAS 143 if the Statement had been adopted on January 1, 2001 (rather than January 1, 2003) are presented below:

	2002 (restated)	2001 (restated)
Net income (historical)	13,470	24,144
Basic net income per common share (historical)	6.24	10.94
Net income (as if Statement 143 had been adopted January 1, 2001)	11,380	22,394
Basic net income per common share (as if Statement 143 had been adopted January 1, 2001)	5.26	10.15
Basic net income per preferred share (as if Statement 143 had been adopted January 1, 2001)	6.14	10.25
Diluted net income per common share (as if Statement 143 had been adopted January 1, 2001)	5.25	10.13
Diluted net income per preferred share (as if Statement 143 had been adopted January 1, 2001)	6.13	10.23

During 2003, the overall asset retirement obligation changed as follows:

Opening balance at January 1, 2003	15,479
Accretion of discount	1,548
New obligations	68
Spending on existing obligations	(3)
Closing balance at December 31, 2003	**17,092**
Less: current portion of asset retirement obligations	(137)
Closing long-term balance at December 31, 2003	**16,955**

The pro forma asset retirement obligations as if Statement 143 had been adopted on January 1, 2002 (rather than January 1, 2003) are as follows:

	2003	2002
Pro forma amounts of liability for asset retirement obligation at beginning of year	15,479	14,071
Pro forma amounts of liability for asset retirement obligation at end of year	17,092	15,479

(in millions of Russian Roubles)

Note 11: Property, Plant and Equipment (continued)

Property, plant and equipment are as follows:

	Cost	Accumulated depreciation, depletion and amortization	Net book value
Oil and gas properties	256,731	124,312	132,419
Buildings and constructions	26,657	8,418	18,239
Machinery and equipment	43,226	30,126	13,100
Assets under construction	13,250	-	13,250
December 31, 2003	**339,864**	**162,856**	**177,008**
Oil and gas properties	235,223	129,168	106,055
Buildings and constructions	27,559	7,806	19,753
Machinery and equipment	38,872	27,415	11,457
Assets under construction	15,183	-	15,183
December 31, 2002 (restated)	**316,837**	**164,389**	**152,448**

As stated in Note 3, the Group calculates depreciation, depletion and amortization using the unit of production method over proved or proved developed oil and gas reserves depending on the nature of the costs involved. The proved or proved developed reserves used in the unit of production method assume the extension of the Group's production license beyond their current expiration dates until the end of the economic lives of the fields as discussed below in further detail.

The Group's oil and gas fields are located principally on the territory of Tatarstan. The Group obtains licenses from the governmental authorities to explore and produce oil and gas from these fields. Most of the Group existing production licenses expire from 2013 to 2019, and the license for the largest field, Romashkinskoye, expires in 2013. The economic lives of the licensed fields extend significantly beyond these dates. Under Russian law, the Group is entitled to renew the licenses to the end of the economic lives of the fields, provided certain conditions are met. Article 10 of the Subsoil Law provides that a license to use a field "shall be" extended at its scheduled termination at the initiative of the subsoil user if necessary to finish production in the field, provided that there are no violations of the conditions of the license. The legislative history of Article 10 indicates that the term "shall" replaced the term "may" in August 2004, clarifying that the subsoil user has an absolute right to extend the license term so long as it has not violated the conditions of the license. The Group has received a letter, dated April 7, 2005, from the Federal Agency for Subsoil Use under the Ministry of Natural Resources of the Russian Federation confirming that, to date, it has not identified any violations of the terms of the Group's licenses that could prevent their extension and that, based on approved development plans and in accordance with the Subsoil Law, the Group's licenses will be extended at the Group's request. The Group's right to extend licenses is, however, dependent on the Group continuing to comply with the terms of the licenses, and management has the ability and intent to do so. Management plan to request the extension of the licenses and are currently in the process of requesting extensions for the Group's most significant fields, including Romashkinksoye. The Group's current production plans are based on the assumption, which management considers to be reasonably certain, that the Group will be able to extend all existing licenses. These plans have been designed on the basis that the Group will be producing crude oil through the economic lives of the fields and not with a view to exploiting the Group's reserves to maximum effect only through the license expiration dates.

Miller & Lents, the Group's independent oil and gas consultants, have confirmed management's view that it is "reasonably certain" that the Group will be allowed to produce oil from the Group's reserves after the expiration of existing production licenses and until the end of the economic lives of the fields. "Reasonable certainty" is the applicable standard for defining proved reserves under the SEC's Regulation S-X, Rule 4-10. Accordingly, management has included in proved reserves in the supplementary information on oil and gas exploration and production activities of the consolidated financial statements as of and for the year ended December 31, 2003 all reserves that otherwise meet the standards for being characterized as "proved" and that the Group estimates the Group can produce through the economic lives of Group's licensed fields.

The SEC staff have indicated that proved reserves generally should be limited to those that can be produced through the license expiration date unless there is a long and clear track record which supports the conclusion that the extension of the license will be granted as a matter of course. The Group believes that the extension of the licenses is a matter of course as fully described above. To assist the financial statement reader in understanding the proved oil reserves that will be produced during the existing license period and those that will be produced during the period of the expected license extension, the proved oil reserves have been presented separately for each of these two periods in the accompanying supplementary oil and gas information.

(in millions of Russian Roubles)

Note 11: Property, Plant and Equipment (continued)

The Group's cash flow from operations is dependent on the level of oil prices, which are historically volatile and are also significantly impacted by the proportion of production that the Group can sell on the export market. Historically, the Group has supplemented its cash flow from operations with additional borrowings and may continue to do so. Should oil prices decline for a prolonged period and should the Group not have access to additional capital, the Group would need to reduce its capital expenditures, which could limit its ability to maintain or increase production and in turn meet its debt service requirements and pay dividends.

Capital leases. The Group leases machinery and equipment. The following is an analysis of the leased property under capital leases:

	At December 31, 2003	**At December 31, 2002**
Machinery and equipment	2,223	-
Less: accumulated amortization	(318)	-
	1,905	**-**

All capital lease transactions are conducted with related parties as further described in Note 19.

The following is a schedule by year of future lease payments under capital leases together with the present value of the future minimum lease payments as of December 31, 2003:

Year ended December 31:	
2004	643
2005	345
2006	173
2007	5
Total future lease payments	**1,166**
Less interest	(164)
Present value of future minimum lease payments	**1,002**
Less current portion	(643)
Long-term portion of capital lease obligations	**359**

(in millions of Russian Roubles)

Note 11: Property, Plant and Equipment (continued)

Social assets. During years ended December 31, 2003, 2002 and 2001 the Group transferred social assets with a net book value of RR 2,162 million (including medical equipment to Medical Center with a net book value of RR 1,917 million), RR 1,293 million and RR 593 million, respectively, to local authorities for no consideration. At December 31, 2003, and December 31, 2002, the Group held social assets with a net book value of RR 4,870 million and RR 5,833 million all of which were constructed after the privatization date. The remaining social assets comprise mainly dormitories, hotels, gyms and others. The Group has no intention to transfer these assets to the local authorities. The Group incurred social infrastructure expenses of RR 279 million, RR 199 million and RR 491 million for the years ended December 31, 2003, 2002, and 2001, respectively, for maintenance that mainly relates to housing, schools and cultural buildings (see also Note 1).

Impairment of property, plant and equipment. In 2001, based on a reassessment of its future development plans and cash flows of its telecommunications subsidiary, the Group wrote off its investment resulting in a charge to operations of RR 394 million, which is included in loss on disposals and impairment in the consolidated statements of operations and comprehensive income for the year ended December 31, 2001.

Note 12: Debt

	At December 31, 2003	At December 31, 2002
Short-term debt		
Foreign currency denominated debt		
Current portion of long-term debt	4,768	6,112
Other foreign currency denominated debt	4,335	5,565
Rouble denominated debt	4,110	4,941
Total short-term debt	**13,213**	**16,618**

	At December 31, 2003	At December 31, 2002
Long-term debt		
Foreign currency denominated debt		
BNP Paribas	8,734	11,743
Credit Suisse First Boston	4,220	5,721
Bank Zenit Eurobonds	2,915	-
Commerzbank AG	-	2,207
Other foreign currency denominated debt	33	491
Rouble denominated debt	1,662	572
Total long-term debt	**17,564**	**20,734**
Less: current portion	(4,768)	(6,112)
Total long-term debt, net current portion	**12,796**	**14,622**

Foreign currency debts are primarily denominated in US Dollars.

