ZOLTAV
resources

ANNUAL REPORT 2017

INTRODUCTION
Corporate Information 1
Chairman's Statement 2
Our Assets 4
Review of Operations 6
Financial Review 10
Corporate and Social Responsibility 12
Board of Directors 14

FINANCIAL INFORMATION
Independent Auditors' Report 16
Financial Statements 18
Notes to the Accounts 22

BOARD OF DIRECTORS

Lea Verny
Independent Non-executive Chairman,
Senior Independent Director
(appointed as a Director on 20 December 2016;
appointed as Chairman on 22 March 2017;
and appointed as Senior Independent Director on 23 May 2017)

Alexander Gorodetsky
Independent Non-executive Director

Andrey Immel
Non-executive Director

Marcus Rhodes
Senior Independent Director
(resigned as Chairman on 22 March 2017;
and resigned as Senior Independent Director on 23 May 2017)

AUDIT COMMITTEE
Lea Verny (Chairman)
Andrey Immel

REMUNERATION AND NOMINATION COMMITTEE
Alexander Gorodetsky (Chairman)
Lea Verny

ADVISERS

CORPORATE ADMINISTRATOR
CO Services Cayman Limited
P.O. Box 10008, Willow House, Cricket Square,
Grand Cayman KY1-1001, Cayman Islands

REGISTERED OFFICE
PO Box 10008, Willow House, Cricket Square,
Grand Cayman KY1-1001, Cayman Islands

BANKERS
Barclays Private Clients International Limited
39-41 Broad Street, St Helier,
Jersey, JE4 8PU, Channel Islands

Deutsche Bank International Limited
St Paul's Gate, New Street, St Helier,
Jersey, JE4 8ZB, Channel Islands

NOMINATED ADVISER
SP Angel Corporate Finance LLP
Prince Frederick House, 35-39, Maddox Street,
London, W1S 2PP, United Kingdom

SOLICITORS
Berwin Leighton Paisner
Adelaide House, London Bridge, London,
EC4R 9HA, United Kingdom

JOINT BROKERS
SP Angel Corporate Finance LLP
Prince Frederick House, 35-39, Maddox Street,
London, W1S 2PP, United Kingdom

Panmure Gordon (UK) Limited
1 New Change, London, EC4M 9AF, United Kingdom

INDEPENDENT AUDITOR
Ernst & Young LLC
Sadovnicheskaya nab., 77, bld. 1, Moscow, 115035, Russia

REGISTRAR
Computershare Investor Services (Cayman) Limited
R&H Trust Co. Ltd, Windward 1,
Regatta Office Park, West Bay Road,
Grand Cayman KY1-1103, Cayman Islands

Management took the strategic decision in 2017 to transition the operational emphasis from production to exploration, while continuing to generate cash from the Permian fields already in production

Zoltav entered an exciting new phase in 2017 which has continued to gather pace in the year to date.

Management took the strategic decision in 2017 to transition the operational emphasis of the Company from production to exploration, while continuing to generate cash from the Permian fields already in production. Zoltav believes there is potential to yield substantial additional reserves and production from the Carbonian and Devonian horizons at Bortovoy which, if proven, would have a transformational impact on the size of the Bortovoy asset. The availability of modern seismic imaging, drilling and production technologies has enabled the Company to develop a work programme targeting these deeper structures which lie approximately 3,500-5,000 m below surface.

A considerable 3D seismic acquisition programme was undertaken in 2017 over the Carbonian and Devonian (and also prospective Permian) structures in the North Mokrous area of the Mokrousovskoye block, and has continued into 2018, using first-class contractors to acquire, process and interpret data. Preliminary interpretation of the first 180 sq km has been completed, with encouraging results announced in March 2018; and up to a further 536 sq km of 3D seismic data (of which 140 sq km has been completed in the year to date prior to the autumn weather pause) is anticipated to be acquired through the remainder of this year. Sufficient interpretation of these data is expected to be completed in time to allow for the positioning and drilling of the first Devonian exploration well, on North Mokrous, now expected in Q1 2019.

In support of the Company's work programme, we were delighted to announce earlier this month the recruitment of a team of highly accomplished former Bashneft and TNK-BP technical executives, led by Yuri Krasnevsky who became Zoltav's Director for Geology and Field Development. They and the rest of the technical staff and consultants are focused on growing the resource and production potential of the Bortovoy Licence.

In the Permian Basin, the horizon from which gas and oil is currently produced on the Bortovoy Licence, varying reservoir thickness and underperforming wells on the Karpenskoye and Zhdanovskoye fields in 2017 caused management to suspend the drilling programme in this structure until the interpretation of high quality 3D seismic data is completed - and additional 3D seismic data is acquired – during the course of 2018.

As a result of the suspension of the Permian Basin drilling programme, revenues from production declined in 2017, in line with management's expectations, by 10% to RUB 1.79 billion (2016: RUB 1.99 billion); while the net production[1] from the Western Gas Plant was an average of 7,075 boe/d (965 toe/d) in 2017, a decline of approximately 13% compared to 8,118 boe/d (1,108 toe/d) in 2016.

Despite this, however, as a result of Zoltav's rigorous commitment to cost and operational efficiencies, including the limitation of plant shut-downs through the application of new and improved chemical processes in the gas treatment unit, the Company was able to achieve a 5% increase in EBITDA[2] to RUB 888 million (2016: RUB 846 million). The EBITDA margin increased to 50% compared to 43% in 2016. Net cash flow from operating activities increased slightly to RUB 728 million (2016: RUB 719 million).

In light of the strategic shift to capital intensive exploration at Bortovoy, development activities on the Koltogor Licences in Western Siberia remain on hold. As a result, the Company made an allowance in the 2017 accounts for the full impairment of this asset (RUB 1.69 billion), which caused a net loss of RUB 1.27 billion (2016: RUB 97 million net profit). Excluding this non-cash item, the Company generated a much-improved net profit of RUB 182 million (an increase of 87%).

Efficient procurement, cost-cutting initiatives and zero-based budgeting allowed Zoltav to generate impressive cost savings across the business, notably a 38% decrease (RUB 114 million) in administrative and operating expenses and a 75% decrease (RUB 107.6 million) in other expenses of non-operating companies of the Group. These cost reductions in 2017 are mostly recurring and accordingly this positions the Company very attractively to leverage the benefits of a future increase in production.

Notwithstanding the anticipated decline in production revenues through 2018 as a result of the suspension of the Permian Basin drilling programme, the Company remains in good financial health, servicing its debt commitments and advancing this exciting exploration programme targeting the deeper structures – a programme in support of which, as announced in April 2018, the Company's two largest shareholders have decided to provide an unsecured loan facility of up to an aggregate US$ 12 million.

We look forward to reporting further progress as the exploration programme progresses.

Léa Verny

Lea Verny
Non-executive Chairman
21 May 2018

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1 Net production is the volume actually sold to customers. It comprises all extracted hydrocarbons, less own consumption and losses. The Company uses net production volumes throughout the 2017 annual report instead of the previously used total extracted volumes.
2 The Company historically calculates consolidated EBITDA as Operating profit added back with Depreciation, Depletion and Amortisation.

Zoltav believes there is potential to yield substantial additional reserves and production from the Carbonian and Devonian horizons at Bortovoy which, if proven, would have a transformational impact on the size of the Bortovoy asset. The availability of modern seismic imaging, drilling and production technologies has enabled the Company to develop a work programme targeting these deeper structures

PRODUCTION

Production from Zoltav's Western Gas Plant on the Bortovoy Licence, Saratov, averaged 7,075 boe/d (965 toe/d) during 2017, a decline of 13% when compared to 8,118 boe/d (1,108 toe/d) in 2016. This comprised average production of 40.4 bcf/d (1.15 mmcm/d) of natural gas and 337 bbls/d (43 t/d) of oil and condensate (2016: 46.0 bcf/d (1.3 mmcm/d) of natural gas and 449 bbls/d (57 t/d) of oil and condensate).

Overall in 2017, the Company produced 2.6 mmboe (2016: 3 mmboe) of gas and liquids, made up of:

- Natural gas: 14.8 bcf (418 mmcm) or 2.5 mmboe (335.5 mtoe) (2016: 16.8 bcf (475.8 mmcm) or 2.8 mmboe (381.9 mtoe))
- Oil and condensate: 122,962 bbls (15,663 t) (2016: 163,967 bbls (20,888 t))

The decline in production volumes during 2017 resulted from the underperformance of certain wells, as announced in the Company's half-year report in September 2017. Karpenskoye Well 117 was shut down in early January 2017 due to water cut; the newly drilled Zhdanovskoye Well 108 was put on production in March 2017 and is delivering materially lower gas production than initially anticipated; the newly drilled Zhdanovskoye Well 30 sidetrack, as announced in October 2017, was unsuccessful and is contributing lower than expected volumes; and water intrusion occurred on Zhdanovskoye Well 8 resulting in the anticipated shutdown of this well in July 2018.

The negative impact of these wells caused an aggregate reduction in production in 2017 of 2.75 bcf (77.9 mmcm) of natural gas and 9,908 bbls (1,626 t) of condensate.

Notwithstanding the performance of these wells, the Company's remaining well stock of 13 continued to produce in line with normal well production profiles.

Zoltav maintained its high focus on operational efficiency to eliminate the impact on profitability arising from the decline in production. For example, the use of new and improved chemical agents for the treatment of gas enabled the Company to reduce planned plant shutdowns by two during the year and save on the associated downtime. Furthermore, Zoltav undertook a programme to modernise the propane compressor cooling system to reduce the temperature during the summer months and thereby reduce the dew point. This enabled the Company to produce additional condensate and improved the quality of the product. For the first time, Zoltav installed sucker-rod pumping units on Karpenskoye Wells 17 and 5D for the secondary recovery of heavy oil, adding 4,286 bbls (546 T) of oil production. To further drive operational efficiencies during the year, Zoltav implemented a system of individual goal-setting for middle-chain technical staff and incentives for bringing additional ideas for operational excellence. This resulted, for example, in a successful scheme to re-use light fractions of hydrocarbons which were previously flared, resulting in an increase in liquids available for sale.

Zoltav is establishing plans to set up a well-head compressor on the Karpenskoye field by July 2018, giving rise to an estimated 128,843 boe (17,567 toe) of additional production annually.

Zoltav maintained its focus on operational efficiency to eliminate the impact on profitability arising from the decline in production, including the use of improved chemical agents for the treatment of gas to reduce planned plant shutdowns

EXPLORATION AND DEVELOPMENT

Bortovoy

As a result of the significant variation in reservoir thickness encountered in the Permian Basin in the Western Fields of the Bortovoy Licence, and operational difficulties encountered with certain wells, management took the decision in October 2017 to suspend the drilling programme in this horizon until the interpretation of high quality 3D seismic data is completed - and additional 3D seismic data is acquired – during the course of 2018.

In parallel, management took the decision to divert capex for the remainder of 2017 and 2018 to an exploration programme targeting the deeper Devonian and Carbonian structures in the west of the Bortovoy Licence, which lie approximately 3,500-5,000 m below surface and which, if proven, would have a transformational impact on the size and production profile of the Bortovoy asset.

A 3D seismic acquisition programme was undertaken in 2017 over the Carbonian and Devonian (and also prospective Permian) structures in the North Mokrous area of the Mokrousovskoye block and has continued in the year to date. Preliminary interpretation of the first 180 sq km has been completed, with encouraging results announced in March 2018; and up to a further 536 sq km of 3D seismic data (of which 140 sq km has been completed in the year to date prior to the autumn weather pause) is anticipated to be acquired through the remainder of 2018. Sufficient interpretation of these data is expected to be completed in time to allow for the positioning and drilling of the first Devonian exploration well, on North Mokrous, now expected in Q1 2019.

In support of the work programme, the Company announced in May 2018 the recruitment of former Bashneft and TNK-BP technical executives, led by Yuri Krasnevsky who became Zoltav's Director for Geology and Field Development.

Koltogor

The Koltogor Licences in the Khantiy Mansisk Autonomous Okrug, Western Siberia are not currently a focus of investment, as the Company is channeling capex into the exploration programme on the Bortovoy Licence. Management notes, however, the activity of the Bazhen Technology Centre launched by Gazprom Neft in 2017 in the same region as the Koltogor Licence. The centre is focusing on the development of advanced independent skills and technologies required for the cost-effective development of hydrocarbons in the Bazhenov formation, in which management believes there is potential in the Koltogor Licences.

