

**TRANSFORMING INTO  
A GLOBAL GAS COMPANY**



Annual Report

# 2017





Annual Report

**2017**

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## NOVATEK—

is one of the largest independent natural gas producers in Russia. The Company is engaged in the exploration, production, processing, transportation and marketing of natural gas, LNG and liquid hydrocarbons.

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# Letter to Shareholders



ALEXANDER NATALENKO  
Chairman of the Board  
of Directors

## DEAR SHAREHOLDERS,

IN TWO THOUSAND AND SEVENTEEN we reached a landmark milestone in the Company's history as we successfully launched our Yamal LNG project and outlined our new corporate strategy to the year 2030. Both events sent a clear and strong message that our future lies in unlocking the vast resource potential of the Yamal and Gydan peninsulas to become one of the largest LNG producers in the world.

On 12 December 2017, we held our Corporate Strategy Day in Moscow that comprehensively outlined our

long-term strategy covering the period up to 2030, highlighting our views of the global markets and how we believe NOVATEK can play a key role in delivering clean-burning, affordable and secure energy to the global markets. The process of **TRANSFORMING INTO A GLOBAL GAS COMPANY** and a major global LNG player began with the successful launch of our first liquefied natural gas (LNG) production in 2017.

From July 2005, when we went public, we used the analogy of the four pillars model to highlight the attractiveness of NOVATEK as an investment opportunity: high quality long life reserves, strong production



LEONID MIKHELSON  
Chairman of the  
Management Board

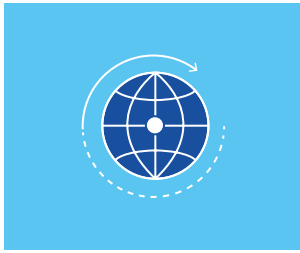


MARK GYETVAY  
Deputy Chairman  
of the Management Board

growth, low operating cost and low risk to commodity price movements. Now we proudly add a fifth column – scalable LNG projects – further strengthening our foundation, our uniqueness, and our investment story. Natural gas will play a leading role in the global future energy mix to 2030 and beyond, and our new corporate strategy transforms NOVATEK into a global gas and LNG power. At the same time we are still focused on our existing business model that is committed to delivering uninterrupted natural gas to the Russian domestic market. This path generates sustainable operating cash flows to fund our larger LNG ambitions.

Natural gas delivered to the markets in the form of LNG will lead the way in a world quickly transforming to a lower carbon, greener environment. NOVATEK's next strategic direction is to become one of the world's largest LNG producers by utilizing our significant low-cost, conventional natural gas resource base combined with the unique experience we gained in LNG development and construction in the Arctic.

We also introduced our new brand identity, a creative interpretation of liquefying gas molecules. Our new corporate identity represents a symbolic break from our past and the beginning of our new future and our



**The process of transforming into a global gas company and a major global LNG player began with the successful launch of our first liquefied natural gas production in 2017.**

bold and contemporary vision to meet the energy challenges of tomorrow and for decades to come.

In December 2017, we successfully commenced producing LNG at the Yamal LNG project first liquefaction train with the nameplate capacity of 5.5 million tons per annum, and made the first LNG tanker shipment using the Arc7 ice-class tanker “Christophe de Margerie”. This event represents an extraordinary accomplishment. Yamal LNG is also a great example of how we implement our strategy leveraging our strengths while maintaining our strong focus on cost control and project execution. We have taken conceptual ideas and transformed these concepts into tangible results. We constructed a world-class LNG project on permafrost, the first of its kind. We developed a test model of a tanker hull and then delivered the first Arc7 ice-class tanker.

The commencement of LNG production was the cumulative result of many months of hard work and dedication by thousands of construction workers, installers, and engineers who have worked and continue to work in Sabetta. We have developed this large-scale project on time and on budget despite harsh climatic conditions and less than ideal market conditions. This accomplishment is something to be very proud of as a company.

Successful development of our first LNG project paves the way to develop the prolific resource base of the Arctic region. In November 2017 we signed a Strategic Cooperation Agreement with the Chinese National Petroleum Company (CNPC) on cooperation in implementing the Arctic LNG 2 project, as well as collaborating in different segments of the LNG and natural gas markets, including LNG trading and gas infrastructure development. Our companies already have a history of effective cooperation, and we believe our continued cooperation will open up new

opportunities for both companies, utilizing our experience in implementing LNG projects combined with the enormous opportunities in the Chinese market, one of the most perspective gas markets globally. In November, we also signed a Memorandum of Understanding with the China Development Bank on cooperation in implementing the Arctic LNG 2 project, as well as other NOVATEK’s projects.

To efficiently develop our vast resource base in the Far North, decrease construction costs and increase the competitiveness of our future LNG-projects, we decided to create an LNG construction center in Russia. In June 2017, we signed a Memorandum of Understanding with the Ministry of Industry and Trade and the Murmansk Region Government on creating a center for the construction of large-scale offshore structures in Belokamenka, located in the Murmansk region.

We are working to optimize LNG transportation logistics via the Northern Sea Route and utilize lower cost conventional LNG tankers to ultimately deliver LNG to the Asian markets. We are studying the economic feasibility of building an LNG transshipment terminal at Kamchatka where the LNG will be delivered from the Yamal and Gydan peninsulas by Arc7 ice-class LNG carriers and then reloaded onto conventional LNG tankers and shipped to the final customers. This transshipment facility will reduce transportation costs as well as provide security of supply for Asian countries requiring flexibility to purchase volumes on short notice and short delivery times. Moreover, we will save a significant amount of travel time between routes, lowering the boil-off gas volumes due to the shorter transport distance. Our boil-off gas will be sold to the local gas network in Kamchatka and cover the operating costs of running the transshipment facility. In 2017, we concluded a Cooperation Agreement with the Kamchatka Territorial Government on building a sea terminal reloading facility.



# 65

**bcm – natural gas sales volumes in 2017**

Our massive hydrocarbon resource position ranks NOVATEK as one of the largest oil and gas companies in the world. Large, high quality, low-cost resource base in the hydrocarbon rich Yamal and Gydan peninsulas underlies our growth strategy. In June and August of 2017, we successfully expanded our resource base by winning the auctions and obtaining the new licenses on the Yamal and Gydan peninsulas complementing our LNG development strategy: Gydanskoye, Verhnetiuteyskoye, West-Seyakhinskoye and Shormovoye fields. During the reporting year, we also acquired South-Khadyryakhinskoye, Syskonsynyinskoye fields, West-Yaroyakhinskiy license area and won an auction for the Osennyi license area thus adding to our resource base within the reach of the Unified Gas Supply System, or UGSS.

In 2017, the Company's reserves were also positively impacted by successful exploration works at the Utrenneye, Kharbeyskoye, West-Yurkharovskoye and Urengoykoye (Samburgskiy license area) fields and production drilling at the South-Tambeyskoye field. Total SEC proved reserves, including the Company's proportionate share in joint ventures, aggregated 15,120 million barrels of oil equivalent (boe), including 2,098 billion cubic meters (bcm) of natural gas and 164 million metric tons (mmt) of liquid hydrocarbons. Total proved reserves increased by 12.8% compared to the year-end 2016, representing a reserve replacement rate of 435% for the year.

Excluding the effect of obtaining new licenses, our total proved reserves increased by 1.3%, representing an organic reserve replacement rate of 134%. At year-end 2017, the Company's reserve to production ratio (or R/P ratio) increased to 29 years as compared to 24 years in 2016. We retained our core competitive advantage being ranked among the lowest cost hydrocarbon producers globally, and our

# 91%

**overall Yamal LNG project progress as of the end of 2017**

lifting costs remained at a very low level of \$0.8 per BOE. We are fully committed to our strategy providing for strict cost control and conservative financial policies.

We are actively working to sustain production levels within the reach of the UGSS, which is one of NOVATEK's strategic priorities. We are working both on new fields' development as well as conducting exploration activities on our current producing assets to drill deeper into the Achimov and Jurassic layers. Technology will be used to increase production at our core domestic assets by using multi-stage fracturing techniques to stimulate production flows in the lower permeable Achimov and Jurassic formations. At the wells drilled in 2017, we have achieved very good flow rates for natural gas and gas condensate as well as higher gas condensate factor than earlier wells, which means we can optimize the cost of our development program and increase profitability of our projects. We will deploy this new deeper drilling program across a range of our fields.

During the past year, total hydrocarbon production totaled 513.3 million barrels of oil equivalent, including 63.40 billion cubic meters of natural gas and 11,774 thousand tons of liquids (gas condensate and crude oil). Loading our gas condensate processing facilities to maximize risk-adjusted margins for many years to come remains our priority, and in 2017, we achieved this objective. In 2017, our processing facilities reached milestone volumes: the Purovsky Plant processed its 65th million tons of gas condensate since its launch in 2005, and the Ust-Luga Complex – its 25th million tons since its launch in 2013.

We increased our natural gas sales volumes to 65.0 bcm in 2017, including the first LNG sales volumes, which was 0.5% higher compared with 2016. In December 2017, NOVATEK sold its first cargo of LNG.

We strengthened our balance sheet. Our current business generates sufficient operating cash flows to internally fund our operations, service our debt and liabilities, and distribute cash to our shareholders in the form of dividends. Our strong cash flow generated from our core domestic business has allowed us to significantly reduce our long-term debt portfolio and maintain strong credit metrics. In 2017, our revenues increased by 8.5% to RR 583 bln and our EBITDA increased by 5.8% to RR 256 bln while our Free Cash Flow increased by 7.6% to RR 151 bln.

Based on the Company's financial results, the Board of Directors recommended to the General Meeting of Shareholders to approve dividends for 2017 at RR 14,95 per share, exceeding the dividend paid out for the previous year by 7,6%.

One of our key priorities is to protect the ecosystems of the vulnerable and fragile environment of the Arctic region where our fields are located. In 2017, NOVATEK remained a constituent of the FTSE4Good Emerging Index of FTSE Russel Ratings and the Vigeo

# 513

mmboe – hydrocarbon production in 2017

# 15.1

bln boe – total hydrocarbon reserves (SEC)

Eiris Best Emerging Markets performers ranking (the 100 most advanced companies in Emerging Markets universe). Besides international acknowledgment of our efforts in environmental protection, social responsibility and corporate governance, we became the winner of the 2017 National Environmental Award named after Vladimir Vernadskiy in the nomination "Science for Ecology" with our Corporate Greenhouse Gas Emissions Control System implemented in 2017.

Stricter environmental standards are redefining the shipping industry's move towards cleaner types of fuels. We are confident that more shipping companies

will opt for LNG to meet stricter emission standards for marine transportation by 2020, and we are ready to facilitate the LNG bunkering market and infrastructure development. In 2017, Novatek Gas & Power, our wholly owned trading subsidiary, has joined the Society for Gas as a Marine Fuel and the SEA\LNG Association to help promote liquefied natural gas as a marine fuel.

It's also important to recognize the management team of NOVATEK and the many dedicated employees of the Company based at each of the subsidiary locations who contribute to **TRANSFORMING NOVATEK INTO A GLOBAL GAS COMPANY**. We would never achieve our strategic

goals without their commitment, dedication and hard work. We truly value their contribution to our success.

On behalf of the Board of Directors and Management Board, we are pleased to present to our valued stakeholders the Company's 2017 Annual Report. We would like to thank everyone for your continued support, as we remain committed to growing NOVATEK in a new strategic direction while implementing the best international practices and principles of sustainable development and corporate governance. We have begun a new chapter in our Company's history.

**We are working both on new fields' development as well as conducting exploration activities on our current producing assets to drill deeper into the Achimov and Jurassic layers.**

**ALEXANDER NATALENKO**  
Chairman of the Board of Directors



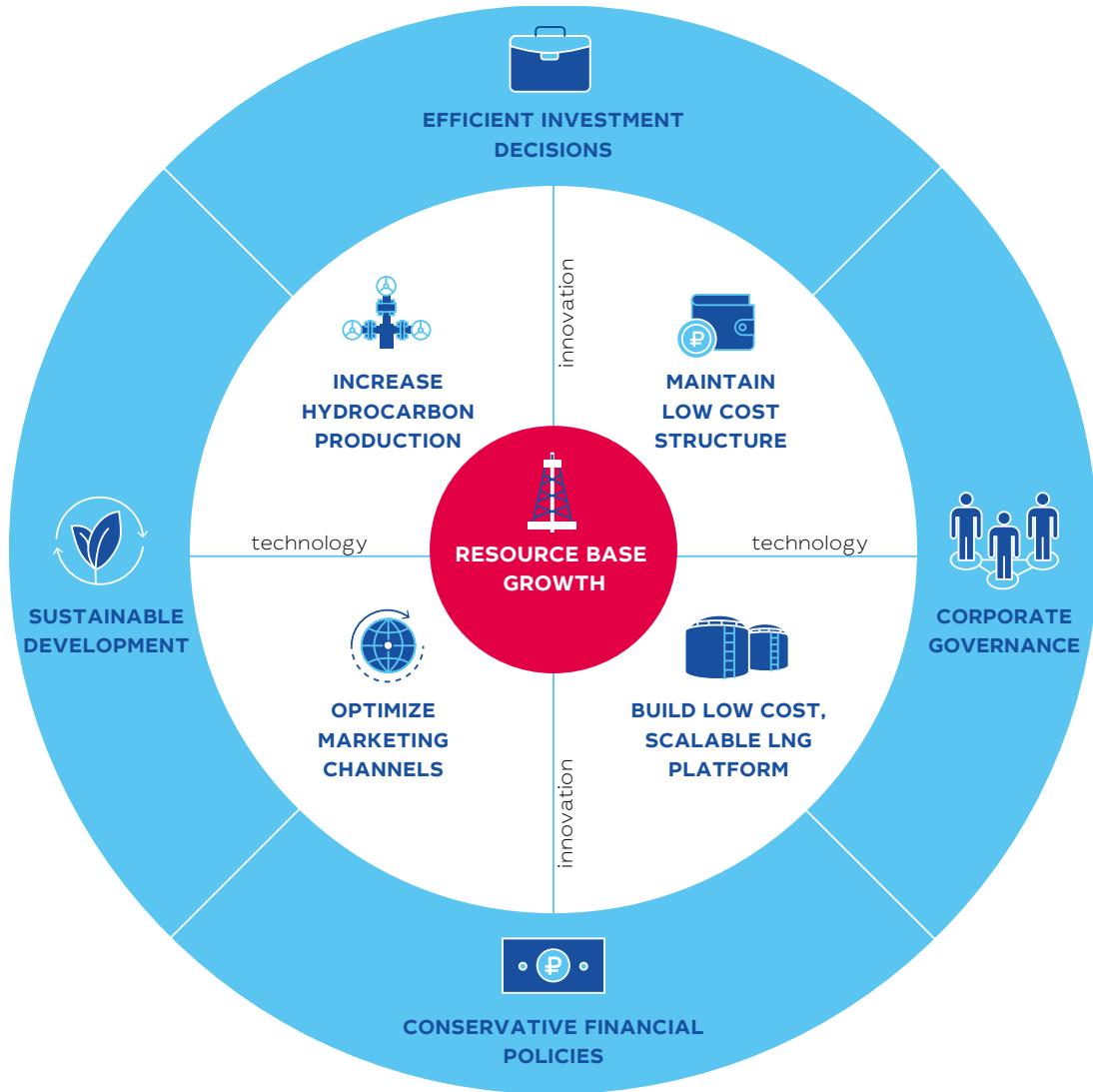
**LEONID MIKHELSON**  
Chairman of the  
Management Board



**MARK GYETVAY**  
Deputy Chairman  
of the Management Board



# Strategic Priorities

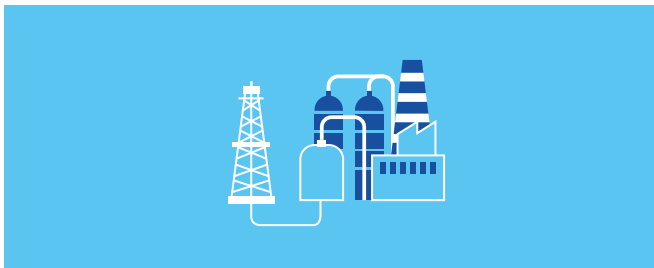


On 12 December 2017, the Company held its Corporate Strategy Day that comprehensively outlined our long-term strategy covering the period up to 2030.

The Company has a number of key competitive advantages to successfully implement its strategy: the size and structure of its hydrocarbon resource base; the close proximity of existing infrastructure to core producing fields; a well-developed customer base for natural gas sales; its own facilities for gas condensate processing and product exports; and a well developed marketing channel for liquefied petroleum gas (LPG). Development of LNG production capacities and LNG

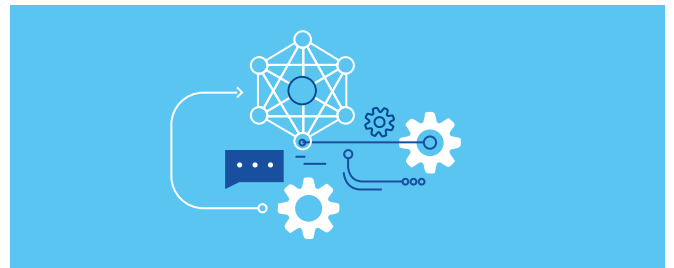
export sales is a key strategic priority for the Company. Another core priority is to increase production within the reach of the Unified Gas Supply System (UGSS) through development of new fields and exploration activities, and complimented by acquisitions which meet certain criteria. Our high level of operational flexibility and our consistent and efficient use of leading edge technologies in production and processing practices as well as our adherence to sound and prudent business management support our competitive position. Our commitment to social responsibility and to observing the latest environmental, health and safety standards are integral parts of NOVATEK's development strategy.

# Leveraging Our Strengths



## RESERVES, PRODUCTION, PROCESSING

- Prolific hydrocarbon resources in Western Siberia, including the Yamal and Gydan Peninsulas and within the reach of Unified Gas Supply System;
- Low cost of processing and production;
- Long-term, sustainable growth in production;
- Established liquids processing value chain.



## TECHNOLOGY AND INNOVATION

- Efficient use of state-of-the-art technologies to monetize prolific resource base;
- Implement high-tech projects in construction of processing facilities;
- Implement LNG projects in the Arctic Circle;
- Implement new innovative technology to build LNG plants on GBS;
- New liquefaction technology adapted for Arctic conditions.



## COMPANY AND PEOPLE

- Transparent governance structure;
- Experienced management, highly qualified technical specialists and dedicated employees;
- High standards of corporate governance, transparency and sustainability;
- Solid track record of project execution.



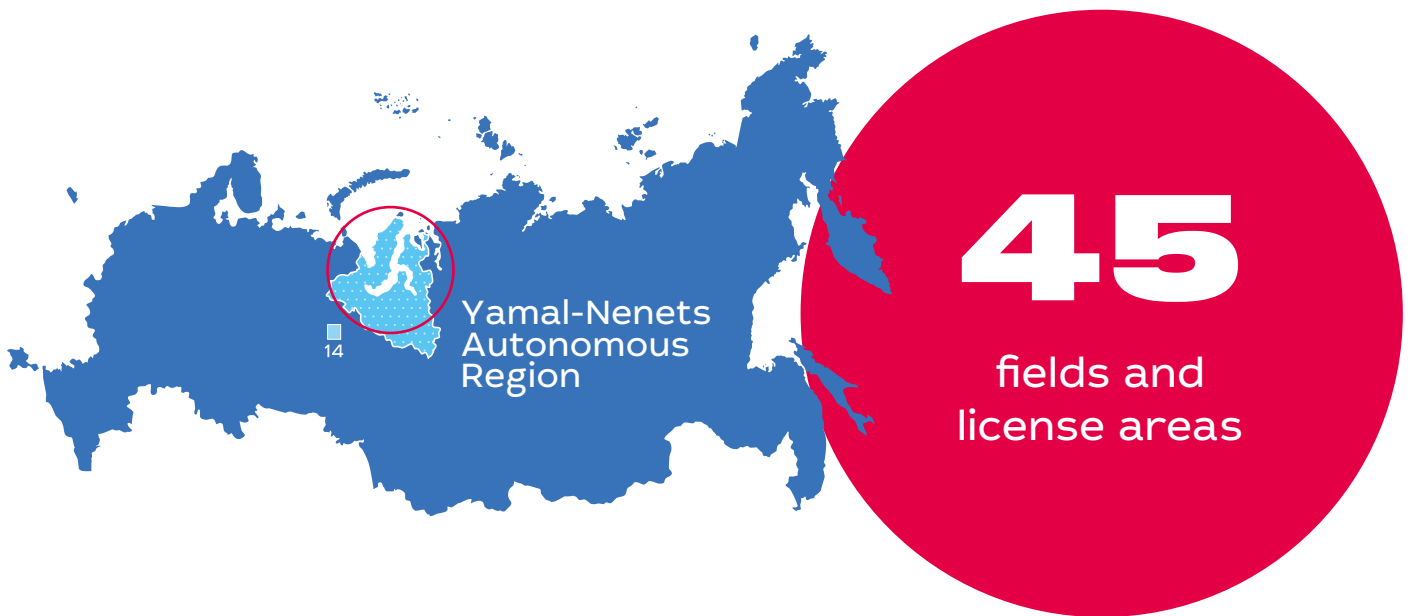
## FINANCE

- Strong financial and operational performance;
- Compelling business model generating sufficient free cash flows;
- Low financial leverage and strong credit metrics;
- Low debt levels and strong creditor protection.

# Hydrocarbon Resource Base

Large, high quality, low-cost hydrocarbon resource base to support strategic objectives





## PRODUCTION

1. Yurkharovskoye field
2. East-Tarkosalinskoye field
3. Khancheyskoye field
4. Olimpiyskiy license area
5. Yumantil'skiy license area
6. Samburgskiy license area
7. North-Urengoy'skoye field
8. North-Khancheyskoye field
9. Yaro-Yakhinskiy license area
10. Termokarstovoye field
11. Yarudeyskoye field
12. South-Tambeyskoye field<sup>1</sup>
13. West-Yaroyakhinskiy license area
14. Syskonsynynskiy license area (located in the Khanty-Mansiysk Autonomous Region)

Yamal LNG

Purovsky Gas Condensate Processing Plant

Gas condensate pipelines of NOVATEK

## PROSPECTIVE FIELDS AND LICENSE AREAS

15. West-Yurkharovskoye field
16. Raduzhnoye field
17. West-Urengoi'skiy license area
18. North-Yubileynoye field
19. North-Russkiy license area
20. North-Russkoye field
21. Dorogovskoye field
22. Ukrainsko-Yubileynoye field
23. Malo-Yamalskoye field
24. West-Chaselskoye field
25. Yevo-Yakhinskoye field
26. North-Chaselskiy license area
27. Utrenneye field<sup>2</sup>
28. Geofizicheskoye field
29. North-Ob'skiy license area
30. East-Tambeyskiy license area
31. North-Tasiyskiy license area
32. East-Tazovskoye field
33. Trekhbugorniy license area
34. Nyakhartinskiy license area
35. Ladertoyskiy license area
36. Nyavuyahskiy license area
37. West-Solpatinskiy license area
38. North-Tanamskiy license area
39. Syadorskiy license area
40. Tanamskiy subsoil area
41. Kharbeyskiy license area
42. Gydanskiy license area
43. Shtormovoy license area
44. Verhnetiuteyskiy + West-Seyakhinskiy LA
45. South-Khadyryakhinskiy license area

1. Yamal LNG Project.

2. Arctic LNG 2 Project.

# Key Events and Achievements 2017



We signed Cooperation Agreements with TechnipFMC, Linde AG and Research and Design Institute for Gas Processing and with JSC Atomenergomash and JSC United Shipbuilding Corporation.

The first liquefaction train at Yamal LNG successfully commenced producing LNG, and the first LNG tanker shipment was made using the Arc7 ice-class tanker “Christophe de Margerie”.

We signed a Memorandum of Understanding with the Ministry of Industry and Trade and the Murmansk Regional Government on creating a center for the construction of large-scale offshore structures.

We held our Corporate Strategy Day that comprehensively outlined our long-term strategy covering the period up to 2030.

We joined the Society for Gas as a Marine Fuel and the SEA\LNG Association.



NOVATEK remained a constituent of the FTS-E4Good Emerging Index of FTSE Russel Ratings and the Vigeo Eiris Best Emerging Markets performers ranking representing the 100 most advanced companies in Emerging Markets universe, and became the winner of the 2017 National Environmental Award named after Vladimir Vernadskiy in the nomination “Science for Ecology” with our Corporate Greenhouse Gas Emissions Control System.







We signed a Memorandum of Understanding (MOU) with the China Development Bank, a Strategic Cooperation Agreement with the Chinese National Petroleum Company (CNPC), a trilateral MOU with Marubeni Corporation and Mitsui O.S.K. Lines, Ltd. and an MOU with Total and Siemens on cooperation in Vietnam.



We signed a Cooperation Agreement with the Kamchatka Territorial Government on building a sea terminal facility for reloading liquefied natural gas (LNG).

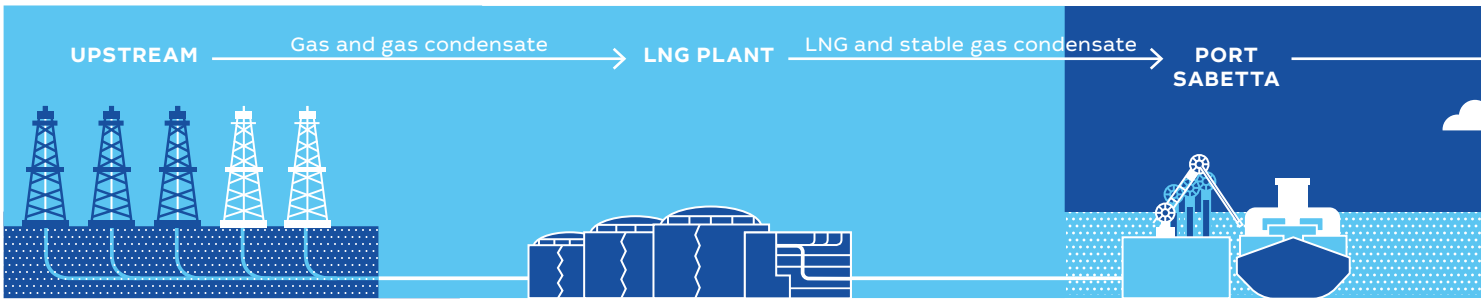


We obtained the new licenses on the Yamal and Gydan peninsulas winning the auctions for Gydanskoye, Verhnetiuteyskoye, West-Seyakhinskoye and Shormovoye fields and acquired the South-Khadyryakhinskoye, Syskonsynyinskoye fields and West-Yaroyakhinskiy license area.



# Yamal LNG Project

**YAMAL LNG is an integrated project for natural gas production, liquefaction and transportation. Starting LNG production at the first train of the plant and loading the first tanker NOVATEK entered the global gas market and became a worldwide gas company.**



**208**

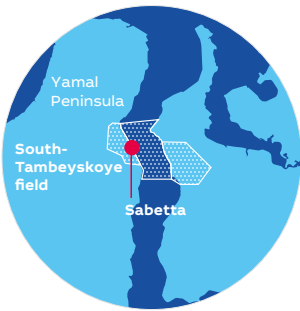
production wells stipulated by the field's development plan

**3**

production trains of liquefaction plant with annual capacity of 5.5 mmt each

**17.4**

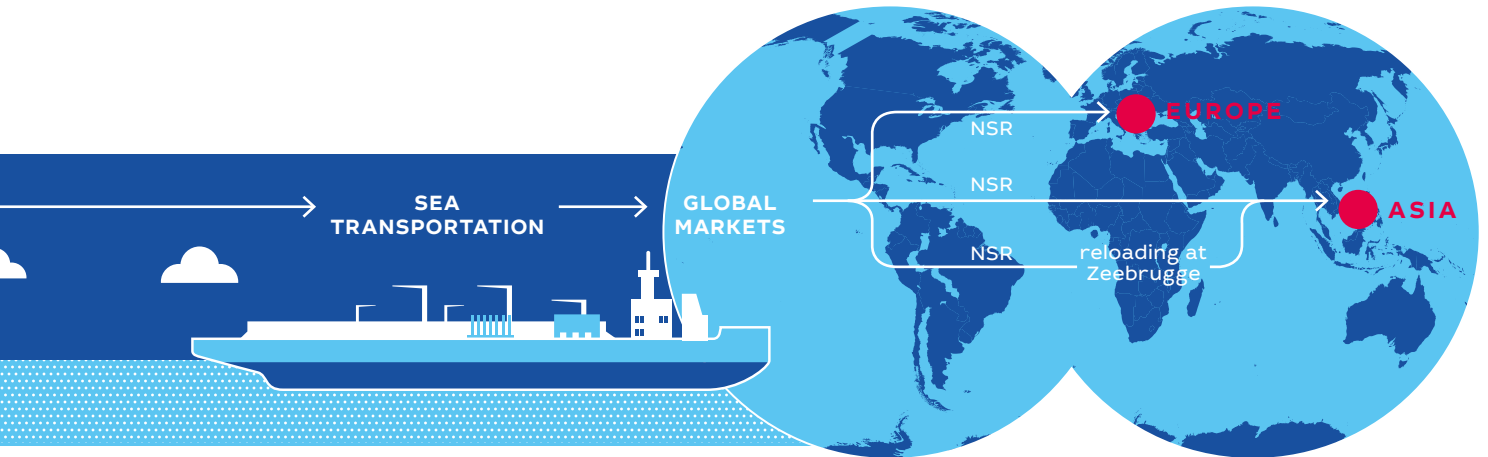
mmt per annum – capacity of the LNG plant



**27**

bcm of natural gas per annum – the field's production potential





**4th**

train with a capacity of 0.9 mmt

**91%**

overall Yamal LNG project progress

**Key Project Advantages**

- Large onshore conventional reserve base with high concentration of reserves;
- Well known geology and proven development technologies;
- Very low F&D and lifting costs;
- High efficiency factor of gas liquefaction process due to sub-zero temperatures;
- Access to both European and Asian markets.



**Arc7**

Ice-class LNG carrier of special design for LNG transportation

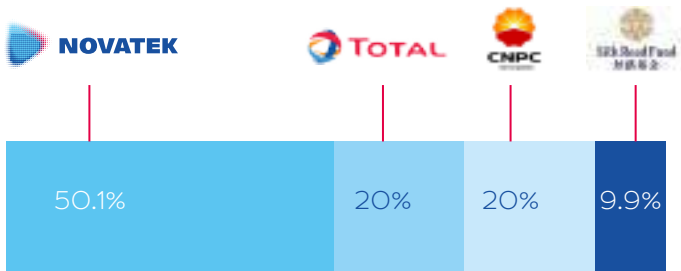
**170**

mcm – Cargo capacity of the Project's ARC7 tankers

**Project Implementation**

As of the end of 2017, the overall project progress was 91%. The South-Tambeyskoye field was estimated to contain 683 bcm of proved natural gas reserves and 21 mmt of proved liquid hydrocarbon reserves (SEC). 103 production wells were drilled at the field, all 142 modules for the LNG plant three trains had been delivered to the site by sea, 137 of them had been installed on the prepared foundations. More than 95% of the LNG volumes produced within the three trains of the project has been contracted on a long-term basis.

# Yamal LNG Project Implementation



Shareholders of Yamal LNG are NOVATEK (50.1%), Total (20%), CNPC (20%) and Silk Road Fund (9.9%).



1974

The South-Tambeyskoye field was discovered

2009

NOVATEK becomes a shareholder of OAO Yamal LNG, which holds license for exploration and production at the South-Tambeyskoye field

2012

FEED  
Sabetta port construction

2013

Drilling start



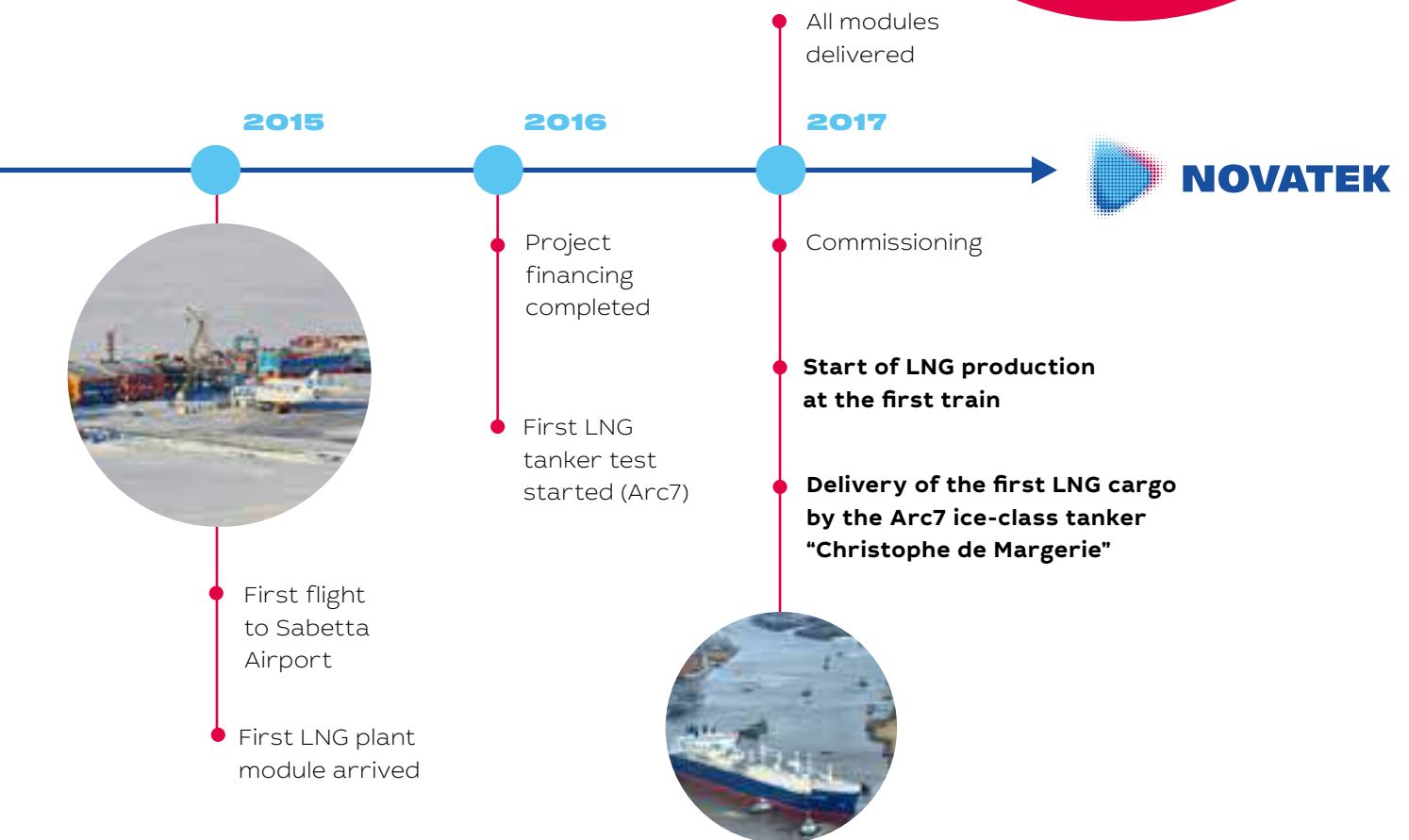
2014

First piling commenced



# 2017

In December 2017, the LNG production started



# LNG Logistics

The geographical location of our projects on Yamal and Gydan Peninsulas allows us to supply LNG to Europe and Asia using the Northern Sea Route and the traditional route through the Sea Route. We plan to build an LNG transshipment terminal on the Kamchatka Peninsula, which will reduce transportation costs and provide direct access to premium markets.

## LNG transshipment complex on the Kamchatka Peninsula



### Concept

- Moored LNG storage ship
- Option to sell FOB Kamchatka

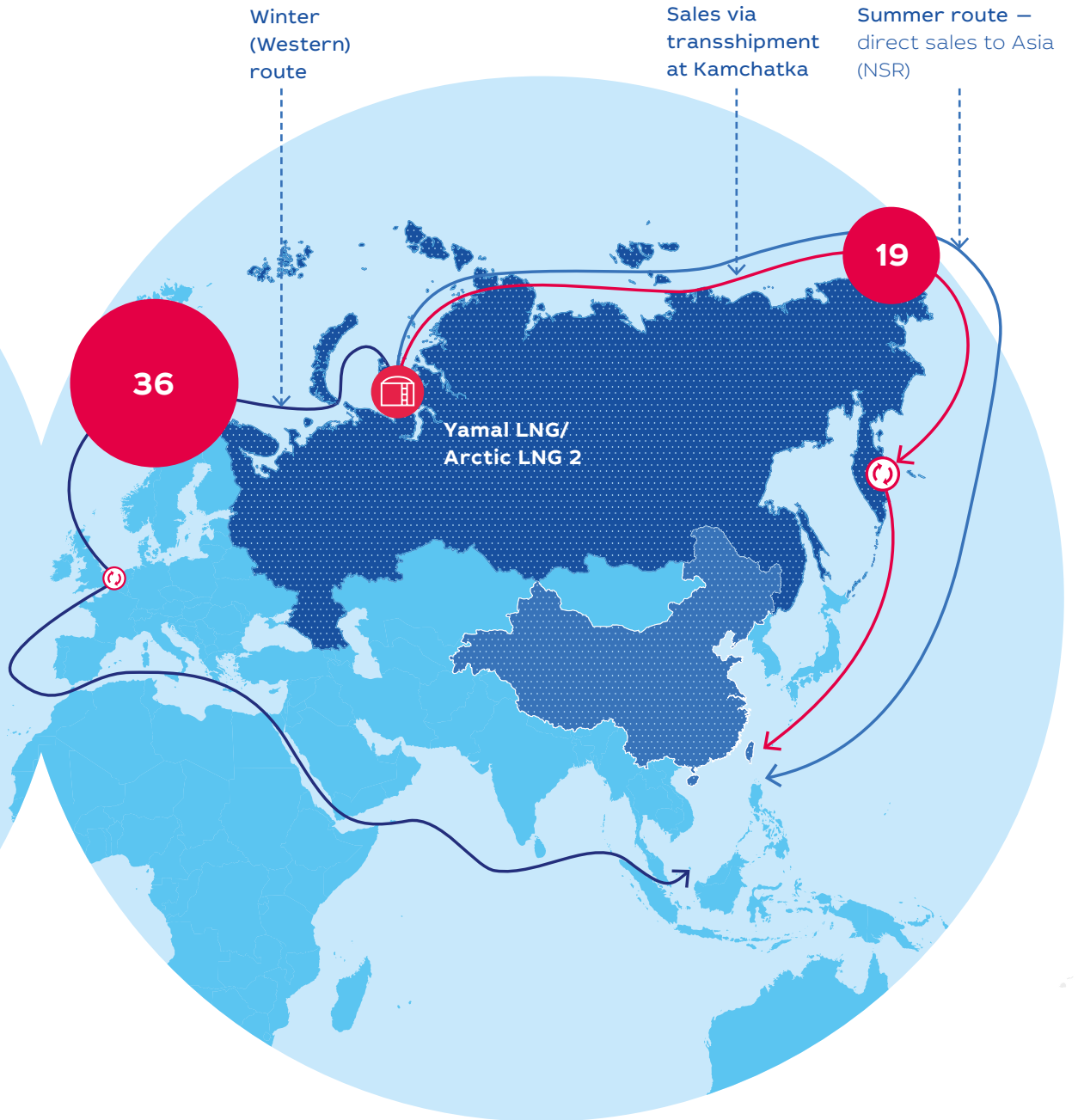
# 3.7

thousand nautical miles from Sabetta

# 20

mln tons per annum – Planned transshipment capacity





- Number of travel days
- ⌛ Transshipment (Europe/ Kamchatka)

# Transforming into a Global Gas Company



**17**

mmt of cargo  
delivered for  
plant construction



**103**

production wells  
drilled



**26**

thousand  
construction  
workers in  
Sabetta

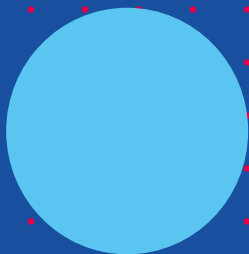


**142**

large plant mod-  
ules delivered



On 5 December, the first train at Yamal LNG successfully commenced producing LNG and on 8 December, the first LNG was loaded onto the ice-class tanker “Christophe de Margerie”.



**650**

companies from 55  
Russia's constituent  
regions

# Key Indicators

	Unit	2016	2017	Change
<b>FINANCIAL INDICATORS</b>				
Total revenues	RR mln	537,472	583,186	8.5%
Normalized profit from operations <sup>1</sup>	RR mln	152,194	163,751	7.6%
Normalized EBITDA (including share in EBITDA of JVs) <sup>1</sup>	RR mln	242,407	256,464	5.8%
Normalized profit attributable to shareholders of PAO NO-VATEK <sup>2</sup>	RR mln	133,759	156,166	16.8%
Normalized earnings per share <sup>2</sup>	RR	44.31	51.78	16.8%
Net cash provided by operating activities	RR mln	173,791	180,399	3.8%
Net cash used for capital expenditures <sup>3</sup>	RR mln	33,905	29,871	(11.9%)
Free cash flow	RR mln	139,886	150,528	7.6%
<b>OPERATING INDICATORS</b>				
Proved natural gas reserves (SEC)	bcm	1,848	2,098	13.5%
Proved liquid hydrocarbon reserves (SEC)	mmt	154	164	6.5%
Total hydrocarbon reserves (SEC)	mmboe	13,402	15,120	12.8%
Production of natural gas	bcm	67.6	63.4	(6.3%)
Production of liquid hydrocarbons	mt	12,441	11,774	(5.4%)
Total production	mln boe	547.0	513.3	(6.2%)
Daily production	mln boe per day	1.49	1.41	(5.9%)
<b>POSITIONS IN RUSSIA</b>				
Share in natural gas production <sup>4</sup>	%	10.5%	9.1%	(1.4) p.p.
Share in liquid hydrocarbon production <sup>4</sup>	%	2.3%	2.2%	(0.1) p.p.

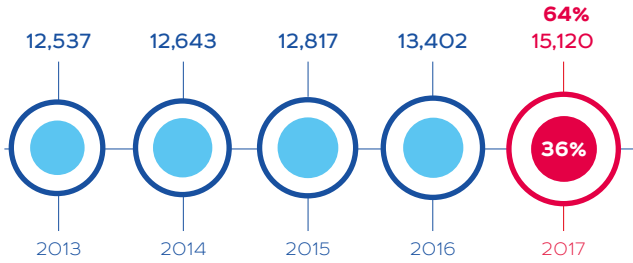
1. Excluding the effect from disposal of interests in joint ventures.

2. Excluding the effects from the disposal of interests in joint ventures, as well as foreign exchange gains (losses).

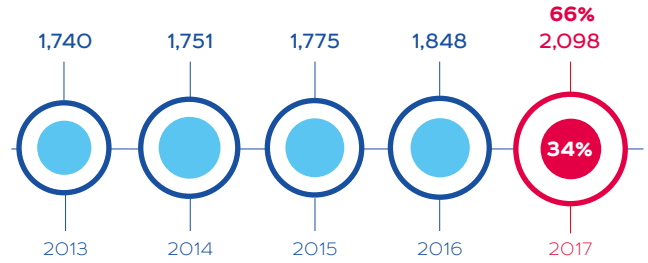
3. Cash used for capital expenditures represents purchases of property, plant and equipment, materials for construction and capitalized interest paid per Consolidated Statement of Cash Flows net of payments for mineral licenses and acquisition of subsidiaries.

4. According to CDU TEK information.

• Total proved hydrocarbon reserves (SEC), mmboe

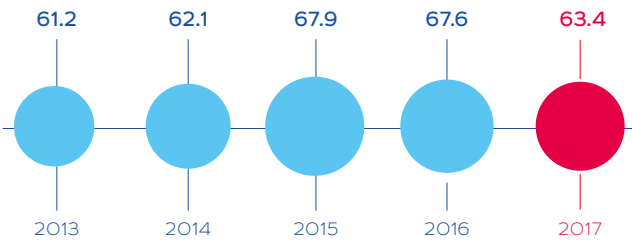


• Proved natural gas reserves (SEC), bcm

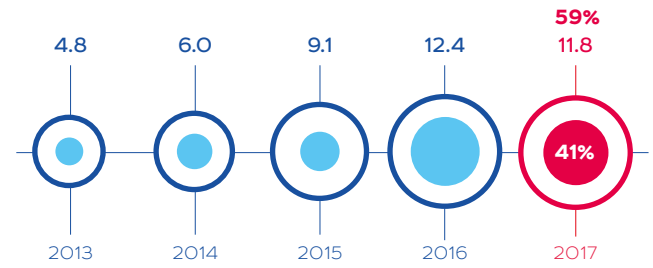


○ Proved undeveloped  
● Proved developed  
○ Proved undeveloped in 2017  
● Proved developed in 2017

• Natural gas production, bcm

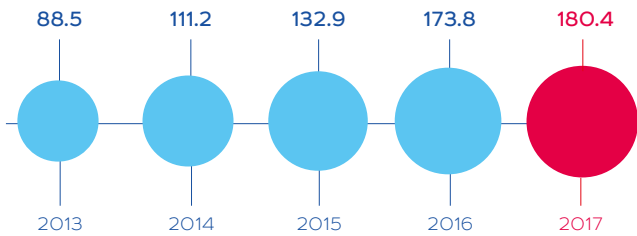


• Liquids production, mmt

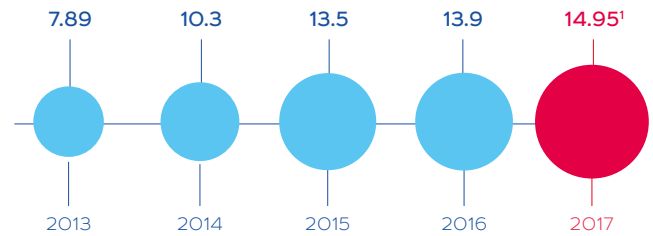


○ Gas condensate  
● Crude oil  
○ Gas condensate in 2017  
● Crude oil in 2017

• Operating cash flow, RR bln



• Dividends per share, RR



1. Recommendation of the Board of Directors.

# Geological Exploration and Production

**Yamal-Nenets Autonomous Region is the world's largest natural gas producing area and accounts for approximately 80% of Russia's natural gas production and approximately 15% of the world's gas production.**

As of 31 December 2017, NOVATEK's SEC proved reserves, including the Company's proportionate share in joint ventures, aggregated 15,120 million barrels of oil equivalent (mmboe), including 2,098 billion cubic meters (bcm) of natural gas and 164 million metric tons (mmt) of liquid hydrocarbons. The Company's proved reserves grew by 12.8%, and the reserve replacement ratio stood at 435%. At year-end 2017, the Company's reserve to production ratio (or R/P ratio) was 29 years.

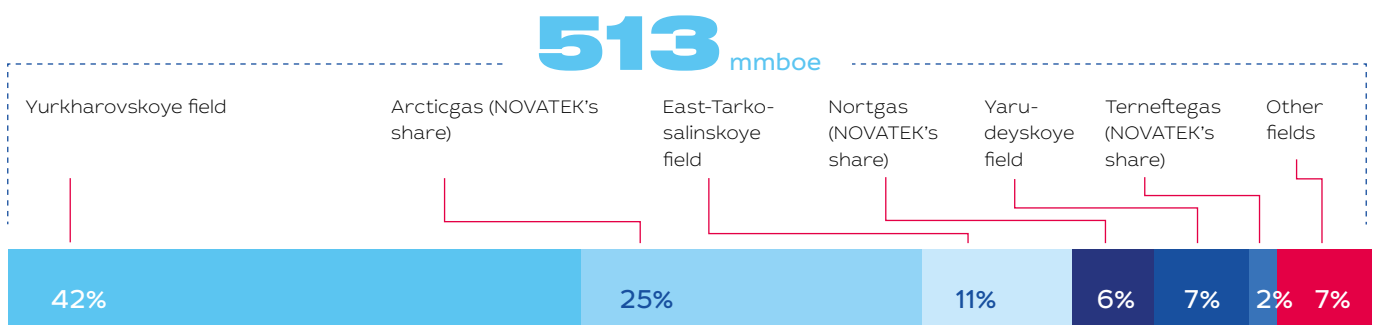
The Company's reserves were positively impacted by successful exploration works at the Utrenneye, Kharbeyenskoye, West-Yurkharovskoye and Urengoyenskoye (Samburgskiy license area) fields, production drilling at the South-Tambeyskoye field, as well as the new licenses obtained through tender auctions (Gydanskoye, Verhnetiuteyskoye and West-Seyakhinskoye fields) and recent asset acquisitions (South-Khadyryakhinskoye, Syskonsynyinskoye fields and West-Yaroyakhinskiy license area).

In 2017, we completed the running of 1,465 square kilometers of 3D seismic works and drilled 25 thousand

meters of exploration drilling. 26 new hydrocarbon deposits were discovered. Production drilling in 2017, including joint ventures, reached 262,000 m, which is 12% above the 2016 number. Increase in the drilling volumes was mainly driven by the development of the Yaro-Yakhinskoye field of Arcticgas with 9 wells drilled there (in 2016 no wells were drilled at the field). A total of 68 production wells, including 55 natural gas and gas condensate and 13 oil wells, were completed and commissioned.

In 2017, NOVATEK produced commercial hydrocarbons at 16 fields. The Company's production (including attributable share in the production of JVs) amounted to 513.3 mmboe, down 6.2% versus 2016. The production volumes at mature fields of our subsidiaries and joint ventures decreased mainly due to natural declines in the reservoir pressure at the current gas producing horizons. The decrease was partially offset by the improved efficiency of associated petroleum gas utilization at our Yarudeyskoye field, as well as the commencement of LNG production at the first LNG train at Yamal LNG in the fourth quarter of 2017.