Short-term foreign currency denominated debt. As of December 31, 2003 other short-term foreign currency denominated debt includes loans from Winter Bank, Credit Suisse Zurich and interbank loans.

In July 2001 the Group entered into a RR 1,042 million (US $30 million) loan agreement with Winter Bank. The loan bears an interest rate of 6 month LIBOR plus 4.5% per annum. The loan must be repaid in full every six months and may be renewed immediately for an additional six months during the three year term of the commitment. The loan matures in November 2004. The amount of loan outstanding as of December 31, 2003 was RR 884 million.

In December 2003, the Group entered into a RR 1,034 million (US $35 million) one month revolving overdraft facility with Credit Suisse Zurich. The monthly revolving loan bears interest at 2.85% per annum and is collateralized by crude oil sales. The amount of loan outstanding as of December 31, 2003 was RR 725 million (US $25 million).

Note 12: Debt (continued)

In November 2003 the Group entered into a RR 3 million (US $0.1 million) loan agreement with Alesworth Ltd. The loan bears interest at 16% per annum and matures in November 2004. The amount of loan outstanding as of December 31, 2003 was RR 3 million.

Interbank loans from foreign banks of RR 2,723 million and RR 2,522 million as at December 31, 2003 and 2002 had effective average interest rates of 6% and 7% per annum, respectively.

Short-term Russian Rouble denominated debt. Russian Rouble denominated short-term debt primarily comprises of loans with Russian banks. Short-term Rouble denominated loans of RR 4,110 million and RR 4,941 million bear contractual interest rates from 10% to 20% and 10% to 25% per annum for the periods ended December 31, 2003 and 2002, respectively. The loans are collateralized by the assets of the Group.

The carrying amount of short-term debt approximate fair value. Weighted average interest rate on short-term debts were 7% and 8% as of December 31, 2003 and 2002, respectively.

Long-term foreign currency denominated debt. In November 2001, the Group entered into a loan agreement with BNP Paribas for RR 3,014 million (US $100 million). The loan bears interest at LIBOR plus 3.5% per annum, is collateralized by crude oil export contracts of 50 thousand tons per month and matures in February 2004. The amount of loan outstanding as of December 31, 2003 was RR 614 million. In October 2002, the Group entered into another loan agreement with BNP Paribas for US $300 million. The amount outstanding under this loan as of December 31, 2003 was RR 8,120 million. The loan proceeds are payable in two tranches. First tranche in the amount US $125 million bears interest of LIBOR plus 4.25% per annum. Second tranche in the amount US $175 million bears interest of LIBOR plus 3.75%, per annum. The loan is collateralized by crude oil export contracts of 120 thousand tons per month, and matures in October 2007. The loan agreements require compliance with certain financial covenants including, but not limited to, minimum levels of consolidated tangible net worth, and maximum debt and interest coverage ratios.

In March 2002 the Group entered into a US $200 million loan agreement with Credit Suisse First Boston. The amount of loan outstanding as of December 31, 2003 was RR 4,220 million (US $143 million). The loan bears interest at LIBOR plus 3.78% per annum, is collateralized by crude oil export contracts of 80 thousand tons per month and matures in March 2007.

In 2003, 2002 and 2001 the Group was in compliance with all covenants required by the loan agreements except for the matter discussed below.

In April 2005, BNP Paribas notified the Group that it considered an event of default to have occurred under the terms of the loan agreement as a result of the Group failure to provide its audited consolidated US GAAP financial statements for the year ended December 31, 2003 and interim consolidated financial information for the six months ended June 30, 2004, and reserved its rights to accelerate amounts outstanding under the loan agreement and to enforce the related security. However, to date BNP Paribas has taken no action in this respect. The Group’s management believes that the delivery to BNP Paribas of the US GAAP audited consolidated financial statements for the year ended December 31, 2003 would cure this event of default.

Eurobonds. Eurobonds issued represent internationally traded long-term notes issued by the Group on June 12, 2003 with a face value of US $125 million and an interest rate of 9.25% payable semi-annually in arrears on June 12 and December 12 in each year commencing on December 31, 2003. The issue matures on June 12, 2006. Effective interest rate on the Eurobonds is 10%. The entire amount of Eurobonds outstanding at December 31, 2003 was RR 2,915 million. The Group is in compliance with the covenant of the financing agreement to maintain a specified capital adequacy ratio. The Group performs trading operations with its Eurobonds.

Other long-term foreign currency denominated debt. During the period ended December 31, 2002 the Group entered into a RR 278 million (US $9 million) loan agreement with West Deutsche Landesbank Vostok. The amount outstanding under this loan as of December 31, 2003 was RR 33 million. The loan bears interest at LIBOR plus 4.5% per annum and is collateralized by crude oil export contracts of approximately 7.5 thousand tons per month. The loan matures in February 2004.

(in millions of Russian Roubles)

Note 12: Debt (continued)

Long-term Russian Rouble denominated debt. Long-term Russian Rouble denominated debt includes debentures and other loans bearing interest rates from 9% to 19%. Debentures outstanding as of December 31, 2003 amounted to RR 1,391 million. Other loans represent non-banking loans. The loans mature between 2004 to 2015.
The fair value of the Group's long-term debt is similar to its book value. Fair value assessment is subject to considerable uncertainty.

Aggregate maturities of long-term debt outstanding at December 31, 2003 are as follows:

2004	4,768
2005	3,996
2006	7,119
2007	1,580
2008	-
2009	70
2010- and thereafter	31
Total long-term debt	**17,564**

Note 13: Notes payable and banking customer deposits

Notes payable are as follows:

	At December 31, 2003	At December 31, 2002
Bank notes payable	3,739	1,707
Other notes payable	4,694	2,641
Less: current notes payable	(6,948)	(3,482)
Notes payable long-term	**1,485**	**866**

Bank notes payable as of December 31, 2003 include short-term and long-term notes payable of Zenit Bank in the amounts of RR 3,528 million and RR 20 million, respectively, and short-term notes payable of Devon Credit Bank in the amount of RR 191 million. Bank notes payable for the year ended December 31, 2002 include short-term and long-term notes payable of Zenit Bank in the amounts of RR 1,640 million and RR 13 million, respectively, and short-term notes payable of Devon Credit Bank in the amount of RR 54 million. Bank notes payable bear contractual interest rates ranging from 8% to 10% both in 2003 and 2002.

Other notes payable as of December 31, 2003 include short-term and long-term trade promissory notes payable to third parties and bear contractual interest rates ranging from 1% to 7%, respectively.

Long-term notes payable in the amounts of RR 578 million, RR 657 million and RR 250 million outstanding at December 31, 2003 are payable in 2005, 2007 and after 2008, respectively.

Banking customer deposits are as follows:

	At December 31, 2003	At December 31, 2002
Term deposits	9,546	9,012
Demand deposits	8,556	4,133
Less: current banking customer deposits	(16,665)	(11,408)
Less: due to related parties	(100)	(585)
Banking customer deposits long-term	**1,337**	**1,152**

Contractual interest rates were 9% and 12% for Russian Rouble interest deposits, and 6% and 6% for foreign currency interest deposits for the periods ended December 31, 2003 and 2002, respectively.

(in millions of Russian Roubles)

Note 13: Notes payable and banking customer deposits (continued)

The carrying values of notes payable and banking customer deposits approximate their fair values.

Long-term banking customer deposits in the amount of RR 1,337 million outstanding at December 31, 2003 is payable in 2005.

