



Ruspetro plc  
Annual Report and Accounts 2012

## Delineating The Prize

$$q = \left[ \frac{kh}{C\mu B} \right] \Delta p J_D$$

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**Ruspetro** has three contiguous oil and gas development licenses totaling 1,205 km<sup>2</sup> on the Krasnoleninsky Arch hydrocarbon bearing formation in Western Siberia, a major oil producing region in Russia.

As at 31 December, 2012 we had proved reserves of 234 million barrels of oil equivalent ('boe') and proved plus probable reserves of 1.838 billion boe.

We produce and sell crude oil and gas condensate and produce petroleum gas as an associated product. The Company has its own metering station at the Transneft pipeline through which it can sell its crude oil to end-customers throughout Europe.

The area in which we are situated has a well-developed infrastructure and an established service industry for hydrocarbon production. This includes Federal highways and the national rail network. The field has access to the local electricity grid and the in-field terrain and infrastructure allow for the year-round production of oil.

The core 'know-how' for an oil and gas company is the ability to predictively model the performance of wells. The defining physics inherent in these models are based on Darcy's Law. This is the equation governing the flow of fluid through a porous medium. Ruspetro uses Darcy's Law as the foundation of our performance-oriented, quantitative approach to oil field development. For performance management, we use Darcy's Law as follows:

$$\frac{kh}{C\mu B}$$

represents the geological and petro-physical properties inherent in the rock – permeability, oil viscosity, and the thickness of the oil bearing zone. The goal of our geological team and our geological model is to pick bottom-hole locations maximizing  $\frac{kh}{C\mu B}$ .

$$\Delta p$$

represents the pressure differential between the reservoir and the well bore at the perforations. The greater this pressure differential, the greater the rate of oil flow. Our operations team seeks to maximize this differential by using electric submersible pumps to minimize hydrostatic pressure in the well bore (keeping the wells 'pumped-off'), while using water injection to maximize pressure in the reservoir. Ruspetro's hydrodynamic model is the guide for this endeavor, acting as a tool to identify injectors and maximize flood efficiency (sweep).

$$J_D$$

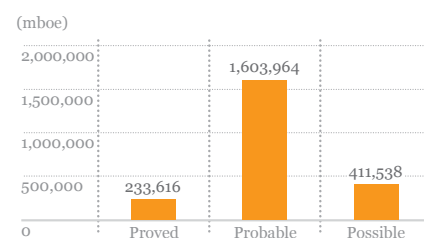
is a variable which represents completion – mathematically the radius of the well bore in relation to the oil bearing formation whether as a simple perforated well or with an increased radius due to fracturing or horizontal drilling. Every fracture or other form of stimulation results in a  $J_D$ . We manage performance in fracture engineering and execution using  $J_D$  as our yardstick.

# Highlights

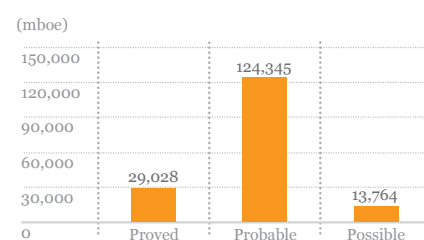
- 97% increase in revenues year on year at US\$76.23 million (net of export duty)
- Full year EBITDA of negative US\$6.2 million, EBITDA for Q4 2012 positive at US\$2.4 million
- Proved reserves up 35% to 234 million boe (31 December 2012). Including 32 million boe increase in oil and condensate reserves and 29 million boe of commercial gas reserves
- Proved and probable gas reserves of 153 million boe
- Average 2012 production up 81% over 2011 at 4,639 boepd
- Net debt of US\$335.8 million at year end, with US\$34.4 million of cash

**US\$76.23m**  
Revenue (2011: US\$38.72m)

## Total reserves (including gas)



## Commercial gas reserves



	2012	2011	Change
Revenue (US\$m)	76.23	38.72	+97%
Well head revenue per barrel (US\$/boe)	24.50	19.83	+24%
Oil and condensate production, total (boe)	1,697,950	935,003	+82%
Average production (boe)	4,639	2,560	+81%
Proved reserves (mmboe)	234	173	+35%
Probable reserves (mmboe)	1,604	1,372	+17%

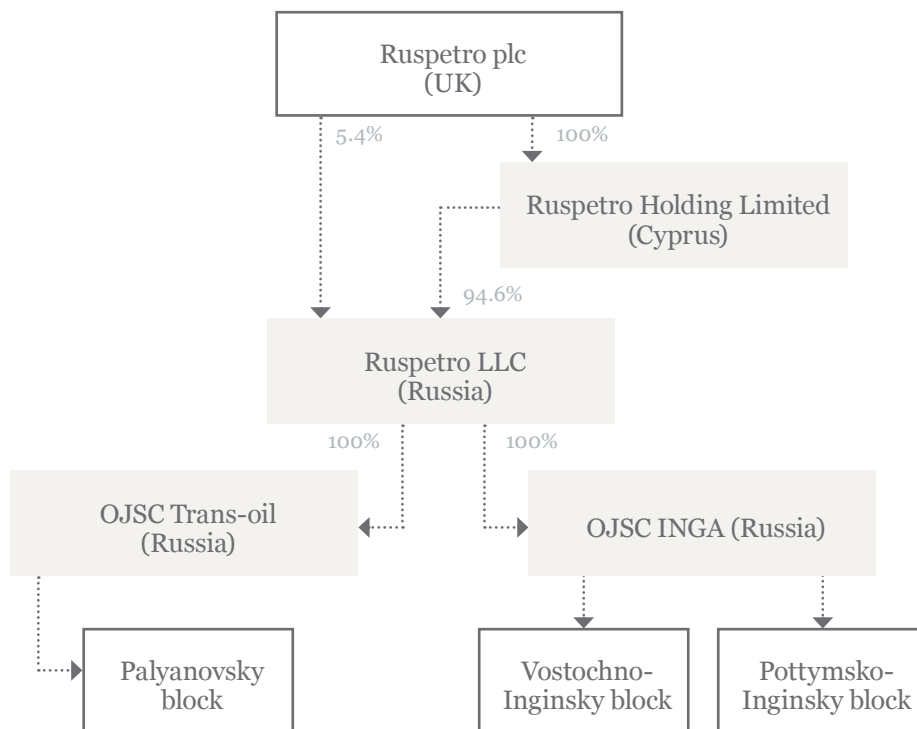
## Contents

01	Highlights
02	Our assets
04	Business model and strategy
06	Chairman's statement
09	Associated gas production
10	CEO's strategic review and update
16	Drilling advances
18	Operating and financial review
26	Crude oil and condensate taxes and duties in Russia
28	Health, Safety and the Environment ('HSE')
32	Board of directors
34	Governance
38	Principal risks and uncertainties
42	Directors' report
45	2012 Directors' remuneration report
57	Independent auditor's report
58	Financial statements
87	Parent Company financial statements Independent auditor's report
95	Shareholder information
96	Contact information



# Our assets

Ruspetro has three exploration and production licenses making up one contiguous field of 1,205 km<sup>2</sup>.



The three licenses are the Pottymsko-Inginsky ('PI') License in the west of the field, the Vostochno-Inginsky ('VI') License in the center of the field and the Palyanovsky License on the north east of the field. The License Blocks are situated in an area with well-developed infrastructure including national pipelines, highways, roads, rail freight terminals and power supply lines.

Each of the Company's three licenses is a combined exploration and production license.

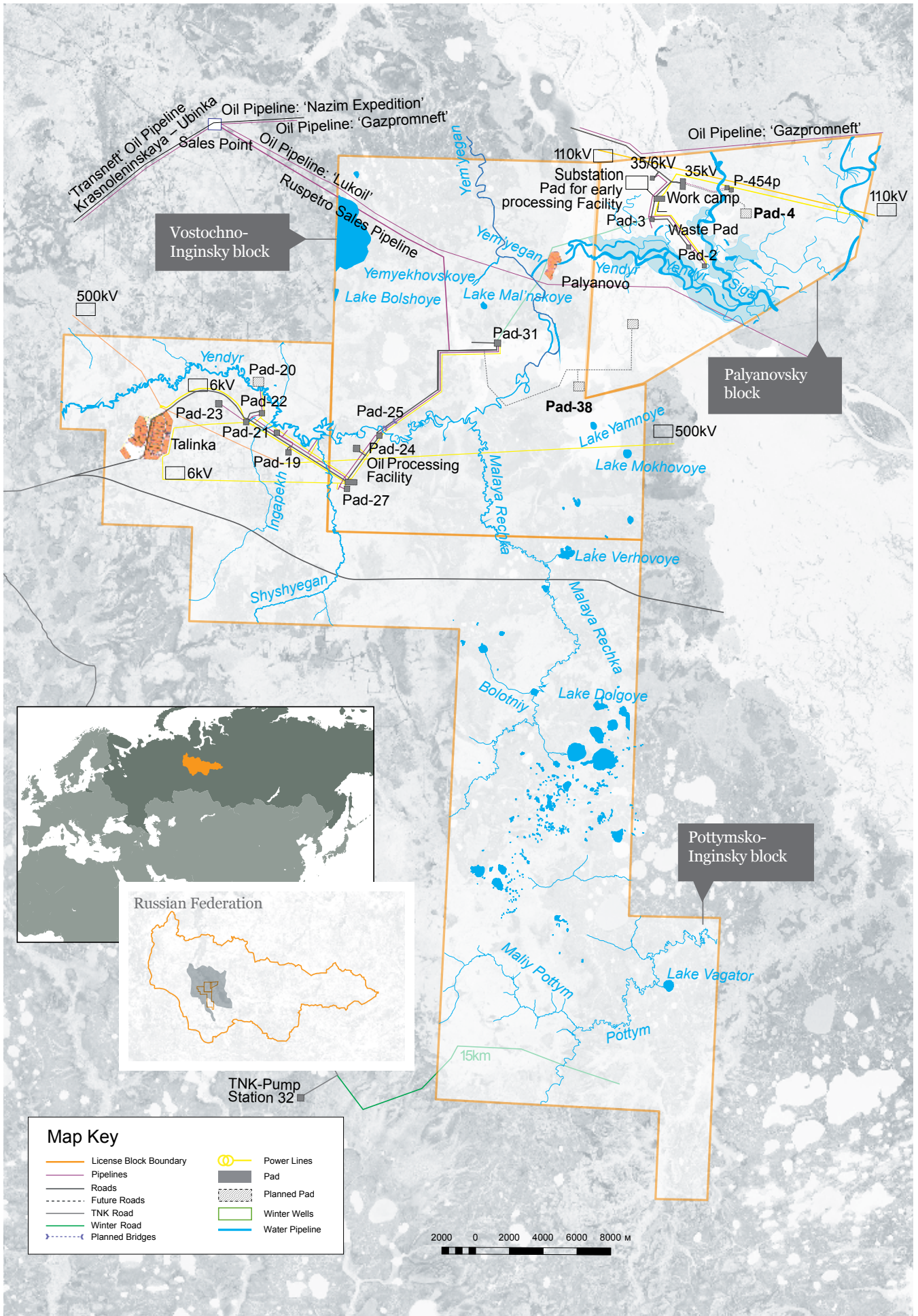
Our license for the Palyanovsky block is due to expire in December 2015 having been extended in December 2012.

The VI license expires in June 2014 and the PI License Block expires in June 2017.

We expect that the licenses will be renewed for the economic lives of the fields although they could be granted for a period less than requested.

The Subsoil Law, as currently in effect, allows for the extension of a subsoil license at the request of the license holder if such extension is necessary to finish exploration or production in the field(s) covered by the license, provided that the license holder has not violated the terms of the license and fulfilled its conditions.

As a result, to the extent that we meet our obligations under the applicable minimum work program required by the licenses and are not in breach of any license obligations or conditions, each of our licenses issued prior to this legislation can be extended, upon expiration, for the economic life of the field.



# Business model and strategy

## Our mission

To maximize production and become the lowest cost producer in the region, delivering market-leading shareholder returns. To vigilantly implement the Company's safety and ethics policies, and its commitment to being a good steward of the environment.

## Our vision

Ruspetro strives to be recognized as a market-leading production company that is successful and responsible. We are focused on achieving superior shareholder returns and delivering the lowest production and development costs in our market segment. We will continue improving the quality of the Company's reserve base through the growth of proved reserves. Management and employees are committed to the highest standards of safety, ethics and environmental performance.

## Objective

### Growth



To increase production and grow our proved reserves base

### Scale



With over 1.8 billion boe of proved and probable reserves our aim is to become a mid-sized oil and gas producer within three years

### Efficiency



To reduce the cost per barrel of oil produced by increasing productivity and efficiency

### Opportunity



Adaptability to develop the Company's assets and the business to maximize profitability

### Execution



To deliver on our production objectives and maximize value creation for shareholders



## 2012 achievements

- Average production up at 4,639 boepd in 2012 from 2,560 boepd in 2011
- Condensate production initiated, significantly increasing average well head revenue per barrel of production
- Proved reserves increased by 35% since December 2011
- Well completions accelerated

- Waterflood commenced in the west of the field enhancing well productivity

- Proved reserves up 35% to 234 million boe
- Proved and probable reserves increased by 19% from 31 December 2011 to 1.84 billion boe
- 29 mmboe of proved gas reserves added
- Processing capacity increased by 220% to 24,000 boepd

- Contiguous license blocks centrally managed
- Seismic reprocessing to improve high probability bottom hole location selection
- Nyagan office closed, field office centralised in Talinka
- Electric submersible pump run life increased by 195%

- New drilling bits reduce drilling time by 26%
- Procurement process automated
- In-field pipeline and electricity networks extended to cover all operating Pads
- Electricity generation utilizing associated gas initiated

- Focusing production towards most cash generative barrels, including condensate
- Gas monetization plan initiated
- Alternative drilling and completion techniques examined
- Advantageous fiscal opportunities evaluated

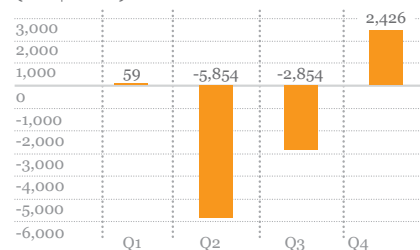
(1) Independently assessed by DeGolyer and MacNaughton

- Condensate processing facility constructed rapidly to process 5,000 boepd per day
- 27km sales pipeline installed from central processing facility to Transneft ahead of schedule and significantly below budget
- Managed multiple contractors to accelerate drilling program

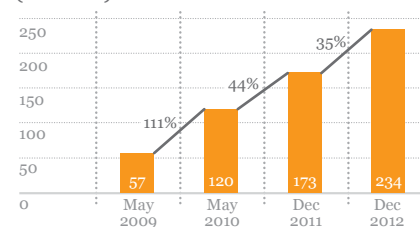
- New sales route via road and rail opened up for condensate production
- Geosciences, drilling, engineering, operations and administration teams expanded
- Surface infrastructure expenditure 18% under budget

## Key Performance Indicators

### EBITDA 2012 (US\$'000)



### Proved reserves (mmboe)

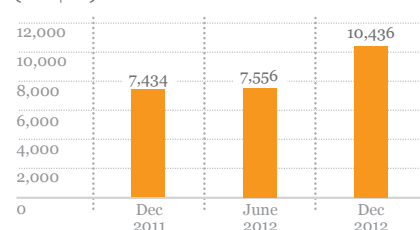


### 2012 activation cost per additional barrel of daily production (US\$)<sup>(1)</sup>

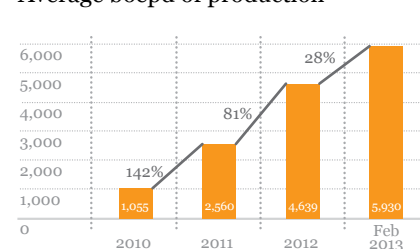
20,000

(1) Defined as capex/total additional daily production (including new production replacing decline)

### Net present value growth of the Company (at 10% discount rate)<sup>(1)</sup> (US\$m)



### Average boepd of production



# Chairman's statement

“We take considerable encouragement from the reserves upgrade, the second since our flotation.”



## Our history

1970s

First drilling into the Krasnoleninsky Arch in Western Siberia

February 1999

Open Joint Stock Company ('INGA') issued with the Pottymsko-Inginsky and Vostochno-Inginsky licenses

March 2002

Palyanovsky license issued to Open Joint Stock Company Trans-oil ('Trans-oil')

2012 was a profoundly challenging year for Ruspetro. The outturn, in terms of production, and consequently returns for our shareholders, was disappointing. But to assess the Company's performance fully, one must also look deeper into all levels of the Company's operations. Here, I have been encouraged by a number of positive developments and above all by the tenacity of my executive colleagues in getting to grips with the challenges in the business.

While in private ownership, Ruspetro had existed on the lightest footprint possible to conserve resources before the commencement of substantial cash flows. As a result, post IPO, the senior executive team has had not only to carry forward the field development program but also to build the Company. I am particularly impressed by the speed and thoroughness with which Don, Tom, Alexander and their colleagues have completed this exercise. We have recruited a strong international team with experience from a variety of operating environments around the world. At a time of human resource shortage in our industry, I am encouraged by the caliber of recruits, and take this as an endorsement of the quality and potential of our business. We now have all the necessary human, technical and engineering resource in our three centers: the London plc office, the Moscow operational center and the Siberian field offices to handle the anticipated growth in the business.



**2004 and 2005**

INGA and Trans-Oil bought by Summa Capital and sold on to Itera Oil & Gas Company

**January 2007**

Miller & Lents reserves' audit indicates 56 million barrels of proved reserves, 102 million barrels of probable reserves and 389 million barrels of possible reserves are contained by the three license blocks

**November 2007**

Ruspetro Holding Limited ('RPH') was incorporated in Cyprus

**February 2008**

Ruspetro LLC acquired from Crossmead Holding Limited by RPH

**June 2008**

Ruspetro LLC acquires INGA and Trans-Oil from Itera Oil & Gas Company for US\$305 million. Transaction financed by US\$225 million loan from Sberbank, US\$25 million loan from Limolines Transport Limited and a US\$55 million loan from Itera Oil & Gas Company

**October 2010**

US\$42 million of new equity capital raised by Ruspetro LLC

**October 2011**

Ruspetro plc incorporated in England and Wales as a public company and acquires 100% of the shares of RPH

**January 2012**

Ruspetro plc lists on the London Stock Exchange having successfully completed its IPO

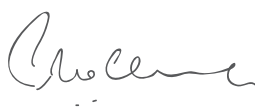
Turning to our assets, despite the challenges of production, we take considerable encouragement from the further increases to our proved and probable hydrocarbon reserves, the second since flotation announced post year end. At these levels, the scale and quality of our reserves provide a basis of full confidence for our medium and long-term production plans. However, in the short term, we have to recognize that technical issues of recovery have frustrated our ambition in 2012.

Varying permeability and lower than expected flow rates in the first half and much higher associated gas production in the second, both presented technical challenges for the management team. Here too, I have been impressed by the adaptability and energy that the senior executive team have shown. For example, the emergence of a gas and condensate play in the north east of our field, while creating a technical challenge, has markedly benefited cash flows.

The construction of pipelines, the structuring and signing of contractual supply relationships for fracturing, the completion of processing facilities, and finally the development of the condensate processing plant in the depths of the Siberian winter are all real proof of the team's resourcefulness and drive. It is on this basis that I am confident we are equal to the tasks ahead, and that stakeholders can expect the operational picture to improve.

Securing further financing is essential for the continued development of the field. In this regard, we are discussing our financial requirements with our major lender and we aim to secure this financing in the near future.

In what has been a challenging year for the business I should like to thank all our employees who have worked with great dedication to carry us through this period. My thanks should also go to my fellow Board members who have been engaged in the business, giving vital, sometimes critical, but always supportive advice. Our commitment to the best governance remains absolute and we continue with our comprehensive monitoring and vigorous pursuit of any possible improvements to the Company's Health, Safety and Environmental performance.



**Christopher Clark**  
Chairman

*"In what has been a challenging year for the business I should like to thank all our employees who have worked with great dedication to carry us through this period."*



# Associated gas production

## *A potential new revenue stream*



### Gas monetization

With significant gas reserves and production and accessible sales points available, associated gas production at Ruspetro may contribute significantly to our revenues in coming years.

Associated gas production is currently 1.6 million cubic meters per day (9,400 boepd) due, in large part, to significant gas production in the Palyanovo condensate field. This production is now being flared and as such is lost revenue for the Company.

As stated in the 31 December 2012 DeGolyer and MacNaughton reserves' audit, the Company has proved and probable gas reserves of 153 million boe.

The Company has recently signed an 'Agreement of Intent' to supply OJSC Fortum, a subsidiary of a leading Finland based electricity generator, with dry gas for eight years. This is projected to generate revenues for the Company of up to US\$700 million during this period.

The Company has already made substantial progress designing the gas processing plant and pipeline required to commercialize the gas and is seeking to arrange the required financing for this project. These elements may be completed by the middle of 2014, putting Ruspetro in a position to market and sell dry gas locally or via the Gazprom pipeline network.

The processing plant will not only enable the Company to sell dry gas to the generating plant in Nyagan but will also increase the efficiency of our condensate production, thereby increasing yields substantially. Additional products resulting from the processing of gas will include large quantities of propane and butane which can be sold commercially from the plant as liquids.

### Gas flaring

The penalties for gas flaring paid in 2012 totaled US\$850,000 under the law in force during the period. The regulations for gas flaring and emission limits, however, have been revised and as a consequence we will not suffer penalties for associated gas flaring as described below.

According to the Russian Federation Government legislation, effective 1 January 2013, companies involved in the production of associated gas are required to reduce the amount of flaring of associated gas to 5% or less of the overall amount of associated gas produced, with the exception of early stage production companies.

Ruspetro, as an early stage production company as defined under the law, can flare up to 100% of its associated petroleum gas for three years or until our proved and probable reserves are depleted by 5%. Depletion, as at 31 December 2012, is less than 1% of the proved and probable reserves of the field.

The gas utilization and commercialization plan as described above for the gas produced in this area will reduce flaring, therefore eliminating future penalties, and optimize the economic potential to the Company of the produced gas.



# CEO's strategic review and update

“The immediate challenge was to increase the pace of development of the Company.”



The Ruspetro team made some significant accomplishments during 2012. Unfortunately, we did not meet our principal objective which was to reach a 10,400 boepd production target. I am sincerely disappointed with that result. Nonetheless, we did achieve a great deal. We created a business that efficiently develops, produces and sells hydrocarbons.

Following our Initial Public Offering ('IPO') on 19 January 2012 we needed to move quickly and accomplish six key objectives, which were to:

- 1) Build a team.
- 2) Develop sales, treatment and access infrastructure urgently.
- 3) Grow production.
- 4) Improve reserve quality by increasing the proved category (1P).
- 5) Develop a strategy to develop and monetize our gas resources.
- 6) Improve the Company's financial performance towards becoming cash flow positive.

*“During the year, we increased the size of our team considerably in order to be able to gain the expertise and management capability necessary to triple our drilling program.”*

### Processing capacity

	boepd
Crude oil	15,000
Condensate	9,000

The immediate challenge was to increase the pace of development of the Company. To do this we needed to get more rigs into operation, start and complete on schedule the construction of a sales pipeline to link the Company's processing facility with the Transneft pipeline network, build a pump station and increase oil treatment capacity. At the time of the IPO, we had only one rig in operation on Pad 21, with no more room for expansion to drill further wells. For other rigs to be activated, we needed to extend existing pads and build the roads, power lines and pipelines to connect them. Within days of the IPO, we began procurement of the pipe for the 27km sales pipeline and in parallel began trenching operations. Concurrently, we started extending Pad 21 in preparation for more drilling. This level of activity, while impressive, did require a more capable team to manage the multiple parallel processes for this pace of field development.

During the year, we increased the size of our team considerably in order to be able to gain the expertise and management capability necessary to triple our drilling program, build-out the required infrastructure, increase our production and improve our understanding of the field. The new team needed to be able to deliver on our fast paced rollout. We were able to bring key people into the Company with both international and local business backgrounds. They have roles and responsibilities throughout the business, in operations, in our subsurface department and in the

finance, legal, human resources and HSE departments both in the head office in Moscow and in our UK plc office in London.

This team executed our field development program successfully by mobilizing four additional rigs in the field over the course of the year and drilling 33 wells whilst improving the surface infrastructure to provide access, electricity and pipelines to all working pads. This also included building and commissioning the 27km sales pipeline ahead of schedule and significantly under budget. The Company now has 15,000 bopd of processing capacity for our crude oil production in our west field area, and 9,000 bopd of processing capacity for condensate and 3 million cubic meters of gas processing capacity per day in the north of the field. The team continues to exceed the regional benchmarks in the construction of pipelines, power lines, roads and facilities.

While the Company made great strides in putting in significant infrastructure quickly and at a lower cost than budgeted, growing production at the tempo we had initially planned proved to be difficult. Our plan at IPO was to continue development of the structural high in the west of the field. Our mapping showed the geology progressing on-trend to the east and west from Pad 21. As we had some existing infrastructure to the east of Pad 21 and knowledge of the formations from 3D seismic, we directed our development efforts in this direction by building Pad 19,

### Key partnerships

One of the main risks to our business is execution. Part of the challenge is to manage the contractors working with us to develop our field and ensure they share our vision and values and respect how we operate. This vision includes timely and accurate execution of projects along with strict adherence to best practice HSE standards. Without contractors sharing our vision and working with us to maintain the highest standards, it is difficult to maintain consistent best practice standards across the field.

Our business relies on close cooperation with a number of contractors to whom we outsource many of our operational functions. During 2012, having been let down by two fracturing service providers, we built a strong relationship with Weatherford in the last quarter of the year. They were able to fulfill the well completion schedule that had fallen behind due to the lack of capacity of our previous fracturing service providers. Building this type of long-term, reliable, mutually beneficial relationship is key to the successful execution of our long-term objectives.

## CEO's strategic review and update continued



### 2012 key milestones

#### First quarter

- IPO raised US\$214 million
- Completed 27km sales pipeline
- Developed in-field pipeline network
- Constructed in-field power lines

#### Staff

Since our IPO, we have considerably increased the size of our team in order to be able to gain the expertise and management capability necessary to increase our production and improve our understanding of the field. Key new hires include Robert Stewart, who heads our production and operations and is based in the field. Robert has 28 years of industry experience with Conoco. Nick De'Ath, formerly of TNK-BP with over 30 years of industry experience, heads our Subsurface Team. John Krupa has joined us from Exillon as Senior Geophysicist. He also has over 30 years of industry experience. We have also made senior appointments to head drilling, workovers and fracturing.

In addition to our operations and subsurface team, we have made key appointments in the finance, legal, human resources and HSE departments.

We are focused on promoting a performance based culture. To do this, we are developing an incentive program structured to deliver optimal performance from our team.



## Second quarter

- 4 MW generating capacity installed utilising associated gas
- Activated three additional drilling rigs
- Production begins in the north east of the field
- 14 wells drilled (five completed)
- Proved reserves increase to 183 million boe
- Accelerated pace of drilling
- Initiated water flood injection on Pad 21
- Initiated condensate sales
- Building geosciences, drilling, engineering, operations and administration teams
- Installed initial treatment facility in the north east

erecting a rig and beginning to drill. After drilling several wells in different areas from Pad 19, we were met by consistently lower permeability than we had found previously. The reservoir rock had similar thickness and in some cases superior porosity to the reservoir accessible from Pad 21 but, due to the lower permeability, the wells were only yielding approximately 150 bopd of initial rate after fracture treatment. At the same time that we were experiencing poor reservoir quality from Pad 19, we were getting better results from the gas-condensate reservoir in the north of the field.

The gas-condensate field provided two positives. Firstly, the well rates and reservoir quality, while variable, were on average better than our findings from Pad 19. Secondly, the Mineral Extraction Tax ('MET') for condensate is approximately US\$20 less per barrel than for crude oil. This lower fiscal burden nearly doubled the Well Head Revenue ('WHR') of production on a per barrel basis.