• Structure of hydrocarbon production in 2017



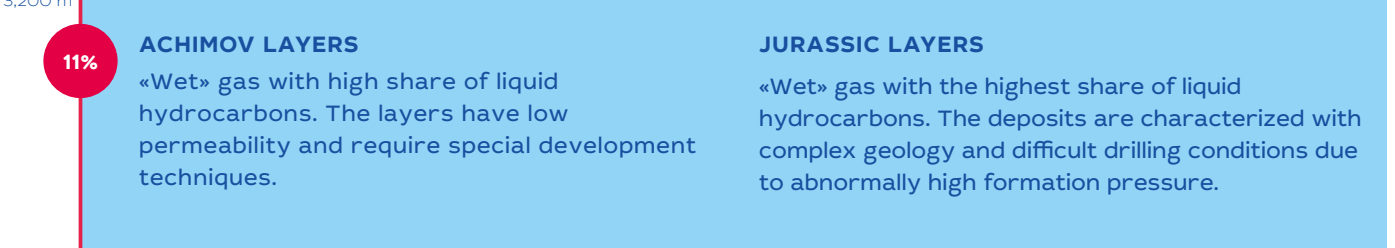
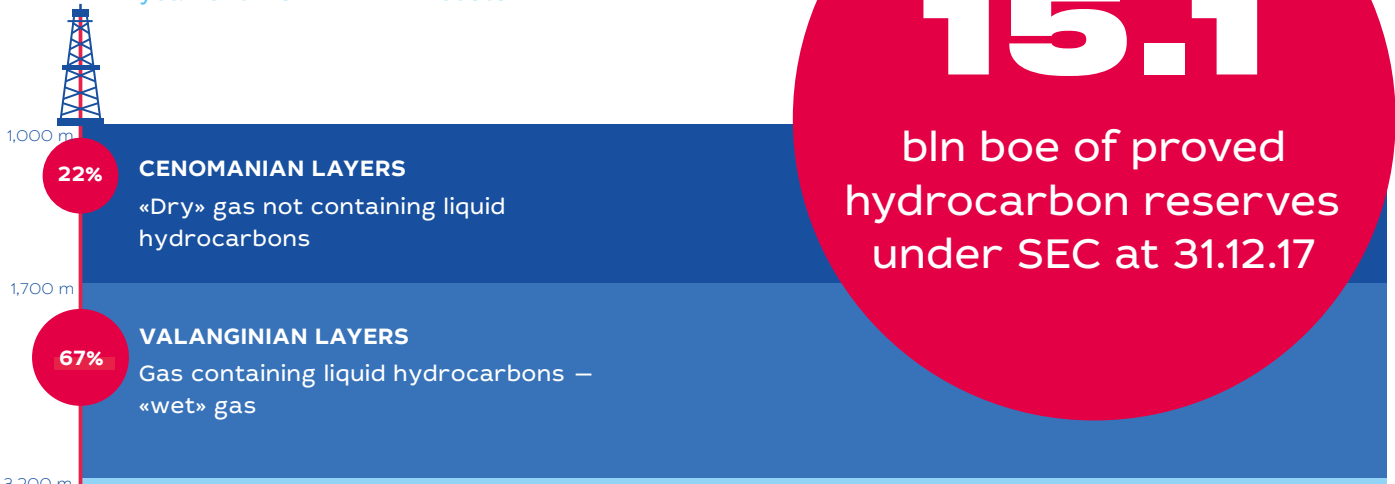
**29**

years – reserve to production ratio at year-end 2017

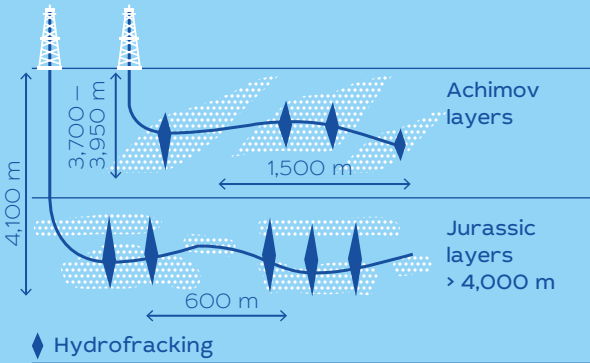
**\$2.3**

per boe – 2013–2017 reserve replacement costs

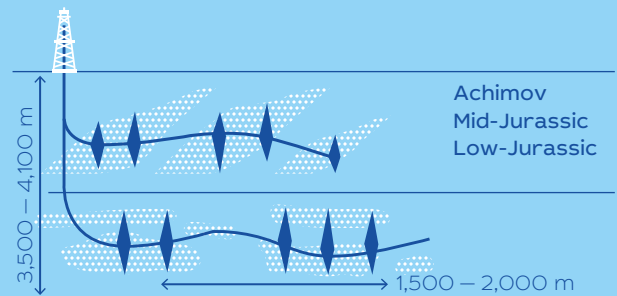
**15.1**  
bln boe of proved hydrocarbon reserves under SEC at 31.12.17



**Technologies to develop deep layers**



Technology previously used



Increase in wells productivity, Including increase in low permeable formations

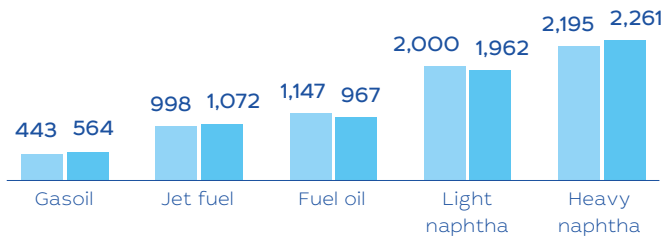
New technology

Main reserves and potential new resource additions from deep layers (Achimov, Jurassic etc.) are located in North-Russkoye cluster, South-Tambeyskoye field, Utrenneye field, Geofizicheskoye field, Olimpiyskiy LA, and West-Yurkharovskiy LA.

Lifting costs will remain low:  
 · Additional production from deeper fields utilize existing infrastructure on legacy fields  
 · Use new technologies

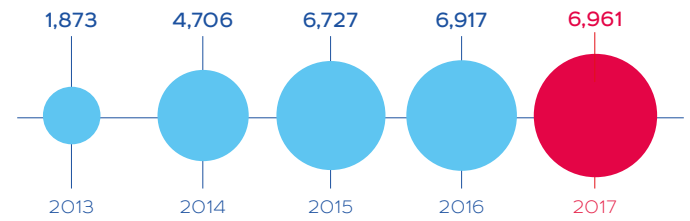
# Ust-Luga Complex

Output, thousand tons







● 2016 ● 2017

Stable gas condensate processing volumes, thousand tons



The six million ton per annum Gas Condensate Fractionation and Transshipment Complex (the “Ust-Luga Complex”) launched in 2013 is located at the all-season port of Ust-Luga on the Baltic Sea. The Ust-Luga Complex processes stable gas condensate into light and heavy naphtha, jet fuel, ship fuel component (fuel oil) and gasoil, and enables us to ship the value-added petroleum products to international markets. The Ust-Luga Complex also allows for transshipment of stable gas condensate to the export markets.

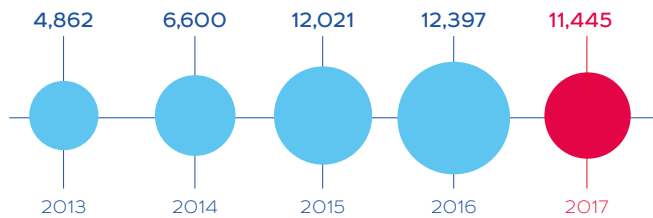
-  Railway transportation of stable gas condensate to Ust-Luga
-  Sea transportation of petroleum products from Ust-Luga
-  Transportation of unstable gas condensate by pipeline
-  Light hydrocarbons transportation by pipeline



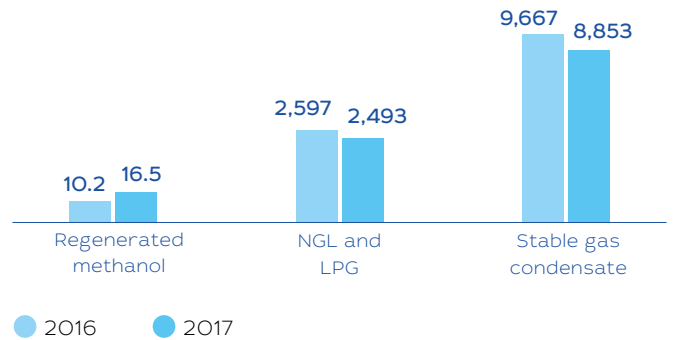
# Purovsky Plant

In 2017, our processing facilities reached milestone volumes: the Purovsky Plant processed its 65th million tons of gas condensate since the launch in 2005, and the Ust-Luga Complex – its 25th million tons since the launch in 2013.

Processing of de-ethanized condensate, thousand tons



Output, thousand tons



The Purovsky Plant is the central element in our vertically integrated value chain that provides us complete operational control over our processing needs and access to higher yielding marketing channels for our stable gas condensate. The Purovsky Plant processes unstable gas condensate into stable gas condensate and natural gas liquids (NGL).

The Purovsky Plant is connected via its own railway line to the Russian rail network at the Limbey rail station. Subsequent to the launch of the Ust-Luga Complex in 2013, most of the stable gas condensate volumes produced at the Purovsky Plant are delivered by rail to Ust-Luga for further processing or transshipment to exports, with the remaining volume of stable gas condensate sold directly from the plant to the domestic market.

All of the NGL volumes (feedstock for LPG production) produced at the plant are delivered by pipeline to SIBUR's Tobolsk Petrochemical Complex for further processing.

# Natural Gas Sales

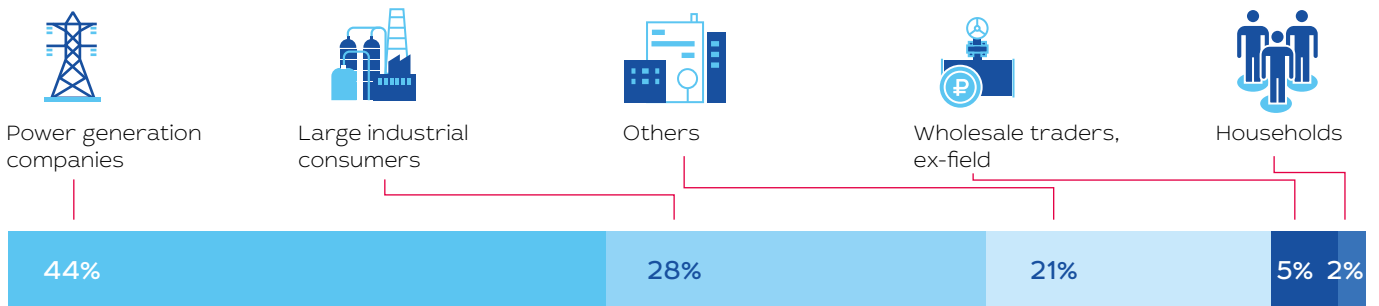
**NOVATEK plays an important role in ensuring supplies of natural gas to the Russian domestic market. During the past year, we supplied natural gas to 39 gas consuming regions of the Russian Federation.**

NOVATEK sells natural gas within the Russian Federation as well as exports natural gas in the form of LNG. The Company started exporting LNG in December 2017 when the first train at Yamal LNG started production.

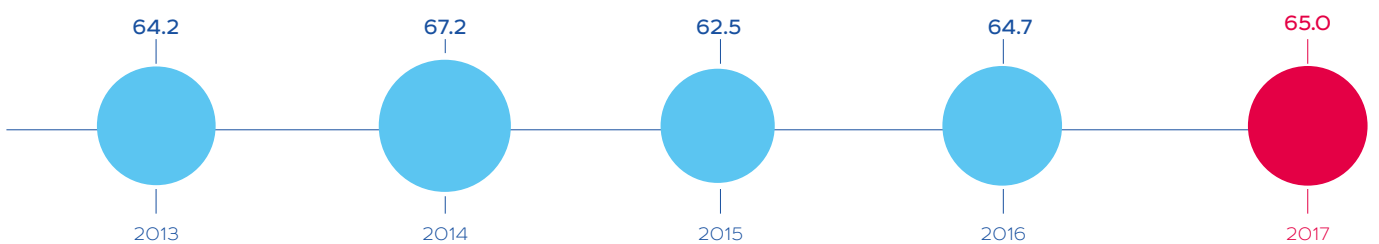
Revenues from natural gas sales in 2017 totaled RR 248 billion, representing a 7.8% increase compared to 2016. The revenue increase was mainly driven by growth in sales to end customers in Russia, the increase of Russian domestic regulated prices, as well as start of LNG deliveries.

The total volume of natural gas sales in 2017, including LNG, amounted to 65.0 bcm, increasing by 0.5% compared to the previous year due to a minor increase in sales volume within the Russian Federation as well as the commencement of LNG export sales.

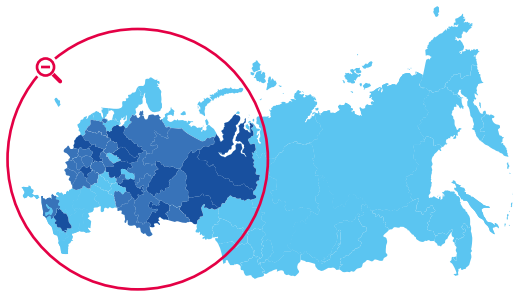
• **Natural gas sales breakdown on the Russian domestic market by customers in 2017**



• **Natural gas sales, bcm**







**39**  
regions of gas sales in the Russian Federation in 2017

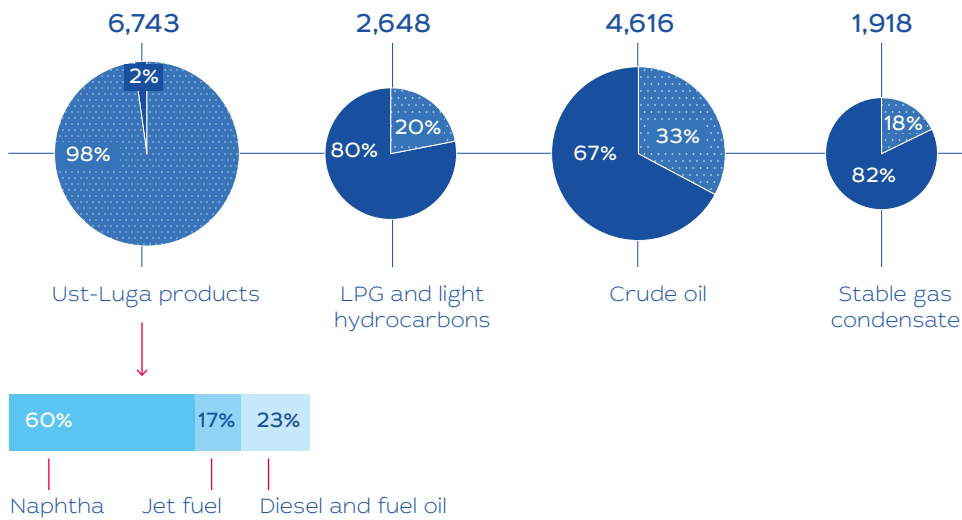
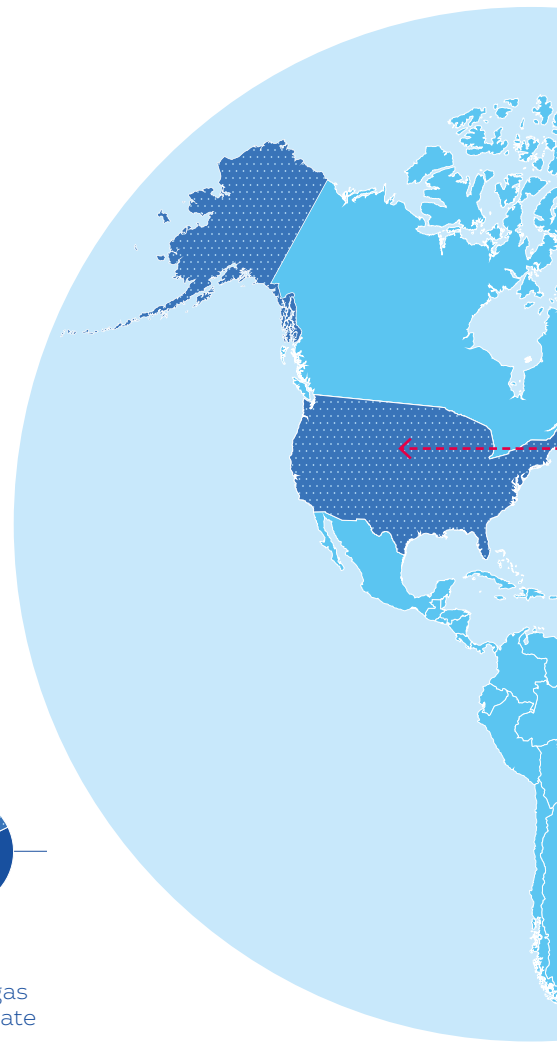
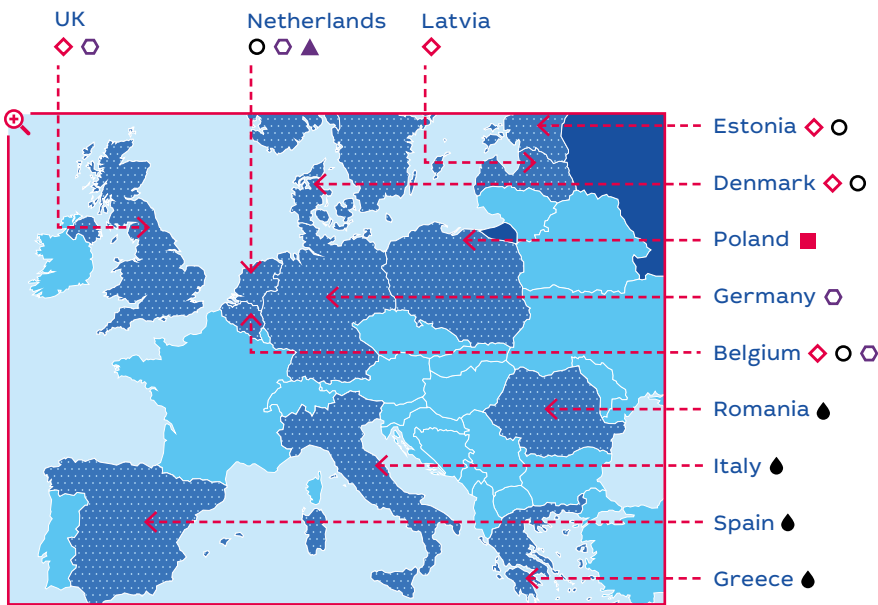


● Main regions of gas sales

● Other regions of gas sales

# Liquids Sales

**NOVATEK sells liquid hydrocarbons (stable gas condensate, petroleum products, light hydrocarbons, LPG and crude oil) domestically and internationally.**



RR **332**

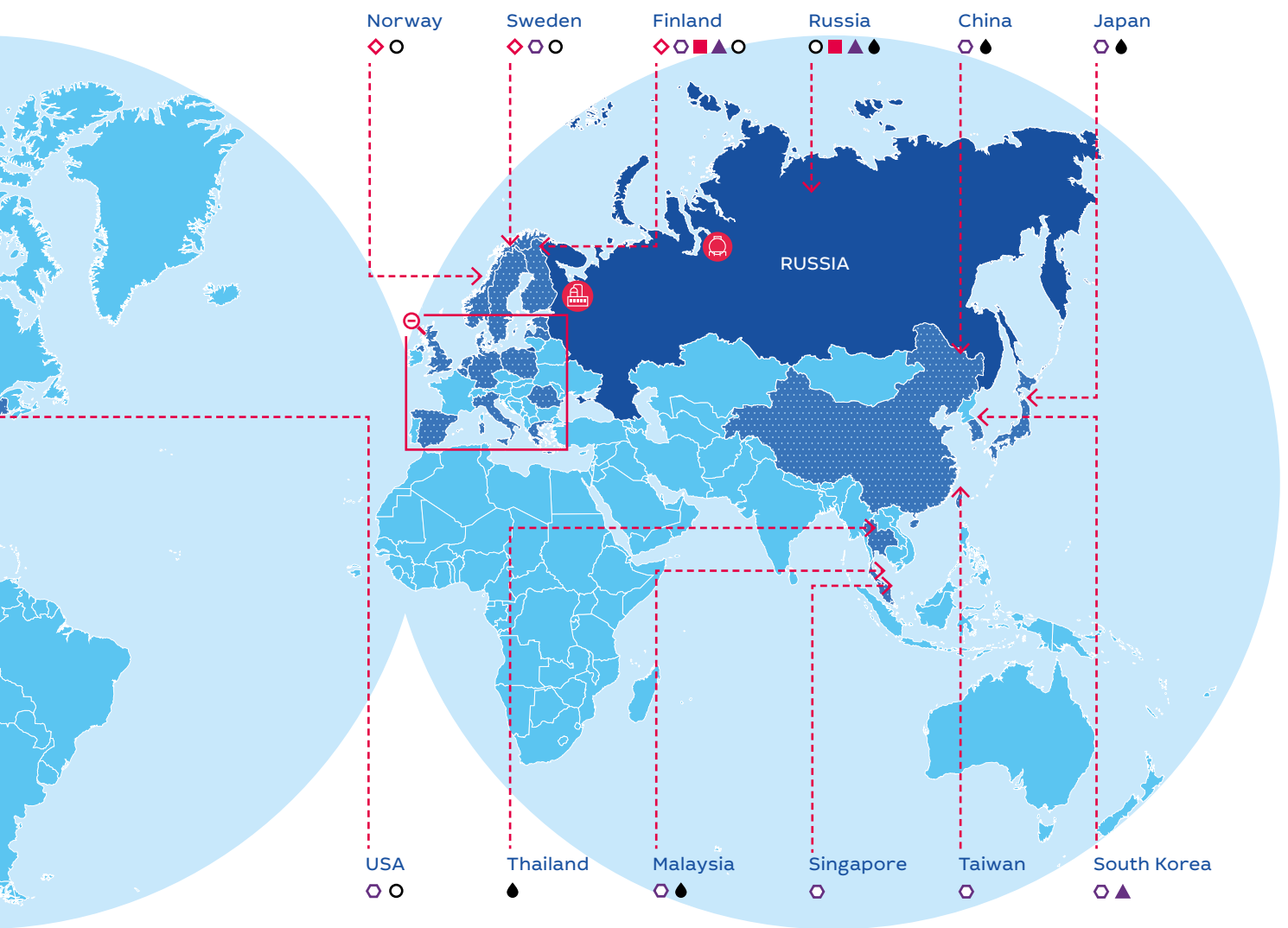
bln – Liquids sales revenues in 2017

**15.9**

mmt – Sales volumes of liquid hydrocarbons in 2017

In 2017, the liquids sales volume reached 15,939 mt, or 5.4% less than in 2016. In 2017, export sales decreased by 8.5% as compared to 2016 and amounted to 9,027 mt.

In 2017, our liquids sales revenues increased to RR 332 billion, or by 9.2% as compared to 2016, mainly driven by higher global oil prices and underlying benchmark prices.



- Domestic market
- Export markets
- Ust-Luga Complex
- Purovsky Plant

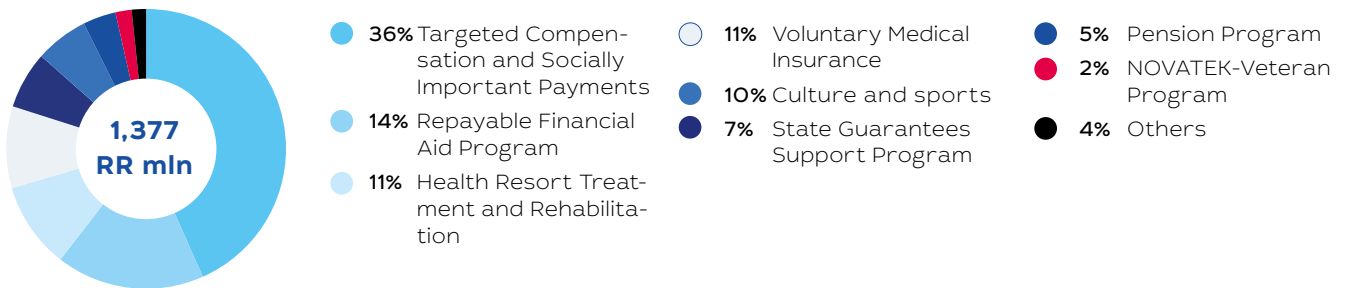
- Exports of LPG and light hydrocarbons
- Exports of crude oil
- ▲ Exports of stable gas condensate

- Exports of Ust-Luga products:
- ◇ Jet fuel
  - Diesel and fuel oil
  - Naphtha

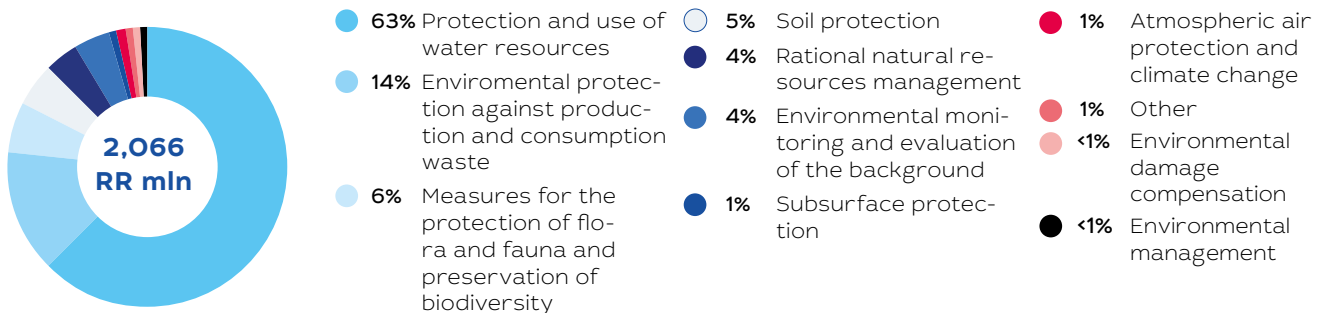
# Environmental and Social Responsibility

**NOVATEK adheres to the principles of effective and responsible business conduct and considers the welfare of its employees and their families, environmental and industrial safety, the creation of a stable and beneficial social environment as well as contributing to Russia's overall economic development as priorities and responsibilities of the Company.**

• Social Expenditures on employees in 2017



• Environmental Expenditures in 2017



NOVATEK’s core producing assets are located in the Far North, a harsh Arctic region with vast mineral resources and a fragile and vulnerable environment. The Company is committed to environmental protection in its operations. In 2017, the Company’s overall expenses on environment protection and sustainable nature management amounted to RR 2,066 mln.

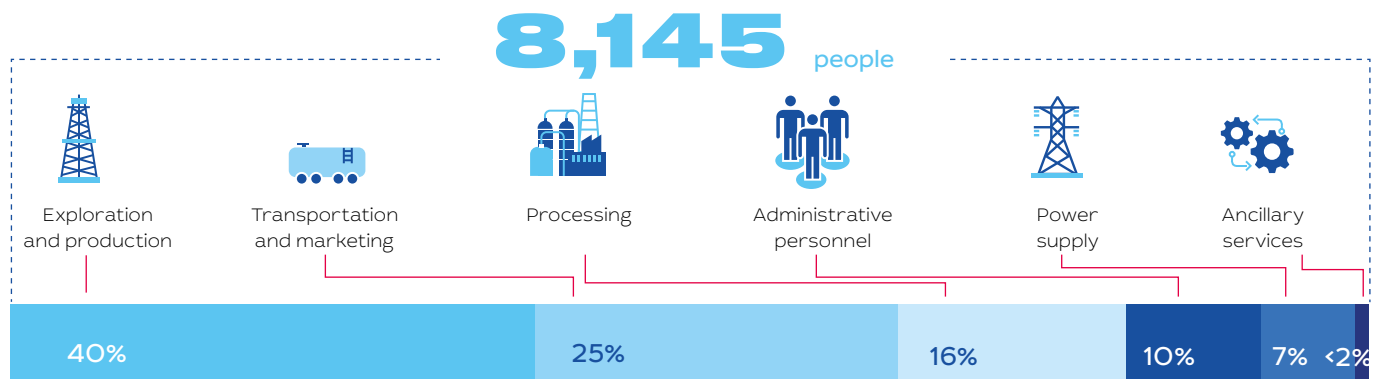
As part of its commitments under the Cooperation Agreement among the Russian Ministry of Natural Resources and Environment, the Russian Federal Service for Supervision of Natural Resource Usage, the Government of the Yamal-Nenets Autonomous Region and NOVATEK, the Company developed a greenhouse gas emission estimation module and approved its Standard SK-ISU-O-012 “Greenhouse Gas Emission Management System”. The system covers all of the Company’s core upstream and refining facilities, namely six (6) producing and two (2) processing entities. This project brings value by improving the accuracy of greenhouse gas emission accounting

and combining estimation with actual measurements. The project “GHG Emission Management System”, implemented by the Company in 2017, was recognized as the winner of the competition for the National Environmental Prize named after V.I. Vernadsky in the nomination “Science for Ecology”.

NOVATEK has in place an occupational health and safety management system which is part of a wider management system and ensures risk management based on the key principle of prioritizing prevention over incident containment and response.

Employees are NOVATEK’s most valuable resource, allowing the Company to grow rapidly and effectively. The Company’s human resource management system is based on the principles of fairness, respect, equal opportunities for professional development, dialogue between management and employees, as well as continuous, comprehensive training and development opportunities for the Company’s employees at all levels.

• NOVATEK’s personnel structure as of 31.12.17



RR **683**  
mln – Expenses on Occupational Health and Safety in 2017

**3,109**  
employees were assessed on industrial safety in 2017

# Management and Corporate Governance

## THE BOARD OF DIRECTORS MEMBERSHIP AS OF 31 DECEMBER 2017

The Company has established an effective and transparent system of corporate governance complying with both Russian and international standards. NOVATEK's supreme governing body is the General Meeting of Shareholders. The corporate governance system comprises the Board of Directors, the Board Committees, and the Management Board, as well as internal control and audit bodies and the Corporate Secretary.

### 3

independent  
Board Members<sup>1</sup>



**MR. ROBERT  
CASTAIGNE**

Born in 1946  
Independent Director  
Member of the Audit  
Committee  
Member of the Remu-  
neration and Nomination  
Committee



**MR. VICTOR  
P. ORLOV**

Born in 1940  
Independent Director  
Chairman of the Remu-  
neration and Nomination  
Committee  
Member of the Audit  
Committee



**MR. ANDREI  
V. SHARONOV**

Born in 1964  
Independent Director  
Chairman of the Audit  
Committee  
Member of the Remu-  
neration and Nomination  
Committee

1. Independent Director as of 31 December 2017 in accordance with the Corporate Governance Code recommended by the Central Bank of Russia and the UK Corporate Governance Code.



**MR. ALEXANDER  
E. NATALENKO**

Born in 1946  
Chairman of the Board  
of Directors  
Chairman of the  
Strategy Committee



**MR. LEONID  
V. MIKHELSON**

Born in 1955  
Chairman of the  
Management Board



**MR. ANDREI  
I. AKIMOV**

Born in 1953  
Member of the Strategy  
Committee



**DR. BURCKHARD  
BERGMANN**

Born in 1943  
Member of the Strategy  
Committee



**MR. MICHAEL  
BORRELL**

Born in 1962  
Member of the Strategy  
Committee



**MR. GENNADY  
N. TIMCHENKO**

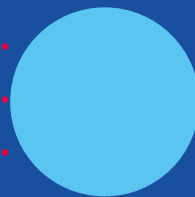
Born in 1952  
Member of the Strategy  
Committee

# Transforming into a Global Gas Company



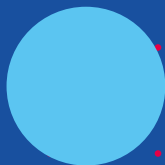
**6.9**

Thousand  
publications in  
foreign media  
in 2017



**12**

meetings between the  
Company management  
and journalists of  
foreign and federal  
international and  
Russian periodicals



**70%**

growth in number  
of TV stories

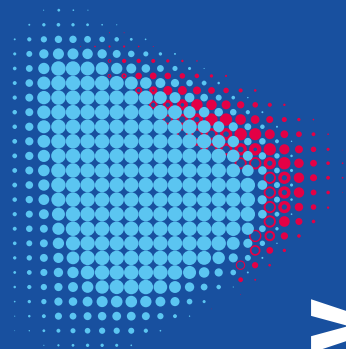


On 12 December 2017, the Company held its Corporate Strategy Day that comprehensively outlined our long-term strategy covering the period up to 2030 and new corporate identity and logo.



**30**

Thousand unique publications on the Company



**>15**

exhibitions, conferences and round tables

# Review of Operating Results

## LICENSES

NOVATEK's core fields and license areas are located in, or in close proximity to, the Yamal-Nenets Autonomous Region (YNAO) of the Russian Federation, which is one of the world's largest natural gas producing regions accounting for approximately 80% of Russian and 15% of global natural gas production. The concentration of the Company's fields in this prolific gas-producing region provides favorable opportunities for increasing NOVATEK's shareholder value with a minimum level of risks, low finding cost, and efficient replacement of reserves. With more than 20 years of operational experience in the region, NOVATEK is in a good position to efficiently monetize its resource base.

Exploration and production of hydrocarbons in Russia is subject to federal licensing regulations.

As of 31 December 2017, NOVATEK subsidiaries and joint ventures held 45 licenses for subsoil use. NOVATEK also entered into a concession agreement on exploration and production of hydrocarbons offshore of the Republic of Montenegro. The duration of licenses for the Company's core fields exceeds 15 years. In particular, the license for the South-Tambeyskoye field is valid until 2045, for the East-Tarkosalinskoye – until 2043, for the Yurkharovskoye field – until 2034, for the Samburgsky license area of Arcticgas – until 2034.

In the reporting year, NOVATEK significantly expanded its portfolio of licenses.

In June, Arctic LNG 1, a subsidiary of the Company, acquired in an auction a license for exploration and production of hydrocarbons within the Gydanskiy license area. The license was issued for 27 years. The

Gydanskiy license area is located in close proximity to the Utrenneye field, the resource base for the Arctic LNG 2 project. The hydrocarbon resources potential of the license area according to the Russian classification totals 4,740 mmboe.

In August, Arctic LNG 2 acquired in an auction an exploration and production license for a federal subsurface area including the Shtormovoye field. The license area is located on the Gydan Peninsula and partially in the Kara Sea Bays of Ob and Gydan. It borders on the Utrenneye field and has the total hydrocarbon resources potential of 7,932 mmboe according to the Russian classification. The license was issued for 30 years.

In August, NOVATEK-YURKHAROVNEFTEGAS acquired in an auction a geological study, exploration and hydrocarbons production license for the license area including the Verkhnetiuteyskoye and West-Seyakhinskoye fields. The license area is located on the Yamal Peninsula in close proximity to the South-Tambeyskoye gas condensate field and has the overall hydrocarbon resources potential of 8,747 mmboe according to Russian classification. The license was issued for 27 years.

In November a transaction was closed for the purchase of Severneft-Urengoy which holds exploration and production license within the West-Yaroyakhinskiy subsoil area with the total resource potential of 918 mmboe under the Russian classification, located in the Purovsky district of the Yamal-Nenets Autonomous Area in close proximity to the existing NOVATEK infrastructure.

In December AO Yuzhno-Khadyryakhskoye was purchased, which holds the exploration and production

license within the South-Khadyryakhinskoye subsoil area with the total resource potential of 228 mmboe under the Russian classification, and which is located in close proximity to the existing infrastructure of the North-Khancheykskoye field being developed by a NOVATEK subsidiary.

In December another entity acquired was Eurotek, which owns an exploration and production license for the Syskonsyninsky subsoil area with a total resource potential of 48 mmboe under the Russian classification. The area is located in the Khanty-Mansiysk Autonomous Region, 120 km to the northwest from Nyagan. In 2017, this license area produced 719.4 mmcm of natural gas and 2.9 thousand tons of gas condensate.

In December, our joint venture Arcticgas acquired in an auction a license for geological study, hydrocarbons exploration and production within the Osenniy license area. Total resource potential of this area is estimated at 4,411 mmboe under the Russian classification. The area is located in the Yamal-Nenets Autonomous Area. The license was issued for 25 years.

On top of that, in December an agreement was made for the acquisition of OOO Chernichnoye, a company that owns an exploration and production license for the Chernichnoye field with a total resource potential of 179 mmboe under the Russian classification. The field is located in close proximity to NOVATEK's existing infrastructure.

NOVATEK strives to strictly observe all of its license obligations and conducts continuous monitoring of license tenders in order to expand its resource base in strategically important regions.

## HYDROCARBON RESERVES

Most of the Company's reserves are located onshore or can be developed from onshore locations and are attributed to the conventional hydrocarbon categories (capable of being exploited using conventional technologies, in contrast to unconventional gas deposits such as shale gas or coal-bed methane).

DeGolyer and MacNaughton ("D&M"), an independent petroleum engineers firm, estimates the Company's reserves on an annual basis under both the SEC and PRMS reserves reporting standards.

As of 31 December 2017, NOVATEK's SEC proved reserves, including the Company's proportionate share

in joint ventures, aggregated 15,120 million barrels of oil equivalent (mmboe), including 2,098 billion cubic meters (bcm) of natural gas and 164 million metric tons (mmt) of liquid hydrocarbons. The Company's proved reserves grew by 12.8%, and the reserve replacement ratio stood at 435%. At year-end 2017, the Company's reserve to production ratio (or R/P ratio) was 29 years.

The Company's reserves were positively impacted by successful exploration works at the Utrenneye, Kharbeykskoye, West-Yurkharovskoye and Urengoykskoye (Samburgskiy license area) fields, production drilling at the South-Tambeyskoye field, as well as the new licenses obtained through tender auctions (Gydanskoye, Verhnetiuteyskoye and West-Seyakhinskoye fields) and recent asset acquisitions (South-Khadyryakhinskoye, Syskonsyninskoye fields and West-Yaroyakhinskiy license area). Excluding the effect of obtaining new licenses, our total proved reserves increased by 1.3%, representing an organic reserve replacement rate of 134%.

As of 31 December 2017, the Company's total PRMS proved and probable reserves, including the Company's proportionate share in joint ventures, aggregated 28,471 mmboe, including 3,879 bcm of natural gas and 366 mmt of liquid hydrocarbons, with a total R/P ratio of 55 years.

The high quality of the reserve base enables NOVATEK to maintain its position as one of the lowest cost producers in the global oil and gas industry. Our average 2017 and five-year (2013–2017) proved reserve replacement costs amounted to RR 25 (USD 0.4) per boe and RR 94 (USD 2.3) per boe, respectively.

SEC proved reserves as of 31 December 2017 (based on the Company's equity ownership interest in joint ventures) and duration of licenses

Field / license area	Ownership	Duration of license	Natural gas reserves, bcm	Liquids reserves, mmt
<b>TOTAL RESERVES</b>	<b>—</b>	<b>—</b>	<b>2 097,9</b>	<b>164,3</b>
Yurkharovskoye	100%	2034	213,5	8,1
South-Tambeyevskoye	50.1% (60% of reserves)	2045	409,5	12,4
Utrenneye	100%	2031	408,5	15,0
Urengoyevskoye (Arcticgas)	53.3%	2034	197,7	46,8
Verkhnetiutevskoye + West-Seyakhinskoye	100%	2044	157,3	1,8
Geofizicheskoye	100%	2034	125,6	0,4
East-Tarkosalinskoye	100%	2043	102,6	22,1
Yarudevskoye	51% (100% of reserves)	2029	9,6	17,2
North-Urengoyevskoye	50%	2038	80,1	6,8
Yaro-Yakhinskoye	53.3%	2034	72,2	8,5
North-Russkoe	100%	2031	53,0	2,5
Kharbeyevskoye	100%	2036	45,4	6,0
Gydanskiy	100%	2044	38,6	0,0
West-Yaroyakhinskiy	100%	2025	24,2	2,6
Samburgskoye	53.3%	2034	25,4	2,6
North-Chaselskoye	53.3%	lifetime of the field	22,4	0,5
Khancheyevskoye	100%	2044	20,4	1,3
Olimpiyskiy license area	100%	2059	27,1	2,2
East-Tazovskoye	100%	2033	17,7	2,5
Termokarstovoye	51%	2097	14,2	3,6
Others	—	—	32,9	1,4

## GEOLOGICAL EXPLORATION

NOVATEK aims to expand its resource base through geological exploration at fields and license areas not only in close proximity to existing transportation and production infrastructure, but also in new potentially prospective hydrocarbon areas. The Company ensures the efficiency of geological exploration work by deploying state-of-the-art technologies and relying on the experience and expertise of the specialists in its geology department, and the Company's Scientific and Technical Center located in Tyumen.

The Company uses a systematic and comprehensive approach to exploration and development of its

fields and license areas, beginning with the collection and interpretation of seismic data to the creation of dynamic field models for the placement of exploration and production wells. We employ modern geological and hydrodynamic modelling as well as new well drilling and completion techniques to maximize the ultimate recovery of hydrocarbons in a cost effective and environmentally prudent manner.

In 2017, NOVATEK continued exploration on the Yamal and Gydan Peninsulas to expand the resource base of LNG projects.

At the Utrenneye field, we drilled an exploration well into the Jurassic layers, whereby two (2) productive

formations with potentially high condensate content were penetrated. Reserves estimation was completed as was the development plan based on six (6) exploration wells drilled between 2014 and 2017, testing of four (4) previously drilled wells, and the running and interpretation of 1,850 square kilometers of 3D seismic. The field's PRMS reserves addition for 2017 is estimated at 245 bcm of natural gas and 12 mmt of gas condensate. The field's PRMS reserves as of 31 December 2017 amounted to 1,029 bcm of natural gas and 49 mmt of gas condensate.

3D seismic (830 square km) was completed in the Trekhbugorniy license area, with the whole area currently covered by 3D seismics. Several prospects were identified in the Cenomanian and Apto-Albian layers and, accordingly, a prospecting well location was chosen.

2D and 3D seismic works were started in the Shtormovoy, Gydanskiy, Verkhnetiuteyskiy and West-Seyakhinskiy license areas.

Exploration also continued at the fields and license areas in the Nadym-Pur-Taz district to sustain pipeline gas production and utilization of the Purovsky Plant.

At the Kharbeyskoye field of the North-Russkoye cluster we tested one (1) well and drilled two (2) wells and discovered four (4) new gas condensate deposits and one (1) gas condensate and oil deposit. The PRMS proved and probable reserves addition amounted to 38 bcm of gas, 2 mmt of condensate and 20 mmt of crude oil.

At the West-Yurkharovskoye field, specifically within the West-Yurkharovskiy license area, a Middle Jurassic well was successfully tested. The Company successfully completed a horizontal well using multi-stage hydro-fracturing at a total vertical depth of 4,100 meters with abnormally high reservoir pressure

of 820 standard atmosphere and co-mingled production from two separate Jurassic horizons. This was the first time that a well completion for an over-pressured Jurassic reservoir was applied in Russia.

The well has been naturally flowing with a gas-condensate mixture flow rate of 650 thousand cubic meters per day. This positive testing results were the outcome of NOVATEK's experience in constructing horizontal wells with multi-stage hydro-fracturing in the abnormally high Jurassic pressure reservoir (anomalous pressure factor of 2.0). The field's PRMS proved and probable reserves addition totaled 37 bcm of gas and 5 mmt of condensate.

An exploration well was drilled in the Samburgskiy license area and confirmed the potential of Achimov gas condensate deposits in the northern part of the area. Following the completion of and production from the two wells drilled previously, a high condensate ratio (up to 800 g/cm) was determined. The PRMS proved and probable reserves addition totaled 95 bcm of gas and 24 mmt of condensate.

An exploration well was drilled at the Yarudeyskoye field confirmed the prospects of 2 Jurassic deposits adding another 8 bcm of gas to PRMS reserves.

In 2017, we completed the running of 1,465 square kilometers of 3D seismic works and drilled 25 thousand meters of exploration drilling.

The successful exploration works contributed 604 bcm of gas, 38 mmt of condensate and 23 mmt of crude oil to the NOVATEK's reserves under the Russian reserve classification, and 344 bcm of gas, 24 mmt of condensate and 23 mmt of crude oil to our PRMS reserves. In the reporting year, 26 new hydrocarbon deposits were discovered.

## Geological Exploration

	Units	2016	2017	Change
<b>3D SEISMIC</b>	square km	989	1,465	48.1%
Subsidiaries	square km	989	1,215	22.9%
Joint ventures	square km	—	250	n/a
<b>2D SEISMIC</b>	linear km	—	—	n/a
Subsidiaries	linear km	—	—	n/a
Joint ventures	linear km	—	—	n/a
<b>EXPLORATION DRILLING</b>	th. m	10.2	24.5	140.2%
Subsidiaries	th. m	10.2	16.2	58.8%
Joint ventures	th. m	—	8.3	n/a

## FIELD DEVELOPMENT

In 2017, NOVATEK continued development activities at our producing and prospective fields. In the reporting year, the Company's subsidiaries invested RR 12.1 bln in the resource base development.

Production drilling in 2017, including joint ventures, reached 262,000 m, which is 12% above the 2016 number. Increase in the drilling volumes was mainly driven by the development of the Yaro-Yakhinskoye field of Arcticgas with 9 wells drilled there (in 2016 no wells were drilled at the field).

A total of 68 production wells, including 55 natural gas and gas condensate and 13 oil wells, were completed and commissioned.

### New facilities commissioned at producing fields

In 2017, two booster compressor stations, with a capacity of 48 MW each, were commissioned at the North-Urengoyskoye field (Eastern Dome) and at the Samburgskoye field. These stations are needed to transport gas and improve its treatment quality.

At the Yarudeyskoye field, the gas treatment unit was upgraded, and a 3S (supersonic) separation unit was commissioned. This allowed to increase the capacity of the gas treatment unit with minimum capital costs, significantly improve the quality of gas drying and increase the yield of liquid hydrocarbons.

As part of the North-Russkoye field development, site preparation has started. Well pads, roads, and infrastructure sites were backfilled.

Preparatory works commenced with excavation and rock blasting works at the yard to construct large-scale offshore structures in Belokamenka, located in the Murmansk Region. Area planning has been performed, and land reclamation is in progress. The con-

tractors were selected and started the construction of dry docks and berths.

## HYDROCARBON PRODUCTION

In 2017, NOVATEK produced commercial hydrocarbons at 16 fields. The Company's production (including attributable share in the production of JVs) amounted to 513.3 mmboe, down 6.2% versus 2016. The production volumes at mature fields of our subsidiaries and joint ventures decreased mainly due to natural declines in the reservoir pressure at the current gas producing horizons. The decrease was partially offset by the improved efficiency of associated petroleum gas utilization at our Yarudeyskoye field, as well as the commencement of LNG production at the first LNG train at Yamal LNG in the fourth quarter of 2017.

Total natural gas production including the Company's share in production of joint ventures aggregated 63.40 bcm, representing approximately 81% of our total hydrocarbon output. The share of gas produced from the gas condensate bearing layers (or "wet gas") in proportion to total gas production was 77%. Production of natural gas decreased by 6.3% as compared to 2016 volumes.

Production of liquid hydrocarbons including the Company's share in production of joint ventures totaled 11,774 thousand tons, of which 59% was gas condensate and the remaining 41% consisted of crude oil. Production of liquid hydrocarbons decreased by 5.4% as compared to 2016, with gas condensate production amounting to 6,892 thousand tons and crude oil production coming to 4,882 thousand tons. Liquid hydrocarbons production share in NOVATEK's aggregate production remained approximately at the level of the previous year and amounted to 19.2%.

In 2017, we continued to achieve some of the lowest lifting costs in the industry. The Company's lifting costs were RR 44.3 (USD 0.76) per boe in 2017.

### Hydrocarbon production (including share in production by joint ventures)

	Units	2016	2017	Change
<b>TOTAL</b>	<b>MMBOE</b>	<b>547.0</b>	<b>513.3</b>	<b>(6.2%)</b>
Gas	mmcm mmboe	67 647 442.4	63 399 414.6	(6.3%)
Liquid hydrocarbons	th. tons mmboe	12 441 104.6	11 774 98.7	(5.4%)

▼ Gross hydrocarbon production (including share in production by joint ventures)

	Gas, mmcm			Liquids, mt		
	2016	2017	Change	2016	2017	Change
<b>TOTAL</b>	<b>67,647</b>	<b>63,399</b>	<b>(6.3%)</b>	<b>12,441</b>	<b>11,774</b>	<b>(5.4%)</b>
Yurkharovskoye (100%)	34,554	30,540	(11.6%)	1,813	1,489	(17.9%)
Arcticgas fields (53.3%)	13,790	13,964	1.3%	4,300	4,190	(2.6%)
East-Tarkosalinskoye (100%)	8,305	7,379	(11.1%)	1,354	1,291	(4.7%)
North-Urengoyenskoye (50%)	5,064	4,291	(15.3%)	519	379	(27.0%)
Khancheyenskoye (100%)	2,529	2,242	(11.3%)	353	274	(22.4%)
Termokarstovoye (51%)	1,185	1,255	5.9%	428	421	(1.6%)
Yarudeyskoye (100%)	562	1,362	142.3%	3,556	3,596	1.1%
Others	1,658	2,366	42.7%	118	134	13.6%

### YAMAL LNG PROJECT

In December 2017, Yamal LNG's Train 1 with a rated capacity of 5.5 mln tons of LNG per annum started LNG production. The first LNG cargo was loaded onto the LNG carrier Christophe de Margerie, the world's first Arc7 ice-class LNG carrier, on 8 December 2017 in the port of Sabetta.

The start of LNG production at the first train represents an important milestone of the Yamal LNG project. This event turns a new page in NOVATEK's history, as the loading of the first LNG cargo means that NOVATEK entered the global gas market and became a worldwide gas company.

The South-Tambeyskoye field located in the North-East of the Yamal Peninsula is the resource base of the Project. Yamal LNG is the operator and the owner of all the assets. As of the end of 2017, the shareholding structure of Yamal LNG was as follows: NOVATEK – 50.1%, Total – 20%, CNPC – 20%, and the Silk Road Fund – 9.9%.

The total LNG liquefaction capacity of the plant will be 17.4 mmt, the capacity of each of the first three trains will be 5.5 mmt. In 2017, the project shareholders approved the plan to build an additional fourth LNG train with a capacity of 0.9 mmt based on proprietary liquefaction technology developed by NOVATEK called the "Arctic Cascade". The low capital expenditures per unit of production and the use of the facility's existing infrastructure to accommodate the additional fourth train will allow the Project sponsors to decrease the unit cost of produced LNG across the whole project.

As of the end of 2017, the overall project progress was 91%. The project's infrastructure includes the sea port, the international airport, automobile roads, power lines, gas gathering lines and living quarters. The shipping infrastructure includes a jetty with two loading berths in the port of Sabetta.

The South-Tambeyskoye field was discovered in 1974 and comprises 42 gas bearing layers with depths ranging between 900 and 3,730 meters and includes three domes. The field is being developed with horizontal wells with drilled lengths up to 5,000 meters and horizontal sections of up to 1,500 meters.

The license for exploration and production at the South-Tambeyskoye field held by Yamal LNG is valid until 2045.

As of 31 December 2017, the field was estimated to contain 683 bcm of proved natural gas reserves and 21 mmt of proved liquid hydrocarbon reserves, under the SEC reserves methodology. In 2017, based on production drilling results, we were able to increase the SEC proved natural gas reserves at the South-Tambeyskoye field by 77 bcm compared to year-end 2016. Based on total proved hydrocarbon reserves, the South-Tambeyskoye field is the largest field in NOVATEK reserves portfolio. According to the PRMS reserves standards, the proved and probable reserves of the South-Tambeyskoye field as of the end of 2017 were appraised at 992 bcm of natural gas and 32 mmt of liquid hydrocarbons.

The field development plan provides for 208 wells to be drilled from 19 well pads. The field's production capacity exceeds 27 bcm of natural gas and 1 mmt of

stable gas condensate per annum. As of the end of the reporting year, 103 production wells were drilled at the South-Tambeyskoye field, exceeding the well stock required for the first two production trains of the LNG plant (93 wells).

At year-end, there were approximately 26 thousand construction workers on site. The Sabetta international airport services regular flights from Novy Urengoy, Moscow and Samara, ensuring high efficiency of shift workers logistics. Regular flights served approximately 364 thousand people in 2017.

To minimize construction activities on site due to challenging climate conditions, a modular approach to the LNG plant construction was selected. The LNG plant will consist of 142 large plant modules with weights ranging from 85 tons to 6,400 tons. The modules were built at contractors' yards.

At year-end 2017, all 142 modules for the LNG plant three trains had been delivered to the site by sea, 137 of them had been installed on the prepared foundations, and commissioning of the equipment for the second trains and third train hook up were underway. All of the main LNG equipment, including three main cryogenic heat exchangers (the core of the natural gas liquefaction technology) for all three trains of the LNG plant, compressor equipment, packages of steel structures and pipe racks, and power plant turbines are on site.

More than 95% of the LNG volumes produced within the three trains of the project has been contracted on a long-term basis. A total of three LNG cargoes were offloaded over the course of December 2017. Specially designed Arc7 ice-class LNG carriers are used for LNG transportation. As of the end of 2017, four Arc7 LNG carriers were put into operation while eleven (11) LNG carriers were under construction.

In June 2017, credit facility agreements were signed with European banks, inter alia Raiffeisen Bank International AG and Intesa Sanpaolo on 14-year credit line facilities for the total amount up to EUR 425 mln with insurance coverage provided by the Swedish export credit agency EKN and the German export credit agency Euler Hermes. The new creditors have joined the terms of the project financing attracted earlier without increasing its overall amount. The new facility agreements with European banks will allow to optimize the Yamal LNG credit portfolio and improve the project's economic value for its shareholders.

## PROCESSING OF GAS CONDENSATE

### Purovsky Plant

Our subsidiaries and joint ventures are producing wet gas, a mixture of natural gas and gas condensate. After being separated and de-ethanized at the field the unstable (de-ethanized) gas condensate is delivered via a system of condensate pipelines owned and operated by the Company for further stabilization at our Purovsky Plant located in the YNAO in close proximity to the East-Tarkosalinskoye field.

The Purovsky Plant is the central element in our vertically integrated value chain that provides us complete operational control over our processing needs and access to higher yielding marketing channels for our stable gas condensate. The Purovsky Plant processes unstable gas condensate into stable gas condensate and natural gas liquids (NGL).

In the reporting period, the Purovsky Plant processed its milestone volume – 65 million tons of gas condensate since the start of operation in 2005.

The Purovsky Plant processed 11,445 mt of de-ethanized gas condensate, representing a 7.7% decrease compared to 2016. The Purovsky Plant's processing capacity is in line with the total production capacity of the fields of NOVATEK and its joint ventures. The output mix included 8,853 mt of stable gas condensate, 2,493 mt of NGL and LPG and 16.5 mt of regenerated methanol.