GROUP RESERVES UNDER PRMS

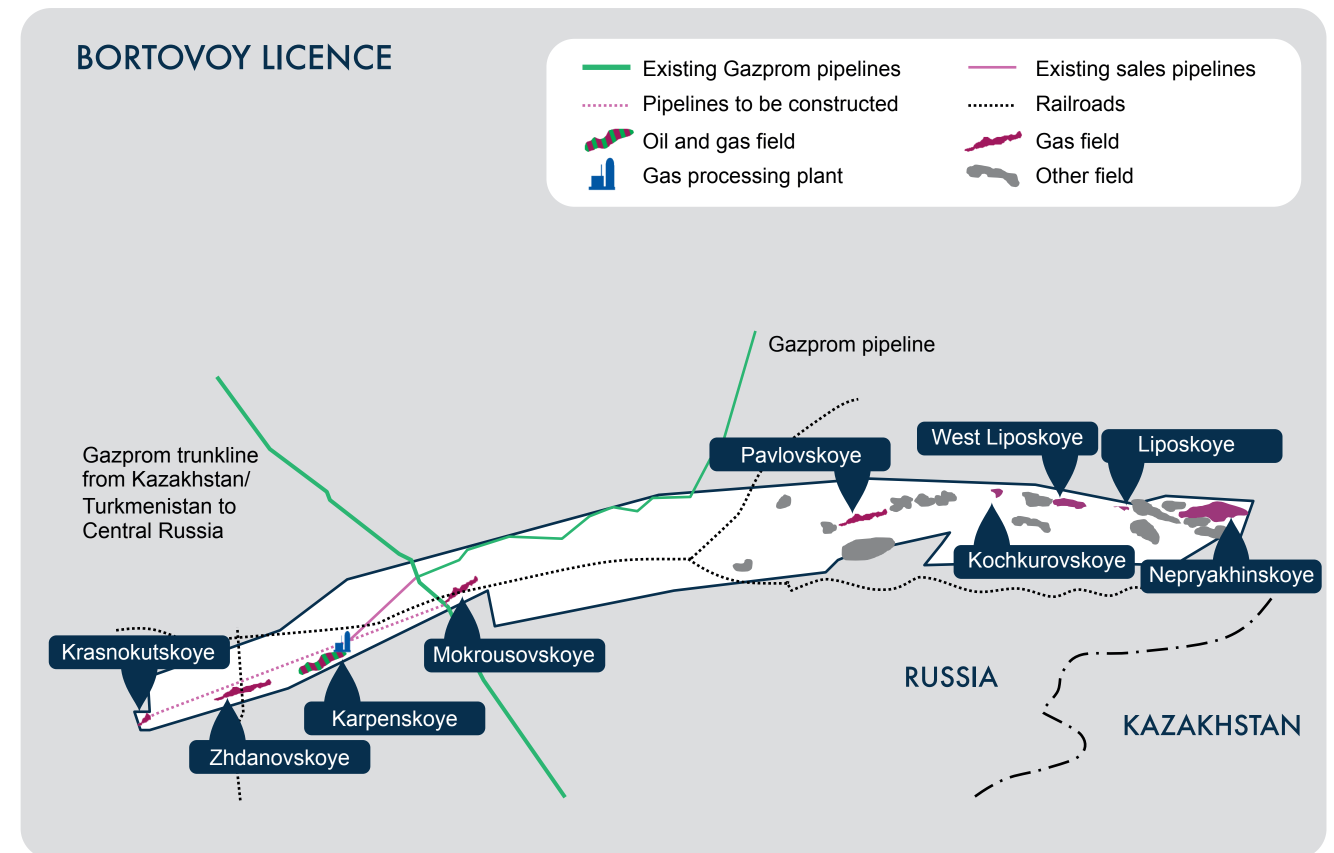
as per latest report of DeGolyer and MacNaughton (May 2014):

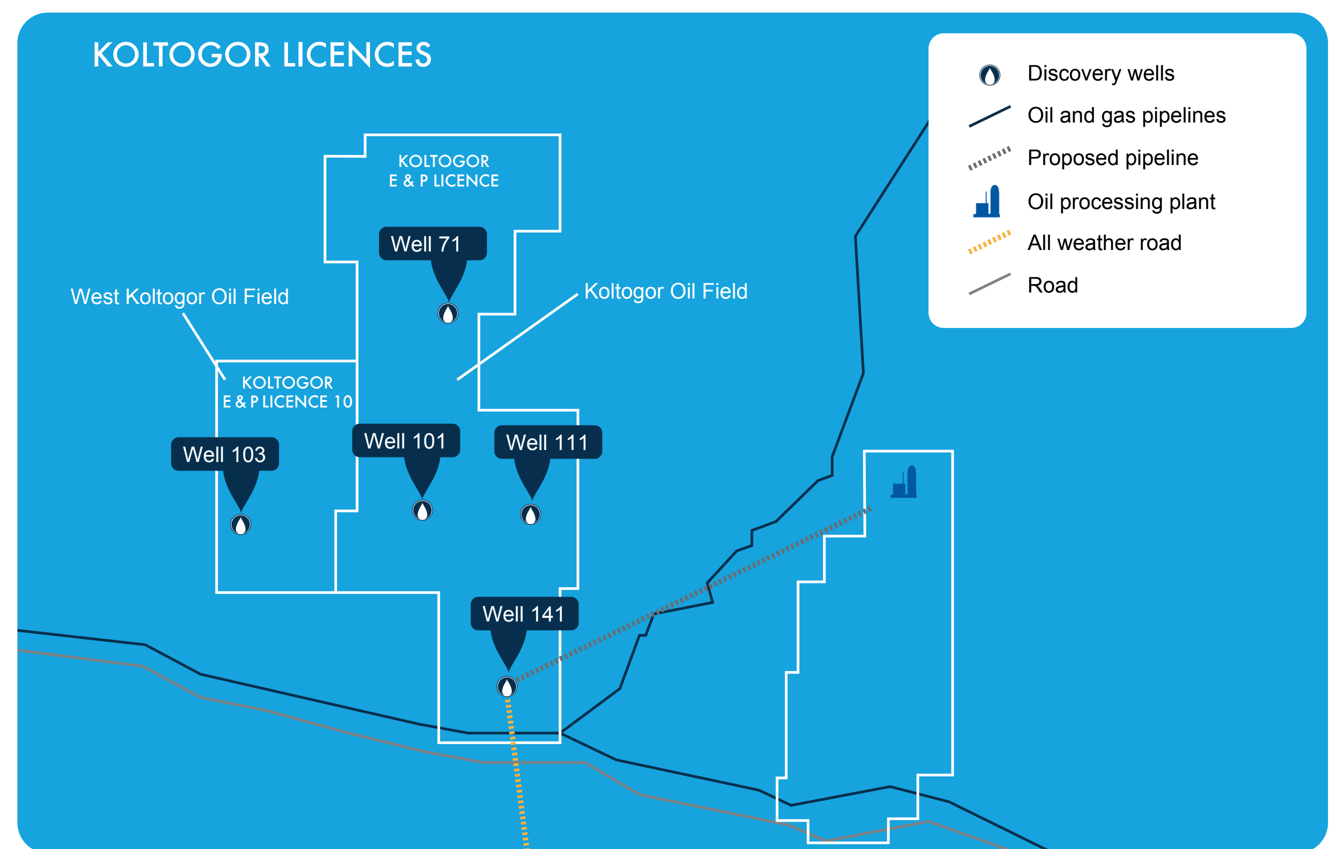
		Proved	Probable	Proved + Probable	Possible
Bortovoy Licence					
Gas	bcf	352.9	396.8	749.7	640.0
Oil & Liquids	mmbbls	2.0	1.8	3.8	2.4
Gas, Oil and Liquids	mmboe	62.0	69.2	131.2	111.2
Koltogor Licences					
Gas	bcf	0.5	23.5	24.0	55.7
Oil	mmbbls	1.6	73.5	75.1	174.0
Gas & Oil	mmboe	1.7	77.5	79.2	183.5
Total					
Gas	bcf	353.4	420.3	773.7	695.7
Oil & Liquids	mmbbls	3.6	75.3	78.9	176.4
Gas, Oil and Liquids	mmboe	63.7	146.7	210.4	294.7

The Company is planning a re-evaluation of reserves under PRMS following completion of the exploration programme currently ongoing on the Bortovoy Licence.

Conversion rates

Tonnes of crude oil produced are translated into barrels using conversion rates reflecting oil density from each of the fields. Crude oil and liquid hydrocarbons expressed in barrels are translated from tonnes using a conversion rate of 7.85 barrels per tonne. Translations of cubic feet to cubic metres are made at the rate of 35.3 cubic feet per cubic metre. Translations of barrels of crude oil and liquid hydrocarbons into barrels of oil equivalent ("boe") are made at the rate of 1 barrel per boe and of cubic feet into boe at the rate of 290 cubic feet per boe.





Management continued to focus throughout 2017 on challenging non-strategic costs, analysing capital expenditures and operating efficiently. As a result, and despite the production decline, Zoltav was able to achieve a 5% increase in EBITDA to RUB 888 million (2016: RUB 846 million).

REVENUE

The Group's revenues in 2017 decreased by 10% to RUB 1.79 billion, compared to RUB 1.99 billion in 2016, as a result of the decline in production.

85% of revenue was derived from gas sold to Mezhregiongaz, a Gazprom subsidiary, at the transfer point on entry to the Central Asia – Center gas pipeline system. The gas prices are fixed in a contract with Mezhregiongaz and are subject to indexation. The Russian Government approved a 3.9% gas price increase from 1 July 2017 and accordingly the Company signed an addendum to its contract with Mezhregiongaz. We anticipate that a further increase of 2% in gas price indexation will be approved by the Russian Government in June 2018 which will further benefit the Company.

The remaining revenue was from oil and condensate sold to a small number of different buyers either directly at the Western Gas Plant or via a petroleum storage depot with access to the railway. The sale price is set through a tender process starting each month following the publication of the Rosneft tender results, which influence domestic oil prices. In 2017, Zoltav started to sell heavy oil produced from Karpenskoye Wells 17 and 5D and priced on a formula linked to Brent quotes on Cortes (part of Thomson Reuters).

Oil prices were favourable in 2017 and Zoltav sold liquid products above the market, according to our net back calculations for oil in our region and with our qualities. The Company began diversifying its portfolio of buyers to reduce dependence on its main purchaser in 2016. These factors resulted in a positive impact on average oil and condensate sales prices which were RUB 2,100/bbl (RUB 16,500/t) in 2017 compared to RUB 1,700/bbl (RUB 13,200/t) in 2016.

COST OF SALES AND G&A COSTS

Total cost of sales was RUB 1.15 billion (2016: RUB 1.15 billion). This comprised RUB 371.6 million of mineral extraction tax (2016: RUB 406.5 million), RUB 437.2 million of depreciation and depletion of assets (2016: RUB 404.7 million) and RUB 338 million of other cost of sales (2016: RUB 344 million).

The Group's operational and G&A costs decreased by 38% to RUB 185 million (2016: RUB 299 million), while other expenses decreased by 75% to RUB 35 million (2016: RUB 143 million), mostly achieved through administrative staff reduction of 20%, cutting non-strategic costs and maintenance optimisation. Examples of material cost savings achieved in the year, include:

- containing the expenses of non-operational entities to a minimum and reducing the cost of administrative personnel - RUB 115 million saving;
- changing the contractor for heavy compressor parts and services - RUB 15 million saving;
- shutting down Heavy Compressor 1540 and redirecting its associated gas flow, allowing the Company to avoid associated maintenance costs; and turning off two out of three power generating units which were also maintenance heavy - RUB 12.8 million saving;
- switching to improved chemical agents for the treatment of gas, enabling the Company to reduce planned plant shutdowns by two during the year and save on the associated downtime - RUB 5 million saving;
- changing the methanol flow and regeneration unit and making the system 'closed-loop' with minimal waste and minimising the procurement of external methanol - RUB 4.6 million saving;
- renegotiating contractual terms for the renting of land plots - RUB 4 million saving; and
- identifying a Russian substitute for an expensive foreign catalyst which was previously used in the sulphur production unit - RUB 2.4 million saving.

Other cost of sales is mainly operating expenses of Diall Alliance, the Bortovoy operating company, which decreased by 2% to RUB 338 million (2016: RUB 344.1 million) despite the expiration of a property tax incentive which was granted by the Saratov regional tax authority during gas plant construction (annual property tax increased from RUB 16.8 million to RUB 47.1 million).

OPERATING PROFIT

Zoltav achieved an operating profit for 2017 of RUB 450 million, compared to RUB 441 million in 2016.

Finance costs of RUB 225 million (2016: RUB 268 million) are mainly represented by interest on the remaining RUB 1.56 billion Sberbank facility. The Company is negotiating terms which management believes will reduce finance costs in 2018.

PROFIT BEFORE TAX

Zoltav generated a RUB 1.43 billion loss, compared to RUB 197 million profit in 2016, due to an impairment allowance amounting to RUB 1.69 billion in respect of the Koltogor Licences for which development activities are currently on hold.

TAXATION

Production based tax for the period was RUB 372 million (2016: RUB 407 million) which is recognised in the cost of sales. The MET tax formula is based on multi-component gas composition, average gas prices and reservoir complexity and maturity. The effective MET rate applicable for the period was flat at RUB 24/mcf or RUB 849/mcm (2016: RUB 23/mcf or RUB 810/mcm).

In addition to production taxes, the Group was subject to a 2.2% property tax which is based on the net book value of Russian assets calculated for property tax purposes. Property tax on the major part of the Bortovoy operating company's assets, including the Western Gas Plant, is paid at a reduced tax rate of 0.1%, in line with tax incentives for regional investment projects. There was no clear legal instruction regarding the maturity of a tax incentive previously referred to in the Company's half-year report, resulting from management's inquiries with the tax authority. Accordingly, the Company recognised an additional tax charge in the amount of RUB 28 million during the year.