Note 14: Other Accounts Payable and Accrued Liabilities

Other accounts payable and accrued liabilities are as follows:

	At December 31, 2003	At December 31, 2002
Salaries and wages payable	2,105	1,606
Insurance provision	1,174	788
Interest payable	505	474
Current portion of asset retirement obligations (Note 11)	137	-
Deferred revenues	113	132
Advances received	33	552
Other accrued liabilities	1,360	2,019
Total other accounts payable and accrued liabilities	**5,427**	**5,571**

Note 15: Taxes

Deferred income taxes reflect the impact of temporary differences between the amount of assets and liabilities recognized for financial reporting purposes and such amounts recognized for statutory tax purposes. Deferred tax assets (liabilities) are comprised of the following at December 31, 2003 and 2002:

	At December 31, 2003	At December 31, 2002
Inventories	4	-
Accounts receivable	3	68
Long-term investments	18	32
Obligations under capital leases	241	-
Other accounts payable	66	39
Prepaid expenses and other current assets	119	-
Deferred tax assets	**451**	**139**
Property, plant and equipment	(21,177)	(20,828)
Inventories	-	(222)
Long-term investments	(353)	(491)
Other liabilities	(388)	(55)
Deferred tax liabilities	**(21,918)**	**(21,596)**
Net deferred tax liability	**(21,467)**	**(21,457)**

At December 31, 2003 and 2002, deferred taxes were classified in the consolidated balance sheet as follows:

	At December 31, 2003	At December 31, 2002
Current deferred tax liability	(196)	(170)
Non-current deferred tax liability	(21,271)	(21,287)
Net deferred tax liability	**(21,467)**	**(21,457)**

(in millions of Russian Roubles)

Note 15: Taxes (continued)

Presented below is a reconciliation between the provision for income taxes and taxes determined by applying the statutory tax rate to income before income taxes:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
		(restated)	(restated)
Income before income taxes and minority interest	14,657	19,304	24,598
Theoretical income tax expense at statutory rate (2003, 2002 – 24%, 2001 – 35%)	3,518	4,633	8,609
Increase (reduction) due to:			
Inflationary effects	-	2,244	3,132
Non-deductible expenses	1,131	434	5,231
Profit exempt from taxable income resulting from qualified capital investments	-	-	(7,676)
Non-taxable income	(275)	(2,195)	(1,629)
Effect of reduction in income tax rate	-	-	(9,352)
Other	208	247	441
Income tax expenses / (benefit)	**4,582**	**5,363**	**(1,244)**

In August 2001, changes in the Russian Tax Code were enacted, which introduced a new income tax rate of 24%, effective January 1, 2002 compared to 35% in 2001. The net deferred tax benefit recognized as a result of remeasuring the deferred tax liability for tax rate changes on an enactment date basis, amounted to RR 9,352 for the year ended December 31, 2001.

In 2001 and prior years in accordance with Russian profit tax legislation, companies had the right to decrease their taxable profit by the amount of their cash used for investment in production property, plant and equipment less depreciation charge for the year but not to exceed 50% of the taxable profit. This investment incentive deduction was accounted for as a reduction of current taxable income in the year in which the deduction arose. On August 6, 2001 the profits tax law was amended to eliminate such deduction effective January 1, 2002.

No provision has been made for additional income taxes of RR 2,794 million on undistributed earnings of a foreign subsidiary. These earnings have been and will continue to be reinvested. These earnings could become subject to additional tax of approximately RR 419 million if they were remitted as dividends.

The Company is subject to a number of taxes other than income taxes, which are detailed as follows:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Unified production tax	19,818	16,940	-
Export tariffs	18,174	11,890	16,697
Excise taxes	2,031	104	135
Property tax	1,389	1,336	1,087
Road users tax	-	1,079	1,285
Mineral restoration tax and royalty	-	-	11,773
Housing fund	-	-	1,432
Research and development tax	-	-	572
Penalties and interest	686	108	35
Other	1,280	531	357
Total taxes other than income taxes	**43,378**	**31,988**	**33,373**

Note 15: Taxes (continued)

Effective January 1, 2002, the unified production tax was introduced and replaced the mineral restoration tax, royalty tax and excise tax on crude oil production. The base tax rate for the unified production tax is set at RR 340 per metric ton of crude oil produced, and is adjusted depending on the market price of Urals blend and the US $/ RR exchange rate. The tax becomes zero if Urals blend price falls to or below US $8.00 per barrel. The rate increased to RR 347 per ton of crude oil produced starting from January 1, 2004. In August 2004, the law was approved that increased the base tax rate for the unified production tax from RR 347 to RR 419 per ton of crude oil starting from January 1, 2005. From January 1, 2007, the unified production tax rate is set by law at 16.5% of the value of extracted crude oil which may be calculated by either reference to actual sale prices of natural resources or the deemed value of natural resources net of Value Added Tax ("VAT") less export duties, transportation expenses and certain other distribution expenses.

In April 2005 the Group received a tax claim from the tax authorities, who conducted tax audit of the Group's tax returns filed for 2001, 2002 and 2003, in the amount of RR 1,380 million. This amount includes both alleged non-payment and under-payment of taxes as well as fines and penalties. In May 2005, as full settlement of the tax claim, the Group paid RR 1,380 million (see also Note 1).

The Russian government has recently revised the Russian tax system. The new tax system is intended to reduce the number of taxes and the overall tax burden on businesses and to simplify the tax laws. However, the revised tax system relies heavily on the judgments of local tax officials and fails to address many of the existing problems. Even in the event of further reforms to tax legislation, they may not result in a reduction of the tax burden on Russian companies and the establishment of a more efficient tax system. Conversely, they may introduce additional tax collection measures. Accordingly, the Group may have to pay significantly higher taxes, which could have a material adverse effect on its business.

Note 16: Share Capital, Additional Capital and Other Comprehensive Income

Authorized share capital. At December 31, 2003 the authorized share capital consists of 2,178,690,700 voting common shares and 147,508,500 non-voting preferred shares; both classes of shares have a nominal value of RR 1.00 per share.

Golden share. OAO Svyazinvestneftekhim, a company wholly owned by the government of Tatarstan, as of December 31, 2003 holds approximately 30.44% of the Company's capital stock. These shares were contributed to Svyazinvestneftekhim by the Ministry of Land and Property Relations of Tatarstan in 2003. Tatarstan also holds a "Golden Share" – a special governmental right – in Tatneft. The exercise of its powers under the Golden Share enables the Tatarstan government to appoint one representative to the Board of Directors and Revision Committee of the Company and to veto certain major decisions, including those relating to changes in the share capital, amendments to the Charter, liquidation or reorganization and "major" and "interested party" transactions as defined under Russian law. The Golden Share currently has an indefinite term. The Tatarstan government also controls a number of the Company's suppliers and contractors, such as the electricity producer OAO Tatenergo and the petrochemicals company OAO Nizhnekamskneftekhim (see also Note 1).

Restricted common and preferred shares. Under the privatization laws of Tatarstan, initially certain common shares were issued subject to restrictions on transfer. These include shares sold to employees at a discount from nominal value and common shares sold to any individual for privatization vouchers. The preferred shares of the Company were also subject to restrictions on transfer. The preferred shares were originally allocated pursuant to applicable privatization laws to employees, former employees, and pensioners who had worked for the Group for a specified period of time. Afterwards by decree of the President of Tatarstan, all restrictions on common and preferred shares have been removed.

(in millions of Russian Roubles)

Note 16: Share Capital, Additional Capital and Other Comprehensive Income (continued)

Rights attributable to preferred shares. Unless a different amount is approved at the annual shareholders meeting, preferred shares earn dividends equal to their nominal value. The amount of a dividend for a preferred share may not be less than the amount of a dividend for a common share.
Preferred shareholders may vote at meetings only on the following decisions:

- the amendment of the dividends payable per preferred share;
- the issuance of additional shares with rights greater than the current rights of preferred shareholders; and
- the liquidation or reorganization of the Company.

The decisions listed above can be made only if approved by 75% of preferred shareholders.

Holders of preferred shares acquire the same voting rights as holders of common shares in the event that dividends are either not declared, or declared but not paid, on preferred shares. On liquidation, the shareholders are entitled to receive a distribution of net assets. Under Russian Joint Stock Companies Law and the Company's charter in case of liquidation preferred shareholders have priority over ordinary shareholders to be paid declared but unpaid dividends on preferred shares and the liquidation value of preference shares, if any.

Amounts available for distribution to shareholders. Amounts available for distribution to shareholders are based on the Company's non-consolidated statutory accounts prepared in accordance with RAR, which differ significantly from US GAAP (see Note 2). The statutory accounts are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the current period net profit calculated in accordance with RAR. However, this legislation and other statutory laws and regulations dealing with distribution rights are open to legal interpretation. For the years ended December 31, 2003 and 2002, the Company had a statutory current profit of RR 11,415 million and RR 6,309 million, respectively, as reported in the published statutory accounts of the Company.

At the annual general meeting of shareholders on June 27, 2003, final dividends of RR 0.10 per common share and RR 1.00 per preferred share, expressed in nominal Russian Roubles, were approved for 2002 for all shareholders. At December 31, 2003 the Company had paid RR 354 million of RR 365 million of its accrued dividends for 2002.

No interim dividends for 2003 were declared.