The Purovsky Plant is connected via its own railway line to the Russian rail network at the Limbey rail station. Subsequent to the launch of the Ust-Luga Complex in 2013, most of the stable gas condensate volumes produced at the Purovsky Plant are delivered by rail to Ust-Luga for further processing or transshipment to exports, with the remaining volume of stable gas condensate sold directly from the plant to the domestic market.

All of the NGL volumes (feedstock for LPG production) produced at the plant are delivered by pipeline to SIBUR's Tobolsk Petrochemical Complex for further processing.



Processing volumes and output of the Purovsky Plant, thousand tons

	2016	2017	Change
<b>PROCESSING OF DE-ETHANIZED CONDENSATE</b>	<b>12,397</b>	<b>11,445</b>	<b>(7.7)%</b>
<b>OUTPUT:</b>			
Stable gas condensate	9,667	8,853	(8.4)%
NGL and LPG	2,597	2,493	(4.0)%
Regenerated methanol	10.2	16.5	61.8%

### Ust-Luga Complex

The six million ton per annum Gas Condensate Fractionation and Transshipment Complex (the "Ust-Luga Complex") launched in 2013 is located at the all-season port of Ust-Luga on the Baltic Sea. The Ust-Luga Complex processes stable gas condensate into light and heavy naphtha, jet fuel, ship fuel component (fuel oil) and gasoil, and enables us to ship the value-added petroleum products to international markets. The Ust-Luga Complex also allows for transshipment of stable gas condensate to the export markets.

In 2017, it processed its milestone volume – 25 million tons of stable gas condensate since the start of operation in 2013.

In the reporting year, the Ust-Luga Complex processed 6,961 mt of stable gas condensate into 6,826 mt of end products, including 4,223 mt of light and heavy naphtha, 1,072 mt of jet fuel and 1,531 mt of ship fuel component (fuel oil) and gasoil.

High value-added petroleum products produced at the Ust-Luga Complex have a significant positive impact on the profitability of our liquid hydrocarbon sales and the Company's cash flow generation. As the Ust-Luga Complex reached its full processing capacity we transshipped stable gas condensate to the export markets by sea.

Processing volumes and output of the Ust-Luga Complex, thousand tons

	2016	2017	Change
<b>STABLE GAS CONDENSATE PROCESSING</b>	<b>6,917</b>	<b>6,961</b>	<b>0.6%</b>
<b>OUTPUT:</b>			
Heavy naphtha	2,195	2,261	3.0%
Light naphtha	2,000	1,962	(1.9)%
Ship fuel component (fuel oil)	1,147	967	(15.7)%
Jet fuel	998	1,072	7.4%
Gasoil	443	564	27.3%

### NATURAL GAS SALES

NOVATEK sells natural gas within the Russian Federation as well as exports natural gas in the form of LNG. The Company started exporting LNG in December 2017 when the first train at Yamal LNG started production. Relatively small LNG volumes are also sold through the Blue Gaz regas station acquired in December 2016.

NOVATEK plays an important role in ensuring supplies of natural gas to the domestic market. During 2017, the Company supplied natural gas to 39 regions of the Russian Federation. Our end users and traders were located primarily in the following regions: the Chelyabinsk, the Khanty-Mansiysk Autonomous Region, Moscow and the city of Moscow, Lipetsk, YNAO, Tyumen, Vologda, Stavropol, Smolensk, Nizhny

Novgorod and Kostroma regions, Perm territory and the Republic of Tatarstan. The above regions accounted for more than 94% of our total gas sales.

The total volume of natural gas sales in 2017, including LNG, amounted to 65.0 bcm, increasing by 0.5% compared to the previous year due to a minor increase in sales volume within the Russian Federation as well as the commencement of LNG export sales. The proportional share of natural gas sales to the domestic end customers increased compared to 2016 and amounted to 94.9% of our total natural gas sales mix.

Revenues from natural gas sales in 2017 totaled RR 248 billion, representing a 7.8% increase compared

to 2016. The revenue increase was mainly driven by growth in sales to end customers in Russia, the increase of Russian domestic regulated prices, as well as start of LNG deliveries.

In order to manage gas demand seasonalities, NOVATEK has entered into an agreement with Gazprom for underground storage services. Natural gas inventories are accumulated during warmer periods when demand is lower and then used to meet increased demand during periods of colder weather. At year-end 2017, our inventories of natural gas in underground gas storage facilities and pipelines amounted to approximately 0.87 bcm.

### ◀ Natural gas sales, mmcm

	2016	2017	Change
<b>TOTAL GAS SALES</b>	<b>64,709</b>	<b>65,004</b>	<b>0.5%</b>
International sales	–	106	n/a
Sales within the Russian Federation, including:	64,709	64,898	0.3%
End customers	59,646	61,560	3.2%
Traders	5,063	3,338	(34.1%)
Share of end customers in domestic gas sales	92.2%	94.9%	2.7 p.p.

### LIQUID HYDROCARBON SALES

NOVATEK sells liquid hydrocarbons (stable gas condensate, petroleum products, light hydrocarbons, LPG and crude oil) domestically and internationally. The Company strives to respond quickly to changing market conditions by optimizing the customer base and supply geography, as well as developing and maintaining logistics infrastructure.

The logistical supply chain varies according to location and type of product – stable gas condensate and LPG are transported by rail, finished petroleum products produced at the Ust-Luga Complex are exported by sea, while crude oil produced from our fields is transported through the trunk pipelines owned and operated by Transneft.

In 2017, the liquids sales volume reached 15,939 mt, or 5.4% less than in 2016. In 2017, export sales decreased by 8.5% as compared to 2016 and amounted to 9,027 mt.

In 2017, our liquids sales revenues increased to RR 332 billion, or by 9.2% as compared to 2016, mainly driven by higher global oil prices and underlying benchmark prices.

Petroleum products from the Ust-Luga Complex accounted for a 42% share of our overall liquids sales volumes. We sold a total of 6,743 mt of petroleum products, including 4,102 mt of naphtha, 1,121 mt of jet fuel and 1,520 mt of fuel oil and gasoil. The majority of petroleum products (98%) were exported. Export volumes were distributed as follows: Europe – 58%, Asia-Pacific – 29%, and North America – 13%. Most of our heavy naphtha was exported to Asia Pacific, light naphtha – to Northwest Europe and North America, and jet fuel, diesel fraction and heavy fuel – to Northwest Europe.

Export and domestic sales of stable gas condensate continued in 2017 as we reached full capacity utilization at the Ust-Luga Complex. Total stable gas condensate sales volumes amounted to 1,918 mt, representing a 32% decrease compared to 2016.

A portion of light hydrocarbons produced at the Purovsky Plant is processed on tolling terms at SIBUR's Tobolsk Petrochemical Complex into marketable LPG, which is then delivered to NOVATEK's customer base, while the rest of the light hydrocarbons volumes are sold to SIBUR. We sold 1,288 mt of light hydrocarbons in 2017.

Marketable LPG sales volumes totaled 1,360 mt in 2017, representing a 9.2% increase compared to 2016. LPG export sales volumes amounted to 536 mt or 39% of the total LPG sales volumes. Novatek Polska, our wholly owned LPG trading company in Poland, sold 509 mt of LPG, representing 95% of our total LPG export sales. Apart from Poland, LPG was also exported to Finland.

In the domestic market, our LPG is sold through large wholesale channels as well as through our network of retail and small wholesale stations. In 2017, large wholesale supplies to the domestic market stood at 679 mt, representing 82% of domestic LPG sales. We also sold LPG via our network of 66 retail stations and seven (7) small wholesale stations in the Chelyabinsk, Volgograd, Rostov and Astrakhan Regions. The combined sales from our retail and wholesale stations totaled 146 mt.

Sales of crude oil in 2017 totaled 4,616 mt, which is 0.7% below the similar indicator from 2016. We sold 67% of our crude oil volumes in the domestic market with the remaining volumes exported.

#### ▾ Liquid hydrocarbon sales, thousand tons

	2016	2017	Change
<b>TOTAL</b>	<b>16,850</b>	<b>15,939</b>	<b>(5.4%)</b>
Petroleum products (Ust-Luga)	6,662	6,743	1.2%
Crude oil	4,650	4,616	(0.7%)
Stable gas condensate	2,812	1,918	(31.8%)
Light hydrocarbons	1,468	1,288	(12.3%)
LPG	1,245	1,360	9.2%
Other	13	14	7.7%

# Environmental and Social Responsibility

**NOVATEK adheres to the principles of effective and responsible business conduct and considers the welfare of its employees and their families, environmental and industrial safety, the creation of a stable and beneficial social environment as well as contributing to Russia's overall economic development as priorities and responsibilities of the Company.**

## ENVIRONMENTAL PROTECTION

NOVATEK's core producing assets are located in the Far North, a harsh Arctic region with vast mineral resources and a fragile and vulnerable environment. The Company is committed to environmental protection in its operations. In 2017, the Company's overall expenses on environment protection and sustainable nature management amounted to RR 2,066 mln.

As part of the "Year of Ecology" in Russia, the NOVATEK Group developed and implemented an Action Plan approved by Chairman of the Management Board. It included the following principle actions:

- another stage of the Biodiversity Program was implemented;
- actions were taken to ensure artificial reproduction of water bio resources within the areas where the Company operates;
- a children's drawing contest was organized and held in Tarko-Sale themed around the Year of Ecology in Russia and the protection of the Far North nature; and
- employees of NOVATEK and its controlled entities took part in Green Spring 2017, a Russia-wide community cleanup event.

As part of its commitments under the Cooperation Agreement among the Russian Ministry of Natural Resources and Environment, the Russian Federal Service for Supervision of Natural Resource Usage, the Government of the Yamal-Nenets Autonomous Region and NOVATEK, the Company developed a greenhouse gas emission estimation module and ap-

proved its Standard SK-ISU-O-012 "Greenhouse Gas Emission Management System". The system covers all of the Company's core upstream and refining facilities, namely six (6) producing and two (2) processing entities. This project brings value by improving the accuracy of greenhouse gas emission accounting and combining estimation with actual measurements. The project "GHG Emission Management System", implemented by the Company in 2017, was recognized as the winner of the competition for the National Environmental Prize named after V.I. Vernadsky in the nomination "Science for Ecology".

Following a re-certification audit by Bureau Veritas Certification Rus, the NOVATEK's Integrated Management System for Environmental Protection, Occupational Health and Safety was found to be in compliance with ISO 14001-2004 and OHSAS 18001-2007.

Environmental monitoring was performed throughout the reporting year at all of the main license areas and production facilities of the Company. During the monitoring process the condition of the environment components is studied, soil, ground, snow cover, water and bed deposit samples are taken. Air contamination level is inspected. The status of fish stock and fodder resources in water areas is studied as are hydrologic and hydrochemical parameters. The samples taken are tested in certified laboratories. Based on the laboratory analysis the condition of the environment components is evaluated as well as its dynamic pattern over the year. The monitoring revealed that the condition of the environment components in the Company's production facility locations is evaluated as stable.

In the reporting year, the Company continued its participation in the Carbon Disclosure Project (CDP), whereby information on greenhouse gas emissions and operations energy efficiency is disclosed, as well as in the CDP Water Disclosure Project to disclose data on the use of water resources. Taking part in these projects, the Company intends to achieve a balance between the climate change risks and efficiency of investment projects. The Company offers all stakeholders full access to its environmental information,

including by publications in federal and local printed media, on its website, and other disclosure means.

NOVATEK was included in the Vigeo Eiris Best Emerging Markets Performers Index and therefore rated among the 100 most stable companies in emerging markets in 2017. NOVATEK is also included in the FTSE4Good international rating index of compliance with the internationally recognized standards in the area of corporate social responsibility.

### Key Environmental Indicators of NOVATEK (including joint ventures)

	Unit	2016	2017	Change
Water consumption	'000 m <sup>3</sup>	2,701	2,779	2.9%
Atmospheric emissions	'000 tons	121.2	108.9	(10.1%)*

\*Decrease in atmospheric emissions is due to implementation of Rational APG Utilization Program (putting on stream a 3S separator) at the Yarudeyskoye oil field.

One of the Company's priorities is the rational usage of resources, including energy resources. The table below sets out the physical volumes and the Russian rouble equivalent of energy resources consumed by the Company in 2017.

### Energy Resource Consumption by NOVATEK in 2017 (including joint ventures)

	Units	Volume	RR mln, net of VAT
Natural gas	mmcm	2,121	2,811.0
Electricity	MW*h	927,183	3,877.6
Heating energy	Gcal	459,435	672.2
Oil	tons	2,150	13.3
Motor gasoline	tons	1,133	40.2
Diesel fuel	tons	6,398	232.1
Other	tons	96,448	14.8

## INDUSTRIAL SAFETY AND OCCUPATIONAL HEALTH

NOVATEK is fully committed to putting the life and health of its employees above operational results, and is aware of its responsibility for ensuring accident-free operations and safe labor conditions for its employees, as well as protecting the health of the population in the areas in which it operates.

NOVATEK has in place an occupational health and safety management system which is part of a wider

management system and ensures risk management based on the key principle of prioritizing prevention over incident containment and response.

The Company is engaged in exploration, production, processing and sales of natural gas and liquid hydrocarbons, which implies setting up complex technological processes for operating fire-and explosion hazardous facilities. Operation of fire-and explosion hazardous facilities requires that work and services at hazardous production facilities be performed in strict compliance with industrial safety laws.

To prevent accidents and incidents, and ensure accident containment and response at Class 1 and 2 hazardous production facilities, a unified industrial safety management system and industrial safety declaration were developed providing estimates and specifying activities for:

- identification, assessment and forecasting of accident risks;
- planning and implementation of accident risk mitigation measures;
- coordination of activities to prevent accidents and incidents;
- industrial control procedure; and
- employees' participation in the development and implementation of accident risk mitigation measures.

NOVATEK Group set up industrial safety assessment commissions to evaluate staff that operates hazardous production facilities according to the annually approved schedule. Safety certification protocols are produced to document the results of staff knowledge tests. In 2017, 3,109 employees were assessed.

During 2017, 344 industrial safety compliance checks were carried out, with results documented in industrial control reports.

To prevent accidents and incidents, technical inspection, certification and testing schedules for technical equipment are developed annually and rigorously followed. These audits are registered with territorial bodies of Rostekhnadzor (Federal Environmental, Industrial and Nuclear Supervision Service of Russia). In 2017, industrial safety audits were carried out on 255 equipment items.

In 2017, NOVATEK ran programs of integrated and targeted audits of controlled entities for compliance with occupational health, industrial, fire and environmental safety requirements by NOVATEK's committee. In the reporting year, the Company conducted integrated audits of four (4) entities, and targeted

audits of eight (8) subsidiaries. Based on their findings, relevant reports were produced, and remedial measures were developed.

To protect the right of employees to occupational health-compliant workplace, special assessments of working conditions are performed to cover all workplaces. When workplaces with harmful working conditions are identified, a range of measures is first implemented to eliminate adverse factors. If these prove impossible to eliminate, the affected employee is granted all guarantees and compensations for operating in harmful working conditions, including screening and regular medical examinations for timely detection of contraindications and signs of occupational diseases. In the reporting year, the Company continued the certification procedure on workplaces. No hazardous working conditions were identified during the inspections. In 2017, NOVATEK Group workplace certification costs totaled approximately RR 2 mln.

Occupational health training is mandatory for all categories of employees and is offered in all controlled entities. Structural unit leaders, including top managers, take courses in training centers, while specialists are offered in-house training opportunities. For that, training programs were developed, and occupational health knowledge testing commissions were set up. In-house occupational health training and knowledge testing not only enable significant cost optimization but also save man-hours as such training and tests take place on the job. In 2017, occupational health training costs amounted to more than RR 6 mln.

The Company's subsidiaries actively use their right to receive a 20% refund of mandatory social insurance payment that are duly transferred to the Social Insurance Fund of the Russian Federation to cover occupational accidents and diseases. In 2017, such refunds across all subsidiaries totaled over RR 16 mln. These funds are mainly used to finance procurement of protective clothing and workplace certifications.

#### Key health and safety indicators of NOVATEK (including joint ventures)

	2016	2017
Accidents at hazardous production facilities	0	0
Incidents at hazardous production facilities	2	2

## HUMAN RESOURCES

Employees are NOVATEK's most valuable resource, allowing the Company to grow rapidly and effectively. The Company's human resource management system is based on the principles of fairness, respect, equal opportunities for professional development, dialogue between management and employees, as well as continuous, comprehensive training and development opportunities for the Company's employees at all levels.

As of the end of 2017, NOVATEK and its subsidiaries had 8,145 employees, 39.8% of whom work in exploration and production, 15.8% in processing, 25.2% in transportation and marketing, 7.2% in power supply, 10.3% are administrative personnel and 1.7% engaged in ancillary services. The predominant age of the personnel is between 30 and 50. The average age of the Company's employees is 40 years.

### Personnel Training and Development

Amid the rapid development of technologies and management systems, our multilevel training and professional development program enable our employees to contribute to raising the Company's competitiveness. In 2017, the primary activities of training and professional development included:

- implementing an In-house Training Program to improve the competences of the Company's employees;
- implementing the Steps in Discovering Talents program for young specialists targeted at training highly qualified personnel whose competence level fully meets business needs;
- developing and improving the Corporate System for the Evaluation of Technical Competencies; and
- engaging young specialists to take part in research and practice conferences.

NOVATEK Scientific and Technical Center (NOVATEK STC) has hosted an In-House Training Program since 2016. In 2017, NOVATEK STC experts developed and delivered training courses on the following subjects: Basics of Well Modelling; Production Mode Analysis by Means of Digital Models; Basics of Gas and Condensate Processing Facility Engineering and Operation; Well Design and Lining; Geomechanics; Field Development Engineering amid Low Exploration Maturity; Basics of Hydrodynamic Studies; and Directional Drilling. A total of 63 employees of the Company's subsidiaries received training under this program in 2017.

In 2017, NOVATEK continued its efforts to advance the professional capabilities of its employees, improve working conditions and train its personnel on safe working practices at its production facilities. A total of 43.4 % of white-and blue-collar workers upgraded their skills. In 2017, the Corporate System for the Evaluation of Technical Competencies tested 648 employees across the Group, including 37 persons who were tested at recruitment and 49 persons – at promotion.

In 2017, we had our fifth class of graduates under the Steps in Discovering Talents Program. Eighteen (18) young specialists graduated from the on-the-job adaptation and professional development program. In autumn 2017, another 34 young specialists joined the program. In 2017 the number of companies – program participants was increased to seven. In 2017, young specialists received the Mentoring Culture training courses together with their mentors. In total, 26 mentors attended the training.

In September 2017, Moscow hosted the 12th Inter-regional Research-to-Practice Conference for the Company's young specialists attended by 42 employees. Based on the results of the competition, all the winners received cash prizes, while five (5) of the first place winners were also awarded a trip to a petroleum training center in France and Italy.

In October 2017, the 3rd Professional Skills Contest among field workers of the NOVATEK Group took place. Totally, 74 participants from 8 entities took part in the event. The Contest was held in two stages and included a theoretical and a practical part with results of both defining the winners.

In 2017, the Innovator Corporate Idea Management System, an automated framework to collect and process employees' proposals on improving and developing business including labor-saving proposals, was launched in NOVATEK and its 11 subsidiaries. More than 250 ideas have been submitted by the employees, and more than 30 were approved for implementation.

### Social Programs

The focus in employee relations is on implementing social programs. According to the Core Concept of the Company's social policy, which was adopted in 2006, the social benefits package for employees includes the following programs:

- **Voluntary medical insurance for employees**

The program includes full outpatient care, dental care, and emergency and scheduled hospitalization.

- **Therapeutic resort treatment**

Employees and their families can purchase health resort vouchers at a discount. Under this program the NOVATEK employees may spend their vacations in 45 health resorts located in Russia's most picturesque settings.

- **Repayable Financial Aid Program**

The special-purpose loans program has two focus areas:

- short-term special-purpose loans intended for employees who experience economic hardship;
- special-purpose interest-free home loans to employees residing in Tarko-Sale, Novy Urengoy, Moscow, Nadym, Sosnovy Bor and Tyumen.

- **Targeted compensation and social support payments**

This program provides targeted free support to the Company's employees in specific life circumstances, including childbirth, the event of natural disasters or fire, compensation for care of a child up to 3 years of age, financial aid for care of disabled children, financial aid for burial, compensation for sports and recreation classes for employees, as well as on the occasion of the jubilee.

- **Pension Program**

Since 2007, NOVATEK has offered its retired employees supplementary benefits in line with the Regulations on Social Benefits for Retired NOVATEK Group Employees. Employees with an employment track record of at least five years with the Company who resign at the full retirement age are entitled to monthly benefit payments from the Company (suspendable in case the retiree gets a job). The benefit amount is subject to the employee's average salary, employment track record and geographical location.

Along with providing an optimum social benefits package, the Company is also committed to creating opportunities for employees to play sports and get involved in sports and cultural events. In 2017, our employees and their family members visited exhibitions at Russia's national museums, classical music

concerts, and attended sporting events like football (soccer) games and acrobatic rock and roll competitions with the Company's assistance.

## **SOCIAL POLICY AND CHARITY**

Social Policy and Charity make up an important part of NOVATEK's activities. In 2017, the Company continued to pay close attention to projects aimed at supporting the culture, preserving and revitalizing national values and spiritual legacy of Russia, promoting and integrating the Russian art into the international cultural space, developing mass and high-performance sports. NOVATEK enters into agreements with regional governments across the Company's footprint and implements programs to improve living standards and preserve the distinctive cultural identity of the indigenous peoples of the Far North.

In 2017, NOVATEK and its subsidiaries invested about RR 2.8 billion in projects and activities related to the support of indigenous peoples, charitable contributions, cultural and educational programs.

### **Cooperation with the regions**

Within the framework of agreements signed with various regions, the Company was investing in YNAO, the Leningrad, Chelyabinsk, Tyumen, and Kostroma Regions throughout 2017. The Company also financed the construction, repairs and upgrades of social infrastructure facilities, earmarked significant funds to implementing educational, cultural, children and youth programs and projects and was supporting low-income families, people with disabilities, the elderly and veterans.

NOVATEK is annually providing assistance to various regions by helping with settlement development, construction and renovation of accommodation, educational facilities and advancing local healthcare.

The Company is directly involved in funding the construction of important social infrastructure facilities across the YNAO, including an 800-student school in the village of Gyda, Taz District.

### **Cooperation with Indigenous Peoples of the Far North**

During the reporting year, NOVATEK provided financial support to the Yamal for Descendants Association of indigenous peoples and its district branches. We



assisted indigenous peoples through financing the purchase of equipment and materials required for the work of fishermen and reindeer herders. NOVATEK financed fuel purchases for air delivery of the nomadic population and food to remote areas. One particular area of support is taking part in organizing and staging ethnic festivals of indigenous peoples as well as provision of funding for environmental program.

### **Educational Programs**

NOVATEK continued to develop the Company's continuing education program, which provides opportunities to gifted students from the regions where we operate to further their education at top-rated universities, participate in NOVATEK internships and, upon completion of their studies, possible employment with the Company.

Recruitment and career guidance for promising employees start with the Gifted Children program implemented at School No. 8 in Novokuybyshevsk, school No. 2 in Tarko-Sale and school No. 81 in Tyumen. Special classes are formed on a competitive basis from the most talented grade 10 and 11 students with above-average test scores.

The Company has also implemented two Grants programs for schoolchildren and teachers living in the Purovsky District of the Yamal-Nenets Autonomous Area.

The Grants program for schoolchildren is aimed at academic and creative development and encouraging a responsible attitude towards studies. Under the program, students in grades five (5) through eleven (11) living in the districts are awarded grants from the Company. In 2017, the Company awarded 38 grants to students under this program.

The Grants program for teachers is intended to raise the prestige of the teaching profession and create favorable conditions for developing new and talented teachers. In 2017, three (3) teachers from the Purovsky District received grants under this program.

In an effort to create conditions for more effective use of university and college resources in preparing students for future professional activities, the Company has developed and successfully implemented the NOVATEK-VUZ program. The program is an action plan for focused, high-quality training for specialists with higher education in key areas of expertise in order to grow the Company's business and meet its

needs for young specialists. The program is based at the Saint-Petersburg University of Mines, the Gubkin Russian State University of Oil and Gas in Moscow and the Tyumen Industrial University.

Students, who have passed their exams with good and excellent results, receive additional monthly payments. During their studies, the students are offered paid field, engineering and directed internships. This experience allows them to apply the knowledge obtained at lectures and seminars to real-life situations and gain experience in the professions they've chosen, while the Company receives an opportunity to meet potential employees.

### **Preserving Cultural Heritage**

In 2017, NOVATEK continued its cooperation with Russia's leading museums including the Russian State Museum, the Moscow Museum of Modern Art, and the Multimedia Art Museum / Moscow House of Photography, and supported the contemporary art and music projects in Russia and abroad.

The Company supported exhibitions "Children of the Soviet State" and "Posters of the Revolutionary Era" in the Russian State Museum to mark the 100th anniversary of the October Revolution, and supported the annual Imperial Gardens of Russia international festival of garden and park art in the Mikhailovsky Garden of St. Petersburg. In 2017, the main theme of the festival was avant-garde art.

In partnership with NOVATEK, the Moscow Museum of Modern Art (MMOMA) presented the exhibition "Nepokorennye Prospect" to celebrate St. Petersburg artists of the 20th century. In the reporting year, NOVATEK also supported launching of the MMOMA Education Center. MMOMA delivered a course of lectures on the history of Russian and foreign art, photography, and architecture at the office of NOVATEK to the Company's employees and their families.

For several years, NOVATEK has been the General Partner of the History of Russia in Photographs, a program of Multimedia Art Museum / Moscow House of Photography. In 2017, exhibitions "Russia. 1917" in St. Petersburg, "The Industrial World of Alexander Rodchenko" in Nizhny Novgorod, "Russia. 20th Century in Photographs. 1941-1945" in Samara, "Lilya Brick. The Journey That Never Happened" in Ulyanovsk took place.

In 2017, NOVATEK continued as the General Partner of the Moscow Soloists Chamber Ensemble led by

Yuri Bashmet. NOVATEK is a permanent partner of the international festival-school of contemporary art TERRITORIYA. As part of the festival in 2017 Russian and foreign performances and exhibitions were shown, as well as an educational program. The Company also supported the activities of the Gogol-center.

In 2017, the Company also sponsored a number of projects abroad. "Peter the Great, a Tsar in France. 1717" exhibition was held in the Palace of Versailles national museum in France, marking the 300th anniversary of Peter I visiting France. MusicAeterna orchestra opened the Salzburg Festival with Mozart's La clemenza di Tito under the baton of Teodor Currentzis.

### **Sports Projects**

NOVATEK attaches great importance to programs for the development of amateur and professional sports. The Company, its subsidiaries and joint ventures regularly hold tournaments in the most popular and widespread sports, such as football, volleyball, swimming, ski, to name a few.

The Company supported the children and youth sports in the regions of its operations. In 2017, the "NOVATEK – Step to Bigger Football" Indoor Football Cups among secondary school teams were held in the Chelyabinsk and Kostroma Regions, which were attended by several thousand boys and girls. The winning teams of the Chelyabinsk and Kostroma championships went to the Russian National Football Team training base in Sochi where the Super Cup match was held.

The Company supported Figure Skating and Ice Hockey Federations of the Yamal-Nenets Autonomous Region, and Student Basketball Association with more than 800 teams and 10,000 boys and girls participating in competitions. The Russian Federation of DanceSport and Acrobatic Rock'n'Roll and the Company support corporate dance sport and acrobatic rock'n'roll clubs in the regions where the Company operates. In April 2017, members of the corporate acrobatic rock'n'roll clubs participated in the first Russia-wide acrobatic rock'n'roll competition where the Kostroma team took the first place.

In the reporting year, NOVATEK continued cooperation with the Football Union of Russia as the General Partner of the Russian National Football Teams. The Company supported woman's volleyball club Dinamo and the NOVA Volleyball Club (Novokuybishevsk).

### **Charity**

In 2017, NOVATEK adopted its Charity Policy, which provides for supporting children in desperate need of medical care residing in the regions where the Company operates. In the reporting year, the Company procured equipment for regional healthcare facilities, and financed children treatment and rehabilitation programs.

The scope of activities undertaken by the All Together volunteer movement, which NOVATEK founded in 2008, expanded. The main volunteer activities were assistance to orphans and children with various illnesses, as well as to seniors.

# Management and Corporate Governance

## CORPORATE GOVERNANCE SYSTEM

NOVATEK strives to commit to the highest standards of corporate governance. We believe that such standards are an essential prerequisite to business integrity and performance and provide a framework for socially responsible management of the Company's operations.

The Company has established an effective and transparent system of corporate governance complying with both Russian and international standards. NOVATEK's supreme governing body is the General Meeting of Shareholders. The corporate governance system comprises the Board of Directors, the Board Committees, and the Management Board, as well as internal control and audit bodies and the Corporate Secretary. The activity of all these bodies is governed by the applicable laws of the Russian Federation, NOVATEK's Articles of association and internal documents available on our website ([www.novatek.ru](http://www.novatek.ru)).

NOVATEK strives to consider the principles of corporate governance outlined in the Corporate Governance Code recommended by the Central Bank of Russia (Information Letter № 06-52/2463 dated 10 April 2014). The Company follows the recommendations of the Code, as well as offering to our shareholders and investors other solutions that are intended to protect their rights and legitimate interests.

Since the Company's shares are listed on the London Stock Exchange in the form of depositary receipts, NOVATEK places great emphasis on the UK Corporate Governance Code and the Regulation of the European Parliament and of the Council on market abuse and follows their recommendations as far as practicable.

The Company adheres to the internal Corporate Governance Code approved by the Board of Directors in 2005 (Minutes No. 60 of 15 December 2005).

The Company also adheres to the internal Code of Business Ethics approved by the Board of Directors in 2011 (Minutes No. 133 of 24 March 2011). The Code establishes general norms and principles governing the conduct of members of the Board of Directors, the Management Board and the Revision Commission, as well as NOVATEK's management and employees, which were drafted on the basis of moral and ethical values and professional standards. The Code also determines the rules governing mutual relationships inside the Company and NOVATEK's relationships with its subsidiaries and joint ventures, shareholders, investors, the government and public, consumers, suppliers, and other stakeholders.

The Company monitors changes of the current legislature and the Listing Rules of PAO Moscow Exchange and harmonizes its internal documents according to the changes. NOVATEK's Regulations on the Corporate Secretary, the Internal Audit Policy, Regulations on Risk Management and Internal Control System and other regulations on the Company's corporate bodies are up to date and don't require any corrections.

On 12 December 2017, the Corporate Strategy Day, the Company's management noted corporate governance as one of the Company's strategic foundations and announced the improvement of corporate governance policy and procedure among the objectives of sustainable development.

In order to improve the efficiency of the corporate governance system, in 2017, the Company updated its information policy. The Board of Directors approved a new edition of the Regulation on informa-

tion policy (on 25 August 2017), taking into account the relevant recommendations of the Corporate Governance Code.

NOVATEK's corporate governance practices make it possible for its executive bodies to effectively manage ongoing operations in a reasonable and good faith manner and solely to the benefit of the Company and its shareholders.

### **GENERAL MEETING OF SHAREHOLDERS**

The General Meeting of Shareholders is NOVATEK's supreme governing body. The activity of the General Meeting of Shareholders is governed by the laws of the Russian Federation, the Company's Articles of association, and the Regulations on the General Meetings approved by NOVATEK's General Meeting of Shareholders in 2005 (Minutes No. 95 of 28 March 2005) with further alterations and amendments.

The General Meeting of Shareholders is responsible for the approval of annual reports, annual financial statements, the distribution of profit, including dividends payout, the election of the Board of Directors and the Revision Commission, approval of the Company's Auditor and other corporate and business matters.

On 21 April 2017, the Annual General Meeting of Shareholders approved the annual report, annual financial statements (in accordance with the Russian Accounting Standards), distribution of profit and the size of dividends based on the results of FY2016. The meeting also elected the Board of Directors and the Revision Commission, as well as approved remuneration to members of the Board of Directors, Revision Commission and the Company's external auditor for 2017.

On 29 September 2017, the Extraordinary General Meeting of Shareholders approved the amount of interim dividend for the first half of 2017.

### **BOARD OF DIRECTORS**

The Board of Directors (the Board) activity is governed by the laws of the Russian Federation, the Company's Articles of association and the Regulations on the Board of Directors approved by NOVATEK's General Meeting of Shareholders in 2005 (Minutes No. 96 of 17 June 2005) with further alterations and amendments.

The Board carries out the overall strategic management of the Company's activity on behalf of and in the interests of all its shareholders, and ensures the Company's efficient and effective performance in order to increase shareholder value in a prudent and responsible manner.

The Board determines the Company's strategy and priority lines of business, endorses long-term and annual business plans, reviews financial performance, internal control, risk management and other matters within its competence, including optimization of corporate and capital structure, approval of major transactions, making decisions on investment projects and recommendations on the size of dividend per share and its payment procedure, and convening General Meeting of Shareholders. The General Meeting of Shareholders elects the members of the Board.

The current members of the Board were elected at the Annual General Meeting of Shareholders on 21 April 2017. The Board of Directors is comprised of nine (9) members, of which eight (8) are non-executive directors. Three (3) directors are considered to be independent in accordance with the Corporate Governance Code recommended by the Central Bank of Russia, the Listing Rules of PAO Moscow Exchange and the UK Corporate Governance Code. The Board Chairman is Alexander E. Natalenko. The Chairman is responsible for leading the Board and ensuring its effectiveness.

The members of NOVATEK's Board have a wide range of expertise as well as significant experience in strategic, operational, financial, commercial and oil and gas activities. The Board members hold regular meetings with NOVATEK's senior management to enable them to acquire a detailed understanding of NOVATEK's business activities and strategy and the key risks impacting the business. In addition to these formal processes, Directors have access to the Company's medium-level managers for both formal and informal discussions to ensure the regular exchange of information needed to participate in the Board meetings and make balanced decisions in a timely manner.

Efficient operation of the Board of Directors is supported by the Corporate Secretary, who has sufficient independence (appointed and dismissed by the Board of Directors) and endowed with the necessary powers and resources to carry out its tasks in accordance with the Regulations on the

Corporate Secretary (Minutes No. 168 of 28 April 2014 with further alterations and amendments).

### Board activities during the 2017 corporate year<sup>1</sup>

To ensure the Company's efficient performance, the Board meetings are convened on a regular basis at least once every two months. During 2017, the Board met nine (9) times, of which five (5) meetings were held in absentia. The following key issues were discussed and respective decision made:

- reviewed and approved the Company's 2017 full year operating and financial results;
- recommended an interim dividend for first half 2017, based on interim financial results for the period, and a full year dividend for 2017, based on full year financial results;
- made decisions to convene an Extraordinary and Annual General Meetings of shareholders, and in 2017, for the first time during the meetings, telecommunications facilities were used to provide shareholders with remote access to participate and to fill out an electronic form of ballots;
- approved the Corporate Strategy for the period up to 2030;
- reviewed and approved NOVATEK's business plan for 2018;
- formed NOVATEK's Management Board and reduced its numerical composition to 11 members;

- approved the Regulation on evaluation of the Board of Directors and its committees; and
- held a self-assessment of the Board of Directors and Committees, resulting in a high assessment of the Company's development strategy, corporate governance, management and Board of Directors interaction, and overall organization and preparation of the Board of Director's and Committees' meetings.

### The Board of Directors membership as of 31 December 2017:

- Alexander E. Natalenko – Chairman of the Board
- Andrei I. Akimov
- Burckhard Bergmann
- Michael Borrell
- Robert Castaigne
- Leonid V. Mikhelson
- Victor P. Orlov
- Gennady N. Timchenko
- Andrei V. Sharonov

During 2017, there were no changes to the composition of NOVATEK's Board of Directors. In accordance with the recommendations of the Corporate Governance Code and the Listing Rules of PAO Moscow Exchange, three (3) of the nine (9) elected members of the Board are considered independent directors.

### Board and Committee Meetings Attendance in the 2017 Corporate Year

Member	Independence <sup>2</sup>	Board of Directors	Audit Committee	Remuneration and Nomination Committee	Strategy Committee
Alexander E. Natalenko		9/9			3/3
Andrei I. Akimov		9/9			3/3
Burckhard Bergmann		9/9			3/3
Michael Borrell		9/9			3/3
Robert Castaigne	independent	9/9	4/4	4/4	
Leonid V. Mikhelson	executive	9/9			
Victor P. Orlov	independent	9/9	4/4	4/4	
Andrei V. Sharonov	independent	9/9	4/4	4/4	
Gennady N. Timchenko		9/9			3/3

1. From the Annual General Meeting of Shareholders on 21 April 2017 until the Annual General Meeting of Shareholders on 20 April 2018.

2. Independent Director as of 31 December 2017 in accordance with the Corporate Governance Code recommended by the Central Bank of Russia and the UK Corporate Governance Code.

## BOARD COMMITTEES

The Company has three (3) Board Committees: the Audit Committee, the Remuneration and Nomination Committee and the Strategy Committee. The Committees' activities are governed by the specific Committee Regulations approved by the Board of Directors and are available on our website.

The Committees play a vital role in ensuring that the high standards of corporate governance are maintained throughout the Company and that specific decisions are analyzed and the necessary recom-

mendations are issued prior to general Board discussions. The minutes of the Committees meetings are circulated to the Board members and are accompanied by necessary materials and explanatory notes.

In order to carry out their duties, the Committees may request information or documents from members of the Company's executive bodies or heads of the Company's relevant departments. For the purpose of considering any issues being within their competence, the Committees may engage experts and advisers having necessary professional knowledge and skills.

### Committees membership as of 31 December 2017

	Audit Committee	Strategy Committee	Remuneration and Nomination Committee
Chairman	Andrei V. Sharonov	Alexander E. Natalenko	Victor P. Orlov
Members	Robert Castaigne Victor P. Orlov	Andrei I. Akimov Burckhard Bergmann Michael Borrell Gennady N. Timchenko	Robert Castaigne Andrei V. Sharonov

#### Audit Committee

The primary function of the Audit Committee is control over financial and operating activities of the Company. In order to assist the Board in performing control functions the Committee is responsible for but not limited to evaluating accuracy and completeness of the Company's full year financial statements, the candidature of the Company's external auditor and the auditor's report, and the efficiency of the Company's internal control procedures and risk management system.

The Audit Committee works actively with the Revision Commission, the external auditor and the Company's executive bodies, inviting NOVATEK's managers responsible for the preparation of the financial statements to attend the Committee meetings.

In corporate year 2017, the Audit Committee met four (4) times.

#### Remuneration and Nomination Committee

The primary functions of the Remuneration and Nomination Committee is the development of an efficient and transparent compensation practice of members of the Company's management, enhancement of the professional expertise and improvement of the Board of Directors' effectiveness.

In order to assist the Board, the Committee performs the following functions:

- develop and regularly review the Company's policy on remuneration of the members of the Board of Directors, members of the collective executive body and the sole executive body of the Company, oversee its implementation and realization;
- preliminarily assess the work of the executive body of the Company for the year in accordance with the Company's remuneration policy;
- annual detailed and formalized performance self-appraisal or external appraisal of the Board of Directors and its members, as well as of BoD Committees, determination of the priority areas for reinforcing the Board of Director's composition;
- interaction with shareholders, which shall not be limited to major shareholders only, with a view to generate recommendations to the shareholders with respect to voting on the election of nominees to the Company's Board of Directors;
- plan appointments of members of the executive body and the sole executive body on the base of continuity principles; and
- supervision over disclosure of information on the Company's shares owned by the members of the Board of Directors and Management Board, and other key management employees.

In corporate year 2017, the Remuneration and Nomination Committee met four (4) times.

## Strategy Committee

The primary functions of the Strategy Committee are the determination of strategic objectives of the operations and control over the implementation of the strategy, as well as recommendations on the dividend policy.

In carrying out its responsibilities and assisting the members of the Board in discharging their duties, the Strategy Committee is responsible for but not limited to:

- evaluating the effectiveness of the Company's operations in the long-term;
- preliminarily reviewing and making recommendations on the Company's participation in other organizations;
- assessing voluntary and mandatory offers to acquire the Company's securities;
- considering the financial model and business valuation of the Company and its business segments in order to make recommendations to the Board of Directors in making decisions on the definition of business priorities of the Company;
- providing recommendations to the Board of Directors on transactions subject to approval by the Board of Directors; and
- providing recommendations to the Board of Directors with respect to the Company's policy on the use of its non-core assets.

In corporate year 2017, the Strategy Committee met three (3) times.

## MANAGEMENT BOARD

NOVATEK's Management Board is a collegial executive body responsible for the day-to-day management of the Company's operations. The Management Board is governed by the laws of the Russian Federation, NOVATEK's Articles of association, decisions of the General Meetings of Shareholders and the Board of Directors and by other internal documents. More information regarding the Management Board's competence is provided in NOVATEK's Articles of association.

Members of the Management Board are elected by the Board of Directors from among the Company's key employees. The Management Board is subordinated to the Board of Directors and the General Meeting of Shareholders. The Chairman of the Management Board is responsible for leading the Board and ensuring its effectiveness as well as organizing the Management Board meetings and implementing

decisions of the General Meeting of Shareholders and the Board of Directors. The Management Board acting as of 31 December 2017 is comprised of eleven (11) members elected by the Board of Directors on 25 August 2017 (Minutes No. 198 of 25 August 2017).

### Management Board Members as of 31 December 2017:

- Leonid V. Mikhelson – Chairman
- Alexander M. Fridman – First Deputy Chairman
- Lev V. Feodosyev – Deputy Chairman – Commercial Director
- Vladimir A. Baskov – Deputy Chairman
- Viktor N. Belyakov – Deputy Chairman of the Management Board for Economics and Finance
- Mark A. Gyetvay – Deputy Chairman
- Denis G. Khramov – Deputy Chairman
- Tatyana S. Kuznetsova – Deputy Chairman – Director of Legal Department
- Igor A. Plesovskikh – Deputy Chairman of the Management Board – Director for Geology
- Ilya V. Tafintsev – Director for Strategic Projects
- Sergey V. Vasyunin – Deputy Chairman of the Management Board – Operations Director

## REMUNERATION TO MEMBERS OF THE BOARD OF DIRECTORS AND MANAGEMENT BOARD

The procedure for calculating the remuneration and compensations to members of NOVATEK's Board of Directors is governed by the Regulations on Remuneration and Compensations payable to members of NOVATEK's Board of Directors approved by the Annual General Meeting of Shareholders (Minutes No. 122 of 24 April 2015). According to the Regulations the remuneration consists of the following types:

- fixed part of remuneration;
- remuneration for attending the Board of Directors meetings; and
- remuneration for attending the meetings of the committees of the Board of Directors.

The fixed part of remuneration to a Board member constitutes RR 10 million per corporate year. The Chairman of the Board of Directors is paid a fixed remuneration for the performance of its functions in the amount of RR 20 million per corporate year. Members of the Board of Directors are also paid remuneration for attending the meetings of the Board of Directors in the maximum amount of RR 3 million per corporate year and remuneration for attending the meetings of the committees of the Board of Directors in the maximum amount of RR 2 million per corporate year. The Board members are also compensated for travel and lodging expenses related

to implementation of their functions as NOVATEK Board of Directors members.

The procedure for and criteria of calculating remuneration to the Chairman and members of NOVATEK's

Management Board, as well as the compensation of their expenses, are prescribed in the Regulations for the Management Board and the employment contracts they sign with the Company.

#### Information on remuneration of members of NOVATEK's Board of Directors and Management Board in 2017, RR mln

	Board of Directors <sup>1</sup>	Management Board
<b>TOTAL PAID, INCLUDING:</b>	134.1	2,171.0
Salaries	–	666.6
Bonuses	–	1,471.0
Fees	133.1	–
Other property advancements	1.0	33.4

1. Some members of NOVATEK's Board of Directors are simultaneously members of the Management Board. Payments to such members in relation to their activities as members of the Management Board are included in the total payments to members of the Management Board.

#### INTERNAL CONTROL AND AUDIT

The Company has a system of internal control over financial and business operations in accordance with international best practices. The process of internal control is an integral part of the risk management process.

The system of internal control consists of the Board of Directors, the Audit Committee, the Chairman of the Management Board, the Management Board, the Revision Commission and the Internal Audit Division.

The primary objects of internal control are PAO NOVATEK, its subsidiaries and joint ventures, and their subdivisions, as well as their ongoing business processes.

In order to combat corruption, mitigate compliance, operational and reputation risks, the Company adopted the Anti-Corruption Policy approved by the Board of Directors on 1 September, 2014 (Minutes No. 170 of 1 September 2014) and the Regulation on NOVATEK Risk Management and Internal Audit System approved by the Board of Directors on 1 September, 2014 (Minutes No. 170 of 1 September 2014) with amendments and additions.

##### Revision Commission

The Revision Commission consisting of four (4) members who are elected at the Annual General Meeting of Shareholders for a period of one year. The com-

petence of the Revision Commission is governed by the Russian Federation Law On Joint Stock Companies No. 208-FZ dated 26 December 1995 as well as the Company's Articles of association and the Regulations on the Revision Commission approved by the General Meeting of Shareholders in 2005 (Minutes No. 95 of 25 March 2005).

The Revision Commission is an internal control body responsible for oversight of the Company's financial and business activities. The Revision Commission performs audits of the Company's financial and business performance for the year, as well as any other period as may be decided by its members or other persons authorized in accordance with Russian Federation law and the Company's Articles of association. The results of these audits are presented in the form of findings by the Revision Commission.

In March 2018, the Revision Commission completed the on-site audit revision of financial and business activity of the Company for the year 2017. As a result, the conclusions about the reliability of the data contained in the Company's 2017 Financial Statements (under the Russian accounting standards) and Annual Report were prepared and submitted to the Annual General Meeting of Shareholders.

##### Internal Audit Division

In order to conduct a systematic, independent evaluation of the reliability and effectiveness of the risk management and internal control system as well as



corporate governance practices the Company performs internal audits of the Company's operations. The internal audit function is implemented by the independent Internal Audit Division, which has operated continuously since 2005.

The Internal Audit Division is functionally subordinate to the Board of Directors and is guided by International professional internal audit standards of Institute of Internal Auditors. The Division also adheres to the principles and rules of conduct stated in internal auditor's Code of Business Conduct of the Institute of Internal Auditors. In 2016, the Board of Directors approved NOVATEK's Internal Audit Policy (Minutes No. 192 of 26 August 2016).

The Division carries out its activities on the basis of an annual plan of inspections approved by the Audit Committee and uses a combination of risk-based and cyclic approaches. According to the results of inspections it develops measures to eliminate identified risks and optimize financial and business activities. Implementation of the measures is monitored on a regular basis.

The Internal Audit Division regularly interacts with the external auditor by exchanging information on action plans, audit results and other matters of significance to ensure the effective discharge of their responsibilities.

To improve the efficiency and optimize the costs the Internal Audit Division employees serve on the revision commissions of subsidiaries and joint ventures.

#### **External Auditor**

The Annual General Meeting of Shareholders appoints an external auditor to conduct independent review of NOVATEK's financial statements. The Audit Committee gives recommendations to the Company's Board of Directors regarding the candidatures of external auditors and the price of their services. Based on the Committee's recommendations, the Board proposes the auditor's candidature for the consideration and for approval by the Annual General Meeting of Shareholders.

AO PricewaterhouseCoopers Audit (an internationally recognized audit firm) was chosen as the Company's external auditor to conduct the audit of the annual financial statements for 2017 under RAS, as well as independent reviews of the Company's quarterly financial statements and audit of the annual financial statements under IFRS.

In selecting the auditor's candidature, attention is paid to level of their professional qualifications, independence, possible risk of any conflict of interest, terms of the contract, and an amount of remuneration requested by the candidates.

The Audit Committee oversees the external auditor's independence and objectivity as well as the quality of the audit conducted. The Committee annually provides to the Board of Directors the results of review and evaluation of the audit opinion regarding the Company's financial statements. The Audit Committee meets with the auditor's representatives at least twice per year.

NOVATEK's management is aware of and accepts recommendations on the independence of the external auditor by restricting such auditor's involvement in providing non-audit services. Remuneration paid to the principle auditors for auditing and other services is specified in Note 24 to the consolidated financial statements prepared in accordance with IFRS standards for 2017.

#### **SHARE CAPITAL**

Our share capital is RR 303,630,600 and consists of 3,036,306,000 ordinary shares, each with a nominal value of RR 0.1. As of 31 December 2017, NOVATEK did not have preference shares.

Our shares are traded in Russian roubles on the Moscow Exchange and have a first grade listing (symbol: NVTK).

The Federal Financial Market Service issued to NOVATEK a permit for circulation of shares beyond the Russian Federation of 910,589,000 ordinary shares comprising 29.99% of the Company's share capital.

Our Global Depositary Receipts (GDR) are listed on the London Stock Exchange (symbol: NVTK), with each GDR representing 10 ordinary shares. As of 31 December 2017, NOVATEK's GDRs were issued on 621,792,560 ordinary shares comprising 20.48% of the Company's share capital.

Equity stakes in NOVATEK's share capital and the number of shares owned by members of the Board of Directors and Management Board<sup>1</sup>

	Equity stake as of 31 December 2017, %	Number of shares
<b>BOARD OF DIRECTORS</b>		
Alexander E. Natalenko	–	–
Andrei I. Akimov	–	–
Burckhard Bergmann	–	–
Michael Borrell	–	–
Robert Castaigne	–	–
Leonid V. Mikhelson	0.7181	21,803,332
Victor P. Orlov	–	–
Andrei V. Sharonov	–	–
Gennady N. Timchenko	–	–
<b>MANAGEMENT BOARD</b>		
Vladimir A. Baskov	0.0288	874,408
Viktor N. Belyakov	–	–
Mark A. Gyetvay	–	–
Sergey V. Vasyunin	0.0003	9,320
Tatyana S. Kuznetsova	0.1944	5,903,035
Igor A. Plesovskikh	–	–
Ilya V. Tafintsev	–	–
Lev V. Feodosyev	–	–
Alexander M. Fridman	0.0817	2,481,049
Denis G. Khramov	–	–

1. The equity stakes are given based on the records in the register of NOVATEK's shareholders and notification received from members of the Board of Directors and Management Board, in accordance with the Russian Federation laws.

In 2017, Leonid V. Mikhelson, member of NOVATEK's Board of Directors, made a transaction with NOVATEK's shares: acquisition of 86,220 shares under a securities sales and purchase agreement (20 December 2017).

## DIVIDENDS

The Company's Dividend Policy is regulated by the Regulations on Dividend Policy of PAO NOVATEK approved by the Board of Directors on 28 April 2014 (Minutes No. 168 of 28 April 2014). According to the regulations, consolidated net income under IFRS is applied for calculation of the dividend size.

NOVATEK's dividend policy is based on keeping the balance between the Company's business goals and shareholder's interests. A decision to pay dividends as well as the amount of the dividend, the payment deadline and form of the dividend is passed by the Annual General Meeting of Shareholders according to the recommendation of the Board of Directors. Dividends are paid twice a year. In determining the recommend-

ed amount of dividend payments to be distributed the Board of Directors consider the current competitive and financial position of the Company, as well as its development prospects, including operating cash flow and capital expenditure forecasts, financing requirements, debt servicing and other such factors as it may deem relevant to maintaining financial stability and flexible capital structure of the Company. NOVATEK is strongly committed to its dividend policy.

On 13 March 2018, the Board of Directors of PAO NOVATEK recommended to the Annual General Meeting of Shareholders to pay dividends for FY 2017 in the amount of RR 8.0 per ordinary share or RR 80 per one Global Depositary Receipt (GDR), exclusive of RR 6.95 of interim dividends per ordinary share or RR 69.50 per one GDR paid for the first six months of 2017.

Thus, should the General Meeting of Shareholders approve the recommended dividend, the dividends for 2017 will total RR 14.95 per ordinary share (RR 149.5 per one GDR), and the total amount of divi-

dends payable for 2017 will be RR 45,392,774,700. This will represent a 7.6% increase in dividend per share compared to 2016.

▼ **Accrued and paid dividends on NOVATEK shares for the period 2012 to 2017**

<b>Dividend Accrual Period</b>	<b>Amount of dividends, RR per share</b>	<b>Total amount of dividends accrued, RR</b>	<b>Total amount of dividends paid, RR</b>
2012	6.86	20,829,059,160	20,829,057,901
2013	7.89	23,956,454,340	23,956,386,795
2014	10.30	31,273,951,800	31,273,942,156
2015	13.50	40,990,131,000	40,990,059,262
2016	13.90	42,204,653,400	42,204,575,052
First half 2017	6.95	21,102,326,700	21,102,282,190

The amount of paid dividends accrued for the years 2012 to 2016, and for the first six months 2017 is reported as of 31 December 2017. Partial payment of the accrued dividends was made due to provision by shareholders of incorrect postal and/or banking details and insufficient information regarding banking or postal details of shareholders.