NET PROFIT

As noted above, the Company made an allowance in the 2017 accounts for the full impairment of the Koltogor Licences (RUB 1.69 billion), which caused a net loss of RUB 1.27 billion (2016: RUB 97 million net profit). Excluding this non-cash item, the Company generated a much-improved net profit of RUB 182 million (an increase of 87%).

CASH

Net cash generated from operating activities was RUB 728 million (2016: RUB 719 million).

Diall Alliance successfully serviced its credit facility with PJSC Sberbank and repaid a further RUB 300 million of the principal amount (RUB 1,860 million at 31 December 2016) according to its schedule. The Company remains in line with the covenants of its credit facility agreement.

Zoltav has sufficient liquidity to fund its current seismic programme and announced in April that the Board of Directors approved an agreement with its two largest shareholders for their provision of an unsecured loan facility of up to an aggregate US$12 million in further support of the exploration programme.

Total cash at the end of the period was RUB 286.75 million (2016: RUB 294 million).

Kirill Suetov
Chief Financial Officer
21 May 2018

FINANCIAL PERFORMANCE AT A GLANCE

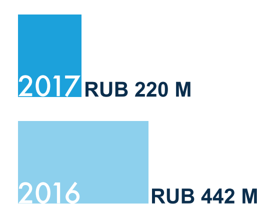
REVENUE

Down 10% on lower production

EBITDA

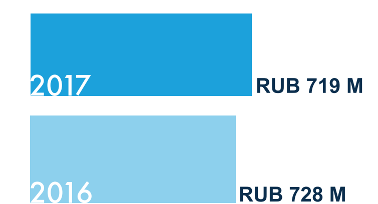
Up 5% from cost and operating efficiencies

SELLING, GENERAL & ADMINISTRATIVE COSTS



Down 50% on cutting of non-strategic costs

NET CASH GENERATION



Up 1% on cost optimisation

HEALTH, SAFETY AND EMPLOYEE WELFARE

Our highest priority is providing a safe and healthy work environment and to conducting our activities in a safe and environmentally protective manner. Our employees and officers are expected to perform their duties consistent with the site-specific safety and environmental rules and regulations and are expected to obey all local, regional and national laws and regulations.

We are committed to the goals of:

- Avoiding harm to all personnel involved in, or affected by, our operations
- Complying with all the applicable legal and other requirements where we operate
- Achieving continual improvement in our HSE performance

We are proud of our HSE achievement of zero injuries to personnel and contractors in 2017.

During the year, Zoltav changed its supplier of personal safety equipment, placing a strong emphasis on weight reduction and stress-testing key equipment including suits, gloves, boots and gas respirators. As a result, we have high-graded the equipment.

The company continues to offer a market leading health insurance plan, which now includes direct access to any nearby clinics.

Zoltav is proud to provide sponsorship for higher technical education for employees seeking to advance their engineering and technology skills.

We undertook a number of community initiatives in 2017, from sponsorships to infrastructure improvements

ENVIRONMENT

Responsible environmental management is a core component of our approach to CSR. We are committed to complying with applicable legislation and to identifying risks to the environment. We recognise that oil and gas exploration and production activities can have an impact on the environment. As such we aim, wherever possible, to implement processes to avoid, mitigate or manage any adverse impacts our operations might have. We are committed to employing highly competent personnel who share the company's values and who are themselves committed to implementing our high standards of environmental performance in everything they do.

The company and its seismic contractor maintained close contact with local communities to ensure minimal impact on communities and wildlife during the substantial seismic programme undertaken in 2017.

We strive to carry out our 3D seismic activities in the most environmentally responsible way

COMMUNITY ENGAGEMENT

Zoltav knows that positive relations with local communities are central to the success of oil and gas operations, and we continually seek both to maximise local involvement and to have a positive impact on local communities. We are also committed to building and utilising skills available locally at all levels.

We continued our active community engagement in the Saratov region, where our Bortovoy Licence and Western Gas Plant are situated, throughout 2017. Among other activities, the company carried out, at its expense, repair and redecoration works to the community centre in Lavrovka village, and repair works to a school in Karpenka village – both in the Krasnokutskiy district of the Saratov region. We drilled water wells in Zhdanovka village and purchased water pumps for the non-stop supply of fresh water. The organisation was also proud to sponsor a local initiative aimed at combatting drugs and crime amongst teenagers through active participation in sports. The company provided uniforms and sporting accessories, covered travel expenses for competitions and funded prizes.

ANTI-BRIBERY & CORRUPTION POLICY

Our policy is to conduct all our business in an honest and ethical manner. We take a zero-tolerance approach to bribery and corruption and are committed to acting professionally, fairly and with integrity in all our business dealings and relationships wherever we operate and implementing and enforcing effective systems to counter bribery. We will uphold all laws relevant to countering bribery and corruption in all the jurisdictions in which we operate.

LEA VERNY
Non-executive Chairman, Senior Independent Director

Lea Verny was appointed as a non-executive director in December 2016. She has significant and high level corporate finance experience, with particular expertise in Russia. Since 2008, Lea Verny has acted as an independent financial adviser on cross-border transactions. Prior to becoming an independent consultant, Lea Verny served as a private banker with Banque Pictet, Switzerland, where she was responsible for developing the bank's activities in Russia, following a career of more than a decade with HSBC. From 2001 to 2007, Lea Verny was Head of Investment Banking for HSBC Bank plc in Moscow, during which time she advised on structured transactions for large Russian and CIS corporations including Lukoil, Rostelekom, Eastern Oil Company and Rosbank. Between 1997 and 2001, Ms Verny was a representative of HSBC Investment Bank plc in Russia, where she was responsible for establishing the bank's presence in the country and developing opportunities specifically within the oil and gas sector. Lea Verny holds a Bachelor's degree in Statistics and International Relations from the Hebrew University in Jerusalem as well as an MBA from INSEAD in France.

ALEXANDER GORODETSKY
Independent Non-executive Director

Alexander Gorodetsky was appointed as a non-executive director in September 2015. He is currently the general partner of Strategy Capital Advisor Limited, a private equity fund established in 2009 with a mandate to invest in projects, including within the oil and gas sector, across the former Soviet Union. Prior to Strategy Capital Advisor Limited, Alexander Gorodetsky was first deputy to the chairman of East One Group, an international investment advisory group providing strategic and investment management services. During his time at East One Group, he assisted in the strategic development of over 25 portfolio companies including GEO ALLIANCE Group, one of the leading independent oil and gas exploration and production groups in Ukraine. From 2000-2006, Alexander Gorodetsky was president/business unit leader for TNK BP Ukraine. He contributed significantly to the increased brand awareness of TNK-BP in the Ukrainian market, where it is among the leading oil and gas companies. He began his career in 1995 within Alfa-Eco, a leading gas and oil trading business in Russia.

ANDREY IMMEL
Non-executive Director

Andrey Immel was appointed as a non-executive director in September 2015. He is an experienced Russian corporate lawyer. He has, since 2012, been the head of the legal department of Moscow-based Contact-Service LLC, a real estate company, where his responsibilities include corporate governance and the provision of legal support for transactions. From 2008-2012, Andrey Immel worked for Himuglemet, a manufacturer of conveyer band and other components for coal mines, both as legal counsel and as a corporate and tax lawyer. His responsibilities included legal due diligence and support for corporate transactions.

To the Shareholders and Board of Directors of Zoltav Resources Inc.

Opinion

We have audited the consolidated financial statements of Zoltav Resources Inc. and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for 2017, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017 and its consolidated financial performance and its consolidated cash flows for 2017 in accordance with International Financial Reporting Standards (IFRSs).

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 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 that are relevant to our audit of the consolidated financial statements in the Russian Federation, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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. For the matter below, our description of how our audit addressed this matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report, including in relation to this matter. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matter below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

KEY AUDIT MATTER	HOW OUR AUDIT ADDRESSED THE KEY AUDIT MATTER
Impairment of exploration and evaluation assets	
In 2017 the Group recognized an impairment of exploration and evaluation assets of Koltogor oil field. We considered this matter to be of most significance in our audit due to significance of the amount of impairment charge and significant judgment involved in its assessment, especially in respect of sources of financing of Koltogor oil field development. Information on impairment of exploration and evaluation assets is disclosed in Note 11 to the consolidated financial statements.	We assessed facts and circumstances suggesting that the carrying amount of exploration and evaluation assets may exceed their recoverable amount. We analysed necessary budgeted expenditure on further exploration for and evaluation of mineral resources in Koltogor oil field. We analyzed the possibility of the Group to finance Koltogor oil field development. We assessed possible sources of financing and management plans in respect of future development.

Other information included in the Annual Report for 2017

Other information consists of the information included in the Annual Report for 2017, other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information.

Our opinion on the consolidated financial statements does not cover the other information and we do 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 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, 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.

Responsibilities of management and the Audit Committee for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs, 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.

The Audit Committee is responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the 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 skepticism 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 Company 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 the Audit Committee 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 the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with it 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 the Audit Committee, 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 partner in charge of the audit resulting in this independent auditor's report is T.L. Okolotina.

T.L. Okolotina
Partner
Ernst & Young LLC
21 May 2018

Details of the audited entity
NAME: Zoltav Resources Inc.
Record made in the Registar of Companies, Cayman Islands on 18 November 2003, Registration Number 130605.
ADDRESS: PO Box 10008, Willow House, Cricket Square, Grand Cayman KY1-1001, Cayman Islands.

Details of the auditor
NAME: Ernst & Young LLC
Record made in the State Register of Legal Entities on 5 December 2002, State Registration Number 1027739707203.
ADDRESS: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050648.

Consolidated statement of comprehensive income for the year ended 31 December 2017
(in '000s of Russian rubles, unless otherwise stated)

	Note	2017	2016
Revenue	4	**1,790,524**	**1,989,430**
Cost of sales			
Mineral extraction tax		(371,620)	(406,499)
Depreciation and depletion		(437,160)	(404,684)
Other cost of sales		(338,032)	(344,104)
Total cost of sales	5	**(1,146,812)**	**(1,155,287)**
Gross profit		**643,712**	**834,143**
Operating, administrative and selling expenses	6	(184,948)	(299,346)
Other income	8	27,005	49,076
Other expenses	8	(35,301)	(142,860)
Operating profit		**450,468**	**441,013**
Impairment of exploration and evaluation assets	11	(1,685,632)	-
Finance income	9	27,960	24,409
Finance costs	9	(225,741)	(267,985)
(Loss)/profit before tax		**(1,432,945)**	**197,437**
Income tax benefit/(expense)	10	162,967	(100,336)
(Loss)/profit for the year attributable to owners of the parent being total comprehensive income		**(1,269,978)**	**97,101**

		RUB	RUB
Loss)/earnings per share attributable to owners of the parent			
Basic	19	(8.95)	0.68
Diluted	19	(8.95)	0.67

Kirill Suetov
Chief Financial Officer

21 May 2018

The accompanying notes on pages 22-46 are an integral part of these consolidated financial statements.

Consolidated statement of financial position as at 31 December 2017
(in '000s of Russian rubles, unless otherwise stated)

	Note	As at 31 December 2017	As at 31 December 2016
ASSETS			
Non-current assets			
Exploration and evaluation assets	11	3,259,353	4,788,314
Property, plant and equipment	12	4,007,302	4,211,254
Total non-current assets		**7,266,655**	**8,999,568**
Current assets			
Inventories	13	20,877	18,830
Trade and other receivables	14	152,574	172,294
Other current non-financial assets	14	11,400	15,186
Cash and cash equivalents	15	286,754	294,254
Total current assets		**471,605**	**500,564**
TOTAL ASSETS		**7,738,260**	**9,500,132**
EQUITY AND LIABILITIES			
Share capital	16	970,218	970,218
Share premium		5,498,009	5,498,009
Other reserves		1,366,172	1,429,341
Accumulated losses		(2,562,988)	(1,356,179)
Total equity		**5,271,411**	**6,541,389**
Non-current liabilities			
Borrowings	21	1,253,014	1,548,789
Provisions	22	386,152	359,153
Other payables	24	62,771	57,874
Deferred tax liabilities	23	270,836	433,888
Total non-current liabilities		**1,972,773**	**2,399,704**
Current liabilities			
Borrowings	21	309,172	311,160
Finance lease liability		1,666	–
Other tax payables	18	89,381	118,500
Trade and other payables	24	93,857	129,379
Total current liabilities		**494,076**	**559,039**
TOTAL LIABILITIES		**2,466,849**	**2,958,743**
TOTAL EQUITY AND LIABILITIES		**7,738,260**	**9,500,132**

The accompanying notes on pages 22-46 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows for the year ended 31 December 2017
(in '000s of Russian rubles, unless otherwise stated)