Net income per share. Under the two-class method of computing net income per share, net income is computed for common and preferred shares according to dividends declared and participation rights in undistributed earnings. Under this method, net income is reduced by the amount of dividends declared in the current period for each class of shares, and the remaining income is allocated to common and preferred shares to the extent that each class may share in income if all income for the period had been distributed.

Other comprehensive income. The balance of accumulated other comprehensive income as reported on the consolidated balance sheet consists of the following components:

	At December 31, 2003	**At December 31, 2002**
Net unrealized gain on available-for-sale securities	43	33
Net foreign currency translation adjustment gain	146	143
Accumulated other comprehensive income	**189**	**176**

(in millions of Russian Roubles)

Note 16: Share Capital, Additional Capital and Other Comprehensive Income (continued)

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
		(restated)	(restated)
Income before cumulative effect of change in accounting principle	10,138	13,470	24,144
Common share dividends	(217)	(239)	(271)
Preferred share dividends	(148)	(148)	(35)
Income available to common and preferred shareholders, net of dividends	**9,773**	**13,083**	**23,838**
Basic:			
Weighted average number of shares outstanding (millions of shares):			
Common	1,983	1,991	2,057
Preferred	148	148	148
Combined weighted average number of common and preferred shares outstanding	2,131	2,139	2,205
Basic net income per share before cumulative effect of changes in accounting principle (RR)			
Common	4.70	6.24	10.94
Preferred	5.59	7.12	11.05
Cumulative effect of changes in accounting principle (RR)			
Common	2.23	-	-
Preferred	2.23	-	-
Basic net income per share (RR)			
Common	6.93	6.24	10.94
Preferred	7.82	7.12	11.05
Diluted:			
Weighted average number of shares outstanding (millions of shares):			
Common	1,988	1,993	2,062
Preferred	148	148	148
Combined weighted average number of common and preferred shares outstanding assuming dilution	2,136	2,141	2,210
Diluted net income per share before cumulative effect of changes in accounting principle (RR)			
Common	4.68	6.23	10.92
Preferred	5.58	7.11	11.02
Cumulative effect of changes in accounting principle (RR)			
Common	2.22	-	-
Preferred	2.22	-	-
Diluted net income per share (RR)			
Common	6.90	6.23	10.92
Preferred	7.80	7.11	11.02

Minority interest. Minority interest is adjusted by dividends paid by the Group's subsidiaries amounting to RR 112 million.

(in millions of Russian Roubles)

Note 17: Stock-Based Compensation

On December 31, 2000 the Board of Director of the Company approved the Company stock compensation plan (the "Plan") for senior management and directors of the Company. Under the provisions of the Plan the Company is entitled to issue options to its directors and senior management on an annual basis based on approval of the Board of Directors. The Board of Directors determines the number and exercise price of options as well as their expiration and vesting periods. In accordance with the Plan for all options issued, the Company reserves the right to repurchase outstanding options at the price determinable as the maximum weighted average daily market price for the preceding three years for trades on the Moscow Interbank Currency Exchange less the exercise price of option.

Option issuance must be registered with the Federal Financial Markets Service (formerly the Federal Commission for the Securities Markets of the Russian Federation) within one year after the approval of the Board of Directors. After registration, the number of options, their exercise prices and other conditions are communicated to the eligible person usually within three weeks after registration through the signing of a security sales contract between the Company or its subsidiary and such person. On the signing date, the option holder pays the non-refundable portion of the exercise price and the remaining amount is payable on the exercise date. The vesting period commences from the date of signing (the grant date).

All options issued in 2003, 2002 and 2001 vest in 270 days from the grant date and expire in 365 days after the grant date. Each option gives the option holders the right to purchase one share of the Company. Since the options are granted with an option repurchase feature and because the Company expects to repurchase the stock options after vesting, variable accounting for stock-based compensation under APB No. 25, *"Accounting for Stock Issued to Employees"*, and related Interpretations is applied. The compensation cost is determined prospectively as an excess of repurchase price over the exercise price of the option until full vesting is achieved. Total compensation cost is allocated rateably over the vesting period and corresponding liability recorded in other accounts payable and accrued liabilities.

In 2003 and 2002 the Company repurchased the options granted in 2002 and 2001 through cash settlement at the price of RR 27.00 and RR 16.50 per option, respectively. The amount of compensation expense in respect of the Plan recognized in the consolidated statements of operations for the years ended December 31, 2003, 2002 and 2001 was RR 179 million, RR 120 million and RR 163 million, respectively.

The following table summarizes the stock option activity for the periods presented:

	2003		**2002**		**2001**	
	Shares	**Price**	**Shares**	**Price**	**Shares**	**Price**
Outstanding, beginning of year	**9,300,000**	**10.50**	**9,395,000**	**0.10**	**-**	**-**
Granted	9,300,000	11.70	9,300,000	10.50	9,395,000	0.10
Repurchased	(9,300,000)	10.50	(9,395,000)	0.10	-	-
Outstanding, end of year	**9,300,000**	**11.70**	**9,300,000**	**10.50**	**9,395,000**	**0.10**
Exercisable, end of year	**-**	**-**	**-**	**-**	**-**	**-**

The remaining lives of options outstanding at December 31, 2003, 2002 and 2001 were 0.50, 0.70 and 0.50 years, respectively.

(in millions of Russian Roubles)

Note 17: Stock-Based Compensation (continued)

The fair value of the Group's stock options is the estimated present value at the date of grant using the Black-Scholes option pricing model with the following assumptions:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Average grant date fair value of options	36.42	17.85	16.40
Assumption used:			
Risk-free interest rate	6.25	18.75	18.75
Dividend yield	1%	1%	1%
Volatility factor	36%	38%	53%
Expected life (years)	1	1	1

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, this option pricing model requires the input of highly subjective assumptions, including the expected stock price volatility.

Note 18: Segment Information

The Group's business activities are conducted predominantly through four business segments: exploration and production, refining and marketing, petrochemicals, and banking. The segments were determined on the way management recognizes the segments within the Group for making operating decisions and how they are evident from the Group structure.

Exploration and production segment activities consist of oil extraction by production divisions. Intersegment sales in exploration and production constitute transfers of crude oil and gas from production divisions to the refining and marketing divisions and subsidiaries.

The Group's investments in equity method investees and equity in the net income of investees accounted for by the equity method are included within exploration and production segments, as the Group's major equity investees are engaged in exploration and production activities. The Group's investments and equity in the income of the equity investees are disclosed in Note 7.

Refining and marketing comprises purchases and sales of crude oil and refined products from the Group's own production divisions and third parties, own refining activities and retailing operations. As in prior years, the Company sold significant volumes of oil to intermediaries, which refine oil in domestic refineries, and purchased refined products processed from its oil.

Sales of petrochemical products include sales of petrochemical raw materials and refined products, which are used in production of tires. Sales of tires are disclosed by geographic segment for the reporting periods.

Other sales include revenues from ancillary services provided by the specialized subdivisions and subsidiaries of the Group, such as sales of oilfield equipment and drilling services provided to other companies in Tatarstan, revenues from the sales of auxiliary petrochemical related services and materials as well as other business activities, which do not constitute reportable business segments.

In accordance with SFAS No.131, *"Disclosures about Segments of an Enterprise and Related Information",* the Group reports bank interest revenue net of interest expense since a majority of the banking segment's revenues are from interest and the management relies primarily on the "spread" between interest revenue and interest expense (net interest revenue) to assess performance of the segment and to make resource allocation decisions.

(in millions of Russian Roubles)

Note 18: Segment Information (continued)

For the years ended December 31, 2003, 2002 and 2001 the Group had one customer which accounted for RR 34,249 million, RR 19,258 million and RR 3,144 million of sales, which represents 22%, 13% and 2% of total sales, respectively. These sales are included within refining and marketing revenues. Management does not believe that the Group is reliant on any particular customer.

The Group evaluates performance of its reportable operating segments and allocates resources based on income or losses before income taxes and minority interest not including non-banking net interest expense and monetary effects. Segment accounting policies are the same as those disclosed in Note 3. Intersegment sales are at prices that approximate market.