The combination of the higher flow rates and the much lower rate of MET currently makes condensate far more cash generative to produce and sell than crude oil. In the second half of the year, we capitalized on this and refocused our drilling strategy towards this condensate rich area. To do this, it was necessary to mobilize rigs and build an early processing facility ('EPF') to stabilize the condensate before it could be taken to its destination refinery by truck and rail. With the increase in gas and

condensate production during the year, several upgrades to the production system were conducted including upgrading the infield pipelines, separation, water disposal and testing equipment.

At the end of 2012, it was necessary to further upgrade the EPF to manage the large volumes of gas production and to dissipate the heat carried to the surface by the gas and condensate production. A heat exchange system, new separators and larger diameter flow lines were all added to the facility to bring the temperature and pressure of the well production to a point whereby the condensate could be stabilized. However, when the heat exchange system was commissioned reservoir pressure decline and the resultant drop in condensate yield meant that condensate production did not rise as initially expected.

The increased gas supply and reserves identified by the development work in the north of the field has been instrumental in pushing forward our gas utilization and monetization strategy. This strategy is discussed in more detail on page 09.

From the Company's inception it has been our stated aim to increase the quality of our reserves. 2012 saw a 35% increase in our proved reserves, which now stand at 234 mmboe. This is a 61 mmboe increase of which 29 mmboe are the proved gas reserves added due to the development of the gas and condensate play in the north of the field.

The respectable current gas production in the north of the field associated with the condensate we are selling presents the potential for a significant gas business for Ruspetro that will enhance our profitability when brought on-line. This was not something that we envisaged to be feasible a year ago. We are currently producing about 1.6 million cubic meters per day (9,400 boepd).

We have been developing a gas monetization plan to allow us to sell our associated petroleum gas to several potential clients. The initial primary customer is a commercial electricity generating plant being constructed in the region. Other potential customers are available via the Gazprom pipeline network, which is beginning to open up in response to the Russian Government's drive towards greater utilization of associated gas by oil producers.

The planning process for a gas processing plant and pipeline is under way and we intend to start building during the winter of 2013 with revenues from the project beginning to be realized in the second half of 2014. The gas business will have relatively low operating costs and thus will become another high margin revenue stream for Ruspetro.

## CEO's strategic review and update continued

### 2012 key milestones

#### Third quarter

- Condensate reaches a third of total production
- Residential man camps established in north east and west of field
- 300 amp step-up transformer installed
- Water injection pump station commissioned

- Condensate early processing facility commissioned
- Central processing upgrade initiated
- In-field pipeline and electricity grid expanded

#### Fourth quarter

- EBITDA positive at US\$2.4 million for the quarter
- Seismic reprocessing begins
- Second rig in condensate play spuds
- Waterflood enhancements evidenced

#### Outlook

Our main priority for 2013 is to deliver on our growing cash generation. We will continue to develop the gas-condensate play in the north of the field. This will help to build our revenues and cash flows, which will give us the flexibility to grow our business significantly in the coming years.

Building production and making sure that we execute our drilling program are the main tasks ahead of us now. We will look to expand our gas business to sell substantially all of the associated gas produced to third parties from the second half of 2014.

In our crude oil area, we will continue to expand waterflood operations as we are now seeing stabilization, and in some cases increases, in reservoir pressures. This is beginning to generate production enhancement opportunities and will continue to do so in 2013. We will also look to resume drilling and increase the range of completion technologies used to optimize production from the varying geology of the field in 2013.

With these aims in mind we are currently working with our lender to arrange the required financing.

#### Conclusion

Over the course of 2012, we increased our proved reserves base as well as the pace of well completions. We have completed the surface infrastructure necessary to build production and have engaged the necessary contractors to ensure an optimal well completion tempo. We identified significant contributions from higher-value condensate which has, in turn, driven a change in direction for our short-term initiatives.

We have gained valuable insights into the characteristics of our field in 2012, marking it out as a year of delineation for Ruspetro. Although there have been some disappointments, we have the measures in place to capitalize on the vast potential of our field. The years ahead will draw on these insights to allow us to effectively exploit the intrinsic value of Ruspetro's assets.



**Don Wolcott**  
Chief executive officer

*“Our main priority for 2013 is to deliver on our growing cash generation.”*

- Early processing facility development initiated for increased production volumes

### Corporate social responsibility

As a business, we are focused on incorporating world class standards for health, safety and the environment ('HSE') into all areas of our operations. We have adopted an HSE policy that has been approved by the Board with the following initial aims:

- To strengthen the HSE team so that standards and policies can be implemented effectively across the Company.
- To develop HSE reporting and investigation processes.
- To report our environmental performance to an international standard in our 2013 annual report.





# Drilling advances

## *Bringing efficiency to the field*

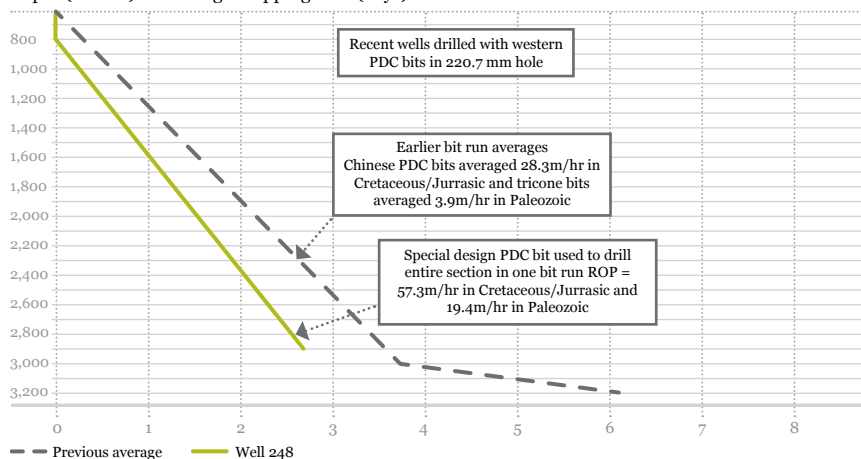


During the year we looked at ways to reduce our drilling times. One of the critical issues causing longer than necessary drilling times was the low rate of penetration by the drill bits being used and the need to change bits during the drilling of a well.

The rig contractors started the year using Chinese PDC bits in the Cretaceous and Jurassic zones, generating a rate of penetration of 28.3m/hr, and tricone bits in the Paleozoic zone averaging 3.9m/hr. Apart from the slow rate of penetration, changing the bit during drilling also delayed the process.

Working with the drilling contractors and a western drill bit manufacturer we developed a PDC bit specifically designed to drill the entire section in one bit run. The rate of penetration increased significantly to 57.3m/hr in the Cretaceous and Jurassic and 19.4m/hr in the Paleozoic without needing to be changed through the entire section.

Depth (meters) vs drilling + tripping time (days)





# Operating and financial review

Our reserves are audited twice yearly by DeGolyer and MacNaughton. The 31 December 2012 audit includes, for the first time, the characterisation of the gas and condensate producing formation in the Palyanovo License Block in the north east of the field.

## Resource potential

Proved reserves have increased by 35% since our 31 December 2011 audit to 234 million barrels of oil equivalent ('mmboe'), of which 205 mmboe are liquids.

The Company currently has proved-developed reserves of approximately 16.1 million barrels of oil and condensate, this compares to 11.6 million barrels as at 31 December 2011, a gain of 40%. We will endeavor to grow these reserves over the coming years as our drilling program expands. Proved and probable ('2P') reserves have increased by 19% to 1.84 billion boe since our 31 December 2011 audit as a result of increased Original Oil in Place identified during ongoing geological work and the discovery and characterization of our gas and gas condensate field in Palyanovo. The total increase in proved reserves was 61 mmboe.

For the first time we now have significant proved and probable gas reserves in our field. We are currently treating and selling some of our condensate, and are developing treatment and delivery systems to monetize the remainder of the gas and gas liquids.

We will continue to migrate probable reserves to proved and proved reserves to proved-developed as we expand our drilling program, deliver water flood results and refine our geological and hydrodynamic models. Increases will come from increased recovery factors driven primarily by water flood operations and changes in our OOIP and geological model as we refine and reprocess our seismic and well test data.

We are continually developing our understanding of the field, by reprocessing the 3D seismic and historical log data that we acquired with the field and by increasing our data set with each additional well drilled. We believe that there remains substantial additional opportunity

in our field in both conventional and unconventional reserves, and we will continue to develop and refine our models through processing new well data and the acquisition and interpretation of new seismic data in the future.

Our next reserves audit will be dated 30 June 2013.

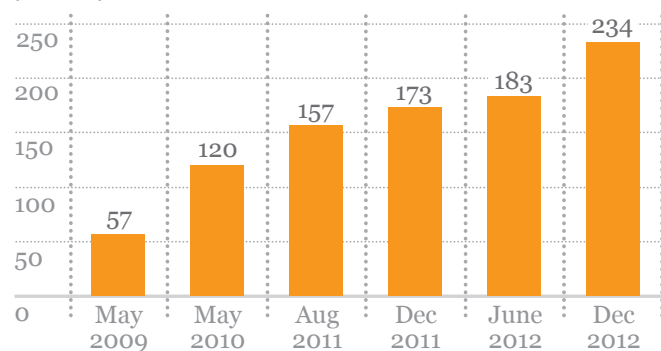
## Modeling our reservoirs

In 2012, the Company assembled a highly experienced subsurface department. Their aim is to define the architecture of our reservoir rocks, defining how much oil is present within the pore spaces of the rock and how best to maximize the production of the oil.

The department is comprised of geologists (who describe the intricacies of the depositional environment and build a 'geocellular' or 'static' computer model of the reservoir); geophysicists (who use seismic surveys to help define the subsurface architecture); petrophysicists (who define the character of the rock and the fluids they contain); and reservoir engineers (who predict and model how the fluids will move in the subsurface).

Our reservoirs are described by our geoscientists as thin, tight, Jurassic fluvial sandstones. This means they were deposited during the 150–200 million years' time-period in a river system that in-filled a rift that formed as the Siberian tectonic plate started to break apart. The tensional forces pulling the earth's crust apart (analogous to the present day Red Sea) gradually waned, however, and the rift failed.

Audited proved reserves (mmboe)



31 December 2012 commercial gas reserves

	mmboe
Proved	29
Probable	124



Erosion of the surrounding uplands caused rivers to deposit 'syn-rift' sediments into the rift. That is to say, the uplands surrounding our area were quite low so only thin river sands were deposited at different times throughout the Jurassic period, referred to as the UK2 – UK10 sequence.

The rift system was occasionally inundated by the Jurassic sea which lay to the north of our field. When the sea encroached, it deposited marine shales, mudstones and silts. The principal incursions are represented by the Radom, Togur and Bazhenov shales; the latter being the final inundation which covered most of West Siberia.

Our Palyanovsky License Block in the north east was originally a broad valley. In this area, it is the fluvial sands of UK8 – UK10 that are productive.

In the Pottymsko-Inginsky License Block, in the west of the field, a small basement high was still emergent during the later Jurassic period. The rivers, during this period, deposited their UK2 – UK3 fluvial sediments in a radial fashion around the small high. It is these horizons that are productive for Ruspetro in this area and we have been producing them from Pad 21.

Because these sands were deposited in a rift system, rivers follow the lowest areas on the downthrown side of faults. Consequently, the connectivity of our thin reservoir sands is disrupted by both stratigraphic variation (the changing direction of rivers) and structural complexity (by faulting). This causes major challenges in defining the actual area a production well will drain oil from

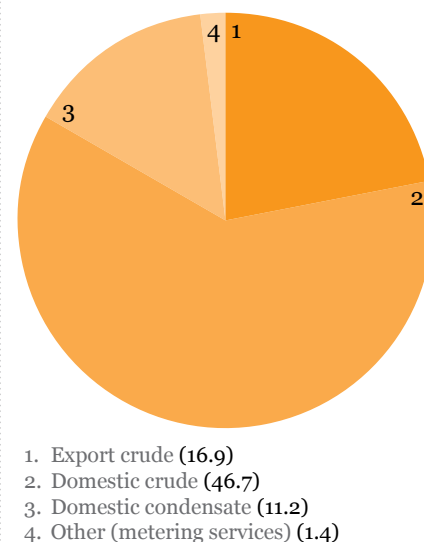
as well as understanding which wells will be affected by the pressure support from water injection wells.

We use seismic data, especially 3D data to help define the subsurface architecture of the reservoir but although we have three 3D cubes covering the northern part of our Licenses the quality needed to be enhanced in order to increase the probability of selecting bottom hole locations with the best productivity.

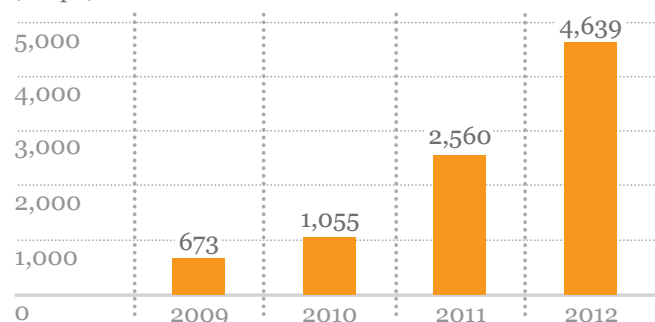
In the latter part of 2012 the subsurface department has been reprocessing the seismic that we have with the latest technology, in order to give greater clarity and enable future wells to be located with greater accuracy. As a second step the department will then be further processing the seismic to provide even greater clarity on how our reservoirs are distributed. At the same time we are acquiring more sophisticated well logs in some of our wells to define the rock physics. This data and information will be used to develop a much more accurate understanding of the reservoir rocks and fluids and thus improve well predictability.

In the north east of the field, in the Palyanovsky License Block, the hydrocarbons appear to be in a gas/condensate phase in the reservoir

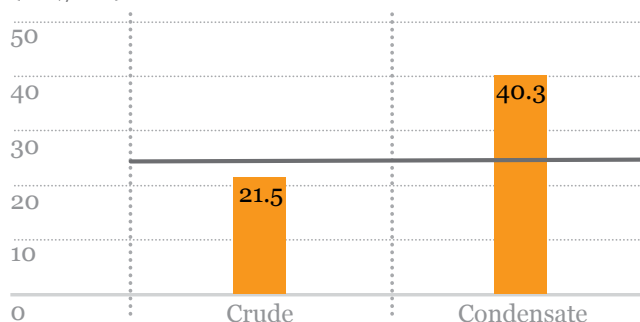
**2012 Revenue from crude and condensate sales and other (US\$m)**



**Average production (boepd)**



**2012 Well head revenue per barrel (US\$/boe)**



— 2012 average US\$24.5

## Operating and financial review continued

rather than black oil. Just as water changes its phase to ice when it is cold or steam when it is hot, so hydrocarbons change their phase depending on temperature and pressure. This not only occurs in the subsurface but also when the hydrocarbons are brought to the surface.

In 2013, the department may investigate the production potential of the 'unconventional' reservoirs which are the hydrocarbon source rocks, most notably the Bazhenov Shale. Technological advancements applied to 'unconventionals' over the past decade, particularly in the US, have revolutionized the oil and gas industry across the world. Initial activity in our area will require detailed investigation of the shale potential which would then be followed by pilot horizontal wells drilled into the shale and multi-stage fractures performed along the horizontal length of the well. This technology may also be applicable to our conventional reservoirs.

In 2013, as our well control increases and our seismic data improves, our static and dynamic models will constantly be updated to reflect more accurately the character and performance of our

reservoirs. This will be the foundation for our increasing production and the continuing growth in our audited oil and gas reserves.

### Sales and marketing

In 2012, the Company produced a total of 1,697,950 bbls of oil of which 1,650,294 was sold. An increase in production of 82% from 2011 production of 935,003 bbls.

21% was crude oil sold for export via the Transneft pipeline system (350,791 bbls). For export sales we work with Glencore plc, an international oil trading company, who sells our crude to a refinery in Hungary. Currently we have a quota to export up to 35% of our production.

We have recently delivered our first crude oil cargo by tanker to Rotterdam in the Netherlands, demonstrating our flexible approach to oil sales and commitment to maximizing our product prices. We remain opportunistic in our approach to sales and price maximization of our high quality crude and condensate. To achieve our net-back goals we have increased our evacuation routes and delivery options considerably since IPO. In addition to pipeline sales to local refineries, we are now able to sell crude oil and condensate in Russia and internationally by truck, rail, barge and tanker. Flexibility in our delivery

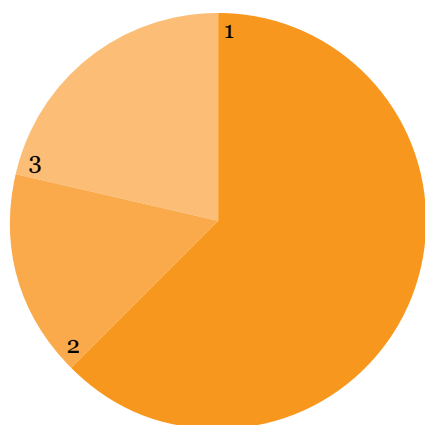
destinations and a broader customer base is the key to maximizing pricing and we will continue to opportunistically explore and develop new ways to realize our hydrocarbons in 2013.

In 2012, we completed our 27km sales pipeline connecting our treatment facility to the Transneft system and built an entirely new facility to treat gas and gas-condensate in our new gas field. We also began preliminary route design for gas and condensate pipelines and the initial engineering for a gas processing plant in our Palyanovo field. We will continue to improve on the existing treatment systems and continue developing our gas processing and pipeline infrastructure during 2013.

Condensate made up 15% of our sales volume in 2012 and 27% of our well head revenue. This product was sold directly to a domestic off-taker from the Early Processing Facility ('EPF'). The off-taker arranges road and rail transport from the EPF and gives Ruspetro a price net of these costs.

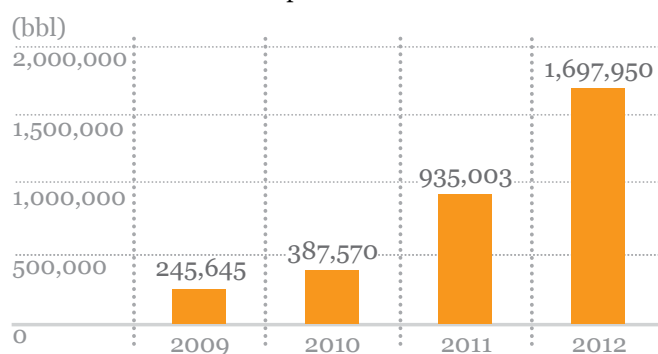
In 2012 Ruspetro also earned US\$1.4 million by providing access to the Transneft pipeline via our metering station to third party oil producers in the region.

2012 sales by market and type (bbl)



1. Domestic crude oil (1,032,045)
2. Domestic condensate (267,458)
3. Export crude (350,791)

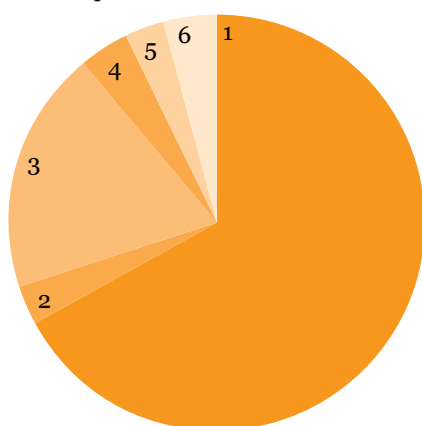
Crude oil and condensate production



### Capital expenditure 2012, actual vs. IPO budget

Facility US\$'000	Actual	IPO Budget	Variance	Variance, %
New wells	66,014	44,400	21,614	+49%
Sales pipeline	4,078	8,900	(4,822)	-54%
In-field pipelines	11,476	4,450	7,026	+158%
Power facilities	2,992	8,000	(5,008)	-63%
Electricity lines	817	1,500	(683)	-46%
Pad construction	4,881	5,000	(119)	-8%
Oil processing facilities	6,674	15,650	(8,976)	57%
Other field infrastructure	1,689	5,780	(4,091)	-71%
Other capex	7,962	–	7,962	n/a
Surface infrastructure sub-total	40,569	49,280	(8,711)	-18%
Total	106,583	93,680	12,904	+14%

2012 Percentage breakdown of capital costs of production wells



1. Drilling (67)
2. Logging/perforation (3)
3. Fracturing (19)
4. Coil-tubing (4)
5. Completion (3)
6. Wellhead and tubing (4)

### Water injection

The Company started its water injection program in June 2012 with the conversion of two wells to water injectors. Water flood increases recoveries through reservoir pressure maintenance and by mobilizing oil towards producing well bores ('Sweep'), and is an integral part of our field development plan.

We are beginning to see physical response to this activity, as modeled, which will enable us to slow or temporarily halt production declines attributed to pressure drop, and possibly create enhancement candidates in some of our well stock. We will also be submitting this empirical data to our reserves auditors and moving some parts of our field further towards water flood recovery factors.

As part of this program, we have installed a water pumping station at the central processing facility that enables the Company to recirculate separated water back to the pads for reinjection into the formations.

## Operating and financial review *continued*



### Drilling

The Company drilled 33 wells in 2012 at a cost of US\$66 million including fracturing and connections to our gathering system. During the year, we mobilized four rigs, two in the west of the field drilling into the UK2 – UK3 formation to produce crude oil and two in the north east of the field drilling into the UK8 – UK10 formations where we had identified a gas and condensate play.

Our drilling program in the west of the field revealed two issues that we are currently addressing. First, that the reservoir pressure in the Pad 21 area has been lowered by historic production in this area and hydraulic communication between bottom-hole locations. Second, while drilling to the east of Pad 21 revealed similar formation structure, thicker oil-bearing intervals and equivalent or better porosity, but upon completion the permeability of the sands and thus the flow-rate was shown to be significantly lower than that previously known on Pad 21.

To address the lower reservoir pressure we have initiated a water injection program in this area, beginning to convert producer wells to water injection wells in the middle of 2012. We have begun to see pressure response in neighboring wells as a result of the waterflooding.

In order for the Company to predictively select higher quality bottom-hole locations across the field, we will need to improve the resolution of our seismic maps and the geophysical clarity of our geological model. To achieve higher resolutions, we have completed some reprocessing and inversion analysis of the existing 2D and 3D seismic that covers 100% and 42% of the field respectively. More detail about our reprocessing program can be found in the section *Modeling our reservoirs* on page 18.



The Company had an average 39 day spud to completion time, of which 21 days were required to drill and case a well. We added drilling contractors to the field in 2012, most significantly with a Weatherford and a SSK rig. Both rigs are capable of best-in-class vertical well drilling times and quality. Both rigs are also capable of drilling horizontal sections.

### Fracturing

Ruspetro designs and implements fracture treatments as a standard completion practice on all new wells. Fractures are designed individually for the zone of interest in a given well, and we employ world-class fracturing service contractors to implement our designs. Mathematically, a fracture is simply a much larger well bore, and provides a large increase in effective permeability and thus the ability of a given well to produce. At the beginning of the year, our international oil service contractors provided fracturing services in the field with consistency. However, increasing demand in the neighboring fields during the year resulted in inconsistent fracture scheduling and delays in the completion of several wells.

We therefore initiated and established a successful relationship with Weatherford International Ltd who, in the second half of the year, became our primary fracturing service contractor in the field. The relationship was advantageous to Weatherford as it allowed them to establish themselves in the region with a depot in our field and a significant number of Ruspetro wells to be fractured. For the Company, it enabled us to bring our completion backlog up to date, allow new wells to be completed on schedule and gave us a consistent, high quality partner in the field to meet our requirements going forward.

### Infrastructure investment and delivery

2012 was a year in which we completed several key infrastructure projects at a speed and cost we believe to be highly competitive in our environment. Transportation, treatment and gathering infrastructure that we built in 2012 will provide processing and evacuation capacity to support production growth for the next several years.

Immediately after our IPO we began work on and completed the 27km sales pipeline that transports crude from our central processing facility to our wholly owned metering station on the Transneft pipeline from where we can sell our crude to Russian and European customers. We completed this project on time and under budget, and eliminated US\$2.28/bbl of trucking costs from our field to our existing Transneft connection point.

The Company completed several projects during the year to secure and strengthen its power supply within the field. We installed a 300 amp step-up transformer at the Talinka substation which provides the main power source for the western part of the field. The Company constructed the necessary in-field power lines to increase drilling and production. We also purchased 4 MW of electricity generators to enable us to utilise some of our associated petroleum gas in electricity production. A petroleum gas generator can reduce the daily cost of power of running a rig to US\$800 from US\$1,500 when compared to using power from the grid. This brings the cost of power to drill a new well down to US\$16,800 from US\$31,500.

The necessary in-field pipeline network has been completed to bring production fluid from the wells to the processing facilities and transport processed water back to the pads via the newly installed water pumping station at the central processing facility.

The in-field electricity grid, the in-field pipeline system for production fluids, processed water for reinjection and the system partially powered by associated gas brings us closer to our goal of having a closed loop production system producing, treating and transporting crude directly from our fields to end-customers world-wide.

### Condensate production

We started selling gas condensate to domestic customers in April 2012 with the completion of well 1004 in the Palyanovo License Block. Condensate refers to 51 degree API light oil being produced in the north of the field.

Condensate production has two main advantages for our business. First, condensate is a premium product in high demand throughout Russia and commands a price premium to crude oil. Second, condensate has been subject to a Mineral Extraction Tax ('MET') of RUR556 per ton in 2012, RUR591 per ton in 2013 and RUR647 per ton in 2014. RUR591 per ton is, currently, the equivalent of approximately US\$2.30 per barrel, as compared to our average MET for crude oil in 2012 of US\$22 per barrel. Consequently, the well head revenue of condensate production is approximately US\$20 per barrel greater than the well head revenue for crude oil production.

This overwhelming net revenue advantage has incentivized the Company to reorient our drilling program towards the condensate producing area of the field in the near term.

Condensate now comprises approximately 20% of our production.

## Operating and financial review continued



*Development in 2013 is primarily aimed at maximizing immediate cash generation from operations. The early processing facility for our condensate production can now stabilise up to 9,000 boepd.*

### Outlook for 2013

In 2013, drilling will be focused on the condensate producing area in the north of the field. We finished drilling on the Pad 1 area in the condensate play in early 2013, and as at the date of this report are mobilizing a rig to Pad 4 in the 'fairway' of our condensate play. We expect to spud the first well from this Pad in late March of 2013.

Development in 2013 is aimed at maximizing cash generation from operations. Condensate production will be the initial target, with crude coming back into focus later in the year as Russia develops its new tax regime for tight conventional and unconventional oil.

During 2013, our subsurface department will be engineering new well and completion designs to unlock our less permeable crude oil plays. Horizontal, multiple fractured wells will be the focus of this engineering work and initial modeling is encouraging as to flow rates and investment efficiencies. As Russia's tax regime develops to stimulate unconventional development, we will also be reviewing our unconventional shale plays in the Bazhenov and the Abalak formations. Our goal is to identify reservoir characteristics, reserves, and the appropriate completion and development approach.

### Financial summary

For 2012, as set out on pages 58 to 86 of this report, we ended the year with revenues of US\$76,230 thousand. This was an increase of 97% from 2011, and was achieved by increasing average production for the year to 4,639 boepd from 2,474 boepd. Full year production

was 1,370,960 boepd of crude oil and 326,990 boepd of condensate and we achieved an exit rate of 6,540 boepd at the end of the year. Revenues are reported net of export duty.

We also generated positive EBITDA of US\$2,426 thousand in the fourth quarter of 2012 thanks, in large part, to our focus on condensate production. EBITDA over the year was negative US\$6,223 thousand with our absolute production and sales volumes being lower than anticipated at the time of our IPO.

### Cost of sales

2012 cost of sales (including depreciation) was US\$74,816 thousand and represented 98% of revenues in 2012 as compared to 135% of revenues in 2011. The increase in the cost of sales was primarily as a result of increasing sales volumes and increasing the scale of the business in anticipation of further sales volume increases.

The higher sales related costs includes MET of US\$31,816 thousand which was 68% higher than the prior year commensurate with an increase in production volumes of 82% year on year. Other sales costs increased by 29%, reflecting both increased production volumes and expenditures in anticipation of the future development of Ruspetro's business. Operating expenses excluding depreciation and MET was approximately \$25,093 thousand compared to \$9,719 thousand in 2011.