	Note	2017	2016
Cash flows from operating activities			
(Loss)/profit before tax		**(1,432,945)**	**197,437**
Adjustments for:			
Depreciation and depletion	12	440,387	408,939
Impairment of exploration and evaluation assets	11	1,685,632	-
Finance costs	9	225,741	267,985
Finance income	9	(27,960)	(24,409)
Loss on disposal of property, plant and equipment, net of income from sale of property, plant and equipment	8	28,652	86,624
Write-off of accounts receivable and other current assets, accounts receivable bad debt provision accrual	8	1,908	26,986
Change in the estimates of decommissioning and environmental restoration provision		(13,448)	(34,076)
Other income and expenses		708	11,317
Operating cash inflows before working capital changes		**908,675**	**940,803**
Decrease/(increase) in inventories		1,590	(6,162)
Change in trade and other receivables and other current non-financial assets		23,430	(19,022)
Decrease in trade and other payables		(16,372)	(22,298)
Increase in other tax payables		(29,119)	27,834
Net cash from operating activities before income tax and interests		**888,204**	**921,155**
Interest received		28,316	25,158
Interest paid	21	(188,660)	(227,138)
Income tax paid		(85)	(105)
Net cash from operating activities		**727,775**	**719,070**
Cash flows from investing activities			
Proceeds from sale of property, plant and equipment		14,633	-
Capital expenditure on exploration and evaluation activities		(132,635)	(56,048)
Purchase of property, plant and equipment		(317,063)	(436,416)
Net cash used in investing activities		**(435,065)**	**(492,464)**
Cash flows from financing activities			
Repayment of obligations under finance leases		(39)	-
Repayment of borrowings	21	(300,000)	(360,000)
Net cash used in financing activities		**(300,039)**	**(360,000)**
Net change in cash and cash equivalents		**(7,329)**	**(133,394)**
Net foreign exchange difference		(171)	(902)
Cash and cash equivalents at the beginning of the year		**294,254**	**428,550**
Cash and cash equivalents at the end of the year	15	**286,754**	**294,254**

The accompanying notes on pages 22-46 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity for the year ended 31 December 2017
(in '000s of Russian rubles, unless otherwise stated)

		Attributable to owners of the Parent					
	Note	Share capital	Share premium	Capital reserve	Employee share-based compensation reserve	Accumulated losses	Total equity
At 1 January 2016		**970,218**	**5,498,009**	**1,343,566**	**85,775**	**(1,453,280)**	**6,444,288**
Profit for the year		-	-	-	-	97,101	**97,101**
Total comprehensive income		-	-	-	-	**97,101**	**97,101**
At 31 December 2016		**970,218**	**5,498,009**	**1,343,566**	**85,775**	**(1,356,179)**	**6,541,389**
At 1 January 2017		**970,218**	**5,498,009**	**1,343,566**	**85,775**	**(1,356,179)**	**6,541,389**
Employee share-based compensation (note 19)		-	-	-	(63,169)	63,169	**-**
Transactions with owners		-	-	-	**(63,169)**	**63,169**	**-**
Loss for the year		-	-	-	-	(1,269,978)	**(1,269,978)**
Total comprehensive income		**-**	**-**	**-**	**-**	**(1,269,978)**	**(1,269,978)**
At 31 December 2017		**970,218**	**5,498,009**	**1,343,566**	**22,606**	**(2,562,988)**	**5,271,411**

The accompanying notes on pages 22-46 are an integral part of these consolidated financial statements.

1. Background

1.1 The Company and its operations

Zoltav Group (the Group) comprises Zoltav Resources Inc. (the Company), together with its subsidiaries:

Name	Place of incorporation	Function	Share of the Company in a subsidiary as of 31 December 2017 and 2016
CenGeo Holdings Limited (hereinafter "CenGeo Holdings")	Cyprus	Holding company	100%
CJSC SibGeCo (hereinafter "SibGeCo")	Russia	Operating company	100%
Royal Atlantic Energy (Cyprus) Limited (hereinafter "Royal")	Cyprus	Holding company	100%
Diall Alliance LLC (hereinafter "Diall")	Russia	Operating company	100%
Zoltav Resource LLC	Russia	Management company	100%

The Company was incorporated in the Cayman Islands on 18 November 2003. The principal activities of the Company and its subsidiaries is the acquisition, exploration, development and production of hydrocarbons in the Russian Federation. The Company's shares are listed on the Alternative Investment Market of the London Stock Exchange.

1.2 Russian business environment

The Group's operations are primarily located in the Russian Federation.

The Russian Federation displays certain characteristics of an emerging market. Its economy is particularly sensitive to oil and gas prices. The legal, tax and regulatory frameworks continue to develop and are subject to frequent changes and varying interpretations. The Russian economy was growing in 2017, after overcoming the economic recession of 2015 and 2016. The economy is negatively impacted by low oil prices, ongoing political tension in the region and international sanctions against certain Russian companies and individuals. The financial markets continue to be volatile.

The combination of the above resulted in reduced access to capital, a higher cost of capital and uncertainty regarding economic growth, which could negatively affect the Group's future financial position, results of operations and business prospects. Management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

1.3 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (EU), International Financial Reporting Interpretations Committee (IFRIC) interpretations, and the Companies Act 2006 applicable to companies reporting under IFRS. The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 2.

1.4 Going concern

The consolidated financial statements have been prepared on a going concern basis as the Directors have concluded that the Group will continue to have access to sufficient funds in order to meet its obligations as they fall due for at least the foreseeable future as explained further in the Directors Report. The Group's current liabilities exceed current assets by 22,471 as at 31 December 2017. For mitigation factors, please, see Note 26.1.

1.5 Disclosure of impact of new and future accounting standards

a) Adoption of new and amended standards

In the preparation of these consolidated financial statements, the Group followed the same accounting policies and methods of computation as compared with those applied in the previous year, except for the adoption of new standards and interpretations and revision of the existing standards as of 1 January 2017. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

Although these new standards and amendments applied for the first time in 2017, they did not have a material impact on the annual consolidated financial statements of the Group.

New/revised standards and Interpretations Adopted in 2017	Effective for annual periods beginning on or after
Annual Improvements to IFRSs 2014-2016 Cycle	
Amendments to IFRS 12 *Disclosure of Interests in Other Entities: Clarification of the scope of disclosure requirements in IFRS 12*	1 January 2017
Amendments to IAS 7: *Disclosure Initiative*	1 January 2017
Amendments to IAS 12: *Recognition to Deferred Tax Assets for Unrealised Losses*	1 January 2017

b) New accounting pronouncements

A number of new and amended standards were not effective for the year ended 31 December 2017 and have not been applied in these consolidated financial statements.

Standards issued but not yet effective in the European Union	Effective for annual periods beginning on or after
Amendments to IAS 40 – *Transfers of Investment Property*	1 January 2018
Amendments to IFRS 4 – Applying IFRS 9 *Financial Instruments* with IFRS 4 *Insurance Contracts*	1 January 2018
Annual improvements to IFRSs 2014-2016 Cycle	1 January 2018
IFRS 9 *Financial Instruments*	1 January 2018
IFRS 15 *Revenue from Contracts with Customers*	1 January 2018
Clarification to IFRS 15 *Revenue from Contracts with Customers*	1 January 2018
IFRIC 22 *Foreign Currency Transactions and Advance Consideration*	1 January 2018
Amendments to IFRS 2 – *Classification and Measurement of Share-based Payment Transactions*	1 January 2018
IFRS 16 *Leases*	1 January 2019
Amendments to IFRS 9: *Prepayment Features with Negative Compensation*	1 January 2019
Annual improvements to IFRSs 2015-2017 Cycle	1 January 2019*
IFRS 17 *Insurance Contracts*	1 January 2021*
IFRIC 23 *Uncertainty over Income Tax Treatments*	1 January 2019*
Amendments to IAS 28: *Long-term Interests in Associates and Joint Ventures*	1 January 2019*
Amendments to IAS 19: *Plan Amendment, Curtailment or Settlement*	1 January 2019*
Amendments to References to the Conceptual Framework in IFRS Standards	1 January 2020*

* Subject to EU endorsement.

IFRS 9 Financial Instruments: Classification and Measurement

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments which reflects all phases of the financial instruments project and replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory.

a) Classification

Loans as well as trade receivables are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. The Group analysed the contractual cash flow characteristics of those instruments and concluded that they meet the criteria for amortised cost measurement under IFRS 9. Therefore, reclassification for these instruments is not required.

b) Impairment
IFRS 9 requires the Group to now use an expected credit loss model for its trade receivables measured at amortised cost and cash in banks, either on a 12-month or lifetime basis. The Group expects to apply the simplified approach and record lifetime expected losses on all trade receivables measured at amortised cost and cash in banks. Given the short-term nature of these assets, the Group considered these changes had insignificant impact.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The principles in IFRS 15 provide a more structured approach to measuring and recognizing revenue. The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2018 with early adoption permitted. Given the basic terms of revenue contracts, reliable customers and absence of significant finance component in sales, the Group preliminary assessed that the impact of IFRS 15 will not be significant. Final evaluation has not been completed yet.

IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

In 2018, the Group will continue to assess the potential effect of IFRS 16 on its financial statements.

From application of the other standards issued but not yet effective the Group expects no effect on its consolidated financial statements.

1.6 Basis of consolidation

The consolidated financial statements comprise the financial statements of the Group and its subsidiaries as at 31 December 2017. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee;
- The ability to use its power over the investee to affect its returns

Generally, there is a presumption that a majority of voting rights results in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement(s) with the other vote holders of the investee;
- Rights arising from other contractual arrangements;
- The Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities and components of equity, while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

1.7 Acquisitions, asset purchases and disposals

Transactions involving the purchases of an individual field interest, or a group of field interests, that do not qualify as a business combination are treated as asset purchases, irrespective of whether the specific transactions involved the transfer of the field interests directly or the transfer of an incorporated entity. Accordingly, no goodwill or deferred tax gross up arises. The purchase consideration is allocated to the assets and liabilities purchased on an appropriate basis. Proceeds from the disposal are applied to the carrying amount of the specific intangible asset or development and production assets disposed of and any surplus is recorded as a gain on disposal in the statement of comprehensive income.

1.8 Business combinations

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, which is measured at acquisition date fair value, and the amount of any non-controlling interests in the acquiree. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability that is a financial instrument and within the scope of IAS 39 Financial Instruments: Recognition and Measurement is measured at fair value with the changes in fair value recognised in the statement of profit or loss.

Goodwill is initially measured at cost being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interests and any previous interest held over the net identifiable assets acquired and liabilities assumed. If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the Group re-assesses whether it has correctly identified all of the assets acquired and all of the liabilities assumed and reviews the procedures used to measure the amounts to be recognised at the acquisition date. If the reassessment still results in an excess of the fair value of net assets acquired over the aggregate consideration transferred, then the gain is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill has been allocated to a cash-generating unit (CGU) and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the cash-generating unit retained.

1.9 Segment reporting

Segment reporting follows the Group's internal reporting structure.

Operating segments are defined as components of the Group where separate financial information is available and reported regularly to the chief operating decision maker ("CODM"), which is determined to be the Board of Directors of the Company. The Board of Directors decides how to allocate resources and assesses operational and financial performance using the information provided.

The CODM receives monthly IFRS-based financial information for the Group and its development and production entities. The Group has other entities that engage as either head office or in a corporate capacity, or as holding companies. Management has concluded that, due to the application of aggregation criteria, separate financial information for segments is not required. No geographic segmental information is presented, as all of the companies' operating activities are based in the Russian Federation.

Management has therefore determined that the operations of the Group comprise one operating segment and the Group operates in only one geographic area – the Russian Federation.

1.10 Foreign currency translation

(a) Functional and presentation currency
The functional currency of the Group entities is the Russian ruble ("RUB"), the currency of the primary economic environment in which the Group operates.

The presentation currency is RUB, which the Board considers more representative for users of these consolidated financial statements to better assess the performance of the Group.

(b) Transactions and balances
Transactions in foreign currencies are initially recorded by the Group's entities at their respective functional currency spot rates at the date the transaction first qualifies for recognition.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date.

Differences arising on the settlement or translation of monetary items are recognised in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions.

(c) Group companies
Loans between Group entities and related foreign exchange gains or losses are eliminated upon consolidation.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities on the acquisition are treated as assets and liabilities of foreign operation and translated at the spot rate of exchange at the reporting date.

The period-end exchange rates and the average exchange rates for the respective reporting periods are indicated below.

	2017	2016
RUB/USD as at 31 December	57.6002	60.6569
RUB/USD average for the year ended 31 December	58.3529	67.0349

1.11 Exploration and evaluation assets

The Company and its subsidiaries apply the successful efforts method of accounting for Exploration and Evaluation ("E&E") costs, in accordance with IFRS 6 *Exploration for and Evaluation of Mineral Resources*. Costs are accumulated on a field-by-field basis.

(a) Drilling, seismic and other costs
Costs directly associated with an exploration well, including certain geological and geophysical costs, and exploration and property leasehold acquisition costs, are capitalised until the reserves are evaluated. If it is determined that a commercial discovery has not been achieved, these costs are charged to expense after the conclusion of appraisal activities. Exploration costs such as geological and geophysical that are not directly related to an exploration well are expensed as incurred.

Capital expenditure is recognised as property, plant and equipment or intangible assets in the financial statements in accordance with the nature of the expenditure and the stage of development of the associated field, i.e. exploration, development, or production. Once commercial reserves are found, exploration and evaluation assets are tested for impairment and transferred to development property, plant and equipment or intangible assets. No depreciation or amortisation is charged during the exploration and evaluation phase.