## INFORMATION TRANSPARENCY

NOVATEK complies with best practices for information disclosure while adhering to a maximum level of transparency. The Regulations on Information Policy approved by the Board of Directors (Minutes No. 198 of 25 August 2017), define main principles for disclosing information and increasing information transparency.

Material information about the Company is disclosed in a timely manner in the form of press releases and material facts notifications through authorized disclosure in accordance with the applicable laws of Russian Federation and United Kingdom. The Company discloses quarterly financial statements in accordance with the Russian ("RAS") and International Financial Reporting Standards ("IFRS"), Management's Discussion and Analysis of Financial Condition and Results of Operations as well as presentations for investors.

The Company's website provides detailed information on all aspects of its activities, including our Sustainability Report. We regularly participate in information disclosure on greenhouse gas emissions and energy efficiency of production – the Carbon Disclosure Pro-

ject (CDP), and on the use of water resources – the CDP Water Disclosure Project, as well as other industry's publications and studies.

In order to further increase the transparency of the Company, and to improve the efficiency of interaction with the external audience and the media, the Management Board of the Company approved changes in the information strategy, which provide for expansion of the range of speakers, securing their levels of information activity and diversification of communication channels.

The Company maintains an ongoing dialogue with shareholders and investors in order to ensure full awareness of investment community about its activities. The main channels of communication with the investment community are through the Chairman of the Management Board, Deputy Chairman and the Investor Relations department. The Company's representatives meet on a regular base with key financial audiences to discuss issues of interest to them. In order to inform our shareholders, investors and all interested parties about the Company's long-term development plans, in December 2017, NOVATEK presented its strategy for the period up to 2030.

Pursuant to the uniform information policy principles, NOVATEK is actively involved in relations with federal, foreign and regional media. In 2017, the Public Relations Department hosted 12 meetings between the Company management and journalists of foreign and federal periodicals and organized six (6) trips to visit the Company's regional production facilities.

At the end of the reporting year, there were more than 30 thousand unique publications on the Company. Among the topics covered were launch of the Yamal LNG project, implementation plans of prospective LNG projects, the Company's plans to create its technological base on the basis of Russian enterprises, cooperation with foreign partners, long-term strategy, assets acquisition, entering new markets and our position on the global LNG market. In 2017, the number of publications on the Company's activities increased by 24% compared to the previous year, the growth of TV stories on Federal channels amounted to 70%.

The number of publications in 2017 in foreign media increased to 6.9 thousand or by 77% compared with the year 2016. The main topics were the Yamal LNG Project implementation and the beginning of commercial LNG deliveries along the Northern Sea route of by Arc7 class tankers. Two press tours were organized for foreign journalists to Sabetta, as well as separate trips of television groups to the plant site.

NOVATEK takes active part in industrial exhibitions and conferences. In 2017, NOVATEK's managers and employees participated in more than 15 exhibitions, conferences and round tables. In 2017, the Company took part in the St. Petersburg International Economic Forum, Eastern Economic Forum, Russian Energy Week, Forum «Arctic: Territory of dialogue», Forum «Arctic: Today and the Future», Exhibition – Forum «Ecotech» as well as governmental delegations within foreign business events. NOVATEK delegation also took part in the work of major international business and industry events – World Economic Forum in Davos, Conference on Natural Gas, LNG and associated gas, Gastech-2017 in Japan, Conference «Oil&Money» in London, X Eurasian Economic Forum in Verona.

The following corporate periodicals are published to inform the Company employees, their family members, and third parties of the Company activities:

the NOVATEK newspaper and the NOVATEK PLUS magazine, containing materials on production plans and results as well as on cultural, sports and charity programs and projects. The main events of NOVATEK are published on the Company's intranet portal.

## REBRANDING

On 12 December, we introduced our new corporate identity alongside of our new corporate strategy up to the year 2030.

Over the past 15 years, the Company has evolved from being primarily a domestic gas producer and has now transitioned into a global gas player through our LNG platform. As a result of this transition it became readily apparent that a new corporate identity and logo was needed, one that was more easily understood as an international visual communication in any language in any part of the world.

One of the key elements of brand identity is the corporate logo. It traditionally includes a graphic mark and a wordmark. The former NOVATEK logo was created in 2003 and was primarily tailored for the Russian domestic market. It consisted of a stylized Russian Cyrillic letter H (“H”) crossed with three blue lines representing the flows of natural gas from various producing horizons. The wide and solid wordmark emphasized confidence, virility, and solidity.

Our new logo symbolizes the vaporizing molecules of natural gas and reflects two aggregate states of methane: liquid and gaseous. The light blue color symbolizes the environmentally friendly fossil of natural gas and our commitment to sustainable development principles, the dark blue color represents the Arctic environment where the Company operates, and the red color means heat and energy. The wordmark or typeset was also revisited and refined, and the new typeface looks contemporary and conveys pure shape and vigor.

Our new brand identity, including our corporate logo, symbolizes the Company's spirit and dynamism, and better reflects our vision of transforming into a global gas power through our unique and value accretive LNG platform. It also conveys our mission and values as the Company leverages its massive hydrocarbon resources into sustainable economic value for all of our stakeholders.

# Additional Information

## RISK MANAGEMENT SYSTEM

The Company's activities are subject to risks inherent only to the Company or associated with the Company's core business.

A multilevel system of risk management has been implemented at the Company. Powers, duties and responsibilities for specific risk management procedures are delegated to different governance levels of the Company depending on the assessment of financial impact of risk. The Company's risk management policy is laid out in the Regulations on OAO NOVATEK Risk Management and Internal Control System approved by the Board of Directors on 1 September 2014 (Minutes No. 170 of 1 September 2014) with amendments.

The Board of Directors' Audit Committee is responsible for the supervision over the reliability and efficiency of the risk management framework and review of the risk management policy. In the reporting year, the Audit Committee after careful review and analysis of the information provided, recognized NOVATEK's risk management activities as compliant with the risk management policy of the Company.

Below is the list of risks and approaches to risk management applied by the Company. The risks described herein are not exhaustive and reflect the opinion on the most material risks based on the estimates of the Company's management.

Risk	Risk description	Risk management approaches used by the Company
<b>OPERATIONAL RISKS</b>		
RISKS OF EMERGENCIES AND INCIDENTS	The Company's subsidiaries and joint ventures are subject to the risks of emergencies and incidents at hazardous production facilities that may entail business interruption, hazardous emissions or spills, which in turn may have a negative effect on the Company's business reputation and financial performance.	<p>The Company performs continuous monitoring of industrial safety compliance, develops and implements organizational and technical measures aimed at mitigating the risks of emergencies and incidents and reducing potential losses as part of its existing integrated industrial safety management system that is certified under the OHSAS 18001:2007 standard. The Company holds property and business interruption insurance policies.</p> <p>The Company adheres to the principle of responsible investments which implies that new design solutions, technologies and equipment installed help significantly mitigate accident risks.</p> <p>The Central Dispatch Office (CDO) operates in the Company, one of its function is to ensure prompt response to production incidents. Since 2017, the functionality of the CDO was expanded by adding centralized control of well construction and worko-</p>

		<p>ver on top of the control of production, treatment and transportation processes of production, treatment and transportation processes.</p> <p>A Digital Field Production Management System was commissioned in Yamal LNG to ensure production management and prompt response to process incidents. It enables promptly calculating the optimum process mode in a semi-automatic way, identifying deviations and planning field operations.</p>
MONOPOLY RISKS	<p>The Company depends on monopoly suppliers of transport services (such as Gazprom, RZD, or Transneft). The Company has no influence on the capacity of transport facilities of the above monopolies and rates established by a Federal body.</p>	<p>The Company enters into long-term agreements and in a timely manner arranges for interaction with monopolies regarding hydrocarbon transportation by pipeline and railway transport.</p> <p>To reduce its dependency, the Company concludes agreements enabling it to use alternative methods of product transportation (an agreement with SIBUR for the supply of light hydrocarbons to Tobolsk Petrochemical Complex).</p>
COMPETITIVE RISKS	<p>The Company operates in an environment of tough competition with Russian and international oil and gas companies in the following areas:</p> <ul style="list-style-type: none"> <li>• obtaining of subsoil licenses and acquisition of companies holding subsoil licenses</li> <li>• selling natural gas on the Russian market</li> <li>• selling liquid hydrocarbons in the Russian and global markets</li> <li>• access to transportation infrastructure, which has technological limitations</li> <li>• employment of highly qualified specialists to work for the Company and its subsidiaries and joint ventures.</li> </ul>	<p>The Company monitors commercially available assets with regard to the objectives of its long-term development strategy, enabling the Company to make an objective assessment of its competitive positions and to take the maximum benefit of its competitive advantages that include extensive regional work experience and synergy with the existing producing, transport, processing and distribution infrastructure.</p> <p>The Company pursues an active marketing policy and takes efforts to expand its customer base, and to enter into long-term agreements with buyers. To diversify its natural gas marketing portfolio, throughout the reporting period the Company was engaged in trading in the Natural Gas Section of the St. Petersburg International Mercantile Exchange.</p> <p>The Company implements an active HR policy and applies efficient mechanisms of attracting and retaining highly qualified employees.</p>
RISKS IN PROCUREMENT OF MATERIALS, WORKS AND SERVICES	<p>Failure to perform their obligations by the counterparties (quality and timeline of procurement, works and services).</p>	<p>The Company has put in place internal regulations and introduced a procedure to qualify counterparties and control performance of obligations. The Company has continuously encouraged its counterparties to improve their production capabilities, while making long-term agreements with the strategic counterparties.</p>
	<p>Procurement of materials, works and services at prices higher than the market.</p>	<p>Counterparties are as far as possible selected on a competitive basis. Strategic approaches ensuring maximum procurement efficiency are defined for the most critical and expensive procurement items.</p>

	<p>Reputational risks deriving from competition restriction and malpractice by employees.</p>	<p>Procedures are developed within the Company that provide for an objective, timely and transparent process of counterparty qualification and selection. There is no discrimination and unwarranted restriction of competition in the Company when developing qualification and technical requirements to counterparties and to the subject of procurement as part of design and qualification as well as at the stage of counterparty selection. The internal regulations in place provide for a maximum transparency procedure of counterparty selection with an adequate system of control over the actions of employees. Open ways to select counterparties are mostly used.</p> <p>Given the volatility in international relations with the countries providing sophisticated oil &amp; gas equipment, the Company pursues import replacement policies where it is appropriate.</p>
<p>COMMODITY PRICE RISKS</p>	<p>As an independent natural gas producer, NOVATEK is not subject to state regulation of natural gas prices. Nevertheless, the Company's prices are strongly influenced by the prices established by a Federal body.</p>	<p>State regulation of gas prices significantly reduces the risk of price volatility on the Russian gas market.</p>
	<p>Moreover, the Company is exposed to the current pricing environment on the Russian and international liquid hydrocarbon markets as it has no power over the contracts' base prices. Reduction of prices for liquid hydrocarbons may have a negative effect on the Company's financial performance.</p>	<p>In view of the vertically integrated production chain for liquid hydrocarbons and taxation peculiarities, the Company does not use commodity derivative financial instruments to reduce the risk of price changes for such type of products.</p>
<p>GEOLOGICAL RISKS</p>	<p>Exploration drilling is associated with multiple risks, including the risk of non-discovery of commercial reserves. Information on the Company's reserves depends on a number of factors and assumptions. Actual production volumes at the fields, along with the costeffectiveness of reserve development may deviate from estimates.</p>	<p>To minimize geological risks, the Company relies on the geological modeling and engages major contractors that apply state-of-the-art exploration technologies and methods.</p> <p>Since 2015, the Company has been employing foreign experts in geology and field development. Individual focused training programs have been implemented for the employees with due regard to periodic testing.</p> <p>The Company makes annual assessment and evaluation of its reserves based on the results of exploration and production drilling and other research information. An independent international adviser evaluates the Company's reserves according to international standards on annual basis.</p> <p>A Digital Field Production Management System was commissioned in Yamal LNG to ensure production management and prompt response to process incidents. It enables promptly calculating the optimum</p>

RISK OF EARLY TERMINATION, SUSPENSION OR RESTRICTION OF THE RIGHT TO USE SUBSURFACE MINERAL RESOURCES	Exploration and production of hydrocarbons in Russia is subject to licensing. The Company is thus exposed to the risk of early termination, suspension or restriction of its right to use subsurface mineral resources.	process mode in a semi-automatic way, identifying deviations and planning field operations.
ENVIRONMENTAL RISKS	The Company is subject to the probability of events having adverse consequences for the environment and caused by a negative impact of its industrial and other activities, as well as natural and technology-related emergencies.	<p>The Company strives to comply, and maintains a continuous monitoring of its compliance with the license agreements and the subsoil use laws, and submits timely requests for adjusting the terms of its license agreements.</p> <p>The Company has an environmental management system according to ISO 14001:2004 standard to ensure rational use of resources and to minimize the adverse effect the Company's operation may have on the environment.</p> <p>The Company adheres to the principle of responsible investment in operations, which implies that new design solutions, technologies and equipment installed help minimize environmental impact.</p>
PROJECT RISKS	Volatile exchange rates of the national currency and unstable lending conditions, growing funding costs, drop in hydrocarbon prices, precarious financial position of contractors and oil and gas equipment suppliers may affect the Company's Investment Program leading to delays in project execution and/or rising project costs.	<p>The Company implements expert review of projects at the project development stage. Investments are only channeled into the projects that are most likely to help the Company achieve its strategic objectives.</p> <p>The Regulation on Investment Projects Preparation, Coordination, Approval, Monitoring and Updating was approved in the Company in 2016. The project risks are evaluated at every stage.</p> <p>The Company has tightened its selection requirements for contractors and suppliers of oil and gas equipment. There is ongoing monitoring of their performance, including on-site visits to the oil and gas equipment plants involved in production and testing of the equipment for the Company.</p>
ETHICAL RISKS	The Company is exposed to the risks of disturbed relationships within the Company and with its subsidiaries and joint ventures, shareholders, investors, the government, the public, consumers or suppliers or other corporate entities or individuals, including the risk of fraud, corruption, and conflict of interest.	<p>In 2011 in order to minimize ethical risks, the Company introduced a Code of Business Conduct and Ethics.</p> <p>The Company is governed by the provisions of the internal Code of Business Conduct and Ethics and Code of Corporate Conduct, as well as the applicable Russian and English law in terms of public company regulation. This mitigates ethical risk to stakeholders and investors.</p> <p>To exclude ethical risks in its relations with third parties, the Company carries out tender procedures to select counterparties and has a well-established internal control and audit system.</p> <p>In 2014 the Board of Directors approved NOVATEK's Anti-Corruption Policy that established key principles and standards of anti-corruption practices for employees and includes a set of corruption prevention measures.</p>



		<p>As part of the Anti-Corruption Policy implementation a Security Hotline is in a 24/7 operation.</p> <p>In 2016, the Company established the procedure for notification and managing the conflicts of interest employees may come across in performing their job duties.</p>
SOCIAL RISKS	<p>The Company is subject to the following risks of a social nature:</p> <ul style="list-style-type: none"> <li>• internal risks associated with a possible incompliance of social programs implemented by the Company with the industry's average level that may lead to a higher labor turnover;</li> <li>• external risks associated with potential impediments in normal production activities caused by the public living in proximity to the production facilities.</li> </ul>	<p>The Company strives to ensure compliance of its social programs with the industry's average level and uses the up-to-date mechanisms for attracting and retaining highly professional employees.</p> <p>The Company's production facilities are located outside densely populated territories, and the Company monitors compliance with the rules and regulations while operating its facilities. The risks related to possible military conflicts, announcement of a state of emergency, or strikes, are insignificant, as the Company operates in economically and socially stable regions.</p>
TERRORISM RISKS	<p>The Company is subject to a risk of terrorist threat.</p>	<p>The Company takes measures required to ensure strict compliance with Federal Law No. 256-FZ of 21 July 2011 concerning the Fuel and Energy Complex Security. A complex of organizational and practical measures is constantly in place to ensure security of facilities, including linear ones.</p>
COUNTRY RISK	<p>NOVATEK is a Russian company operating in a number of Russian regions. Country risk is defined by the fact that Russia is still an emerging economy, the economic environment of which is not sufficiently stable.</p> <p>In 2015, a precipitous decline in crude oil prices and international sanctions caused volatility in foreign currencies, growing inflation rates, an increase in interest rates and an economic growth slowdown. The said factors have a negative impact on the Company's operational and financial performance.</p>	<p>Active marketing and financial policy enable the Company to mitigate the country risk.</p> <p>Moreover, the Company's management continuously analyzes the macro-economic environment and makes prompt decisions to mitigate potential risks.</p>
REGIONAL RISK	<p>The Company produces and processes hydrocarbons within Western Siberia, a region with a challenging climate.</p>	<p>The Company's vulnerability to region-specific impacts is insignificant and is entirely taken into account by the Company's management at the facilities design and operation stage.</p>
RISKS OF INFORMATION TECHNOLOGY AND INFORMATION SECURITY (CYBER-RISKS)	<p>The Company is exposed to the risks in the area of information technologies and information security, such as unauthorized access and changing or destroying digital assets.</p>	<p>The Company uses a multilevel system for digital assets protection, namely: all information systems are classified, owners and terms for provision of access rights are defined in relation to each of them, information storage and archiving terms are regulated. The Company makes use of licensed software only.</p>

The information technology development strategy of NOVATEK has been developed and approved to ensure the Company's sustainable development.

## FINANCIAL RISKS

CREDIT RISK	<p>The Company is exposed to a risk of losses related to a failure by counterparties to perform their contractual financial obligations when due, and in particular depends on the reliability of banks in which the Company deposits its available cash.</p>	<p>When selling natural gas on the domestic market, the Company continuously monitors the financial soundness of its consumers and takes actions in case there are overdue payments.</p> <p>Most of NOVATEK's international liquid sales are made to major customers with independent ratings. Almost all domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis.</p> <p>When selecting banks, the Company is governed by the bank's reliability confirmed by international ratings.</p>
REINVESTMENT RISK	<p>The Company's business requires substantial investments into field exploration and development, followed by the production, transportation, and processing of natural gas, oil, gas condensate and petroleum products. Insufficient funding for these and other expenditures may affect the Company's financial standing and performance.</p>	<p>The Company's capital investment plans are defined in its long-term development strategy, are revised on an annual basis and are generally in line with the Company's ability to generate cash flow from operations taking into account the need to pay dividend and service its debt.</p>
INTEREST RISKS	<p>As a major borrower, the Company is subject to risks associated with an increase in interest rates. Interest rates on some of the Company's loans may be linked to floating international and Russian base rates which dynamics are hard to predict. Volatile interest rates may restrict the use of borrowed capital as a financing source for the Company's investment activity and may increase interest rate expenses.</p>	<p>The Company pursues a balanced debt policy and strives to maximize the share of long-term liabilities with fixed rates in its debt portfolio. The Company strives to maintain flexibility in its investment program.</p>
CURRENCY RISKS	<p>Part of the Company's liabilities is denominated in foreign currencies, which may lead to losses in the event of Russian rouble depreciation. On the other hand, part of the Company's proceeds is also denominated in foreign currencies, which may lead to losses in the event of Russian rouble appreciation.</p>	<p>The liabilities expressed in foreign currency on the one hand, and export proceeds on the other generally offset each other and serve as a natural mechanism to hedge currency risks.</p>
LIQUIDITY RISK	<p>Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.</p>	<p>The Company's approach to managing liquidity risk is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation. In managing its liquidity risk, NOVATEK maintains an adequate ratio between cash reserves</p>

		<p>and debt, monitors forecast and actual cash flows and matches the financial assets and liabilities maturity profiles.</p> <p>The Company uses various short-term borrowings. The Company may use credit facilities and bank overdrafts to satisfy its short-term finance needs. To satisfy its needs for cash on a more permanent basis, the Company will normally raise long-term loans in the available markets.</p>
INFLATION RISK	<p>Changes in the consumer price index have an impact on NOVATEK's profitability and, as a consequence, its financial standing. The significant currency depreciation in 2015 caused a surge in inflation rates, which are impossible to accurately predict.</p>	<p>NOVATEK may not be able to predict the inflation level, since, apart from the consumer price level, it is necessary to take into account the change in the real purchasing power of the Russian rouble, the pricing conditions in liquid hydrocarbon export markets, and government policy in relation to tariffs for natural gas.</p> <p>NOVATEK monitors the consumer price index and accordingly acts to mitigate its costs.</p>
<b>LEGAL RISKS</b>		
RISK OF LAW CHANGES	<p>The Company is subject to a risk of facing consequences of changes in Russian laws in the following areas:</p> <ul style="list-style-type: none"> <li>• currency laws (in areas concerning export/import and borrowing operations)</li> <li>• tax laws (in areas regulating taxation systems and rates applicable to companies in general, and to companies producing and marketing natural gas and liquid hydrocarbons, specifically)</li> <li>• customs laws (in areas concerning the export of liquid hydrocarbons, including petroleum products); and</li> <li>• licensing requirements for natural resource extraction.</li> </ul>	<p>The Company is constantly monitoring draft laws enabling it to evaluate the consequences of such changes and to take them into account in its plans.</p>
LITIGATION RISKS	<p>The Company may be involved as a defendant or plaintiff in a number of proceedings arising in the normal course of its business.</p>	<p>When conducting its business, the Company adheres to the principle of prudence. Due to this fact, as of the approval date of the Annual Report, the Company was not involved in any material litigation and the associated risks are insignificant.</p>
RISK OF SANCTIONS	<p>In 2014, the Company was included into the US sectoral sanctions list whereby the US persons are prohibited to participate in providing financing to the Company for more than 60 days. The sanctions imposed restrict the Company's ability to refinance its debt.</p> <p>Furthermore, there is a risk of tougher US sanctions and risk of including the Company into other countries' sanctions lists, which may undermine the Company performance.</p>	<p>The Company follows a balanced financial policy enabling it to minimize its fundraising needs. Moreover, the Company still has a full access to the Russian capital market and a limited access to the international market.</p> <p>In case the US sanctions are toughened and the Company is included in other countries' sanctions lists, the Company management will make every possible effort to minimize the negative impact on the Company's business operations and financial standing.</p>

## RISK INSURANCE

Risk insurance is an integral part of NOVATEK's risk management system. In 2017, the insurance coverage guaranteed adequate protection against the risks of damage to the business of the Company or its subsidiaries and joint ventures. Insurance is provided by reputable insurance companies that have high ratings by the leading rating agencies (Standard & Poor's, Fitch Ratings, Expert RA, A.M. Best) with partial reinsurance of risks by major international insurance and reinsurance companies.

### Obligatory Risk Insurance

The Company and its subsidiaries and joint ventures fully meet the requirements of the applicable laws for maintaining obligatory insurance, such as civil liability insurance of:

- owners of hazardous production facilities; and
- owners of transport vehicles.

### Optional Risk Insurance

To reduce the risk of financial losses, the Company and its subsidiaries and affiliates maintain the following types of optional insurance:

- Insurance of the risk of property damage/loss, including the risk of mechanical failures;
- Insurance of the risk of damage from business interruption;
- Insurance of risks related to prospecting, exploration and production (risk of loss of control over a well); and
- Management liability insurance.

Since 2013, the Company implemented a comprehensive program of property and business risk insurance with respect to its and its subsidiaries' and joint venture's key assets. The cumulative insured amount for the risks of property damage and business interruption as at the end 2017 was RR 713 billion. The implemented program is viewed by the Company's management as an efficient measure for mitigating the consequences of potential accidents and provides additional guarantees for the attainment of the expected net profit and key indicators of the Company's performance.

In the reporting year, no insured major accidents or incidents occurred.

Since the end of 2016, one of NOVATEK's subsidiaries has been insuring its receivables with a view to as-

sess how efficiently this instrument is used to manage risks.

For more than 12 years the Company has maintained a management liability insurance for the top management of the Company and its subsidiaries against possible third-party claims for any losses incurred through any wrong action (or decision) made by its management bodies. The overall limit of all insurance coverage is Euro 120 mln.

## INFORMATION ON MEMBERS OF NOVATEK'S BOARD OF DIRECTORS

### MR. ALEXANDER E. NATALENKO

Chairman of NOVATEK's Board of Directors and Chairman of its Strategy Committee

Born in 1946

Mr. Natalenko completed his studies at the Irkutsk State University in 1969 with a primary focus in Geological Engineering. Subsequently, he worked with the Yagodinskaya, Bagdarinskaya, Berelekhskaya, Anadirskaya and East-Chukotskaya geological expeditions. In 1986, Mr. Natalenko headed the North-East Industrial and Geological Association and, in 1992, he was elected president of AO "Magadan Gold & Silver Company". He subsequently held various executive positions in Russian and foreign geological organizations. From 1996 to 2001, Mr. Natalenko held the position of Deputy Minister of Natural Resources of the Russian Federation. From 2013 to 2015 he was a member of the Board of Directors of AO Rosgeologia. From 2004 to present he is the Chairman of NOVATEK's Board of Directors.

Mr. Natalenko is the recipient of the State Prize of the Russian Federation and an Honored Geologist of Russia.

### MR. ANDREI I. AKIMOV

Member of NOVATEK's Board of Directors and Member of its Strategy Committee

Born in 1953

Mr. Akimov graduated from the Moscow Financial Institute in 1975 where he specialized in international economics. Between 1974 and 1987, Mr. Akimov held various executive positions in the Bank for Foreign Trade of the USSR. From 1985 to 1987 he served as Deputy Chief General Manager of the Bank for Foreign Trade branch in Zurich (Switzerland) and between 1987 and 1990, Mr. Akimov was the Chairman

of the Management Board of Donau Bank in Vienna (Austria). From 1991 to 2002 he was Managing Director of financial company, IMAG Investment Management & Advisory Group AG (Austria). Since 2003, Mr. Akimov has been the Chairman of the Management Board, the Deputy Chairman of the Board of Directors of Gazprombank (OAO). He is a member of Board of Directors of PAO Gazprom, Gazprombank (AO), AO Rosneftegaz, OOO Gazprom gas motor fuel, Bank GPB International S.A. and other.

#### **DR. BURCKHARD BERGMANN**

[Member of NOVATEK's Board of Directors, and Member of its Strategy Committee](#)

Born in 1943

Mr. Bergmann, born in Sendenhorst (Germany), studied physics at Freiburg and Aachen Universities from 1962 to 1968 and was awarded a doctorate in engineering by Aachen University of Technology in 1970. From 1968 to 1969, he worked at the German Federal Ministry for Research and Technology and from 1969 to 1972 at the Jülich Nuclear Research Centre. In 1972, Mr. Bergmann joined Ruhrgas AG (from 1 July 2004 – E.ON Ruhrgas AG), heading the LNG Purchasing Department. In 1978, he became Head of the Gas Purchasing Division responsible for gas purchasing, commercial aspects of gas transmission and storage, as well as gas billing. In January 1980, he was elected as a member of the Management Board of E.ON Ruhrgas AG, serving from June 1996 as its Vice-Chairman and from June 2001 to February 2008 as its Chairman. From March 2003 to February 2008 he was also a member of the Board of Management of E.ON AG.

Mr. Bergmann is a Chairman of the Advisory Board of Accumulatoren-Werke Hoppecke GmbH and a member of the Advisory Boards for Dana Gas, Dubai. Since October 2012 he is a member of the board of trustees of RAG Stiftung. Between 1998 and 2000, Mr. Bergmann held the position of President of Eurogas (the European Union of the Natural Gas Industry) and between 2000 and 2010 he was Vice-Chairman of the Board of the German East-West Trade Committee. Mr. Bergmann was a member of the Board of Gazprom OAO from 2000 to 2011.

Mr. Bergmann holds the following distinctions: Commander of the Royal Norwegian Order of Merit (1997), Foreign Member of the Academy of Technological Sciences of the Russian Federation, Order of Merit of the State of North Rhine-Westphalia (2004), Director

of the Year, Moscow (2007), Officer's Cross of the Order of Merit of the Federal Republic of Germany (2008) and the Russian Order of Friendship (2011).

#### **MR. MICHAEL BORRELL**

[Member of NOVATEK's Board of Directors and Member of its Strategy Committee](#)

Born in 1962

Mr. Borrell graduated from the University of Cambridge with a degree in Chemical and Mechanical Engineering (Master of Science – 1993, Bachelor – 1984). He joined TOTAL in 1985. Mr. Borrell worked with the affiliated companies of the concern; from 1995 he held a number of senior management positions in TOTAL. From 2003, he worked at the position of Vice-President for Corporate Planning and Business Development in Total E&P Indonesia. In July 2006, he was appointed President and CEO of TOTAL E&P Canada in Calgary. From September 2009 to June 2010, he was Vice President of the Caspian Area and Central Asia for TOTAL Exploration and Production. From July 2010, he served as First Vice President of Continental Europe and Central Asia. From January 2015 to September 2017, he worked as Senior Vice-President of Europe and Central Asia. From September 2017, he has been appointed Senior Vice President North Sea and Russia, which comprises the United Kingdom, Norway, Denmark, the Netherlands and Russia.

#### **MR. ROBERT CASTAIGNE**

[Independent member of NOVATEK's Board of Directors](#)  
[Member of the Remuneration and Nomination Committee of NOVATEK's Board of Directors](#)  
[Member of the Audit Committee of NOVATEK's Board of Directors](#)

Born in 1946

Mr Castaigne graduated from the Ecole Centrale de Lille in 1968 and the Ecole nationale supérieure du pétrole et des moteurs, he holds a doctorate in economics. He has spent his whole career at TOTAL SA, first as an engineer, then in various positions. From 1994 to 2008, he was Member of the Executive Committee, Executive Vice-President and Chief Financial Officer of TOTAL SA. He is Member of SANOFI's Board of Directors and Chairman of its Audit Committee, Member of VINCI's Board of Directors and its Audit and Remuneration Committees, Member of Societe Generale's Board of Directors and its Nomination and Audit and Internal Control Committees. He is Chevalier of the National Order of the Legion of Honour.

**MR. LEONID V. MIKHELSON**

Member of NOVATEK's Board of Directors  
Chairman of NOVATEK's Management Board  
Born in 1955

Mr. Mikhelson received his primary degree from the Samara Institute of Civil Engineering in 1977, where he specialized in Industrial Civil Engineering. That same year, Mr. Mikhelson began his career as foreman of a construction and assembling company in Surgut, Tyumen region, where he worked on the construction of the first section of Urengoi-Chelyabinsk gas pipeline. In 1985, Mr. Mikhelson was appointed Chief Engineer of Ryazantruboprovodstroy. In 1987, he became General Director of Kuibishevtruboprovodstroy, which in 1991, was the first company in the region to sell its shares and became private company, AO SNP NOVA. Mr. Mikhelson remained SNP NOVA's Managing Director from 1987 through 1994. Subsequently, he became a General Director of the management company "Novafininvest".

Since 2003, Mr. Mikhelson has served as a member of the Board of Directors and Chairman of the Management Board of NOVATEK. From March 2008 to December 2010, he has been a member of the Board of Directors and the Chairman of the Board of Directors of AO Stroytransgas. From 2009 to 2010 he was the Chairman of the Board of Directors of OAO Yamal LNG and from 2008 to 2011 he was a member of the Board of Directors of OOO Art Finance. From 2011 he is the Chairman of the Board of Directors of PAO SIBUR Holding and from 2011 to 2013 he was a member of the Supervisory Board of the OAO Russian Regional Development Bank. Mr. Mikhelson is the recipient of the Russian Federation's Order of the Badge of Honor, the Order of Merit for the Fatherland 2 degree and the title of honor "Honored man of the gas industry".

**MR. VICTOR P. ORLOV**

Independent member of NOVATEK's Board of Directors  
Chairman of NOVATEK's Remuneration and Nomination Committee  
Member of NOVATEK's Audit Committee  
Born in 1940

In 1968, Mr. Orlov graduated from the Tomsk State University as a geological engineer with a degree in "Geological survey and exploration of mineral deposits", and in 1986 from the Academy of National Economy under the USSR Council of Ministers, with a specialty in "Economics and Management of a National Economy".

From 1957 to 1963, he worked at coal mine and served in the Soviet Army. From 1968 to 1975, he was head of a geological survey, prospecting and exploration works in the geological organizations of Western Siberia, held positions of the geologist, chief geologist, chief of geological exploration crew. 1975–1978 — Consultant on geological exploration works in Iran. 1979–1981 — Deputy Head of the Geological Division of the Production Geological Association of central areas of Russia (Tsentrgeologiya). 1981–1986 — Deputy Head of Geology and Production departments of the Ministry of Geology of the RSFSR. 1986–1990 — CEO of Tsentrgeologiya. 1990–1992 — Deputy Minister of Geology of the USSR, First Deputy Chairman of the RSFSR State Committee for Geology and Use of Energy and Mineral Resources. 1992–1996 — Chairman of the Russian Federation Committee on Geology and Mineral Resources. 1996–1999 — Minister of Natural Resources of the Russian Federation. 2001–2012 — Member of the Federation Council of the Federal Assembly of the Russian Federation. 2001–2004 — First Deputy Chairman of the Federation Council Committee on Natural Resources and Environmental Protection. 2004–2011 — Chairman of the Federation Council Committee on Natural Resources and Environmental Protection. From 1998 to present — President of "Russian Geological Society" public organization. Author and co-author of over 300 scientific publications.

Professor, Doctor of Economics (1991), Candidate of geological-mineralogical sciences (1974), an Honored Geologist of Russia. Laureate of the State Prize of the Russian Federation in the field of science and technology. He was awarded the Order of Merit for the Fatherland 4 degree (2001), the Order of Honor (2015), 18 non-governmental awards, including 3 appreciation letters of the President of the Russian Federation, 2 Certificates of Merit of the Government of the Russian Federation.

**MR. ANDREI V. SHARONOV**

Independent member of NOVATEK's Board of Directors  
Chairman of NOVATEK's Audit Committee  
Member of NOVATEK's Remuneration and Nomination Committee  
Born in 1964

Mr. Sharonov graduated from the Ufa Aviation Institute and the Russian Academy of State Service at the President of the Russian Federation.

1989–1991 — Member of the USSR Parliament, until 1996 he headed the Committee for Matters Concerning Young Persons of the Russian Federation. From

1996 to 2007 — Head of Department, Deputy Minister, State Secretary in the Ministry of Economic Development and Trade of the Russian Federation. From 2007 to 2010 — Managing Director and Chairman of the Board of Directors of ZAO Investment Company Troika Dialog, head of the investment banking sector. From 2010 to 2013 — Deputy Mayor of Moscow for economic policy, was responsible for budgeting, procurement, industrial policy and business support, regulated market of trade and services. Served as a Chairman of the Regional Energy Commission. Mr. Sharonov is a deputy Head of the Executive Committee of the Moscow Urban Forum. From 2013 to 2016 — Dean of SKOLKOVO Business School and in September 2016 he was elected President of the Business School.

He is currently Chairman of the Board of Directors, an Independent member of the Board of Directors of OOO Management Company NefteTransService; a member of the Boards of Directors of PAO Sovcomflot and PAO PhosAgro, a member of the Supervisory Board of the Bank VTB (PAO).

Candidate of sociological sciences, an Honored Economist of the Russian Federation. He is the recipient of the “Aristos” Award in the “Independent Director” category in 2009, the National Award “Director of the Year — 2009” in the “Independent Director” category and the International Award “Person of the Year — 2012” in the “Business reputation” category, special award for personal contribution to the development of corporate management in 2016 from the Independent Directors Association and the Russian Union of Industrialists and Entrepreneurs. He was awarded the Order of Honor of the Russian Federation.

#### **MR. GENNADY N. TIMCHENKO**

Member of NOVATEK’s Board of Directors  
Member of NOVATEK’s Strategy Committee  
Born in 1952

In 1976, Mr. Timchenko graduated with a Master’s of Science from the Mechanical University in Leningrad. He began his career at the Izjorskii Factory in Leningrad, an industrial plant which made components for the energy industry. Between 1982 and 1988, he was a Senior Engineer at the Ministry of Foreign Trade. Mr. Timchenko has more than 20 years of experience in Russian and International energy sectors and he has built interests in trading, logistics and transportation related companies.

In 1988, Mr. Timchenko became a vice president of Kirishineftekhimexport, the export and trading arm

of the Kirishi refinery. In 1991, he worked for Urals Finland which specialized in oil and petrochemical trading. Between 1994 and 2001, Mr. Timchenko was managing Director of IPP OY Finland and IPP AB Sweden. Between 1997 and 2014, he co-founded Gunvor, a leading independent oil-trading company. Mr. Timchenko was a member of the Board of Directors of OOO Transoil and OOO BalttransService, and Airfix Aviation OY. Since 2009, he is a member of the Board of Directors of PAO NOVATEK. He is a member of the Board of Directors of PAO SIBUR Holding, the Chairman of the Board of Directors, President of the Ice Hockey Club SKA St-Petersburg, as well as the Chairman of the Board of Directors of OOO Kontinental Hockey League, a member of the Board of Trustees of the All-Russian public organization Russian Geographical Society, the Chairman of the Russian Council of the NPO Russian Chinese Business Council, the Chairman of the Board to promote OCD, Vice-President of the Olympic Committee of the Russian Federation, the Chairman of the Economic Council of the Franco-Russian Chamber of Commerce (CCIFR).

#### **ZULMIRA A. RAZAKOVA**

NOVATEK’s Corporate Secretary

Ms. Razakova holds a higher legal education degree and began working for NOVATEK in 2004. Between 2007 and 2012, Ms. Razakova held the position of lead specialist of the Management Board and Board of Directors staff. In April 2012, Ms. Razakova was elected as Secretary of the Board of Directors. Since 2014, Ms. Razakova has been NOVATEK’s Corporate Secretary.

#### **INFORMATION ON MEMBERS OF NOVATEK’S MANAGEMENT BOARD**

#### **MR. LEONID V. MIKHELSON**

Chairman of NOVATEK’s Management Board  
Member of NOVATEK’s Board of Directors  
Born in 1955

Details on Mr. Leonid V. Mikhelson are available in the “Information on Members of NOVATEK’s Board of Directors” section.

#### **MR. VLADIMIR A. BASKOV**

Deputy Chairman of NOVATEK’s Management Board  
Born in 1960

In 1986, Mr. Baskov graduated from the Moscow Higher Police School of the USSR. In 2000, he com-

pleted courses at the Management Academy at the Russian Ministry for Internal Affairs. From 1981 to 2003, he served in various departments within the Russian Ministry for Internal Affairs. From 1991 to 2003, Mr. Baskov held managerial positions within the aforementioned Ministry's organizational structures. In 2003 he was appointed Director of the Business Support Department for NOVATEK. In 2005 he was appointed Deputy Chairman of NOVATEK's Management Board and in 2007 he became a member of NOVATEK's Management Board. Candidate of legal Sciences. He was awarded the Order For Personal Courage, the Russian Federation's Order of the Badge of Honor and other state and departmental awards: Honorary Diplomas of the President of the Russian Federation, the Minister of Internal Affairs, the Governor of the Moscow Region. He also has the awards of the Russian Orthodox Church (Order of Holy Prince Daniel of Moscow, Order of Seraphim of Sarov and a medal of St. Sergius).

**MR. VIKTOR N. BELYAKOV**

Deputy Chairman of the Management Board for Economics and Finance

Born in 1973

Mr. Belyakov graduated from Tver State Technical University majoring in Automated Data Processing and Management Systems (1995) and in Information Systems in Economics (1997). In 2000, he completed an MBA degree program with Kingstone University (UK). A holder of CMA (Certified Management Accountant).

From 2004 till 2014 Mr. Belyakov worked for PAO Uralkali, where he successively held the positions of Head of Division, Deputy Chief Financial Officer, Chief Financial Officer, Vice President for Finance, Deputy General Director, Executive Director. In 2015 he was appointed Vice President for Economics and Finance of PAO Far East Shipping Company (FESCO group). In February 2016, Viktor Belyakov joined PAO NOVATEK in the position of Deputy Chairman of the Management Board for Economics and Finance.

**MR. MARK A. GYETVAY**

Deputy Chairman of NOVATEK's Management Board

Born in 1957

Mr. Gyetvay studied at Arizona State University (Bachelor of Science, Accounting, 1981) and later at Pace University, New York (Graduate Studies in Strategic Management, 1995). After graduation, Mr.

Gyetvay worked in various capacities at a number of U.S. independent oil and gas companies where he specialized in financial and economic analysis for both upstream and downstream segments of the petroleum industry.

In 1994, Mr. Gyetvay began his work at Coopers and Lybrand, as Director, Strategic Energy Advisory Services. He subsequently moved to Moscow in 1995 with Coopers & Lybrand to lead the oil and gas practice. He was admitted as a partner of PricewaterhouseCoopers Global Energy where he assumed the role of client service engagement partner, Utilities and Mining practice, based in Russia (Moscow office). Mr. Gyetvay was an engagement partner on various energy and mining clients providing overall project management, financial and operational expertise, maintaining and supporting client service relationships as well as serving as concurring partner on transaction services to the petroleum sector.

Mr. Gyetvay is a Certified Public Accountant (inactive status), a member of the American Institute of Certified Public Accountants and an associate member of the Society of Petroleum Engineers. He is a recognized expert in the oil and gas industry, a frequent speaker at various industry and investor conferences, has published numerous articles on various oil and gas industry topics and was a former member of PwC's Petroleum Thought Leadership team. He has been recognized by Investor Relations Magazine as one of the best CFO's in Russia and the CIS, and more recently by Institutional Investor magazine as one of the Top Five CFO's in Europe's Oil and Gas sector. Finance Monthly magazine named Mark Gyetvay the Best CFO in Russia for the years 2015, 2016 and 2017, and recently he received the Game Changer 2017 Award for Russia.

From 2003 to 2014, Mr. Gyetvay was a member of NOVATEK's Board of Directors and served on the Investment and Strategy Committee. From 2003 to 2014, he has been Chief Financial Officer and, in August 2007, Mr. Gyetvay was elected to NOVATEK's Management Board. In July 2010, he became Deputy Chairman of NOVATEK's Management Board.

**MR. SERGEY V. VASYUNIN**

Deputy Chairman of the Management Board – Operations Director

Born in 1967

In 1993, Sergey Vasyunin graduated from the Ufa Oil Institute, specializing in the Development and Oper-



ation of Oil and Gas Fields. Between 1993 and 1997, Mr. Vasyunin was employed with Condor as deputy director, Stroykomplekt as head of sales department, and with OAO Spetsnefteenergomontazhavtomatika – as marketing engineer. From 1998, he worked in the Urengoygazprom industrial association of OAO Gazprom where he served in the capacity of an oil, gas and condensate production foreman. Between 2002 and 2017, Mr. Vasyunin was employed in the positions of gas condensate production shop manager, deputy general director for operations, and first deputy general director – chief engineer of OOO NOVATEK-YURKHAROVNEFTEGAS. In April 2017, he was appointed Deputy Chairman of the Management Board – Director for Operations of NOVATEK.

In 2005, the Russian Ministry of Industry and Energy issued a commendation to Sergey Vasyunin. He holds the Honored Employee of NOVATEK title.

#### **MS. TATYANA S. KUZNETSOVA**

Deputy Chairman of NOVATEK's Management Board  
 Director of NOVATEK's Legal Department  
 Born in 1960

Ms. Kuznetsova graduated from the Far East State University with a degree in Law. From 1986, she was Senior Legal Advisor for a legal bureau. In 1993, Ms. Kuznetsova became Deputy General Director for Legal Issues and from 1996, Marketing Director for OAO Purneftegasgeologiya. In 1998, she was appointed Deputy General Director of OAO Nordpipes. Since 2002, she has been Director of the Legal Department for NOVATEK. Since 2005, she has been the Deputy Chairman of NOVATEK's Management Board – Director of NOVATEK's Legal Department and in August 2007, she became a member of NOVATEK's Management Board. Ms. Kuznetsova has the title "Honored employee of PAO NOVATEK", and is awarded the Order of Merit for the Fatherland 2 degree.

#### **MR. IGOR A. PLESOVSKIKH**

Deputy Chairman of the Management Board – Director for Geology  
 Born in 1970

In 1993, Mr. Plesovskikh graduated from Tyumen Industrial Institute specialising in Oil and Gas Geology.

He has over 20 years of experience in the oil and gas industry. He started his career as Assistant Driller at Noyabrskneftegaz, subsequently holding the

positions of General Director at Urengoyneftegazgeologia, General Director at YARGEO, Deputy General Director – Chief Geologist at NOVATEK-TARKO-SALENEFTEGAZ, Deputy General Manager of the Federal Agency for Subsoil Use Rosnedra and Deputy General Director – Chief Geologist at ITERA Oil & Gas Company.

In December 2015, he joined PAO NOVATEK in the capacity of Deputy Chairman of the Management Board – Director for Geology.

Igor Plesovskikh has been awarded the Certificate of Merit of the Ministry of Natural Resources and Environment of the Russian Federation.

#### **MR. ILYA V. TAFINTSEV**

Member of the Management Board –  
 Director for Strategic Projects  
 Born in 1985

In 2006 Mr. Tafintsev obtained a BA in Economics from the Higher School of Economics in Moscow. In 2007 graduated from University of London, where he majored in Investment and Finance. From 2007 to 2011 Mr. Tafintsev held the position of Deputy Head of PAO NOVATEK's Representative Office in London. In 2011–2014, he was a Finance & Investment Advisor with United Bureau of Consultants Limited.

Since 2013 he has served as a Strategic Projects Director of PAO NOVATEK, a member of the Board of Directors at SIBUR Holding. From 2014 to 2016 he was Chairman of the Board of Directors of OAO Yamal LNG. In December 2015, Mr. Tafintsev was appointed Member of the Management Board – Director for Strategic Projects of PAO NOVATEK.

#### **MR. LEV V. FEODOSYEV**

Deputy Chairman of NOVATEK's Management Board –  
 Commercial Director  
 Born in 1979

In 2002, Mr. Feodosyev graduated from the Bauman Moscow State Technical University with a degree in Machinery and Foundry Engineering Technologies. In 2002, Mr. Feodosyev was appointed lead specialist at the Ministry of Energy of the Russian Federation. From 2003, he has served as lead specialist, senior specialist, adviser, deputy head of section, Deputy Director of Department at the Ministry of Economic Development and Trade of the Russian Federation.

From October 2007, Mr. Feodosyev worked in NOVATEK as Director of the Strategic Planning and Development Department. From 2011, he was appointed as Deputy Commercial Director, Director of the Marketing and Gas Sales Department of NOVATEK. Since February 2015, he has been appointed Commercial Director, Deputy Chairman of the Management Board of NOVATEK.

In 2014, Mr. Feodosyev was awarded NOVATEK's Honorary Certificate.

### **MR. ALEXANDER M. FRIDMAN**

First Deputy Chairman of NOVATEK's Management Board

Born in 1951

In 1973, Mr. Fridman graduated from the Gubkin Institute of Oil and Gas in Moscow, with a degree in Oil and Gas Fields Development and Exploitation. Since 1973, he was employed by various Gazprom companies: as Chief Engineer of Nadymgazprom, Head of the Production and Technical Department of the Industrial Association, and Chief Engineer of Mostransgaz's Kaluga Department for Gas Transportation and Underground Storage. From 1992 to 2003, he was Technical Director, First Deputy General Director of a joint venture established by PAO Gazprom and DKG-EAST (Hungary). Since 2003 Mr. Fridman was the Deputy General Director of Novafininvest. In 2004, Mr. Fridman was elected Deputy Chairman of the Management Board of PAO NOVATEK. In August 2007, he was appointed a member of NOVATEK's Management Board. From February 2015 First Deputy Chairman of the Management Board of PAO NOVATEK. Mr. Fridman is the recipient of the title of honor "Honored man of the oil and gas industry".

### **MR. DENIS G. KHRAMOV**

Deputy Chairman of the Management Board

Born in 1975

Graduated in 1997 from the Urals State Law Academy with a degree in Law. In 1999 completed a master's course in Private Law with the Russian School of Private Law. In 2004, he obtained his candidate degree in Law.

From 1995 he was an in-house counsel at Transneftgaz CJSC. In 1997, he joined the Legal Center for Northern Territories as a lawyer and was subsequently appointed Chief Specialist and Deputy Head

of Department with the Russian Ministry of Fuel and Energy in 1999.

In 2001, he was appointed Deputy Head of Department and Head of Department with the Russian Ministry of Economic Development and Trade.

In 2002, he joined Zarubezhneft JSC as Deputy Head of Division with the responsibility of supervising subsoil use, economic and financial affairs. In 2007 he became Senior Lawyer at LeBoeuf, Lamb, Greene & MacRae LLP.

From 2008 he held a number of positions with the Ministry of Natural Resources and Environment of the Russian Federation, including Chief Officer for State Policy and Regulation in Geology and Subsoil Use and Deputy Minister of Natural Resources and Environment of the Russian Federation, and was appointed First Deputy Minister of Natural Resources and Environment of the Russian Federation in 2014. During his service with the Russian Ministry of Natural Resources and Environment, he was in charge of economic and financial affairs, geology and subsoil use.

His outstanding service was recognized with awards at different levels.

In December 2015, he was appointed Deputy Chairman of the Management Board at PAO NOVATEK.

### **REPORT ON MAJOR, AND INTERESTED-PARTY TRANSACTIONS THAT THE COMPANY DID IN THE REPORTING YEAR**

Information in this section of the Annual report 2017 is not provided pursuant to the Order of the Government of the Russian Federation No. 10 dated 15 January 2018.

### **CORPORATE GOVERNANCE CODE COMPLIANCE REPORT**

This Corporate Governance Code Compliance Report (hereinafter "the Report") was reviewed at the meeting of PAO NOVATEK's Board of Directors on [13 March 2018 (Minutes No. 204)].

The Board of Directors certifies that data in this Report contain full and reliable information on compliance by the Company with the principles and recommendations of the Corporate Governance Code for 2016.

When assessing our compliance with corporate governance principles as set out in the Code we were

guided by the Guidelines for Reporting on Compliance with the Corporate Governance Code recommended by the Bank of Russia in its Letter No. IN-06-52/8 dated 17 February 2016.

An overview of the most relevant aspects of the corporate governance model and practices in the Company is presented in the Corporate Governance section of this Annual Report.