Compared with 2011 depletion, depreciation and amortization decreased by US\$5,820 thousand, or 25%, to

US\$17,907 thousand, as a result of an increase in the proved developed reserve base, partly offset by an increase in production. Other costs of sales include sundry costs and costs of materials used in production.

### Selling and administrative expenses ('S&A')

S&A expenses (excluding share-based payments) increased to US\$28,446 thousand, or 90% from 2011. S&A expenses include oil transportation costs, payroll expenses, rent, professional services, property and land taxes, bank charges and other expenses, including costs associated with Ruspetro's status as a public company. A full breakdown of the S&A can be found on page 73. The increase in S&A, reflects the management resources and expertise required for an increased scale of operational activity and production.

### Comprehensive loss for the year

The Company recorded a loss for the year of US\$27,284 thousand. This was approximately 68% lower than the 2011 loss of US\$85,063 thousand. After translating the results to the presentation currency, which resulted in a gain of US\$6,061 thousand, the total comprehensive loss for the year was US\$21,223 thousand.

### Cash flow

Our IPO raised net cash proceeds of US\$213,699 thousand with the issue of 126,128,848 new Ordinary shares bringing the total number of Ordinary shares in issue to 333,381,480 of ten pence each.

## Outstanding debt at year end 2012

Lender	Amount (US\$m)	Outstanding interest rate	Maturity
AKB 'Sberbank'	289.1	10.9% p.a.	April 2015
Limolines Transport Limited	61.8	LIBOR +10% p.a.	May 2015
Makayla Investments Limited	19.0	LIBOR +10% p.a.	August 2013
Crossmead Holding Limited	0.3	9% p.a.	Past due
<b>Total</b>	<b>370.2</b>		

We started the year with \$1,294 thousand in cash, after receiving US\$213,699 thousand net cash from our IPO we repaid debt of US\$18,575 thousand and paid interest during the year of US\$50,645 thousand. We spent US\$66,014 thousand on drilling (49% higher than our development plan at IPO) and US\$40,569 million on infrastructure development (18% lower than budgeted in our development plan at IPO) during the year. After an operating cash outflow before working capital adjustments of US\$7,511 thousand, working capital adjustments of negative \$1,291 thousand and a currency translation difference of positive US\$3,941 thousand we ended the year with a closing cash balance of US\$34,416 thousand.

### Purchase of property, plant and equipment ('PP&E')

The Company invested US\$106,583 thousand in property, plant and equipment in 2012 representing an increase in investment over 2011 of 230%. PP&E assets were US\$226,736 thousand at the end of the period, an increase of 104%, whilst mineral rights and other intangibles increased by 6% to US\$425,551 thousand.

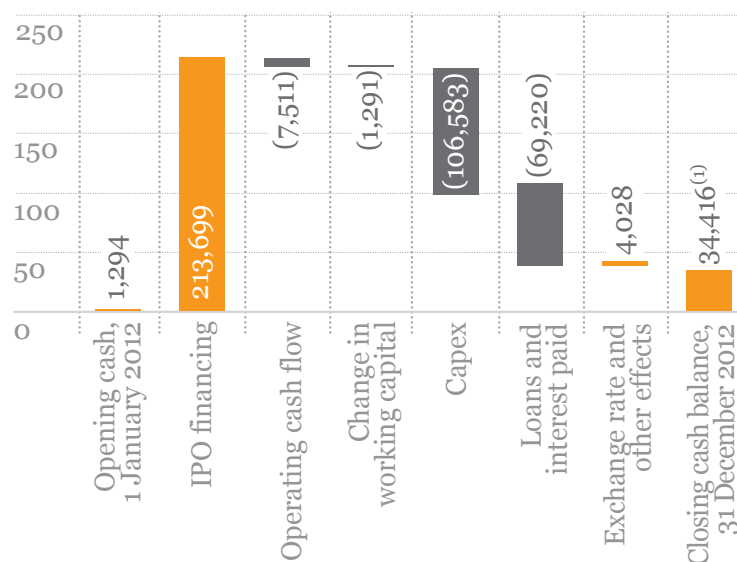
### Financing of Ruspetro's current operations and future development

On the basis of its current financial resources and its existing external and shareholder debt finance, Ruspetro's development in 2013 and beyond will require additional funding.

While the existing US\$289.1 million facility with Sberbank is due in April 2015, securing financing is essential for the continued development of the field. Therefore Ruspetro is currently evaluating a number of financing options including additional financing and term extension of its existing debt with our major lender. Such discussions are currently underway and it is hoped that this refinancing is agreed in the near future.

If additional financing is not obtained, the Group may be unable to realize its assets and discharge its liabilities in the normal course of business. Management considers that these circumstances represent a material uncertainty that may cast doubt on the Group's and Company's ability to continue as a going concern.

2012 cash flow profile  
(US\$m)



(1) Year end cash balance adjusted by US\$87 thousand due to reorganization

# Crude oil and condensate taxes and duties in Russia

## Mineral Extraction Tax ('MET')

MET is applied to all hydrocarbon production in the Russian Federation. It is a production volume based tax and is paid monthly.

## Crude oil

For crude oil, MET is calculated by multiplying the extracted quantity of dewatered, desalted and stabilized oil by the base rate per ton of crude oil produced and by the adjustment ratio that reflects changes in the RUB/US\$ exchange rate and the depletion rate of the subject field, according to the following formula:  $\text{RUB } 470 \times (P-15) \times K / 261 \times C_d \times C_r$  where:

- RUB 470 is the base rate that has been increased from RUB 446 per ton of crude oil as of 1 January, 2013;
- P is the average price for Urals crude on international oil markets (Mediterranean and Rotterdam oil markets) in US\$ per barrel during the prior month;
- K is the average Ruble per US\$ exchange rate established by the Central Bank of Russia during the prior month;
- $C_d$  is the depletion coefficient based upon the depletion of each field.  $C_d$  is calculated according to the following formula:  $3.8 - 3.5 \times N/V$  Where: N is the cumulative production of an oilfield including production losses; and V is the sum of the reserves of the Russian categories A, B, C1 and C2; and
- $C_r$  is a new coefficient applicable as of 1 January, 2012 to reflect the amount of resources for a particular subsoil area.

The formula for calculation of the crude oil extraction tax rate provides for a cut-off price of Urals blend crude oil at or below which the tax rate amounts to zero. Since 1 January, 2009, the cut-off price has been US\$15.00 per barrel.

The depletion coefficient is applicable to mature fields with more than 80% depletion. A coefficient of 1.0 applies to a field with up to 80% depletion and this is reduced on a sliding scale from 80% to 100% depletion (in increments of 0.035 for each 1% of depletion). The minimum coefficient is 0.3 for oilfields with a depletion rate above 100%. The depletion rate is based on crude oil production and reserves information reported to the Russian Government.

Assuming the average monthly US\$/RUB exchange rate is constant and the depletion factor equals 1.0, each increase in the average world market price of Urals blend oil by US\$1.00 per barrel above the cut-off price of US\$15.00 per barrel will result in an increase in the tax rate of approximately US\$1.61 per ton of oil extracted (or US\$0.22 per barrel of oil extracted using a conversion factor of 7.33 barrels per ton).

For example:

Conv. ratio	bbl/ton	7.33
Urals	US\$/bbl	112
MET base	RUR/t	470
Exchange rate	RUB/US\$	30
<b>MET</b>	<b>US\$/bbl</b>	<b>22.70</b>

## Condensate

The MET rate for condensate was also amended on 1 January, 2012. Instead of the ad valorem rate of 17.5%, the following fixed rates in Rubles per ton have been set:

- 556 Rubles per ton for 2012;
- 591 Rubles per ton for 2013; and
- 647 Rubles per ton from 1 January, 2014.

As compared with the ad valorem rate applied earlier, the new MET rates for condensate reduce the tax burden significantly for this type of product.

## Export duty

The rate of export duty is linked to the average Urals price in US\$ per barrel as follows:

Urals price <sup>(1)</sup>	Export duty <sup>(1)(2)</sup>
Below US\$109.50 per ton (US\$15.00 per barrel)	Export duty is not levied
US\$109.50 to US\$146.00 per ton (US\$15.00 to US\$20.00 per barrel)	35.0% of the difference between Urals price and US\$109.50 per ton (US\$15.00 per barrel)
US\$146.00 to US\$182.00 per ton (US\$20.00 to US\$25.00 per barrel)	US\$12.78 per ton (US\$1.75 per barrel) plus 45.0% of the difference between Urals price and US\$146.00 per ton (US\$20.00 per barrel)
Above US\$182.50 per ton (US\$25.00 per barrel)	US\$29.20 per ton (US\$4.00 per barrel) plus 60.0% of the difference between Urals price and US\$182.50 per ton (US\$25.00 per barrel)

(1) Assumes a conversion factor of 7.3 barrels per ton.

(2) The average Urals price per barrel used is the average price during the prior month.



With a RUB/US\$ exchange rate of 30 and a barrels per ton rate of 8.3 this gives a 2013 MET rate for condensate of US\$2.37 per barrel.

#### Export duty

For example:

Urals price	US\$/bbl	112
Export duty	US\$/bbl	56.20

Since December 2008, the Russian Government has been revising the crude oil export duty monthly on the basis of the immediately preceding month's average crude oil price. By introducing this measure the Russian Government intended to limit the exposure of oil exporting companies to severe declines in crude oil prices. Previously the rates of export duty were revised every two months.

The rate of export duty for condensate is not applicable to our operations as we sell our condensate to domestic customers only.



# Health, Safety and the Environment ('HSE')

Ruspetro is committed to HSE and is working to improve its performance across these areas by improving the safety and security of its operations, increasingly protecting and remediating the environment and building relationships with the local communities in which we work.

## HSE

### Introduction

Ruspetro has set its goals for HSE as:

- to take care of the Company's employees;
- to create a high quality working environment;
- to enhance the living standards of the communities within which we operate; and
- to produce responsibly from the Company's assets.

Ruspetro is committed to these goals and is working to improve its performance across these areas by improving the safety and security of its operations, increasingly protecting and remediating the environment and building relationships with the local communities in which we work.

The Company's main assets are the three license blocks it holds on the Krasnoleninsky Arch near Khanty-Mansiysk in Western Siberia. Ruspetro is committed to developing the resources within its asset base in a responsible manner, respecting all key stakeholders.

There are two communities based within our license blocks: Talinka with a population of about 4,200 and Palyanovo with a population of about 200. The Company has its operational

base in Talinka, where it manages day-to-day field operations. By basing our operations here we are bringing increased investment, activity and employment to the community whilst improving the management of our production activities.

### Safety performance

Production of oil and gas has inherent risks that Ruspetro is working to effectively manage. During 2012, there have been no official lost time accidents reported to the Russian authorities by Ruspetro. A lost time accident is an incident which results in an employee being absent from work for at least five days or shifts, as defined by the Russian Government.

The Company, however, reports incidents internally in order to build its reporting systems to international standards. These reported incidents are as follows:

**Lost Time Injury ('LTI')** – A fatality or lost time accident. The number of LTIs is the sum of fatalities and lost time accidents. A LTI will be one which results in an employee or contractor being absent from work for three days or work shifts. During 2012, Ruspetro had no LTI.

### Lost Time Injury Frequency ('LTIF')

– The number of lost time injuries (fatalities and lost work day cases) per 200,000 work hours. The LTIF for Ruspetro in 2012 was zero.

### Total Recordable Incident Frequency ('TRIF')

– A broad measure aiming to capture all incidents, defined as the total number of recordable incidents these include fatalities, injuries resulting in greater than one day or shift away from work, the restricted ability of an employee to work due to injury, an incident treated with first aid and any unplanned hydrocarbon release per 200,000 work hours. Since standard reporting started in August 2012, Ruspetro's TRIF was 14.7.

### Motor Vehicle Incident Frequency ('MVIF')

– The total number of motor vehicle crashes per 1,000,000km. Since standard reporting started in August 2012 at the Company the MVIF was 2.4.



In addition to these internationally recognized measures, the Company has developed internal safety standards to improve our approach to safety issues. These standards are based upon recognized international

standards within the industry developed to address the main risks faced by the industry. Supervisors and employees have been trained so that they can ensure the workforce is in compliance with these standards. The standards are:

Standard	Purpose
<i>Leadership</i>	To create an expectation of supervisors and employees to work safely and a duty to raise concerns
<i>Incident Investigation and Reporting</i>	To require that all incidents are reported and investigated and that any recommendations to prevent a reoccurrence are implemented
<i>Personal Protective Equipment ('PPE')</i>	To ensure PPE is worn and maintained to protect employees and contractors
<i>Safe Systems of Work</i>	To ensure employees and contractors are provided with a safe place to work and that the risks associated with their work are described to them
<i>Isolate Energy Sources</i>	The processing of oil and gas exposes employees and contractors to sources of energy such as pressure and electricity. To ensure work is performed safely these sources of energy needs to be separated from the working area and secured with controlled systems
<i>Ground Disturbances &amp; Confined Space Entry</i>	To ensure the safety from potentially dangerous atmospheres or other hidden hazards for staff working in places with restricted access
<i>Lifting Operations</i>	The transfer of large and heavy equipment on our sites needs to be managed to ensure the safety of staff
<i>Working Safety at Height</i>	To protect staff working at height and those below the work site
<i>Transportation Safety</i>	To ensure the safe use of cars and vehicles
<i>Smoking, Alcohol &amp; Drug Abuse</i>	To prohibit the use of any substances (legal or otherwise) which reduces an employee's or contractor's ability to perform their work safely

To continually improve safety standards, the Company believes that it is crucial to report all incidents and determine their causes. The Company is adopting recognized procedures and processes to provide consistency of reporting and to ensure supervisors are involved in identifying and implementing corrective actions. The Company is also working with its main contractors to ensure they report transparently to the Company.

When reported incidents are able to give a large enough statistical reference point as to where the main issues are arising, the Company will be able to prioritize efforts to improve safety performance and measure the effects of those efforts.

### Security

The Company aims to improve the security of its assets and information by establishing transparent processes and procedures for its operations, finances and procurement. Work has started on ensuring transparent processes are implemented for dealing with counter parties and the procurement of goods and services. This work will continue in 2013.

*The protection of physical assets has been upgraded through the installation of security cameras at all the Company's operational locations and with GPS tracking devices installed in both the Company's own and contractor vehicles to ensure their efficient utilization.*

There are currently six cameras in operation with another 18 planned for installation to cover production areas and primary road access points. We also plan to install office access control systems and video equipment in all offices by the end of the first half of 2013.





### Environmental performance

The Company's duty of care to the environment is of key importance. During 2012, the Company has adopted an environmental protection program via its main production subsidiaries OJSC INGA and OJSC Trans-oil. The production of oil causes four possible routes of contamination:

- atmospheric emissions – principally through the flaring or venting of associated gas;
- water emissions – mainly from produced water;
- solid wastes – mainly drilling cuttings; and
- oil spillages and leaks.

The program aims to:

- reduce waste at source through design and operation;
- recover or recycle the emissions of production (e.g. the re-injection of produced water);
- protect the natural water bodies and soil from contamination or damage from operations;
- optimize the use of existing land for pipeline and transportation routes and operational sites whilst also minimizing land use in sensitive natural, community or historical areas;
- monitor the impact of operations on the environment; and
- clean up any waste materials or oil spills using recognized reclamation procedures to allow the environment to recover.

In order to address its atmospheric emissions during 2012, the Company installed approximately 4 MW of electricity generation powered by associated gas. This is intended to supply in-field power demands.

Over the course of the year, the Company paid approximately US\$850,000 in penalties for the flaring of associated gas in compliance with the Russian state legislation. In November 2012, the Federal Government adopted a decree significantly increasing penalties for associated petroleum gas flaring when overall cumulative production to date exceeds 5% of the reserves of the reservoir. This decree came into effect from 1 January 2013 with the aim of improving the utilization of associated gas by the oil industry. The Company's low level of current reservoir depletion,



at approximately 1%, currently means that, within the framework of the new decree, the Company has no flaring penalties to pay until the end of 2015. The Company is, however, currently putting in place a strategy to utilize 100% of its associated gas production from 2015.

*Due to the decree, increased monitoring will be required and plans are already in place to install additional gas meters in early 2013 to provide the required data.*

During 2012, the Company carried out remediation works to contaminated land, including:

- the reclamation of 0.3 hectares of land from oil contamination;
- the processing of 9,800 cubic meters of drilling cuttings;
- the reclamation of 2,760 square meters of sludge pits; and
- the reclamation of 6,300 cubic meters of sludge pits from legacy drilling works inherited by the Company.

Further remediation work is planned in 2013, when the weather improves after winter. This work includes further work on legacy drilling.

For the reporting year 2013, the Company will be required, under UK Government regulations, to comply with the guidelines for the reporting of Greenhouse Gas Emissions. In preparation for this we are working with TruCost, a leading consultancy collecting and analyzing environmentally impactful company data. With TruCost, we will be collecting and reporting the relevant emission data from our operations.

### **Community relations**

In order to help support the communities in which we operate the Company has agreements with the local authorities in Talinka and the local regional authority of the Otyabrskiy region. These agreements have been renewed for 2013. During 2012, the Company invested approximately US\$250,000 into the local community to provide support for the local school in Talinka and create a road infrastructure for the village of Palyanovo. These works will be continued in 2013.

Additionally, Ruspetro will continue to support the local community, encouraging qualified staff to move to the area, by investing in a number of projects. These include supporting the school in Talinka by:

- funding a school trip to the IVth International Festival of Musicians and Artists 'Visiting the Fairy-Tale';
- equipping a cartoon animation lab; and
- purchasing sports equipment and costumes for the Center of Recreation and Culture.

And improving local medical facilities by purchasing:

- medical supplies for the dental center; and
- medical equipment for the clinic, including a defibrillator.

### **People**

The Company has employed many highly qualified staff during 2012, attracted to work for the Company due to its:

- production base and management team;
- the dynamic, fast paced working environment; and
- the international and progressive team environment.

During 2012, the Company has put in place processes to employ and retain staff and enable them to grow and develop within the organization.

These processes include:

- workforce planning – to ensure the future staffing needs of the Company are met;
- performance management – to identify individual contributions to the Company's success;
- career ladders – to encourage individual growth and development;
- long-term rewards – to incentivize and retain key staff;
- intra company communications – to transmit clear and consistent information on Company performance;
- technical and management training – to ensure employees and managers have the skills required to perform their roles effectively; and
- coaching and mentoring – to develop staff through experience at work and encourage staff to give their best effort.

Ruspetro has recruited over 80 additional staff in 2012 across our locations. These hires included staff in the London office for plc related tasks, strengthening the operational staff in Talinka and building out the corporate functions in Moscow. During the year 58 employees left Ruspetro resulting in an overall turnover rate of 27%. Approximately 5% of staff turnover occurred with the relocation of the operational base from Nyagan to Talinka and the closure of the Nyagan office. Nyagan is approximately 2 hours drive from the production sites whilst Talinka is located beside the production facilities. Relocating the functions to Talinka has improved performance within the operational groups.

Critically, highly experienced internationally experienced professionals have been recruited in the areas of reservoir engineering, geology, operations and drilling.

During 2012, Ruspetro developed a quarterly performance review system for all staff. This will be further refined in 2013 to clearly identify highly performing employees and to improve the transparent link between Company performance, individual contribution and reward.

To attract and retain staff, the Company's remuneration policy has been developed and is presented in this report. Ruspetro has also introduced a competitive set of benefits including life and medical insurance for all employees and a long-term incentive plan. A reward policy for all staff has been developed.

# Board of directors

The Board of directors has nine members, including four independent non-executive directors.



**Chris Clark**  
**Chairman**

Mr Clark, aged 71, was appointed chief executive of Johnson Matthey in 1998. He took the company into the FTSE 100 in 2002 and retired two years later. He was subsequently chairman of Associated British Ports Holdings plc. He was chairman of URENCO Limited from 2006 to 2011. He became chairman of OAO Severstal, in 2006.

Mr Clark attended Trinity College, Cambridge and Brunel University, London and is a qualified metallurgist.



**Don Wolcott**  
**Chief executive officer**

Mr Wolcott, aged 51, worked for Yukos Oil from 1999 to 2005 as senior vice president for production and reservoir performance. At Yukos, he was responsible for all aspects of its production and reservoir performance business. From 1996 to 1998 Mr Wolcott worked at Schlumberger Oil Field Services and prior to that at ARCO Alaska Inc. from 1989 to 1994.

Mr Wolcott has a PhD in petroleum engineering from the Colorado School of Mines.



**Tom Reed**  
**Chief financial officer**

Mr Reed, aged 42, was a private equity and M&A advisor and investor based in Moscow prior to joining Ruspetro. Mr Reed has worked in Russia on the origination, trading, and research of equity and equity derivatives, distressed debt, and debt derivatives since 1995. Mr Reed was an advisor to VR Capital and Raven Russia, and a founding shareholder of Rising Star Media. He has advised and invested in several private companies in Russia.

Mr Reed graduated from the University of South California with a BA in Humanities, emphasis in philosophy, minor in finance.



### **Alexander Chistyakov**

#### **Executive director and president**

Mr Chistyakov, aged 40, prior to joining Ruspetro was first deputy chairman of the Russian Federal Grid Company's (UES) management from 2002, having joined in 1999. In 1998 he was the head of the economic analysis department and deputy director of the financial department at Russia's Federal Agency on Industry (Rosprom). Prior to that, he was deputy director of investment management at Menatep Bank, and deputy general director of Alliance Menatep.

Mr Chistyakov has a master's degree in marketing and finance and a PhD in economics from the Leningrad-na-Voznesenske Finance and Economics Institute.



### **Rolf Stomberg**

#### **Non-executive senior independent director**

Mr Stomberg, aged 72, is the chairman of the supervisory board of LANXESS AG, and he is the senior independent director of OAO Severstal. He spent 30 years with BP plc, where he last held the position of CEO of BP's downstream business and managing director on the main board. After this he was a non-executive director on the boards of numerous international companies.

Mr Stomberg has a doctorate of economics from Hamburg University.



### **James Gerson**

#### **Non-executive director**

Mr Gerson, aged 40, is general director of JSC Lonburg and serves as a director of JSC Sestroetsk Tool Works and JSC New Era. From 2000 to 2003 he was head of investor relations at JSC Lenenergo, and from 1997 to 1999 he worked at Rothschild.

Mr Gerson has a BA in Russian and east European history from London University.



### **Robert Jenkins**

#### **Independent non-executive director**

Mr Jenkins, aged 59, is a chartered accountant (KPMG) and has 20 years' Russia-related investment experience, including in private equity with Framlington Group, as finance director of UK AIM mining exploration company, Eurasia Mining, and as CFO of oil exploration and production company Urals Energy. Mr Jenkins is a partner in Russia focused Northstar Corporate Finance and also a non-executive director of Toledo Mining Corporation, UK AIM listed and engaged in nickel exploration and production in the Philippines.

Mr Jenkins has an MA in modern history and modern languages (Russian) from Oxford University.



### **Joe Mach**

#### **Independent non-executive director**

Mr Mach, aged 64, is the principal of Houston Consultants, an investment company based in Texas. Mr Mach served as vice president responsible for exploration and production at Yukos E&P from 1999 until 2006. Prior to Yukos, Mr Mach worked for Schlumberger from 1976 until 1999. He has been a Society of Petroleum Engineers member since 1970.

Mr Mach has a BSc degree in petroleum engineering from the University of Tulsa and served as chairman of the universities petroleum engineering advisory board.



### **James McBurney**

#### **Independent non-executive director**

Mr McBurney, aged 54, is CEO of White Tiger Gold Limited. Before this he was CEO of HCF International Advisors and JNR (UK) Limited, and he headed the European Natural Resources investment banking at Bank of America in London, was a managing director with Merrill Lynch's Energy & Power Group in New York, and was an executive director in M&A with Goldman Sachs in New York and London. Prior to his banking career he served for five years as an infantry officer in the US Marine Corps.

Mr McBurney received an MBA from Harvard Business School and a BA, cum laude, from Yale College.

# Governance

## Introduction

Ruspetro seeks to maintain a high standard of corporate governance and places great emphasis on ensuring these standards are maintained throughout the business. The Board provides specific guidance on corporate governance as a central part of its role of providing leadership and direction to the Company.

## Governance of the Company

The Company is committed to the principles of corporate governance and since the Company was listed on the London Stock Exchange on 19 January 2012, the Company has embraced and fully supported the principles contained in the UK Corporate Governance Code 2010 and 2012 (the 'Code') by which the Board is accountable to shareholders.

## The Board of directors of Ruspetro plc (the 'Board') Membership of the Board

The Board comprises nine directors made up of the chairman, chief executive officer, chief financial officer, president and executive director, senior independent non-executive directors and four other non-executive directors. Biographical details of each of the members of the Board are set out in the preceding section of the annual report and details of the executive directors' service contracts and the non-executive directors' letters of appointment are set out in the Directors' Remuneration Report.

## The role of the Board

The Board's role is to provide entrepreneurial leadership of the Company's business within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board sets out its vision for the Company's strategic aims, ensures that the necessary financial and human resources are in place for the Company to meet its objectives and to review management performance. The Board sets out the Company's values and standards and ensures that its obligations to its shareholders and others are understood and met.

## Board balance and independence

The composition of the Board comprises an appropriate balance of expertise, experience, independence and depth of knowledge of the Company to enable the Board to discharge its respective duties and responsibilities effectively. The Board includes a combination of executive and non-executive directors, including independent non-executives, to provide a balance of perspectives and to ensure that no individual director or group of directors can dominate the decisions of the Board. The Board has three committees; the audit committee, nomination committee and remuneration committee, the composition of which is reviewed from time to time to ensure that undue reliance is not placed on any one chairman or member. During the year the chairman met the other non-executive directors without the attendance of the executive directors on a number of occasions.

## Independent and non-executive directors

The non-executive directors contribute independent and objective judgment on issues of strategy and Company performance, including compliance to corporate standards throughout the organisation. Mr. Stomberg is the Company's senior independent non-executive director. The Company considers all non-executive directors to be independent non-executive directors within the meaning of 'independent' as defined in the Code, except Mr James Gerson who represents Limolines Transport Limited. The Company confirms that all non-executive directors have sufficient time available to fulfil their obligations to the Company.

## Election and re-election of directors

Directors will stand for re-election at the 2013 annual general meeting as required by the Companies Act 2006 and as recommended by the Code. For election of a non-executive director, the Board will set out for shareholders the merits of the individual's appointment and the chairman will confirm the effectiveness and commitment of the individual.

## New appointments to the Board

The appointment of new Board members will be conducted and appointments made based on individual qualities that will fulfill the requirements of the Company in meeting its objectives, and to maintain a healthy balance in the composition and balance of the Board.

## Information and support

The chairman, through the company secretary, ensures that the members of the Board and its committees receive accurate, timely and clear information. The Board receives induction and training on corporate governance and the Code, and assistance with professional development as appropriate to Board members' needs and roles. All directors have access to the advice and services of the company secretary and, have the opportunity to take independent professional advice, at the Company's expense, in support of the proper discharge and execution of their duties.

## Chairman and CEO

A clear division of the roles and responsibilities in the leadership of the Company is demonstrated by the separate appointments of the chairman and chief executive officer. The chairman is responsible to the shareholders for the overall performance of the Board and the Company; the chief executive officer is responsible to the Board for the effective delivery of the Company's strategic objectives and for its operational performance.

## Performance evaluation

Board performance evaluation is conducted annually. The executive directors' performance is evaluated by the non-executive directors; the chairman's evaluation is led by the senior independent director with the other non-executive directors. The non-executive directors, excluding the chairman, are evaluated by the chairman and chief executive officer, taking into account the views of the executive directors. The Board committees are reviewed by the senior independent non-executive director and the chief executive officer, taking into account the views of the other executive directors in addition to self performance assessments by those committees. The Board reviews its own performance as a whole by consolidating and discussing the foregoing reviews and in 2012 by the conduct of a self-assessment review.