(b) Sub-soil licences
Costs incurred prior to the award of oil and gas licences, concessions and other exploration rights are expensed in profit or loss. Costs incurred on the acquisition of a licence interest are initially capitalised on a licence by licence basis and are capitalised within exploration and evaluation assets and held un-depleted until the exploration phase of the licence is complete or commercial reserves have been discovered at which time the costs are transferred to development assets as part of property, plant and equipment – oil and gas assets.

1.12 Property, plant and equipment

(a) Property, plant and equipment − oil and gas assets
Oil and gas assets are stated at cost less accumulated depletion or accumulated depreciation and, where relevant, impairment costs.

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms and pipelines, as well as on the drilling of development wells into commercially proved reserves, is capitalised within property, plant and equipment. When development is completed on a specific field, it is transferred to producing assets within property, plant and equipment. No depreciation or amortisation is charged during the development phase.

Development and production assets are accumulated generally on a field by field basis and represent the cost of developing the commercial reserves discovered and bringing them into production, together with E&E expenditures incurred in finding commercial reserves and transferred from intangible E&E assets as described above. The cost of development and production assets also includes the cost of acquisitions and purchases of such assets, directly attributable overheads, any costs directly attributable to bringing the asset into operation, and the cost of recognising provisions for future restoration and decommissioning, if any.

Major facilities may be capitalised separately if they relate to more than one field or to the licence area as a whole. Subsequent expenditure is capitalised only if it either enhances the economic benefits of the development/production asset or replaces part of the existing development/ production asset. Any costs remaining associated with the part replaced are expensed. Directly attributed overheads are capitalised where they relate to specific exploration and development activities.

(i) Depletion
Oil and gas properties in production, including wells and directly related pipeline costs, are depreciated using the unit-of-production method. Sub-soil licences and other licences capitalised as part of oil and gas properties in production are amortised also using the unit-of-production method. Unit-of-production rates are based on proved reserves of the field concerned, which are oil, gas and other mineral reserves estimated to be recovered from existing facilities using current operating methods. The unit-of-production rate for the amortisation of field development costs takes into account expenditures incurred to date.

(ii) Depreciation
Major oil and gas facilities that have a shorter useful life than the lifetime of the related fields are depreciated on a straight-line basis over the expected useful life of the facility. Depreciation of items of such assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives:

Buildings and constructions	15-30 years
Machinery and equipment	5 years

The asset's residual values and useful lives are reviewed, and adjusted as appropriate, at the end of each reporting period.

(b) Property, plant and equipment − other business and corporate assets
Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing asset to the working condition and to the location for its intended use. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other costs, such as repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

The gain or loss arising from a retirement or disposal is determined as the difference between the sales proceeds and the carrying amount of the assets, and is recognised in the income statement.

Depreciation is provided on buildings and facilities, motor vehicles, office equipment and furniture at rates calculated to write off the cost, less estimated residual value, evenly over the asset's expected useful life.

For depreciation purposes, useful lives are estimated as follows:

Other equipment and furniture	5 years
Motor vehicles	5 years

1.13 Impairment of non-current assets

(i) Impairment indicators
The Group assesses, at each reporting date, whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Group estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or CGU's fair value less costs of disposal and its value in use. The recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs of disposal, recent market transactions are taken into account. If no such transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded companies or other available fair value indicators.

The Group bases its impairment calculation on detailed budgets and forecast calculations, which are prepared separately for each of the Group's CGUs to which the individual assets are allocated. These budgets and forecast calculations generally cover a period of five years. A long-term growth rate is calculated and applied to project future cash flows after the fifth year.

Impairment losses of continuing operations are recognised in the statement of profit or loss in expense categories consistent with the function of the impaired asset, except for properties previously revalued with the revaluation taken to OCI. For such properties, the impairment is recognised in OCI up to the amount of any previous revaluation.

For assets excluding goodwill, an assessment is made at each reporting date to determine whether there is an indication that previously recognised impairment losses no longer exist or have decreased. If such indication exists, the Group estimates the asset's or CGU's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount or the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of profit or loss unless the asset is carried at a revalued amount, in which case the reversal is treated as a revaluation increase.

(ii) Calculation of recoverable amount
The recoverable amount of assets is the greater of their value in use and fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(iii) Cash generating units
For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash generating unit to which the asset belongs. The Group's cash generating units are the smallest identifiable groups of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

For the purposes of assessing impairment, exploration and evaluation assets subject to testing are grouped with existing cash generating units of production fields that are located in the same geographical region. For development and production assets the cash generating unit applied for impairment test purposes is generally the field. For shared infrastructure a number of field interests may be grouped together where surface infrastructure is used by several fields in order to process production for sale.

(iv) Reversals of impairment
An impairment loss is reversed to the extent that the factors giving rise to the impairment charge are no longer prevalent. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion, depreciation or amortisation, if no impairment loss had been recognised.

Taxes on income in the interim periods are accrued using the tax rate that would be applicable to expected total annual profit or loss.

1.14 Inventories

Unsold natural gas and hydrocarbon liquids and sulphur in storage are stated at the lower of cost of production or net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

Materials and supplies inventories include chemicals necessary for production activities and spare parts for the maintenance of production facilities. Materials and supplies inventories are recorded at cost and are carried at amounts which do not exceed the expected recoverable amount from use in the normal course of business. Cost of inventory is determined on a weighted average basis. Cost of finished goods comprises direct materials and, where applicable, direct labour plus attributable overheads based on a normal level of activity and other costs associated in bringing inventories to their present location and condition, but excludes borrowing costs.

1.15 Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Financial assets and financial liabilities are recognised when, and only when, the Group becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in the statement of comprehensive income.

(a) Financial assets
The Group classifies its financial assets into one of the following categories: financial assets at fair value through profit or loss and loans and receivables.

Regular purchases of financial assets are recognised on the trade date. Management determines the classification of its financial assets at initial recognition depending on the purpose for which the financial assets were acquired and, where allowed and appropriate, re-evaluates this designation at every reporting date. The accounting policies adopted for each category are:

Financial assets at fair value through profit or loss
Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term, or if they are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking.

Financial assets may be designated at initial recognition at fair value through profit or loss if the following criteria are met:

- The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or losses on them on a different basis; or

- The assets are part of a group of financial assets which are managed and their performance is evaluated on a fair value basis, in accordance with a documented risk management strategy and information about the group of financial assets is provided internally on that basis to the key management personnel.

Subsequent to initial recognition, the financial assets included in this category are measured at fair value, with changes in fair value recognised in the statement of comprehensive income. Fair value is determined by reference to active market transactions or using a valuation technique where no active market exists. Fair value gains or losses do not include any dividend or interest earned on these financial assets. Dividend and interest income is recognised on an accruals basis.

Other receivables
Other receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are initially measured at fair value and subsequently measured at amortised cost using the effective interest method, less any impairment losses. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction cost.

Impairment losses on other receivables are provided for when objective evidence is received that the Group will not be able to collect amounts due to it in accordance with the original terms of the receivables. The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, excluding future credit losses that have not been incurred, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The amount of the loss is recognised in the statement of comprehensive income for the period in which the impairment occurs.

Objective evidence of impairment of individual financial assets includes observable data that comes to the attention of the Group about one or more of the following loss events:

- Significant financial difficulty of the debtor;

- A breach of contract, such as default or delinquency in interest or principal payments;

- It becoming probable that the debtor will enter bankruptcy or other financial reorganisation; and

- Significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor.

Loss events in respect of a group of financial assets include observable data indicating that there is a measurable decrease in the estimated future cash flows from the group of financial assets. Such observable data includes but is not limited to adverse changes in the payment status of debtors in the group, and national or local economic conditions that correlate with defaults on the assets in the group.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed to the extent that it does not result in a carrying amount of the financial asset exceeding what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed.

The amount of the reversal is recognised in OCI in the period in which the reversal occurs.

(b) Financial liabilities and equity
Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities. The accounting policies adopted in respect of financial liabilities and equity instruments are set out below.

Other financial liabilities
Other financial liabilities include trade and other payables and are recognised initially at fair value and subsequently measured at amortised cost, using the effective interest method.

Equity instruments
Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

(c) Derecognition
Financial assets are derecognised when the rights to receive cash flows from the assets expire, or the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and the cumulative gain or loss that had been recognised directly in equity is recognised in the statement of comprehensive income.

For financial liabilities, they are removed from the balance sheet when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid is recognised in the statement of comprehensive income.

1.16 Cash and cash equivalents

Cash and short-term deposits in the statement of financial position comprise cash at banks and on hand and short-term deposits with a maturity of three months or less, which are subject to an insignificant risk of changes in value. For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and short-term deposits, as defined above, net of outstanding bank overdrafts as they are considered an integral part of the Group's cash management.

1.17 Borrowings

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of profit or loss.

1.18 Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

All provisions are reviewed at each reporting date and adjusted to reflect the current best estimate.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future uncertain events not wholly within the control of the Group are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

A provision for decommissioning is made for the cost of decommissioning assets at the time when the obligation to decommission arises. Such provision represents the estimated discounted liability for costs which are expected to be incurred in removing production facilities and site restoration at the end of the producing life of each field. A corresponding item of property, plant and equipment is also created at an amount equal to the provision. This is subsequently depreciated as part of the capital costs of the production facilities. Any change in the present value of the estimated expenditure attributable to changes in the estimates of the cash flow or the current estimate of the discount rate used are reflected as an adjustment to the provision and the property, plant and equipment. The unwinding of the discount is recognised as a finance cost.

Provisions for environmental restoration, restructuring costs and legal claims are recognised when: the group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

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. The increase in the provision due to passage of time is recognised as interest expense.

1.19 Share capital, share premium and capital reserves

Ordinary shares are classified as equity. Share capital is determined using the nominal value of shares that have been issued. Any transaction costs associated with the issuing of shares are deducted from the share premium (net of any related income tax benefit) to the extent they are incremental costs directly attributable to the equity transaction. Any discount on the issue of ordinary shares is deducted from the share premium account.

The share premium is recognised on the difference between the par value of a share and its selling price.

The capital reserve brought forward arose on the disposal of all the subsidiaries to its former holding company (Crosby Capital Limited), reverse acquisition of Crosby Capital Limited and on a group reorganization during the years ended 31 December 2010, 31 December 2004 and 31 December 2000 respectively.

1.20 Revenue recognition

Revenue, which is the fair value of consideration received or receivable, is recognised when it is probable that economic benefits will flow to the Group and when the revenue can be measured reliably. Revenue is shown net of value added tax, returns, rebates and discounts and after eliminating sales within the Group. The following criteria must also be met before revenue is recognised:

(i) Sale of goods

Revenue from the sale of oil, gas, and condensate is recognised when significant risks and rewards pass to the customer.

(ii) Interest income

Interest income is recognised on a time-proportion basis using the effective interest method.

1.21 Mineral extraction tax

In the Russian Federation MET is payable on the extraction of hydrocarbons, including natural gas, crude oil and condensate, and is levied based on quantities of natural resources extracted multiplied by the applicable MET rate for the product and field in question. MET is a production based tax (as opposed to income) and is accrued as a tax on production and recorded within cost of sales.

1.22 Current and deferred income tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in the statement of comprehensive income, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case the tax is also recognised in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Company's subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not accounted for if it arises from the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

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 tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

1.23 Employee benefits

(a) Retirement benefit schemes

No pension contributions were payable in the year. The Group participated only in defined contribution pension schemes and paid contributions to independently administered funds on a mandatory or contractual basis. The assets of these schemes are held separately from those of the Group in independently administered funds. The retirement benefit schemes are generally funded by payments from employees and by the relevant company. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense on an accruals basis.

(b) Share-based employee compensation

The Group operates equity-settled share-based compensation plans to remunerate its Directors and key management.

All services received in exchange for the grant of any share-based compensation are measured at their fair values. These are indirectly determined by reference to the fair value of the share options and warrants awarded. Their value is appraised at the grant date and excludes the impact of any non-market vesting conditions.

All share-based compensation is ultimately recognised as an expense in the statement of comprehensive income unless it qualifies for recognition as an asset, with a corresponding credit to the employee share-based compensation reserve in equity. If vesting periods or other vesting conditions apply, the expense is allocated over the vesting period, based on the best available estimate of the number of share options expected to vest. Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. Estimates are subsequently revised if there is any indication that the number of share options expected to vest differs from previous estimates. No adjustment to expense recognised in prior periods is made if fewer share options ultimately are exercised than vested.

Upon exercise of share options or warrants the proceeds received net of any directly attributable transaction costs up to the nominal value of the shares issued are allocated to share capital and the amount previously recognised in the employee share-based compensation reserve will be transferred out with any excess being recorded as share premium.

When the share options or warrants have vested and then lapsed, the amount previously recognised in the employee share-based compensation reserve is transferred to retained earnings or accumulated losses.

(c) Bonus plans

The Group recognises a liability and an expense for bonuses where contractually obliged or where there is a past practice that has created a constructive obligation.