Segment sales and other operating revenues. Reportable operating segment sales and other operating revenues are stated in the following table:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Exploration and production			
Intersegment sales	93,155	84,394	91,528
Total exploration and production	**93,155**	**84,394**	**91,528**
Refining and marketing			
Crude oil	11,346	11,901	32,371
Refined products	23,545	24,378	18,971
Domestic sales	34,891	36,279	51,342
Crude oil	9,470	11,510	6,997
Refined products	336	30	705
CIS sales[1]	9,806	11,540	7,702
Crude oil	69,511	57,886	55,855
Refined products	19,950	19,968	24,183
Non – CIS sales[2]	89,461	77,854	80,038
Total refining and marketing	**134,158**	**125,673**	**139,082**
Petrochemicals			
Intersegment sales	233	322	1,311
Tires - domestic sales	7,764	7,046	2,517
Tires - CIS sales	1,799	908	38
Tires - non-CIS sales	739	814	163
Petrochemical and refined products	1,281	1,152	1,415
Total petrochemicals	**11,816**	**10,242**	**5,444**
Banking			
Net interest income – intersegment	530	335	265
Net interest income	1,001	845	1,350
Total banking	**1,531**	**1,180**	**1,615**
Total segment sales	**240,660**	**221,489**	**237,669**
Other sales	9,177	10,038	12,797
Elimination of intersegment sales	(93,918)	(85,051)	(93,104)
Elimination of income from equity investments reported separately in the consolidated statements of operations and comprehensive income	(101)	(148)	(501)
Total sales and other operating revenues	**155,818**	**146,328**	**156,861**

[1] - CIS is an abbreviation for Commonwealth of Independent States (excluding the Russian Federation).

[2] - Non-CIS sales of crude oil and refined products are mainly made to European markets.

(in millions of Russian Roubles)

Note 18: Segment Information (continued)

Segment earnings and assets. Segment earnings are as follows:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
		(restated)	(restated)
Segment earnings (loss)			
Exploration and production	13,566	18,227	19,585
Refining and marketing	2,730	2,627	3,846
Petrochemicals	(311)	(139)	337
Banking	421	811	1,275
Total segment earnings	**16,406**	**21,526**	**25,043**
Exchange loss	(225)	(1,042)	(851)
Monetary gain	-	871	1,764
Interest expense, net	(1,524)	(2,051)	(1,358)
Income before income taxes and minority interest	**14,657**	**19,304**	**24,598**

Segment assets are as follows:

	At December 31, 2003	At December 31, 2002
Assets		
Exploration and production	186,632	161,420
Refining and marketing	38,814	37,623
Petrochemicals	8,924	9,591
Banking	28,347	17,654
Total assets	**262,717**	**226,288**

The Group's assets and operations are primarily located and conducted in Russia.

Segment depreciation, depletion and amortization and additions to property, plant and equipment are as follows:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
		(restated)	(restated)
Depreciation, depletion and amortization			
Exploration and production	7,150	5,938	5,315
Refining and marketing	742	667	462
Petrochemicals	924	912	346
Banking	34	24	16
Total segment depreciation, depletion and amortization	**8,850**	**7,541**	**6,139**
Additions to property, plant and equipment			
Exploration and production	21,320	10,519	18,824
Refining and marketing	2,766	3,576	5,027
Petrochemicals	1,768	818	939
Banking	86	612	20
Total additions to property, plant and equipment	**25,940**	**15,525**	**24,810**

(in millions of Russian Roubles)

Note 19: Related Party Transactions

Transactions are entered into in the normal course of business with significant shareholders, directors and companies with which the Group has significant shareholders and directors in common (see also Note 1). These transactions include sales of crude oil and refined products, purchases of electricity and banking transactions.

In 2003 the Group transferred RR 672 million to several companies outside the Russian Federation unrelated to the Group which the Group intended to use for an acquisition of Company's shares. The shares acquired for the benefit of the Group were accumulated by one of these companies located in Cyprus with the intention of being used by the Group in the development and establishment of an anticipated incentive scheme for its senior employees. In 2003, RR 570 million of the total funds transferred were used in the acquisition of 20,676,875 Group's shares and reported in the consolidated financial statements as common shares held in treasury as of December 31, 2003. The remaining funds of RR 98 million were recorded within other prepaid expenses and other current assets as of December 31, 2003. In January 2004, an additional 2,788,300 shares were acquired using these funds. All shares accumulated by the Cyprus based company were transferred to the Group in November 2004.

The transactions for each year and the outstanding balances at each year end with related parties are as follows:

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Sales of crude oil	23,644	12,387	10,452
Volumes of crude oil sales (thousand tons)	4,409	3,037	3,460
Sales of refined products	14,080	9,621	5,632
Volumes of refined product sales (thousand tons)	4,101	2,817	2,036
Sales of petrochemical products	671	645	1,232
Other sales	704	429	-
Purchases of crude oil	(798)	(1,330)	(11,457)
Volumes of crude oil purchases (thousand tons)	249	376	3,372
Purchases of refined products	-	(6)	(1,837)
Volumes of refined products purchases (thousand tons)	-	1	838
Purchases of petrochemical products	(2,072)	(2,001)	(2,546)
Purchases of electricity	(2,940)	(3,038)	(2,324)
Other purchases	(1,186)	(761)	(946)
Sales of investment (AK Bars Bank shares sold to FLK)	-	-	403
Interest receivable	12	38	33
Bank commission receivable	6	22	55
Additions to property, plant and equipment	(2,223)	-	-

(in millions of Russian Roubles)

Note 19: Related Party Transactions (continued)

	At December 31, 2003	At December 31, 2002
Assets		
Trade accounts receivable (Note 6)	5,546	1,380
Notes receivable	440	1,883
Loans and advances to customers (Note 10)	645	842
Due from related parties	**6,631**	**4,105**
Liabilities		
Banking customer deposits (Note 13)	(100)	(585)
Loans payable	(394)	(111)
Trade accounts payable	(540)	(66)
Due to related parties	**(1,034)**	**(762)**
Capital lease obligations	(1,002)	-
Other		
Common shares held in treasury for an anticipated incentive scheme, at cost (20,676,875 shares at December 31, 2003)	570	-
Loan guarantee obligations	(181)	(211)

The Group continued to enter into back-to-back crude oil transactions with various parties. These transactions are not recorded as purchases and sales of crude oil but the net commission amounting to RR 956 million, RR 1,514 million, and RR 1,414 million, of which nil, nil and RR 595 million were associated with transactions with related parties, for the years ended December 31, 2003, 2002 and 2001, respectively, are included within selling, general and administrative expenses. The volumes of crude oil sold and purchased under these transactions were 853 thousand, 2,829 thousand, and 2,500 thousand tons for the years ended December 31, 2003, 2002 and 2001, respectively.

Note 20: Financial Instruments and Risk Management

Fair values. The carrying amounts of short-term financial instruments approximate fair value because of the relatively short period of time between the origination of these instruments and their expected realization.

Information concerning the fair value of long-term investments is disclosed in Note 7.

Information concerning the fair value of loans receivable and advances is disclosed in Note 10.

Information concerning the fair value of short-term and long-term debt is disclosed in Note 12.

Information concerning the fair value of notes payable and banking customer deposits is disclosed in Note 13.

Credit risk. The Group’s financial instruments that are potentially exposed to concentrations of credit risk consist primarily of accounts receivables, cash and cash equivalents, prepaid VAT as well as loans receivable and advances. A significant portion of the Groups’s accounts receivable is due from domestic and export trading companies. The Group does not generally require collateral to limit the exposure to loss; however, sometimes letters of credit and prepayments are used. Although collection of these receivables could be influenced by economic factors affecting these entities, management believes there is no significant risk of loss to the Group beyond provisions already recorded.

The Group deposits available cash mostly with financial institutions in the Russian Federation. Deposit insurance for deposits of legal entities is not offered to financial institutions operating in the Russian Federation. To manage this credit risk, the Group allocates its available cash to a variety of Russian banks and Russian affiliates of international banks. Management periodically reviews the credit worthiness of the banks in which it deposits cash.

Prepaid VAT, representing amounts payable or paid to suppliers, is recoverable from the tax authorities via offset against VAT payable to the tax authorities on the Group's revenue or direct cash receipts from the tax authorities. Management periodically reviews the recoverability of the balance of prepaid VAT and believes it is fully recoverable within one year.

Note 20: Financial Instruments and Risk Management (continued)

The Group's banks take on exposures to credit risk which is the risk that a counter party will be unable to pay amounts in full when due. The banks structure the level of credit risk they undertake by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Limits on the level of credit risk by product, borrower and industry sector are reviewed regularly. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Note 21: Commitments and Contingent Liabilities

Guarantees and commitments. At December 31, 2003, the Group was liable for certain contingent obligations under various contractual arrangements. Credit-related commitments comprise Zenit Bank loan commitments and guarantees of RR 1,809 million and RR 2,062 million at December 31, 2003 and 2002, respectively. The contractual amount of these commitments represents the value at risk if the bank's clients default and all existing collateral becomes worthless. The Group is required to recognize a liability at inception for the fair value of the obligation as a guarantor for guarantees issued or modified after December 31, 2002. The Group has not recognized a liability either because the guarantees were issued prior to December 31, 2002 and have not been subsequently modified, or because the fair value of the obligations is not material.