## Board meetings

The Board held seven meetings during the year ended 31 December 2012. The directors' attendance at those meetings is detailed in the following table:

Directors	Board (7 meetings)
Chris Clark	7
Don Wolcott	7
Tom Reed	7
Alexander Chistyakov	5
Rolf Stomberg	7
Robert Jenkins	7
James McBurney	7
Joe Mach	7
James Gerson	7



The key items reviewed and actions taken by the Board during the year include the following:

**Leadership and strategy** – The review and approval of operational reports, budgets, a senior secured notes offering and the conversion to equity in the Company of the outstanding shareholder loan and accrued interest of Limolines Transport Limited.

**Performance, risk and internal control** – Review of financial statements, annual report, approval of Interim Management Statement, review of the effectiveness of the Company's risk management and of the internal control systems and procedures including financial, operational and compliance controls.

**Governance** – The Board evaluated all elements of the Company's business including related party transactions with consideration of the UK Bribery Act and the UK Corporate Governance Code.

**Shareholder communications** – Approving preliminary announcement of annual results, annual report, half yearly report, quarterly announcements, and the release of any other Company announcements to the London Stock Exchange's Regulatory News Service.

### Remuneration and awards

The Board sets the level of directors' remuneration by reference to company peer group data and by retaining independent remuneration consultants. This process establishes levels of compensation that are commensurate with their position in the Company and enables the Company to attract and retain outstanding candidates. The remuneration of each director is set out in their respective service agreements and appointment letters. The payment or award of remuneration which is subject to performance criteria in the computation of bonuses and awards, is assessed and recommended to the Board by the remuneration committee. Details of directors' remuneration and interests are set out in the remuneration report.

### Committees of the Board

#### Audit committee

The members of the audit committee are Mr Jenkins, chairman, and two independent non-executive directors, Mr Stomberg and Mr McBurney. Mr Jenkins, previously finance director and chief financial officer of Russian mining and energy companies and as an investment banker active in Russian energy transactions, possesses the recent and relevant financial experience to head the audit committee. The audit committee meets at least quarterly, with the Company's chief financial officer and the Company's auditor, PricewaterhouseCoopers LLP, in attendance as required by the business of the meetings.

The terms of reference of the audit committee have been approved by the Board. The audit committee chairman reviews the financial reporting of all of the Company's subsidiaries and the committee reviews the Company's accounting, internal control and risk assurance policies. In addition, it monitors the implementation, development, compliance and effectiveness of such internal policies and procedures in order to assess their impact on the integrity of the Company's financial statements. It also reviews public announcements relating to financial performance and results.

The audit committee reports to the Board and will raise any matters to the Board which it considers require the Board's attention. The committee will make recommendations as appropriate including those for the Board to put to shareholders at the annual general meeting.

The audit committee maintains an objective relationship with the Company's auditor PricewaterhouseCoopers LLP and meets with them on a periodic basis. The Company may also, from time to time, ask them to perform non-audit engagements. In such circumstances, the continued objectivity and independence of the auditor is an objective of the Company. This is met by delegating to the audit committee the responsibility for the review and recommendation to the Board of the materiality and nature of the non-audit engagement and its possible impact on the audit engagement.

The audit committee, having reviewed the independence and effectiveness of the auditors and being satisfied that the auditors remain independent and effective in their role, has not considered it necessary to carry out a tender process this year, and has therefore recommended to the Board that the existing auditors PricewaterhouseCoopers LLP be reappointed. PricewaterhouseCoopers LLP have expressed their willingness to continue as auditors.

The audit committee also considered the Financial Reporting Council's proposals on auditor rotation and agreed that the implications for the Company should be reviewed in 2013.

The following main items of business were considered by the audit committee during the year:

**Financial and business reporting** – The review and approval of financial statements, the annual report and accounts, the half yearly report, IMS statements and related announcements issued to the London Stock Exchange Regulatory News Service.

**Risk and internal control** – The assessment and review of risks, and the mitigating actions/contingency plans for those risks; review of internal controls including new financial controls to cover the implementation and on-line availability of the Purchase Order ('PO') and the Authorisation For Expenditure ('AFE') systems and the review of procedures for the adoption of new counter-parties to the Approved Contractors List ('ACL'); review plans for the development of an Enterprise Resource Planning System ('ERP'), which enables the integration of financial, operational and technical data into one database; review of internal monthly financial reporting of actual results versus the budget and review of capital and operational expenditure budgets; review of related party transactions policy and procedures as well as the implementation of a company whistle-blowing policy and the introduction of a global independent 'whistle-blower' hotline accessible in many languages; review of material litigation as well as of Health, Safety and the Environment ('HSE') reports.

**Compliance** – The review of the Company's compliance with the terms and conditions of its operating licenses as well as of the Palyanovo license extension application; consideration of an internal audit function with the decision, given the size and maturity of the Company, to develop such function at a later stage.

**Audit** – The review of the audit findings report, the audit plan and the management representation letter.

**External auditor** – The review and approval of the engagement letter and the fee proposal of PricewaterhouseCoopers LLP.

## Governance *continued*

### Remuneration committee

The members of the remuneration committee are Mr Stomberg, as chairman, Mr Clark, Mr Mach and Mr McBurney. The members are considered by the Board to be independent. The remuneration committee met twice in 2012 to assist the Board in determining the remuneration and contracts of the directors and senior management of the Company. The terms of reference of the remuneration committee are approved by the Board.

The remuneration committee has engaged the services of specialist remuneration consultants to provide guidance. No director is involved in setting his own remuneration.

The remuneration report, which includes details of the award of share options in Ruspetro plc together with information relating to directors' service contracts and appointment letters, is set out on pages 45 to 56.

During the year the remuneration committee considered the following main items of business:

**Remuneration** – The review of a report from remuneration consultants on the remuneration of executive directors and senior management with a decision not to change executive directors' remuneration in 2013 and to consider senior management on an individual basis.

**Bonuses** – The approval of 2012 Key Performance Indicators for the executive directors' bonus scheme and consideration of whether bonuses are to be paid to executive directors.

**Long Term Incentive Plan** – The approval of the introduction of a Long Term Incentive Plan ('LTIP') and the review and approval of the 2013 LTIP rules and metrics.

**Share options** – The approval of share option awards to employees (not executive directors).

**Reporting and governance** – The approval of the remuneration report disclosures. The review of proxy voting by shareholders. The approval of remuneration and reward policies.

### Nomination committee

The members of the nomination committee are Mr Clark, as chairman, Mr Mach and Mr McBurney. External advisors are also invited to attend meetings as and when appropriate. The nomination committee meets at least annually and more frequently as may be required for the proposed appointment of new members to the Board. The activities for which the nomination committee is responsible are set out in the terms of reference.

During the year the nomination committee considered the following main items of business:

**Succession planning** – Succession planning proposals were discussed.

**Composition of the Board** – The size, composition and skill set of the Board were reviewed with a decision not to recommend any changes to the Board at this time. The impact of the Davies Report 'Women on Boards' was discussed with a decision not to recommend an additional Board appointment at this time. Although the nomination committee concurs with the conclusions of the report that diversity, in its broadest sense, improves Board performance it welcomed the decision not to impose quotas regarding gender balance.

**Board and committee effectiveness** – A review of Board and committee effectiveness by means of an internal evaluation was carried out. The matters arising from that review were addressed.

**Governance** – The provisions of the revised UK Corporate Governance Code 2012, its impact and compliance requirements for the business were reviewed and considered.

The nominations committee supports the importance of having diversity of thought and representation on the Board. As the committee considers future Board composition and succession planning, it will seek applicants from a wide range of backgrounds to ensure that the candidate best equipped to bring the right combination of skills and experience to benefit the Company are identified. However in terms of gender the Company operates in an environment with low representation of women at all levels of the industry. In order to address this, the Company operates equal opportunity policies in all areas of its activities. The aim, over time, is that women as a percentage of the workforce will increase and create a pool of talent from which to recruit its senior positions.

The Board, separately from the nominations committee, periodically reviews the individual attributes and experience of its members and from time to time identify the need for additional, replacement and successor appointments, and the refreshing of Board committees. The nomination committee will convene to review and recommend appointments proposed by the Board.

### Committee meetings

The various committees met regularly and the members' attendance at those meetings is detailed in the table below:

Director	Audit (5 meetings)	Remuneration (2 meetings)	Nomination (1 meeting)
Chris Clark	–	2	1
Don Wolcott	–	–	–
Tom Reed	–	–	–
Alexander Chistyakov	–	–	–
Rolf Stomberg	5	2	–
Robert Jenkins	5	–	–
James McBurney	5	2	1
Joe Mach	–	2	1
James Gerson	–	–	–

### Internal controls and risk management

#### Board responsibility

The Board is responsible for determining the nature and extent of the significant risks it is prepared to accept in achieving the Company's strategic objectives.

#### Compliance

Ruspetro has complied with the Code in the 2012 financial year and has continued to develop policies and procedures that will ensure compliance with the Code and the related Financial Services Authority Listing Rules.

#### Control environment

Responsibility levels are communicated throughout the business through documented Board policy and implemented through a matrix of control procedures including the segregation of duties.

#### Internal control

The Board implements and maintains risk management and internal control systems to support the Company's activities and ensure they comply with the minimum requirements of

the Code. Specifically the Company is establishing a continuous process for identifying, evaluating and managing the significant risks of the business, and to regularly review the effectiveness of the Company and its subsidiaries' risk management and internal control systems.

### **Business risk**

The Company has an ongoing process, in accordance with best practice, that identifies, evaluates and manages risks faced by the Company. This is based on each operational and corporate function producing a risk matrix which identifies the key business risks, the probability of those risks occurring, their impact if they do occur and the actions being taken to manage those risks to the desired level. From these the Company has compiled a risk register, containing the key risks facing the Company during conduct of its business. The register is regularly reviewed and discussed by the audit committee.

In the light of the provisions of the UK Bribery Act 2010, the non-compliance of which could expose the Company to unlimited fines and other consequences it is the Company's intention in 2013 to introduce additional measures into the business to reinforce its zero tolerance approach to bribery and corruption, including the provision of an on-line anti-bribery and corruption training programme for all new and existing employees.

Risk acceptance and reduction objectives are defined with particular attention given to safety and environmental factors, and applied to ensure that the risks are at a level that is as low as reasonably practicable. The directors are working closely with operational and functional management to ensure compliance with the Company's policies, procedures and risk management processes. These are designed to manage rather than eliminate the risk of failure in order to achieve business objectives.

### **Management structure**

The Board has overall responsibility for the Company and its subsidiaries. There is a formal schedule of matters specifically reserved for decision by the Board. The executive directors, led by the chief executive officer, are responsible and accountable for all aspects of the Group's business affairs.

### **Financial reporting**

The Company maintains an effective and reliable accounting system and has developed a broader management information system during the year. The Board receives a monthly report that monitors actual performance against budget and forecasts for oil and gas production, gross revenue and well head revenue, capital expenditure and development progress. It also provides the Board with information on key issues including treasury, cash flow forecasting and the financial implications of sensitivities to changes in commodity prices and exchange rates. The Company also maintains an effective and reliable suite of policies, procedures and controls in preparing consolidated financial statements. These controls include rigorous review of the process and output data and technical support and review to ensure accounting tools and business systems are robust.

### **Budgetary process**

There is a comprehensive budgeting system with an annual budget approved by the Board covering capital expenditure, public offering proceeds, cash flow, the income statement and the balance sheet. Monthly results are reported against budget, and revised forecasts are prepared regularly. Separate approval processes and authority limits are in place for budgeted and unbudgeted expenditure items.

### **Corporate accounting and procedures**

Responsibility levels are communicated throughout the Company and its subsidiaries using a table of delegated authorities appropriate to each part of the business, through written corporate accounting procedures and policies common to all companies along with company specific procedures and controls, which are continually reviewed and updated as required. The review of the application of internal financial control and operational procedures is carried out during visits to the field operations offices by the directors and senior Moscow office management.

### **Investment appraisal**

Capital investment is regulated by the budgetary process and authorisation levels. For expenditure beyond specified levels, detailed written proposals have to be submitted to the Board. Capital expenditures are reviewed with major overruns in terms of cost and time being investigated.

### **Quality and integrity of personnel**

The integrity and competence of personnel is ensured through high recruitment standards and subsequent training courses. High quality personnel are seen as an essential part of the control environment. The ethical standards expected of employees are communicated through corporate presentations of policies including, identification and prevention of fraud, anti-money laundering and bribery including the UK Bribery Act, whistle-blower, ethical practices, and a share dealing code.

The Company is committed to operating in an environment that provides personnel with a safe and accessible means to report concerns without concern of reprisal and a whistle-blowing hotline service for all staff and contractors, has been introduced which will report directly to the chairman of the audit committee.

### **Internal audit**

The audit committee has conducted an annual review into whether it is appropriate for the Company to establish an internal audit function. The Board places great emphasis on the importance of risk management and control at all operating levels in the business and is developing an appropriate framework.

The Board has concluded that the Company's procedures, policies and systems are appropriate and suitable to enable the Board to safeguard shareholders' investment and the Company's assets.

### **Communication with shareholders**

Information about the activities of the Company and its subsidiaries are provided in the annual report and accounts and the half-yearly report which are sent to shareholders. The Company has made quarterly IMS and periodic operational updates via the London Stock Exchange's Regulatory News Service. A regular dialogue has been developed with institutional shareholders, for which the Board as a whole has responsibility. Enquiries from individuals on matters relating to their shareholding and the business of the Company are welcomed and are dealt with in an informative and timely manner.

### **Annual general meeting**

Shareholders are encouraged to attend and participate in general meetings to discuss the progress of the Company. The Annual General Meeting of Ruspetro plc will be held at 11.00am at White & Case, 5 Old Broad Street, London EC2N 1DW on Wednesday 17 April 2013.

## Governance

## Principal risks and uncertainties

Ruspetro's current stage of development, the geographical area in which we operate and the business of oil and gas development and production all mean that the business is exposed to a wide variety of risks.

Our approach is to actively understand and monitor the risks we are exposed to, and then manage solutions to them so that their potential adverse effects are minimized.

The following table describes risks that we face and outlines our approach to mitigating them:

## INTERNAL AND OPERATIONAL RISKS

Risk	Description
<b>Reservoir Performance</b>	Ruspetro's hydrocarbon reservoirs may not perform as expected, exposing Ruspetro to reduced cash flow and challenges in funding planned development. This under performance may be due to unforeseen geological factors, formation damage during drilling or completion or overestimation of forecast production. Accordingly, forecast reservoir performance is critical in deciding on development options for specific assets, as well as allocation of Ruspetro's financial resources generally.
<b>Recruitment and retention of key people and critical skills</b>	Ruspetro's ability to maintain a competitive position and implement its business strategy and meet its oil production targets depends to a large degree on recruiting and retaining the services of its senior operational management team, and contractors with the requisite critical skills.
<b>License status and oil and gas field permitting</b>	Renewal of Ruspetro's exploration and production licenses (expiring in 2014, 2015 and 2017) is of critical importance as, in this context, is the satisfactory fulfilment of license conditions.
<b>Procurement and contract management, capital and operating expenditure</b>	<p>Lack of effectiveness in negotiating and managing purchases and contracts could increase costs for Ruspetro and/or cause delays to project completions and operations, negatively impacting production, cash flow and value generation.</p> <p>The vetting of counterparties, in particular for business ethics and integrity as well as financial and operating capability, represents an associated risk area.</p>
<b>Health, Safety, Environment and Community Relations ('HSEC')</b>	Failure to put in place and operate a rigorous HSEC regime can endanger and negatively effect stakeholders. Adverse publicity from any poor performance in these areas could negatively effect Ruspetro. It could be held responsible for failing to address any contamination or damage to license and surrounding areas, with significant associated costs.
<b>Protection of Company Property</b>	Damage, theft or interference to Ruspetro's physical or intellectual assets can stop or limit production resulting in reduced cash flow, increased costs and negative reputation reducing stakeholder confidence in Ruspetro.



Inherent probability	Potential impact	Our approach
Medium/High	High	Ruspetro's senior management is focused on and has proven expertise in modelling, managing and maximizing oil reservoir performance and recovery, including through the application of proven sophisticated fracturing, water injection and other oil production enhancement techniques.
Medium/High	High	The Group has recruited additional qualified staff in most functional and technical areas to achieve its oil field development plan objectives. The additional experience recruited has reduced this risk but some positions remain critical to implementing the business strategy. Innovative reward systems to attract world class contractors are also being introduced.
Medium	High	Non-compliance with certain license conditions has been remedied. Applicable license conditions are being fulfilled, and these are largely internally controllable. While license renewal is not expected to be problematic, it will be essential to demonstrate an effective gas utilization program.
Low	High	<p>Ruspetro operates effective policies, procedures and controls in relation to prior approval of supplier counterparties and competitive procurement within strict levels of delegated authority with the objective of achieving arms-length, transparent purchasing.</p> <p>Ruspetro, its Board and audit committee monitor carefully and undertake close, regular scrutiny of the effectiveness of the Company's policies.</p>
Low	High	<p>Ruspetro treats HSEC as a priority, and its Board has formally adopted appropriate policies across the HSEC area. In order to manage effectively its rapid oil field development plan, Ruspetro will appoint a Russia-based, senior HSEC manager reporting directly to the CEO, along with local managers responsible for ensuring the implementation and monitoring of Ruspetro's policies across the HSEC area.</p> <p>Ruspetro has budgeted for appropriate expenditures to comply with applicable laws and regulations, as well as to contribute to the economic and social benefit and development of the region in which it operates.</p> <p>Ruspetro has put in place appropriate insurance arrangements to manage and mitigate its potential financial exposure risks in the HSEC area.</p>
Medium	Medium	Development and implementation of a security strategy protecting physical and intellectual assets which aims to improve training, processes and procedures for security personnel and improve technological components of physical security, and secure assets through robust fraud-risk management.

## Governance

### Principal risks and uncertainties *continued*

#### EXTERNAL AND FINANCIAL RISKS

Risk	Description
<b>Political Environment</b>	<p>The political environment in the Russian Federation is volatile. There have been and there is the risk of actions by its executive and judicial authorities that may adversely affect the performance of businesses operating in the country.</p> <p>Political instability in Russia or an increase in the perceived risk of investing in Russia could be materially detrimental to Ruspetro's business.</p>
<b>Exchange Rate and Inflation</b>	<p>Ruspetro's oil revenues are linked to international market prices, and, as a result, it is not protected against the negative effect of continuing cost inflation in Russia (e.g. currently at over 5% per annum) or demand led industry specific inflation.</p> <p>Exchange rate movement in particular in that of RUB: USD could impact negatively Ruspetro's financial position. This reflects, in particular, the current profile of its costs, revenues and sources of capital.</p>
<b>Access to Finance</b>	<p>Implementation of Ruspetro's development plan may require it to raise additional finance of either a debt or equity nature and market conditions may preclude this, including on terms which Ruspetro considers satisfactory. In addition, Ruspetro's existing level of borrowings may constrain it from raising additional debt finance. This may result in it not being able to implement its development plan and realize the inherent value of the oil and gas in its existing license areas.</p> <p>Ruspetro has a significant level of bank and shareholder debt, with the risk that it may not be able to meet its debt service obligations, either out of cash flow or refinancing.</p>
<b>Oil and Gas Market Prices</b>	<p>Although Russia's taxation regime for its oil producers does give some protection against declines in market prices, significantly lower market prices than those assumed in Ruspetro's development plan would nevertheless result in materially reduced net revenue contribution.</p> <p>Ruspetro is exposed to both Russian domestic market and international oil and gas price movements. It does not currently enter into any forward sales price hedging agreements.</p>
<b>Bribery and Corruption</b>	<p>Bribery and corruption is known to be an area of vulnerability for businesses operating in Russia, and as such, Ruspetro may be exposed to such risks. In addition, the UK Bribery Act requires that companies introduce adequate procedures to combat bribery at all levels and areas of their business.</p>

Inherent probability	Potential impact	Our approach
Medium	High	<p>This risk cannot be influenced by the management of the Company. However, the Group monitors changes in the political environment and reviews changes to the relevant legislation, policies and practices. The continuing need for oil production as a vital source of state revenue and the recent proposed changes in legislation for Mineral Extraction Tax indicates that the environment for oil producers remains favorable.</p>
Low	Medium	<p>Ruspetro's policy and practice is to match, as far as practicable, receipts and payments in the same currency, in particular in relation to Russian rouble transactions.</p> <p>Ruspetro's risk monitoring will include the review of its actual projected financial position in relation to its US dollar-denominated debt.</p> <p>In order to mitigate such inherent external risks, Ruspetro's business model and strategy target a superior net Well Head Revenue contribution, including through the production and sale of oil condensate, and competitively low operating and other costs to achieve a resulting high level of profitability so as to reduce its potential exposure to the impact of either exchange rate movements or cost inflation.</p>
High	High	<p>Ruspetro considers that its strategic concentration on the development of its existing licenses in growing both its production and proved reserves may maximize its ability to attract both debt and equity finance.</p> <p>Ruspetro's Board will keep under review its debt service obligations in the light of financial performance.</p>
Medium	Medium	<p>In order to manage such risks, Ruspetro has structured its development plan to be financially feasible at significantly lower oil prices than those of today.</p> <p>Ruspetro's sales arrangements effectively mitigate any revenue collection risks. Ruspetro sells its oil production in the domestic market to a limited number of local off-takers at transparent arms-length market prices, with payment in full on delivery. It exports entirely through Glencore International plc, the world's largest international commodity trading company, with sales contracted quarterly at stipulated volumes and arms-length current market prices, 60% pre-payment and the balance of 40% paid the following month.</p>
Medium	High	<p>Ruspetro prohibits bribery and corruption in any form by all employees and by those working for and/or connected with the business.</p> <p>The Company pays special attention to this in its systems, in particular for the approval of counterparties and expenditure.</p> <p>Employees are expected to report bribery or attempted bribery to their line managers even if it is only suspected or attempted in line with the Company whistle-blower policy which has been implemented across the business together with the introduction of an independent whistle-blower hot line to enable any concerns of wrongdoing to be voiced without fear of reprisal.</p> <p>Ruspetro has developed a code of conduct and a supporting statement of ethics which is compliant with the Bribery Act 2010 and its guidance and is in the process of implementing this. The communication of the new code is to be implemented in the forthcoming year by a training program for management, employees and contractors globally.</p>

# Governance

## Directors' report

The directors have the pleasure in presenting their annual report and audited accounts for the period ending 31 December 2012. These will be presented to shareholders at the Annual General Meeting of the Company, which is scheduled to be held at 11.00am on Wednesday 17 April 2013 at the Offices of White & Case, 5 Old Broad Street, London EC2N 1DW.

### Principal business activities

The Company's principal activity is the development and production of oil and gas on three contiguous license blocks of 1,205km<sup>2</sup> situated in the Krasnoleninsky Arch near Khanty-Mansiysk, western Siberia, Russia. Ruspetro is the 100% license holder of the Pottymsko-Inginsky, Vostochno-Inginsky and Palyanovsky license blocks, which make up 100% of the Company's oil and gas producing assets.

Ruspetro's licenses expire in June 2014 (Vostochno-Inginsky block) and June 2017 (Pottymsko-Inginsky block). In December 2012 the license for the Palyanovsky block was extended until December 2015, with an expectation that it and the other licenses will be further extended for the economic life of the fields, which run until between 2029 and 2040. This is in accordance with recent legislation allowing the license holder to extend the licenses for the economic life of the fields as long as Ruspetro meets its minimum obligations and is not in breach of any license conditions.

### Corporate information

This annual report contains the consolidated financial statements of Ruspetro plc (the 'Company') and its subsidiaries (the 'Group') for the year ended 31 December 2012, and the financial statements of Ruspetro plc (the 'Parent') for the period ended 31 December 2012.

### Business review

A full review of the activities of the Company during the year and recent events, as well as details of the Company's approach to its business and its strategy for creating value over the longer term, is contained in the chairman's statement on pages 6 and 7, the chief executive officer's statement on pages 10 to 15 and the operating and financial review on pages 18 to 25.

### Corporate governance

The Company is required to comply with the 2010 Code which is issued by the Financial Reporting Council and is referred to in the listing rules. This can be found at the Financial Reporting Council website at [www.frc.org.uk](http://www.frc.org.uk). A report on corporate governance and compliance with the provisions of the Code is set out on pages 34 to 37.

### Results and dividends

Ruspetro's results for the year ended 31 December 2012 are set out in the Company's consolidated income statement on page 58. The loss attributable to equity holders of the Company was US\$21,223 thousand. A final dividend for the year ended 31 December 2012 has not been declared.

### Directors

The names and biographies of current directors are set out on pages 32 and 33.

Ruspetro plc was incorporated as a public company in England and Wales on 20 October 2011 and Mr Wolcott and Mr Reed were appointed directors at incorporation, with the remaining directors being appointed to the Board on 2 December 2011.

### Directors' appointment and retirement

Directors may be appointed by ordinary resolution of shareholders or by the Board. A director holds office only until the next annual general meeting and, if not reappointed at such annual general meeting, shall vacate office at its conclusion. At every annual general meeting all the directors at the date of the notice convening the annual general meeting shall retire from office. If the Company does not fill the vacancy at the meeting at which a director retires, the retiring director shall be deemed to have been reappointed unless at the meeting it is resolved not to fill the vacancy or unless a resolution for the reappointment of the director is put to the meeting and lost.

This is in accordance with current best practice as outlined in the UK Corporate Governance Code 2010 which provides for all directors of FTSE companies to be subject to re-election by their shareholders every year.

### Directors' indemnities

Directors and officers of the Company are indemnified under the articles of association of the Company as provided by the Companies Act 2006. In addition, the Company has entered into deeds of indemnity with each director in respect of proceedings brought about by third parties, subject to the conditions set out in the Companies Act 2006.



### Directors' interests

The number of Ordinary shares of Ruspetro plc in which the directors (or a person connected with a director) were beneficially interested, as at 31 December 2012 was as follows:

Director	Number of existing Ordinary shares	Number of options granted as at 31 December 2012 <sup>(3)</sup>
Christopher Clark	100,000	—
Don Wolcott <sup>(1)</sup>	22,860,000	6,217,579
Tom Reed	3,271,440	4,145,053
Alexander Chistyakov	43,208,393	—
Rolf Stomberg	70,000	—
James Gerson <sup>(2)</sup>	99,150,000	—
Robert Jenkins	50,000	—
Joe Mach	—	—
James McBurney	40,000	—

(1) Don Wolcott, a director of the Company, owns 100% of Wind River Management Limited and is the beneficial owner of such shares.

(2) Limolines owns 99,150,000 shares. James Gerson, a director of the Company, is a consultant to Limolines and is deemed to be beneficially interested in such shares.

(3) The grant was in respect of 5% of the issued share capital of the Company as at the date immediately prior to admission to trading on the London Stock Exchange and prior to the issue of the Ordinary shares in connection with the initial public offering of the Company on the 19 January 2012.

### Share capital

The issued share capital of Ruspetro plc as at 31 December 2012 was 333,381,480 Ordinary shares of 10 pence each. Ruspetro plc is listed on the London Stock Exchange, and its first day of trading was 19 January 2012. The rights and obligations attached to these shares are governed by English law and the Company's articles of association.

### Voting rights

Ordinary shareholders are entitled to receive notice, attend and speak at the general meetings of the Company. Every shareholder shall have one vote for every share of which he is the holder if he is present in person, by proxy or, if a corporate shareholder, by a duly authorized representative.

A shareholder, entitled to attend and vote at a general meeting, may appoint one or more proxies to attend and vote instead of him. If a shareholder appoints more than one proxy he must specify the number of shares which each proxy is entitled to exercise rights over.

No shareholder holds securities carrying special rights as to the control of the Company. There are no agreements between holders of securities that are known to the Company which may result in restrictions on the transfer of voting rights.

### Transfer of shares

A member may transfer all or any of his certificated shares by an instrument of transfer in any usual form or in any form which the Board may approve. An instrument of transfer shall be signed by or on behalf of the transferor and, unless the share is fully paid, by or on behalf of the transferee. An instrument of transfer need not be under seal. The transferor shall remain the holder of the shares concerned until the name of the transferee is entered in the register in respect of the shares.