(d) Social obligations

Wages, salaries, contributions to the Russian Federation state pension and social insurance funds, paid annual leave, sick leave and bonuses are accrued in the year in which the associated services are rendered by the employees of the Group.

e) Valuations of share options or warrants granted

Estimating fair value for share-based payment transactions requires determination of the most appropriate valuation model, which depends on the terms and conditions of the grant. This estimate also requires determination of the most appropriate inputs to the valuation model, including the expected life of the share option or appreciation right, volatility and dividend yield, and making assumptions about them. The fair value of share options or warrants granted was calculated using the Black-Scholes Pricing Model, which requires the input of highly subjective assumptions, including the volatility of the share price. Because changes in subjective input assumptions can materially affect the fair value estimate, in the opinion of the Directors of the Group the existing model will not always necessarily provide a reliable single measure of the fair value of the share options. Details of the inputs are set out in Note 19 to the financial statements.

2. Critical accounting estimates and judgements

The preparation of consolidated financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimates are revised and in any future years affected. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

2.1 Income taxes

The Group is subject to income and other taxes. Significant judgement is required in determining the provision for income tax and other taxes due to the complexity of tax legislation of the Russian Federation. The taxation system in the Russian Federation continues to evolve and is characterised by frequent changes in legislation, as well as official pronouncements and court decisions which are sometimes contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer.

Deferred tax assets are recognised to the extent that it is probable for each subsidiary to generate enough taxable profits to utilise deferred income tax recognised. Significant management judgement is required to determine the amount of deferred tax assets recognised, based upon the likely timing and the level of future taxable profits. Management prepares cash-flow forecasts to support the recoverability of deferred tax assets. Cash flow models are based on a number of assumptions relating to oil prices, operating expenses, production volumes, etc. These assumptions are consistent with those used by independent reserve engineers. Management also takes into account uncertainties related to future activities of the subsidiaries and going concern considerations. When significant uncertainties exist, deferred tax losses are not recognised even if the recoverability of these is supported by cash flow forecasts. Refer to further details in Note 22.

2.2 Provision for decommissioning and environmental restoration

This provision is significantly affected by changes in technology, laws and regulations which may affect the actual cost of decommissioning and environmental restoration to be incurred at a future date. The estimate is also impacted by the discount rates used in the provisioning calculations. The discount rates used are the Russian government bond rates.

Under the current levels of enforcement of existing legislation, management believes there are no significant liabilities in addition to amounts which are already accrued and which would have a material adverse effect on the financial position of the Group.

The Group's exploration, development and production activities involve the use of wells, related equipment and operating sites. Generally, licences and other regulatory acts require that such assets be decommissioned upon the completion of production. According to these requirements, 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 licence requirements, as well as actual dismantling and other related costs. These liabilities are measured by the Group using the present value of the estimated future costs of decommissioning of these assets. The discount rate is reviewed at each reporting date and reflects risk free rate. The Group adjusts specific cash flows for risk.

2.3 Impairment of assets

(a) Exploration and evaluation

An impairment exercise will be performed at the end of the exploration and evaluation process.

When, at the end of the exploration and evaluation stage, commercial reserves are determined to exist in respect of a particular field, the Group performs an impairment test in relation to costs capitalised. Where reserves are determined in sufficient quantity to justify development, the associated assets are transferred to property, plant and equipment.

If no potentially commercial hydrocarbons are discovered, the exploration asset is written off through the statement of profit or loss and other comprehensive income as a dry hole. If extractable hydrocarbons are found and, subject to further appraisal activity (e.g., the drilling of additional wells), it is probable that they can be commercially developed, the costs continue to be carried as an intangible asset while sufficient/continued progress is made in assessing the commerciality of the hydrocarbons. Costs directly associated with appraisal activity undertaken to determine the size, characteristics and commercial potential of a reservoir following the initial discovery of hydrocarbons, including the costs of appraisal wells where hydrocarbons were not found, are initially capitalised as an intangible asset.

(b) Development and production

When the fields enter the production phase, the recoverable amounts of cash-generating units and individual assets will be determined based on the higher of value-in-use calculations and fair values less costs to sell. These calculations will require the use of estimates and assumptions. It is reasonably possible that the oil price assumption may change which may then impact the estimated life of the field and may then require a material adjustment to the carrying value of long-term assets.

The Group monitors internal and external indicators of impairment relating to its tangible and intangible assets. There were no such indicators of possible impairment identified during the reporting years covered by these consolidated financial statements.

2.4 Evaluation of reserves and resources

Estimates of proved reserves are used in determining the depletion and amortization charge for the period and assessing whether any impairment charge or reversal of impairment is required for development and producing assets. As of 31 December 2017 and 2016 proved reserves were estimated by reference to an independent international oil and gas engineering firm report dated 22 May 2014, by reference to available geological and engineering data, and only include volumes for which access to market is assured with reasonable certainty.

When the fields enter the development and production phase, estimates of reserves are inherently imprecise, require the application of judgments and are subject to regular revision, either upward or downward, based on new information such as from the drilling of additional wells and changes in economic factors, including product prices, contract terms or development plans. Changes to the Group's estimates of proved reserves affect prospectively the amounts of the depletion and amortization charge, decommissioning assets and provisions where changes in reserve estimates cause the estimated useful lives of assets to be revised.

Depletion is provided for based on the production profile on a field by field basis, which may exceed the existing licence period. Licence extensions are generally awarded by the licence authorities in Russia as a matter of course, provided that production plans demonstrate that additional time is required to economically produce at the field and that the development and production requirements of the initial licence grant have been met.

2.5 Sub-soil licences

The Group is subject to periodic reviews of its activities by governmental authorities in Russia with respect to the requirements of its sub-soil licences, and seeks amendments to the licences when supported by the results of ongoing exploration and development activities. The requirements under the licences are subject to interpretation and enforcement policies of the relevant authorities. In management's opinion, as of 31 December 2017, there are no non-compliance issues that will have an adverse effect on the financial position or operating results of the Group.

3. Determination of fair value

Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

3.1 Other receivables

The fair value of other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes.

3.2 Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. Fair value of the non-derivative financial assets is disclosed in Note 3.3 to the financial statements.

3.3 Assets and liabilities not measured at fair value but for which fair value is disclosed

Fair values analysed by level in the fair value hierarchy of assets and liabilities of the Group not measured at fair value are as follows:

	31 December 2017		31 December 2016	
	Fair value	Carrying value	Fair value	Carrying value
Financial assets				
Trade and other receivables	152,574	152,574	172,294	172,294
Total assets	**152,574**	**152,574**	**172,294**	**172,294**
Financial liabilities				
Borrowings	1,614,108	1,562,186	1,851,695	1,859,949
Trade and other payables	93,857	93,857	129,379	129,379
Obligation under finance leasing	1,666	1,666	–	–
Other non-current payables	63,328	62,771	59,967	57,874
Total liabilities	**1,771,437**	**1,720,480**	**2,038,832**	**2,047,202**

The fair value of borrowings and other non-current payables is based on cash flows discounted using a market rate of 9.34% (2016: 11.93%). The fair values of borrowings and other non-current payables are within level 2 of the fair value hierarchy. The fair value of trade and other receivables is within level 3 hierarchy.

4. Revenue

The Group's operations comprise one class of business being oil and gas exploration, development and production and all revenues are from one geographic region, the Saratov Region in the Russian Federation. Companies incorporated outside of Russia provide support to the operations in Russia.

Revenue is primarily from the sale of three products:

	2017	2016
Gas sales	1,528,637	1,708,103
Oil sales	115,358	137,982
Condensate sales	142,445	136,968
Sulphur sales	4,084	6,377
Total sales	**1,790,524**	**1,989,430**

All gas sales are made to one customer, Gazprom Mezhregiongaz Saratov LLC, under a long-term contract effective until 31 December 2020 with terms reviewed annually. Condensate and oil are sold to local buyers. The sales of all products are denominated in RUB.

5. Cost of sales

	2017	2016
Depreciation and depletion	437,160	404,684
Mineral extraction tax	371,620	406,499
Wages and salaries	108,422	108,238
Materials and supplies	69,029	95,310
Other taxes and royalties	50,096	21,204
Repair and maintenance	37,928	39,750
Compensation benefits to operating personnel	13,739	16,812
Other	58,818	62,790
Total cost of sales	**1,146,812**	**1,155,287**

6. Operating, administrative and selling expenses

	2017	2016
Wages and salaries including director's fee	131,774	215,868
Field development costs	13,268	397
Accountancy, legal and consulting services	14,335	39,023
Rent expense	6,081	13,691
Travelling	3,259	1,996
Audit services	2,268	9,848
Depreciation	3,227	4,255
Insurance	2,094	2,888
Office expenses	1,773	3,187
Computers and software	809	2,218
Other	6,060	5,975
Total operating, administrative, selling expense	**184,948**	**299,346**

7. Salaries and other employee benefits

	2017	2016
Salaries and other employee benefits	253,935	340,918
Total	**253,935**	**340,918**

Salaries and other employee benefits are included in other cost of sales and operating, administrative and selling expenses.

Average monthly Number of Employees for the year (including executive directors):

	2017 Employees	2016 Employees
Administrative	58	83
Operating	181	184
Total	**239**	**267**

8. Other income and expenses

	2017	2016
Change in decommissioning and environmental restoration provision	13,448	34,076
Penalties received	11,367	15,000
Net income from sale of property, plant and equipment	2,017	–
Net foreign exchange difference	173	–
Other income	**27,005**	**49,076**
Loss on disposal of property, plant and equipment	(30,669)	(86,624)
Write-off of accounts receivable and other current assets, accounts receivable bad debt provision accrual	(1,908)	(26,986)
Charitable contributions	(1,255)	(3,122)
Bank charges	(181)	(1,034)
Penalties paid	–	(11,810)
Net foreign exchange difference	–	(7,982)
Loss on financial assets at fair value through profit or loss	–	(4,020)
Other	(1,288)	(1,282)
Other expenses	**(35,301)**	**(142,860)**

9. Finance income and finance costs

	2017	2016
Finance income		
Interest on bank deposits	27,960	24,409
Total finance income	**27,960**	**24,409**
Finance costs		
Interest on borrowings (Note 20)	(190,897)	(228,538)
Unwinding of the discount on decommissioning and environmental restoration provision (Note 21)	(29,884)	(35,898)
Unwinding of the discount on recognition non-current payables	(4,896)	(3,549)
Other finance costs	(64)	-
Total finance costs	**(225,741)**	**(267,985)**

10. Income tax benefit/(expense)

The tax charge for the year comprises:

	2017	2016
Deferred tax benefit/(expense)	163,052	(100,231)
Current tax expense	(85)	(105)
Total income tax benefit/(expense)	**162,967**	**(100,336)**

Reconciliation between expected and actual taxation charge is provided below.

	2017	2016
(Loss)/profit before income tax	**(1,432,945)**	**197,437**
Theoretical tax benefit/(charge) at applicable income tax rate of 20% (2016: 20%)	**286,589**	**(39,467)**
Effect of different foreign tax rates	(6,278)	(27,357)
Effect of unrecognised deferred tax assets	(108,715)	(21,422)
Tax effect of expenses not deductible for tax purposes	(8,629)	(12,090)
Total income tax benefit/(expense)	**162,967**	**(100,336)**

The Group's income was subject to tax at the following tax rates:

	2017	2016
The Russian Federation	20.0%	20.0%
The Republic of Cyprus	12.5%	12.5%
Cayman Islands	0%	0%

The Group is subject to Cayman income tax, otherwise the majority of the Group's operations are located in the Russian Federation. Thus 20% tax rate is used for theoretical tax charge calculations.

11. Exploration and evaluation assets

	Sub-soil licences	Exploration and evaluation works capitalised, including seismic works	Total
Balance at 1 January 2016	**2,101,062**	**2,589,304**	**4,690,366**
Additions	86,962	23,478	**110,440**
Transfer to property, plant and equipment	-	(1,217)	**(1,217)**
Change in the estimates of decommissioning provision	-	(11,275)	**(11,275)**
Balance at 31 December 2016	**2,188,024**	**2,600,290**	**4,788,314**
Additions	14,597	136,564	**151,161**
Transfer from property, plant and equipment	-	978	**978**
Change in the estimates of decommissioning provision	-	4,532	**4,532**
Impairment	(1,164,893)	(520,739)	**(1,685,632)**
Balance at 31 December 2017	**1,037,728**	**2,221,625**	**3,259,353**

Additions during 2017 are mostly represented by seismic works at the North Mokrousovskoye field (during 2016: exploration and production licence acquisition at the West Koltogor oil field).

In management's opinion, as at 31 December 2017 there were no non-compliance issues in respect of the licences that would have an adverse effect on the financial position or the operating results of the Group.

Impairment

In 2017 the Group revised its investment strategy with a primary focus on exploration and further development of the Deep Devonian structure on the Bortovoy Licence. As a result, the forecasted amount of investments in the development of the Koltogor Licences cannot be confirmed. Accordingly, the probability of the Koltogor Licences' development becomes uncertain. The Group recognised an impairment loss of the total book value of exploration and evaluation assets of the Koltogor Licences as of 31 December 2017.