Operating environment. While there have been improvements in the economic situation in the Russian Federation in recent years, the country continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in any countries outside of the Russian Federation, restrictive currency controls, and relatively 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.

Taxation. Russian tax legislation is subject to varying interpretations and constant changes. Further, the interpretations of tax legislation by tax authorities as applied to the transactions and activities of the Group may not coincide with that of management. Also interpretations on the application of the tax legislation may vary between regional and Federal tax authorities. As a result, transactions may be challenged by tax authorities and the Group may be assessed for additional taxes, penalties and interest. Consolidated tax returns are not required under existing Russian tax legislation and tax audits are performed on an individual entity basis only. Tax periods remain open to review by the tax authorities for three years.

Environmental contingencies. The Group, through its predecessor entities, has operated in Tatarstan for many years without developed environmental laws, regulations and Group policies. Environmental regulations and their enforcement are currently being considered in the Russian Federation and the Group is monitoring its potential obligations related thereto. The outcome of environmental liabilities under proposed or any future environmental legislation cannot reasonably be estimated at present, but could be material. Under existing legislation, however, management believes that there are no probable liabilities that are in addition to the immaterial amounts already accrued in the consolidated financial statements, which would have a material adverse effect on the operating results or financial position of the Group.

Legal contingencies. The Group is subject to various lawsuits and claims arising in the ordinary course of business. The outcomes of such contingencies, lawsuits or other proceedings cannot be determined at present. In the case of all known contingencies, the Group accrues a liability when the loss is probable and the amount is reasonably estimable. Based on currently available information, management believes that it is remote that future costs related to known contingent liability exposures will exceed current accruals by an amount that would have a material adverse impact on the Group's consolidated financial statements.

In 2003 OAO "TAIF", a related party to the Group, brought a case before the Arbitration Court of Tatarstan Republic claiming a return of equipment leased to OAO "Nizhnekamsk NPZ", a subsidiary of the Group (the "Refinery"), because of breach by the Refinery of several provisions of the lease agreement dated December 29, 2001. This equipment was installed at the Refinery in 2002 and represents vital assets for the operations of the Refinery. On October 6, 2003 the Arbitration Court ruled in favor of OAO "TAIF" and this decision was reinforced by the instance of appeals of the Arbitration Court of Tatarstan Republic on January 13, 2004. Currently, the Refinery operates at full capacity and no actions have been taken by OAO "TAIF" to remove the leased equipment. The management of the Group believes that the government of Tatarstan Republic will not allow OAO "TAIF" to proceed with the court decision and cease operations of the Refinery or to claim any other compensation from the Refinery for the breach of the lease agreement. Therefore management believes there is no financial statements impact from this court ruling (see also Note 1).

Note 21: Commitments and Contingent Liabilities (continued)

Social commitments. The Group contributes significantly to the maintenance of local infrastructure and the welfare of its employees within Tatarstan, which includes contributions towards the construction, development and maintenance of housing, hospitals and transport services, recreation and other social needs. Such funding is periodically determined by the Board of Directors after consultation with governmental authorities and recorded as expenditures when incurred.

In addition, the Group is committed to make certain contributions which are determined solely at the discretion of the Group's or its subsidiaries' management but not less than the minimum annual payment regulated by current Russian legislation. Also the provisions of collective agreements concluded on an annual basis between the Company or its subsidiary and their employees require the Group to pay certain post-employment and other benefits, to follow health and safety standards as well as a variety of other social benefits in excess of those required by law. In 2003, 2002 and 2001 the contributions to the non-governmental pension plan and post-employment benefit payments were not material (see also Note 1).

Transportation of crude oil. The Group benefits from the blending of its crude oil in the Transneft pipeline system since the Group's crude oil production is generally of a lower quality than that produced by other regions of the Russian Federation which supply through the same pipeline system. There is currently no equalization scheme for differences in crude oil quality within the Transneft pipeline system and the implementation of any such scheme is not determinable at present. However, if this practice were to change, the Group's business could be materially and adversely affected.

Banking contingent liabilities. Zenit Bank fiduciary assets and trust arrangements at nominal value amounted to RR 10,857 million and RR 4,148 million at December 31, 2003 and 2002, respectively, and are recorded off balance sheet as they are not assets of Zenit Bank. There is no insurance coverage maintained.

The Central Bank of Russian Federation requires banks to maintain a capital adequacy ratio of 10% of risk-weighted assets, computed based on Russian accounting legislation. As of December 31, 2003 and 2002, the Zenit Bank and Devon-Credit Bank capital adequacy ratio on this basis exceeded the statutory minimum.

Note 22: Subsequent Events

TUPRAS auction. In January 2004, Efremov Kautschuk GmbH ("EKG"), a subsidiary of OAO "Efremovsky Zavod Sinteticheskogo Kauchuka" was pronounced winner of a privatization auction for 65.8% of Turkey's oil refining company – Türkiye Petrol Rafinerileri A.Ş. ("TUPRAS"). OAO "Efremovsky Zavod Sinteticheskogo Kauchuka" is a related company to the Group because of representation of the Group's senior managers on the Board of Directors of OAO "Efremovsky Zavod Sinteticheskogo Kauchuka". Subsequently EKG formed a consortium with Zorlu Holding A.S. and established a joint venture, Tatneft Zorlu Petrol Yatirimlari Ve Ticaret A.S. ("Tatneft-Zorlu"), in which the Company agreed to purchase 50% if Tatneft-Zorlu acquires the shares in TUPRAS.

In November 2004 the Turkish High Administrative Court cancelled the results of the auction and, therefore, the Company's undertaking to purchase 50% in Tatneft-Zorlu from EKG was terminated. In May 2005 the Turkish government announced a new auction for 51% of the shares in TUPRAS. The Group is not participating in this new auction and has no commitment to participate in any future auction or tender for the sale of TUPRAS' shares, which may be organized by the Turkish government, or otherwise to acquire any shares in TUPRAS.

New significant borrowings. In March 2004 the Group issued 1 million unsecured bonds with a nominal value of RR 1,000 per bond for RR 1,000 million. Bonds carry a coupon yield of 8.69% for the first and the second payments due in September 2004 and March 2005. Subsequent coupon yields are determined by the Chairman of the Board of Zenit Bank. Bonds mature in March 2007.

Repayments of loans. In 2004 - 2005 the Group was repaying its debts in accordance with the original schedules of repayment.

Note 22: Subsequent Events (continued)

Transactions with government authorities (see also Note 1). In the first quarter of 2004 upon receipt of the letter from the Tax Ministry of Tatarstan the Group offset previously recognized receivable due from the Tax Ministry (see Note 9) against income tax, VAT and unified production tax liability in the amount of RR 2,251 million.

In September 2004 the Group entered into a RR 2,000 million loan agreement with OAO "Svyazinvestneftekhim", a company controlled by Tatarstan government. The loan interest rate is 0,01% per annum and matures in March 2014.

In 2004 the Group purchased promissory notes issued by entity "Tatgospostavki", a unitary company controlled by Tatarstan government, in the amount of RR 960 million in order to finance social expenditures planned under Tatarstan's budget at the request of Tatarstan government.

Dividends. At the annual general meeting of shareholders on June 25, 2004, final dividends of RR 0.30 per common share and RR 1.00 per preferred share, expressed in nominal Russian Roubles, were approved for 2003 for all shareholders.

At the extraordinary general meeting of shareholders on November 6, 2004, interim dividends of RR 0.67 per common share and RR 1.00 per preferred share, expressed in nominal Russian Roubles, were approved for the nine months ended September 30, 2004 for all shareholders.

At the annual general meeting of shareholders in June 2005, additional dividends of RR 0.23 per common share and RR 0 per preferred share, expressed in nominal Russian Roubles, were approved for 2004 for all shareholders.

Transactions with employees' stock options. In 2004 the Company repurchased the options granted in 2003 through cash settlement at the price of RR 40.26 per option.