All transfers which are in uncertificated form shall be effected by means of the relevant system unless the CREST Regulations provide otherwise.

The Board may, in its absolute discretion, refuse to register the transfer of a certificated share which is not a fully paid share, provided that the refusal does not prevent dealings in shares in the Company from taking place on an open and proper basis. The Board may also refuse to register the transfer of a certificated share unless the instrument of transfer is:

- lodged, stamped (if stampable), at the office or at another place appointed by the Board, accompanied by the certificate for the share to which it relates and such other evidence as the Board may reasonably require to show the right of the transferor to make the transfer;
- in respect of one class of share only; and
- in favor of not more than four persons.

If the Board refuses to register a transfer of a share in certificated form, it shall send the transferee notice of its refusal within two months after the date on which the instrument of transfer was lodged with the Company.

## Governance

### Directors' report *continued*

No fee shall be charged for the registration of any instrument of transfer or other document relating to or affecting the title to a share.

Subject to the provisions of the CREST Regulations, the Board may permit the holding of shares in any class of shares in uncertificated form and the transfer of title to shares in that class, by means of a relevant system and may determine that any class of shares shall cease to be a participating security.

If a notice is given to a member in respect of a share, which is subsequently transferred, a person entitled to that share is bound by the notice if it was given to the member before the person entitled to that share was entered into the register as the holder of that share.

#### Amendments to the articles of association

Any amendment to the articles of association of the Company may be made by special resolution of the shareholders being a resolution proposed with not less than 21 days' notice as a special resolution and passed by more than 75% majority of those voting on the resolution.

#### Post balance sheet events:

Note 27 to the financial statements details all significant events after the balance sheet date of 31 December 2012.

#### Supplier payment policy

It is Ruspetro's payment policy to settle agreed outstanding accounts, in respect of all suppliers, in accordance with the terms and conditions agreed with the suppliers when placing the orders. Suppliers are made aware of these payment conditions.

#### Financial instruments

Ruspetro's use of financial instruments, together with objectives and policies on financial risk and exposure to foreign currency, credit, commodity, liquidity and interest rate risk can be found in note 25 to the financial statements.

#### Going concern

On the basis of the assumptions and cash flow forecasts prepared, the directors have assumed that the Group will continue to operate within both available and prospective financing facilities. Accordingly, the Group financial statements are prepared on the going concern basis and do not include any adjustments that would be required in the event that the loan holders request repayment and alternative finance is not available. Further details on the basis of preparation of the financial statements is available in note 2 of the consolidated financial statements on page 62 of this report.

#### Audit information

Each of the directors at the date of the approval of this report confirms that:

So far as the directors are aware there is no relevant audit information of which the Company's auditors are unaware; and the director has taken all the steps that he ought to have taken as director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of the information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

#### Donations

No donations of a political nature were made.

Further details are available in community relations section on page 31 of this report.

#### Auditors

PricewaterhouseCoopers LLP, the Company's auditors, have indicated their willingness to continue in office and resolutions seeking to reappoint them as the Company's auditors and to authorize the directors to determine their remuneration will be proposed at the forthcoming Annual General Meeting.

The Company's Annual General Meeting will be held at 11 am on Wednesday, 17 April 2013 at the Offices of White & Case 5 Old Broad Street, London, EC2N 1DW. Details of the meeting and the resolutions to be proposed are set out in a separate Notice of Meeting which accompanies this annual report.

By order of the Board.




**Tom Reed and Don Wolcott**  
Directors of Ruspetro plc  
18 March 2013

## Governance

# 2012 Directors' remuneration report

### Letter from the chairman of the remuneration committee

#### Dear Shareholder,

On behalf of the remuneration committee, I am pleased to introduce the directors' remuneration report for the year ended 31 December 2012, our first full year as a premium listed Company on the London Stock Exchange.

In line with our commitment to high standards of corporate governance, we have adopted some of the proposals from the Department for Business, Innovation and Skills ('BIS') regarding revised remuneration reporting regulations in advance of being required to do so. There are therefore three main sections to this report:

- **2013 Policy Report:** This sets out the elements of our remuneration policy going forward and discusses the key factors that were taken into account in setting this policy.
- **2012 Implementation Report:** This sets out how the remuneration policy has been implemented during the year, including the payments being made to directors and the link between performance and executive pay.
- **Audited information:** This section contains details of the directors' emoluments during the year to 31 December 2012 and has been audited in accordance with the current regulations for executive remuneration reporting.

#### Business context

During 2012 the Company has made significant progress. The Company drilled 33 wells against a plan for 24 new wells, installed a sales pipeline from the production location as well as other infrastructure projects. These projects were completed on schedule and within budget. The Company has also made significant progress in establishing internal policies and procedures with improvements to management reporting processes, reporting of safety incidents.

However, the production results have been disappointing with production below the end of year target, even accounting for the production of higher value condensate over crude oil. Similarly the financial results have disappointed. These issues are reflected in the performance of Ruspetro's share price on the London Stock Exchange during 2012.

#### Remuneration policy

During 2012, the remuneration committee worked on developing a remuneration policy that will support our vision of being recognized as a leading independent oil and gas producer, focused on providing superior shareholder returns.

Accordingly, a significant proportion of total remuneration for executive directors is performance-related so that any pay-out is aligned with the value created for our shareholders.

Prior to the Company's IPO, the committee decided to make an award of market priced share options, at the suggestion of the founding shareholders, to Don Wolcott, CEO, and Tom Reed, CFO. This was in order to further increase their alignment with shareholders, as the inherent share price hurdle will ensure that rewards for both executive directors will only be available if value has been created for our shareholders, and recognize their contribution in preparing the Company for IPO.

Going forward, any long-term incentive awards to executive directors will be in the form of performance shares under the Performance Share Plan ('PSP'), under which awards will only be earned subject to the satisfaction of stretching performance conditions relating to relative total shareholder return and the capital expenditure per incremental barrel of production.

In line with best practice, awards under the PSP will be subject to 'malus' provisions which will enable the committee to cancel or reduce awards prior to vesting in certain circumstances.

The annual bonus plan sets stretching targets for the executives on three key areas; production, financial performance and progress on corporate governance and operation activities.

#### Annual General Meeting

This report will be subject to an advisory vote at the Annual General Meeting on 17 April 2013. I will be happy to answer questions at the Annual General Meeting on our Remuneration Policy and the remuneration committee's activities and look forward to receiving your support.



#### Rolf Stomberg

**Chairman of the Remuneration Committee**  
18 March 2013

## Governance

### 2012 Directors' remuneration report *continued*

This report has been prepared on behalf of the Board by the remuneration committee and will be subject to an advisory vote at the Annual General Meeting on 17 April 2013.

The report has been prepared in accordance with the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (the 'Regulations') and meets the relevant requirements of the UK Listing Rules and the principles and provisions of the UK Corporate Governance Code.

In accordance with the Regulations, PricewaterhouseCoopers LLP, the Company's auditors, have audited the information as specified by the Companies Act 2006 for their audit which is included in the tables on the directors' emoluments, share awards granted to executive directors and the directors' interests in shares, together with the associated footnotes, on page 55 of this report.

#### 2013 policy report

##### Remuneration policy

Ruspetro's executive remuneration policy has been set with the objective of attracting, motivating and retaining the highest calibre executives in a manner that is consistent with best practice and aligned with the interests of shareholders.

Within these guiding principles, the remuneration policy for executive directors and other senior managers is set to ensure the following key goals are achieved:

- To provide a structure and level of pay which attracts and retains executives and senior managers capable of delivering the Company's strategic objectives and providing leadership within the relevant competitive markets, including relevant FTSE listed companies, Russian companies with a London listing and other Oil & Gas peers.
- To provide clear and transparent performance incentives to reward the attainment of key strategic goals and to align the remuneration of executives and senior managers with the interests of shareholders.
- Ensures that rewards provided through the remuneration policy are fairly earned and justified by performance. To that effect, a significant proportion of remuneration should be performance related and linked to both individual and corporate performance. Within the performance-related element, there should be an appropriate balance between short-term and long-term objectives.
- To ensure that inappropriate operational and financial risk-taking is neither encouraged nor rewarded through the Company's remuneration policies. The committee ensures that account is taken of environmental, social and governance risks when setting remuneration and is comfortable that remuneration packages do not raise such risks by motivating irresponsible behavior.
- The pay of executive directors and senior managers takes into account: (i) pay and conditions throughout the Company and (ii) corporate governance best practice.

The following table sets out a discussion of each element of the remuneration package for executive directors.

#### Future policy table from 1 January 2013 – executive directors

Element	Purpose and link to strategy	Opportunity level	Operation	Performance metrics
Salary	<ul style="list-style-type: none"> <li>— To provide fixed pay that is sufficient to attract and retain an experienced management team with significant expertise in successfully developing assets that are similar to Ruspetro.</li> </ul>	<ul style="list-style-type: none"> <li>— Salaries for executive directors were set prior to the IPO by reference to FTSE 250 companies and other Russian companies in the natural resources sector listed in London.</li> <li>— Salaries for executive directors were not increased in respect of 2013. The executive directors' salaries will therefore remain at the following levels:               <ul style="list-style-type: none"> <li>• CEO: US\$1,360,000</li> <li>• CFO: US\$827,000</li> <li>• President &amp; ED: US\$500,000</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>— Typically reviewed annually.</li> <li>— Benchmarked against UK companies of a similar size and complexity, relevant Oil &amp; Gas peers and other UK-listed companies from Russia and the CIS region operating in similar sectors, as these are the companies against which Ruspetro competes for executive talent.</li> </ul>	<ul style="list-style-type: none"> <li>— The performance of the individual in the role is one of the considerations that will be taken into account by the committee in setting the level of salary and any future increases.</li> </ul>
Benefits	<ul style="list-style-type: none"> <li>— To provide competitive benefits, in line with similarly sized companies and typical Russian practice.</li> </ul>	<ul style="list-style-type: none"> <li>— n/a</li> </ul>	<ul style="list-style-type: none"> <li>— Benefits include medical insurance, car allowance, life insurance and permanent health insurance.</li> <li>— The Company does not currently operate a pension scheme.</li> </ul>	<ul style="list-style-type: none"> <li>— None.</li> </ul>



Element	Purpose and link to strategy	Opportunity level	Operation	Performance metrics
Annual bonus	<ul style="list-style-type: none"> <li>— To incentivize and reward the achievement of both corporate and individual performance.</li> <li>— KPIs are consistent with the Company's short-term and medium-term objectives.</li> </ul>	<ul style="list-style-type: none"> <li>— Target performance: 100% of salary for the CEO and 75% of salary for the other executive directors.</li> <li>— Maximum opportunity: 150% of salary for the CEO and 100% of salary for the other executive directors.</li> </ul>	<ul style="list-style-type: none"> <li>— The annual bonus period runs from 1 January to 31 December.</li> <li>— Targets are set annually by the committee and are assessed following the year end.</li> <li>— All bonuses will be paid in cash although the committee may require part of the payment to be made in shares.</li> </ul>	<ul style="list-style-type: none"> <li>— Company objectives may include production, financial and the achievement of strategic and operational milestones.</li> <li>— No bonus will be payable unless the minimum level of performance has been met for both the Company and the individual element</li> <li>— The metrics for the annual bonus includes production measures (end of year production rate), financial measures (capital and operational budget control) and strategic and operational milestones. Greater weighting towards production and financial metrics will be used.</li> </ul>
Performance Share Plan ('PSP')	<ul style="list-style-type: none"> <li>— To link a substantial proportion of reward to the achievement of strategic targets which will drive the creation of long-term shareholder value as Ruspetro moves into the next stage of its development.</li> </ul>	<ul style="list-style-type: none"> <li>— Maximum award level under the plan of 150% of salary for the CEO and 125% of salary for other executive directors.</li> </ul>	<ul style="list-style-type: none"> <li>— Annual awards of performance shares which are only earned subject to the achievement of performance conditions over a three year period.</li> <li>— Malus: Share awards may be reduced or cancelled at any time prior to vesting, at the discretion of the remuneration committee, following events such as a material misstatement of results, failure of risk management, breach of health and safety regulations or serious reputational damage to the Company.</li> </ul>	<ul style="list-style-type: none"> <li>— The measures used for the PSP share plan do not repeat the measures used for the annual bonus plan. A financial measure of Total Shareholder Return against a group of peer companies will be used. A second operational measure will be used to evaluate the efficiency of capital expenditure required to increase production.</li> </ul>

### Annual bonus plan

Each year, the remuneration committee will assess the Company's performance against the metrics set at the beginning of the financial year. These will include production, financial and the achievement of strategic and operational milestones. Metrics will be defined according to these categories with greater weighting given to the production and financial metrics as appropriate for a Company at Ruspetro's stage of development. The overall performance assessment may be adjusted to account for exceptional items such as major health, safety and environmental incidents, major changes in oil price or actions by third party companies.

The overall Company performance assessment may be adjusted to reflect an individual executive's contribution to determine a final performance and bonus award. Therefore, no bonus will be payable unless the minimum level of performance has been met for both the Company and the individual element. The overall maximum opportunity under the annual bonus is 150% of salary for the CEO and 100% of salary for the other executive directors.

## Governance

### 2012 Directors' remuneration report *continued*

#### Performance share plan

The remuneration committee will decide during the second quarter of 2013 if an award of performance shares will be made to the executive directors under the Performance Share Plan and the details of the measures against which Company performance will be assessed. However, the performance measures will be 50% relative total shareholder return against the peer group of companies listed below, and 50% against capital dollar spent per incremental barrel of production achieved over the vesting period.

#### List of peer companies for Relative Total Shareholder Return

Company	Main areas of production
Ruspetro	Russia
Ophir Energy	West & East Africa
Premier Oil	UK, Norway, Africa, Middle East and Asia
Cairn Energy	Greenland, Spain, Nepal and Albania
Genel Energy	Iraq, Turkey
Essar Energy	India, Indonesia, Madagascar, Nigeria and Vietnam
Afren	Nigeria and Cote d'Ivoire
SOCO International	Vietnam and Africa
EnQuest	North Sea
Salamander Energy	Indonesia, Thailand, Vietnam, Laos
Heritage Oil	Iraq, Malta, Pakistan, Tanzania, Mali, DR Congo, Russia and Libya
Alliance Oil Company	Russia & CIS
Petropavlovsk	Russia & CIS
JKX Oil and Gas	Russia & CIS
Exilion	Russia

The overall maximum opportunity under the performance share plan is 150% of salary for the CEO and 125% of salary for the other executive directors.

#### Chairman's and non-executive directors' fees

Non-executive director remuneration is set by the chairman of the Board and the executive directors. No director is involved in setting his own fee.

The table below shows the remuneration policy in place for non-executive directors.

### Future policy table from 1 January 2013 – non-executive directors

Element	Purpose and link to strategy	Operation	Fee level
Non-executive director fees	<ul style="list-style-type: none"> <li>Set at a level to enable the Company to attract and retain high calibre non-executive directors with substantial experience of leading and advising large international companies within Ruspetro's sector and with experience in Russia and the UK.</li> </ul>	<ul style="list-style-type: none"> <li>Fees are set to take account of the typical time commitment and the level of involvement expected, as well as the challenging sector and geography within which the Company operates insofar as this impacts the demands placed on the role.</li> </ul>	<ul style="list-style-type: none"> <li>Non-executive chairman: US\$516,200 (£325,000 paid in sterling)</li> <li>Senior independent director: US\$240,000</li> <li>Non-executive director basic fee: US\$200,000</li> <li>Additional fee for committee chairmanship: <ul style="list-style-type: none"> <li>Audit committee: US\$45,000<sup>(i)</sup></li> <li>Remuneration committee: US\$20,000</li> <li>Nomination committee: US\$20,000</li> </ul> </li> <li>Additional fee for committee membership: US\$20,000</li> <li>In addition, should the fee payable to any director be diminished by the imposition of taxation other than that of the directors' tax residence, as a result of the Company's activities and domicile in the UK, the Company will increase the amount of fees payable to ensure that no director is disadvantaged as a result.</li> </ul>

(i) The fee for the chairman of the audit committee reflects the high importance of managing risk and compliance in the Company's operations and the time commitment required from the committee chairman.

### Consideration of conditions elsewhere in the Group

When setting the policy and levels of directors' pay, the remuneration committee is mindful of its responsibility to consider the pay and employment conditions of employees elsewhere within the Group.

In particular, the committee takes into account the salary increases provided to the general employee population. The committee has also reviewed the Company-wide reward policy, including the benefit offerings at different levels throughout the organization, and is satisfied that this policy is appropriate for the Group, supports the business's objectives and is consistent with the policy for executive directors.

The following table provides a summary of the increase in salary for the executive directors for 2013, as compared with the 8% increase for employees rated as above average performance throughout the Group. General inflation in Russia has been approximately 6% during 2012.

	Salary increase (effective 1 January 2013)
Executive directors	0%
Employees rated as performance 'Above Average'	8%
Other Employees	0–6%

## Governance

### 2012 Directors' remuneration report *continued*

#### Shareholder considerations

The remuneration committee is committed to ongoing dialogue with our shareholders and welcomes feedback on our remuneration policy and its application.

During February 2013, the remuneration committee chairman or the Company secretary entered into dialogue with a number of our institutional shareholders, as well as representatives from the Association of British Insurers ('ABI') and Institutional Shareholder Services ('ISS'). The purpose of these discussions was to discuss the Company's overall approach to remuneration and consult with shareholders on the proposed performance conditions under the PSP to Executive Directors.

Shareholders views were taken into consideration when formulating our policy. Shareholders expressed their disappointment with the performance of the Company's share price and stated that this reflected the missed production and financial targets.

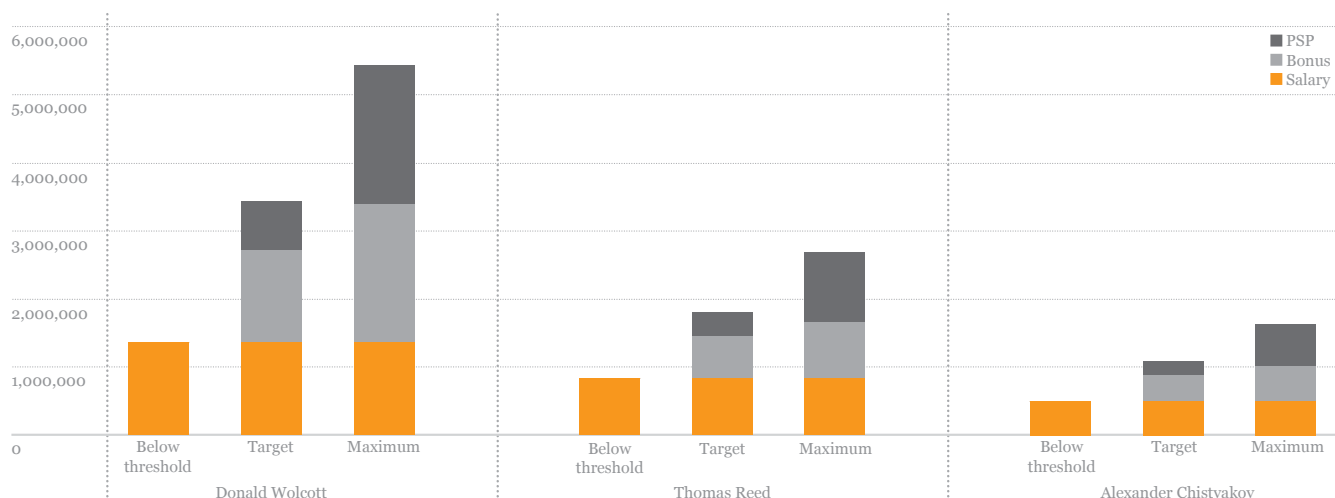
#### Remuneration scenarios based on 2013 policy for executive directors

The chart below shows hypothetical values of the ongoing remuneration package for executive directors under three assumed performance scenarios:

- **Below threshold.** Assumes no bonus is paid and no shares vest under the PSP.
- **Target performance.** Assumes payment of the target bonus of 100% of salary for the CEO and 75% of salary for other executive directors; and threshold vesting under the PSP of 25% of the award.
- **Maximum performance.** Assumes maximum bonus is earned (150% of salary for the CEO and 100% of salary for the other executive directors) and maximum vesting under the PSP.

Salary and benefits remain at the same level under all three performance scenarios. The chart reflects ongoing remuneration policy and therefore excludes the value of the pre-IPO options granted to the CEO and the CFO.

#### Remuneration scenarios



Note: the benefits provided to the executive directors are limited and represent a small percentage (less than 10%) of their base salary. Therefore this element has not been included in the scenarios.

#### Service contracts

The following section sets out the main provisions relating to remuneration contained in the directors' service contracts.

#### Executive directors

Each executive director's terms of appointment are set out in a service agreement with Ruspetro plc which may be terminated at any time by either party providing 12 months' notice.



The executive directors are also subject to certain restrictive covenants during the term of their agreement. They are not permitted to take up any office or employment with, or have any direct or indirect interest in any firm or Company which is in direct or indirect competition with the Group or any Company in which any member of the Group has an interest, without the consent of the Board.

Their service agreements also contain a general non-competition covenant in relation to the Group for six months from the date of termination.

Details of executive directors' contracts with Ruspetro plc are shown below.

Name	Commencement of appointment	Date of service contract	Notice period
Don Wolcott	1 December 2011	16 December 2011	12 months
Tom Reed	1 December 2011	16 December 2011	12 months
Alexander Chistyakov	1 December 2011	16 December 2011	12 months

Any termination payments to executive directors would be subject to the policy set out below.

#### Exit payment policy for executive directors

The Company operates the following policy in respect of exit payments:

- Notice periods do not exceed 12 months on either side.
- Termination payments in lieu of notice are restricted to a maximum of 12 months' salary plus the cost to the Company of providing contractual benefits.
- The executive directors do not have any contractual entitlement to a termination payment in lieu of notice in relation to bonus amounts and vesting of shares under the PSP. The committee has the discretion to determine an appropriate bonus amount, which would be subject to performance up to the date of termination and pro-rated for time. Vesting under any share incentive arrangements would be determined in accordance with the rules of such plan. Typically under the rules of the PSP, outstanding awards for good leavers will be pro-rated for time served and any performance conditions will continue to apply. For bad leavers, any unvested awards will lapse.
- In any exit payment scenario, the remuneration committee will give due consideration to the circumstances under which a director left.

#### Non-executive directors

Non-executive directors do not have service contracts and their terms are set out in a letter of appointment.

Each appointment is for an initial term of three years, subject to being re-elected as a director at each annual general meeting and may be terminated with a notice period of one month (three months' notice in the case of the Board Chairman).

Non-executive directors are not entitled to any compensation on leaving the Board.

Name	Commencement of appointment	Date of letter of appointment	Notice period
Christopher Clark	2 December 2011	9 December 2011	3 months
Rolf Stomberg	2 December 2011	9 December 2011	1 month
Robert Jenkins	2 December 2011	9 December 2011	1 month
James McBurney	2 December 2011	9 December 2011	1 month
Joe Mach	2 December 2011	9 December 2011	1 month
James Gerson	2 December 2011	9 December 2011	1 month

## Governance

### 2012 Directors' remuneration report *continued*

#### Remuneration committee

##### Membership and terms of reference

The remuneration committee was established by the Board prior to the Company's listing on the London Stock Exchange and its members, all of whom were appointed at the time of its establishment, are shown in the table below.

Name	Role
Rolf Stomberg	Chairman
Christopher Clark	Member
Joe Mach	Member
James McBurney	Member

In line with the principles of the UK Corporate Governance Code, the committee comprises solely of independent non-executive directors and the Board chairman, who was considered independent on appointment.

No other non-executive directors were members of the committee during the year.

Under its terms of reference, the committee's main responsibility is to determine the Company's overall framework for remuneration and to set the remuneration packages for the executive directors, the Chairman of the Board and other members of senior management. The committee is also responsible for the design and operation of all share incentive plans.

The remuneration of the non-executive directors is determined by the chairman of the Board and the executive directors.

##### Advice to the committee

During the year to 31 December 2012, the following advisors provided services to the committee:

- Deloitte LLP ('Deloitte') – provision of advice on various remuneration matters under consideration by the Committee including on the preparation of this remuneration report. Deloitte is a member of the Remuneration Consultants Group and provides advice in line with its code of conduct in relation to executive remuneration consulting in the UK.
- White & Case LLP – provision of legal advice in relation to share plans and service contracts.

The Committee met twice in 2012 with all members in attendance at both meetings.

In addition to the services described above, other parts of Deloitte provided unrelated taxation services to the Group. The remuneration committee does not consider there to be any conflict of interest in this regard.

Furthermore, the committee invited the chief executive officer, the chief financial officer, the HR director and the Company secretary to attend its meetings as necessary. No person provided input or was involved when their own remuneration was being discussed.

##### Discussion of individual remuneration elements

##### Salary

Salaries for executive directors were set prior to Ruspetro's listing on the London Stock Exchange by reference to the FTSE 250 Index and other Russian/CIS companies in the natural resources sector listed in London. These are the companies against which Ruspetro competes for executive talent.

The committee has made no salary increases for 2013 to any of the executive directors.

Both the current salary levels and salaries with effect from 1 January 2013 are shown below. Executives have two elements to their salary, a UK element and a Russian element.

Name	2012 base annual salary (UK)	2012 base annual salary (Russia)	Total 2012 salary
Don Wolcott	US\$200,000	US\$1,233,432	US\$1,433,432
Tom Reed	US\$200,000	US\$682,679	US\$882,679
Alexander Chistyakov	US\$200,000	US\$415,282	US\$615,282

### Benefits in kind

During the year, executive directors received private medical insurance cover, a car and driver if required, life insurance and permanent health insurance. The Company does not currently operate any pension plans for executive directors or any other employees.

### Annual bonus plan

The target bonus for 2012 was 100% of base salary for the CEO and 75% of base salary for the other two executive directors, with a maximum opportunity of 150% and 100% of base salary, respectively.

The actual bonus payable in respect of 2012 has been determined by the committee taking into account the following factors:

- End of year production at approximately 6,500 boepd against a target of 10,400 boepd. However 1,500 boepd condensate which achieves a higher level of income due to a lower rate of the Mineral Extraction Tax. The final production rate is approximately 8,000 boepd.
- End of year average daily production of 4,600 boepd against target of 7,600 boepd. See note above regarding additional value of condensate.
- EBITDA of -US\$5.8 million against target of US\$26 million for the year.
- Very successful completion of the infrastructure projects to handle increased oil production.
- Development of a HSE management and reporting system.
- Development of monthly management information reporting.

Despite the progress to date on the installation and commissioning of production infrastructure, the development of the corporate governance processes and procedures, the Board of directors believe the missed production and financial targets and resulting poor performance for shareholders of the market value of the Company do not justify a bonus to the executive directors in respect of 2012.

### Pre-IPO option awards to the CEO and CFO

As previously disclosed, prior to the Company's IPO on the London Stock Exchange, the Company (following the recommendation of the remuneration committee) granted market priced options to Don Wolcott and Tom Reed on 17 January 2012, with an exercise price equal to the IPO offer price.

The granting of these options was intended to further enhance the alignment between executive directors and shareholders, as the inherent share price hurdle will ensure that rewards will only be earned if shareholder value has been created. In addition, these options were intended to reward the contribution of the directors in preparing the Company for IPO.

These options vest in equal tranches on the first, second and third anniversary of the grant date. The options can be exercised between the third and tenth anniversary of the date of grant. The vesting of these options is not subject to the satisfaction of any performance criteria.

The number of options granted to each Executive Director is shown on page 43 of the report.

### Performance Share Plan (the 'PSP')

The remuneration committee will decide during the second quarter of 2013 if an award of performance shares will be made to the executive directors under the Performance Share Plan and the details of the measures against which Company performance will be assessed. However, the performance measures will be 50% against relative total shareholder return and 50% against capital dollar spent per incremental barrel of production achieved during the period.

The final target value for efficiency of capital expenditure to increase production (US\$ of Capex per incremental barrel) will be determined during the second quarter based on the financial budget agreed with the Board of directors.