12. Property, plant and equipment

	Oil and gas assets	Motor vehicles	Other equipment and furniture	Construction work in progress	Total
Cost at 1 January 2016	**4,542,928**	**17,245**	**7,711**	**257,826**	**4,825,710**
Additions	93,761	-	244	281,460	**375,465**
Reclassification	205,009	-	-	(205,009)	**-**
Transfer from exploration and evaluation assets	1,217	-	-	-	**1,217**
Transfer to inventory	-	-	-	(2,902)	**(2,902)**
Change in the estimates of decommissioning provision	(1,913)	-	-	(3,320)	**(5,233)**
Disposals	(15,540)	-	-	(78,131)	**(93,671)**
Cost at 31 December 2016	**4,825,462**	**17,245**	**7,955**	**249,924**	**5,100,586**
Additions	171,739	8,193	82	99,060	**279,074**
Reclassification	265,311	-	-	(265,311)	**-**
Transfer from exploration and evaluation assets	-	-	-	(978)	**(978)**
Transfer to inventory	(947)	-	-	(2,690)	**(3,637)**
Change in the estimates of decommissioning provision	5,261	-	-	-	**5,261**
Disposals	(64,782)	(7,363)	(74)	(11,423)	**(83,642)**
Cost at 31 December 2017	**5,202,044**	**18,075**	**7,963**	**68,582**	**5,296,664**
Accumulated depreciation, depletion and impairment					
Balance at 1 January 2016	**(473,797)**	**(9,475)**	**(4,168)**	**-**	**(487,440)**
Depreciation and depletion	(401,790)	(6,641)	(508)	-	**(408,939)**
Disposals	7,047	-	-	-	**7,047**
Balance at 31 December 2016	**(868,540)**	**(16,116)**	**(4,676)**	**-**	**(889,332)**
Depreciation and depletion	(434,755)	(5,137)	(495)	-	**(440,387)**
Disposals	34,518	5,765	74	-	**40,357**
Balance at 31 December 2017	**(1,268,777)**	**(15,488)**	**(5,097)**	**-**	**(1,289,362)**
Net book value at 1 January 2016	**4,069,131**	**7,770**	**3,543**	**257,826**	**4,338,270**
Net book value at 31 December 2016	**3,956,922**	**1,129**	**3,279**	**249,924**	**4,211,254**
Net book value at 31 December 2017	**3,933,267**	**2,587**	**2,866**	**68,582**	**4,007,302**

13. Inventories

	31 December 2017	31 December 2016
Natural gas and hydrocarbon liquids (at lower of cost and net realisable value)	7,119	6,047
Materials and supplies (at cost)	13,758	12,783
Total inventories	**20,877**	**18,830**

Materials and supplies mainly comprised liquid feedstock and maintenance parts.

14. Trade and other receivables and other current non-financial assets

	31 December 2017	31 December 2016
Trade receivables, gross	151,855	169,915
Other accounts receivable, gross	1,635	2,379
Allowance for doubtful accounts	(916)	–
Total trade and other receivables	**152,574**	**172,294**
Prepayments	11,173	12,783
VAT receivable	72	2,403
Other taxes prepaid	155	–
Total other current non-financial assets	**11,400**	**15,186**

As of 31 December 2017 trade and other receivables in the amount 152,574 (31 December 2016: 172,294) were neither past due, nor impaired. As of 31 December 2017 trade and other receivables in the amount of 916 (31 December 2016: 0) were past due and impaired.

Prepayments are advance payments for services to be rendered within the next twelve months.

Current VAT receivable is expected to be recovered within the next twelve months.

15. Cash and cash equivalents

Cash and cash equivalents consist of cash at bank and the majority of cash held is denominated in RUB.

The Group's exposure to credit risk related to cash and cash equivalents are disclosed in Note 27.

16. Share capital

At 31 December 2017 and 2016	Number of ordinary shares	Nominal value, USD'000	Nominal value, RUB'000
Authorised (par value of USD 0.20 each)	250,000,000	50,000	1,708,672
Issued and fully paid (par value of USD 0.20 each)	141,955,386	28,391	970,218

17. Dividends

In accordance with the relevant legislation applicable to the Group, the Group's distributable reserves are limited to the balance of retained earnings as recorded in the Company's statutory financial statements prepared in accordance with International Financial Reporting Standards. No dividends were declared or paid in 2017 and 2016.

18. Other taxes payable

	31 December 2017	31 December 2016
VAT payable	37,627	67,769
Mineral extraction tax	32,119	35,647
Property tax	10,010	4,711
Other taxes payable	9,625	10,373
Total	**89,381**	**118,500**

19. Earning per share

Basic earnings per share is calculated by dividing the profit attributable to owners of the Company by the weighted average number of ordinary shares in issue during the year.

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. During the year ended 31 December 2017 share options had an antidilutive effect on the loss per share. During the year ended 31 December 2016 share options had a dilutive effect on the earnings per share.

	2017	2016
(Loss)/profit attributable to owners of the Company – Basic and diluted	(1,269,978)	97,101
	Number of Shares	Number of Shares
Weighted average number of shares for calculating basic earnings per share	141,955,386	141,955,386
Antidilutive/dilutive potential ordinary shares – share options	202,500	1,952,500
Weighted average number of shares for calculating diluted earnings per share	142,157,886	143,907,886

	RUB	RUB
Basic (loss)/earnings per share	(8.95)	0.68
Antidiluted/diluted (loss)/earnings per share	(8.95)	0.67

20. Share-based payments

20.1 Share options

At 31 December 2017, the Company had a total of 202,500 outstanding share options (31 December 2016: 1,952,500).

Options which are lapsed or are cancelled prior to their exercise date are deleted from the register of outstanding options and are available for re-use.

	31 December 2017		31 December 2016	
Grant date	Number	Option exercise price (pence)	Number	Option exercise price (pence)
11 January 2005	–	–	–	–
23 March 2006	–	–	–	–
23 February 2007	–	–	–	–
11 January 2008	202,500	445	202,500	445
31 October 2012	–	–	1,750,000	20
	202,500		**1,952,500**	

No share options were granted during the year ended 31 December 2017.

20.2 Initial share options

The Company adopted an employee Share Option Scheme on 4 March 2005 (the "Share Option Scheme") in order to incentivise key management and staff at that time. The following share options were granted to former employees and directors of the Company under the Initial Share Option Scheme adopted on 4 March 2005 ("Initial Share Options") and are still in existence:

	2017		2016	
	Number	Weighted average exercise price (pence)	Number	Weighted average exercise price (pence)
Outstanding at 1 January	**202,500**	**445**	**202,500**	**445**
Outstanding at 31 December	**202,500**	**445**	**202,500**	**445**

Share options granted under the Initial Share Option Scheme were exercisable as follows:

- The first 30% of the options between the first and tenth anniversary of the grant date;
- The next 30% of the options between the second and tenth anniversary of the grant date; and
- The remaining options between the third and tenth anniversary of the grant date.

Equity-settled share-based payments are measured at fair value (excluding the effect of non market-based vesting conditions) as determined through use of the binomial option pricing model, at the grant date. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Company's estimate of shares that will eventually vest.

The binomial option pricing model is applied to the granting of share options in respect of calculating the fair values. Key inputs to the model are as follows:

	Share options			
	11 January 2005	23 March 2006	23 February 2007	11 January 2008
Share price at grant	20.75p	93.25p	36.25p	22.25p
Option exercise price	21.15p	95.20p	32.65p	22.25p
Expected life of option	10 years	10 years	10 years	10 years
Expected volatility	60-65%	60-65%	60-65%	60-65%
Expected dividend yield	5.0%	5.0%	5.0%	5.0%

Volatility has been based on the historical trading performance of the Company and comparable companies. The risk free rate has been determined based on 10-year government bonds.

20.3 Directors Share Options

Share options granted to certain existing Directors of the Company on 31 October 2012 ("Directors Share Options") were exercisable at any time between the commencement of the option period and third anniversary of the grant date. Share options granted under this scheme were as follows:

	2017		2016	
	Number	Weighted average exercise price (pence)	Number	Weighted average exercise price (pence)
Outstanding at 1 January	**1,750,000**	**20**	**1,750,000**	**20**
Expired	1,750,000	20	-	-
Outstanding at 31 December	**-**	**-**	**1,750,000**	**20**

During 2014 the exercisable period of the remaining options was extended from 30 October 2015 to 30 October 2017. As of 31 December 2017 all Directors Share options have expired.

The Black-Scholes formula is the option pricing model applied to the grant of share options in respect of calculating the fair values. Key inputs to the model are as follows:

Share options	31 October 2012
Share price at grant	3.45p
Option exercise price	1.00p
Expected life of option	3 years
Expected volatility	216.1%
Expected dividend yield	0.0%
Risk free rate	0.49%
Fair value per share option	3.342p
Exchange rate used (USD: GBP)	1.62525

Volatility has been based on the Company's trading performance from 1 January 2011. The risk free rate has been determined based on 5-year government bonds.

21. Borrowings

	2017	2016
Non-revolving credit facility – liability, as at 1 January	**1,859,949**	**2,218,549**
Including current liability	311,160	373,378
Interest accrued	190,897	228,538
Interest paid	(188,660)	(227,138)
Repayment	(300,000)	(360,000)
Non-revolving credit facility, as at 31 December	**1,562,186**	**1,859,949**
Including current liability	309,172	311,160

In 2014, the Group entered into non-revolving credit facility agreement with Sberbank of Russia OJSC with a maximum facility amount of 2,400,000. Contractual currency is RUB. The facility was drawn down in full in 2014. The maturity date is 30 April 2021, being the 7-year anniversary of the facility entered into. The Group is obliged to repay the principal amount of the loan in 24 tranches commencing on 11 May 2015 and on a quarterly basis from then on with a final repayment tranche payable on the maturity date. The interest rate is fixed and contracted as 10.98% per annum. In October 2017 the Group concluded additional agreement, where the interest rate was resettled as 10.73% per annum. Sberbank may unilaterally amend the interest rate in the event of increases in the refinancing rate of the Central Bank of Russia. The Group paid an upfront commission on the facility of 1% of the facility amount (24,000) and there is a drawdown charge of 0.25% per year on the balance of the facility not drawn by the Group within the established timeframe. The Group has the option to prepay the loan in whole or in part at any time, subject to the payment of a fee. The Group provided certain warranties and representations to Sberbank in the agreement. The agreement contains certain loan covenants and events of default which are customary for a facility of this type. The Group was in compliance with all covenants as of 31 December 2017 and 31 December 2016. The loan is secured by the Group, such security being granted pursuant to various pledge and mortgage deeds entered into by the Group on or about the date of the Sberbank Facility. The carrying value of property, plant and equipment pledged as of 31 December 2017 amounted to 2,775,473 (31 December 2016: 2,901,916).

The outstanding principal amount of the facility as of 31 December 2017 was 1,560,000 (31 December 2016: 1,860,000). The credit facility debt is measured at amortised cost, using the effective interest method.

Additionally the Group entered into 100,000 revolving loan facility on 13 December 2017. The interest is 10,5% for disbursed amount and 0,5% for remaining part of the limit. The maturity date is 12 December 2018. There were no drawings in 2017.

22. Decommissioning and environmental restoration provision

The decommissioning and environmental restoration provision represents the net present value of the estimated future obligations for abandonment and site restoration costs which are expected to be incurred at the end of the production lives of the gas and oil fields which is estimated to be within 20 years.

	2017	2016
Provision as at 1 January	**359,153**	**358,000**
Additions	770	15,839
Unwinding of discount	29,884	35,898
Change in estimate of decommissioning and environmental restoration provision	(3,655)	(50,584)
Provision as at 31 December	**386,152**	**359,153**

This provision has been created based on the Group's internal estimates. Assumptions based on the current economic environment have been made which the directors believe are a reasonable basis upon which to estimate the future liability. These estimates are reviewed regularly to take into account any material changes to the assumptions. However, actual decommissioning costs will ultimately depend upon future market prices for the necessary dismantlement works required, which will reflect market conditions at the relevant time. Furthermore, the timing is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil prices and future operating costs, which are inherently uncertain.

The provision reflects two liabilities: one is to dismantle the property, plant and equipment assets and the other is to restore the environment. The decommissioning part of the provision is reversed when an oil well is abandoned and corresponding capitalised costs are expensed. The environmental part of the provision is reversed when the expenses on restoration are actually incurred.

The provision is reversed when the corresponding capitalised costs directly attributable to an exploration and evaluation asset are expensed as it is determined that a commercial discovery has not been achieved and the restoration of the corresponding environment has been completed.

The Group reviews the application of inflation rates used for the provision estimation each half-year end. The inflation rate used in the estimation of the provision as of 31 December 2017 was 3.77% in 2017, decreasing to 3.64% in 2036 (as of 31 December 2016: 5.8% in 2017, decreasing to 4.0% in 2036). The discount rates used to determine the decommissioning and environmental restoration provision are based on Russian government bond rates. As of 31 December 2017 discount rate varies from 7.62% to 7.79% (as of 31 December 2016: from 8.53% to 8.57%) depending on expected period of abandonment and site restoration for each gas and oil fields.