№	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
<b>1.1</b>	<b>THE COMPANY SHOULD ENSURE EQUITABLE AND FAIR TREATMENT OF EVERY SHAREHOLDER EXERCISING THEIR RIGHT TO TAKE PART IN MANAGING THE COMPANY.</b>			
1.1.1	The Company ensures the most favorable conditions for its shareholders to participate in the general meeting, develop an informed position on agenda items of the general meeting, coordinate their actions, and voice their opinions on items considered.	1. The Company's internal document approved by the general meeting of shareholders and governing the procedures for holding the general meeting is publicly available.  2. The Company provides accessible means of communication via hotline, e-mail or an online forum for shareholders to voice their opinions and submit questions on the agenda in preparing for the general meeting. The Company performed the above actions in advance of each general meeting held in the reporting period.	This principle is complied with.	–
1.1.2	The procedure for giving notice of, and providing relevant materials for, the general meeting enables shareholders to properly prepare for attending the general meeting.	1. The notice of an upcoming general meeting of shareholders is posted (published) online at least 30 days prior to the date of the general meeting.  2. The notice of an upcoming meeting specifies the meeting venue and documents required for admission.  3. Shareholders were given access to the information on who proposed the agenda items and who proposed nominees to the company's board of directors and the revision commission.	This principle is complied with.	–
1.1.3	In preparing for, and holding of, the general meeting, shareholders were able to receive clear and timely information on the meeting and related materials, put questions to the company's executive bodies and the board of directors, and to communicate with each other.	1. In the reporting period, shareholders were able to put questions to members of executive bodies and members of the board of directors before and during the annual general meeting.	This principle is complied with.	–

	<p>2. The position of the board of directors (including dissenting opinions entered into the minutes) on each agenda item of general meetings held in the reporting period was included in the materials to the general meeting of shareholders.</p>	<p>This principle is not fully complied with.</p>	<p>When convening General Meetings of Shareholders, the board of directors reviews all agenda items of the relevant meeting and presents them to the Meeting for consideration or provides necessary advice.</p> <p>Materials to the General Meeting of Shareholders include recommendations of the board of directors as required by law.</p> <p>In accordance with paragraph 1 of Art. 54 of the Russian Federal Law "On Joint Stock Companies", the list of information (materials) provided to shareholders in preparation for the General Meeting of Shareholders is determined by the Board of Directors. Accordingly, the Board of Directors, if it deems it necessary, to include its position on the issues on the agenda of the general meeting of shareholders, if it deems it necessary.</p> <p>The Company considers the established procedure to be balanced, not bearing any risks for the Company and its shareholders, and does not plan to change the existing approach.</p>
	<p>3. The Company gave duly authorized shareholders access to the list of persons entitled to attend the General Meeting, as from the date of its receipt by the Company, for all general meetings held in the reporting period.</p>	<p>This principle is complied with.</p>	<p>—</p>
<p>1.1.4 There were no unjustified difficulties preventing shareholders from exercising their right to request that a General Meeting be convened, to propose nominees to the Company's governing bodies, and to make proposals for the agenda of the General Meeting.</p>	<p>1. In the reporting period, shareholders were able to submit, within at least 60 days after the end of the relevant calendar year, proposals for the agenda of the Annual General Meeting.</p> <p>2. In the reporting period, the Company did not reject any proposals for the agenda or nominees to the company's governing bodies due to misprints or other insignificant flaws in the shareholder's proposal.</p>	<p>This principle is complied with.</p>	<p>—</p>

1.1.5	Each shareholder was able to freely exercise their voting right in the simplest and most convenient way.	1. An internal document (internal policy) of the Company provides that each participant of the General Meeting may request a copy of the ballot filled out by them and certified by the counting commission before the end of the relevant meeting.	This principle is complied with.	–
1.1.6	The procedure for holding a General Meeting set by the Company provides equal opportunities for all persons attending the Meeting to voice their opinions and ask questions.	1. General Meetings of Shareholders held in the reporting period in the form of a meeting (i.e. joint presence of shareholders) provided for sufficient time for making reports on and for discussing agenda items.	This principle is complied with.	–
		2. Nominees to the Company's governing and control bodies were available to answer questions of shareholders at the Meeting at which their nominations were put to vote.	This principle is complied with.	–
		3. When passing resolutions on preparing and holding General Meetings of Shareholders, the board of directors considered using telecommunication means for remote access of shareholders to General Meetings in the reporting period	This principle is complied with.	–
<b>1.2 SHAREHOLDERS ARE GIVEN EQUAL AND FAIR OPPORTUNITIES TO SHARE PROFITS OF THE COMPANY IN THE FORM OF DIVIDENDS.</b>				
1.2.1	The Company has designed and put in place a transparent and clear mechanism to determine the dividend amount and payout procedure.	1. The Company has drafted and disclosed a dividend policy approved by the board of directors.  2. If the Company's dividend policy uses reporting figures to determine the dividend amount, then relevant provisions of the dividend policy take into account the consolidated financial statements.	This principle is complied with.	–
1.2.2	The Company does not resolve to pay out dividends if such payout, while formally compliant with law, is economically unjustified and may lead to a false representation of the Company's performance.	1. The Company's dividend policy clearly identifies financial / economic circumstances under which the Company shall not pay out dividends.	This principle is complied with.	–
1.2.3	The Company does not allow for dividend rights of its existing shareholders to be impaired.	1. In the reporting period, the Company did not take any actions that would lead to the impairment of the dividend rights of its existing shareholders.	This principle is complied with.	–

1.2.4	The Company makes every effort to prevent its shareholders from using other means to profit (gain) from the Company other than dividends and liquidation value.	1. To prevent shareholders from using other means to profit (gain) from the Company other than dividends and liquidation value, the Company's internal documents provide for controls to timely identify and approve deals with affiliates (associates) of the Company's substantial shareholders (persons entitled to use votes attached to voting shares) where the law does not formally recognize such deals as related-party transactions.	This principle is not complied with.	This principle is not complied with as the Company believes that statutory controls are sufficient for relevant purposes. The Company does not transact with persons under control by substantial shareholders, which prevents substantial shareholders from profiting (gaining) from the Company.  The Company does not see any risks in the established practice, as the system of procurement procedures introduced in the Company ensures the conclusion of contracts on market terms.
<b>1.3 CORPORATE GOVERNANCE FRAMEWORK AND PRACTICES SHOULD ENSURE EQUALITY FOR THE SHAREHOLDERS OWNING THE SAME TYPE (CLASS) OF SHARES, INCLUDING MINORITY AND NON-RESIDENT SHAREHOLDERS, AND THEIR EQUITABLE TREATMENT BY THE COMPANY.</b>				
1.3.1	The Company has created conditions for fair treatment of each shareholder by the Company's governing and control bodies, including conditions that rule out abuse by major shareholders against minority shareholders.	1. In the reporting period, procedures for management of potential conflicts of interest among substantial shareholders were efficient, while the board of directors paid due attention to conflicts, if any, between shareholders.	This principle is – complied with.	
1.3.2	The Company does not take any actions that lead or may lead to artificial redistribution of corporate control.	1. No quasi-treasury shares were issued or used to vote in the reporting period.	This principle is – complied with.	
<b>1.4 SHAREHOLDERS ARE PROVIDED WITH RELIABLE AND EFFICIENT MEANS OF RECORDING THEIR RIGHTS TO SHARES AND ARE ABLE TO FREELY DISPOSE OF THEIR SHARES WITHOUT ANY HINDRANCE.</b>				
1.4.1	Shareholders are provided with reliable and efficient means of recording their rights to shares and are able to freely dispose of their shares without any hindrance.	1. The Company's registrar maintains the share register in an efficient and reliable way that meets the needs of the Company and its shareholders.	This principle is – complied with.	
<b>2.1 THE BOARD OF DIRECTORS PROVIDES STRATEGIC MANAGEMENT OF THE COMPANY, DETERMINES KEY PRINCIPLES OF, AND APPROACHES TO, SETTING UP A CORPORATE RISK MANAGEMENT AND INTERNAL CONTROL FRAMEWORK, MONITORS PERFORMANCE BY THE COMPANY'S EXECUTIVE BODIES, AND PERFORMS OTHER KEY FUNCTIONS.</b>				
2.1.1	The board of directors is responsible for appointing and dismissing execu-	1. The board of directors has the authority stipulated in the Articles of Association to appoint and	This principle is not fully complied with	The issue of determining the amount of remuneration paid to the Chairman of the Man

	<p>remove members of executive bodies and to set out the terms and conditions of their contracts.</p>	<p>agement Board based on the results of the work for the year, falls within the authority of the Board of Directors.</p> <p>In accordance with the Company's Articles of Association, the members of the Management Board are elected by the Board of Directors from among the Company's employees, solely on the recommendation of the Chairman of the Management Board. The amounts of official salaries and other terms of employment contracts with the Company's employees, including members of the Management Board, are determined by the Chairman of the Management Board taking into account the parameters of the Company's business plan approved by the Board of Directors.</p> <p>The Company considers the established procedure to be effective, balanced, not bearing any risks for the Company and its shareholders, and does not plan to change the existing approach.</p>
	<p>2. The board of directors reviewed the report(s) by the sole executive body or members of the collective executive body on the implementation of the company's strategy</p>	<p>This principle is complied with. —</p>
<p>2.1.2 The board of directors sets key long-term targets for the company, assesses and approves its key performance indicators and key business goals, as well as the strategy and business plans for the company's core lines of business.</p>	<p>At its meetings in the reporting period, the board of directors reviewed strategy implementation and updates, approval of the company's financial and business plan (budget), and criteria and performance (including interim) of the company's strategy and business plans.</p>	<p>This principle is complied with. —</p>
<p>2.1.3 The Board of Directors defines the Company's risk management and internal control principles and approaches.</p>	<p>1. The Board of Directors defined the Company's risk management and internal control principles and approaches.</p>	<p>This principle is complied with. —</p>

		2. The Board of Directors assessed the company's risk management and internal control system in the reporting period.		
2.1.4	The board of directors determines the company's remuneration and reimbursement (compensation) policy for its directors, members of executive bodies and other key executives.	<p>1. The company developed and put in place a remuneration and reimbursement (compensation) policy (policies), approved by the board of directors, for its directors, members of executive bodies and other key executives.</p> <p>2. At its meetings in the reporting period, the Board of Directors discussed matters related to such policy (policies).</p>	This principle is not fully complied with.	<p>The costs of the Management Board members and other key executives of the Company shall be reimbursed (compensated) under the applicable legislation.</p> <p>Remuneration of members of the Management Board and other key employees of the Company shall be effected upon the decision of the Chairman of the Management Board within the amount determined with consideration of the parameters of the Company's business plan approved by the Board of Directors.</p> <p>The Board of Directors also determines the remuneration of the Chairman of the Management Board based on the performance of the Company in the reporting year.</p> <p>The Company considers the established procedure to be balanced, not bearing any risks for the Company and its shareholders, and does not plan to change the existing approach.</p>
2.1.5	The board of directors plays a key role in preventing, identifying and resolving internal conflicts between the company's bodies, shareholders and employees.	<p>1. The board of directors plays a key role in preventing, identifying and resolving internal conflicts.</p> <p>2. The company set up mechanisms to identify transactions leading to a conflict of interest and to resolve such conflicts.</p>	This principle is complied with.	–
2.1.6	The board of directors plays a key role in ensuring that the company is transparent, timely and fully discloses its information, and provides its shareholders with unhindered access to the company's documents.	<p>1. The board of directors approved the company's information policy regulations.</p> <p>2. The company identified persons responsible for implementing the information policy.</p>	This principle is complied with.	–



2.1.7 The board of directors controls the company's corporate governance practices and plays a key role in material corporate events of the company.	1. In the reporting period, the board of directors reviewed the company's corporate governance practices.	This principle is – complied with.
<b>2.2 THE BOARD OF DIRECTORS IS ACCOUNTABLE TO THE COMPANY'S SHAREHOLDERS.</b>		
2.2.1 Performance of the board of directors is disclosed and made available to the shareholders.	1. The company's annual report for the reporting period includes the information on individual attendance at board of directors and committee meetings.  2. The annual report discloses key performance assessment results of the board of directors in the reporting period.	This principle is – complied with.
2.2.2 The chairman of the board of directors is available to communicate with the company's shareholders.	1. The company has in place a transparent procedure enabling shareholders to forward questions and express their position on such questions to the chairman of the board of directors.	This principle is – complied with.
<b>2.3 THE BOARD OF DIRECTORS MANAGES THE COMPANY IN AN EFFICIENT AND COMPETENT MANNER AND MAKE FAIR AND INDEPENDENT JUDGMENTS AND DECISIONS IN LINE WITH THE BEST INTERESTS OF THE COMPANY AND ITS SHAREHOLDERS.</b>		
2.3.1 Only persons of impeccable business and personal reputation who have knowledge, expertise and experience required to make decisions within the authority of the board of directors and essential to perform its functions in an efficient way are elected to the board of directors.	1. The procedure for assessing the board of directors' performance established in the company includes, inter alia, assessment of professional qualifications of the board members.  2. In the reporting period, the board of directors (or its nomination committee) assessed nominees to the board of directors for required experience, knowledge, business reputation, absence of conflicts of interest, etc.	This principle is – complied with.
2.3.2 The company's directors are elected via a transparent procedure that enables shareholders to obtain information on nominees sufficient to judge on their personal and professional qualities.	1. Whenever the agenda of the general meeting of shareholders included election of the board of directors, the company provided to shareholders the biographical details of all nominees to the board of directors, the results of their assessment carried out by the board of directors (or its nomination committee), and the information on whether the nominee meets.	This principle is – complied with.

		the independence criteria set forth in Recommendations 102–107 of the Code, as well as the nominees' written consent to be elected to the board of directors.	
2.3.3	The board of directors has a balanced membership, including in terms of directors' qualifications, experience, expertise and business qualities, and enjoys its shareholders' trust.	1. As part of assessment of the board of directors' performance run in the reporting period, the board of directors reviewed its requirements to professional qualifications, experience and business skills.	This principle is complied with. —
2.3.4	The company has a sufficient number of directors to organize the board of directors' activities in the most efficient way, including ability to set up committees of the board of directors and enable the company's substantial minority shareholders to elect a nominee to the board of directors for whom they vote.	1. As part of assessment of the board of directors' performance run in the reporting period, the board of directors considered whether the number of directors met the company's needs and shareholders' interests.	This principle is complied with.
<b>2.4 THE BOARD OF DIRECTORS INCLUDES A SUFFICIENT NUMBER OF INDEPENDENT DIRECTORS.</b>			
2.4.1	An independent director is a person who is sufficiently professional, experienced and independent to develop their own position, and capable of making unbiased judgements in good faith, free of influence by the company's executive bodies, individual groups of shareholders or other stakeholders. It should be noted that a nominee (elected director) who is related to the company, its substantial shareholder, substantial counterparty or competitor of the company, or related to the government, may not be considered as independent under normal circumstances.	1. In the reporting period, all independent directors met all independence criteria set out in Recommendations 102–107 of the Code or were deemed independent by the board of directors.	This principle is complied with. —
2.4.2	The company assesses compliance of nominees to the board of directors and reviews compliance	1. In the reporting period, the board of directors (or its nomination committee) made a judgement on independence of each nominee to the board of	This principle is complied with. —

	<p>of independent directors with independence criteria on a regular basis. In such assessment, substance should prevail over form.</p>	<p>of directors and provided its opinion to shareholders.</p> <p>2. In the reporting period, the board of directors (or its nomination committee) reviewed, at least once, the independence of incumbent directors listed by the company as independent directors in its annual report.</p> <p>3. The company has in place procedures defining the actions to be taken by a member of the board of directors if they cease to be independent, including the obligation to timely notify the board of directors thereof.</p>		
2.4.3	<p>Independent directors make up at least one third of the elected board members.</p>	<p>1. Independent directors make up at least one third of the board members.</p>	<p>This principle is complied with.</p>	<p>–</p>
2.4.4	<p>Independent directors play a key role in preventing internal conflicts in the company and in ensuring that the company performs material corporate actions.</p>	<p>1. Independent directors (with no conflicts of interest) run a preliminary assessment of material corporate actions implying a potential conflict of interests and submit the results to the board of directors.</p>	<p>This principle is not fully complied with.</p>	<p>In accordance with the Company's Articles of Association, the Regulations on the Board of Directors and the Regulations on the Committees of the Board of Directors, a large block of issues related to significant corporate actions is preliminarily considered by the Audit Committee and the Remuneration Committee consisting of independent directors. In addition, most of such decisions shall be approved by the Board of Directors, if 8 out of 9 directors voted for the corresponding decision. Thus, any two independent directors may block the adoption of an undesirable decision in their opinion.</p> <p>The Company believes that independent directors have sufficient capacity to assess significant corporate actions.</p>
<p><b>2.5 THE CHAIRPERSON OF THE BOARD ENSURES THAT THE BOARD OF DIRECTORS DISCHARGES ITS DUTIES IN THE MOST EFFECTIVE AND EFFICIENT WAY.</b></p>				
2.5.1	<p>The board of directors is chaired by an independent director, or a senior independent director supervising the activities of other independent directors and</p>	<p>1. The board of directors is chaired by an independent director, or a senior independent director is appointed from among the independent directors.</p>	<p>This principle is not fully complied with.</p>	<p>The role of independent directors on the Company's Board of Directors is very important, since the Audit Committee and the Remuneration and Nomination Committee of the Board</p>

	interacting with the chairman of the board of directors is chosen from among the elected independent directors.	2. The role, rights and duties of the chairman of the board of directors (and, if applicable, of the senior independent director) are duly set out in the company's internal documents.		of Directors are comprised of independent directors only. Formally, the Chairman of the Board of Directors is not an Independent Director. However, the Chairman of the Board of Directors meets all independence criteria, except for his tenure on the Board of Directors. For chairmanship purposes, the directors elected the most experienced of the Board members who is not an independent director.  The Company considers the established procedure to be balanced and does not plan to change the existing approach.
2.5.2	The chairman of the board of directors maintains a constructive environment at meetings, enables free discussion of agenda items, and supervises the execution of resolutions passed by the board of directors.	1. Performance of the chairman of the board of directors was assessed as part of assessment of the board of directors' performance in the reporting period.	This principle is complied with.	–
2.5.3	The chairman of the board of directors takes all steps necessary for the timely provision to members of the board of directors of information required to pass resolutions on agenda items.	1. The company's internal documents set out the duty of the chairman of the board of directors to take all steps necessary for the timely provision to members of the board of directors with materials on agenda items of the board meeting.	This principle is complied with.	–
<b>2.6 DIRECTORS ACT REASONABLY AND IN GOOD FAITH IN THE BEST INTERESTS OF THE COMPANY AND ITS SHAREHOLDERS, ON A FULLY INFORMED BASIS AND WITH DUE CARE AND DILIGENCE.</b>				
2.6.1	Directors pass resolutions on a fully informed basis, with no conflict of interest, subject to equal treatment of the company's shareholders, and assuming normal business risks.	1. The company's internal documents provide that a director should notify the board of directors of any existing conflict of interest as to any agenda item of the meeting of the board of directors or its committee, prior to discussion of the relevant agenda item.  2. The company's internal documents provide that a director should abstain from voting on any item in connection with which they have a conflict of interest.	This principle is complied with.	–

		3. The company has in place a procedure enabling the board of directors to get professional advice on matters within its remit at the expense of the company.	
2.6.2	The rights and duties of directors are clearly stated and incorporated in the company's internal documents.	1. The company adopted and published an internal document that clearly defines the rights and duties of directors.	This principle is complied with. –
2.6.3	Directors have sufficient time to perform their duties.	1. Individual attendance at board and committee meetings, as well as time devoted to preparation for attending meetings, was recorded as part of the procedure for assessing the board of directors in the reporting period.  2. Under the company's internal documents, directors notify the board of directors of their intentions to be elected to governing bodies in other entities (apart from the entities controlled by, or affiliated to, the company), and of their election to such bodies.	This principle is complied with. –
2.6.4	All directors shall have equal access to the company's documents and information. Newly elected directors are furnished with sufficient information about the company and performance of the board of directors as soon as possible.	1. Under the company's internal documents, directors are entitled to access documents and make requests on the company and its controlled entities, while executive bodies of the company should furnish all relevant information and documents.  2. The Company has in place a formalized onboarding program for newly elected Directors.	This principle is complied with. –
<b>2.7 MEETINGS OF THE BOARD OF DIRECTORS, PREPARATION FOR SUCH MEETINGS AND PARTICIPATION OF BOARD MEMBERS THEREIN ENSURE EFFICIENT PERFORMANCE BY THE BOARD OF DIRECTORS.</b>			
2.7.1	Board meetings are held as needed, taking into account the scale of operations and goals of the company at a particular time.	1. The board of directors held at least six meetings in the reporting year.	This principle is complied with. –
2.7.2	The company's internal regulations stipulate the procedure to prepare for and hold the board's meetings, enabling the directors to make proper preparations for them.	1. The company has an approved internal document that describes the procedure for arranging and holding meetings of the board of directors and sets out, in particular, that the notice of the meeting shall be given, as a rule, at least five days prior to such meeting.	This principle is complied with. –

2.7.3 The format of the meeting of the board of directors is determined taking into account the importance of items on the agenda. The most important matters are dealt with at meetings of the board of directors held in person.	1. The company's charter or internal document provides for the most important matters (as per the list set out in Recommendation 168 of the Code) to be passed at in-person meetings of the board of directors.	This principle is complied with.	–
2.7.4 Resolutions on most important matters relating to the company's operations are passed at a meeting of the board of directors by a qualified majority or by a majority of all elected board members.	1. The company's charter provides for the most important matters set out in Recommendation 170 of the Code to be passed at a meeting of the board of directors by a qualified majority of at least three quarters or by a majority of all elected board members.	This principle is not fully complied with.	<p>The Company's Articles of association do not provide for resolutions of the Board to be passed by qualified majority on the following matters:</p> <ul style="list-style-type: none"> <li>• submission to the General Meeting of matters relating to the Company's liquidation</li> <li>• submission to the General Meeting of matters relating to amendments to the Company's Articles of association</li> <li>• review of material issues relating to operations of legal entities controlled by the Company.</li> </ul> <p>The Company deems sufficient the existing norm stipulated in the legislation and the Articles of Association according to which decisions on amendments and additions in the Company's Articles of Association, including approval of the latter in a new wording, as well as on Company's liquidation, appointment of a winding up commission and approval of the interim and final liquidation balance shall be made by the general shareholders meeting by the three-fourths majority of the votes of shareholders holding the voting shares and taking part in the general shareholders meeting.</p> <p>The Company considers the established procedure to be balanced, not bearing any risks, and does not plan to change the existing approach.</p>

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## 2.8 THE BOARD OF DIRECTORS SETS UP COMMITTEES FOR PRELIMINARY CONSIDERATION OF THE MOST IMPORTANT ISSUES RELATED TO THE BUSINESS OF THE COMPANY.

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2.8.1 To preview matters related to controlling the company's financial and business activities, it is recommended to set up an audit committee comprised of independent directors.	<ol style="list-style-type: none"> <li>1. The board of directors has set up an audit committee comprised solely of independent directors.</li> <li>2. The company's internal documents set out the tasks of the audit committee, including those listed in Recommendation 172 of the Code.</li> <li>3. At least one member of the audit committee represented by an independent director has experience and knowledge of preparing, analyzing, assessing and auditing accounting (financial) statements.</li> <li>4. Meetings of the audit committee were held at least once a quarter during the reporting period.</li> </ol>	This principle is — complied with.
2.8.2 To preview matters related to adopting an efficient and transparent remuneration scheme, a remuneration committee is set up, comprised of independent directors and headed by an independent director who is not the chairman of the board of directors.	<ol style="list-style-type: none"> <li>1. The board of directors has set up a remuneration committee comprised solely of independent directors.</li> <li>2. The remuneration committee is headed by an independent director who is not the chairman of the board of directors.</li> <li>3. The company's internal documents set out the tasks of the remuneration committee, including those listed in Recommendation 180 of the Code.</li> </ol>	This principle is — complied with.
2.8.3 To preview matters related to talent management (succession planning), professional composition and efficiency of the board of directors, a nomination (HR) committee is set up, predominantly comprised of independent directors.	<ol style="list-style-type: none"> <li>1. The board of directors has set up a nomination committee (its tasks listed in Recommendation 186 of the Code are fulfilled by another committee, the Remuneration and Nomination Committee) predominantly comprised of independent directors.</li> <li>2. The company's internal documents set out the tasks of the nomination committee (or the tasks of the committee with combined functions), including those listed in Recommendation 186 of the Code.</li> </ol>	This principle is — complied with.

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2.8.4 Taking into account the company's scope of business and level of risks, the company's board of directors made sure that the composition of its committees is fully in line with company's business goals. Additional committees were either set up or not deemed necessary (strategy committee, corporate governance committee, ethics committee, risk management committee, budget committee, health, safety and environment committee, etc.).	1. In the reporting period, the board of directors considered whether the composition of its committees was in line with the board's tasks and the company's business goals. Additional committees were either set up or not deemed necessary.	This principle is complied with.	–
2.8.5 Committees are composed so as to enable comprehensive discussions of matters under preview, taking into account the diversity of opinions.	1. Committees of the board of directors are headed by independent directors.  2. The company's internal documents (policies) include provisions stipulating that persons who are not members of the audit committee, the nomination committee and the remuneration committee may attend committee meetings only by invitation of the chairman of the respective committee.	This principle is not fully complied with.	The Board of directors' audit committee and remuneration and nomination committee are not only headed by but also fully consist of independent directors.  Formally, the director heading an additional committee, the Strategy Committee, is not an independent director. However, he meets all independence criteria, except for his tenure on the Board of Directors.  The Company does not see any risks in this.
2.8.6 Committee chairmen inform the board of directors and its chairman on the work of their committees on a regular basis.	1. During the reporting period, committee chairmen reported to the board of directors on the work of committees on a regular basis.	This principle is complied with.	–
<b>2.9 THE BOARD OF DIRECTORS ENSURES PERFORMANCE ASSESSMENT OF THE BOARD OF DIRECTORS, ITS COMMITTEES AND MEMBERS OF THE BOARD OF DIRECTORS.</b>			
2.9.1 The board of directors' performance assessment is aimed at determining the efficiency of the board of directors, its committees and members, consistency of their work with the company's development requirements, as well as bolstering the work of the board of directors and	1. Self-assessment or external assessment of the board of directors' performance carried out in the reporting period included performance assessment of the committees, individual members of the board of directors and the board of directors in general.	This principle is complied with.	–



	identifying areas for improvement.	2. Results of self-assessment or external assessment of the board of directors' performance carried out in the reporting period were reviewed at the in-person meeting of the board.		
2.9.2	Performance of the board of directors, its committees and directors is assessed on a regular basis at least once a year. An external organization (advisor) is engaged at least once in three years to conduct an independent assessment of the board of directors' performance.	1. The company engaged an external advisor to conduct an independent assessment of the board of directors' performance at least once over the last three reporting periods.	This principle is not complied with.	Over the past three reporting periods the Company has not engaged an external entity (advisor) to conduct an independent assessment of the Board of Director's performance. The Company did not run any self-assessment of the Board of Directors' performance in the reporting period.
<b>3.1</b>	<b>THE COMPANY'S CORPORATE SECRETARY ENSURES EFFICIENT ONGOING INTERACTION WITH SHAREHOLDERS, COORDINATES THE COMPANY'S EFFORTS TO PROTECT SHAREHOLDER RIGHTS AND INTERESTS AND SUPPORTS THE ACTIVITIES OF THE BOARD OF DIRECTORS.</b>			
3.1.1	The corporate secretary has the knowledge, experience and qualifications sufficient to perform his/her duties, as well as an impeccable reputation and the trust of shareholders.	1. The company has adopted and published an internal document – regulations on the corporate secretary.  2. The biographical data of the corporate secretary are published on the corporate website and in the company's annual report with the same level of detail as for members of the board of directors and the company's executives.	This principle is – complied with.	
3.1.2	The corporate secretary is sufficiently independent of the company's executive bodies and has the powers and resources required to perform his/her tasks.	The board of directors approves the appointment, removal and additional remuneration of the corporate secretary.	This principle is – complied with.	
<b>4.1</b>	<b>REMUNERATION PAID BY THE COMPANY IS SUFFICIENT TO ATTRACT, MOTIVATE AND RETAIN PERSONS WHO HAVE COMPETENCIES AND QUALIFICATIONS REQUIRED BY THE COMPANY. DIRECTORS, EXECUTIVE BODY MEMBERS AND OTHER KEY MANAGERS ARE REMUNERATED AS PER THE COMPANY'S REMUNERATION POLICY.</b>			
4.1.1	The amount of remuneration paid by the company to members of the board of directors, executive bodies and other key executives creates sufficient incentives for them to work efficiently, while enabling the company to engage and retain	1. The company has in place an internal document (internal documents) – the policy (policies) on remuneration of members of the board of directors, executive bodies and other key executives, which clearly defines (define) the approaches to remuneration of the above persons.	This principle is not fully complied with.	Relevant comments are provided in items 2.1.1. and 2.1.4 hereof.

	competent and qualified specialists. At the same time, the company avoids unnecessarily high remuneration, as well as unjustifiably large gaps between remunerations of the above persons and the company's employees.		
4.1.2	The company's remuneration policy is developed by the remuneration committee and approved by the board of directors. The board of directors, assisted by the remuneration committee, ensures control over the introduction and implementation of the company's remuneration policy, revising and amending it as required.	1. During the reporting period, the remuneration committee considered the remuneration policy (policies) and the practical aspects of its (their) introduction and presented relevant recommendation to the board of directors as required.	This principle is – complied with.
4.1.3	The company's remuneration policy includes transparent mechanisms for determining the amount of remuneration due to members of the board of directors, executive bodies and other key executives of the company, and regulates all types of expenses, benefits and privileges provided to such persons.	1. The company's remuneration policy (policies) includes (include) transparent mechanisms for determining the amount of remuneration due to members of the board of directors, executive bodies and other key executives of the company, and regulates (regulate) all types of expenses, benefits and privileges provided to such persons.	This principle is – not fully com- plied with. Relevant comments are provid- ed in items 2.1.1. and 2.1.4 hereof.
4.1.4	The company defines a policy on reimbursement (compensation) of costs detailing a list of reimbursable expenses and specifying service levels that members of the board of directors, executive bodies and other key executives of the company can claim. Such policy can make part of the company's remuneration policy.	1. The remuneration policy (policies) defines (define) the rules for reimbursement of costs incurred by members of the board of directors, executive bodies and other key executives of the company.	This principle is – complied with.
<b>4.2 DIRECTORS' REMUNERATION ENSURES THAT THEIR FINANCIAL INTERESTS ARE ALIGNED WITH LONG-TERM FINANCIAL INTERESTS OF SHAREHOLDERS.</b>			
4.2.1	The company pays fixed annual remuneration to members of the board of directors.	1. Fixed annual remuneration was the only form of monetary remuneration payable to members of the board of directors for their service	This principle is – complied with.

<p>The company does not pay remuneration for attending particular meetings of the board of directors or its committees.</p> <p>The company does not apply any form of short-term motivation or additional financial incentive for members of the board of directors.</p>	<p>on the board of directors during the reporting period.</p>		
<p>4.2.2 Long-term ownership of the company's shares helps align the financial interests of members of the board of directors with long-term interests of shareholders to the utmost. At the same time, the company does not link the right to dispose of shares to performance targets, and members of the board of directors do not participate in stock option plans.</p>	<p>1. If the company's internal document(s) – the remuneration policy (policies) stipulates (stipulate) provision of the company's shares to members of the board of directors, clear rules for share ownership by board members are defined and disclosed, aimed at stimulating long-term ownership of such shares.</p>	<p>Not applicable, since the Regulations on Remuneration and Compensations Payable to Members of PAO NOVATEK board of directors does not provide for remuneration of the directors with company shares.</p>	<p>–</p>
<p>4.2.3 The company does not provide for any extra payments or compensations in the event of early termination of office of members of the board of directors resulting from the change of control or any other reasons whatsoever.</p>	<p>1. The company does not provide for any extra payments or compensations in the event of early termination of office of members of the board of directors resulting from the change of control or any other reasons whatsoever.</p>	<p>This principle is</p>	<p>– complied with.</p>
<p><b>4.3 REMUNERATION OF EXECUTIVE BODY MEMBERS AND OTHER KEY MANAGERS IS LINKED TO THE COMPANY'S RESULTS AND THEIR PERSONAL CONTRIBUTION THERETO.</b></p>			
<p>4.3.1 Remuneration due to members of executive bodies and other key executives of the company is determined in a manner providing for reasonable and justified ratio of the fixed and variable parts of remuneration, depending on the company's performance and the employee's personal contribution.</p>	<p>1. In the reporting period, annual performance results approved by the board of directors were used to determine the amount of the variable part of remuneration due to members of executive bodies and other key executives of the company.</p> <p>2. During the latest assessment of the system of remuneration for members of executive bodies and other key executives of the compa-</p>	<p>This principle is not fully complied with.</p>	<p>The procedure for defining and payment of bonuses to members of the Management Board and other key executives existing in the Company does not allow receipt of such payments by the persons named. The Company believes the executive bodies' members' civil liability norms set out in the applicable law to be sufficient.</p>

	<p>company, the board of directors (remuneration committee) made sure that the company applies efficient ratio of the fixed and variable parts of remuneration.</p> <p>3. The company has in place a procedure that guarantees return to the company of bonus payments illegally received by members of executive bodies and other key executives of the company.</p>			
4.3.2	<p>The company put in place a long-term incentive programme for members of executive bodies and other key executives of the company with the use of the company's shares (options and other derivative instruments where the company's shares are the underlying asset).</p>	<p>1. The company has in place a long-term incentive program for members of executive bodies and other key executives of the company with the use of the company's shares (financial instruments based on the company's shares).</p> <p>2. The long-term incentive program for members of executive bodies and other key executives of the company implies that the right to dispose of shares and other financial instruments used in this program takes effect at least three years after such shares or other financial instruments are granted. The right to dispose of such shares or other financial instruments is linked to the company's performance targets.</p>	<p>This principle is not complied with.</p>	<p>Currently, The Company does not consider necessary implementing a long-term incentive program for members of executive bodies and other key executives of the company with the use of the Company's shares (financial instruments based on the Company's shares).</p>
4.3.3	<p>The compensation (golden parachute) payable by the company in case of early termination of powers of members of executive bodies or key executives at the company's initiative, provided that there have been no actions in bad faith on their part, does not exceed the double amount of the fixed part of their annual remuneration.</p>	<p>1. In the reporting period, the compensation (golden parachute) payable by the company in case of early termination of the powers of executive bodies or key executives at the company's initiative, provided that there have been no actions in bad faith on their part, did not exceed the double amount of the fixed part of their annual remuneration.</p>	<p>This principle is – complied with.</p>	
<b>5.1</b>	<b>THE COMPANY PUT IN PLACE AN EFFECTIVE RISK MANAGEMENT AND INTERNAL CONTROL SYSTEM TO GUARANTEE, IN A REASONABLE MANNER, FULFILLMENT OF THE COMPANY'S GOALS.</b>			
5.1.1	<p>The board of directors of the Company has de-</p>	<p>1. Functions of different management bodies and divisions of the</p>	<p>This principle is – complied with.</p>	

	<p>defined the Company's risk management and internal control principles and approaches.</p>	<p>company in the risk management and internal controls are clearly defined in the company's internal documents /relevant policy approved by the board of directors.</p>		
5.1.2	<p>The company's executive bodies ensure establishment and continuous operation of efficient risk management and internal controls in the company.</p>	<p>1. The company's executive bodies ensured the distribution of functions and powers related to risk management and internal controls between the heads (managers) of divisions and departments accountable to them.</p>	<p>This principle is complied with.</p>	–
5.1.3	<p>The company's risk management and internal controls ensure an objective, fair and clear view of the current state and future prospects of the company, the integrity and transparency of the company's reporting, as well as reasonable and acceptable risk exposure.</p>	<p>1. The company has in place an approved anti-corruption policy.</p> <p>2. The company established an accessible method of notifying the board of directors or the board's audit committee of breaches of any violations of the law, the company's internal procedures and code of ethics.</p>	<p>This principle is complied with.</p>	–
5.1.4	<p>The company's board of directors shall take necessary measures to make sure that the company's risk management and internal controls are consistent with the principles of, and approaches to, its setup determined by the board of directors, and that the system is functioning efficiently.</p>	<p>1. In the reporting period, the board of directors or the Board's audit committee assessed the efficiency of the company's risk management and internal controls. Key results of this assessment are included in the company's annual report.</p>	<p>This principle is complied with.</p>	–
<p><b>5.2 THE COMPANY ARRANGES FOR AN INTERNAL AUDIT, TO ASSESS RELIABILITY AND PERFORMANCE OF THE RISK MANAGEMENT AND INTERNAL CONTROL SYSTEM ON A REGULAR AND INDEPENDENT BASIS.</b></p>				
5.2.1	<p>The company set up a separate business unit or engaged an independent external organization to carry out internal audits.</p> <p>Functional and administrative reporting lines of the internal audit department are delineated. The internal audit unit functionally reports to the board of directors.</p>	<p>1. To perform internal audits, the company set up a separate business unit – internal audit division, functionally reporting to the board of directors or to the audit committee, or engaged an independent external organization with the same line of reporting.</p>	<p>This principle is complied with.</p>	–

5.2.2	The internal audit division assesses the performance of the internal controls, risk management, and corporate governance. The company applies generally accepted standards of internal audit.	<p>1. In the reporting period, the performance of the internal controls and risk management was assessed as part of the internal audit procedure.</p> <p>2. The company applies generally accepted approaches to internal audit and risk management.</p>	This principle is – complied with.
<b>6.1 THE COMPANY AND ITS OPERATIONS ARE TRANSPARENT FOR ITS SHAREHOLDERS, INVESTORS AND OTHER STAKEHOLDERS.</b>			
6.1.1	The company has developed and implemented an information policy ensuring an efficient exchange of information by the company, its shareholders, investors, and other stakeholders.	<p>1. The company's board of directors approved an information policy developed in accordance with the Code's recommendations.</p> <p>2. The board of directors (or its committee) reviewed the company's compliance with its information policy at least once in the reporting period.</p>	This principle is – complied with.
6.1.2	The company discloses information on its corporate governance and practice, including detailed information on compliance with the principles and recommendations of the Code.	<p>1. The company discloses information on its corporate governance and general principles of corporate governance, including disclosure on its website.</p> <p>2. The company discloses information on the membership of its executive bodies and board of directors, independence of the directors and their membership in the board's committees (as defined by the Code).</p> <p>3. If the company has a controlling person, the company publishes a memorandum of the controlling person setting out this person's plans for the company's corporate governance.</p>	This principle is – complied with.
<b>6.2 THE COMPANY DISCLOSES UP-TO-DATE, COMPLETE AND RELIABLE INFORMATION ON ITS OPERATIONS IN DUE TIME, TO ENABLE ITS SHAREHOLDERS AND INVESTORS TO MAKE INFORMED DECISIONS.</b>			
6.2.1	The company discloses information based on the principles of regularity, consistency and promptness, as well as availability, reliability, completeness and comparability of disclosed data.	1. The company's information policy sets out approaches to, and criteria for, identifying information that can have a material impact on the company's evaluation and the price of its securities, as well as procedures ensuring timely disclosure of such information.	This principle is – complied with.

	<p>2. If the company's securities are traded on foreign organized markets, the company ensured concerted and equivalent disclosure of material information in the Russian Federation and in the said markets in the reporting year.</p> <p>3. If foreign shareholders hold a material portion of the company's shares, information was disclosed both in the Russian language and one of the most widely used foreign languages in the reporting period.</p>		
6.2.2	<p>The company avoids a formalistic approach to information disclosure and discloses material information on its operations, even if disclosure of such information is not required by law.</p>	<p>1. In the reporting period, the company disclosed annual and 6M financial statements prepared under the IFRS. The company's annual report for the reporting period included annual financial statements prepared under the IFRS, along with the auditor's report.</p> <p>2. The company discloses full information on its capital structure in accordance with Recommendation 290 of the Code both in the annual report and on the company's website.</p>	<p>This principle is not fully complied with.</p> <p>The Company discloses its capital structure to the extent required by the applicable laws.</p>
6.2.3	<p>The company's annual report, as one of the most important tools of its information exchange with shareholders and other interested parties, contains information enabling assessment of the company's annual performance results.</p>	<p>1. The company's annual report contains information on the key aspects of its operating and financial performance.</p> <p>2. The company's annual report contains information on the environmental and social aspects of the company's operations.</p>	<p>This principle is – complied with.</p>
<p><b>6.3 THE COMPANY PROVIDES INFORMATION AND DOCUMENTS REQUESTED BY ITS SHAREHOLDERS IN ACCORDANCE WITH PRINCIPLES OF FAIRNESS AND EASE OF ACCESS.</b></p>			
6.3.1	<p>The company provides information and documents requested by its shareholders in accordance with principles of fairness and ease of access.</p>	<p>1. The company's information policy establishes the procedure for providing shareholders with easy access to information, including information on legal entities controlled by the company, as requested by shareholders.</p>	<p>This principle is not fully complied with.</p> <p>The Company's Information Policy determines an easy procedure for providing shareholders with access to information, with the exception of information on legal entities controlled by the Company, the provision of which is not prescribed for by law.</p>
6.3.2	<p>When providing information to shareholders, the company shall ensure reasonable balance between the interests of particular</p>	<p>1. In the reporting period, the company did not refuse any shareholder requests for information, or such refusals were justified.</p>	<p>This principle is – complied with.</p>

shareholders and its own interests consisting in preserving the confidentiality of important commercial information which may materially affect its competitiveness.

2. In cases defined by the information policy, shareholders are warned of the confidential nature of the information and undertake to maintain its confidentiality.

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**7.1 ACTIONS WHICH WILL OR MAY MATERIALLY AFFECT THE COMPANY'S SHARE CAPITAL STRUCTURE AND ITS FINANCIAL POSITION AND ACCORDINGLY THE POSITION OF ITS SHAREHOLDERS ("MATERIAL CORPORATE ACTIONS") ARE TAKEN ON FAIR TERMS ENSURING THAT THE RIGHTS AND INTERESTS OF THE SHAREHOLDERS AND OTHER STAKEHOLDERS ARE OBSERVED.**

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7.1.1	Material corporate actions include restructuring of the company, acquisition of 30% or more of the company's voting shares (takeover), execution by the company of major transactions, increase or decrease of the company's authorised capital, listing or de-listing of the company's shares, as well as other actions which may lead to material changes in the rights of shareholders or violation of their interests. The company's charter provides a list (criteria) of transactions or other actions classified as material corporate actions within the authority of the company's board of directors.	<p>1. The company's charter includes a list of transactions or other actions deemed to be material corporate actions, and their identification criteria. Resolutions on material corporate actions are referred to the jurisdiction of the board of directors. When execution of such corporate actions is expressly referred by law to the jurisdiction of the general shareholders meeting, the board of directors presents relevant recommendations to shareholders.</p> <p>2. According to the company's charter, material corporate actions include at least: company reorganization, acquisition of 30% or more of the company's voting shares (in case of takeover), entering in major transactions, increase or decrease of the company's charter capital, listing or de-listing of the company's shares.</p>	This principle is not fully complied with.	<p>The Company's Articles of Association does not contain a separate section with a list of significant corporate actions. At the same time, decision-making on issues related to significant corporate actions falls within the authority of the Board of Directors.</p> <p>The Company does not see any risks in this.</p>
7.1.2	The board of directors plays a key role in passing resolutions or making recommendations on material corporate actions, relying on the opinions of the company's independent directors.	1. The company has in place a procedure enabling independent directors to express their opinions on material corporate actions prior to approval thereof.	This principle is not fully complied with.	Relevant comments are provided in items 2.4.4. and 2.5.1 hereof.
7.1.3	When taking material corporate actions which would affect rights or legitimate interests of shareholders, equal terms and conditions are guaranteed for all shareholders; if the statutory procedure designed to protect shareholders' rights proves	<p>1. Due to specifics of the company's operations, the company's charter contains less stringent criteria for material corporate actions than required by law.</p> <p>2. All material corporate actions in the reporting period were duly approved before they were taken.</p>	This principle is not fully complied with.	In the reporting period one material corporate action was subsequently approved in accordance with the applicable law.

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insufficient, additional measures are taken to protect their rights and legitimate interests. In doing so, the company is guided by the corporate governance principles set forth in the Code, as well as by formal statutory requirements.

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**7.2 THE COMPANY PROVIDES A PROCEDURE FOR TAKING MATERIAL CORPORATE ACTIONS THAT WOULD ENABLE ITS SHAREHOLDERS TO RECEIVE FULL INFORMATION ABOUT SUCH ACTIONS IN DUE TIME AND INFLUENCE THEM, AND ALSO GUARANTEE THAT THE SHAREHOLDER RIGHTS ARE OBSERVED AND DULY PROTECTED WHEN SUCH ACTIONS ARE TAKEN.**

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7.2.1 Information about material corporate actions is disclosed with explanations of the grounds, circumstances and consequences.	1. In the reporting period, the company disclosed information about its material corporate actions in due time and in detail, including the grounds for, and timelines of, such actions.	This principle is – complied with.
7.2.2 Rules and procedures related to material corporate actions taken by the company are set out in the company's internal documents.	1. The company's internal documents set out a procedure for engaging an independent appraiser to estimate the value of assets either disposed of or acquired in a major transaction or a related-party transaction.  2. The company's internal documents set out a procedure for engaging an independent appraiser to estimate the value of shares acquired and redeemed by the company.  3. The company's internal documents provide for an expanded list of grounds on which the company's directors and other persons as per the applicable law are deemed to be related parties to the company's transactions.	This principle is not complied with.  The need to involve an appraiser for the valuation of the purchase price of the Company's shares is provided by the current legislation. There is no need to duplicate this requirement in the internal documents of the Company.

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## FORWARD-LOOKING STATEMENTS

This Annual Review includes 'forward-looking information' within the meaning of Section 27A of the US Securities Act of 1933, as amended, and Section 21E of the US Securities Exchange Act of 1934, as amended. Certain statements included in this Annual Report and Accounts, including, without limitation, statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions and other statements, which are other than statements of historical facts. The words "believe," "expect," "anticipate," "intends," "estimate," "forecast," "project," "will," "may," "should" and similar expressions identify forward-looking statements. Forward-looking statements include statements regarding: strategies, outlook and growth prospects; future plans and potential for future growth; liquidity, capital resources and capital expenditures; growth in demand for our products; economic outlook and industry trends; developments of our markets; the impact of regulatory initiatives; and the strength of our competitors. The forward-looking statements in this Annual Review are based upon various assumptions, many of which are based, in turn, upon further assumptions, including without limitation, management's examination of historical operating trends, data contained in our records and other data available from third parties. Although we believe that these assumptions were reasonable when made, these assumptions are inherently subject to significant uncertainties and contingencies, which are difficult or impossible to predict and are beyond our control. As a result, we may not achieve or accomplish these expectations, beliefs or projections. In addition, important factors that, in our view, could cause actual results to differ materially from those discussed in the forward-looking statements include:

- changes in the balance of oil and gas supply and demand in Russia and Europe;
- the effects of domestic and international oil and gas price volatility and changes in regulatory conditions, including prices and taxes;
- the effects of competition in the domestic and export oil and gas markets;
- our ability to successfully implement any of our business strategies;
- the impact of our expansion on our revenue potential, cost basis and margins;
- our ability to produce target volumes in the event, among other factors, of restrictions on our access to transportation infrastructure;
- the effects of changes to our capital expenditure projections on the growth of our production;

- potentially lower production levels in the future than currently estimated by our management and/or independent petroleum reservoir engineers;
- inherent uncertainties in interpreting geophysical data;
- changes to project schedules and estimated completion dates;
- our success in identifying and managing risks to our businesses;
- the effects of changes to the Russian legal framework concerning currently held and any newly acquired oil and gas production licenses;
- changes in political, social, legal or economic conditions in Russia and the CIS;
- the effects of technological changes;
- the effects of changes in accounting standards or practices.

This list of important factors is not exhaustive. When relying on forward-looking statements, one should carefully consider the foregoing factors and other uncertainties and events, especially in light of the political, economic, social and legal environment in which we operate. Such forward looking statements speak only as of the date on which they are made. Accordingly, we do not undertake any obligation to update or revise any of them, whether as a result of new information, future events or otherwise. We do not make any representation, warranty or prediction that the results anticipated by such forward-looking statements will be achieved, and such forward-looking statements represent, in each case, only one of many possible scenarios and should not be viewed as the most likely or standard scenario. The information and opinions contained in this document are provided as at the date of this review and are subject to change without notice.

## TERMS AND ABBREVIATIONS

Mentions in this Annual Report of “PAO NOVATEK”, “NOVATEK”, “the Company”, “we” and “our” refer to PAO NOVATEK and/or its subsidiaries (according to IFRS methodology) and/or joint ventures (accounted for on an equity basis according to IFRS standards), depending upon the context, in which the terms are used.

<b>barrel</b>	one stock tank barrel, or 42 US gallons of liquid volume
<b>bcm</b>	billion cubic meters
<b>boe</b>	barrels of oil equivalent
<b>km</b>	kilometer(s)
<b>mboe</b>	thousand boe
<b>mcm</b>	thousand cubic meters
<b>mt</b>	thousand metric tons
<b>mboe</b>	million boe
<b>mmcm</b>	million cubic meters
<b>mmt</b>	million metric tons
<b>ton</b>	metric ton
<b>SEC</b>	United States Securities and Exchange Commission
<b>PRMS</b>	Petroleum Resources Management System
<b>YNAO</b>	Yamal-Nenets Autonomous Region
<b>RR</b>	Russian rouble
<b>LPG</b>	liquified petroleum gases
<b>LNG</b>	liquified natural gas

## CONVERSION FACTORS

1000 cubic meters of gas = 6.54 boe.

To convert crude oil and gas condensate reserves from tons to barrels we used various coefficients depending on the liquids density at each field.

**PAO NOVATEK**

**IFRS CONSOLIDATED  
FINANCIAL STATEMENTS**

**FOR THE YEAR ENDED  
31 DECEMBER 2017**

**AND INDEPENDENT  
AUDITOR'S REPORT**

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## Independent Auditor's Report

TO THE SHAREHOLDERS AND BOARD OF DIRECTORS OF PAO NOVATEK:

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### Our opinion

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

### What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2017;
- the consolidated statement of income for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of cash flows for the year then ended;
- the consolidated statement of changes in equity for the year then ended; and
- the notes to the consolidated financial statements, which include significant accounting policies and other explanatory information.

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### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements of the Auditor's Professional Ethics Code and Auditor's Independence Rules that are relevant to our audit of the consolidated financial statements in the Russian Federation. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

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### Our audit approach

#### Overview

#### Materiality

Overall group materiality: 7,000 million Russian Roubles (“RUB”) which represents 4% of adjusted profit before tax excluding currency exchange differences, net gain on disposal of interests in joint ventures and the Group's share of joint ventures' currency exchange differences net of income tax.

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#### Audit scope

- We conducted audit work covering all significant components and balances in Russia, Switzerland, Singapore and Republic of Cyprus.
- The group engagement team visited all significant locations in Russia and Switzerland.
- Our audit scope addressed more than 99% of the Group's revenues and more than 99% of the Group's absolute value of underlying profit before tax.

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#### Key audit matters

- Accounting for trading activities in Europe;
- Valuation of non-commodity financial derivatives.



We designed our audit by determining materiality and assessing the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

**Materiality**

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, if any, both individually and in aggregate on the financial statements as a whole.

<b>Overall group materiality</b>	RUB 7,000 million
<b>How we determined it</b>	4% of adjusted profit before tax excluding currency differences, net gain on disposal of interests in joint ventures and share of joint ventures' currency differences net of income tax.
<b>Rationale for the materiality benchmark applied</b>	<p>We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark. The use of adjusted profit before tax mitigates the effect of volatility (that could be material) caused by non-recurring factors such as gains on disposals of assets and foreign exchange differences and provides a more stable basis for determining materiality, focusing on the underlying profitability of the Group.</p> <p>We chose 4% which is consistent with quantitative materiality thresholds used for profit-oriented companies in this industry and prior year approach.</p>

**Key audit matters**

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

Key audit matter	How our audit addressed the Key audit matter
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*Accounting for trading activities in Europe*

The Group conducts natural gas foreign trading in active markets under long-term and short-term purchase and sales contracts. The Group also purchases and sells various derivative instruments (with reference of the delivery points to the European natural gas hubs) in order to increase delivery optimization and decrease exposure to the risk of negative changes in natural gas prices.

The fair value of long-term natural gas derivative contracts involving the physical delivery of natural gas is determined using internal models and other valuation techniques (the mark-to-market and mark-to-model analysis) due to the absence of quoted prices or other observable, market-corroborated data, for the duration of the contracts.

We focused on this area because of the complexity of

We critically evaluated the appropriateness and consistency of key valuation assumptions used for the measurement of the contracts to ensure that the resulting valuation is reasonable.

We tested material valuations in detail and sought additional external evidence. We assessed the methodologies used, and the judgements and assumptions made. We identified the market data input used by the Group and tested them against independent data.

We tested the appropriateness of the valuation methodology applied and the integrity of the models used, and noted no material issues. We also tested the accuracy of the contractual inputs and the appropriateness of key valuation inputs including price and discount rates, and noted no material



## Key audit matter

## How our audit addressed the Key audit matter

the models and because model parameters are inherently subject to judgement applied by management.

issues.

Where the Group entered into new significant contracts in the year, we tested the contracts and assumptions used to assess whether the accounting treatment adopted is in accordance with International Accounting Standard 39.

We also gained an understanding of the controls that are in place for these trading activities.

We identified no material issues.

### *Valuation of non-commodity financial derivatives*

Certain shareholders' loans provided by the Group to its joint ventures include embedded derivatives that modify the cash flows of the loans based on financial and non-financial variables. The terms and conditions of each of these loans related to those variables were defined as a single compound embedded derivative. The Group designated these loans as financial assets at fair value through profit or loss. In accordance with IFRS, such loans are measured at fair value at each reporting date.

We focused on this area because of the significant impact of the valuation results on the financial statements of the Group and the fact that the measurement of the fair value of these loans is based on judgement and estimates applied by management which can be highly subjective.

We evaluated the appropriateness and consistency of key valuation assumptions (such as expected free cash flows of the joint ventures, production volumes, and discount rates used) to ensure that the resulting valuation of the financial instruments is reasonable. Those assumptions mainly referred to the Group's projections of future expected free cash flows to be generated by the joint ventures and estimates of market interest rates applied in the valuation. We also tested the accuracy of the contractual inputs and analyzed the appropriateness of the valuation methodology.