Changes in Group's composition. In April 2005 the Group decreased its share in the equity of a major subsidiary, Zenit Bank (the "Bank"), by selling 26.75% of the Bank's shares to three Cyprus based companies, acting for the benefit of certain beneficiaries of Urals Energy, which is not related to the Group. As a result of this transaction, as of April 28, 2005 the Group no longer controls the Bank and will account for its remaining 25.95% equity investment in the Bank under equity method in its US GAAP financial statements for the periods subsequent to the sale. The sales price for the Bank's shares, RR 1,214 million (US$ 41.2 million), was determined based on the results of an independent evaluation. The sale of 26.75% of the bank's shares resulted in a loss on disposal of approximately RR 700 million.

In September 2004 the Group increased its shareholding in AK Bars bank from 19.9% to 30% for RR 2,000 million.

In December 2003, together with the government of Tatarstan, OAO Tatneftekhiminvest-Holding, OAO Nizhnekamskneftekhim, LG International Corp. and LG Engineering and Construction Corp., the Group signed a letter of intent contemplating future joint work on the construction of an oil refining and petrochemical complex on the territory of Tatarstan. The Group subsequently formed OAO TKNK in order to carry out feasibility studies and arrange for financing of the construction of the oil refining and petrochemical complex. The Group holds a 45.5% interest in OAO TKNK; OAO Nizhnekamksneftekhim holds a 36.4% interest; OAO Svyazinvestneftekhim holds a 9.1% interest; and LG International Corp. holds a 9.1% interest. In September 2004, TKNK entered into a non-binding engineering, procurement and construction works arrangement with LG International Corp. and LG Engineering and Construction Corp. that sets forth the basic terms by which the LG parties are to carry out engineering, procurement and construction work on oil refinery and petrochemical complexes in Nizhnekamsk. TKNK and the LG parties entered into a further non-binding engineering, procurement and construction work arrangement in December 2004 that provides for the construction of certain refining equipment in Nizhnekamsk. In May 2004, the Group provided TKNK with a RR 127 million (US $4.3 million) loan for financing feasibility studies and services as part of developing the oil refining and petrochemical complex. In addition, the Group has invested RR40 million into the first phase of the construction of the oil refining plant. In accordance with preliminary feasibility studies of construction of the oil refining plant prepared by LG, total necessary investment will amount to approximately RR 53 billion (US $1.8 billion). However, at this stage the Group cannot predict the level of additional capital investment that may be required from the Group in connection with this project as the financing structure of the venture has yet to be determined.

(in millions of Russian Roubles)

In accordance with SFAS No. 69, "*Disclosures about Oil and Gas Producing Activities*", this section provides supplemental information on oil and gas exploration and production activities of the Group.

The Group's oil and gas production is predominantly in Tatarstan within the Russian Federation; therefore, all of the information provided in this section pertains entirely to that region.

Oil Exploration and Production Costs

The following tables set forth information regarding oil exploration and production costs. The amounts reported as costs incurred include both capitalized costs and costs charged to expense during the year.

Costs Incurred in Exploration and Development Activities

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Exploration costs	1,091	1,153	1,140
Development costs	6,679	7,807	14,091
Total costs incurred in exploration and development activities	**7,770**	**8,960**	**15,231**

Property acquisitions are immaterial to the Group's oil activities.

Capitalized Costs of Proved Oil Properties

	At December 31, 2003	At December 31, 2002
		(restated)
Wells, support equipment and facilities	256,731	235,223
Uncompleted wells, equipment and facilities	3,837	4,346
Total capitalized costs of proved oil properties	**260,568**	**239,569**
Accumulated depreciation, depletion and amortization (Note 11)	(124,312)	(129,168)
Net capitalized costs of proved oil properties	**136,256**	**110,401**

The following information pertains to the drilling activities of the Group:

	Year ended December 31, 2004	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
Net productive development wells drilled	359	420	427	610
Net productive exploratory wells drilled	29	28	35	32
Total wells drilled	**388**	**448**	**462**	**642**

As of December 31, 2004 and 2003 the number of net productive oil wells were 18,659 and 19,209, respectively.

For the five months ended May 31, 2005 the Group drilled 135 new productive wells. The Group received an additional four licenses for the exploration and production of hydrocarbon materials in deposits on the territory of the Samara and Orenburg Regions in a license tenders held in 2005.

(in millions of Russian Roubles)

Results of Operations for Oil and Gas Producing Activities

The Group's results of operations from oil producing activities are shown below. Proved natural gas reserves do not represent a significant portion of the Group's total reserves.

In accordance with SFAS 69, results of operations do not include general corporate overhead and monetary effects nor their associated tax effects. Income taxes are based on statutory rates for the year, adjusted for tax deductions, tax credits and allowances.

	Year ended December 31, 2003	Year ended December 31, 2002	Year ended December 31, 2001
		(restated)	(restated)
Revenues from net production:			
Sales	79,344	70,360	78,957
Transfers[1]	13,811	14,034	12,571
Total revenues from net production	**93,155**	**84,394**	**91,528**
Less:			
Production costs[2]	26,562	24,521	26,821
Exploration expenses	812	463	839
Depreciation, depletion and amortization	6,985	5,677	5,182
Taxes other than income taxes	32,977	25,977	20,331
Related income taxes	6,197	6,661	6,904
Results of operations for oil and gas producing activities	**19,622**	**21,095**	**31,451**

[1] Transfers represent crude oil transferred to the refining subsidiaries at the estimated market price of those transactions.
[2] Production costs include transportation expenses and accretion of discount in accordance with SFAS 143.

The average sales price (including transfers) per ton for 2003, 2002 and 2001 are RR 3,736, RR 3,391 and RR 3,682, respectively. The average production cost per ton for 2003, 2002, and 2001 are RR 1,065, RR 985 and RR 1,079, respectively.

Proved Oil Reserves

As determined by the Group's independent reservoir engineers, Miller and Lents, Ltd., the following information presents the balances of proved oil reserves at December 31, 2003, 2002 and 2001. The definitions used are in accordance with applicable US Securities and Exchange Commission ("SEC") regulations.

Proved reserves are the estimated quantities of oil which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions. In some cases, substantial new investments in additional wells and related facilities will be required to recover these proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

Management believes that proved reserves should include quantities which are expected to be produced after the expiry dates of the Group's production licenses. Most significant licenses expire in 2013. Management believes the licenses may be extended at the initiative of the Group and management expects to extend such licenses for properties expected to produce subsequent to their license expiry date. The Group has disclosed information on proved oil and gas reserve quantities and standardized measure of discounted future net cash flows for periods up to and past the license expiry dates separately (see Note 11).

Proved developed reserves are those reserves which are expected to be recovered through existing wells with existing equipment and operating methods. Undeveloped reserves are those reserves which are expected to be recovered as a result of future investments to drill new wells and/or to install facilities to collect and deliver the production from existing and future wells.

"Net" reserves exclude quantities due to others when produced.

(in millions of Russian Roubles)

Proved Oil Reserves (continued)

A significant portion of the Group's total proved reserves are classified as either developed non-producing or undeveloped. The developed non-producing proved reserves can be produced from existing well bores but require capital costs for workovers, recompletions, or restoration of shut-in wells or additional completion work or future recompletion prior to the start of production. Of the developed non-producing proved reserves, a significant portion represents existing wells which are expected to be put back into production at a future date.