23. Deferred tax liabilities

Movements in temporary differences during the year:

	31 December 2017	Recognised in profit or loss	31 December 2016
Decommissioning provision	45,382	1,014	44,368
Other current assets and liabilities	11,435	1,895	9,540
Tax loss carry-forwards	299,178	111	299,067
Deferred tax assets	**355,995**	**3,020**	**352,975**
Exploration and evaluation assets	(355,784)	220,659	(576,443)
Property, plant and equipment	(269,650)	(61,472)	(208,178)
Borrowings	(1,397)	845	(2,242)
Deferred tax liabilities	**(626,831)**	**160,032**	**(786,863)**
Net deferred tax liabilities	**(270,836)**	**163,052**	**(433,888)**

	31 December 2016	Recognised in profit or loss	31 December 2015
Decommissioning provision	44,368	2,023	42,345
Other current assets and liabilities	9,540	(4,599)	14,139
Tax loss carry-forwards	299,067	(18,046)	317,113
Deferred tax assets	**352,975**	**(20,622)**	**373,597**
Exploration and evaluation assets	(576,443)	(15,525)	(560,918)
Property, plant and equipment	(208,178)	(65,195)	(142,983)
Borrowings	(2,242)	1,111	(3,353)
Deferred tax liabilities	**(786,863)**	**(79,609)**	**(707,254)**
Net deferred tax liabilities	**(433,888)**	**(100,231)**	**(333,657)**

Deferred income tax assets are not fully recognised for impairment of exploration and evaluation assets and tax losses mainly carried forward for SibGeCo to the extent that the utilisation of the related tax benefit through future taxable profits is not probable. The Group has not recognised deferred income tax assets of 591,346 (2016: 482,631) The Group has tax losses that are available indefinitely for offsetting against future taxable profits of the companies in which the losses arose.

Management assessed that recognised deferred tax assets will be fully offset against future taxable profits in 2020-2026.

24. Trade and other payables

	31 December 2017	31 December 2016
Current trade payables	64,052	93,143
Payables to employees	24,310	20,512
Accrued expenses	5,495	15,724
Total current payables	**93,857**	**129,379**
Non-current other payables	62,771	57,874
Total non-current payables	**62,771**	**57,874**

25. Operating leases

Operating lease payments are mainly rentals by the Group of land, office space and equipment required for use on a temporary basis. Leases are normally signed on a short term basis of one to two years with options to extend.

Non-cancelable and cancelable operating lease payments recognised within cost of sales and operating, administrative and selling expenses in the consolidated statement of comprehensive income for the year amounted to 9,639 (2016: 32,953).

At the reporting date the Group's outstanding commitments for future minimum lease payments under non-cancellable leases fall due as follows:

	31 December 2017	31 December 2016
Within one year	3,002	2,598
In two to five years	14,496	11,405
More than five years	32,518	27,141
Total	**50,016**	**41,144**

26. Financial instruments and financial risk management

The Group has exposure to the following risks from its use of financial instruments:

- Liquidity risk;
- Market risk;
- Credit risk;

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

The Group's risk management policies deal with identifying and analysing the risks faced by the Group, setting appropriate risk limits and controls, and monitoring risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its internal policies, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

26.1 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 monitors the risk of cash shortfalls by means of current liquidity planning. The Group's approach to managing liquidity is to ensure, as far as possible, 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. This approach is used to analyse payment dates associated with financial assets, and also to forecast cash flows from operating activities. The contractual maturities of financial liabilities are presented including estimated interest payments.

The Group's current liabilities exceed current assets by 22,471 as at 31 December 2017. The Group plans to cover liquidity gap by cash inflows from operating activity in 2018. For additional liquidity risk mitigation as of 31 December 2017 the Group has unused borrowing facility in the amount of 100,000 (see Note 20).

With all the above the Group management considers the liquidity risk as low.

The table below summarises the maturity profile of the Group's financial liabilities based on contractual undiscounted payments:

	Total	Less than 1 year	1-3 years	Over 3 years
Financial liabilities as at 31 December 2017				
Borrowings	**1,871,795**	452,638	1,282,464	136,693
Trade and other payables	**175,546**	93,857	–	81,689
Obligations under finance lease	**1,666**	1,666	–	–
Total	**2,047,341**	**548,161**	**1,282,464**	**218,382**

	Total	Less than 1 year	1-3 years	Over 3 years
Financial liabilities as at 31 December 2016				
Borrowings	**2,357,003**	487,329	1,124,968	744,706
Trade and other payables	**211,068**	129,379	–	81,689
Total	**2,568,071**	**616,708**	**1,124,968**	**826,395**

26.2 Market risk

Market risk includes interest risk and foreign currency exchange rate risk.

(a) Interest risk

The Group has exposure to interest risk since the Group's subsidiary, Diall Alliance LLC, entered into a non-revolving credit facility agreement with Sberbank and, according to the terms of the agreement, Sberbank may unilaterally amend the interest rate in the event of increases in refinancing rates of the Central Bank of Russia. Sberbank had not amended the interest rate by the reporting date.

(b) Foreign currency exchange rate risk

The Group does not have any significant exposure to foreign currency risk, as no significant sales, purchases or borrowings are denominated in a currency other than the functional currency.

The Group's operations are carried in the Russian Federation, where all of its revenue, costs and financing from both Sberbank and intra-group lending are denominated in RUB. As a result there is no exposure at the operating subsidiary level to foreign currency exchange risk movements.

26.3 Credit risk

Credit risk arises principally from the Group's financial investments, trade and other receivables and cash and cash equivalents. It is the risk that the value of the Group's investments will not be recovered and the risk that the counterparty fails to discharge its obligation in respect of the Group's trade and other receivables and cash balances. The maximum exposure to credit risk equals the carrying value of these items in the financial statements.

The Group is largely dependent on one customer (Gazprom Mezhregiongaz Saratov LLC) for a significant portion of revenues. Gazprom Mezhregiongaz Saratov LLC accounted for 85.4% and 85.6% of the Group's total revenue in 2017 and 2016 respectively. The loss or the insolvency of this customer for any reason, or reduced sales of the Group's principal product, could significantly reduce the Group's ongoing revenue and/or profitability, and could materially and adversely affect the Group's financial condition. The credit rating assigned to Gazprom by Standard & Poor's is BB+. To manage credit risk and exposure to the loss of the key customer, the Group has entered into a long-term contract with Gazprom Mezhregiongaz Saratov LLC, effective till 31 December 2020. As for the smaller customers, the Group imposes minimum credit standards that the customers must meet before and during the sales transaction process.

Credit risk related to cash and cash equivalents is reduced by placing funds with banks with acceptable credit ratings.

To limit exposure to credit risk on cash and cash equivalents management's policy is to hold cash and cash equivalents in reputable financial institutions. During 2017 cash was held mainly with Sberbank, Bank Rossiysky Capital and Gazprom Bank.

	31 December 2017	31 December 2016
Ba2.ru, Moody's	163,328	291,683
ruBBB-, Expert RA	115,000	–
Ba3.ru, Moody's	105	–
Other	8,321	2,571
Total cash and cash equivalents	**286,754**	**294,254**

Capital management

The Group considers its capital and reserves attributable to equity shareholders to be the Group's capital. In managing its capital, the Group's primary long-term objective is to provide a return for its equity shareholders through capital growth. Going forward, the Group may seek additional investment funds and also maintain a gearing ratio that balances risks and returns at an acceptable level, while maintaining a sufficient funding base to enable the Group to meet its working capital needs. Details of the Group's capital are disclosed in the interim statement of changes in equity.

There have been no significant changes to management's objectives, policies or processes in the period, nor has there been any change in what the Group considers to be capital.

The Group companies are in compliance with externally imposed capital requirements as of 31 December 2017 and 31 December 2016.

27. Commitments and contingencies

27.1 Capital commitments

Capital expenditure contracted for at the end of the reporting period but not yet incurred at 31 December 2017 was 483,042, net of VAT (31 December 2016: 249,723, net of VAT).

27.2 Insurance

The insurance industry in the Russian Federation is in a developing state and many forms of insurance protection common in other parts of the world are not generally available. The Group's insurance currently includes cover for damage to or loss of assets, third-party liability coverage (including employer's liability insurance), in each case subject to excesses, exclusions and limitations. However, there can be no assurance that such insurance will be adequate to cover losses or exposure to liability, or that the Group will continue to be able to obtain insurance to cover such risks. Until the Group obtains adequate insurance coverage there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

27.3 Litigation

The Group has been involved in a number of court proceedings (both as a plaintiff and as a defendant) arising in the normal course of business. In the opinion of management there are no current legal proceedings or other claims outstanding which could have a material adverse effect on the results of operations, financial position or cash flows of the Group and which have not been accrued or disclosed in these financial statements.

As at 31 December 2016, the Group was engaged in litigation proceedings as a defendant. During 2017 the litigation was lost by the Group, provision created in the amount 3,454 as of 31 December 2016 was used in 2017. No provision for litigations was accrued as at 31 December 2017.

27.4 Taxation contingencies

Russian tax, currency and customs law allows for various interpretations and is subject to frequent changes. Management's interpretation of legislation as applied to the Company's transactions and activities may be challenged by regional or federal authorities.

The Group operates in a number of foreign jurisdictions besides Russian Federation. The Group includes companies established outside the Russian Federation that are subject to taxation at rates and in accordance with the laws of jurisdictions in which the companies of the Group are recognised as tax residents. Tax liabilities of foreign companies of the Group are determined on the basis that foreign companies of the Group are not tax residents of the Russian Federation, nor do they have a permanent representative office in the Russian Federation and are therefore not subject to income tax under Russian law, except for income tax deductions at the source.

In 2017, there was further implementation of mechanisms aimed at avoiding tax evasion using low-tax jurisdictions and aggressive tax planning structures. In particular, these changes included the definition of the concept of beneficial ownership, the tax residence of legal entities at the place of actual activities, as well as the approach to taxation of controlled foreign companies in the Russian Federation.

In addition, the concept of tax benefits for all taxes levied on the territory of the Russian Federation was legislatively established, with a focus on the presence of a business objective in the conduct of business operations, as well as confirmation of the fulfillment of obligations under the agreements concluded by the parties to the contract, or by the person to whom these obligations were transferred under a contract or law. This adjustment significantly changes the concept of recognizing the fact that taxpayers receive unreasonable tax benefits, which will have a significant impact on the prevailing judicial practice. At the same time, the practical mechanism for applying this rule has not yet been fully resolved, and judicial practice on the changes introduced is not formed.

These changes and recent trends in applying and interpreting certain provisions of Russian tax law indicate that the tax authorities may take a tougher stance in interpreting legislation and reviewing tax returns. The tax authorities may thus challenge transactions and accounting methods that they have never challenged before. As a result, significant taxes, penalties and fines may be accrued. It is not possible to determine the amounts of constructive claims or evaluate the probability of a negative outcome. Tax audits may cover a period of three calendar years immediately preceding the audited year. Under certain circumstances, the tax authorities may review earlier tax periods.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the impact on these consolidated financial statements if the authorities were successful in enforcing their interpretations could be significant.

27.5 Environmental matters

The Group's operations are in the upstream oil and gas industry in the Russian Federation and its activities may have an impact on the environment. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement stance of government authorities is continually being reconsidered. The Group periodically evaluates its obligations related thereto. The outcome of environmental liabilities under proposed or future legislation, or as a result of stricter interpretation and enforcement of existing legislation, cannot reasonably be estimated at present, but could be material.

Under the current levels of enforcement of existing legislation, management believes there are no significant liabilities in addition to amounts already accrued as a part of the decommissioning provision and which would have a material adverse effect on the financial position or results of the Group.

28. Related party transactions

During the period there were no operations with related parties, except for key management remunerations. Key management comprises Board of Directors members.

The remuneration of key management comprised salary and bonuses in the amount of 17,451 (2016: 57,175) resulting from the reduction of the Company's and Zoltav Resources LLC's Board of Directors members' remuneration.

29. Events after the reporting date

On 3 April 2018 the Group agreed preferential terms for the unsecured loan facility of up to an aggregate US$ 12 million provided by the two largest shareholders. The loan purpose is to finance exploration programme on Bortovoy. The loan was approved by the Board of Directors and an appropriate announcement was made.

30. Availability of annual report and financial statements and General Meeting

Copies of the Group's annual report and consolidated financial statements will be sent to Registered Shareholders but may not be sent to holders of Depository Interests. The annual report and financial statements will be available for inspection at the Group's registered office and may also be viewed on the Group's website at: www.zoltav.com. Notice of a General Meeting will be sent to shareholders in due course.

GLOSSARY

"barrel" or "bbls"	a stock tank barrel, a standard measure of volume for oil, condensate and natural gas liquids, which equals 42 US gallons
"bcf"	billion cubic feet
"bcm"	billion cubic metres
"boe"	barrel of oil equivalent
"toe"	tonnes of oil equivalent
"/d"	per day
"mcf"	thousand cubic feet
"mcm"	thousand cubic metres
"mmboe"	million barrels of oil equivalent
"mmcf"	million cubic feet
"mmcm"	million cubic metres
"mmT"	million tonnes
"mT"	thousand tonnes
"mToe"	thousand tonnes of oil equivalent

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