We identified no material issues.

### **How we tailored our group audit scope**

We tailored the scope of our audit in order to perform sufficient work to be able to give an opinion on the consolidated financial statements as a whole, taking into account the geographic and management structure of the Group, the accounting processes and controls and the industry in which the Group operates.

In establishing the overall group audit strategy and plan, we determined the type of work that needed to be performed at the reporting units by the group engagement team and by the component auditors from other PwC network firms. For each reporting unit we issued specific instructions to the component auditors within our audit scope. We determined the level of our and component auditors involvement we needed to be involved in the audit process at those reporting units so as to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the consolidated financial statements as a whole. We determined whether we required an audit of full scope of financial information or whether a defined scope of specified procedures was sufficient.

The group consolidation, financial statements disclosures and a number of complex items are audited directly by the PAO NOVATEK audit engagement team. These items include the assessment of accounting estimates performed by management in respect of fair values and classification of financial assets and liabilities, deferred income tax asset recognition, estimation of oil and gas reserves, impairment of financial and non-financial assets, impairment provision for trade receivables, pension obligations, asset retirement obligations and assessment of joint arrangements.

By performing the procedures described above at the individual component level, combined with the additional procedures performed at the group level, we have obtained sufficient and appropriate audit evidence regarding the financial information of the Group to provide a basis for our opinion on the consolidated financial statements.

### *Other information*

Management is responsible for the other information. The other information comprises report "Management's discussion and analysis of financial condition and results of operations of PAO NOVATEK for the years ended 31 December 2017 and 2016" (but does not include the consolidated financial statements and our auditor's report thereon), which we obtained prior to the date of this auditor's report, and "Quarterly Issuer's Report of PAO NOVATEK for the first quarter of 2018" as well as "Annual Report Review of PAO NOVATEK for 2017", which are expected to be made available to us after that date.





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

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

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

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### *Responsibilities of management and those charged with governance for the consolidated financial statements*

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

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

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

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### *Auditor's responsibilities for the audit of the consolidated financial statements*

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

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

- identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management;
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

The certified auditor responsible for the audit resulting in this independent auditor's report is A.G. Yashkov.

AO PricewaterhouseCoopers Audit

20 February 2018  
Moscow, Russian Federation



A.G. Yashkov, certified auditor (licence no. № 01-001391), AO PricewaterhouseCoopers Audit

Audited entity: PAO NOVATEK

Independent auditor: AO PricewaterhouseCoopers Audit

State registration certificate №1461/94, issued by the administration of Oktyabrskiy district of Samara on 16 August 1994.

State registration certificate № 008.890, issued by the Moscow Registration Chamber on 28 February 1992.

Certificate of inclusion in the Unified State Register of Legal Entities regarding the legal entity registered before 1 July 2002 No. 1026303117642 issued by the Inspectorate of the Russian Ministry of Taxes and Levies of Novokuybyshevsk, Samara Region on 20 August 2002.

Certificate of inclusion in the Unified State Register of Legal Entities issued on 22 August 2002 under registration № 1027700148431.

Location of the Company according to the Charter: Russian Federation, Yamalo-Nenetski state, Purovsky region, Tarko-Sale.

Member of Self-regulated organization of auditors «Russian Union of auditors» (Association).

Mailing address: 629850, Yamalo-Nenetski state, Purovsky region, Tarko-Sale, Pobedi str., 22 "a".

ORNZ 11603050547 in the register of auditors and audit organizations.

**PAO NOVATEK**  
**Consolidated Statement of Financial Position**  
(in millions of Russian roubles)

	Notes	At 31 December 2017	At 31 December 2016
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	6	360,051	331,795
Investments in joint ventures	7	285,326	259,650
Long-term loans and receivables	8	211,901	209,145
Other non-current assets	9	33,448	30,484
<b>Total non-current assets</b>		<b>890,726</b>	<b>831,074</b>
<b>Current assets</b>			
Inventories	10	11,084	9,044
Current income tax prepayments		43	581
Trade and other receivables	11	44,503	41,586
Prepayments and other current assets	12	31,863	33,248
Cash and cash equivalents	13	65,943	48,301
<b>Total current assets</b>		<b>153,436</b>	<b>132,760</b>
<b>Total assets</b>		<b>1,044,162</b>	<b>963,834</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Non-current liabilities</b>			
Long-term debt	14	141,448	161,296
Long-term lease liabilities	27	5,776	-
Deferred income tax liabilities	26	26,167	24,656
Asset retirement obligations		7,303	7,605
Other non-current liabilities		3,851	3,766
<b>Total non-current liabilities</b>		<b>184,545</b>	<b>197,323</b>
<b>Current liabilities</b>			
Short-term debt and current portion of long-term debt	15	14,302	55,469
Current portion of long-term lease liabilities	27	1,520	-
Trade payables and accrued liabilities	17	49,001	38,462
Current income tax payable		2,846	747
Other taxes payable		16,289	14,113
<b>Total current liabilities</b>		<b>83,958</b>	<b>108,791</b>
<b>Total liabilities</b>		<b>268,503</b>	<b>306,114</b>
<b>Equity attributable to PAO NOVATEK shareholders</b>			
Ordinary share capital		393	393
Treasury shares		(8,353)	(6,913)
Additional paid-in capital		31,297	31,297
Currency translation differences		(3,283)	(724)
Asset revaluation surplus on acquisitions		5,617	5,617
Retained earnings		732,168	618,680
<b>Total equity attributable to PAO NOVATEK shareholders</b>	18	<b>757,839</b>	<b>648,350</b>
<b>Non-controlling interest</b>		<b>17,820</b>	<b>9,370</b>
<b>Total equity</b>		<b>775,659</b>	<b>657,720</b>
<b>Total liabilities and equity</b>		<b>1,044,162</b>	<b>963,834</b>

The accompanying notes are an integral part of these consolidated financial statements.

  
L. Mikhelson  
Chairman of the Management Committee

20 February 2018

  
M. Gyetvay  
Chief Financial Officer

**PAO NOVATEK****Consolidated Statement of Income**

(in millions of Russian roubles, except for share and per share amounts)

	Notes	Year ended 31 December:	
		2017	2016
<b>Revenues</b>			
Oil and gas sales	19	579,819	533,857
Other revenues		3,367	3,615
<b>Total revenues</b>		<b>583,186</b>	<b>537,472</b>
<b>Operating expenses</b>			
Purchases of natural gas and liquid hydrocarbons	20	(161,443)	(134,268)
Transportation expenses	21	(137,192)	(133,462)
Taxes other than income tax	22	(49,494)	(44,053)
Depreciation, depletion and amortization	6	(34,523)	(34,631)
Materials, services and other	23	(20,768)	(19,133)
General and administrative expenses	24	(17,170)	(18,126)
Exploration expenses	6	(1,819)	(2,087)
Net impairment expenses		(52)	(178)
Change in natural gas, liquid hydrocarbons and work-in-progress		2,602	439
<b>Total operating expenses</b>		<b>(419,859)</b>	<b>(385,499)</b>
Net gain on disposal of interests in joint ventures	5	-	73,072
Other operating income (loss), net		424	221
<b>Profit from operations</b>		<b>163,751</b>	<b>225,266</b>
<b>Finance income (expense)</b>			
Interest expense	25	(7,712)	(11,570)
Interest income	25	15,872	18,732
Change in fair value of non-commodity financial instruments	27	(7,178)	10,387
Foreign exchange gain (loss), net	25	13,676	(25,490)
<b>Total finance income (expense)</b>		<b>14,658</b>	<b>(7,941)</b>
Share of profit (loss) of joint ventures, net of income tax	7	22,430	90,839
<b>Profit before income tax</b>		<b>200,839</b>	<b>308,164</b>
<b>Income tax expense</b>			
Current income tax expense		(35,227)	(35,577)
Deferred income tax benefit (expense), net		858	(7,514)
<b>Total income tax expense</b>	26	<b>(34,369)</b>	<b>(43,091)</b>
<b>Profit</b>		<b>166,470</b>	<b>265,073</b>
Profit attributable to:			
Non-controlling interest		10,083	7,278
Shareholders of PAO NOVATEK		156,387	257,795
Basic and diluted earnings per share (in Russian roubles)		51.85	85.41
Weighted average number of shares outstanding (in millions)		3,016.2	3,018.5

The accompanying notes are an integral part of these consolidated financial statements.

**PAO NOVATEK**  
**Consolidated Statement of Comprehensive Income**  
(in millions of Russian roubles)

	Notes	Year ended 31 December:	
		2017	2016
<b>Profit</b>		<b>166,470</b>	<b>265,073</b>
<b>Other comprehensive income (loss)</b>			
<b>Items that will not be reclassified subsequently to profit (loss)</b>			
Remeasurement of pension obligations	16	(724)	(121)
Share of remeasurement of pension obligations of joint ventures		(100)	(21)
		<b>(824)</b>	<b>(142)</b>
<b>Items that may be reclassified subsequently to profit (loss)</b>			
Currency translation differences		(2,580)	4,368
Share of currency translation differences of joint ventures		21	-
		<b>(2,559)</b>	<b>4,368</b>
<b>Other comprehensive income (loss)</b>		<b>(3,383)</b>	<b>4,226</b>
<b>Total comprehensive income</b>		<b>163,087</b>	<b>269,299</b>
Total comprehensive income attributable to:			
Non-controlling interest		10,083	7,278
Shareholders of PAO NOVATEK		153,004	262,021

The accompanying notes are an integral part of these consolidated financial statements.

**PAO NOVATEK**  
**Consolidated Statement of Cash Flows**  
(in millions of Russian roubles)

	Notes	Year ended 31 December:	
		2017	2016
<b>Profit before income tax</b>		<b>200,839</b>	<b>308,164</b>
<b>Adjustments to profit before income tax:</b>			
Depreciation, depletion and amortization		34,523	34,631
Impairment expenses (reversals), net		52	178
Foreign exchange loss (gain), net		(13,676)	25,490
Loss (gain) on disposal of assets, net		305	(73,072)
Interest expense		7,712	11,570
Interest income		(15,872)	(18,732)
Share of loss (profit) in joint ventures, net of income tax	7	(22,430)	(90,839)
Change in fair value of			
non-commodity financial instruments		7,178	(10,387)
Revaluation of commodity derivatives through loss (profit)		9	1,778
Decrease (increase) in long-term advances given		655	(3,331)
Other adjustments		240	152
<b>Working capital changes</b>			
Decrease (increase) in trade and other receivables, prepayments and other current assets		(786)	2,592
Decrease (increase) in inventories		(2,607)	(861)
Increase (decrease) in trade payables and accrued liabilities, excluding interest and dividends payable		6,592	9,953
Increase (decrease) in taxes payable, other than income tax		1,962	2,836
<b>Total effect of working capital changes</b>		<b>5,161</b>	<b>14,520</b>
Dividends received from joint ventures		2,383	-
Interest received		5,949	1,983
Income taxes paid excluding actual payments relating to disposal of stakes in joint ventures		(32,629)	(28,314)
<b>Net cash provided by operating activities</b>		<b>180,399</b>	<b>173,791</b>
<b>Cash flows from investing activities</b>			
Purchases of property, plant and equipment		(24,783)	(27,662)
Payments for mineral licenses		(9,786)	(1,928)
Purchases of materials for construction		(1,697)	(929)
Purchases of intangible assets		(780)	(508)
Acquisition of joint ventures	5	(1,583)	-
Additional capital contributions to joint ventures	7	(2,269)	(19,565)
Payments for acquisition of subsidiaries net of cash acquired	5	(15,706)	(2,961)
Proceeds from disposal of stakes in joint ventures	5	-	84,978
Costs to sell stakes in joint ventures	5	-	(2,634)
Actual income tax payments relating to disposal of stakes in joint ventures		-	(9,932)
Interest paid and capitalized		(3,391)	(5,314)
Guarantee fees paid		(1,315)	(1,061)
Loans provided to joint ventures	8	(5,211)	(6,645)
Repayments of loans provided to joint ventures	8	8,246	6,038
<b>Net cash provided by (used for) investing activities</b>		<b>(58,275)</b>	<b>11,877</b>

**PAO NOVATEK**  
**Consolidated Statement of Cash Flows**  
(in millions of Russian roubles)

	Notes	Year ended 31 December:	
		2017	2016
<b>Cash flows from financing activities</b>			
Proceeds from long-term debt		-	6,373
Repayments of long-term debt		(53,035)	(82,753)
Repayments of short-term debt			
with original maturity more than three months		(136)	(21,300)
Net increase (decrease) in short-term debt			
with original maturity three months or less		(56)	(5,040)
Interest on debt paid		(6,526)	(11,423)
Dividends paid to shareholders	18	(42,075)	(41,653)
Payments of lease liabilities		(567)	-
Purchases of treasury shares	18	(1,442)	(916)
<b>Net cash used for financing activities</b>		<b>(103,837)</b>	<b>(156,712)</b>
Net effect of exchange rate changes on cash and cash equivalents		(645)	(9,842)
<b>Net increase (decrease) in cash and cash equivalents</b>		<b>17,642</b>	<b>19,114</b>
Cash and cash equivalents at the beginning of the period		48,301	29,187
<b>Cash and cash equivalents at the end of the period</b>		<b>65,943</b>	<b>48,301</b>

The accompanying notes are an integral part of these consolidated financial statements.

**PAO NOVATEK****Consolidated Statement of Changes in Equity**

(in millions of Russian roubles, except for number of shares)

	<i>Number of ordinary shares (in millions)</i>	<b>Ordinary share capital</b>	<b>Treasury shares</b>	<b>Additional paid-in capital</b>	<b>Currency translation differences</b>	<b>Asset revaluation surplus on acquisitions</b>	<b>Retained earnings</b>	<b>Equity attributable to PAO NOVATEK shareholders</b>	<b>Non- controlling interest</b>	<b>Total equity</b>
<b>1 January 2016</b>	<b>3,019.1</b>	<b>393</b>	<b>(5,997)</b>	<b>31,297</b>	<b>(5,092)</b>	<b>5,617</b>	<b>399,861</b>	<b>426,079</b>	<b>2,092</b>	<b>428,171</b>
Profit	-	-	-	-	-	-	257,795	257,795	7,278	265,073
Other comprehensive income (loss)	-	-	-	-	4,368	-	(142)	4,226	-	4,226
<b>Total comprehensive income</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>4,368</b>	<b>-</b>	<b>257,653</b>	<b>262,021</b>	<b>7,278</b>	<b>269,299</b>
Dividends (Note 18)	-	-	-	-	-	-	(41,653)	(41,653)	-	(41,653)
Effect from other changes in joint ventures' net assets (Note 7)	-	-	-	-	-	-	2,819	2,819	-	2,819
Purchase of treasury shares (Note 18)	(1.4)	-	(916)	-	-	-	-	(916)	-	(916)
<b>31 December 2016</b>	<b>3,017.7</b>	<b>393</b>	<b>(6,913)</b>	<b>31,297</b>	<b>(724)</b>	<b>5,617</b>	<b>618,680</b>	<b>648,350</b>	<b>9,370</b>	<b>657,720</b>
Profit	-	-	-	-	-	-	156,387	156,387	10,083	166,470
Other comprehensive loss	-	-	-	-	(2,559)	-	(824)	(3,383)	-	(3,383)
<b>Total comprehensive income (loss)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(2,559)</b>	<b>-</b>	<b>155,563</b>	<b>153,004</b>	<b>10,083</b>	<b>163,087</b>
Dividends (Note 18)	-	-	-	-	-	-	(42,075)	(42,075)	(1,633)	(43,708)
Purchase of treasury shares (Note 18)	(2.1)	-	(1,440)	-	-	-	-	(1,440)	-	(1,440)
<b>31 December 2017</b>	<b>3,015.6</b>	<b>393</b>	<b>(8,353)</b>	<b>31,297</b>	<b>(3,283)</b>	<b>5,617</b>	<b>732,168</b>	<b>757,839</b>	<b>17,820</b>	<b>775,659</b>

The accompanying notes are an integral part of these consolidated financial statements.



## PAO NOVATEK

### Notes to the Consolidated Financial Statements

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

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#### 1 ORGANIZATION AND PRINCIPAL ACTIVITIES

PAO NOVATEK (hereinafter referred to as “NOVATEK” or the “Company”) and its subsidiaries (hereinafter jointly referred to as the “Group”) is an independent oil and gas company engaged in the acquisition, exploration, development, production, processing, and marketing of hydrocarbons with its oil and gas operations located mainly in the Yamal-Nenets Autonomous Region (“YNAO”) of the Russian Federation. The Group delivers its natural gas and its liquid hydrocarbons on both the Russian domestic and international markets.

The Group sells its natural gas on the Russian domestic market at unregulated market prices (except for deliveries to residential customers); however, the majority of natural gas sold on the Russian domestic market by all producers is sold at prices regulated by the governmental agency of the Russian Federation that carries out state regulation of prices and tariffs for goods and services of natural monopolies in energy, utilities and transportation. The Group’s natural gas sales volumes on the domestic market fluctuate on a seasonal basis mostly due to Russian weather conditions, with sales peaking in the winter months of December and January and troughing in the summer months of July and August.

In December 2017, the Group’s joint venture OAO Yamal LNG started production at the first train of its natural gas liquefaction plant (hereinafter referred to as the “LNG Plant”) based on the resources of the South-Tambeyskoye field, located in the YNAO. Annual capacity of the LNG Plant after launching of the three trains will amount to 16.5 million tons of liquefied natural gas (5.5 million tons for each train) and up to 1.2 million tons of stable gas condensate. At the end of 2017, the shareholders of Yamal LNG approved a decision on construction of the fourth train with the capacity of about 0.9 million tons of LNG per year that will expand the overall LNG plant capacity from 16.5 million tons to 17.4 million tons of LNG per year. The Group purchases portion of produced liquefied natural gas (“LNG”) and sells it on the international markets. The Group’s LNG sales volumes are not subject to significant seasonal fluctuations.

The Group also purchases and sells natural gas on the European market under long-term and short-term supply contracts to carry out its foreign commercial trading activities, as well as conducts LNG regasification business in Poland.

The Group processes unstable gas condensate at its Purovsky Gas Condensate Processing Plant located in close proximity to its fields into stable gas condensate and liquefied petroleum gas. The majority of stable gas condensate is further processed at the Group’s Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea into higher-value refined products (naphtha, jet fuel, gasoil and fuel oil). The remaining stable gas condensate volumes are sold on domestic and international markets. The Group sells its liquid hydrocarbons at prices that are subject to fluctuations in underlying benchmark crude oil, naphtha and other gas condensate refined products prices. The Group’s liquids sales volumes are not subject to significant seasonal fluctuations.

In July 2017, NOVATEK acquired a 51 percent ownership interest in OOO Cryogas-Vysotsk for a cash consideration of RR 1,583 million. Cryogas-Vysotsk undertakes a project for construction of the first train of a medium-scale plant for natural gas liquefaction with annual capacity of 660 thousand tons, located at the port of Vysotsk on the Baltic Sea.

In November 2017, the Group acquired a 100 percent ownership interest in OOO Severneft-Urengoy, an oil and gas company located in YNAO, for a cash consideration of RR 13,062 million. Severneft-Urengoy is a holder of the license for exploration and production of hydrocarbons within the West-Yaroyakhinsky license area.

In December 2017, the Group acquired 100 percent ownership interests in AO Eurotek and AO South-Khadyryakhinskoye which held the licenses for exploration and production of hydrocarbons within the Syskonsyninskiy license area located in Khanty-Mansiysk Autonomous Region and the South-Khadyryakhinskiy license area located in YNAO, respectively, for total cash consideration of RR 5,412 million.

In February 2018, a Group’s subsidiary OOO Kola Yard was renamed to OOO NOVATEK-Murmansk to align with the uniform brand image for NOVATEK.

## PAO NOVATEK

### Notes to the Consolidated Financial Statements

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

## 2 BASIS OF PREPARATION

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of available-for-sale financial assets and financial instruments categorised at fair value through profit or loss. In the absence of specific IFRS guidance for oil and gas producing companies, the Group has developed accounting policies in accordance with other generally accepted accounting principles for oil and gas producing companies, mainly US GAAP, insofar as they do not conflict with IFRS principles.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

**Functional and presentation currency.** The consolidated financial statements are presented in Russian roubles, the Group’s reporting (presentation) currency and the functional currency for the Company and the majority of the Group’s subsidiaries.

Transactions denominated in foreign currencies are converted into the functional currency of each entity at the exchange rates prevailing on the date of transactions. Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency of each entity by applying the year end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies valued at cost are converted into the functional currency of each entity at the initial exchange rate. Non-monetary assets that are remeasured to fair value, recoverable amount or realizable value, are converted at the exchange rate applicable to the date of remeasurement. Exchange gains and losses resulting from foreign currency remeasurement into the functional currency are included in profit (loss) for the reporting period.

On consolidation the assets and liabilities (both monetary and non-monetary) of the Group entities whose functional currency is not the Russian rouble are translated into Russian roubles at the closing exchange rate at each balance sheet date. All items included in the shareholders’ equity, other than profit or loss, are translated at historical exchange rates. The financial results of these entities are translated into Russian roubles using exchange rates at the dates of the transactions or the average exchange rate for the period when this is a reasonable approximation. Exchange adjustments arising on the opening net assets and the profits for the reporting period are taken to other comprehensive income and reported as currency translation differences in the consolidated statement of changes in equity and the consolidated statement of comprehensive income.

Exchange rates for foreign currencies in which the Group conducted significant transactions or had significant assets and/or liabilities in the reporting period were as follows:

<i>Russian roubles to one currency unit</i>	At 31 December 2017	At 31 December 2016	Average rate for the year ended 31 December:	
			2017	2016
US dollar (USD)	57.60	60.66	58.35	67.03
Euro (EUR)	68.87	63.81	65.90	74.23
Polish zloty (PLN)	16.51	14.44	15.48	17.03

**Exchange rates and restrictions.** The Russian rouble is not a fully convertible currency outside the Russian Federation and, accordingly, any remeasurement of Russian rouble amounts to US dollars or any other currency should not be construed as a representation that such Russian rouble amounts have been, could be, or will in the future be converted into other currencies at these exchange rates.

**Reclassifications.** Certain reclassifications have been made to the comparative figures to conform to the current period presentation with no effect on profit for the period or shareholder’s equity.

### **3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Adoption of new and amended standards and interpretations.** In 2017, the Group adopted all IFRS, amendments and interpretations which are effective 1 January 2017 and relevant to its operations. None of them had material impact on the Group's consolidated financial statements. In addition, the following new standards were early adopted by the Group starting from the annual period beginning on 1 January 2017:

**IFRS 15, Revenue from Contracts with Customers.** The standard introduces the core principle that revenue must be recognized when the goods or services are transferred to the customer, at the transaction price. Any discounts on the contract price must generally be allocated to the separate elements of contracts with customers. When the consideration varies for any reason, minimum amounts must be recognized if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalized and amortized over the period when the benefits of the contract are consumed.

In accordance with the transition provisions in IFRS 15, the Group elected to apply the new rules retrospectively to each prior period presented. The application of the standard had no material impact on the Group's consolidated financial statements and therefore the comparative period information was not restated.

**IFRS 16, Leases.** The standard requires lessees to recognize right-of-use assets and lease liabilities for most leases. In accordance with the transition provisions in IFRS 16, the Group chose to apply the new rules retrospectively with the cumulative effect of initially applying the standard recognized at 1 January 2017. The Group followed allowed practical expedients and did not apply the new standard to leases for which the lease term ended within twelve months of the date of transition.

As a result, at 1 January 2017, the Group recognized in the consolidated statement of financial position right-of-use assets and lease liabilities in the amount of RR 256 million, with no effect on opening retained earnings. In the consolidated statement of income for the year ended 31 December 2017, the Group has recorded RR 459 million and RR 119 million in depreciation, depletion and amortization and interest expense, respectively, in relation to leases accounted for under IFRS 16.

If the previous standard, IAS 17, *Leases*, was applied, the Group would have recorded for the year ended 31 December 2017 RR 366 million, RR 128 million and RR 5 million in transportation expenses, general and administrative expenses and in materials, services and other expenses, respectively, instead of the above mentioned depreciation, depletion and amortization and interest expenses.

**Principles of consolidation.** These consolidated financial statements present the assets, liabilities, equity, income, expenses and cash flows of PAO "NOVATEK" and its subsidiaries as those of a single economic entity. Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvements with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date that control ceases.

Intercompany transactions, balances and unrealized gains on transactions between group companies are eliminated. The Group and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

**Joint arrangements.** The Group undertakes a number of business activities through joint arrangements, which exist when two or more parties have joint control. Joint arrangements are classified as either joint operations or joint ventures, based on the contractual rights and obligations between the parties to the arrangement.

Interests in joint ventures are accounted for using the equity method. With regard to joint operations, the Group records its share of assets, liabilities, revenues and expenses of its joint operations in the consolidated financial statements on a line-by-line basis.

Under the equity method, an investment in a joint venture is initially recognized at cost. The difference between the cost of an acquisition and the share of the fair value of the joint venture's identifiable net assets represents goodwill upon acquiring the joint venture.

**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Post-acquisition changes in the Group's share of net assets of a joint venture are recognized as follows: (a) the Group's share of profits or losses is recorded in the consolidated profit or loss for the year as share of financial result of joint ventures; (b) the Group's share of other comprehensive income or loss is recognized in other comprehensive income or loss and presented separately; (c) dividends received or receivable from a joint venture are recognized as a reduction in the carrying amount of the investment; (d) all other changes in the Group's share of the carrying value of net assets of joint ventures are recognized within retained earnings in the consolidated statement of changes in equity.

After application of the equity method, including recognizing the joint venture's losses, the entire carrying amount of the investment is tested for impairment as a single asset whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

When the Group's share of losses in a joint venture equals or exceeds its interest in the joint venture, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the joint ventures. The interest in a joint venture is the carrying amount of the investment in the joint venture together with any long-term interests that, in substance, form part of the Group's net investment in the joint venture, including receivables and loans for which settlement is neither planned nor likely to occur in the foreseeable future.

Unrealized gains on transactions between the Group and its joint ventures are eliminated to the extent of the Group's interest in joint ventures; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Group.

**Business combinations.** The acquisition method of accounting is used to account for acquisitions of subsidiaries. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest.

Goodwill is measured by deducting the net assets of the acquiree from the aggregate of the consideration transferred for the acquiree, the amount of non-controlling interest in the acquiree and fair value of an interest in the acquiree held immediately before the acquisition date. Any negative amount ("negative goodwill") is recognized in profit or loss, after management reassesses whether it identified all the assets acquired and all liabilities and contingent liabilities assumed and reviews appropriateness of their measurement.

The consideration transferred for the acquiree is measured at the fair value of the assets transferred, equity instruments issued and liabilities incurred or assumed, including fair value of assets or liabilities from contingent consideration arrangements but excludes acquisition related costs such as advisory, legal, valuation and similar professional services.

**Disposals of subsidiaries, associates or joint ventures.** When the Group ceases to consolidate a subsidiary or account for an investment using the equity method because of a loss of control, joint control or significant influence, any retained interest in the entity is remeasured to its fair value, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are recycled to profit or loss.

If the ownership interest in a joint venture is reduced but joint control is retained or replaced with significant influence, the Group continues to apply the equity method and does not remeasure the retained interest; only a proportionate share of the amounts previously recognized in other comprehensive income are reclassified to profit or loss where appropriate.

**Extractive activities.** The Group follows the successful efforts method of accounting for its oil and gas properties and equipment whereby property acquisitions and development costs are capitalized, and exploration costs (geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity), excluding exploratory drilling expenditures and exploration license acquisition costs, are recognized within operating expenses in the consolidated statement of income as incurred.

## PAO NOVATEK

### Notes to the Consolidated Financial Statements

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

#### 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Exploration license acquisition costs and exploratory drilling costs are recognized as exploration assets within property, plant and equipment until it is determined whether proved reserves justifying their commercial development have been found. If no proved reserves are found, the relevant costs are charged to the consolidated statement of income. When proved reserves are determined, exploration license acquisition costs are reclassified to proved properties acquisition costs and exploratory drilling costs are reclassified to development expenditure categories within property, plant and equipment. Exploration license acquisition costs and exploratory drilling costs recognized as exploration assets are reviewed for impairment on an annual basis.

The cost of 3-D seismic surveys used to assist production, increase total recoverability and determine the desirability of drilling additional development wells within proved reservoirs are capitalized as development costs. All other seismic costs are expensed as incurred.

Production costs and overheads are charged to expense as incurred.

**Property, plant and equipment.** Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation, depletion, amortization and impairment.

The cost of self-constructed assets includes the cost of direct materials, direct employee related costs, a pro-rata portion of depreciation of assets used for construction and an allocation of the Group's overhead costs.

Depreciation, depletion and amortization of oil and gas properties and equipment is calculated using the unit-of-production method for each field based upon total proved reserves for costs associated with acquisitions of proved properties and common infrastructure facilities, and proved developed reserves for other development costs, including wells. Where unit-of-production method does not reflect useful life and pattern of consumption of particular oil and gas assets, such as processing facilities serving several properties, those assets are depreciated on a straight-line basis.

Property, plant and equipment, other than oil and gas properties and equipment, are depreciated on a straight-line basis over their estimated useful lives. Land and assets under construction are not depreciated.

The estimated useful lives of the Group's property, plant and equipment depreciated on a straight-line basis are as follows:

	<u>Years</u>
Machinery and equipment	5-15
Processing facilities	20-30
Buildings	25-50

At each reporting date management assesses whether there is any indication of impairment in respect of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less selling costs and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash generating units). The carrying amount is reduced to the recoverable amount and the impairment loss is recognized in profit or loss for the respective period. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

**Borrowing costs.** Interest costs on borrowings and exchange differences arising from foreign currency borrowings (to the extent that they are regarded as an adjustment to interest costs) used to finance the construction of property, plant and equipment are capitalized during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are recognized in the consolidated statement of income.

**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Asset retirement obligations.** An asset retirement obligation is recognized when the Group has a present legal or constructive obligation to dismantle, remove and restore items of property, plant and equipment whose construction is substantially completed. The obligation is recognized when incurred at the present value of the estimated costs of dismantling the assets, including abandonment and site restoration costs, and are included within the carrying value of property, plant and equipment.

Changes in the asset retirement obligation relating to a change in the expected pattern of settlement of the obligation, or in the estimated amount of the obligation or in the discount rates, are treated as a change in an accounting estimate in the current period. Such changes are reflected as adjustments to the carrying value of property, plant and equipment and the corresponding liability. Changes in the obligation resulting from the passage of time are recognized in the consolidated statement of income as interest expense.

**Leases.** A contract is (or contains) a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

Right-of-use assets are initially measured at cost and depreciated by the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The cost of right-of-use assets comprises of initial measurement of the lease liability, any lease payments made before or at the commencement date and initial direct costs. After the commencement date, the right-of-use assets are carried at cost less accumulated depreciation and impairment losses in accordance with IAS 16, *Property, plant and equipment*.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date and subsequently measured at amortized cost with the interest expense recognized within finance income (expense) in the consolidated statement of income.

In accordance with IFRS 16, the Group elected not to apply accounting requirements under this standard to short-term leases.

**Non-current assets held for sale.** Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell.

The Group ceases to use the equity method of accounting in relation to the interest in a joint venture or an associate classified as an asset held for sale.

**Inventories.** Natural gas, gas condensate, crude oil and gas condensate refined products are valued at the lower of cost or net realizable value. The cost of inventories includes direct cost of materials, direct operating costs, and related production overhead expenses and is recorded on a first-in-first-out (“FIFO”) basis. Net realizable value is the estimate of the selling price in the ordinary course of business, less selling expenses.

Materials and supplies are carried at amounts which do not exceed their respective recoverable amounts in the normal course of business.

**Financial instruments.** Derivative instruments are accounted for at fair value and are carried as financial assets when fair value is positive and as financial liabilities when fair value is negative. Gains or losses arising from changes in the fair value of derivative instruments are included in the consolidated statement of income. The Group does not apply hedge accounting.

Certain shareholders’ loans provided by the Group to its joint ventures include embedded derivatives that modify cash flows of the loans based on financial (market interest rates) and non-financial (interest rate on borrowings of the lender and free cash flows of the borrower) variables. The risks relating to these variables are interrelated; therefore, terms and conditions of each of these loans related to those variables were defined as a single compound embedded derivative. The Group designated these loans as financial assets at fair value through profit or loss (see Note 27).

**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

The difference between the loan proceeds and the fair value at initial recognition is recorded as the Group's investment in the joint ventures. Subsequently, the loans are measured at fair value at each reporting date with recognition of the revaluation through profit or loss. Interest income and foreign exchanges differences (calculated using the effective interest method), and remaining effect from fair value remeasurement are disclosed separately in the consolidated statement of income.

Where there is an active market for a commodity, commodity contracts are accounted for as derivatives except for contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a commodity in accordance with the Group's expected purchase, sale or usage requirements. Gains or losses arising from changes in the fair value of commodity derivatives are recognized within other operating income (loss) in the consolidated statement of income (see Note 27).

Derivatives embedded in other non-derivative financial instruments or in non-financial host contracts are recognized as separate derivatives when their risks and economic characteristics are not closely related to those of the host contracts, and the host contracts are not carried at fair value.

A pricing formula in a purchase or sale contract will, for instance, be considered to be closely related to the host purchase or sales contract if the price formula is related to the market for such host contracts. Where there is no active market for the commodity, the Group assesses the characteristics of such a price to be closely related to the host contract if the price formula is based on relevant indexations commonly used by other market participants. Contracts are assessed for embedded derivatives when the Group becomes a party to them, including at the date of a business combination.

Loans and receivables with fixed or determinable payments that are not quoted in an active market are recognized initially at fair value, normally being the transaction price, plus directly attributable transaction costs, and subsequently carried at amortized cost using the effective interest method. Loans and receivables are analyzed for impairment on a debtor by debtor basis. A provision for impairment of loans and receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to their original terms.

The Group's debt, trade payables and other non-derivative liabilities are classified as financial liabilities measured at amortized cost. Financial liabilities included in this category are initially recognized at fair value less directly attributable transaction costs and subsequently are measured at amortized cost using the effective interest method.

The effective interest rate is the rate that exactly discounts future cash payments and receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying value of the financial asset or financial liability.

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position only when there is a legally enforceable right to offset the recognized amounts, and there is an intention to either settle on a net basis, or to realize the asset and settle the liability simultaneously.

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

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. Provisions are reassessed at each reporting date, and those changes in the provisions resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain.

**Pension obligations.** The Group performs mandatory contributions to the Pension Fund of the Russian Federation on behalf of its employees based on gross salary payments. These contributions represent a defined contribution plan, are expensed when incurred and are included in the employee compensation in the consolidated statement of income.

**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

The Group also operates a non-contributory post-employment defined benefit plan based on employees' years of service and average salary (see Note 16). The liability recognized in the consolidated statement of financial position in respect of the defined benefit pension plan is the present value of the defined benefit obligations at the balance sheet date. The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method.

Actuarial gains and losses on assets and liabilities arising from experience adjustments and changes in actuarial assumptions are charged or credited to other comprehensive income in the period in which they arise. They are not reclassified to profit or loss in subsequent periods. Past-service costs are recognized in profit or loss in the period when a plan is amended or curtailed.

**Non-financial guarantees.** The Group issued a number of shareholder guarantees that provide compensation to third parties if a joint venture fails to perform a contractual obligation. Such guarantees meet the definition of insurance contracts and are accounted for under IFRS 4, *Insurance contracts*. Liabilities for a non-financial guarantee are recognized when an outflow of resources embodying economic benefits required to settle the obligation is probable. The liabilities are recognized in the amount of best estimates of such an outflow.

**Income taxes.** The income tax charge or benefit comprises current tax and deferred tax and is recognized in the consolidated statement of income unless it relates to transactions that are recognized, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to or recovered from the tax authorities in respect of taxable profits or losses for the current and prior periods. Russian tax legislation allows to prepare and file a single, consolidated income tax declaration by the taxpayers' group comprised of a holding company and any number of entities with at least 90 percent ownership in each (direct or indirect). Eligible taxpayers' group must be registered with tax authorities and meet certain conditions and criteria. The tax declaration can be submitted then by any member of the group. The Group prepares a consolidated tax return for the taxpayers's group including the Company and majority of its subsidiaries in Russia.

Deferred tax assets and liabilities are recognized on temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or when the tax loss carry forwards will be utilized. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilized.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes balances relate to the same taxation authority and the same taxable entity, consolidated tax group of entities or different taxable entities where there is an intention to settle the balances on a net basis. Deferred tax assets and liabilities are netted only with respect to individual companies of the Group (for companies outside the consolidated tax group of companies) and within the consolidated tax payers' group of companies.

The Group controls the reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains upon their disposal. The Group does not recognize deferred tax liabilities on such temporary differences except to the extent that management expects the temporary differences to reverse in the foreseeable future.

**Treasury shares.** Where any Group company purchases PAO NOVATEK's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to PAO NOVATEK shareholders until the shares are cancelled or reissued or disposed. Where such shares are subsequently reissued or disposed, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to PAO NOVATEK shareholders. Treasury shares are recorded at weighted average cost. Gains or losses resulting from subsequent sales of shares are recorded in the consolidated statement of changes in equity, net of associated costs including taxation.



**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Dividends.** Dividends are recognized as a liability and deducted from shareholders' equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed or declared after the balance sheet date but before the consolidated financial statements are authorized for issue.

**Revenue recognition.** Revenues represent the fair value of consideration received or receivable for the sale of goods and services in the normal course of business, net of discounts, export duties, value-added tax, excise and fuel taxes.

Revenues from oil and gas sales are recognized when control over such products has transferred to a customer, which refers to ability to direct the use of, and obtain substantially all of the remaining benefits from the products. The Group considers indicators of the transfer of control, which include, but are not limited to the following: the Group has a present right to payment for the products; the Group has transferred physical possession of the products; the customer has legal title to the products; the customer has the significant risks and rewards of ownership of the products; the customer has accepted the products. Not all of the indicators have to be met for management to conclude that control has transferred and revenue could be recognized. Management uses judgement to determine whether factors collectively indicate that the customer has obtained control over the products. Revenues from services are recognized in the period in which the services are rendered.

When the consideration includes a variable amount, minimum amounts must be recognized that are not at significant risk of reversal. If sales contract includes the variability associated with market price it represents a separated embedded derivative that is treated as part of revenue. Accordingly, at the date of sale the sales price is determined on a provisional basis, and the fair value of the final sales price adjustment is re-estimated continuously with changes in fair value recognized as an adjustment to revenue.

Trade receivables are recognized when the goods are transferred as this is the point in time that the consideration is unconditional and only the passage of time is required before the payment is due. No significant element of financing is deemed present as the sales are made with short-term credit terms consistent with market practice.

**General and administrative expenses.** General and administrative expenses represent overall corporate management and other expenses related to the general management and administration of the business unit as a whole. They include management and administrative compensation, legal and other advisory expenses, insurance of administrative buildings, social expenses and compensatory payments of general nature not directly linked to the Group's oil and gas activities, charity and other expenses necessary for the administration of the Group.

**Earnings per share.** Earnings per share are determined by dividing the profit or loss attributable to PAO NOVATEK shareholders by the weighted average number of shares outstanding during the reporting period.

**Consolidated statement of cash flows.** Cash and cash equivalents comprises cash on hand, cash deposits held with banks and short-term highly liquid investments which are readily convertible to known amounts of cash and which are not subject to significant risk of change in value and have an original maturity of three months or less.

The Group reports cash receipts and the repayments of short-term borrowings which have a maturity of three months or less on a net basis in the consolidated statement of cash flows.

**4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS**

Consolidated financial statements prepared in accordance with IFRS require management to make estimates which management reviews on a continuous basis, by reference to past experience and other factors considered as reasonable. Adjustments to accounting estimates and assumptions are recognized in the period in which the estimate is revised if the change affects only that period or in the period of the revision and subsequent periods, if both are affected. Management also makes certain judgments, apart from those involving estimations, in the process of applying the Group's accounting policies.

Judgments and estimates that have the most significant effect on the amounts reported in these consolidated financial statements are described below.

**4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)**

***Fair values of financial instruments.*** The fair value of financial assets and liabilities, other than financial instruments that are traded in active markets, is determined by applying various valuation methodologies. Management uses its judgment to make assumptions primarily based on market conditions existing at each reporting date.

Discounted cash flow analysis is used for loans and receivables as well as debt instruments that are not traded in active markets. The effective interest rate is determined by reference to the interest rates of financial instruments available to the Group in active markets. In the absence of such instruments, the effective interest rate is determined by reference to the interest rates of active market financial instruments available adjusted for the Group's specific risk premium estimated by management.

For commodity derivative contracts where observable information is not available, fair value estimations are determined using mark-to-market analysis and other acceptable valuation methods, for which the key inputs include future prices, volatility, price correlation, counterparty credit risk and market liquidity. Fair values of the Group's commodity derivative contracts and sensitivities are presented in Note 27.

Fair value estimation of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and free cash flows from the borrower's strategic plans approved by the shareholders of the joint ventures. Fair values of the shareholders' loans to joint ventures and sensitivities are presented in Note 27.

***Deferred income tax asset recognition.*** Management assesses deferred income tax assets at each reporting date and determines the amount recorded to the extent that realization of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimations based on prior years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

***Estimation of oil and gas reserves.*** Oil and gas reserves have a direct impact on certain amounts reported in the consolidated financial statements, most notably depreciation, depletion and amortization, as well as impairment expenses and asset retirement obligations. The Group's principal oil and gas reserves have been independently estimated by internationally recognized petroleum engineers whereas other oil and gas reserves of the Group have been determined based on estimates of mineral reserves prepared by the Group's management in accordance with internationally recognized definitions.

Depreciation rates on oil and gas assets using the unit-of-production method are based on proved developed reserves and total proved reserves estimated by the Group in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves. The Group also uses estimated probable and possible reserves to calculate future cash flows from oil and gas properties, which serve as an indicator in determining their economic lives and whether or not property impairment is present.

A portion of the reserves estimated by the Group includes reserves expected to be produced beyond license expiry dates. The Group's management believes that there is requisite legislation and past experience to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the current license expiry dates.

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, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans. In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As those fields are further developed, new information may lead to further revisions in reserve estimates.

**4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)**

***Impairment of investments in joint ventures and property, plant and equipment.*** Management assesses whether there are any indicators of possible impairment of investments in joint ventures and property, plant and equipment at each reporting date based on events or circumstances that indicate that the carrying value of assets may not be recoverable. Such indicators include changes in the Group's business plans, changes in commodity prices leading to unprofitable performances, changes in product mixes, and for oil and gas properties, significant downward revisions of estimated proved reserves. When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows.

***Impairment provision for trade receivables.*** The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators to determine that the receivables are potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates. When there is no expectation of recovering additional cash for an amount receivable, it is written off against the associated provision.

***Pension obligations.*** The costs of defined benefit pension plans and related current service costs are determined using actuarial valuations. The actuarial valuations involve making demographic assumptions (mortality rates, age of retirement, employee turnover and disability) as well as financial assumptions (discount rates, expected rates of return on assets, future salary and pension increases). Due to the long-term nature of these plans, such estimates are subject to significant uncertainty.

***Asset retirement obligations.*** The Group's exploration, development and production activities involve the use of wells, related equipment and operating sites, oil and gas gathering and treatment facilities and in-field pipelines. Generally, licenses and other regulatory acts require that such assets be decommissioned upon the completion of production, i.e. the Group is obliged to decommission wells, dismantle equipment, restore the sites and perform other related activities. The Group's estimates of these obligations are based on current regulatory or license requirements, as well as actual dismantling and related costs.

The Group's management believes that due to the limited history of gas and gas condensate processing plants activities, the useful lives of these assets are indeterminable (while certain of the operating components and equipment have definite useful lives). Because of these reasons, and the lack of clear legal requirements as to the recognition of obligations, the present value of an asset retirement obligation for such processing facilities cannot be reasonably estimated and, therefore, legal or contractual asset retirement obligations related to these assets are not recognized.

In accordance with the guidelines of IFRIC 1, *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, the amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the reporting date based on current legislation where the Group's respective operating assets are located, and is subject to change because of modifications, revisions and changes in laws and regulations and their interpretation thereof. Estimating future asset retirement obligations is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**5 ACQUISITIONS AND DISPOSALS*****Acquisition of AO Eurotek and AO South-Khadyryakhinskoye***

In December 2017, the Group acquired 100 percent ownership interests in AO Eurotek and AO South-Khadyryakhinskoye which held the licenses for exploration and production of hydrocarbons within the Syskonsyninskiy license area located in Khanty-Mansiysk Autonomous Region and the South-Khadyryakhinskiy license area located in YNAO, respectively, for total cash consideration of RR 5,412 million.

In accordance with IFRS 3, *Business Combinations*, the Group assessed fair values of the identified assets and liabilities of acquired companies at the acquisition date:

<i>AO Eurotek and AO South-Khadyryakhinskoye</i>	<b>Fair values at the acquisition date</b>
Property, plant and equipment	2,466
Deferred income tax assets	680
Cash and cash equivalents	2,701
Other current assets	101
Non-current liabilities	(375)
Trade payables and accrued liabilities	(161)
<b>Total identifiable net assets</b>	<b>5,412</b>
Purchase consideration	(5,412)
<b>Goodwill</b>	<b>-</b>

The financial and operational activities of the acquired companies would not have a material impact on the Group's revenues, if the acquisition had occurred in January 2017. The financial results of these companies after the acquisition date did not have a material impact on the Group's revenues and results for the year ended 31 December 2017.

***Acquisition of OOO Severneft-Urengoy***

In November 2017, the Group acquired a 100 percent ownership interest in OOO Severneft-Urengoy, an oil and gas company located in YNAO, for a cash consideration of RR 13,062 million. Severneft-Urengoy is a holder of the license for exploration and production of hydrocarbons within the West-Yaroyakhinsky license area.

In accordance with IFRS 3, *Business Combinations*, the Group assessed fair values of the identified assets and liabilities of OOO Severneft-Urengoy at the acquisition date:

<i>OOO Severneft-Urengoy</i>	<b>Fair values at the acquisition date</b>
Property, plant and equipment	14,252
Other non-current assets	140
Cash and cash equivalents	67
Other current assets	208
Deferred income tax liabilities	(858)
Other non-current liabilities	(145)
Current liabilities	(602)
<b>Total identifiable net assets</b>	<b>13,062</b>
Purchase consideration	(13,062)
<b>Goodwill</b>	<b>-</b>

## PAO NOVATEK

### Notes to the Consolidated Financial Statements

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

#### 5 ACQUISITIONS AND DISPOSALS (CONTINUED)

The financial and operational activities of Severneft-Urengoy would have increased the Group's revenues by an additional RR 6.3 billion, if the acquisition had occurred in January 2017. The financial results of this company after the acquisition date did not have a material impact on the Group's revenues and results for the year ended 31 December 2017.

##### *Acquisition of a participation interest in OOO Cryogas-Vysotsk*

In July 2017, NOVATEK acquired a 51 percent ownership interest in OOO Cryogas-Vysotsk for a cash consideration of RR 1,583 million. Cryogas-Vysotsk undertakes a project to construct the first train of a medium-scale plant for natural gas liquefaction with annual capacity of 660 thousand tons, located at the port of Vysotsk on the Baltic Sea.

The Charter of Cryogas-Vysotsk stipulates that key financial and operating decisions regarding its business activities are subject to unanimous approval by the Board of Directors. Consequently, the voting mechanism effectively establishes joint control over Cryogas-Vysotsk and the Group accounts for the investment under the equity method.

In accordance with IFRS 11, *Joint Arrangements*, the Group assessed fair values of the identified assets and liabilities of Cryogas-Vysotsk at the acquisition date:

<i>OOO Cryogas-Vysotsk</i>	<b>Fair values at the acquisition date</b>
Property, plant and equipment	15,804
Deferred income tax assets	111
Prepayments and other current assets	1,393
Cash and cash equivalents	447
Short-term debt	(13,199)
Other current liabilities	(1,453)
<b>Total identifiable net assets</b>	<b>3,103</b>
Purchase consideration	1,583
Fair value of the Group's interest in net assets (RR 3,103 million at 51 percent ownership)	(1,583)
<b>Goodwill</b>	<b>-</b>

##### *Acquisition of Blue Gaz Sp. z o.o.*

In December 2016, in order to expand activities on Polish market, the Group acquired a 100 percent participation interest in Blue Gaz Sp. z o.o. the owner of a regasification station in Poland, for total cash consideration of RR 26 million (PLN 2 million), which was paid by the end of 2016. The financial and operational activities of Blue Gaz Sp. z o.o. would not have a material impact on the Group's revenues and results for the year ended 31 December 2016 if the acquisition had occurred in January 2016.

##### *Acquisition of OOO Evrotek-Yuh*

In April 2016, the Group acquired a 100 percent participation interest equity stake in OOO Evrotek-Yuh for RR 6 million. Evrotek-Yuh was a holder of the license for exploration and production of hydrocarbons within the Ladertoyskiy license area located on the Gydan peninsula in YNAO. Evrotek-Yuh had no notable operating activities up to and as at the acquisition date and accordingly, this acquisition is outside the definition of "business" as defined in IFRS 3, *Business Combinations*. The acquisition cost has been fully allocated to the cost of the license.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**5 ACQUISITIONS AND DISPOSALS (CONTINUED)*****Disposal of an ownership interest in OAO Yamal LNG***

In December 2015, the Group and China's investment fund Silk Road Fund Co. Ltd., signed the Share Purchase Agreement on the disposal of a 9.9 percent equity stake in Yamal LNG, the Group's joint venture, to the fund. The transaction contained a set of conditions precedent and, in accordance with IFRS 5, *Non-current assets held for sale and discontinued operations*, the Group's 9.9 percent equity stake in Yamal LNG has been classified as an asset held for sale at 31 December 2015. The asset's carrying amount of RR 7,987 million was determined based on the net assets of Yamal LNG on the date of the agreement.

In March 2016, the transaction was closed upon the completion of the conditions precedent, and the Group recognized the disposal of the 9.9 percent equity stake in Yamal LNG. The transaction included a cash payment and the provision of a 15-year tenor loan to the Group for the purpose of financing the Yamal LNG project (see Note 14). Concurrently, the Group committed to provide cash contributions to the capital of Yamal LNG with regard to the interest disposed on the same terms that were previously applied upon the entrance of TOTAL S.A. and China National Petroleum Corporation into the project.

The following table summarizes the consideration details and shows the gain on the sale of the ownership interest in Yamal LNG:

	<b>RR million</b>
Cash payment received (EUR 1,087 million at exchange rate of 78.18 to EUR 1.00)	84,978
Adjustment to fair value at initial recognition of the loan from Silk Road Fund (see Note 14)	9,173
Less: 49.9 percent share in the Group's liability in relation to capital contributions to Yamal LNG <sup>(*)</sup> (USD 149 million at exchange rate of 70.15 to USD 1.00)	(10,458)
Less: carrying amount of the Group's disposed 9.9 percent interest in the equity investment previously classified as held for sale	(7,987)
Costs to sell	(2,634)
<b>Gain on the sale of ownership interest before income tax</b>	<b>73,072</b>

<sup>(\*)</sup> – excluding the Group's 50.1 percent share in Yamal LNG's capital increase as a result of these contributions.

Consequently, the Group recognized a gain on the transaction of RR 57,677 million, net of associated income tax of RR 15,395 million.