Net proved reserves of crude oil at December 31, 2003:

	Net proved reserves of crude oil recoverable up to license expiry dates		**Net proved reserves of crude oil recoverable past license expiry dates**		**Total net proved reserves of crude oil**	
	(millions of barrels)	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*
Net proved developed producing reserves	1,448	204	2,067	290	3,515	494
Net proved developed non-producing reserves	531	75	1,536	215	2,067	290
Net proved developed reserves	**1,979**	**279**	**3,603**	**505**	**5,582**	**784**
Net proved undeveloped reserves	137	19	240	34	377	53
Net proved developed and undeveloped reserves	**2,116**	**298**	**3,843**	**539**	**5,959**	**837**

Net proved reserves of crude oil at December 31, 2002:

	Net proved reserves of crude oil recoverable up to license expiry dates		**Net proved reserves of crude oil recoverable past license expiry dates**		**Total net proved reserves of crude oil**	
	(millions of barrels)	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*
Net proved developed producing reserves	1,567	220	1,840	258	3,407	478
Net proved developed non-producing reserves	627	88	1,485	208	2,112	296
Net proved developed reserves	**2,194**	**308**	**3,325**	**466**	**5,519**	**774**
Net proved undeveloped reserves	168	24	285	40	453	64
Net proved developed and undeveloped reserves	**2,362**	**332**	**3,610**	**506**	**5,972**	**838**

(in millions of Russian Roubles)

Proved Oil Reserves (continued)

Net proved reserves of crude oil at December 31, 2001:

	Net proved reserves of crude oil recoverable up to license expiry dates		**Net proved reserves of crude oil recoverable past license expiry dates**		**Total net proved reserves of crude oil**	
	(millions of barrels)	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*	*(millions of barrels)*	*(millions of tones)*
Net proved developed producing reserves	1,621	228	1,539	216	3,160	444
Net proved developed non-producing reserves	718	101	1,157	162	1,875	263
Net proved developed reserves	**2,339**	**329**	**2,696**	**378**	**5,035**	**707**
Net proved undeveloped reserves	173	24	247	35	420	59
Net proved developed and undeveloped reserves	**2,512**	**353**	**2,943**	**413**	**5,455**	**766**

(in millions of Russian Roubles)

Movements in Proved Oil Reserves

	Net proved reserves of crude oil recoverable up to license expiry dates		**Net proved reserves of crude oil recoverable past license expiry dates**		**Total net proved reserves of crude oil**	
	(millions of barrels)	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*	*(millions of barrels)*	*(millions of tons)*
Balance at December 31, 2000	**2,303**	**324**	**3,641**	**510**	**5,944**	**834**
Revisions	384	54	(698)	(97)	(314)	(43)
Production	(175)	(25)	-	-	(175)	(25)
Balance at December 31, 2001	**2,512**	**353**	**2,943**	**413**	**5,455**	**766**
Revisions	25	4	667	93	692	97
Production	(175)	(25)	-	-	(175)	(25)
Balance at December 31, 2002	**2,362**	**332**	**3,610**	**506**	**5,972**	**838**
Revisions	(70)	(9)	233	33	163	24
Production	(176)	(25)	-	-	(176)	(25)
Balance at December 31, 2003	**2,116**	**298**	**3,843**	**539**	**5,959**	**837**

Standardized Measure, Including Year-to-Year Changes Therein, of Discounted Future Cash Flows

For the purposes of the following disclosures, estimates were made of quantities of proved reserves and the periods in which they are expected to be produced. Future cash flows were computed by applying year-end prices (as described below) to the Group's estimated annual future production from proved oil reserves. Future development and production costs were computed by applying year-end costs to be incurred in producing and further developing the proved reserves. Future income taxes were computed by applying, generally, year-end statutory tax rates (adjusted for tax deductions, tax credits and allowances) to the estimated future pretax cash flows. The discount was computed by application of a 10% discount factor. The calculations assumed the continuation of existing political, economic, operating and contractual conditions at each of December 31, 2003, 2002, and 2001. However, such arbitrary assumptions have not necessarily proven to be the case in the past and may not in the future. Other assumptions of equal validity would give rise to substantially different results. As a result, future cash flows calculated under this methodology are not necessarily indicative of the Group's future cash flows nor the fair value of its oil reserves.

The net price used in the forecast of future net revenue is the weighted average year end price received for sales domestically, for exports to Commonwealth of Independent States ("CIS") countries, and for exports to non-CIS countries, after adjustments, where applicable, for certain costs, duties, and taxes. The weighted average net prices per ton used in the forecasts for 2003, 2002, and 2001, are US $120.61, US $93.81 and US $81.89 (US $16.93, US $13.17 and US $11.50 per barrel), respectively.

	Year ended December 31, 2003		
	Future cash flows attributable to net proved reserves recoverable up to license expiry dates	Future cash flows attributable to net proved reserves recoverable past license expiry dates	Future cash flows attributable to total recoverable net proved reserves
Future cash inflows from production	1,092,195	1,984,230	3,076,425
Future development and production costs	(636,470)	(1,237,051)	(1,873,521)
Future income taxes	(157,631)	(121,647)	(279,278)
Future net cash flows	**298,094**	**625,532**	**923,626**
10% annual discount	(109,124)	(527,740)	(636,864)
Discounted future net cash flows	**188,970**	**97,792**	**286,762**

(in millions of Russian Roubles)

Standardized Measure, Including Year-to-Year Changes Therein, of Discounted Future Cash Flows (continued)

	Year ended December 31, 2002		
	Future cash flows attributable to net proved reserves recoverable up to license expiry dates	Future cash flows attributable to net proved reserves recoverable past license expiry dates	Future cash flows attributable to total recoverable net proved reserves
Future cash inflows from production	1,005,955	1,537,793	2,543,748
Future development and production costs	(637,002)	(1,016,709)	(1,653,711)
Future income taxes	(97,381)	(107,108)	(204,489)
Future net cash flows	**271,572**	**413,976**	**685,548**
10% annual discount	(102,970)	(343,204)	(446,174)
Discounted future net cash flows	**168,602**	**70,772**	**239,374**

	Year ended December 31, 2001		
	Future cash flows attributable to net proved reserves recoverable up to license expiry dates	Future cash flows attributable to net proved reserves recoverable past license expiry dates	Future cash flows attributable to total recoverable net proved reserves
Future cash inflows from production	1,018,291	1,192,994	2,211,285
Future development and production costs	(683,160)	(814,821)	(1,497,981)
Future income taxes	(91,967)	(71,449)	(163,416)
Future net cash flows	**243,164**	**306,724**	**549,888**
10% annual discount	(93,774)	(255,707)	(349,481)
Discounted future net cash flows	**149,390**	**51,017**	**200,407**

Changes in the Standardized Measure of Discounted Future Net Cash Flows From Proved Reserve Quantities

	Year ended December 31, 2003		
	Future cash flows attributable to net proved reserves recoverable up to license expiry dates	Future cash flows attributable to net proved reserves recoverable past license expiry dates	Future cash flows attributable to total net proved reserves
Beginning of year	**168,602**	**70,772**	**239,374**
Sales and transfers of oil produced, net of production costs and other operating expenses	(34,194)	-	(34,194)
Net change in prices received per ton, net of production costs and other operating expenses	77,633	35,356	112,989
Change in estimated future development costs	4,532	(8,347)	(3,815)
Revisions of quantity estimates	(8,514)	5,024	(3,490)
Development costs incurred during the period	6,958	-	6,958
Accretion of discount	21,228	8,195	29,423
Net change in income taxes	(41,721)	13,847	(27,874)
Changes in production rate and other	(5,554)	(27,055)	(32,609)
End of year	**188,970**	**97,792**	**286,762**

(in millions of Russian Roubles)

Changes in the Standardized Measure of Discounted Future Net Cash Flows From Proved Reserve Quantities (continued)

	Year ended December 31, 2002		
	Future cash flows attributable to net proved reserves recoverable up to license expiry dates	Future cash flows attributable to net proved reserves recoverable past license expiry dates	Future cash flows attributable to total net proved reserves
Beginning of year	**149,390**	**51,017**	**200,407**
Sales and transfers of oil produced, net of production costs and other operating expenses	(33,896)	-	(33,896)
Net change in prices received per ton, net of production costs and other operating expenses	50,332	7,082	57,414
Change in estimated future development costs	(1,565)	(510)	(2,075)
Revisions of quantity estimates	3,676	28,673	32,349
Development costs incurred during the period	8,104	-	8,104
Accretion of discount	18,861	4,953	23,814
Net change in income taxes	(8,155)	(10,976)	(19,131)
Changes in production rate and other	(18,145)	(9,467)	(27,612)
End of year	**168,602**	**70,772**	**239,374**

	Year ended December 31, 2001		
	Future cash flows attributable to net proved reserves recoverable up to license expiry dates	Future cash flows attributable to net proved reserves recoverable past license expiry dates	Future cash flows attributable to total net proved reserves
Beginning of year	**299,447**	**95,533**	**394,980**
Sales and transfers of oil produced, net of production costs and other operating expenses	(44,376)	-	(44,376)
Net change in prices received per ton, net of production costs and other operating expenses	(225,457)	(123,632)	(349,089)
Change in estimated future development costs	(27,409)	11,089	(16,320)
Revisions of quantity estimates	26,574	(34,697)	(8,123)
Development costs incurred during the period	14,392	-	14,392
Accretion of discount	42,325	11,987	54,312
Net change in income taxes	104,187	55,208	159,395
Changes in production rate and other	(40,293)	35,529	(4,764)
End of year	**149,390**	**51,017**	**200,407**