## Governance

### 2012 Directors' remuneration report *continued*

The following sets out details in respect of the intended June 2013 PSP grants.

	Discussion
<b>Performance Conditions</b>	<ul style="list-style-type: none"> <li>— 50% against Total Shareholder Return against a group of peer companies</li> <li>— 50% against the efficiency of capital expenditure required to increase production</li> </ul>
<b>Targets set in respect of 2013 to 2015</b>	<ul style="list-style-type: none"> <li>— Total Shareholder Return</li> <li>— Below Median = 0% (0% of LTIP Award)</li> <li>— Median = 35% (17.5% of LTIP Award)</li> <li>— Upper Quartile = 100% (50% of LTIP Award)</li> <li>— Efficiency of Capital expenditure to increase production</li> <li>— Greater than 10% less than target efficiency = 0% (0% of LTIP Award) 10% less than above target efficiency = 35% (17.5% of LTIP Award)</li> <li>— At target efficiency = 75% (37.5% of LTIP Award) at 10% or below of target efficiency = 100% (50% of LTIP Award)</li> </ul>

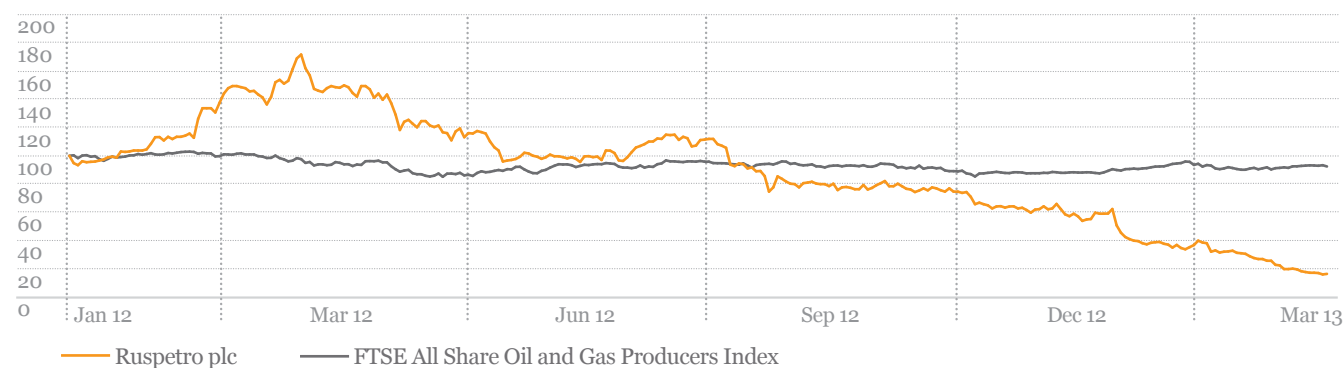
#### Directors' shareholdings

The executive directors already hold significant shareholdings in the Company, as shown in the table below as at 31 December 2012:

	Don Wolcott	Tom Reed	Alexander Chistyakov
Shares beneficially held	22,860,000	3,271,440	43,208,393
Shares currently deferred subject to continuous employment only or no forfeiture provisions	6,217,579	4,145,053	—
Total number of shares	29,077,579	7,416,493	43,208,393
Value of shareholding assuming share price of £0.7900 at 31 December 2012	£22,971,287	£5,859,029	£34,134,630
Shareholding as a multiple of salary <sup>(1)</sup>	27.3	12.6	108.4

(1) Average exchange for 31 December 2012 used is US\$1.6153/£1.0000

#### Total Shareholder Return



Source: Thomson Reuters DataStream

The chart above shows the Company's total shareholder return since trading for Ruspetro shares began on the London Stock Exchange on 19 January 2012 against the FTSE All Share Oil & Gas Producers Index.

The FTSE All Share Oil & Gas Producers Index was chosen as it is a broad based index of which the Company is a constituent.



**AUDITED INFORMATION****Directors' emoluments for the year ended 31 December 2012**

US\$'000	Salary/fees	Benefits	Bonus	Total 2012	Total 2011
<b>Executive directors</b>					
Don Wolcott	1,433	36	—	1,469	462
Tom Reed	883	27	—	910	354
Alexander Chistyakov	615	30	—	645	161
<b>Non-executive Directors</b>					
Christopher Clark	576 <sup>(1)</sup>	12	—	588	47
Rolf Stomberg	288 <sup>(2)</sup>	—	—	288	25
Robert Jenkins	273 <sup>(3)</sup>	—	—	273	22
James McBurney	268 <sup>(3)</sup>	—	—	268	22
Joe Mach	240	—	—	240	20
James Gerson	200	—	—	200	17

(1) Mr Clark's fees are paid in GBP, converted from USD at exchange rate of the day. Average exchange for 2012 used is US\$1.5832/£1.0000.

(2) Dr Stomberg's fees are paid in euros, converted from USD. Average exchange rate used is 1.2831 euros/US\$1.0000.

(3) The Directors are based in the UK and salary and fees are paid in GBP. Average exchange for 2012 used is US\$1.5832/£1.0000.

**Share option awards to executive directors**

Director	Date of grant	Number of options granted	Options exercised in year	Options at end of year	Exercise price (p)	Date from which exercisable	Expiry date
Don Wolcott <sup>(1)</sup>	17 Jan 2012	6,217,579	—	6,217,579	134	17 Jan 2015	17 Jan 2022
Tom Reed <sup>(1)</sup>	17 Jan 2012	4,145,053	—	4,145,053	134	17 Jan 2015	17 Jan 2022

(1) The exercise of these options is not subject to the satisfaction of any performance criteria.

The highest and lowest closing prices for the Company's shares during the year ended 31 December 2012 was £2.3000 and £0.7225 respectively. The closing price for a Ruspetro plc share on 31 December 2012 was £0.7900.

## Governance

2012 Directors' remuneration report *continued***Directors' interests in shares**

The table below sets out the interests of each director of the Company (as well as the interests held by his or her connected persons) in the Company's shares, excluding interests under share options, the dates stated:

Director	19 January 2012 <sup>(1)</sup>	31 December 2012
Don Wolcott	22,860,000	22,860,000
Tom Reed	3,271,440	3,271,440
Alexander Chistyakov	34,768,560	43,208,393
Christopher Clark	—	100,000
Rolf Stomberg	—	70,000
Robert Jenkins	—	50,000
James McBurney	—	40,000
Joe Mach	—	—
James Gerson <sup>(2)</sup>	99,150,000	99,150,000

(1) Number of shares held by each director as at admission of the Company's shares on the Official List of the London Stock Exchange.

(2) Limolines owns 99,150,000 shares. James Gerson is a consultant to Limolines and is deemed to be beneficially interested in such shares.

There has been no change in the interests of the directors and their connected persons between 31 December 2012 and the date of this report.

This report has been approved by the remuneration committee of the Board on 18 February 2013 and signed on its behalf by:



**Rolf Stomberg**

**Chairman of the remuneration committee**

18 March 2013

# Financial statements

## Independent auditor's report

### Independent auditors' report to the members of Ruspetro plc

We have audited the group financial statements of Ruspetro plc for the year ended 31 December 2012 which comprise the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Financial Position, the Consolidated Statement of Changes in Equity, the Consolidated Statement of Cash Flows, the significant accounting policies and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on financial statements

In our opinion the group financial statements:

- give a true and fair view of the state of the group's affairs as at 31 December 2012 and of its loss and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

### Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the group financial statements are prepared is consistent with the group financial statements;

### Emphasis of matter

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of the disclosure made in note 2 to the financial statements concerning the Group's ability to continue as a going concern. This ability is dependent whether the Group can obtain additional financing and an extension of the maturities of the existing debt facilities from the respective lenders and shareholders. This condition, along with the other matters explained in note 2 to the financial statements, indicate the existence of a material uncertainty which may cast significant doubt about the Group's and Company's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Group and Company was unable to continue as a going concern.

### Matters on which we are required to report by exception

We have nothing to report in respect of the following: Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or

Under the Listing Rules we are required to review:

- the directors' statement, in relation to going concern;
- the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

### Other matter

We have reported separately on the parent company financial statements of Ruspetro plc for the period ended 31 December 2012 and on the information in the Directors' Remuneration Report that is described as having been audited. That report includes an emphasis of matter.



### Kevin Reynard (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Aberdeen  
20 March 2013

### Notes:

- a) The maintenance and integrity of the Ruspetro plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## Financial statements

**Consolidated statement of comprehensive income**

for the year ended 31 December 2012 (presented in US\$ thousands, except otherwise stated)

	Note	Year ended 31 December	
		2012	2011
Revenue	7	76,230	38,718
Cost of sales	8	(74,816)	(52,355)
<b>Gross profit/(loss)</b>		<b>1,414</b>	<b>(13,637)</b>
Selling and administrative expenses	9	(40,481)	(14,982)
Other income/(expenses), net	10	20,215	(1,385)
<b>Operating loss</b>		<b>(18,852)</b>	<b>(30,004)</b>
Finance costs	11	(29,815)	(33,126)
Change in fair value of call option	17	(3,240)	–
Foreign exchange gain/(loss), net		23,804	(25,535)
<b>Loss before income tax</b>		<b>(28,103)</b>	<b>(88,665)</b>
Income tax benefit	12	819	3,602
<b>Loss for the period</b>		<b>(27,284)</b>	<b>(85,063)</b>
<b>Other comprehensive income</b>			
Exchange difference on translation to presentation currency		6,061	7,291
<b>Total comprehensive loss for the period</b>		<b>(21,223)</b>	<b>(77,772)</b>
<b>Loss attributable to:</b>			
Equity holders of the parent		(27,284)	(81,095)
Non-controlling interests		–	(3,968)
<b>Loss for the period</b>		<b>(27,284)</b>	<b>(85,063)</b>
<b>Total comprehensive loss attributable to:</b>			
Equity holders of the parent		(21,223)	(74,169)
Non-controlling interests		–	(3,603)
<b>Total comprehensive loss for the period</b>		<b>(21,223)</b>	<b>(77,772)</b>
<b>Loss per share</b>			
Basic and diluted loss per ordinary share (US\$)	26	(0.09)	(0.41)

The accompanying notes on pages 62 to 86 are an integral part of these consolidated financial statements.



**Don Wolcott**  
Chief executive officer



**Tom Reed**  
Chief financial officer



## Financial statements

## Consolidated statement of financial position

as at 31 December 2012 (presented in US\$ thousands, except otherwise stated)

	Note	Year ended 31 December	
		2012	2011
<b>Assets</b>			
<b>Non-current assets</b>			
Property, plant and equipment	13	226,736	111,313
Mineral rights and other intangibles	14	425,551	401,513
		652,287	512,826
<b>Current assets</b>			
Inventories	15	2,567	2,610
Trade and other receivables	16	19,721	5,810
Income tax prepayment		37	36
Other current assets	17	24	–
Cash and cash equivalents	18	34,416	1,294
		56,765	9,750
<b>Total assets</b>		709,052	522,576
<b>Shareholders' equity</b>			
Share capital	19	51,226	7
Share premium	19	220,506	49,994
Retained loss		(87,741)	(60,208)
Exchange difference on translation to presentation currency		(24,061)	(30,122)
Other reserves		20,517	–
<b>Equity, retained earnings/(loss) and other reserves attributable to Parent</b>		180,447	(40,329)
Non-controlling interests	19	–	(408)
<b>Total equity</b>		180,447	(40,737)
<b>Liabilities</b>			
<b>Non-current liabilities</b>			
Borrowings	20	348,493	360,250
Provision for dismantlement	21	7,697	5,961
Deferred tax liabilities	12	89,900	85,726
Other non-current liabilities	17	15,365	–
		461,455	451,937
<b>Current liabilities</b>			
Borrowings	20	21,804	46,197
Trade and other payables	22	39,721	13,496
Taxes payable other than income tax		4,544	4,226
Other current liabilities		1,081	47,457
		67,150	111,376
<b>Total liabilities</b>		528,605	563,313
<b>Total equity and liabilities</b>		709,052	522,576

The accompanying notes on pages 62 to 86 are an integral part of these consolidated financial statements.

The financial statements on pages 58 to 86 were approved by the Board of Directors on 20 March 2013.



**Don Wolcott**  
Chief executive officer



**Tom Reed**  
Chief financial officer

## Financial statements

## Consolidated statement of changes in equity

for the year ended 31 December 2012 (presented in US\$ thousands, except otherwise stated)

	Note	Attributable to owners of the Parent					Total	Non-controlling interest	Total equity
		Share capital	Share premium	Retained earnings/ (accumulated loss)	Exchange difference on translation to presentation currency	Other reserves			
Balance as at 1 January 2011		6	39,989	20,887	(37,049)	–	23,833	3,195	27,028
Loss for the period		–	–	(81,095)	–	–	(81,095)	(3,968)	(85,063)
Other comprehensive income for the period		–	–	–	6,927	–	6,927	365	7,291
Total comprehensive income/(loss) for the period		–	–	(81,095)	6,927	–	(74,168)	(3,603)	(77,772)
Issue of share capital		1	10,005	–	–	–	10,006	–	10,006
Balance as at 31 December 2011		7	49,994	(60,208)	(30,122)	–	(40,329)	(408)	(40,737)
Balance as at 1 January 2012		7	49,994	(60,208)	(30,122)	–	(40,329)	(408)	(40,737)
Loss for the period		–	–	(27,284)	–	–	(27,284)	–	(27,284)
Other comprehensive income for the period		–	–	–	6,061	–	6,061	–	6,061
Total comprehensive income/(loss) for the period		–	–	(27,284)	6,061	–	(21,223)	–	(21,223)
Reorganization of the Group	19	31,818	(49,994)	(249)	–	18,176	(249)	408	159
Issue of share capital	19	19,401	220,506	–	–	–	239,907	–	239,907
Share options of shareholders	17	–	–	–	–	(9,694)	(9,694)	–	(9,694)
Share-based payment compensation	19	–	–	–	–	12,035	12,035	–	12,035
Balance as at 31 December 2012		51,226	220,506	(87,741)	(24,061)	20,517	180,447	–	180,447

The accompanying notes on pages 62 to 86 are an integral part of these consolidated financial statements.



**Don Wolcott**  
Chief executive officer



**Tom Reed**  
Chief financial officer

## Financial statements

## Consolidated statement of cash flows

for the year ended 31 December 2012 (presented in US\$ thousands, except otherwise stated)

	Note	Year ended 31 December	
		2012	2011
<b>Cash flows from operating activities</b>			
Loss before income tax		(28,103)	(88,665)
Adjustments for:			
Depreciation, depletion and amortization	13, 14	19,762	24,524
Foreign exchange (income)/loss		(23,804)	25,535
Finance costs	11	29,815	33,126
Change in fair value of call option	17	3,240	–
Gain on settlement of Makayla debt	10	(21,282)	–
Share-based payment compensation	19	12,035	–
Other operating expenses		826	2,286
<b>Operating cash outflows before working capital adjustments</b>		<b>(7,511)</b>	<b>(3,194)</b>
Working capital adjustments:			
Change in trade and other receivables		(964)	(530)
Change in inventories		43	(472)
Change in trade and other payables		12,259	(648)
Change in other taxes receivable/payable		(12,629)	4,292
<b>Net cash flows used in operating activities</b>		<b>(8,802)</b>	<b>(552)</b>
<b>Cash flows from investing activities</b>			
Purchase of property, plant and equipment		(106,583)	(32,335)
<b>Net cash used in investing activities</b>		<b>(106,583)</b>	<b>(32,335)</b>
<b>Cash flows from financing activities</b>			
Proceeds from issue of share capital (net)	19	213,699	10,006
Repayments of loans and borrowings		(18,575)	–
Interest paid		(50,645)	–
Cash inflow on reorganization		87	–
<b>Net cash generated from financing activities</b>		<b>144,566</b>	<b>10,006</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>29,181</b>	<b>(22,881)</b>
Effect of exchange rate changes on cash and cash equivalents		3,941	5,310
Cash and cash equivalents at the beginning of the period		1,294	18,865
<b>Cash and cash equivalents at the end of the period</b>		<b>34,416</b>	<b>1,294</b>

The accompanying notes on pages 62 to 86 are an integral part of these consolidated financial statements.



**Don Wolcott**  
Chief executive officer



**Tom Reed**  
Chief financial officer

## Financial statements

# Notes to the consolidated financial statements

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands, except otherwise stated)

### 1. Corporate information

The consolidated financial statements of Ruspetro plc (the 'Parent' or 'Ruspetro') and its subsidiaries, together referred to as 'the Group' for the year ended 31 December 2012 were approved by its Board of Directors on 20 March 2013.

The Parent was incorporated in the United Kingdom on 20 October 2011 as a public company under the provisions of the Companies Act 2006 of England and Wales. The Parent's registered office is 57–59 St James's Street, London, SW1A 1LD England.

On 18 January 2012, the Parent became a company of the Group through a series of shares exchanges (see Note 19).

Although these consolidated financial statements have been released in the name of the Parent, they represent an in-substance continuation of the existing Group, headed by Ruspetro Holding Limited (the 'Previous Parent') and the following accounting treatment has been applied to account for the reorganization:

- the consolidated assets and liabilities of the subsidiaries were recognized and measured at the pre-reorganization carrying amounts, without restatement to fair value;
- the retained earnings and other equity balances recognized in the consolidated statement of financial position reflect the consolidated retained earnings and other equity balances of the Previous Parent immediately prior to the reorganization, and the results of the period from 1 January 2012 to the date of the reorganization are those of the Previous Parent as the Parent was not active prior to the reorganization. Subsequent to the reorganization, the equity structure reflects the applicable movements in equity of the Parent, including the equity instruments issued to effect the reorganization and the Initial Public Offering ('IPO') (Note 19); and
- comparative numbers presented in the consolidated financial statements are those reported in the consolidated financial statements of the Previous Parent for the year ended 31 December 2011.

The principal activities of the Group are exploration for and production of crude oil. The operating subsidiaries of the Group – OJSC INGA and OJSC Trans-oil (hereinafter referred to as INGA and Trans-oil respectively) hold three licenses for exploration for and extraction of crude oil and natural gas in the Khanty-Mansiysk region of the Russian Federation.

Details of subsidiaries consolidated within the Group are as follows:

Company	Business activity	Country of incorporation	Year of incorporation	Effective ownership	
				31 December 2012	2011
Ruspetro Holding Limited	Holding company	Republic of Cyprus	2007	100%	100%
Ruspetro LLC ('Ruspetro Russia')	Crude oil sale	Russian Federation	2005	100%	95%
INGA	Exploration and production of crude oil	Russian Federation	1998	100%	95%
Trans-oil	Exploration and production of crude oil	Russian Federation	2001	100%	95%

On 19 January 2012, LLC Sberbank Capital transferred its 5% participating interest in Ruspetro Russia to the Company in consideration for a pro rata number of shares in the Parent. As of this date, all of the Group's subsidiaries were 100% owned.

### 2. Basis of preparation

These consolidated financial statements of the Parent, including those of its subsidiaries (the 'Group') have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. The consolidated financial statements are prepared under the historical cost convention, modified for fair values under IFRS.

The consolidated financial statements are presented in US dollars ('US\$') and all values are rounded to the nearest thousand unless otherwise indicated.

### Going concern

These consolidated financial statements are prepared on a going concern basis, which presumes that the Group will be able to realize its assets and discharge its liabilities in the normal course of business in the foreseeable future.

At 31 December 2012, the Group had net current liabilities of US\$10,385 thousand, which included cash in hand of US\$34,416 thousand. Furthermore, the Group has a long-term loan from Sberbank amounting to US\$286,671 thousand, which is repayable in May 2015, together with long-term shareholder loans of US\$61,822 thousand which are also repayable in May 2015.

Management consider that the continued operational existence of the Group is dependent upon the ability to make further investment in field development in order to increase hydrocarbon production and sales. In response to these circumstances, management are in discussions with existing lenders with regard to the provision of additional long-term debt financing and the extension of the maturity of the existing long-term loans.



## 2. Basis of preparation *continued*

Management consider the additional financing and the maturity extension of existing debt will provide sufficient financial resources such that the Group can further invest in field development with the intention of raising production. Management further consider that the additional cash flows to be generated from production would allow the Group to service debt, further increase production and fund other Group activities. In developing their cash flow forecasts, management have a number of significant assumptions. These include assumptions as to future hydrocarbon prices, taxes, production volumes, and inflation and are further discussed in Note 4.

Agreements with the existing lenders as to additional financing and maturity extension have not been entered into as of the date of these financial statements. In the event that such additional financing and maturity extension is not obtained, the Group may be unable to realize its assets and discharge its liabilities in the normal course of business. These circumstances represent a material uncertainty that may cast significant doubt on the Group's and Parent's ability to continue as a going concern.

However, on the basis of the assumptions and cash flow forecasts prepared, management have assumed that the Group will continue to operate within both available and prospective facilities. Accordingly, the Group financial statements are prepared on the going concern basis and do not include any adjustments that would be required in the event that the loan holders do request repayment and alternative finance is not available.

## 3. Summary of significant accounting policies

### Principles of consolidation

#### Subsidiaries

Subsidiaries are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases.

All intercompany transactions, balances and unrealized gains on transactions between Group companies are eliminated; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

The financial statements of the subsidiaries are prepared for the same reporting year as the Parent, using consistent accounting policies.

#### Business combinations

The Group uses the acquisition method of accounting to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognizes any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognized directly in profit or loss.

#### Oil and natural gas exploration, evaluation and development expenditure

Oil and gas exploration activities are accounted for in a manner similar to the successful efforts method. Costs of successful development and exploratory wells are capitalized.

#### Development costs

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of development wells, including unsuccessful development or delineation wells, is capitalized within oil and gas properties.

#### Property, plant and equipment, Mineral rights and other intangibles

Oil and gas properties and other property, plant and equipment, including mineral rights are stated at cost, less accumulated depletion, depreciation and accumulated impairment losses.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of the decommissioning obligation, and for qualifying assets, borrowing costs. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

## Financial statements

# Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

### 3. Summary of significant accounting policies *continued*

#### **Depreciation and Depletion**

Oil and gas properties are depreciated on a unit-of-production basis over proved developed reserves of the field concerned, except in the case of assets whose useful life is shorter than the lifetime of the field, in which case the straight-line method is applied. Mineral rights are depleted on the unit-of-production basis over proved and probable reserves of the relevant area.

Other property, plant and equipment are generally depreciated on a straight-line basis over their estimated useful lives as follows:

	Years
Buildings and constructions	30–50
Other property, plant and equipment	1–6

#### **Major maintenance and repairs**

Expenditure on major maintenance refits or repairs comprises the cost of replacement assets or parts of assets, inspection costs and overhaul costs. Where an asset or part of an asset that was separately depreciated and is now written off is replaced and it is probable that future economic benefits associated with the item will flow to the Group, the expenditure is capitalized. Where part of the asset was not separately considered as a component, the replacement value is used to estimate the carrying amount of the replaced assets which is immediately written off. Inspection costs associated with major maintenance programs are capitalized and amortized over the period to the next inspection. All other maintenance costs are expensed as incurred.

#### **Intangible assets**

Intangible assets are stated at the amount initially recognized, less accumulated amortization and accumulated impairment losses. Intangible assets include computer software.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. Amortization is calculated on a straight-line basis over their useful lives, except for mineral rights that are depleted on the unit-of-production basis as explained above.

#### **Impairment of assets**

The Group monitors internal and external indicators of impairment relating to its tangible and intangible assets.

The recoverable amounts of Cash Generating Units ('CGU') and individual assets have been determined based on the higher of value-in-use (VIU) calculations and fair values less costs to sell (FVLCS). These calculations 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.

Given the shared infrastructure and interdependency of cash flows related to the three licenses the Group holds, the assets are considered to represent one CGU, which is the lowest level where largely independent cash flows are deemed to exist.

#### **Share option plan**

The share option plan, under which the Group has the ability to choose whether to settle it in cash or equity instruments at the discretion of the Board of Directors is accounted for as an equity settled transaction. The fair value of the options granted by the Parent to employees is measured at the grant date and calculated using the trinomial option pricing model and recognized in the consolidated financial statements as a component of equity with a corresponding amount recognized in selling, general and administrative expenses over the time share reward vest to the employee.

Modifications of the terms or conditions of the equity instruments granted in a manner that reduces the total fair value of the share-based payment arrangement or is not otherwise beneficial to the employee, are accounted for as services received in consideration for the equity instruments granted as if the modification had not occurred.

#### **Financial instruments**

A financial instrument is any contract that gives rise to financial assets or liabilities.

Financial assets within the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, or available for sale financial assets, as appropriate. When financial assets are recognized initially, they are measured at fair value, plus directly attributable transaction costs for all financial assets not carried at fair value through profit or loss.

The Group determines the classification of its financial assets at initial recognition.

### 3. Summary of significant accounting policies *continued*

Financial instruments carried on the consolidated statement of financial position include loans and receivables, cash and cash equivalent balances, borrowings, accounts payable and put and call options. The particular recognition and measurement methods adopted are disclosed in the individual policy statements associated with each item.

An obligation to acquire own shares is classified as a liability. The liability to repurchase own shares is initially recognized at the fair value of consideration payable (being the net present value of estimated redemption amount) and it is recorded as deduction of equity. Subsequent changes (revision of estimate, unwinding of discount) are recognized in profit or loss. If options are not exercised, the amount recognised as a liability is transferred to equity.

Rights to acquire own shares are classified as assets. The right to repurchase own shares is initially recognized at the fair value of consideration payable, estimated using the Black-Scholes option pricing model, and it is recorded as increase of equity. Subsequent changes (revision of estimate) are recognized in profit and loss.

#### **Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are subsequently carried at amortized cost using the effective interest method less any provision for impairment.

A provision for impairment is recognized when there is an objective evidence that the Group will not be able to collect all amounts due according to the original terms of the loans and receivables. The amount of provision is the difference between the assets' carrying value and the present value of the estimated future cash flows, discounted at the original effective interest rate. The change in the amount of the loan or receivable is recognized in profit or loss. Interest income is recognized in profit or loss by applying the effective interest rate.

#### **Cash and cash equivalents**

Cash and cash equivalents in the consolidated statement of financial position comprise cash at banks and on hand and short-term deposits with an original maturity of three months or less.

For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts if any.

#### **Borrowings and accounts payable**

The Group's financial liabilities are represented by accounts payable and borrowings.

Borrowings are initially recognized at fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortized cost using the effective interest method; any difference between the initial fair value of the consideration received (net of transaction costs) and the redemption amount is recognized as an adjustment to interest expense over the period of the borrowings.

A financial liability is derecognized when the obligation under the liability is discharged or canceled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the profit or loss.

#### **Impairment of financial assets**

The Group assesses at the end of each reporting period whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is an objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

#### **Inventories**

Inventories are stated at the lower of cost and net realizable value. Cost of inventory is determined on the weighted average basis. The cost of finished goods and work in progress comprises raw material, direct labor, other direct costs and related production overheads (based on normal operating capacity) but excludes borrowing costs. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated cost of completion and selling expenses.

## Financial statements

# Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

### 3. Summary of significant accounting policies *continued*

#### Provisions

##### General

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to any provision is presented in profit or loss net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using rates that reflect, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as finance costs.

##### Provision for dismantlement

Provision for dismantlement is related primarily to the conservation and abandonment of wells, removal of pipelines and other oil and gas facilities together with site restoration activities related to the Group's license areas. When a constructive obligation to incur such costs is identified and their amount can be measured reliably, the net present value of future decommissioning and site restoration costs is capitalized within property plant and equipment with a corresponding liability. Provisions are estimated based on engineering estimates, license and other statutory requirements and practices adopted in the industry and are discounted to net present value using discount rates reflecting adjustments for risks specific to the obligation.

Adequacy of such provisions is periodically reviewed. Changes in provisions resulting from the passage of time are reflected in profit or loss each year under finance costs. Other changes in provisions, relating to a change in the expected pattern of settlement of the obligation, changes in the discount rate or in the estimated amount of the obligation, are treated as a change in accounting estimate in the period of the change and are reflected as an adjustment to the provision and a corresponding adjustment to property, plant and equipment. If a decrease in the liability exceeds the carrying amount of the asset, the excess is recognized immediately in profit or loss.