As a result of this transaction, the Group's interest in Yamal LNG is 50.1 percent. The Group continues to exercise joint control over Yamal LNG and recognizes it as a joint venture, and, accordingly, accounts for this investment under the equity method.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**6 PROPERTY, PLANT AND EQUIPMENT**

Movements in property, plant and equipment, for the reporting periods are as follows:

	Oil and gas properties and equipment	Assets under construction and advances for construction	Other	Total
Cost	348,268	64,778	15,195	428,241
Accumulated depreciation, depletion and amortization	(93,886)	-	(2,643)	(96,529)
<b>Net book value at 31 December 2015</b>	<b>254,382</b>	<b>64,778</b>	<b>12,552</b>	<b>331,712</b>
Additions	3,099	29,191	26	32,316
Transfers	58,674	(59,001)	327	-
Acquisition of subsidiaries	53	-	-	53
Changes in asset retirement costs	2,990	-	-	2,990
Depreciation, depletion and amortization	(33,836)	-	(522)	(34,358)
Disposals, net	(645)	(192)	(81)	(918)
Cost	412,352	34,776	15,402	462,530
Accumulated depreciation, depletion and amortization	(127,635)	-	(3,100)	(130,735)
<b>Net book value at 31 December 2016</b>	<b>284,717</b>	<b>34,776</b>	<b>12,302</b>	<b>331,795</b>
Effect of change in accounting policy (see Note 3)	16	-	240	256
Cost	412,368	34,776	15,642	462,786
Accumulated depreciation, depletion and amortization	(127,635)	-	(3,100)	(130,735)
<b>Net book value at 1 January 2017</b>	<b>284,733</b>	<b>34,776</b>	<b>12,542</b>	<b>332,051</b>
Additions	1,797	46,238	29	48,064
Transfers	42,740	(43,640)	900	-
Acquisition of subsidiaries (see Note 5)	14,873	1,756	89	16,718
Changes in asset retirement costs	(1,486)	-	-	(1,486)
Depreciation, depletion and amortization	(33,943)	-	(668)	(34,611)
Disposals, net	(371)	(207)	(27)	(605)
Currency translation differences	(99)	3	16	(80)
Cost	479,569	38,926	16,709	535,204
Accumulated depreciation, depletion and amortization	(171,325)	-	(3,828)	(175,153)
<b>Net book value at 31 December 2017</b>	<b>308,244</b>	<b>38,926</b>	<b>12,881</b>	<b>360,051</b>

Included in additions to property, plant and equipment for the years ended 31 December 2017 and 2016 are capitalized interest and foreign exchange differences of RR 3,827 million and RR 5,314 million, respectively.

Included within assets under construction and advances for construction are advances to suppliers for construction and equipment of RR 6,554 million and RR 1,438 million at 31 December 2017 and 2016, respectively.

In 2017, the Group purchased through auctions oil and gas exploration and production licenses for the Shtormovoy, the Gydanskiy, the Upper-Tiuteyskiy and the West-Seyakhinskiy license areas located in the YNAO for the total amount of RR 9,727 million, which were included in additions to oil and gas properties and equipment.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)**

In 2016, the Group purchased through auctions oil and gas exploration and production licenses for the Nyakhartinskiy and Syadorskiy license areas located in the YNAO and the Tanamskiy license area located in Krasnoyarsk Territory for the total amount of RR 1,928 million, which were included in additions to oil and gas properties and equipment.

The table below summarizes the Group's carrying values of total acquisition costs of proved and unproved properties included in oil and gas properties and equipment:

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Proved properties acquisition costs	58,951	47,243
Less accumulated depletion of proved properties acquisition costs	(18,001)	(16,782)
Unproved properties acquisition costs	11,376	10,069
<b>Total acquisition costs</b>	<b>52,326</b>	<b>40,530</b>

The Group's management believes these costs are recoverable as the Group has plans to explore and develop the respective fields.

Reconciliation of depreciation, depletion and amortization (DDA):

	<u>Year ended 31 December:</u>	
	<u>2017</u>	<u>2016</u>
Depreciation, depletion and amortization of property, plant and equipment	34,611	34,358
Add: DDA of intangible assets	639	554
Less: DDA capitalized in the course of intra-group construction services	(727)	(281)
<b>DDA as presented in the consolidated statement of income</b>	<b>34,523</b>	<b>34,631</b>

At 31 December 2017 and 2016, no property, plant and equipment were pledged as security for the Group's borrowings. No impairment was recognized in respect of oil and gas properties and equipment for the years ended 31 December 2017 and 2016.

Capital commitments are disclosed in Note 28.

**Leases.** Included in property, plant and equipment at 31 December 2017 are the right-of-use assets primarily related to long-term agreements on time chartering of marine tankers. Movements in the carrying amounts of the right-of-use assets for the reporting period are as follows:

	<u>At 31 December 2016</u>	<u>At 1 January 2017<sup>(*)</sup></u>	<u>Additions</u>	<u>Depreciation</u>	<u>Other movements</u>	<u>At 31 December 2017</u>
Oil and gas properties and equipment	-	16	7,123	(375)	(130)	6,634
Other	-	240	500	(129)	-	611
<b>Total net book value</b>	<b>-</b>	<b>256</b>	<b>7,623</b>	<b>(504)</b>	<b>(130)</b>	<b>7,245</b>

<sup>(\*)</sup> – effect of initial application of IFRS 16, *Leases*, recognized at 1 January 2017 (see Note 3).



**PAO NOVATEK****Notes to the Consolidated Financial Statements**

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**6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)**

The maturity analysis of lease liabilities is disclosed in Note 27.

*Exploration for and evaluation of mineral resources.* The amounts of assets, liabilities, expense and cash flows arising from the exploration and evaluation of mineral resources comprise the following:

	Year ended 31 December:	
	2017	2016
<b>Net book value of assets at 1 January</b>	<b>15,472</b>	<b>14,744</b>
Additions	6,345	5,297
Expensed	-	(3)
Acquisition of subsidiaries	834	7
Reclassification to proved properties and development expenditures	(4,846)	(4,573)
<b>Net book value of assets at 31 December</b>	<b>17,805</b>	<b>15,472</b>
Liabilities	689	384
Cash flows used for operating activities	1,819	1,891
Cash flows used for investing activities	5,749	4,085

For the years ended 31 December 2017 and 2016, within operating expenses the Group has recognized exploration expenses in the amount of RR 1,819 million and RR 2,087 million, respectively. These expenses included employee compensations in the amount of RR 301 million and RR 300 million, respectively.

**7 INVESTMENTS IN JOINT VENTURES**

	At 31 December 2017	At 31 December 2016
<i>Joint ventures:</i>		
OAo Yamal LNG	126,377	126,688
OOO Yamal Development	73,873	55,228
ZAO Nortgas	50,519	51,222
OOO SeverEnergiya (through Artic Russia B.V. at 31 December 2016)	27,666	24,449
OOO Cryogas-Vysotsk	3,841	-
ZAO Terneftegas	3,050	2,063
<b>Total investments in joint ventures</b>	<b>285,326</b>	<b>259,650</b>

The Group considers that Yamal LNG, Yamal Development, Nortgas, SeverEnergiya, Artic Russia, Cryogas-Vysotsk and Terneftegas constitute jointly controlled entities on the basis of the existing contractual arrangements. The Charters and Shareholders' agreements of these entities stipulate that strategic and/or key decisions of a financial, operating and capital nature require effectively the unanimous approval by all participants or by a group of participants. The Group accounts for its shares in joint ventures under the equity method.

*OAo Yamal LNG.* The Group holds a 50.1 percent ownership in Yamal LNG, along with TOTAL S.A. (20 percent), China National Petroleum Corporation ("CNPC", 20 percent) and Silk Road Fund Co. Ltd. (9.9 percent). The joint venture is responsible for implementing the Yamal LNG project including the construction of production facilities for natural gas, gas condensate and liquefied natural gas based on the resources of the South-Tambeyskoye field, located on the Yamal peninsula in the YNAO. Yamal LNG is the holder of the LNG export license. In December 2017, Yamal LNG started production on the first train of the LNG Plant and commenced LNG deliveries to international markets.

At 31 December 2017 and 2016, the Group's 50.1 percent ownership in Yamal LNG was pledged in connection with credit line facility agreements signed by Yamal LNG with a number of Russian and foreign banks to obtain external project financing.

## PAO NOVATEK

### Notes to the Consolidated Financial Statements

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

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#### 7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

**ZAO Nortgas.** The Group holds a 50 percent ownership in Nortgas, its joint venture with PAO Gazprom Neft. Nortgas operates the North-Urengoykoye field, located in the YNAO.

**OOO SeverEnergiya, Artic Russia B.V. and OOO Yamal Development.** SeverEnergiya through its wholly owned subsidiary AO Arcticgas operates the Samburgskoye, Urengoykoye and Yaro-Yakhinskoye fields, located in the YNAO.

At 31 December 2016, the Group held an effective 53.3 percent participation interest in SeverEnergiya through two of the Group's other joint ventures, Artic Russia and Yamal Development. Artic Russia was owned by the Group (a 13.6 percent participation interest) and Yamal Development (an 86.4 percent participation interest). Yamal Development was a joint venture of the Group and PAO Gazprom Neft with a 50 percent participation interest held by each investor. Artic Russia and Yamal Development held direct 49 and 51 percent participating interests, respectively, in SeverEnergiya.

In June 2017, as part of the restructuring procedures to simplify the ownership structure in SeverEnergiya and Arcticgas and to eventually achieve parity shareholdings by the Group and Gazprom Neft, Artic Russia was liquidated, and its assets and liabilities were distributed between its shareholders. As a result, the Group obtained a direct 6.7 percent participation interest in SeverEnergiya, and Yamal Development's direct participation interest in SeverEnergiya increased from 51 to 93.3 percent. The Group's effective participation interest in SeverEnergiya did not change and was 53.3 percent at 31 December 2017.

Subsequent to the reporting date, in January 2018, Yamal Development and SeverEnergiya were merged with Arcticgas. As a result, the Group and Gazprom Neft obtained direct participation interests in Arcticgas, 53.3 percent and 46.7 percent, respectively. The Group's management expects that further steps to achieve parity shareholdings in Arcticgas will be undertaken in the nearest future.

**ZAO Terneftegas.** The Group holds a 51 percent ownership in Terneftegas, its joint venture with TOTAL S.A. (49 percent). Terneftegas operates the Termokarstovoye field, located in the YNAO.

**OOO Cryogas-Vysotsk.** The Group holds a 51 percent ownership interest in Cryogas-Vysotsk acquired in July 2017 (see Note 5). Cryogas-Vysotsk is a joint venture with AO Gazprombank group (49 percent). The joint venture is carrying out a project for construction of the first train of a medium-scale plant for natural gas liquefaction with annual capacity of 660 thousand tons, located at the port of Vysotsk on the Baltic Sea.

At 31 December 2017, the Group's 51 percent ownership interest in Cryogas-Vysotsk was pledged in connection with credit line facility agreements signed by the joint venture with a Russian bank to obtain external project financing.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

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**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

The table below summarizes the movements in the carrying amounts of the Group's joint ventures:

	Year ended 31 December:	
	2017	2016
<b>At 1 January</b>	<b>259,650</b>	<b>154,725</b>
Share of profit from operations	39,854	33,655
Share of finance income (expense)	(10,297)	74,236
Share of total income tax benefit (expense)	(7,127)	(17,052)
<b>Share of profit (loss) of joint ventures, net of income tax</b>	<b>22,430</b>	<b>90,839</b>
Share of other comprehensive loss of joint ventures	(79)	(21)
Acquisitions of joint ventures (see Note 5)	1,583	-
Group's costs capitalized in investments	1,328	753
Contributions to equity	2,269	9,802
Dividends received from joint ventures	(2,383)	-
Effect from initial measurement of loans provided by the Group to joint ventures (see Note 27)	-	836
Effect from other changes in joint ventures' net assets	-	2,819
Elimination of the Group's share in profits of joint ventures from hydrocarbons balances purchased by the Group from joint ventures and not sold at the reporting date	528	(103)
<b>At 31 December</b>	<b>285,326</b>	<b>259,650</b>

For the years ended 31 December 2017 and 2016, the Group recorded commission fees in the amount of RR 1,328 million and RR 753 million, respectively, for the guarantee received from the State Corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank)" (see Note 28) as an increase to the investment in Yamal LNG.

In October 2017, the capital of Cryogas-Vysotsk was increased through proportional contributions by its participants totalling RR 4,449 million, of which RR 2,269 million was contributed by NOVATEK.

In September 2016, the capital of Yamal LNG was increased through a cash contribution made by the Group as a result of the disposal of the 9.9 percent stake in Yamal LNG (see Note 5) in the amount of RR 19,565 million. The Group's 50.1 percent share in Yamal LNG's capital increase was recorded in the Group's investment in Yamal LNG in the amount of RR 9,802 million. The Group's shareholding in Yamal LNG did not change notably as a result of this capital contribution.

For the year ended 31 December 2017, Nortgas declared dividends in the total amount of RR 4,766 million, of which RR 2,383 million were attributable to NOVATEK.

For the year ended 31 December 2016, the Group recorded an increase in equity in the amount of RR 2,819 million from the initial measurement of the disproportional loans provided to Yamal LNG by other shareholders.

The Group eliminates its share in profits of joint ventures from natural gas and liquid hydrocarbons balances purchased by the Group from its joint ventures and not sold at the reporting date.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

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**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

The summarized statements of financial position for the Group's principal joint ventures are as follows:

<i>At 31 December 2017</i>	<b>Yamal LNG</b>	<b>SeverEnergia</b>	<b>Nortgas</b>
Property, plant and equipment and materials for construction	1,741,465	380,715	135,180
Other non-current non-financial assets	391	276	44
Non-current financial assets	-	155,527	12,226
<b>Total non-current assets</b>	<b>1,741,856</b>	<b>536,518</b>	<b>147,450</b>
Cash and cash equivalents	29,297	8,658	1,409
Other current financial assets	19,793	17,484	2,550
Current non-financial assets	16,994	948	321
<b>Total current assets</b>	<b>66,084</b>	<b>27,090</b>	<b>4,280</b>
Non-current financial liabilities	(1,484,498)	(101,936)	(20,970)
Non-current non-financial liabilities	(38,705)	(56,873)	(23,149)
<b>Total non-current liabilities</b>	<b>(1,523,203)</b>	<b>(158,809)</b>	<b>(44,119)</b>
Trade payables and accrued liabilities	(26,946)	(16,892)	(693)
Other current financial liabilities	(5,294)	(29,647)	(3,881)
Current non-financial liabilities	(112)	(12,948)	(2,000)
<b>Total current liabilities</b>	<b>(32,352)</b>	<b>(59,487)</b>	<b>(6,574)</b>
<b>Net assets</b>	<b>252,385</b>	<b>345,312</b>	<b>101,037</b>
<i>At 31 December 2016</i>			
Property, plant and equipment and materials for construction	1,265,939	385,404	138,768
Other non-current non-financial assets	273	278	47
Non-current financial assets	6,061	120,655	11,213
<b>Total non-current assets</b>	<b>1,272,273</b>	<b>506,337</b>	<b>150,028</b>
Cash and cash equivalents	12,842	13,517	277
Other current financial assets	23,211	15,520	2,639
Current non-financial assets	14,314	1,013	631
<b>Total current assets</b>	<b>50,367</b>	<b>30,050</b>	<b>3,547</b>
Non-current financial liabilities	(1,016,196)	(130,872)	(24,795)
Non-current non-financial liabilities	(35,798)	(57,555)	(23,544)
<b>Total non-current liabilities</b>	<b>(1,051,994)</b>	<b>(188,427)</b>	<b>(48,339)</b>
Trade payables and accrued liabilities	(17,628)	(14,308)	(1,302)
Other current financial liabilities	-	(29,355)	-
Current non-financial liabilities	(148)	(11,669)	(1,490)
<b>Total current liabilities</b>	<b>(17,776)</b>	<b>(55,332)</b>	<b>(2,792)</b>
<b>Net assets</b>	<b>252,870</b>	<b>292,628</b>	<b>102,444</b>

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(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

The summarized statements of comprehensive income (loss) of the Group's principal joint ventures are presented below:

<i>For the year ended 31 December 2017</i>	<b>Yamal LNG</b>	<b>SeverEnergia</b>	<b>Nortgas</b>
Revenue	3,613	147,207	23,087
Depreciation, depletion and amortization	(895)	(22,903)	(6,914)
Profit from operations	528	66,734	5,581
Change in fair value of non-commodity financial instruments	27,110	-	-
Foreign exchange gain (loss), net	(26,089)	1	-
Profit before income tax	1,505	63,232	4,400
Income tax expense	(4,589)	(10,482)	(950)
<b>Profit (loss), net of income tax</b>	<b>(3,084)</b>	<b>52,750</b>	<b>3,450</b>
Other comprehensive loss	(94)	(66)	(91)
<b>Total comprehensive income (loss)</b>	<b>(3,178)</b>	<b>52,684</b>	<b>3,359</b>
<i>For the year ended 31 December 2016</i>			
Revenue	2,722	133,229	25,697
Depreciation, depletion and amortization	(650)	(26,451)	(7,749)
Profit from operations	670	55,585	4,368
Change in fair value of non-commodity financial instruments	(25,223)	-	-
Foreign exchange gain (loss), net	200,485	25	-
Profit before income tax	176,043	47,806	2,436
Income tax expense	(28,952)	(7,930)	(574)
<b>Profit, net of income tax</b>	<b>147,091</b>	<b>39,876</b>	<b>1,862</b>
Other comprehensive loss	(27)	(23)	(14)
<b>Total comprehensive income</b>	<b>147,064</b>	<b>39,853</b>	<b>1,848</b>

The information above reflects the amounts presented in the financial statements of the joint ventures adjusted for differences in accounting policies between the Group and the joint ventures.

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(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

Reconciliation of the summarized financial information presented to the Group's share in net assets of the joint ventures:

<i>As at and for the year ended 31 December 2017</i>	<b>Yamal LNG</b>	<b>SeverEnergia</b>	<b>Nortgas</b>
<b>Net assets at 1 January 2017</b>	<b>252,870</b>	<b>292,628</b>	<b>102,444</b>
Profit (loss), net of income tax	(3,084)	52,750	3,450
Other comprehensive loss	(94)	(66)	(91)
Other equity movements	2,693	-	-
Dividends	-	-	(4,766)
<b>Net assets at 31 December 2017</b>	<b>252,385</b>	<b>345,312</b>	<b>101,037</b>
Ownership	50.1%	53.3%	50%
<b>Group's share in net assets</b>	<b>126,377</b>	<b>184,155</b>	<b>50,519</b>
<i>As at and for the year ended 31 December 2016</i>			
<b>Net assets at 1 January 2016</b>	<b>77,442</b>	<b>252,775</b>	<b>100,596</b>
Profit, net of income tax	147,091	39,876	1,862
Other comprehensive loss	(27)	(23)	(14)
Other equity movements	28,364	-	-
<b>Net assets at 31 December 2016</b>	<b>252,870</b>	<b>292,628</b>	<b>102,444</b>
Ownership	50.1%	53.3%	50%
<b>Group's share in net assets</b>	<b>126,688</b>	<b>156,059</b>	<b>51,222</b>

At 31 December 2017 and 2016, the Group's cumulative investments in SeverEnergia and Yamal Development totaled RR 101,539 million and RR 79,677 million, respectively, which differed from the Group's share in the net assets of SeverEnergia. The differences of RR 82,616 million and RR 76,382 million mainly related to the Group's interest in debt liabilities of Yamal Development, through which the Group held indirect interests in SeverEnergia.

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**8 LONG-TERM LOANS AND RECEIVABLES**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Long-term loans	183,233	184,621
Long-term interest receivable	29,130	24,390
Other long-term receivables	429	442
<b>Total</b>	<b>212,792</b>	<b>209,453</b>
Less: current portion of long-term loans	(891)	(308)
<b>Total long-term loans and receivables</b>	<b>211,901</b>	<b>209,145</b>

The Group's long-term loans by borrowers are as follows:

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
OAo Yamal LNG	175,568	173,845
OOO Cryogas-Vysotsk	5,211	-
ZAO Terneftegas	2,454	3,201
OOO Yamal Development	-	7,575
<b>Total long-term loans</b>	<b>183,233</b>	<b>184,621</b>

**OAo Yamal LNG.** In accordance with the Shareholders' agreement, the Group provided US dollar and Euro credit line facilities to Yamal LNG, the Group's joint venture. The loans interest rate is set based on market interest rates and interest rates on borrowings of shareholders. The repayment schedule is linked to free cash flows of the joint venture.

**OOO Cryogas-Vysotsk.** The Group provided Russian rouble denominated loans under agreed credit line facilities to Cryogas-Vysotsk, the Group's joint venture. The loans are repayable not later than 2033 and bear variable interest rates.

**OOO Yamal Development.** The Group provided Russian rouble denominated loans under agreed credit line facilities to Yamal Development, the Group's joint venture. In 2017, the loans and accrued interest were fully repaid to the Group ahead of the maturity schedule.

**ZAO Terneftegas.** In accordance with the Shareholders' agreement, the Group provided US dollar denominated loans to Terneftegas, the Group's joint venture. The loans interest rate is set based on market interest rates and interest rates on borrowings of shareholders. The repayment schedule is linked to free cash flows of the joint venture.

During 2017, Terneftegas repaid to the Group a part of the loans and accrued interest in the total amount of RR 910 million.

No provisions for impairment of long-term loans and receivables were recognized at 31 December 2017 and 31 December 2016. The carrying values of long-term loans and receivables approximate their respective fair values.

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(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**9 OTHER NON-CURRENT ASSETS**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
<i>Financial assets</i>		
Commodity derivatives	1,705	1,172
Other financial assets	10	13
<i>Non-financial assets</i>		
Long-term advances	20,228	20,882
Deferred income tax assets	6,898	4,671
Materials for construction	2,694	2,004
Intangible assets, net	1,665	1,510
Other non-financial assets	248	232
<b>Total other non-current assets</b>	<b>33,448</b>	<b>30,484</b>

At 31 December 2017 and 2016, the long-term advances represented advances to OAO Russian Railways. The advances were paid in accordance with the Strategic Partnership Agreement signed with Russian Railways in 2012.

**10 INVENTORIES**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Natural gas and liquid hydrocarbons	8,711	6,765
Materials and supplies (net of provision of RR 4 million at 31 December 2017 and 2016)	2,337	2,247
Other inventories	36	32
<b>Total inventories</b>	<b>11,084</b>	<b>9,044</b>

No inventories were pledged as security for the Group's borrowings or payables at both dates.

**11 TRADE AND OTHER RECEIVABLES**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Trade receivables (net of provision of RR 284 million and RR 196 million at 31 December 2017 and 2016, respectively)	43,387	40,606
Other receivables (net of provision of RR 19 million and RR 22 million at 31 December 2017 and 2016, respectively)	1,116	980
<b>Total trade and other receivables</b>	<b>44,503</b>	<b>41,586</b>

Trade receivables in the amount RR 8,921 million and RR 5,362 million at 31 December 2017 and 2016, respectively, are secured by letters of credit, issued by banks with investment grade rating. The Group does not hold any other collateral as security for trade and other receivables (see Note 27 for credit risk disclosures).

The carrying values of trade and other receivables approximate their respective fair values. Trade and other receivables were categorized as Level 3 in the fair value measurement hierarchy described in Note 27.

Trade and other receivables that are less than three months past due are generally not considered for impairment unless other indicators of impairment exist. Trade and other receivables of RR 3,357 million and RR 4,269 million at 31 December 2017 and 2016, respectively, were past due but not impaired. The Group has assessed the payment history of these accounts and recognized impairment where deemed necessary.



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**11 TRADE AND OTHER RECEIVABLES (CONTINUED)**

The ageing analysis of these past due but not impaired trade and other receivables is as follows:

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Up to 90 days past-due	2,544	3,628
91 to 360 days past-due	669	561
Over 360 days past-due	144	80
<b>Total past due but not impaired</b>	<b>3,357</b>	<b>4,269</b>
Not past due and not impaired	41,146	37,317
<b>Total trade and other receivables</b>	<b>44,503</b>	<b>41,586</b>

Movements in the Group provision for impairment of trade and other receivables are as follows:

	<u>Year ended 31 December:</u>	
	<u>2017</u>	<u>2016</u>
<b>At 1 January</b>	<b>218</b>	<b>113</b>
Additional provision recorded	58	269
Acquisition of subsidiaries	55	-
Receivables written off as uncollectible	(21)	(68)
Provision reversed	(7)	(96)
<b>At 31 December</b>	<b>303</b>	<b>218</b>

The provision for impaired trade and other receivables has been included in the consolidated statement of income in net impairment expenses.

**12 PREPAYMENTS AND OTHER CURRENT ASSETS**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
<i>Financial assets</i>		
Commodity derivatives	2,117	2,920
Current portion of long-term loans receivable (see Note 8)	891	308
<i>Non-financial assets</i>		
Value-added tax receivable	8,057	10,456
Recoverable value-added tax	7,284	5,736
Prepayments and advances to suppliers	6,326	5,998
Deferred transportation expenses for liquid hydrocarbons	2,140	1,903
Deferred transportation expenses for natural gas	1,965	1,901
Deferred export duties for liquid hydrocarbons	1,829	1,643
Prepaid customs duties	561	1,756
Other non-financial assets	693	627
<b>Total prepayments and other current assets</b>	<b>31,863</b>	<b>33,248</b>

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(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**13 CASH AND CASH EQUIVALENTS**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Cash at current bank accounts	28,994	31,525
Bank deposits with original maturity of three months or less	36,949	16,776
<b>Total cash and cash equivalents</b>	<b>65,943</b>	<b>48,301</b>

All deposits are readily convertible to known amounts of cash and are not subject to significant risk of change in value (see Note 27 for credit risk disclosures).

**14 LONG-TERM DEBT**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
<i>Corporate bonds</i>		
Eurobonds – Ten-Year Tenor (par value USD 1 billion, repayable in 2022)	57,481	60,503
Eurobonds – Ten-Year Tenor (par value USD 650 million, repayable in 2021)	37,364	39,318
Eurobonds – Four-Year Tenor (par value RR 14 billion, repaid in 2017)	-	13,996
<i>Bank loans</i>		
Syndicated term credit line facility	13,280	41,906
Other bank loans	6,887	6,381
<i>Other borrowings</i>		
Loan from Silk Road Fund	39,716	41,125
Other loans	1,022	13,536
<b>Total</b>	<b>155,750</b>	<b>216,765</b>
Less: current portion of long-term debt	(14,302)	(55,469)
<b>Total long-term debt</b>	<b>141,448</b>	<b>161,296</b>

**Eurobonds.** In December 2012, the Group issued US dollar denominated Eurobonds in the amount of USD 1 billion. The US dollar denominated Eurobonds were issued with an annual coupon rate of 4.422 percent, payable semi-annually. The Eurobonds have a ten-year tenor and are repayable in December 2022.

In February 2011, the Group issued US dollar denominated Eurobonds in the amount of USD 650 million. The US dollar denominated Eurobonds were issued with an annual coupon rate of 6.604 percent, payable semi-annually. The Eurobonds have a ten-year tenor and are repayable in February 2021.

In February 2013, the Group issued four-year tenor Russian rouble denominated Eurobonds in the amount of RR 14 billion. The Russian rouble denominated Eurobonds were issued with an annual coupon rate of 7.75 percent, payable semi-annually. In February 2017, the RR 14 billion Eurobonds were fully repaid at its maturity date.

**Syndicated term credit line facility.** In June 2013, the Group obtained a USD 1.5 billion unsecured syndicated term credit line facility from a range of international banks and withdrew the full amount under the facility by June 2014. The loan was repayable until July 2018 by quarterly equal installments starting from June 2015. The facility included the maintenance of certain restrictive financial covenants. In February 2018, the credit line facility was fully repaid ahead of its maturity schedule.

## PAO NOVATEK

### Notes to the Consolidated Financial Statements

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#### 14 LONG-TERM DEBT (CONTINUED)

**Other bank loans.** In December 2016, the Group obtained a EUR 100 million credit line facility from the Russian subsidiary of a foreign bank which is repayable in December 2019. The facility includes the maintenance of certain restrictive financial covenants.

**Loan from Silk Road Fund.** As part of the transaction for the sale of the Group's 9.9 percent equity stake in OAO Yamal LNG in December 2015, the Group obtained a loan from Silk Road Fund for financing of the Yamal LNG project (see Note 5).

The loan is repayable until December 2030 by semi-annual equal installments starting from December 2019 and includes the maintenance of certain restrictive financial covenants.

**Other loans.** At 31 December 2017 and 2016, other loans represented Russian rouble denominated loans, which were provided to one of the Group's subsidiaries by its non-controlling shareholder. The loans were initially repayable until the end of 2017, which was subsequently extended to the end of 2018. During the years ended 31 December 2017 and 2016, a portion of the loans and accrued interest in the amount of RR 13,375 million and 8,673 million, respectively, was repaid.

The fair value of long-term debt including its current portion was RR 167,760 million and RR 224,183 million at 31 December 2017 and 2016, respectively. The fair value of the corporate bonds was determined based on market quote prices (Level 1 in the fair value measurement hierarchy described in Note 27). The fair value of other long-term loans was determined based on future cash flows discounted at the estimated risk-adjusted discount rate (Level 3 in the fair value measurement hierarchy described in Note 27).

Scheduled maturities of long-term debt at the reporting date were as follows:

<i>Maturity period:</i>	<b>At 31 December 2017</b>
1 January 2019 to 31 December 2019	8,614
1 January 2020 to 31 December 2020	3,453
1 January 2021 to 31 December 2021	40,816
1 January 2022 to 31 December 2022	60,937
After 31 December 2022	27,628
<b>Total long-term debt</b>	<b>141,448</b>

**Available credit line facilities.** At 31 December 2017, the Group had available long-term credit line facilities from banks with credit limits in the amounts of RR 100 billion, the equivalent of USD 750 million, and EUR 50 million. The facilities include the maintenance of certain restrictive financial covenants.

#### 15 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT

At 31 December 2017 and 2016, short-term debt and current portion of long-term debt consisted only of the current portion of long-term debt in the amount of RR 14,302 million and RR 55,469 million, respectively.

**Loans with original maturity three months or less.** In 2017 and 2016, the Group had available revolving credit line facilities under which the obtained loans with original maturities of three months or less to finance trade activities were secured by cash revenues from specifically determined liquid hydrocarbons export sales contracts. At 31 December 2017 and 2016, these loans were repaid.

**Available credit line facilities.** At 31 December 2017, the Group had available a short-term revolving credit line facility from a Russian bank, with a credit limit in the amount of RR 20 billion.

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**16 PENSION OBLIGATIONS**

**Defined contribution plan.** For the years ended 31 December 2017 and 2016, total amounts recognized as an expense in respect of payments made by employer on behalf of employees to the Pension Fund of the Russian Federation were RR 2,111 million and RR 1,853 million, respectively.

**Defined benefit plan.** The Group operates a post-employment benefit program for its retired employees. Under the current terms of pension program, employees who are employed by the Group for more than five years and retire from the Group on or after the statutory retirement age will receive lump sum retirement benefit and monthly payments from NOVATEK for life unless they are actively employed. The amounts of payments to be disbursed depend on the employee's average salary, duration and location of employment.

The program represents an unfunded defined benefit plan and is accounted for as such under provisions of IAS 19, *Employee Benefits*. The present value of the defined benefit obligation is included in other non-current liabilities in the consolidated statement of financial position. The impact of the program on the consolidated financial statements is disclosed below.

The movements in the present value of the defined benefit obligation are as follows:

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<b>At 1 January</b>	<b>2,249</b>	<b>1,905</b>
Interest cost	197	201
Current service cost	181	126
Benefits paid	(118)	(105)
Pension plan revision	(35)	-
Actuarial remeasurement arising from:		
- changes in financial assumptions	345	110
- changes in demographic assumptions	122	(24)
- experience adjustments	257	36
<b>At 31 December</b>	<b>3,198</b>	<b>2,249</b>
<i>Defined benefit plan (benefits) costs were recognized in:</i>		
Materials, services and other (as employee compensation)	225	184
General and administrative expenses (as employee compensation)	153	143
Other operating income (loss)	(35)	-
Other comprehensive loss	724	122

The principal actuarial assumptions used are as follows:

	<b>At 31 December 2017</b>	<b>At 31 December 2016</b>
Weighted average discount rate	6.9%	8.3%
Projected annual increase in employee compensation	4.0%	5.0%
Expected increases to pension benefits	4.3%	6.5%

The discount rate was determined by reference to Russian rouble denominated bonds issued by the Government of the Russian Federation chosen to match the duration of the post-employment benefit obligations. The assumed average salary and pension payment increases for Group employees have been calculated on the basis of inflation forecasts, analysis of increases of past salaries and the general salary policy of the Group. Mortality assumptions are based on the Russian mortality tables published by the State Statistics Committee of the Russian Federation from the year 2010 adjusted for estimates of mortality improvements in the future periods, which management believes are the most conservative and prudent Russian whole-population mortality tables available.

Management has assessed that reasonable changes in the principal significant actuarial assumptions will not have a significant impact on the consolidated statement of income or the consolidated statement of comprehensive income or the liability recognized in the consolidated statement of financial position.

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**17 TRADE PAYABLES AND ACCRUED LIABILITIES**

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
<i>Financial liabilities</i>		
Trade payables	30,936	25,828
Commodity derivatives	3,333	2,754
Dividends payable to non-controlling interest	1,633	-
Interest payable	1,221	1,821
Other payables	775	463
<i>Non-financial liabilities</i>		
Advances from customers	4,474	2,483
Salary payables	472	338
Other liabilities and accruals	6,157	4,775
<b>Total trade payables and accrued liabilities</b>	<b>49,001</b>	<b>38,462</b>

The carrying values of trade payables and accrued liabilities approximate their respective fair values. Trade and other payables were categorized as Level 3 in the fair value measurement hierarchy described in Note 27.

During the years ended 31 December 2017 and 2016, advances from customers in the amount of RR 2,422 million and RR 3,952 million, respectively, remained at the beginning of the respective period were recognized as revenue.

**18 SHAREHOLDERS' EQUITY**

*Ordinary share capital.* Share capital issued and paid in consisted of 3,036,306,000 ordinary shares with a par value of RR 0.1 each at 31 December 2017 and 2016. The total authorized number of ordinary shares was 10,593,682,000 shares at both dates.

*Treasury shares.* In accordance with the *Share Buyback Programs* authorized by the Board of Directors, the Group's wholly owned subsidiary, Novatek Equity (Cyprus) Limited, purchases ordinary shares of PAO NOVATEK in the form of Global Depository Receipts (GDRs) on the London Stock Exchange (LSE) and ordinary shares on the Moscow Exchange through the use of independent brokers. NOVATEK also purchases its ordinary shares from shareholders where required by Russian legislation.

During the years ended 31 December 2017 and 2016, the Group purchased 2.1 million and 1.4 million ordinary shares (both ordinary shares and GDRs) at a total cost of RR 1,440 million and RR 916 million, respectively. At 31 December 2017 and 2016, the Group held in total (both ordinary shares and GDRs) 20.7 million and 18.6 million ordinary shares at a total cost of RR 8,353 million and RR 6,913 million, respectively. The Group has decided that these shares do not vote.

*Dividends.* Dividends (including tax on dividends) declared and paid were as follows:

	<u>Year ended 31 December:</u>	
	<u>2017</u>	<u>2016</u>
Dividends payable at 1 January	1	1
Dividends declared (*)	42,075	41,653
Dividends paid (*)	(42,075)	(41,653)
<b>Dividends payable at 31 December</b>	<b>1</b>	<b>1</b>
Dividends per share declared during the year (in Russian roubles)	13.95	13.80
Dividends per GDR declared during the year (in Russian roubles)	139.50	138.00

(\*) – excluding treasury shares.

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**18 SHAREHOLDERS' EQUITY (CONTINUED)**

The Group declares and pays dividends in Russian roubles. Dividends declared in 2017 and 2016 were as follows:

Final for 2016: RR 7.00 per share or RR 70.00 per GDR declared in April 2017	21,254
Interim for 2017: RR 6.95 per share or RR 69.50 per GDR declared in September 2017	21,102

<b>Total dividends declared in 2017</b>	<b>42,356</b>
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Final for 2015: RR 6.90 per share or RR 69.00 per GDR declared in April 2016	20,951
Interim for 2016: RR 6.90 per share or RR 69.00 per GDR declared in September 2016	20,951

<b>Total dividends declared in 2016</b>	<b>41,902</b>
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*Distributable retained earnings.* The basis for distribution of profits of a company to shareholders is defined by Russian legislation as net profit presented in its statutory financial statements prepared in accordance with the Regulations on Accounting and Reporting of the Russian Federation, which may differ significantly from amounts calculated on the basis of IFRS. At 31 December 2017 and 2016, NOVATEK's closing balances of the accumulated profit including the respective year's net statutory profit totaled RR 445,104 million and RR 366,928 million, respectively.

**19 OIL AND GAS SALES**

	Year ended 31 December:	
	2017	2016
Natural gas	247,663	229,716
Naphtha	111,979	103,103
Crude oil	77,102	64,952
Other gas and gas condensate refined products	69,066	57,163
Liquefied petroleum gas	40,016	31,652
Stable gas condensate	33,993	47,271
<b>Total oil and gas sales</b>	<b>579,819</b>	<b>533,857</b>

**20 PURCHASES OF NATURAL GAS AND LIQUID HYDROCARBONS**

	Year ended 31 December:	
	2017	2016
Unstable gas condensate	107,082	93,854
Natural gas	51,053	38,119
Other liquid hydrocarbons	3,308	2,295
<b>Total purchases of natural gas and liquid hydrocarbons</b>	<b>161,443</b>	<b>134,268</b>

The Group purchases not less than 50 percent of the natural gas volumes produced by its joint venture ZAO Nortgas, some volumes of natural gas produced by its joint venture OOO SeverEnergiya (through its wholly owned subsidiary, AO Arcticgas), all volumes of natural gas produced by its joint venture ZAO Terneftegas and, commencing December 2017, some volumes of liquefied natural gas produced by its joint venture OAO Yamal LNG (see Note 30).

The Group purchases all volumes of unstable gas condensate produced by its joint ventures Nortgas, SeverEnergiya (through its wholly owned subsidiary, Arcticgas) and Terneftegas at ex-field prices based on benchmark reference crude oil prices (see Note 30).

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**21 TRANSPORTATION EXPENSES**

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Natural gas transportation by trunk and low-pressure pipelines	93,686	84,808
Stable gas condensate and liquefied petroleum gas transportation by rail	29,832	31,838
Crude oil transportation by trunk pipelines	7,622	6,654
Gas condensate refined products, stable gas condensate and crude oil transportation by tankers	5,980	9,997
Other	72	165
<b>Total transportation expenses</b>	<b>137,192</b>	<b>133,462</b>

**22 TAXES OTHER THAN INCOME TAX**

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

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Unified natural resources production tax	45,459	40,997
Property tax	3,673	2,793
Other taxes	362	263
<b>Total taxes other than income tax</b>	<b>49,494</b>	<b>44,053</b>

**23 MATERIALS, SERVICES AND OTHER**

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Employee compensation	9,032	7,558
Repair and maintenance	2,853	3,026
Materials and supplies	1,966	1,838
Complex of services for preparation, transportation and processing of hydrocarbons	1,914	2,062
Electricity and fuel	1,221	1,101
Liquefied petroleum gas volumes reservation expenses	918	1,017
Fire safety and security expenses	749	660
Transportation services	727	641
Rent expenses	308	257
Insurance expenses	307	372
Other	773	601
<b>Total materials, services and other</b>	<b>20,768</b>	<b>19,133</b>

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**24 GENERAL AND ADMINISTRATIVE EXPENSES**

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Employee compensation	11,065	12,327
Social expenses and compensatory payments	2,735	2,184
Legal, audit, and consulting services	839	1,019
Business travel expense	560	624
Fire safety and security expenses	419	387
Advertising expenses	410	370
Repair and maintenance expenses	231	200
Rent expenses	90	214
Other	821	801
<b>Total general and administrative expenses</b>	<b>17,170</b>	<b>18,126</b>

*Auditor's fees.* AO PricewaterhouseCoopers Audit has served as the independent external auditor of PAO NOVATEK for each of the reported financial years. The independent external auditor is subject to appointment at the Annual General Meeting of shareholders based on the recommendations from the Board of Directors. The aggregate fees for audit and other services rendered by PricewaterhouseCoopers Audit to the parent company of the Group included within legal, audit, and consulting services are as follows:

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Audits of PAO NOVATEK (audit of the Group's consolidated financial statements and audit of statutory financial statements of PAO NOVATEK)	34	34
Other services	9	9
<b>Total auditor's fees and services</b>	<b>43</b>	<b>43</b>

**25 FINANCE INCOME (EXPENSE)**

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<i>Interest expense (including transaction costs)</i>		
Interest expense on fixed rate debt	8,234	11,469
Interest expense on variable rate debt	2,001	4,828
<b>Subtotal</b>	<b>10,235</b>	<b>16,297</b>
Less: capitalized interest	(3,391)	(5,314)
<b>Interest expense on debt</b>	<b>6,844</b>	<b>10,983</b>
Provisions for asset retirement obligations:		
effect of the present value discount unwinding	749	587
Interest expense on lease liabilities	119	-
<b>Total interest expense</b>	<b>7,712</b>	<b>11,570</b>



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**25 FINANCE INCOME (EXPENSE)( CONTINUED)**

<i>Interest income</i>	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Interest income on loans receivable	13,747	17,597
Interest income on cash, cash equivalents and deposits	2,125	1,135
<b>Total interest income</b>	<b>15,872</b>	<b>18,732</b>

<i>Foreign exchange gains (losses)</i>	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Gains	48,322	41,124
Losses	(34,646)	(66,614)
<b>Total foreign exchange gain (loss), net</b>	<b>13,676</b>	<b>(25,490)</b>

**26 INCOME TAX**

*Reconciliation of income tax.* The table below reconciles actual income tax expense and theoretical income tax, determined by applying the statutory tax rate to profit before income tax.

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Profit before income tax	200,839	308,164
Theoretical income tax expense at statutory rate of 20 percent	40,168	61,633
Increase (decrease) due to:		
Non-deductible differences in respect of the Group's share of loss (profit) of joint ventures	(4,592)	(18,147)
Non-deductible differences in respect of net gain on disposal of interests in joint ventures	-	781
Tax benefits relating to priority investment projects	(1,312)	(1,540)
Other differences	105	364
<b>Total income tax expense</b>	<b>34,369</b>	<b>43,091</b>

A number of the Group's investment projects were included by the government authorities in the list of priority projects, in respect of them the Group was able to apply a reduced income tax rate of 16.5 percent and 15.5 percent for the years ended 31 December 2017 and 2016, respectively.

Domestic and foreign components of current income tax expense were:

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Russian Federation income tax	34,811	35,025
Foreign income tax	416	552
<b>Total current income tax expense</b>	<b>35,227</b>	<b>35,577</b>

**PAO NOVATEK**

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**26 INCOME TAX (CONTINUED)**

*Effective income tax rate.* The Russian statutory income tax rate for 2017 and 2016 was 20 percent.

The Group recognizes in profit before income tax its share of net profit (loss) from joint ventures, which influences the consolidated profit of the Group but does not result in additional income tax expense (benefit) at the Group's level. Net profit (loss) of joint ventures was recorded in their financial statements on an after-tax basis. The Group holds at least a 50 percent interest in each of its joint ventures, and dividend income from these joint ventures is subject to a zero withholding tax rate according to the Russian tax legislation.

Without the effect of net profit (loss) and dividends from joint ventures the effective income tax rate for the years ended 31 December 2017 and 2016 was 19.3 percent and 19.8 percent, respectively.

In respect of PAO NOVATEK and majority of its Russian subsidiaries, the Group submits a single consolidated income tax return in accordance with Russian tax legislation (see Note 3).

*Deferred income tax.* Differences between IFRS and Russian statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes.

Deferred income tax balances are presented in the consolidated statement of financial position as follows:

	<u>At 31 December 2017</u>	<u>At 31 December 2016</u>
Long-term deferred income tax asset (other non-current assets)	6,898	4,671
Long-term deferred income tax liability	(26,167)	(24,656)
<b>Net deferred income tax liability</b>	<b>(19,269)</b>	<b>(19,985)</b>

Movements in deferred income tax assets and liabilities during the years ended 31 December 2017 and 2016 are as follows:

	<u>At 31 December 2017</u>	<u>Acquisition of subsidiaries</u>	<u>Statement of Income effect</u>	<u>Statement of Comprehensive Income effect</u>	<u>At 31 December 2016</u>
Property, plant and equipment	(31,983)	(1,637)	(1,614)	15	(28,747)
Intangible assets	(346)	(97)	62	2	(313)
Inventories	(297)	(7)	(23)	(17)	(250)
Other	(639)	-	(212)	24	(451)
<b>Deferred income tax liabilities</b>	<b>(33,265)</b>	<b>(1,741)</b>	<b>(1,787)</b>	<b>24</b>	<b>(29,761)</b>
<i>Less: deferred tax assets offset</i>	<i>7,098</i>	<i>883</i>	<i>1,110</i>	<i>-</i>	<i>5,105</i>
<b>Total deferred income tax liabilities</b>	<b>(26,167)</b>	<b>(858)</b>	<b>(677)</b>	<b>24</b>	<b>(24,656)</b>
Tax losses carried forward	3,607	549	504	12	2,542
Property, plant and equipment	3,102	949	1,085	-	1,068
Inventories	2,438	-	279	6	2,153
Loans receivable	1,996	-	650	-	1,346
Asset retirement obligations	1,389	52	(122)	(5)	1,464
Trade payables and accrued liabilities	1,237	-	318	6	913
Other	227	13	(69)	(7)	290
<b>Deferred income tax assets</b>	<b>13,996</b>	<b>1,563</b>	<b>2,645</b>	<b>12</b>	<b>9,776</b>
<i>Less: deferred tax liabilities offset</i>	<i>(7,098)</i>	<i>(883)</i>	<i>(1,110)</i>	<i>-</i>	<i>(5,105)</i>
<b>Total deferred income tax assets</b>	<b>6,898</b>	<b>680</b>	<b>1,535</b>	<b>12</b>	<b>4,671</b>
<b>Net deferred income tax liabilities</b>	<b>(19,269)</b>	<b>(178)</b>	<b>858</b>	<b>36</b>	<b>(19,985)</b>

**PAO NOVATEK**

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**26 INCOME TAX (CONTINUED)**

	At 31 December 2016	Statement of Income effect	Statement of Comprehensive Income effect	At 31 December 2015
Property, plant and equipment	(28,747)	(1,989)	2	(26,760)
Intangible assets	(313)	66	-	(379)
Inventories	(250)	(34)	-	(216)
Other	(451)	171	(14)	(608)
<b>Deferred income tax liabilities</b>	<b>(29,761)</b>	<b>(1,786)</b>	<b>(12)</b>	<b>(27,963)</b>
<i>Less: deferred tax assets offset</i>	<i>5,105</i>	<i>848</i>	<i>-</i>	<i>4,257</i>
<b>Total deferred income tax liabilities</b>	<b>(24,656)</b>	<b>(938)</b>	<b>(12)</b>	<b>(23,706)</b>
Tax losses carried forward	2,542	(616)	(2)	3,160
Inventories	2,153	683	(1)	1,471
Asset retirement obligations	1,464	634	-	830
Loans receivable	1,346	(2,662)	-	4,008
Property, plant and equipment	1,068	304	-	764
Trade payables and accrued liabilities	913	147	59	707
Assets held for sale	-	(4,316)	-	4,316
Other	290	98	8	184
<b>Deferred income tax assets</b>	<b>9,776</b>	<b>(5,728)</b>	<b>64</b>	<b>15,440</b>
<i>Less: deferred tax liabilities offset</i>	<i>(5,105)</i>	<i>(848)</i>	<i>-</i>	<i>(4,257)</i>
<b>Total deferred income tax assets</b>	<b>4,671</b>	<b>(6,576)</b>	<b>64</b>	<b>11,183</b>
<b>Net deferred income tax liabilities</b>	<b>(19,985)</b>	<b>(7,514)</b>	<b>52</b>	<b>(12,523)</b>

Deferred income tax assets expected to be realized within twelve months as of 31 December 2017 and 2016 were RR 3,902 million and RR 3,356 million, respectively. Deferred tax liabilities expected to be reversed within twelve months of 31 December 2017 and 2016 were RR 936 million and RR 701 million, respectively.

At 31 December 2017, the Group had recognized deferred income tax assets of RR 3,607 million (31 December 2016: RR 2,542 million) in respect of unused tax loss carry forwards of RR 18,373 million (31 December 2016: RR 13,102 million). In accordance with tax legislation of Russian Federation effective 1 January 2017, taxable profits can be reduced in the amount of tax losses carried forward for relief during unlimited period of time, at the same time in 2017 to 2020 tax losses carried forward cannot exceed 50 percent of taxable profits. Up until 2017, the tax legislation set a limit period for tax losses to be carried forward for relief against taxable profits for ten years after they were incurred. In determining future taxable profits and the amount of tax benefits that are probable in the future, the Group's management makes judgments including expectations regarding the Group's ability to generate sufficient future taxable income and the projected time period over which deferred tax benefits will be realized.

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS**

The accounting policies and disclosure requirements for financial instruments have been applied to the line items below:

<i>Financial assets</i>	At 31 December 2017		At 31 December 2016	
	Non-current	Current	Non-current	Current
<b><i>Loans and receivables</i></b>				
Long-term loans receivable	5,211	-	7,575	-
Trade and other receivables	29,559	44,503	24,832	41,586
Cash and cash equivalents	-	65,943	-	48,301
Other	10	-	13	-
<b><i>At fair value through profit or loss</i></b>				
Long-term loans receivable	177,131	891	176,738	308
Commodity derivatives	1,705	2,117	1,172	2,920
<b>Total financial assets</b>	<b>213,616</b>	<b>113,454</b>	<b>210,330</b>	<b>93,115</b>
<b><i>Financial liabilities</i></b>				
<b><i>At amortized cost</i></b>				
Long-term debt	141,448	14,302	161,296	55,469
Long-term lease liabilities	5,776	1,520	-	-
Trade and other payables	-	32,932	-	28,112
Dividends payable to non-controlling interest	-	1,633	-	-
<b><i>At fair value through profit or loss</i></b>				
Commodity derivatives	649	3,333	1,517	2,754
<b>Total financial liabilities</b>	<b>147,873</b>	<b>53,720</b>	<b>162,813</b>	<b>86,335</b>

**Fair value measurement.** The Group evaluates the quality and reliability of the assumptions and data used to measure fair value in accordance with IFRS 13, *Fair Value Measurement*, in the three hierarchy levels as follows:

- i. quoted prices in active markets (Level 1);
- ii. inputs other than quoted prices included in Level 1 that are directly or indirectly observable in the market (externally verifiable inputs) (Level 2);
- iii. inputs that are not based on observable market data (unobservable inputs) (Level 3).

**Commodity derivative instruments.** The Group conducts natural gas foreign trading in active markets under long-term and short-term purchase and sales contracts, as well as purchases and sells various derivative instruments (with reference to the European natural gas hubs) for delivery optimization and to decrease exposure to the risk of negative changes in natural gas prices.

These contracts include pricing terms that are based on a variety of commodities and indices, and/or volume flexibility options that collectively qualify them under the scope of IAS 39, *Financial instruments: recognition and measurement*, although the activity surrounding certain contracts involves the physical delivery of natural gas. All contracts mentioned above are recognized in the consolidated statement of financial position at fair value with movements in fair value recognized in the consolidated statement of income.

The fair value of long-term natural gas derivative contracts involving the physical delivery of natural gas is determined using internal models and other valuation techniques (the mark-to-market and mark-to-model analysis) due to the absence of quoted prices or other observable, market-corroborated data, for the duration of the contracts. Due to the assumptions underlying their fair value, the natural gas derivatives contracts are categorized as Level 3 in the fair value hierarchy, described above.

The fair value of short-term natural gas derivative contracts involving the physical delivery of natural gas and likewise contracts used for the price risk management and delivery optimization is determined based on available futures quotes in the active market (mark-to-market analysis) (Level 1).

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The amounts recognized by the Group in respect of the natural gas derivative contracts measured in accordance with IAS 39, *Financial instruments: recognition and measurement*, are as follows:

<i>Commodity derivatives</i>	At 31 December 2017	At 31 December 2016
Within other non-current and current assets	3,822	4,092
Within other non-current and current liabilities	(3,982)	(4,271)
	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<i>Included in other operating income (loss)</i>		
Operating income (loss) from natural gas foreign trading	289	1,970
Change in fair value	(9)	(1,778)

The table below represents the effect on the fair value estimation of natural gas derivative contracts that would occur from price changes by ten percent by one megawatt-hour in 12 months after the reporting date:

<i>Effect on the fair value</i>	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Increase by ten percent	(1,572)	(1,673)
Decrease by ten percent	1,572	1,673

**Recognition and remeasurement of the shareholders' loans to joint ventures.** Terms and conditions of the shareholders' loans provided by the Group to its joint ventures OAO Yamal LNG and ZAO Terneftegas contain certain financial (benchmark interest rates adjusted for the borrower credit risk) and non-financial (actual interest rates on the borrowings of shareholders, expected free cash flows of the borrower and expected maturities) variables and in accordance with the Group's accounting policy were classified as financial assets at fair value through profit or loss.