#### Taxes

##### Income tax

The income tax expense comprises current and deferred taxes calculated based on the tax rates that have been enacted or substantively enacted at the end of the reporting period. Current and deferred taxes are charged or credited to profit or loss except where they are attributable to items which are charged or credited directly to equity, in which case the corresponding tax is also taken to equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred taxes provide for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred tax arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recognized for all deductible temporary differences and carry forward of unused tax credits and unused tax losses only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences or carry forward losses can be utilized.

Unrecognized deferred tax assets are reassessed at the end of each reporting period and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are offset when the Group has a legally enforceable right to set off current tax assets and liabilities, when deferred tax balances are referred to the same governmental body (i.e. federal, regional or local) and the same subject of taxation and when the Group intends to perform an offset of its current tax assets and liabilities.

##### Value added tax

Russian Value Added Tax ("VAT") at a standard rate of 18% is payable on the difference between output VAT on sales of goods and services and recoverable input VAT charged by suppliers. Output VAT is charged on the earliest of the dates: either the date of the shipment of goods (works, services) or the date of advance payment by the buyer. Input VAT could be recovered when purchased goods (works, services) are accounted for and other necessary requirements provided by the tax legislation are met.

VAT related to sales and purchases is recognised in the consolidated balance sheet on a gross basis and disclosed separately as a current asset and liability.



### 3. Summary of significant accounting policies *continued*

#### **Mineral extraction tax**

Mineral extraction tax on hydrocarbons, including natural gas and crude oil, is due on the basis of quantities of natural resources extracted. Mineral extraction tax for crude oil is determined based on the volume produced per fixed tax rate (RUR419 per ton) adjusted depending on the monthly average market prices of the Urals blend and the RUR/US\$ exchange rate for the preceding month. The ultimate amount of the mineral extraction tax on crude oil depends also on the depletion and geographic location of the oil field. Mineral extraction tax on gas condensate is determined based on a fixed percentage from the value of the extracted mineral resources. Mineral extraction tax is accrued as a tax on production and recorded within cost of sales.

#### **Equity**

##### *Share capital*

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares and options are shown in equity as a deduction, net of tax, from the proceeds. Any excess of the fair value of shares issued or liabilities extinguishment over the par value of shares issued is recorded as share premium.

##### *Other reserves*

Other reserves include reserve on reorganisation of the Group (Note 19), the amount of initial recognition of share options of shareholders (Note 17) and amount related to fair value of directors' options (Note 17).

##### *Non-controlling interests*

Non-controlling interests ('NCI') is the equity in subsidiaries not attributable, directly or indirectly, to the Parent. NCI at the end of the reporting period represents the non-controlling shareholders' portion of the carrying value of the identifiable assets and liabilities of the subsidiary. NCI are presented within equity, separately from the equity, attributable to the Parent's shareholders.

The Group treats transactions with NCI as transactions with equity owners of the Group. For purchases from NCI the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recognized in equity.

#### **Revenue recognition**

Revenue is measured at the fair value of the consideration received or receivable for goods provided or services rendered less any trade discounts, value added tax and similar sales-based taxes after eliminating sales within the Group.

Revenue from sale of crude oil and gas condensate is recognized when the significant risks and rewards of ownership have been transferred to the customer, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and costs incurred or to be incurred in respect of this transaction can be measured reliably. If the Group agrees to transport the goods to a specified location, revenue is recognized when goods are passed to the customer at the designated location.

Other revenue is recognized in accordance with contract terms.

Interest income is accrued on a regular basis by reference to the outstanding principal amount and the applicable effective interest rate, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. Dividend income is recognized where the shareholders' right to receive a dividend payment is established.

#### **Leases**

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

#### **Borrowing costs**

Borrowing costs directly relating to the acquisition, construction or production of a qualifying capital project under construction are capitalized and added to the project cost during construction until such time that the assets are substantially ready for their intended use i.e. when they are capable of production. Where funds are borrowed specifically to finance a project, the amount capitalized represents the actual borrowing costs incurred. Where surplus funds are available for a short term out of money borrowed specifically to finance a project, the income generated from such short-term investments is also capitalized and deducted from the total capitalised borrowing cost. Where the funds used to finance a project form part of general borrowings, the amount capitalized is calculated using a weighted average of rates applicable to relevant general borrowings of the Group during the period. All other borrowing costs are recognized in the profit or loss as finance costs in the period in which they are incurred.

## Financial statements

# Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

### 3. Summary of significant accounting policies *continued*

#### Employee benefits

Wages, salaries, contributions to the Russian Federation state pension and social insurance funds, paid annual leave and sick leave, bonuses are expensed as incurred.

#### Foreign currency translation

Foreign currency transactions are initially recognized in the functional currency at the exchange rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange in effect at the end of the reporting period.

The US dollar ('US\$') is the presentation currency of the Group and the functional currency of the Parent. The functional currency of subsidiaries operating in the Russian Federation is the Russian Rouble ('RUR'). The assets and liabilities of the subsidiaries are translated into the presentation currency of the Group at the rate of exchange ruling at the end of each of the reporting periods. Income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions). All the resulting exchange differences are recorded in other comprehensive income.

The US\$ to RUR exchange rates were 30.37 and 32.20 as at 31 December 2012 and 31 December 2011, respectively and the average rates for the year ended 31 December 2012 and 2011 were 31.07 and 28.74, respectively. The US\$ to GBP exchange rates were 0.62 and 0.65 as at 31 December 2012 and 31 December 2011, respectively and the average rates for the year ended 31 December 2012 and 2011 were 0.63 and 0.62, respectively. The decrease in the US\$ to RUR exchange rate for the year ended 31 December 2012 has resulted in a gain of US\$23,804 thousand in the consolidated statement of comprehensive income and an adjustment of US\$6,061 thousand in Other comprehensive income (refer to Notes 13 and 14).

### 4. Significant accounting judgments, estimates and assumptions

In the application of the Group's accounting policies management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources.

The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

The most significant areas of accounting requiring the use of the Group's management estimates and assumptions relate to oil and gas reserves; useful economic lives and residual values of property, plant and equipment; impairment of tangible assets; provisions for dismantlement; taxation and allowances.

#### Subsoil licenses

The Group conducts operations under exploration and production licenses which require minimum levels of capital expenditure and mineral production, timely payment of taxes, provision of geological data to authorities and other such requirements. The current periods of the Group's licenses expire between June 2014 and June 2017.

Regulatory authorities exercise considerable discretion in issuing and renewing licenses and in monitoring licensees' compliance with license terms. The loss of license would be considered a material adverse event for the Group.

It is management's judgment that each of the three licenses held by the Group will be renewed for the economic lives of the fields which are projected to be up to 2040 (two licenses held by INGA) and 2029 (the license held by Trans-oil). The appraised economic lives of the fields are used as the basis for reserves estimation, depletion calculation and impairment analysis. In making this assessment, management consider that the license held by Trans-oil, which was extended for three years to December 2015, will be further extended. This further extension will be depended on management demonstrating to licensing authorities that associated petroleum gas produced in the course of oil production is being utilised.

#### Useful economic lives of property, plant and equipment and Mineral rights

##### *Oil and gas properties and mineral rights*

The Group's oil and gas properties are depleted over the respective life of the oil and gas fields using the unit-of-production method based on proved developed oil and gas reserves (Note 13). Mineral rights are depleted over the respective life of the oil and gas fields using the unit-of-production method based on proved and probable oil and gas reserves (Note 14).

Reserves are determined using estimates of oil in place, recovery factors and future oil prices.

#### 4. Significant accounting judgments, estimates and assumptions *continued*

When determining the life of the oil and gas field, assumptions that were valid at the time of estimation, may change when new information becomes available. The factors that could affect the estimation of the life of an oil and gas field include the following:

- changes of proved and probable oil and gas reserves;
- differences between actual commodity prices and commodity price assumptions used in the estimation of oil and gas reserves;
- unforeseen operational issues; and
- changes in capital, operating, processing and reclamation costs, discount rates and foreign exchange rates possibly adversely affecting the economic viability of oil and gas reserves.

Any of these changes could affect prospective depletion of mineral rights and oil and gas assets and their carrying value.

#### **Other non-production assets**

Property, plant and equipment other than oil and gas properties are depreciated on a straight-line basis over their useful economic lives (Note 13). Management at the end of each reporting period reviews the appropriateness of the assets useful economic lives and residual values. The review is based on the current condition of the assets, the estimated period during which they will continue to bring economic benefit to the Group and their estimated residual value.

#### *Estimation of oil and gas reserves*

Unit-of-production depreciation, depletion and amortization charges are principally measured based on Group's estimates of proved developed and proved and probable oil and gas reserves. Estimates of proved and probable reserves are also used in determination of impairment charges and reversals. Proved and probable reserves are estimated by independent international reservoir engineers, by reference to available geological and engineering data, and only include volumes for which access to market is assured with reasonable certainty.

Information about the carrying amounts of oil and gas properties and the depreciation, depletion and amortization charged is provided in Notes 13 and 14.

Estimates of oil and gas 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, observation of long-term reservoir performance under producing conditions and changes in economic factors, including product prices, contract terms or development plans. Changes to the Group's estimates of proved and probable reserves affect prospectively the amounts of depreciation, depletion and amortization charged and, consequently, the carrying amounts of mineral rights and oil and gas properties.

Were the estimated proved reserves to differ by 10% from management's estimates, the impact on depletion would be as follows:

Increase/decrease in reserves estimation	Effect on loss before tax for the year ended 31 December	
	2012	2011
+10%	(1,628)	(2,132)
-10%	1,989	2,606

#### *Provision for dismantlement*

The Group has a constructive obligation to recognize a provision for dismantlement for its oil and gas assets (Note 21). The fair values of these obligations are recorded as liabilities on a discounted basis, which is typically at the time when assets are installed. The Group performs analysis and makes estimates in order to determine the probability, timing and amount involved with probable required outflow of resources. Estimating the amounts and timing of such dismantlement costs requires significant judgment. The judgment is based on cost and engineering studies using currently available technology and is based on current environmental regulations. Provision for dismantlement is subject to change because of change in laws and regulations, and their interpretation.

Estimated dismantlement costs, for which the outflow of resources is determined to be probable, are recognized as a provision in the Group's financial statements.

#### *Impairment of non-current assets*

The Group accounts for the impairment of non-current assets in accordance with IAS 36 Impairment of Assets. Under IAS 36, the Group is required to assess the conditions that could cause assets to become impaired and to perform a recoverability test for potentially impaired assets held by the Group. These conditions include whether a significant decrease in the market value of the assets has occurred, whether changes in the Group's business plan for the assets have been made or whether a significant adverse change in the business environment has arisen.

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

#### 4. Significant accounting judgments, estimates and assumptions *continued*

Subsequent to the year end, the Group's shares have been trading at a level which indicate that the market capitalization of the Group is below the carrying value of net assets. This has resulted in a review of the Group's non-current assets (Oil and Gas properties and Mineral Rights) to determine whether they are impaired as at the reporting date.

If there are indications of loss in value, the recoverable amount is estimated. The recoverable amount is the higher of the assets FVLCS, or its VIU. Management consider that an appropriate approach to determining FVLCS is by discounting the post-tax cash flows expected to be generated by the oil and gas assets, net of associated selling costs, taking into account those assumptions that market participants would use in estimating fair value. The VIU is a discounted cash flow calculation based on continued use of the assets in its present condition, excluding potential exploitation of improvement or expansion potential.

The determination of the recoverable amount for both the FVLCS and the VIU involves assumptions as to future hydrocarbon prices, taxes, production volumes, and inflation. The models also use estimates of proved developed for VIU and proved and probable reserves for FVLCS as developed by the independent Reservoir Engineers, DeGolyer and MacNaughton. Estimated cash flows are discounted with a risk adjusted discount rate derived as the weighted average cost of capital ('WACC'). For the Group's businesses the pre-tax nominal discount rate is estimated at 12%.

Based on our estimation of fair value less cost of sale, we do not consider that the Group's non-current assets are impaired as of 31 December 2012.

#### *Assumptions used in developing cash flow forecasts of the Group*

Assumptions	Value
Average crude oil price	USD 101 per barrel
Average effective rate of mineral extraction tax of crude oil	RUB 4,700 per ton
Average effective rate of mineral extraction tax of gas condensate	RUB 590 per ton
Production volume of crude oil over economic life of the fields	438,574 thousand barrels
Production volume of gas condensate over economic life of the fields	13,584 thousand barrels
Inflation	5%

As the FVLCS is sensitive to changes in production volume and to changes in average crude oil price the impairment of oil and gas properties may occur if crude oil initial flow rate per well would be equal to 220 barrels per day or average crude oil price per barrel would be equal to US\$60.

#### *Taxation*

The Group is subject to income and other taxes. Significant judgment is required in determining the provision for income tax and other taxes due to complexity of the tax legislation of the Russian Federation. Deferred tax assets are recognized to the extent that it is probable that it will generate enough taxable profits to utilize deferred income tax recognized. Significant management judgment is required to determine the amount of deferred tax assets recognized, based upon the likely timing and the level of future taxable profits. Management prepares cash flow forecasts to support 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 reservoir engineers. Management also takes into account uncertainties related to future activities of the Group and going concern considerations. When significant uncertainties exist deferred tax assets arising from losses are not recognized even if recoverability of these is supported by cash flow forecasts.

#### *Segment reporting*

Management views the Group as one operating segment and uses reports for the entire Group to make strategic decisions. 98% and 97% of total revenues from external customers in 2012 and 2011 respectively were derived from sales of crude oil and gas condensate. These sales are made to domestic and international oil traders. Although there are a limited number of these traders the Group is not dependent on any one of them as crude oil is widely traded and there are a number of other potential buyers of this commodity. The Group's operations are entirely located in Russia.

#### *Gain on settlement of Makayla Investment Limited liability*

Management views the difference between the carrying value of the liability to Makayla Investments Limited ('Makayla') and the fair value of shares issued for the settlement of the liability is a gain because in effect the transaction was settled with a third party (Note 10).

The Parent's Board of Directors evaluates performance of the entity on the basis of different measures, including total expenses, capital expenditures, operating expenses per barrel and others.



## 5. Adoption of the new and revised standards

At the date of approval of these consolidated financial statements the following accounting standards, amendments and interpretations were issued by the International Accounting Standards Board and IFRS Interpretations Committee in the year ended 31 December 2012, but are not yet effective and therefore have not been applied:

### (i) Not endorsed by the European Union

#### *New standards and interpretations*

- IFRS 9 – Financial Instruments (effective for annual periods beginning on or after 1 January 2015).

#### *Amendments*

- Improvements to IFRSs 2009–2011 (effective for annual periods beginning on or after 1 January 2013).
- Amendments to IFRS 10, IFRS 11 and IFRS 12 (effective for annual periods beginning on or after 1 January 2013) – Transition Guidance.
- Amendments to IFRS 10, IFRS 12 and IAS 27 (effective for annual periods beginning on or after 1 January 2014) – Investment Entities.

### (ii) Endorsed by the European Union

#### *New standards and interpretations*

- IFRS 10 Consolidated Financial Statements.
- IFRS 11 Joint Arrangements.
- IFRS 12 Disclosure of Interests in Other Entities.
- IFRS 13 Fair Value Measurement.
- IAS 27 Separate Financial Statements.
- IAS 28 Investments in Associates and Joint Ventures.

#### *Amendments*

- Amendments to IFRS 7 Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities.
- IFRS 1 – First-time Adoption of International Financial Reporting Standards (effective for annual periods beginning on or after 1 January 2013) – Government Loans.
- Amendments to IAS 32 Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities.
- Amendments to IFRS 1 First-time Adoption of International Financial Reporting Standards – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters.
- Amendments to IAS 12 Income Taxes – Deferred Tax: Recovery of Underlying Assets.
- Amendments to IAS 1 Presentation of Items of Other Comprehensive Income.
- Amendments to IAS 19 Employee Benefits.

Management expects that the adoption of these accounting standards in future periods will not have a material effect on the financial statements of the Group.

## 6. Segment reporting

The management views the operations of the Group as one operating segment. Should the Group diversify its operations the financial reporting will be adjusted to reflect the change.

The Chief operating decision maker evaluates performance of the Group on the basis of different measures, including production volumes, related revenues, capital expenditures, operating expenses per barrel and others.

## 7. Revenue

	Year ended 31 December	
	2012	2011
Revenue from crude oil sales	63,614	37,595
Revenue from gas condensate sales	11,230	—
Other revenue	1,386	1,123
<b>Total revenue</b>	<b>76,230</b>	<b>38,718</b>

Other revenue includes proceeds from third parties for crude oil transportation.

For the years ended 31 December 2012 and 2011, revenue from export sales of crude oil amounted to US\$16,877 thousand and US\$11,120 thousand, respectively.

Revenues from some individual customers in the crude oil and gas condensate segment approximately equaled or exceeded 10% of total Group's segment revenue.

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**7. Revenue** *continued*

Customer	Year ended 31 December	
	2012	2011
Customer 1	20,047	23,794
Customer 2	16,877	11,120
Customer 3	16,831	–
Customer 4	8,779	–
Customer 5	7,774	–
	<b>70,308</b>	<b>34,914</b>

**8. Cost of sales**

	Year ended 31 December	
	2012	2011
Mineral extraction tax	31,816	18,909
Depletion, depreciation and amortization	17,907	23,727
Production services	6,727	2,534
Repairs and maintenance	5,476	1,716
Transportation services	4,541	2,854
Employee benefit expense	5,264	1,855
Reserves evaluation	815	503
Change of inventories	812	(180)
Other	1,458	437
<b>Total cost of sales</b>	<b>74,816</b>	<b>52,355</b>

Depletion, depreciation and amortization expense for the year ended 31 December 2012 has decreased compared to 2011 due to the increase in estimates of proved developed reserves (Note 28). Oil and gas property, plant and equipment are primarily depleted on the unit of production basis over proved developed reserves of the fields concerned. The effect on the unit of production depletion resulting from the increase in estimates of proved developed reserves is somewhat offset by the increase in property, plant and equipment and the increase in hydrocarbons production compared to the corresponding period.

Production services include mainly pump rent, geophysics and electricity. Production services for the year ended 31 December 2012 have increased compared to 2011 primarily due to increased levels of production activity.

**9. Selling and administrative expenses**

	Year ended 31 December	
	2012	2011
<b>Selling expenses</b>		
Oil transportation costs	2,564	1,949
<b>Administrative expenses</b>		
Employee benefit expense	10,345	6,684
Share-based payment compensation (Note 19)	12,035	–
Professional services	4,259	2,787
Taxes, other than income tax	3,288	1,172
Depreciation and amortization	1,855	797
Rent expenses	1,698	217
IT, telecom and other information services	1,039	22
Travel expenses	981	422
Bank charges	414	101
Other	2,003	831
<b>Total selling and administrative expenses</b>	<b>40,481</b>	<b>14,982</b>

Oil transportation costs represent the cost of transferring oil to export customers through the ‘Transneft’ pipeline system.

Professional services include insurance, recruiting expenses, public relations expenses.

Other selling and administrative expenses include primarily inventories, penalties services and security services.

## 9. Selling and administrative expenses *continued*

### **Auditor's remuneration**

During the year the Group obtained the following services from the Parent's auditor and its associates:

	Year ended 31 December	
	2012	2011
Fees payable to the Parent's auditor and its associates for the audit of Company and consolidated financial statements	486	355
Fees payable to the Parent's auditor and its associates for other services:		
– The audit of the Parent's subsidiaries	–	–
– Audit-related assurance services	–	–
– Tax advisory services	16	–
– Tax compliance service	–	–
– Other assurance services – reporting accountant for the IPO	1,922	–

### **Employee benefit expense**

The employee numbers and costs incurred in the reporting years were as follows:

	Year ended 31 December	
	2012	2011
Wages and salaries	13,505	7,569
Social security costs	2,104	970
<b>Total employee costs</b>	<b>15,609</b>	<b>8,539</b>
Share-based payment compensation	12,035	–
Average number of employees (including directors)	183	129

Details of the remuneration of key management personnel are given in Note 24.

### **Directors' remuneration**

	Year ended 31 December	
	2012	2011
Don Wolcott	1,433	462
Tom Reed	883	–
Alexander Chistyakov	615	–
Christopher Clark	576	–
Rolf Stomberg	288	–
Robert Jenkins	273	–
James McBurney	268	–
Joe Mach	240	–
James Gerson	200	–
<b>Total directors' remuneration</b>	<b>4,776</b>	<b>462</b>

### **Directors' interests**

	Year ended 31 December	
Number of ordinary shares in the Parent	2012	2011
Alexander Chistyakov	43,208,393	–
Don Wolcott	29,077,579	762
Tom Reed	7,416,493	–
Christopher Clark	100,000	–
Rolf Stomberg	70,000	–
Robert Jenkins	50,000	–
James McBurney	40,000	–
<b>Total number of ordinary shares in the Parent held by directors</b>	<b>79,962,465</b>	<b>762</b>

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**10. Other income**

On 13 December 2011, Itera Group Limited agreed to sell a receivable from Ruspetro relating to deferred consideration arising from the acquisition of INGA and Trans-oil (the 'Itera debt') to Makayla Investments Limited ('Makayla'), a related party and shareholder of the Parent. As at 31 December 2011, Ruspetro had a related liability including accrued interest of US\$47,453 thousand recorded in its consolidated financial statements.

Makayla negotiated the terms of settlement with Itera and agreed to buy the receivable at an amount lower than the carrying value. Makayla passed on this benefit to Ruspetro by entering into an agreement dated 13 December 2011 with Ruspetro, granting it the option to acquire the debt owing to Makayla by no later than 25 January 2012 for US\$26,171 thousand.

On 18 January 2012, the Parent Company issued 12,707,584 Ordinary shares at £1.34 each to Makayla to acquire this debt for a total fair value of US\$26,171 thousand. Management is of the view that the difference between the carrying value of the liability and the fair value of shares issued is a gain because in effect the transaction was settled with a third party. Accordingly, an amount of US\$21,282 thousand representing the difference between the nominal value of the debt and the fair value of the issued Ordinary shares was recognized as other income.

**11. Finance costs**

	Year ended 31 December	
	2012	2011
Interest expense on borrowings	27,912	30,304
Unwinding discount of put option liabilities (Note 17)	1,058	–
Unwinding discount of provision for dismantlement (Note 21)	682	494
Interest on payables and other current liabilities	163	2,328
<b>Total finance costs</b>	<b>29,815</b>	<b>33,126</b>

For the years ended 31 December 2012 and 2011, borrowing costs amounting to US\$5,220 thousand and US\$3,753 thousand, respectively, were capitalized in Property, plant and equipment and are not included above. The capitalization rate used to determine the amount of borrowing costs eligible for capitalization for both of the years ended 31 December 2012 and 2011 was 10% per annum.

**12. Income tax**

The major components of income tax expense for the years ended 31 December 2012 and 2011 are:

	Year ended 31 December	
	2012	2011
Current income tax expense	–	–
Deferred tax benefit	819	3,602
<b>Total income tax benefit</b>	<b>819</b>	<b>3,602</b>

Income tax for the reporting period is calculated in accordance with the policy disclosed in Note 3.

Profit before taxation for financial reporting purposes is reconciled to the tax calculation for the period as follows:

	Year ended 31 December	
	2012	2011
<b>Loss before income tax</b>	<b>(28,103)</b>	<b>(88,665)</b>
Income tax benefit at applicable tax rate	5,621	17,733
Tax effect of losses for which no deferred income tax asset was recognized	(9,026)	(18,523)
Tax effect for losses utilized	10,333	5,725
Tax effect of share-base payment compensation	(2,407)	–
Tax effect of Sberbank capital share options	(1,129)	–
Tax effect of non-deductible expenses	(2,573)	(1,333)
<b>Income tax (expense)/benefit</b>	<b>819</b>	<b>3,602</b>

Differences between IFRS and statutory taxation regulations in Russia give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rate of 20% for Group companies incorporated in the Russian Federation.



## 12. Income tax *continued*

The movements in deferred tax assets and liabilities relates to the following:

	1 January 2012	Recognized in the Income statement	Exchange differences	31 December 2012
<b>Liabilities</b>				
Property, plant and equipment	(6,427)	289	(265)	(6,403)
Mineral rights and intangible assets	(80,300)	50	(4,809)	(85,059)
Accounts payable	682	277	57	1,016
Accounts receivable	319	203	24	546
<b>Deferred income tax liabilities</b>	<b>(85,726)</b>	<b>819</b>	<b>(4,993)</b>	<b>(89,900)</b>

	1 January 2011	Recognized in the Income statement	Exchange differences	31 December 2011
<b>Liabilities</b>				
Property, plant and equipment	(9,459)	2,565	467	(6,427)
Mineral rights and intangible assets	(85,053)	101	4,652	(80,300)
Accounts payable	580	596	(494)	682
Accounts receivable	(51)	340	30	319
<b>Deferred income tax liabilities</b>	<b>(93,983)</b>	<b>3,602</b>	<b>4,655</b>	<b>(85,726)</b>

The Group did not recognise deferred income tax assets of US\$37,180 thousand and US\$38,935 thousand, in respect of losses that can be carried forward against future taxable income amounting to US\$185,899 thousand and US\$194,675 thousand as at 31 December 2012 and 31 December 2011, respectively. As at 31 December 2012 losses amounting to US\$70,031 thousand, US\$43,020 thousand, US\$28,990 thousand and US\$43,858 thousand expire in 2018, 2019, 2020, 2021 respectively. As at 31 December 2011 losses amounting to US\$76,565 thousand, US\$43,020 thousand, US\$28,990 thousand and US\$46,100 thousand expire in 2018, 2019, 2020, 2021 respectively.

## 13. Property, plant and equipment

	Oil and gas properties	Other property, plant and equipment	Construction in progress	Total
<b>Cost as at 1 January 2012</b>	<b>106,324</b>	<b>2,632</b>	<b>38,432</b>	<b>147,388</b>
Additions	–	–	127,104	127,104
Transfers to fixed assets	97,999	8,332	(106,331)	–
Change in provision for dismantlement (Note 21)	665	–	–	665
Disposals	(926)	(79)	(155)	(1,160)
Effect of translation to presentation currency	8,355	454	2,153	10,962
<b>Cost as at 31 December 2012</b>	<b>212,417</b>	<b>11,339</b>	<b>61,203</b>	<b>284,959</b>
<b>Accumulated depletion and impairment as at 1 January 2012</b>	<b>(34,957)</b>	<b>(1,118)</b>	<b>–</b>	<b>(36,075)</b>
Charge for the period	(17,452)	(1,839)	–	(19,291)
Disposals	426	65	–	491
Effect of translation to presentation currency	(3,194)	(154)	–	(3,348)
<b>Accumulated depletion and impairment as at 31 December 2012</b>	<b>(55,177)</b>	<b>(3,046)</b>	<b>–</b>	<b>(58,223)</b>
<b>Net book value as at 31 December 2012</b>	<b>157,240</b>	<b>8,293</b>	<b>61,203</b>	<b>226,736</b>

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**13. Property, plant and equipment** *continued*

	Oil and gas properties	Other property, plant and equipment	Construction in progress	Total
Cost as at 1 January 2011	78,502	2,877	31,800	113,179
Additions	—	—	40,751	40,751
Transfers to fixed assets	33,091	191	(33,282)	—
Change in provision for dismantlement (Note 21)	1,727	—	—	1,727
Disposals	—	(42)	(281)	(323)
Effect of translation to presentation currency	(6,996)	(394)	(556)	(7,946)
Cost as at 31 December 2011	106,324	2,632	38,432	147,388
Accumulated depletion and impairment as at 1 January 2011	(14,835)	(727)	—	(15,562)
Charge for the period	(23,454)	(551)	—	(24,005)
Disposals	—	24	—	24
Effect of translation to presentation currency	3,332	136	—	3,468
Accumulated depletion and impairment as at 31 December 2011	(34,957)	(1,118)	—	(36,075)
Net book value as at 31 December 2011	71,367	1,514	38,432	111,313

For the year ended 31 December 2012, additions to Construction in progress are primarily made up of additions to production facilities, including wells as well as additions to infrastructure. As at 31 December 2012, the construction in progress balance mainly represents exploration and production wells and oil production infrastructure not finalized (e.g. pads, electricity grids, etc.).