The following table summarizes the movements in the carrying amounts of shareholders' loans provided to Yamal LNG and Terneftegas and related interest receivable:

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<b>At 1 January</b>	<b>198,454</b>	<b>216,136</b>
Loans provided	-	6,645
Repayment of the loans and accrued interest	(910)	(1,298)
Initial measurement at fair value allocated to increase the Group's investments in joint ventures (see Note 7)	-	(836)
Subsequent remeasurement at fair value recognized in profit (loss) as follows:		
– Interest income (using the effective interest rate method)	13,106	16,248
– Foreign exchange gain (loss), net	3,579	(48,828)
– Remaining effect from changes in fair value (attributable to free cash flows of the borrowers and interest rates)	(7,178)	10,387
<b>At 31 December</b>	<b>207,051</b>	<b>198,454</b>

Fair value measurement of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and free cash flows models based on the borrower's strategic plans approved by the shareholders of the joint ventures. Due to the assumptions underlying fair value estimation, shareholders' loans are categorized as Level 3 in the fair value hierarchy, described above.

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The fair value of the shareholders' loans is sensitive to benchmark interest rates changes. The table below represents the effect on fair value of the shareholders' loans that would occur from one percent changes in the benchmark interest rates.

<i>Effect on the fair value</i>	Year ended 31 December:	
	2017	2016
Increase by one percent	(11,560)	(13,038)
Decrease by one percent	12,536	14,272

**Financial risk management objectives and policies.** In the ordinary course of business, the Group is exposed to market risks from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on the degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial results. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position.

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

**Market risk.** Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Group's financial results or the value of its holdings of financial instruments. The primary objective of mitigating these market risks is to manage and control market risk exposures, while optimizing the return on risk.

The Group is exposed to market price movements relating to changes in commodity prices such as crude oil, oil and gas condensate refined products and natural gas (commodity price risk), foreign currency exchange rates, interest rates, equity prices and other indices that could adversely affect the value of the Group's financial assets, liabilities or expected future cash flows.

(a) *Foreign exchange risk*

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to the US dollar and Euro. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble, the US dollar and Euro. The Group may utilize foreign currency derivative instruments to manage the risk exposures associated with fluctuations on certain firm commitments for sales and purchases, debt instruments and other transactions that are denominated in currencies other than the Russian rouble, and certain non-Russian rouble assets and liabilities.

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The carrying amounts of the Group's financial instruments are denominated in the following currencies:

<i>At 31 December 2017</i>	<b>Russian rouble</b>	<b>US dollar</b>	<b>Euro</b>	<b>Other</b>	<b>Total</b>
<i>Financial assets</i>					
<i>Non-current</i>					
Long-term loans receivable	5,211	79,459	97,672	-	182,342
Trade and other receivables	527	17,231	11,801	-	29,559
Commodity derivatives	-	-	1,705	-	1,705
Other	-	-	-	10	10
<i>Current</i>					
Trade and other receivables	21,822	16,360	3,730	2,591	44,503
Current portion of long-term loans receivable	-	891	-	-	891
Commodity derivatives	-	-	2,117	-	2,117
Cash and cash equivalents	16,392	36,449	12,745	357	65,943
<i>Financial liabilities</i>					
<i>Non-current</i>					
Long-term debt	-	(134,561)	(6,887)	-	(141,448)
Long-term lease liabilities	(340)	(5,360)	(3)	(73)	(5,776)
Commodity derivatives	-	-	(649)	-	(649)
<i>Current</i>					
Current portion of long-term debt	(1,022)	(13,280)	-	-	(14,302)
Current portion of long-term lease liabilities	(116)	(1,349)	(2)	(53)	(1,520)
Trade and other payables	(25,651)	(3,563)	(3,505)	(213)	(32,932)
Dividends payable to non-controlling interest	(1,633)	-	-	-	(1,633)
Commodity derivatives	-	-	(3,333)	-	(3,333)
<b>Net exposure</b>	<b>15,190</b>	<b>(7,723)</b>	<b>115,391</b>	<b>2,619</b>	<b>125,477</b>

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

<i>At 31 December 2016</i>	<b>Russian rouble</b>	<b>US dollar</b>	<b>Euro</b>	<b>Other</b>	<b>Total</b>
<b>Financial assets</b>					
<i>Non-current</i>					
Long-term loans receivable	7,575	79,484	97,254	-	184,313
Trade and other receivables	3,530	13,815	7,487	-	24,832
Commodity derivatives	-	-	1,172	-	1,172
Other	-	-	-	13	13
<i>Current</i>					
Trade and other receivables	23,525	15,297	1,841	923	41,586
Current portion of long-term loans receivable	-	308	-	-	308
Commodity derivatives	-	-	2,920	-	2,920
Cash and cash equivalents	10,346	18,116	19,544	295	48,301
<b>Financial liabilities</b>					
<i>Non-current</i>					
Long-term debt	-	(154,915)	(6,381)	-	(161,296)
Commodity derivatives	-	-	(1,517)	-	(1,517)
<i>Current</i>					
Current portion of long-term debt	(27,532)	(27,937)	-	-	(55,469)
Trade and other payables	(23,593)	(2,319)	(2,064)	(136)	(28,112)
Commodity derivatives	-	-	(2,754)	-	(2,754)
<b>Net exposure</b>	<b>(6,149)</b>	<b>(58,151)</b>	<b>117,502</b>	<b>1,095</b>	<b>54,297</b>

The Group chooses to provide information about market risk and potential exposure to hypothetical loss from its use of financial instruments through sensitivity analysis disclosures in accordance with IFRS requirements.

The sensitivity analysis depicted in the table below reflects the hypothetical loss that would occur assuming a ten percent increase in exchange rates and no changes in the portfolio of instruments and other variables at 31 December 2017 and 2016, respectively:

<i>Effect on profit before income tax</i>	<b>Increase in exchange rate</b>	<b>Year ended 31 December:</b>	
		<b>2017</b>	<b>2016</b>
RUB / USD	10%	(772)	(5,815)
RUB / EUR	10%	11,539	11,750

The effect of a corresponding ten percent decrease in exchange rate is approximately equal and opposite.

*(b) Commodity price risk*

The Group's overall commercial trading strategy in natural gas and liquid hydrocarbons is centrally managed. Changes in commodity prices could negatively or positively affect the Group's results of operations. The Group manages the exposure to commodity price risk by optimizing its core activities to achieve stable price margins.

**Natural gas supplies on the Russian domestic market.** As an independent natural gas producer, the Group is not subject to the government's regulation of natural gas prices, except for those volumes sold to residential customers. Nevertheless, the Group's prices for natural gas sold are strongly influenced by the prices regulated by the governmental agency of the Russian Federation that carries out state regulation of prices and tariffs for goods and services of natural monopolies in energy, utilities and transportation.

There were no changes in regulated wholesale natural gas prices on the domestic market (excluding residential customers) since 1 January 2016 until 30 June 2017. From 1 July 2017, regulated wholesale natural gas prices were increased by 3.9 percent.



**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

Management believes it has limited downside commodity price risk for natural gas in the Russian Federation and does not use commodity derivative instruments for trading purposes. The Group's natural gas purchase and sales contracts in the domestic market are entered to meet supply requirements to fulfil contract obligations or for own consumption and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*. However, to effectively manage the margins achieved through its natural gas trading activities, management has established targets for volumes sold to wholesale traders and end-customers.

**LNG supplies on international markets.** In 2017, the Group sold liquefied natural gas purchased from its joint venture Yamal LNG on international markets under short-term contracts at prices based on benchmark reference natural gas prices at the major natural gas hubs. These Group's purchase and sales contracts are entered to meet supply requirements to fulfil contract obligations and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*.

**LNG regasification activity in Poland.** The Group purchases LNG in Poland at prices depending on natural gas prices quoted in Poland and sells regasified LNG as natural gas on the Polish market based on the prices regulated by the Energy Regulatory Office through Blue Gaz Sp. z o.o., the Group's wholly owned subsidiary. These purchase and sales contracts are entered by the Group to meet supply requirements and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*.

**Natural gas trading activities on the European and other foreign markets.** The Group purchases and sells natural gas on the European and other foreign markets under long-term and short-term supply contracts, as well as purchases and sells different derivative instruments based on formulas with reference to benchmark natural gas prices quoted for the North-Western European natural gas hubs, crude oil and oil products prices and/or a combination thereof. Therefore, the Group's results from natural gas foreign trading and derivative instruments foreign trading are subject to commodity price volatility based on fluctuations or changes in the respective benchmark reference prices.

Natural gas foreign trading activities and respective foreign derivative instruments are executed by Novatek Gas & Power GmbH, the Group's wholly owned subsidiary, and are managed within the Group's integrated trading function.

**Liquid hydrocarbons supplies.** The Group sells its crude oil, stable gas condensate and gas condensate refined products under spot contracts. Naphtha and stable gas condensate volumes sold to the Asian-Pacific Region, European and North American markets are primarily based on benchmark reference crude oil prices of Brent IPE and Dubai and/or naphtha prices, mainly of Naphtha Japan and Naphtha CIF NWE or a combination thereof, plus a margin or discount, depending on current market situation. Other gas condensate refined products volumes sold mainly to the European market are based on benchmark reference jet fuel prices of Jet CIF NWE and gasoil prices of Gasoil 0.1 percent CIF NWE plus a margin or discount, depending on current market situation. Crude oil sold internationally is based on benchmark reference crude oil prices of Brent dated, or Dubai, plus a premium or a discount, and on a transaction-by-transaction basis or based on benchmark reference crude oil prices of Brent and Urals or a combination thereof for volumes sold domestically.

As a result, the Group's revenues from the sales of liquid hydrocarbons are subject to fluctuations in the crude oil and gas condensate refined products benchmark reference prices. The Group's liquid hydrocarbons purchase and sales contracts are entered to meet supply requirements to fulfil contract obligations or for own consumption and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*.

(c) *Cash flow and fair value interest rate risk*

The Group is subject to interest rate risk on financial liabilities with variable interest rates. Changes in interest rates impact primarily debt by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). To mitigate this risk, the Group's treasury function performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In cases where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favorable interest rate terms.

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The interest rate profiles of the Group's interest-bearing financial instruments were as follows:

	At 31 December 2017		At 31 December 2016	
	RR million	Percent	RR million	Percent
At fixed rate	141,448	91%	161,323	74%
At variable rate	14,302	9%	55,442	26%
<b>Total debt</b>	<b>155,750</b>	<b>100%</b>	<b>216,765</b>	<b>100%</b>

The Group centralizes the cash requirements and surpluses of controlled subsidiaries and the majority of their external financing requirements, and applies, on its consolidated net debt position, a funding policy to optimize its financing costs and manage the impact of interest rate changes on its financial results in line with market conditions. In this way, the Group is able to ensure that the balance between the floating rate portion of its debt and its cash surpluses has a low level of exposure to any change in interest rates over the short term. This policy makes it possible to significantly limit the Group's sensitivity to interest rate volatility.

The Group's financial results are sensitive to changes in interest rates on the floating rate portion of the Group's debt portfolio. If the interest rates applicable to floating rate debt were to increase by 100 basis points (one percent) at the reporting dates, assuming all other variables remain constant, it is estimated that the Group's profit before taxation would decrease by the amounts shown below:

<i>Effect on profit before income tax</i>	Year ended 31 December:	
	2017	2016
Increase by 100 basis points	143	554

The effect of a corresponding 100 basis points decrease in interest rate is approximately equal and opposite.

The Group is examining various ways to manage its cash flow interest rate risk by using a combination of floating and fixed interest rates. No swaps or other similar instruments were in place at 31 December 2017 and 2016, or during the years then ended.

**Credit risk.** Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if a counterparty defaults on its contractual obligations.

Credit risk is managed on a Group level and arises from cash and cash equivalents, including short-term deposits with banks, as well as credit exposures to customers, including outstanding trade receivables and committed transactions. Cash and cash equivalents are deposited only with banks that are considered by the Group during the whole deposit period to have minimal risk of default.

The Group's trade and other receivables consist of a large number of customers, spread across diverse industries and geographical areas. The Group has developed standard credit payment terms and constantly monitors the status of trade and other receivables and the creditworthiness of the customers.

Most of the Group's international natural gas and liquid hydrocarbons sales are made to customers with independent external ratings; however, if the customer has a credit rating below BBB-, the Group requires the collateral for the trade receivable to be in the form of letters of credit from banks with an investment grade rating. Most of domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis.

As a result of the domestic regional natural gas trading activities, the Group is exposed to the risk of payment defaults of small and medium-sized industrial users and individuals. To minimize credit risk the Group monitors the recoverability of these debtors by analyzing ageing of receivables by type of customers and their respective prior payment history.

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

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The table below highlights the Group's trade and other receivables to published credit ratings of its counterparties and/or their parent companies:

<i>Moody's, Fitch and/or Standard &amp; Poor's</i>	At 31 December 2017	At 31 December 2016
Investment grade rating	14,676	12,913
Non-investment grade rating	12,661	5,062
No external rating	17,166	23,611
<b>Total trade and other receivables</b>	<b>44,503</b>	<b>41,586</b>

The table below highlights the Group's cash and cash equivalents balances to published credit ratings of its banks and/or their parent companies:

<i>Moody's, Fitch and/or Standard &amp; Poor's</i>	At 31 December 2017	At 31 December 2016
Investment grade rating	49,857	38,087
Non-investment grade rating	15,916	10,194
No external rating	170	20
<b>Total cash and cash equivalents</b>	<b>65,943</b>	<b>48,301</b>

Investment grade ratings classification referred to as Aaa to Baa3 for Moody's Investors Service, and as AAA to BBB- for Fitch Ratings and Standard & Poor's.

In addition, the Group provides long-term loans to its joint ventures for development, construction and acquisitions of oil and gas assets. Required amount of loans and their maturity schedules are based on the budgets and strategic plans approved by the shareholders of the joint ventures.

**Liquidity risk.** Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. In managing its liquidity risk, the Group maintains adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows and matches the maturity profiles of financial assets and liabilities.

The Group prepares various financial plans (monthly, quarterly and annually) which ensures that the Group has sufficient cash on demand to meet expected operational expenses, financial obligations and investing activities for a period of 30 days or more. The Group has entered into a number of short-term credit facilities. Such credit lines and overdraft facilities can be drawn down to meet short-term financing needs. To fund cash requirements of a more permanent nature, the Group will normally raise long-term debt in available international and domestic markets.

**PAO NOVATEK**

**Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The following tables summarize the maturity profile of the Group's financial liabilities, except of natural gas derivative contracts, based on contractual undiscounted payments, including interest payments:

<i>At 31 December 2017</i>	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years	Total
Debt at fixed rate					
<i>Principal</i>	-	8,890	107,061	32,055	148,006
<i>Interest</i>	7,272	7,272	16,655	6,163	37,362
Debt at variable rate					
<i>Principal</i>	14,314	-	-	-	14,314
<i>Interest</i>	168	-	-	-	168
Lease liabilities	1,606	1,494	4,393	937	8,430
Trade and other payables	32,932	-	-	-	32,932
Dividends payable to non-controlling interest	1,633	-	-	-	1,633
<b>Total financial liabilities</b>	<b>57,925</b>	<b>17,656</b>	<b>128,109</b>	<b>39,155</b>	<b>242,845</b>
<i>At 31 December 2016</i>					
Debt at fixed rate					
<i>Principal</i>	14,000	-	56,358	98,633	168,991
<i>Interest</i>	8,179	7,636	20,823	10,841	47,479
Debt at variable rate					
<i>Principal</i>	41,532	13,998	-	-	55,530
<i>Interest</i>	866	144	-	-	1,010
Trade and other payables	28,112	-	-	-	28,112
<b>Total financial liabilities</b>	<b>92,689</b>	<b>21,778</b>	<b>77,181</b>	<b>109,474</b>	<b>301,122</b>

The following table represents the maturity profile of the Group's derivative commodity contracts based on undiscounted cash flows:

<i>At 31 December 2017</i>	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years	Total
Cash inflow	45,120	29,028	54,785	-	128,933
Cash outflow	(46,422)	(28,182)	(54,572)	-	(129,176)
<b>Net cash flows</b>	<b>(1,302)</b>	<b>846</b>	<b>213</b>	<b>-</b>	<b>(243)</b>
<i>At 31 December 2016</i>					
Cash inflow	39,310	25,336	57,713	13,704	136,063
Cash outflow	(39,144)	(25,871)	(57,570)	(13,655)	(136,240)
<b>Net cash flows</b>	<b>166</b>	<b>(535)</b>	<b>143</b>	<b>49</b>	<b>(177)</b>

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

**Reconciliation of liabilities arising from financing activities.** The movements in the Group's liabilities arising from financing activities for the year ended 31 December 2017 are as follows:

	Long-term debt and interest payables	Long-term lease liabilities	Total
<b>At 31 December 2016</b>	<b>218,586</b>	-	<b>218,586</b>
<b>At 1 January 2017<sup>(*)</sup></b>	<b>218,586</b>	<b>256</b>	<b>218,842</b>
Cash flows	(63,144)	(567)	(63,711)
<b>Non-cash movements</b>			
Non-cash additions	-	7,623	7,623
Interest accrued	10,235	119	10,354
Foreign exchange movements	(8,706)	(135)	(8,841)
<b>At 31 December 2017</b>	<b>156,971</b>	<b>7,296</b>	<b>164,267</b>

<sup>(\*)</sup> – effect of initial application of IFRS 16, *Leases*, recognized at 1 January 2017 (see Note 3).

**Capital management.** The primary objectives of the Group's capital management policy are to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain investor, market and creditor confidence to support its business activities.

Prior to 2015, the Group had investment grade credit ratings of Baa3 by Moody's Investors Service, BBB- by Fitch Ratings, and BBB- by Standard & Poor's. In February 2015, following the decrease of the sovereign credit rating of the Russian Federation by both Standard & Poor's and Moody's Investors Service, the Group's investment grade credit rating was also downgraded to noninvestment level BB+ and Ba1, respectively. In November 2016, the Group's credit rating was upgraded to investment level BBB- by Standard & Poor's. In December 2017, the Group's credit rating was upgraded to investment level BBB by Fitch Ratings. In January 2018, the Group's credit rating was upgraded to investment level Baa3 by Moody's Investors Service. The Group has established certain financial targets and coverage ratios that it monitors on a quarterly and annual basis to maintain its credit ratings.

The Group manages its capital on a corporate-wide basis to ensure adequate funding to sufficiently meet the Group's operational requirements. The majority of external debts raised to finance NOVATEK's wholly owned subsidiaries are centralized at the parent level, and financing to Group entities is facilitated through inter-company loan arrangements or additional contributions to share capital.

The Group has a stated dividend policy that distributes not less than 30 percent of the Group's consolidated net profit determined according to IFRS, adjusted for one-off profits (losses). The dividend payment for a specific year is determined after taking into consideration future earnings, capital expenditure requirements, future business opportunities and the Group's current financial position. Dividends are recommended by the Board of Directors of NOVATEK and approved by the NOVATEK's shareholders.

The Group defines the term "capital" as equity attributable to PAO NOVATEK shareholders plus net debt (total debt less cash and cash equivalents). There were no changes to the Group's approach to capital management during 2017. At 31 December 2017 and 2016, the Group's capital totaled RR 847,646 million and RR 816,814 million, respectively.

**28 CONTINGENCIES AND COMMITMENTS**

**Operating environment.** The Russian Federation continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is in practice not convertible in most countries outside of the Russian Federation, and relatively high inflation. In addition, the Russian economy is particularly sensitive to world oil and gas prices; therefore, significant prolonged declines in world oil prices have a negative impact on the Russian economy. The tax, currency and customs legislation is subject to varying interpretations, frequent changes and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

The Group's business operations are primarily located in the Russian Federation and are thus exposed to the economic and financial markets of the Russian Federation.

Developments in Ukraine during 2014 and the subsequent negative reaction of the world community have had and may continue to have a negative impact on the Russian economy, including difficulties in obtaining international funding, devaluation of national currency and high inflation. These and other events, in case of escalation, may have a significant negative impact on the operating environment in the Russian Federation.

**Sectoral sanctions imposed by the U.S. government.** On 16 July 2014, the Office of Foreign Assets Control (OFAC) of the U.S. Treasury included PAO NOVATEK on the Sectoral Sanctions Identification List (the "List"), which prohibits U.S. persons or persons within the United States from providing new financing to the Group for longer than 60 days (prior to 28 November 2017, this restriction applied to new financing with a maturity of more than 90 days). Whereas all other transactions, including financial, carried out by U.S. persons or within the United States with the Group are permitted. The inclusion on the List has not impacted the Group's business activities, in any jurisdiction, nor does it affect the Group's assets and debt.

Management has reviewed the Group's capital expenditure programs and existing debt portfolio and has concluded that the Group has sufficient liquidity, through internally generated (operating) cash flows, to adequately fund its core oil and gas business operations including finance of planned capital expenditure programs of its subsidiaries, as well as to repay and service all Group's short-term and long-term debt existing at the current reporting date and, therefore, inclusion on the List does not adversely impact the Group's operational activities.

The Group together with its foreign partners currently raises necessary financing for our joint ventures from non-US debt markets and lenders.

**Contractual commitments.** At 31 December 2017, the Group had contractual capital expenditures commitments aggregating approximately RR 49 billion (at 31 December 2016: RR 13 billion) mainly for construction of future LNG projects (through 2022) and for development at the Yarudeyskoye (through 2018), the East-Tarkosalinskoye (through 2019), the Yurkharovskoye (through 2019), the North-Russkoye (through 2019) and the West-Yaroyakhinskoye (through 2018) fields all in accordance with duly signed agreements.

In September 2016, the Group and Eni S.p.A. (hereinafter referred to as the "Concessionaries") formed a joint operation with a 50 percent participation interest held by each Concessionary under a Concession Contract with the State of Montenegro for the exploration and production of hydrocarbons on four offshore blocks located in the Adriatic Sea. The Group's commitments with regard to this joint operation relate to performance obligations of the Concessionaries to conduct mandatory work program exploration activities as stipulated by the Concession Contract. The maximum amount to be paid to the State of Montenegro by the Group in case of non-performance during the first exploration period of up to four years ending in 2020 is EUR 42.5 million. The outflow of resources embodying economic benefits required to settle this contingent liability is not probable; therefore, no provision for this liability was recognized in the consolidated financial statements.

The Group has entered into a number of agreements, maturing after the twelve months from the reporting date, relating to time chartering of marine tankers with service terms up to six years for transportation of liquid hydrocarbons. At 31 December 2017, the Group's future minimum payments under the time charter agreements for which provision of the services has not yet commenced amounted to RR 2.7 billion (at 31 December 2016: RR 11.5 billion).

**28 CONTINGENCIES AND COMMITMENTS (CONTINUED)**

**Non-financial guarantees.** The aggregated amount of non-financial guarantees in respect of the Yamal LNG project issued by the Group to a number of third parties (the Ministry of Finance of the Russian Federation, Russian and foreign banks, LNG-vessels owners, LNG-terminal owners) in favor of the Group's joint venture OAO Yamal LNG and its subsidiary totaled USD 3.0 billion and EUR 6.6 billion at 31 December 2017 (at 31 December 2016: USD 3.0 billion and EUR 3.1 billion). These non-financial guarantees have various terms depending mostly on the successful project completion (finalization of the LNG plant construction and achievement of its full production capacity). For certain factors as stipulated in the project financing agreements, the Group plans to issue in the future non-financial guarantees covering the project post-completion period.

With regard to the Group's obligations under the non-financial guarantee issued to the banks providing project financing to Yamal LNG, the State Corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank)" issued in favor of the banks a counter guarantee for the amount not exceeding the equivalent of USD 3 billion.

The aggregated amount of non-financial guarantees issued by the Group to a Russian bank in favor of the Group's joint venture Cryogas-Vysotsk totaled EUR 49 million at 31 December 2017.

The outflow of resources embodying economic benefits required to settle the obligations under these non-financial guarantees issued by the Group is not probable; therefore, no provision for these liabilities was recognized in the consolidated financial statements.

**Taxation.** Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Correspondingly, the relevant regional and federal tax authorities may periodically challenge management's interpretation of such taxation legislation as applied to the Group's transactions and activities. Furthermore, events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in its interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued in the consolidated financial statements.

**Mineral licenses.** The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its mineral licenses. Management cooperates with governmental authorities to agree on remedial actions necessary to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties or license limitation, suspension or revocation. The Group's management believes any issues of non-compliance will be resolved through negotiations or corrective actions without any material adverse effect on the Group's financial position, results of operations or cash flows.

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**28 CONTINGENCIES AND COMMITMENTS (CONTINUED)**

The majority of the Group's oil and gas fields and license areas are located in the YNAO. Licenses are issued by the Federal Agency for the Use of Natural Resources of the Russian Federation and the Group pays unified natural resources production tax to produce crude oil, natural gas and unstable gas condensate from these fields and contributions for exploration of license areas. The principal licenses of the Group and its joint ventures and their expiry dates are:

Field	License holder	License expiry date
<i>Subsidiaries:</i>		
Salmanovskoye (Utrenneye)	OOO Arctic LNG 2	2031
Yurkharovskoye	OOO NOVATEK-Yurkharovneftegas	2034
Upper-Tiuteyskoye and West-Seyakhinskoye	OOO NOVATEK-Yurkharovneftegas	2044
West-Yurkharovskoye	OOO NOVATEK-Yurkharovneftegas	2029
East-Tarkosalinskoye	OOO NOVATEK-Tarkosaleneftegas	2043
North-Russkoye	OOO NOVATEK-Tarkosaleneftegas	2031
Kharbeyskoye	OOO NOVATEK-Tarkosaleneftegas	2036
Urengoyenskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftegas	2059
Khancheyenskoye	OOO NOVATEK-Tarkosaleneftegas	2044
East-Tazovskoye	OOO NOVATEK-Tarkosaleneftegas	2033
Dorogovskoye	OOO NOVATEK-Tarkosaleneftegas	2033
North-Khancheyenskoye + Khadyryakhinskoye	OOO NOVATEK-Tarkosaleneftegas	2029
Dobrovolskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftegas	2059
Geofizicheskoye	OOO Arctic LNG 1	2034
Gydanskoye	OOO Arctic LNG 1	2044
Yarudeyskoye	OOO Yargeo	2029
West-Yaroyakhinskoye	OOO Severneft-Urengoy	2025
South-Khadyryakhinskoye	AO South-Khadyryakhinskoye	2031
Malo-Yamalskoye	OOO NOVATEK-Yarsaleneftegas	2034
<i>Joint ventures:</i>		
South-Tambeyskoye	OOO Yamal LNG	2045
Urengoyenskoye (within the Samburgskiy and Yevo- Yakhinskiy license areas)	AO Arcticgas <sup>(*)</sup>	2034
Yaro-Yakhinskoye	AO Arcticgas	2034
Samburgskoye	AO Arcticgas	2034
North-Chaselskoye	AO Arcticgas	Life of field
Yevo-Yakhinskoye	AO Arcticgas	2034
North-Urengoyenskoye	ZAO Nortgas	2038
Termokarstovoye	ZAO Terneftegas	2097

(\*) – subsidiary of OOO SeverEnergiya

Management believes the Group has the right to extend its licenses beyond the initial expiration date under the existing legislation and intends to exercise this right on all of its fields.



**28 CONTINGENCIES AND COMMITMENTS (CONTINUED)**

*Environmental liabilities.* The Group operates in the oil and gas industry in the Russian Federation and abroad. The enforcement of environmental regulation in the Russian Federation and other countries of operation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations and, as obligations are determined, they are recognized as an expense immediately if no future benefit is discernible. Potential liabilities arising as a result of a change in interpretation of existing regulations, civil litigation or changes in legislation cannot be estimated. Under existing legislation, management believes that there are no probable liabilities, which will have a material adverse effect on the Group's financial position, results of operations or cash flows.

*Legal contingencies.* The Group is subject of, or party to a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Group and which have not been accrued or disclosed in the consolidated financial statements.

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

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**29 PRINCIPAL SUBSIDIARIES AND JOINT VENTURES**

The principal subsidiaries and joint ventures of the Group and respective effective ownership in the ordinary share capital at 31 December 2017 and 2016 are set out below:

	Ownership percent at 31 December:		Country of incorporation	Principal activities
	2017	2016		
<b>Subsidiaries:</b>				
OOO NOVATEK-Yurkharovneftegas	100	100	Russia	Exploration and production
OOO NOVATEK-Tarkosaleneftegas	100	100	Russia	Exploration and production
OOO Yargeo	51	51	Russia	Exploration, development and production
OOO Arctic LNG 1	100	100	Russia	Exploration and development
OOO Arctic LNG 2	100	100	Russia	Exploration and development, construction of LNG plant
OOO Arctic LNG 3	100	100	Russia	Exploration and development
OOO NOVATEK-Murmansk (formerly OOO Kola Yard)	100	100	Russia	Construction of large-scale offshore structures
OOO NOVATEK-Purovsky ZPK	100	100	Russia	Gas Condensate Processing Plant
OOO NOVATEK-Transervice	100	100	Russia	Transportation services
OOO NOVATEK-Ust-Luga	100	100	Russia	Fractionation and Transshipment Complex
OOO NOVATEK-AZK	100	100	Russia	Wholesale and retail trading
OOO NOVATEK-Chelyabinsk	100	100	Russia	Trading and marketing
OOO NOVATEK-Kostroma	100	100	Russia	Trading and marketing
OOO NOVATEK-Perm	100	100	Russia	Trading and marketing
OOO NOVATEK Moscow Region	100	100	Russia	Trading and marketing
Novatek Gas & Power GmbH	100	100	Switzerland	Trading and marketing
Novatek Gas & Power Asia PTE. Ltd	100	100	Singapore	Trading and marketing
Novatek Polska Sp. z o.o.	100	100	Poland	Trading and marketing
Blue gaz Sp. z o.o.	100	100	Poland	LNG regasification, trading and marketing
<b>Joint ventures:</b>				
OOO Yamal LNG	50.1	50.1	Russia	Exploration and development, production of LNG
OOO Yamal Development	50	50	Russia	Holding company
OOO SeverEnergia (includes a producing subsidiary, AO Articgas, see Note 7)	53.3	53.3	Russia	Holding company
ZAO Nortgas	50	50	Russia	Exploration and production
ZAO Terneftegas	51	51	Russia	Exploration and production
OOO Cryogas-Vysotsk	51	-	Russia	Construction of medium-scale LNG plant

**PAO NOVATEK****Notes to the Consolidated Financial Statements**

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**30 RELATED PARTY TRANSACTIONS**

Transactions between NOVATEK and its subsidiaries, which are related parties of NOVATEK, have been eliminated on consolidation and are not disclosed in this Note.

For the purposes of these consolidated financial statements, parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. Management has used reasonable judgments in considering each possible related party relationship with attention directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions, which unrelated parties might not, and transactions between related parties may not be affected on the same terms, conditions and amounts as transactions between unrelated parties.

<i>Related parties – joint ventures</i>	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<b>Transactions</b>		
Purchases of natural gas and liquid hydrocarbons	(137,784)	(112,498)
Interest income on loans issued	13,640	17,524
Dividends received	2,383	-
Other revenues	1,481	844
Materials, services and other	(193)	(91)
<hr/>		
<i>Related parties – joint ventures</i>	<b>At 31 December 2017</b>	<b>At 31 December 2016</b>
<b>Balances</b>		
Long-term loans receivable	182,342	184,313
Interest on long-term loans receivable	29,130	24,496
Trade payables and accrued liabilities	19,785	15,440
Current portion of long-term loans receivable	891	308
Trade receivables	246	423

The terms and conditions of the loans receivable from the joint ventures are disclosed in Note 8.

The Group issued non-financial guarantees in favor of its joint ventures as described in Note 28.

<i>Related parties – parties under control of key management personnel</i>	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<b>Transactions</b>		
Liquid hydrocarbons transportation by rail	(9,496)	(9,405)
Purchases of construction services (capitalized within property, plant and equipment)	(661)	(343)
Materials, services and other	(16)	(72)
<hr/>		
<i>Related parties – parties under control of key management personnel</i>	<b>At 31 December 2017</b>	<b>At 31 December 2016</b>
<b>Balances</b>		
Prepayments and other current assets	565	478
Trade payables and accrued liabilities	504	270
Advances for construction	195	23

Transactions with related parties also included loans, which were provided to one of the Group's subsidiaries by its non-controlling shareholder (see Note 14).

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#### 30 RELATED PARTY TRANSACTIONS (CONTINUED)

**Key management personnel compensation.** The Group paid to key management personnel (members of the Board of Directors and the Management Committee) short-term compensation, including salary, bonuses and excluding dividends the following amounts:

<i>Related parties – members of the key management personnel</i>	Year ended 31 December:	
	2017	2016
Board of Directors	133	132
Management Committee	2,138	1,956
<b>Total compensation</b>	<b>2,271</b>	<b>2,088</b>

Such amounts include personal income tax and are net of payments to non-budget funds made by the employer. Some members of key management personnel have direct and/or indirect interests in the Group and receive dividends under general conditions based on their respective shareholdings.

#### 31 SEGMENT INFORMATION

The Group's activities are considered by the chief operating decision maker (hereinafter referred to as "CODM", represented by the Management Committee of NOVATEK) to comprise one operating segment: "exploration, production and marketing".

Starting from 2017, the Group's management reviews financial information on the results of operations of the reporting segment prepared based on IFRS. Previously, the Group's internal reporting reviewed by CODM was prepared in accordance with Regulations on Accounting and Reporting of the Russian Federation ("RAR").

The CODM assesses reporting segment performance based on profit comprising among others revenues, depreciation, depletion and amortization, interest income and expense, income tax and other items as presented in the Group's consolidated statement of income. The CODM also reviews capital expenditures of the reporting segment for the period defined as additions to property, plant and equipment (see Note 6).

**Geographical information.** The Group operates in the following geographical areas:

- *Russian Federation* – exploration, development, production and processing of hydrocarbons, and sales of natural gas, stable gas condensate, gas condensate refined products, liquefied petroleum gas, crude oil and gas condensate refined products;
- *Countries of Europe (primarily, the Netherlands, Belgium, Sweden, Denmark, Finland, the United Kingdom, Italy, Poland and Montenegro)* – exploration activities within joint operations, sales of naphtha, stable gas condensate, gas condensate refined products, crude oil, liquefied petroleum gas and natural gas;
- *Countries of the Asia-Pacific region (primarily, China, Taiwan, South Korea, Japan and Singapore)* – sales of naphtha, stable gas condensate, gas condensate refined products and crude oil;
- *Countries of North America (primarily, the USA)* – sales of naphtha.
- *Countries of the Middle East (primarily, Oman)* – sales of naphtha and crude oil.

## PAO NOVATEK

### Notes to the Consolidated Financial Statements

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#### 31 SEGMENT INFORMATION (CONTINUED)

Geographical information for the years ended 31 December 2017 and 2016 is as follows:

	Year ended 31 December:	
	2017	2016
Russia	351,318	315,856
Europe	152,439	132,854
Asia-Pacific region	77,204	84,936
North America	25,962	26,052
Middle East	-	7,416
Less: export duties	(27,104)	(33,257)
Total outside Russia	228,501	218,001
<b>Total oil and gas sales</b>	<b>579,819</b>	<b>533,857</b>

Revenues pertaining to geographical information are prepared based on the products geographical destination. For products transported by tankers, the geography is determined based on the location of the port of discharge/transshipment designated by the Group's customer. Substantially all of the Group's operating assets are located in the Russian Federation.

**Major customers.** For the years ended 31 December 2017 and 2016, the Group had one major customer to whom individual revenue exceeded 10 percent of total external revenues, which represented 19 percent (RR 110.3 billion) and 18 percent (RR 97.7 billion) of total external revenues, respectively. The Group's major customer resides within the Russian Federation.

#### 32 SUBSEQUENT EVENTS

In February 2018, the Group won an auction held by ALROSA group to purchase 100 percent participation interest equity stakes in Maretiom Investments Limited and Velarion Investments Limited for RR 30.3 billion, of which RR 21 billion were paid in January 2018 as the auction participation deposit. These companies are the owners of 100 percent participation interests in AO Geotransgas and OOO Urengoyskaya gasovaya kompaniya, the holders of the licenses for exploration and production of hydrocarbons within the Beregovoy and Ust-Yamsoveyskiy license areas located in YNAO, respectively. The transaction is expected to be closed in the nearest future.

In January 2018, the Group acquired a 100 percent participation interest equity stake in OOO Chernichnoye for RR 616 million. OOO Chernichnoye is a holder of the license for exploration and production of hydrocarbons within the Chernichniy license area located in YNAO.

In January 2018, the Group, Total S.A. and Eni S.p.A., through their subsidiaries NOVATEK Lebanon SAL, Total E&P Liban SAL and Eni Lebanon B.V. (hereinafter referred to as the "Right holders"), entered into Exploration and Production Agreements for Petroleum Activities with the Lebanese Republic for the exploration and production of hydrocarbons on two offshore blocks located in the Eastern Mediterranean (hereinafter referred to as the "Exploration and Production Agreements"). The Exploration and Production Agreements stipulate that the Group is assigned a 20 percent participating interest and the Right holders are committed to undertake specified joint upstream activities during the exploration phase within five years. The Group considers that the Exploration and Production Agreements constitute a joint arrangement classified as a joint operation in accordance with IFRS 11, *Joint Arrangements*.

### **33 NEW ACCOUNTING PRONOUNCEMENTS**

The following new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2018, and which the Group has not early adopted:

Amendments to IFRS 10, Consolidated financial statements, and IAS 28, Investments in associates and joint ventures (issued in September 2014, in November 2015 the effective date was postponed indefinitely). These amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The amendments stipulate that a full gain or loss is recognized when a transaction involves a business. A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are held by a subsidiary. The Group is considering the implications of these amendments for the Group's consolidated financial statements, and the timing of their adoption by the Group.

IFRS 9, Financial Instruments: Classification and Measurement (issued in July 2014 and effective for annual periods beginning on or after 1 January 2018, early adoption is permitted). The standard introduces new requirements for classification and measurement of financial instruments, impairment, and hedge accounting. The Group assesses that the adoption of this standard will not have a material impact on the Group's consolidated financial statements.

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES**

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”). In the absence of specific IFRS guidance for the oil and gas industry, the Group has reverted to other relevant disclosure standards, mainly US GAAP, that are consistent with norms established for companies in the oil and gas industry. While not required under IFRS, this section provides unaudited supplemental information on oil and gas exploration and production activities but excludes disclosures regarding the standardized measures of discounted cash flows related to oil and gas activities.

The Group’s exploration and production activities are mainly within the Russian Federation; therefore, majority of the information provided in this section pertains to this country. The Group operates through various oil and gas production subsidiaries, and also has an interest in oil and gas companies that are accounted for under the equity method.

**Oil and Gas Exploration and Development Costs**

The following tables set forth information regarding oil and gas acquisition, exploration and development activities. The amounts reported as costs incurred include both capitalized costs and costs charged to expense, these costs do not include LNG liquefaction and transportation operations (amounts in millions of Russian roubles).

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
<b>Costs incurred in exploration and development activities</b>		
Acquisition of unproved properties	1,040	1,928
Acquisition of proved properties	10,594	-
Exploration costs	7,958	4,828
Development costs	16,481	23,550
<b>Total costs incurred in exploration and development activities</b>	<b>36,073</b>	<b>30,306</b>
The Group’s share in joint ventures’ cost incurred in exploration and development activities	19,214	71,408
	<b>At 31 December 2017</b>	<b>At 31 December 2016</b>
<b>Capitalized costs relating to oil and gas producing activities</b>		
Proved and unproved properties	70,327	57,312
Wells, related equipment and facilities	265,708	236,137
Support equipment and facilities	105,424	88,202
Uncompleted wells, related equipment and facilities	27,312	30,138
<b>Total capitalized costs relating to oil and gas producing activities</b>	<b>468,771</b>	<b>411,789</b>
Less: accumulated depreciation, depletion and amortization	(161,083)	(119,674)
<b>Net capitalized costs relating to oil and gas producing activities</b>	<b>307,688</b>	<b>292,115</b>
The Group’s share in joint ventures’ capitalized costs relating to oil and gas producing activities	469,475	476,608

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

**Results of Operations for Oil and Gas Producing Activities**

The Group's results of operations for oil and gas producing activities are shown below. The results of operations for oil and gas producing activities do not include general corporate overhead or its associated tax effects. Income tax is based on statutory rates. In the following table, revenues from oil and gas sales are comprised of the sale of hydrocarbons produced by the Group's subsidiaries and include processing costs, related to processing facilities of the Group's subsidiaries as well as transportation expenses to customers (amounts in millions of Russian roubles).

	<b>Year ended 31 December:</b>	
	<b>2017</b>	<b>2016</b>
Revenues from oil and gas sales	279,252	276,037
Lifting costs	(14,071)	(14,233)
Transportation expenses	(73,356)	(76,356)
Taxes other than income tax	(48,842)	(43,844)
Depreciation, depletion and amortization	(31,644)	(32,049)
Exploration expenses	(1,819)	(2,087)
<b>Total production costs</b>	<b>(169,732)</b>	<b>(168,569)</b>
Results of operations for oil and gas producing activities before income tax	109,520	107,468
Less: related income tax expenses	(21,904)	(21,494)
<b>Results of operations for oil and gas producing activities of the Group's subsidiaries</b>	<b>87,616</b>	<b>85,974</b>
Share of profit of joint ventures	34,969	29,821
<b>Total results of operations for oil and gas producing activities</b>	<b>122,585</b>	<b>115,795</b>

**Proved Oil and Gas Reserves**

The Group's oil and gas reserves estimation and reporting process involves an annual independent third party reserve appraisal as well as internal technical appraisals of reserves. The Group maintains its own internal reserve estimates that are calculated by qualified engineers and technical staff working directly with the oil and gas properties. The Group's technical staff periodically updates reserve estimates during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The Group estimates its oil and gas reserves in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves.

The oil and gas reserve estimates reported below are determined by the Group's independent petroleum reservoir engineers, DeGolyer and MacNaughton ("D&M"). The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for the reserve determination. The Group's and D&M's technical staffs meet to review and discuss the information provided, and upon completion of this process, senior management reviews and approves the final reserve estimates issued by D&M.

The following reserve estimates were prepared using standard geological and engineering methods generally accepted by the petroleum industry. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history.



**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

The following information presents the quantities of proved oil and gas reserves and changes thereto as at and for the years ended 31 December 2017 and 2016.

Extensions of production licenses are assumed to be at the discretion of the Group. Management believes that proved reserves should include quantities which are expected to be produced after the expiry dates of the Group's production licenses. The principal licenses of the Group for exploration and production expire between 2029 and 2059. Legislation of the Russian Federation states that, upon expiration, a license is subject to renewal at the initiative of the license holder provided that further exploration, appraisal, production or remediation activities are necessary and provided that the license holder has not violated the terms of the license. Management intends to extend its licenses for properties expected to produce beyond the license expiry dates.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such 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.

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, to re-complete existing wells and/or install facilities to collect and deliver the production.

Net reserves exclude quantities due to others when produced.

The reserve quantities below include 100 percent of the net proved reserve quantities attributable to the Group's consolidated subsidiaries and the Group's ownership percentage of the net proved reserves quantities of the joint ventures including volumes of natural gas consumed in hydrocarbons production and development activities. Production and reserves of the South-Tambeyskoye field of Yamal LNG are reported at 60 percent including an additional 9.9 percent interest not owned by the Group, since the Group assumes certain economic and operational risks related to this interest (previously was reported at 50.1 percent). A portion of the Group's total proved reserves are classified as either developed non-producing or undeveloped. Of the non-producing reserves, a portion represents existing wells which are to be returned to production at a future date.

For convenience, reserves estimates are provided both in English and Metric units.

**PAO NOVATEK**  
**Unaudited Supplemental Oil and Gas Disclosures**

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

Net proved reserves of natural gas are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	Billions of cubic feet	Billions of cubic meters	Billions of cubic feet	Billions of cubic meters	Billions of cubic feet	Billions of cubic meters
<b>At 31 December 2015</b> <sup>(1)</sup>	<b>37,241</b>	<b>1,055</b>	<b>26,713</b>	<b>756</b>	<b>63,954</b>	<b>1,811</b>
Changes attributable to:						
Revisions of previous estimates	789	22	1,923	55	2,712	77
Extension and discoveries	633	18	360	10	993	28
Production	(1,678)	(48)	(711)	(20)	(2,389)	(68)
<b>At 31 December 2016</b> <sup>(1)</sup>	<b>36,985</b>	<b>1,047</b>	<b>28,285</b>	<b>801</b>	<b>65,270</b>	<b>1,848</b>
Changes attributable to:						
Revisions of previous estimates	(76)	(2)	374	10	298	8
Extension and discoveries	1,485	42	1,154	33	2,639	75
Acquisitions <sup>(2)</sup>	8,117	230	-	-	8,117	230
Production	(1,523)	(43)	(716)	(20)	(2,239)	(63)
<b>At 31 December 2017</b>	<b>44,988</b>	<b>1,274</b>	<b>29,097</b>	<b>824</b>	<b>74,085</b>	<b>2,098</b>
<b>Net proved developed reserves (included above)</b>						
At 31 December 2015	17,089	484	7,995	226	25,084	710
At 31 December 2016	14,399	407	8,487	240	22,886	647
At 31 December 2017	12,685	359	12,820	363	25,505	722
<b>Net proved undeveloped reserves (included above)</b>						
At 31 December 2015	20,152	571	18,718	530	38,870	1,101
At 31 December 2016	22,586	640	19,798	561	42,384	1,201
At 31 December 2017	32,303	915	16,277	461	48,580	1,376

<sup>(1)</sup> As a result of changes in the presentation of natural gas production and reserves volumes taking into account fuel gas volumes, and the revision of the Group's reported share in production and reserves of South-Tambeyskoye field of Yamal LNG (see above), total net proved natural gas reserves as at 31 December 2016 and 2015 were increased by 3,307 billion of cubic feet (93 billion cubic meters) and 1,281 billion of cubic feet (36 billion cubic meters), respectively.

<sup>(2)</sup> In 2017, the Group acquired oil and gas exploration and production licenses for the Upper-Tiuteyskoye, the West-Seyakhinskoye and the Gydanskoye fields and 100 percent ownership interests in OOO Severneft-Urengoy, AO South-Khadyryakhinskoye and AO Eurotek, exploration and production license holders of the East-Urengoisoye+North-Esetinskoye, the South-Khadyryakhinskoye and the Syskonsyninskoye fields, respectively.

The net proved reserves of natural gas reported in the table above included reserves attributable to a non-controlling interest in a Group's subsidiary of 167 billion of cubic feet (five billion cubic meters) and 178 billion of cubic feet (five billion cubic meters) at 31 December 2017 and 2016, respectively, and reserves attributable to an additional 9.9 percent interest in Yamal LNG not owned by the Group (see above) of 2,386 billion of cubic feet (68 billion cubic meters) and 2,121 billion of cubic feet (60 billion cubic meters) at 31 December 2017 and 2016, respectively.

**PAO NOVATEK**  
**Unaudited Supplemental Oil and Gas Disclosures**

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

Net proved reserves of crude oil, gas condensate and natural gas liquids are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	Millions of barrels	Millions of metric tons	Millions of barrels	Millions of metric tons	Millions of barrels	Millions of metric tons
<b>At 31 December 2015</b>	<b>551</b>	<b>68</b>	<b>660</b>	<b>75</b>	<b>1,211</b>	<b>143</b>
Changes attributable to:						
Revisions of						
previous estimates	116	11	59	8	175	19
Extension and discoveries	15	1	18	3	33	4
Production	(59)	(7)	(46)	(5)	(105)	(12)
<b>At 31 December 2016<sup>(1)</sup></b>	<b>623</b>	<b>73</b>	<b>691</b>	<b>81</b>	<b>1,314</b>	<b>154</b>
Changes attributable to:						
Revisions of						
previous estimates	33	4	(12)	(2)	21	2
Extension and discoveries	61	8	62	7	123	15
Acquisitions <sup>(2)</sup>	40	5	-	-	40	5
Production	(55)	(7)	(43)	(5)	(98)	(12)
<b>At 31 December 2017</b>	<b>702</b>	<b>83</b>	<b>698</b>	<b>81</b>	<b>1,400</b>	<b>164</b>
<b>Net proved developed reserves (included above)</b>						
At 31 December 2015	305	38	302	34	607	72
At 31 December 2016	275	33	326	37	601	70
At 31 December 2017	307	38	359	41	666	79
<b>Net proved undeveloped reserves (included above)</b>						
At 31 December 2015	246	30	358	41	604	71
At 31 December 2016	348	40	365	44	713	84
At 31 December 2017	395	45	339	40	734	85

<sup>(1)</sup> As a result of the revision of the Group's reported share in production and reserves of South-Tambeyskoye field of Yamal LNG (see above), total net proved crude oil, gas condensate and natural gas liquids reserves as at 31 December 2016 were increased by 14 million of barrels (two million metric tons).

<sup>(2)</sup> In 2017, the Group acquired oil and gas exploration and production licenses for the Upper-Tiuteyskoye, the West-Seyakhinskoye and the Gydanskoye fields and 100 percent ownership interests in OOO Severneft-Urengoy, AO South-Khadyryakhinskoye and AO Eurotek, exploration and production license holders of the East-Urengoiskoye+North-Esetinskoye, the South-Khadyryakhinskoye and the Syskonsyninskoye fields, respectively.

The net proved reserves of crude oil, gas condensate and natural gas liquids reported in the table above included reserves attributable to a non-controlling interest in a Group's subsidiary of 65 million of barrels (eight million metric tons) and 66 million of barrels (nine million metric tons) at 31 December 2017 and 2016, respectively, and reserves attributable to an additional 9.9 percent interest in Yamal LNG not owned by the Group (see above) of 17 million of barrels (two million metric tons) and 14 million of barrels (two million metric tons) at 31 December 2017 and 2016, respectively.

**PAO NOVATEK**  
**Contact Information**

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PAO NOVATEK was incorporated as a joint stock company in accordance with the Russian law and is domiciled in the Russian Federation.

The Group's registered office is:

Ulitsa Pobedy 22a  
629850 Tarko-Sale  
Yamal-Nenets Autonomous Region  
Russian Federation

The Group's office in Moscow is:

Ulitsa Udaltsova 2  
119415 Moscow  
Russian Federation

Telephone: 7 (495) 730-60-00  
Fax: 7 (495) 721-22-53

[www.novatek.ru](http://www.novatek.ru)

# Contact Information

## OFFICE IN TARKO-SALE

22-A, Pobedy Street, 629850, Tarko-Sale, Purovsky district, Yamal-Nenets Autonomous Region, Russia

## OFFICE IN MOSCOW

2, Udaltsova Street, 119415, Moscow, Russia

## CENTRAL INFORMATION SERVICE

Tel: +7 495 730-6000  
Fax: +7 495 721-2253  
E-mail: [novatek@novatek.ru](mailto:novatek@novatek.ru)

## PRESS SERVICE

Tel: +7 495 721-2207  
E-mail: [press@novatek.ru](mailto:press@novatek.ru)

## INVESTOR RELATIONS

Tel: +7 495 730-6013  
Fax: +7 495 730-6000  
E-mail: [ir@novatek.ru](mailto:ir@novatek.ru)

## REGISTRAR

AO "Independent Registrar Company"  
8 Ivana Franko Street,  
121108, Moscow, Russia

Tel: +7 495 926-8160  
Fax: +7 495 926-8178  
E-mail: [info@nrcreg.ru](mailto:info@nrcreg.ru)

## GDR PROGRAM ADMINISTRATOR

The Bank of New York Mellon  
Depositary Receipts  
101 Barclay Street, 22W, New York, NY 10286, USA

New York +1 212 815-4158  
London +44 207 163-7512  
Moscow +7 495 967-3110

## INDEPENDENT AUDITOR

AO PricewaterhouseCoopers Audit  
White Square Office Center, Butyrsky Val 10,  
125047, Moscow, Russia

Tel: +7 495 967-6000  
Fax: +7 495 967-6001

## INDEPENDENT RESERVES AUDITOR

DeGolyer and MacNaughton  
5001 Spring Valley Road, Suite 800, East Dallas  
Texas 75244, USA

Tel: +1 214 368-6391  
Fax: +1 214 369-4061  
E-mail: [degolyer@demac.com](mailto:degolyer@demac.com)

## WEBSITE:

[www.novatek.ru](http://www.novatek.ru) (Russian version)  
[www.novatek.ru/eng](http://www.novatek.ru/eng) (English version)