None of the Group's property, plant and equipment was pledged as at the reporting dates.

**14. Mineral rights and other intangibles**

	Mineral rights	Other intangible assets	Total
Cost as at 1 January 2012	402,351	53	402,404
Additions	—	266	266
Effect of translation to presentation currency	24,139	1	24,140
Cost as at 31 December 2012	426,490	320	426,810
Accumulated depletion and impairment as at 1 January 2012	(855)	(36)	(891)
Charge for the period	(452)	(19)	(472)
Effect of translation to presentation currency	102	1	104
Accumulated depletion and impairment as at 31 December 2012	(1,205)	(54)	(1,259)
Net book value as at 1 January 2012	401,496	17	401,513
Net book value as at 31 December 2012	425,285	266	425,551

	Mineral rights	Other intangible assets	Total
Cost as at 1 January 2011	425,032	47	425,079
Additions	—	9	9
Effect of translation to presentation currency	(22,681)	(3)	(22,684)
Cost as at 31 December 2011	402,351	53	402,404
Accumulated depletion and impairment as at 1 January 2011	(423)	(22)	(445)
Charge for the period	(453)	(19)	(472)
Effect of translation to presentation currency	103	1	104
Accumulated depletion and impairment as at 31 December 2011	(855)	(36)	(891)
Net book value as at 1 January 2011	424,609	25	424,634
Net book value as at 31 December 2011	401,469	17	401,513

Intangible assets of the Group are not pledged as security for liabilities and their titles are not restricted.

## 15. Inventories

	31 December	
	2012	2011
Spare parts, consumables and other inventories	1,990	2,022
Crude oil	577	588
<b>Total inventories</b>	<b>2,567</b>	<b>2,610</b>

The Group did not have any obsolete or slow-moving inventory at either of the reporting dates.

## 16. Trade and other receivables

	31 December	
	2012	2011
Trade receivables	1,998	1,702
Other receivables and prepayments	1,849	1,181
VAT recoverable	15,874	2,927
<b>Total trade and other receivables</b>	<b>19,721</b>	<b>5,810</b>

Trade receivables are mainly denominated in US\$ and are not past-due or impaired. Other receivables and prepayments are mostly RUR denominated and relate to counterparties with no history of delays in settlements. VAT recoverable is used to offset against amounts due for mineral extraction tax or recovered in cash. The VAT is recovered within three to six months from its initiation, following a review by the tax authorities.

As at 31 December 2012 and 31 December 2011, the Group did not have any past due or impaired receivables. In determining the recoverability of trade and other receivables the Group considers any change in the credit quality of the receivable from the date credit was initially granted up to the reporting date.

## 17. Options on shares of the Parent

On 2 December 2011, the Parent and LLC 'Sberbank Capital' entered into an option agreement which became effective on 17 January 2012, pursuant to which LLC 'Sberbank Capital' granted the Parent a call option to acquire the 10,362,632 Ordinary shares held by LLC 'Sberbank Capital'. The call option may be exercised once only at any time prior to the day which is 15 months from the date of IPO, at an exercise price equal to the IPO Price (£1.34) per share less 10%.

The fair value of this call option amounted to US\$24 thousand as at 31 December 2012. The fair value of this option was calculated using the Black-Scholes option pricing model and was recognized in these consolidated financial statements as a current asset.

The following table presents the changes of fair value of call option for the year ended 31 December 2012:

	2012
<b>As at 1 January</b>	<b>—</b>
Initial recognition of the option	4,059
Change in fair value of call option	(3,240)
Foreign exchange loss related to call option	(795)
<b>As at 31 December</b>	<b>24</b>

The following assumptions were used in calculating the fair value of this call option:

	Year ended 31 December 2012
Market price	£0.79
Exercise price	£1.206
Expected volatility	37.1%
Expected life	0.3 years
Risk-free interest rate	1.0%
Expected dividend yield	Zero

Expected volatility was determined on the basis of the historic share price volatility of certain peer companies of the Group.

In addition, pursuant to this agreement, LLC 'Sberbank Capital' may put the Ordinary shares issued back to the Parent. The put option may be exercised once only at any time between the second and third anniversary of Admission, which took place on 24 January 2012, at an exercise price equal to the Offer Price (£1.34) less 20%. With respect to the put option, a non-current liability of US\$15,365 thousand has been recorded as at 31 December 2012.

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**17. Options on shares of the Parent** *continued*

The following table presents the changes of value of put option for the year ended 31 December 2012:

	2012
As at 1 January	–
Initial recognition of the option	13,753
Unwinding of discount	1,058
Foreign exchange loss related to put option	554
As at 31 December	15,365

**18. Cash and cash equivalents**

	31 December	
	2012	2011
Cash in bank denominated in US\$	13,402	264
Cash in bank denominated in GBP	10,796	–
Cash in bank denominated in RUR	10,218	1,030
Total cash and cash equivalents	34,416	1,294

Cash balances generally carry no interest. The Group holds its cash with Sberbank (Moody's rating Baa1/D+/P2 (Stable) at 31 December 2012), Bank of America (Moody's rating Baa2/P2 (Negative) at 31 December 2012), Citibank (Moody's rating A3/D+/P2 (Negative) at 31 December 2012) and Bank of Cyprus (Moody's rating Caa1/E/NP (Negative) at 31 December 2012).

**19. Shareholders' equity****Share capital**

	31 December	
	2012	2011
Ordinary share capital	51,226	7

The issued share capital of the Previous Parent as at 31 December 2011 comprised 6,563 fully paid Ordinary shares at a nominal value of US\$1 each.

**Reorganization of the Group and Initial Public Offering ('IPO')**

On 18 January 2012, a new holding structure became effective. The reorganization was effected through a series of shares exchanges as described below.

On 18 January 2012, the existing shareholders of the Previous Parent transferred their shares in the Previous Parent to the Parent in consideration for the issue of 196,890,000 Ordinary shares in the Parent, representing 95% of the issued share capital of the Parent at the date of transfer with nominal value of £0.10 each.

On 19 January 2012, LLC Sberbank Capital transferred its 5% participating interest in Ruspetro Russia to the Parent in consideration for the issue of 10,362,632 Ordinary shares in the Parent, representing approximately 5% of the issued share capital of the Parent at the date of transfer with nominal value of £0.10 each.

Also on 19 January 2012, the Parent completed an IPO on the London Stock Exchange. As a result of the IPO, 126,128,848 Ordinary shares were issued with nominal value of £0.10 each at a price of £1.34 per Ordinary share, including 12,707,584 Ordinary shares to the value of US\$26.2 million in settlement of the debt owing to Makayla, related to the original Itera debt (Note 10). The IPO-related transaction costs amounted to US\$19 million.

The net consideration received amounted to US\$213.7 million.

	Number of shares (pcs.)	Share capital	Share premium	Exchange of shares during group reorganization (included in other reserves)
As at 1 January 2012	6,563	7	49,994	–
Conversion of shares of Previous Parent to shares of Parent	207,246,069	31,818	(49,994)	18,176
Initial Public Offering ('IPO')	126,128,848	19,401	220,506	–
Including to acquire Makayla debt	12,707,584	1,955	24,216	–
As at 31 December 2012	333,381,480	51,226	220,506	18,176

## 19. Shareholders' equity *continued*

### Directors' options

On 17 January 2012, the Parent granted two executive directors the options to acquire 10,362,632 Ordinary shares with an exercise price of £1.34. These options are outstanding as at the balance sheet date. At grant date the options were not subject to service and performance conditions, therefore the value of these options was expensed immediately. In February 2013 the terms of the options were amended by introduction of vesting periods which are as follows: the options vest in three equal installments on 17 January 2013, 17 January 2014 and 17 January 2015. After those dates the options are exercisable any time up to 16 January 2022.

The fair value of the options amounted to US\$12,035 thousand and was calculated using the Trinomial option pricing model and recognized in these consolidated financial statements as a component of equity, with a corresponding amount recognized in selling, general and administrative expenses.

The following assumptions were used in calculating the fair value:

	As at the grant date
Offer price	£1.34
Exercise price	£1.34
Volatility	38.45%
Expected life	10 years
Risk-free interest rate	4.65%
Expected dividend yield	Zero

Expected volatility was determined on the basis of the historic share price volatility of the certain peer companies of the Group.

## 20. Borrowings

	31 December	
	2012	2011
<b>Current</b>		
Sberbank	2,469	45,000
Short-term loans from shareholders of the Parent	19,335	1,197
<b>Total current borrowings</b>	<b>21,804</b>	<b>46,197</b>
	31 December	
	2012	2011
<b>Non-current</b>		
Sberbank	286,671	287,116
Long-term loans from shareholders of the Parent	61,822	73,134
<b>Total long-term borrowings</b>	<b>348,493</b>	<b>360,250</b>

### Sberbank credit facility

The Group has a non-revolving US\$ denominated credit facility from Sberbank which had the following terms at the date of obtaining the credit facility: a limit of US\$250,000 thousand expiring in 2013 with an annual interest rate of 14%. The Parent has pledged all its shares in INGA and Trans-oil as part of the terms of the credit facility.

In 2010, the annual interest rate on the facility was reduced to 9%, increasing to 10.9% from 1 October of that year.

On 25 November 2011, the terms of Sberbank's credit facility were amended whereby, inter alia, repayments of a portion of accrued interest and its principal were deferred until April 2015, and future accrued interest is to be payable half-yearly in May and November of each year. These amendments did not substantially alter the terms of the original credit facility, and were therefore not treated as extinguishment of an existing liability and recognition of a new liability. The present value difference arising from the amendments was recognized over the remaining life of the instrument by adjusting the effective interest rate.

According to the Amended Agreement, on 3 February 2012, Ruspetro paid a portion of the accrued interest, which amounted to US\$27,055 thousand together with US\$17,945 thousand of principal, with further repayments of outstanding interest of US\$10,639 thousand and US\$12,618 thousand made on 25 May 2012 and on 26 November 2012, respectively.

The Group recognized a net foreign exchange gain amounting to US\$19,512 thousand and a net foreign exchange loss amounting to US\$20,439 thousand during the years ended 31 December 2012 and 2011 respectively on the Sberbank credit facility and outstanding accrued interest which is denominated in US\$.



## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**20. Borrowings** *continued***Loans from shareholders of the Parent**

The Group has a number of US\$ denominated loans obtained from the Shareholders of the Parent. All of these loans are unsecured and the interest rate on most of these loans is Libor +10% per annum. Certain loans have matured by 31 December 2012 and are presented as current liabilities as at this date.

On 17 January 2012, the Parent and one of the shareholders agreed that the Parent will issue new Ordinary shares to that shareholder on the date that is 13 months from the date of Admission in full settlement of a loan obtained from the shareholder. On 18 February 2013, a decision was taken not to proceed with the conversion.

**21. Provision for dismantlement**

The provision for dismantlement 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 oil and gas fields which is estimated to be in 21 years from 31 December 2012.

	2012	2011
As at 1 January	5,961	4,155
Additions for new obligations and changes in estimates (Note 13)	665	1,727
Unwinding of discount (Note 11)	682	494
Effect of translation to presentation currency	389	(415)
As at 31 December	7,697	5,961

This provision has been created based on management's internal estimates. Assumptions, based on the current economic environment, have been made which management believe are a reasonable basis upon which to estimate future dismantlement liability. These estimates are reviewed regularly to take into account any material changes to the assumptions. However, actual dismantlement 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 levels. This in turn will depend upon future oil and gas prices and future operating costs which are inherently uncertain.

**22. Trade and other payables**

	31 December	
	2012	2011
Trade payables	34,242	11,649
Other non-financial liabilities	5,479	1,847
Total trade and other payables	39,721	13,496

Trade and other payables are denominated primarily in Russian Roubles.

**23. Capital commitments and other contingencies****Capital commitments**

The Group did not have any non-cancellable capital commitments at 31 December 2012 or 2011.

**License commitments**

The Group's exploration and production licenses require certain operational commitments. These include performance criteria certain of which have not been fully met during 2012. The directors note that breach of license performance conditions has not given rise to any material fines or penalties. Furthermore, management has been undertaking particular actions to meet required license performance criteria. The directors also note that the Group's production program has been inspected by the Russian licensing authorities subsequent to 31 December 2012 and that no material fines or penalties have resulted.

**Liquidity of subsidiary undertakings**

In accordance with the legal framework in the Russian Federation, creditors and tax authorities may initiate bankruptcy procedures against an entity with negative net assets. Ruspetro Russia as at 31 December 2012 reported net liabilities under Russian GAAP. However, no such bankruptcy procedures have been initiated either by the creditors or the tax authorities against them. The directors consider their net liability position to be normal given that the Company is still at a development stage.

### 23. Capital commitments and other contingencies *continued*

#### Operating lease commitments – Group as lessee

The Group has entered into leases for land plots, woodlots and motor vehicles. The land in the Russian Federation on which the Group's production facilities are located is owned by the State. The Group leases land through operating lease agreements, which expire in various years through 2021. These leases have renewal terms at the option of the lessee at lease payments based on market prices at the time of renewal. There are no restrictions placed upon the lessee by entering into these leases.

Future minimum lease payments under non-cancellable operating leases as at 31 December 2012 and 2011 were as follows:

	31 December	
	2012	2011
Within one year	774	245
After one year but not more than five years	907	231
More than five years	22	35
<b>Total capital commitments and other contingencies</b>	<b>1,703</b>	<b>511</b>

#### Operating risks and contingencies

##### *Pledge of shares*

On the opening of its credit facility with Sberbank, the Group provided to Sberbank as collateral its shares in INGA and Trans-oil.

##### *Taxation contingencies*

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities in the Russian Federation.

Recent events within the Russian Federation indicate that the Russian tax authorities may be taking a more assertive position in their interpretation of the prevailing legislation and assessments, and it is possible that transactions and activities which have not been challenged in the past may be challenged in the future. The Supreme Arbitration Court of the Russian Federation has issued guidance to lower courts on reviewing tax cases providing a systemic roadmap for anti-avoidance claims, and it is possible that this will significantly increase the level and frequency of tax authorities' scrutiny. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Amended Russian transfer pricing legislation took effect from 1 January 2012. The new transfer pricing rules are considered to be more technical and, to a certain extent, more aligned with the international transfer pricing principles developed by the Organization for Economic Cooperation and Development ('OECD'). The new legislation provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of controlled transactions (transactions with related parties and some types of transactions with unrelated parties), provided that the transaction price is not arm's length. Management has implemented internal controls to be in compliance with the new transfer pricing legislation.

Management believes the transfer pricing documentation that the Group has prepared, as required by the new Russian tax legislation, provides sufficient evidence to support the Group's tax positions and related tax returns. Given that the implementation of the new Russian transfer pricing rules has not yet been reviewed by tax authorities and courts, the impact of any challenge of the Group's transfer prices cannot be reliably estimated; however, it may be significant to the financial conditions and/or the overall operations of the Group.

The Group includes companies incorporated outside of Russia. Tax liabilities of the Group are determined on the assumptions that these companies are not subject to Russian profits tax because they do not have a permanent establishment in Russia. Russian tax laws do not provide detailed rules on taxation of foreign companies. It is possible that with the evolution of the interpretation of these rules and the changes in the approach of the Russian tax authorities, the non-taxable status of some or all of the foreign companies of the Group in Russia may be challenged. The impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial condition and/or the overall operations of the entity.

Management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount is accrued for in these consolidated financial statements.

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**24. Related party disclosures****Compensation of key management personnel of the Group**

Key management includes executive directors of the Group. The compensation paid or payable to key management for employee services is shown below:

	31 December	
	2012	2011
Share-based payment compensation (Note 19)	12,035	–
Employee remuneration	2,931	772
Benefits in kind	93	–
Non-executive directors fees	1,844	–

Ruspetro had rented office space from a company, in which one of its directors has an interest, for an annual rent and service charge of RUR5,255 thousand/US\$169 thousand (excluding VAT) pursuant to a lease dated 1 January 2010. The lease terminated on 1 May 2012.

All related party transactions are on an arm's length basis and no financial period end balances have arisen as a result of these transactions.

**Loans from related parties**

The Group has a number of loans from shareholders of the Parent with the following balances:

	2012	2011
As at 1 January	74,331	67,133
Interest accrued	7,790	7,198
Principal amount repaid	(630)	–
Interest repaid	(334)	–
As at 31 December	81,157	74,331

The effective interest rates and conversion options of loans received are disclosed in Note 20.

**25. Financial risk management objectives and policies**

The Group's principal financial liabilities comprise accounts payable, bank borrowings and other loans, and obligations under the put option. The main purpose of these financial liabilities and instruments is to manage short-term cash flow and raise finance for the Group's capital expenditure program. The Group has various financial assets such as accounts receivable and cash, which arise directly from its operations.

It is, and has been throughout the years ended 31 December 2012 and 2011, the Group's policy that no speculative trading in derivatives shall be undertaken.

The main risks that could adversely affect the Group's financial assets, liabilities or future cash flows are commodity price risk, interest rate risk, foreign currency risk, liquidity risk and credit risk. Management reviews and agrees policies for managing each of these risks which are summarized below.

The following discussion also includes a sensitivity analysis that is intended to illustrate the sensitivity to changes in market variables on the Group's financial instruments and show the impact on profit or loss and shareholders' equity, where applicable. Financial instruments affected by market risk include bank loans and overdrafts, accounts receivable, accounts payable and accrued liabilities.

The sensitivity has been prepared for the years ended 31 December 2012 and 2011 using the amounts of debt and other financial assets and liabilities held as at those statement of financing position dates.

**Capital risk management**

The Group considers capital to comprise both debt and equity. Total debt comprises long-term and short-term loans and borrowings, as shown in the consolidated statement of financial position. Equity of the Group comprises share capital, share premium, other reserves, retained earnings and non-controlling interests. Equity of the Group was equal to US\$180,447 thousand and US\$(40,737) thousand as at 31 December 2012 and 2011 respectively.

Total debt of the Group was equal to US\$370,297 thousand and US\$406,447 thousand as at 31 December 2012 and 31 December 2011 respectively.

## 25. Financial risk management objectives and policies *continued*

### **Capital risk management** *continued*

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide adequate levels of financing for its current development and production activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, issue new shares, attract new or repay existing loans and borrowings.

The Group manages its capital structure and makes adjustments to it, based on the funds available to the Group, in order to support its construction and production activities. The Group is at the development stage; as such it is dependent on external financing to fund its activities. In order to carry out its planned construction and production activities and pay for administrative costs, the Group will spend its existing capital and raise additional amounts as needed.

There were no changes in the Group's approach to capital management during the period. As at 31 December 2012 and 2011, the Group was not subject to any externally imposed capital requirements (except for described in Note 23). As at 31 December 2012 the Group was not subject to any covenants.

### **Commodity price risk**

The Group sells crude oil and gas condensate under spot contracts on a monthly basis. Sales are centrally managed and during the reporting periods were made principally to domestic customers. The basis for determining the export price is the average monthly price of Brent crude. Changes in commodity prices can affect the Group's financial performance, either positively or negatively and make the Group's revenues subject to volatility in line with fluctuations in crude oil reference prices. Currently the Group does not use commodity derivative instruments to mitigate the risk of crude oil price volatility.

The table below provides the sensitivity of the Group's revenues to a 10% change in price of crude oil.

Commodity price risk	Year ended 31 December	
	2012	2011
Favorable +10%	7,484	3,760
Unfavorable -10%	(7,484)	(3,760)

For the purposes of this analysis, the effect of a variation in crude oil prices on Group's profit is calculated independently of any change in another assumption. In reality, changes in one factor may contribute to changes in another, which may magnify or counteract the sensitivities.

### **Interest rate risk**

The Group is exposed to interest rate risk, however the possible impact of changes in interest rates are not significant since the Group's major borrowings are at fixed interest rates. There is no specific policy in place to hedge against possible adverse changes in interest rates.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's loss before tax through the impact on floating rate borrowings.

Increase/decrease in interest rate	Year ended 31 December	
	Effect on loss before tax	
	2012	2011
+1.0%	809	743
-1.0%	(809)	(743)

### **Foreign currency risk**

The Group has transactional currency exposures. Such exposure arises from borrowing in currencies other than the functional currency. The Group limits foreign currency risk by monitoring changes in exchange rates in the currencies in which its cash and borrowings are denominated.

The following table demonstrates the sensitivity to a reasonably possible change in the RUR:US\$ exchange rate, with all other variables held constant, of the Group's loss before tax due to changes in the carrying value of monetary assets and liabilities.

Increase/decrease in RUR:US\$ exchange rate	Year ended 31 December	
	Effect on loss before tax	
	2012	2011
+15%	(37,714)	(43,319)
-15%	51,025	58,609

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands unless otherwise noted)

**25. Financial risk management objectives and policies** *continued***Liquidity risk**

The Group monitors liquidity risk by monitoring its debt rating and the maturity dates of existing debt.

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2012 and 2011 based on contractual undiscounted payments.

	31 December 2012					Total
	On demand	Less than 1 year	1 to 2 years	2 to 5 years	> 5 years	
Borrowings (including interest)	303	45,171	24,962	376,126	–	446,562
Trade payables	–	34,242	–	–	–	34,242
Other non-current liabilities	–	–	–	17,952	–	17,952
Other current liabilities	–	1,081	–	–	–	1,081
	303	80,494	24,962	394,078	–	499,837

	31 December 2011					Total
	On demand	Less than 1 year	1 to 2 years	2 to 5 years	> 5 years	
Borrowings (including interest)	1,197	69,757	44,638	402,543	–	518,135
Trade payables	–	11,649	–	–	–	11,649
Other current liabilities	–	47,457	–	–	–	47,457
	1,197	128,863	44,638	402,543	–	577,241

**Credit risk**

The Group manages its own exposure to credit risk. The Group trades only with recognized, creditworthy third parties. All external customers undergo a creditworthiness check. The Group performs an ongoing assessment and monitoring of financial position and the risk of default. In addition, receivable balances are monitored on an ongoing basis thus the Group's exposure to bad debts is not significant.

The Company had one major customer in 2012 being an international oil trader and accounting for at least 22% of total sales in 2012. Other sales are made to domestic customers. The Group is not dependent on any of its major customers or any one particular customer as there is a liquid market for crude oil. Analysis of sales to key customers is included into Note 7.

With respect to credit risk arising from the other financial assets of the Group, which comprise cash and cash equivalents, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments. The credit risk on cash is limited because the counterparties are either highly rated banks or banks approved by the management of the Group. Approval is made after certain procedures to assess reliability and creditability of banks are performed.

**Fair values**

The Group has financial instruments carried at fair value only in the 'Level 3' category.

The different levels have been defined as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1).
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2).
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

The following table presents the Group's assets and liabilities that are carried at fair value at 31 December 2012. As at 31 December 2011 the Group had no assets or liabilities measured at fair value through profit or loss.

	31 December 2012
<b>Financial assets</b>	
Other current assets (Note 17)	24



## 25. Financial risk management objectives and policies *continued*

Set out below is a comparison by category of carrying amounts and fair values of all of the Group's financial instruments that are carried at amortized cost in the financial statements:

	Carrying amount		Fair value	
	31 December 2012	31 December 2011	31 December 2012	31 December 2011
<b>Financial assets</b>				
Cash and cash equivalents	34,416	1,294	34,416	1,294
Trade receivables	1,998	1,702	1,998	1,702
<b>Financial liabilities</b>				
Trade payables	32,897	11,649	32,897	11,649
Borrowings	370,297	406,447	370,297	406,447

## 26. Loss per share

### Basic

Basic earnings per share are calculated by dividing the profit attributable to equity holders of the Parent by the weighted average number of Ordinary shares in issue during the period.

For comparability, weighted average number of Ordinary shares in issue for the year ended 31 December 2011 presented as if the Parent was the Group company in 2011. For calculation of number of shares outstanding in 2011 the number of shares issued on reorganization was used.

	Year ended 31 December	
	2012	2011
Loss attributable to equity holders of the Parent/Previous parent	27,284	81,095
Weighted average number of Ordinary shares in issue	315,539,053	196,890,000
Basic loss per share (US\$)	0.09	0.41

### Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of Ordinary shares to assume conversion of all dilutive potential Ordinary shares.

The Parent has incurred a loss from continuing operations for the year ended 31 December 2012 and the effect of considering the exercise of the options on the Parent's shares would be anti-dilutive, that is, it would reduce the loss per share.

## 27. Events after the statement of financial position date

In February 2013, the terms of the options to two executive directors (See Note 19) were amended by introduction of vesting periods which are as follows: the options vest in three equal instalments on 17 January 2013, 17 January 2014 and 17 January 2015. After those dates the options are exercisable anytime up to 16 January 2022. As these modifications decreased the total value of the options and are not beneficial to the employees, management continues to account for these options as if the modification has not occurred.

There have been no other material events after the end of reporting period which require disclosure in these consolidated financial statements.

## 28. Supplementary information (Unaudited)

### Reserve quantity information

For the purposes of evaluation of reserves as of 31 December 2012, 2011 and 2010 the Parent used the oil and gas reserve information prepared by DeGolyer and MacNaughton, independent reservoir engineers, prepared in accordance with Petroleum Resources Management System ('PRMS') definition and classification system.

Developed reserves are expected quantities to be recovered from existing wells and facilities.

Proved reserves are those quantities of petroleum, which, by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under defined economic conditions, operating methods, and government regulations. If deterministic methods are used, the term reasonable certainty is intended to express a high degree of confidence that the quantities will be recovered. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate.

## Financial statements

Notes to the consolidated financial statements *continued*

for the year ended 31 December 2012 (all tabular amounts are in US\$ thousands, except otherwise noted)

**28. Supplementary information (Unaudited) continued**

Probable reserves are those additional reserves which analysis of geoscience and engineering data indicate are less likely to be recovered than proved reserves but more certain to be recovered than possible reserves. It is equally likely that actual remaining quantities recovered will be greater than or less than the sum of the estimated proved plus probable reserves (2P). In this context, when probabilistic methods are used, there should be at least a 50% probability that the actual quantities recovered will equal or exceed the 2P estimate.

Due to the inherent uncertainties and the necessarily limited nature of reservoir data, estimates of reserves are inherently imprecise, require the application of judgment and are subject to change as additional information becomes available.

Management has included within proved reserves significant quantities which the Group expects to produce after the expiry dates of certain of its current production licenses. The Subsoil Law of the Russian Federation states that, upon expiration, a license is subject to renewal at the initiative of the license holder provided that further exploration, appraisal, production or remediation activities are necessary and provided that the license holder has not violated the terms of the license. Since the law applies both to newly issued and old licenses, management believes that licenses will be renewed upon their expiration for the remainder of the economic life of each respective field.

Estimated net proved crude oil reserves for the period ended 31 December 2012 and 31 December 2011, are shown in '000 barrels in the table set out below.

	2012	2011
As at 1 January	172,624	157,785
Revisions of previous estimates	33,618	15,750
Production	(1,654)	(911)
As at 31 December	204,588	172,624

Estimated net proved developed crude oil reserves as at 31 December 2010, 31 December 2011 and 31 December 2012 are shown in the table set out below.

	'000 barrels
31 December 2010	6,306
31 December 2011	11,556
31 December 2012	16,126

Estimated net probable crude oil reserves as at 31 December 2010, 31 December 2011 and 31 December 2012 are shown in the table set out below.

	'000 barrels
31 December 2010	1,279,564
31 December 2011	1,372,028
31 December 2012	1,479,619

Estimated net proved gas reserves as at 31 December 2010, 31 December 2011 and 31 December 2012 are shown in the table set out below.

	Millions of cubic feet
31 December 2010	—
31 December 2011	—
31 December 2012	174,166

Estimated net probable gas reserves as at 31 December 2010, 31 December 2011 and 31 December 2012 are shown in the table set out below.

	Millions of cubic feet
31 December 2010	—
31 December 2011	—
31 December 2012	746,071

# Parent Company financial statements

## Independent auditor's report

### Independent auditors' report to the members of Ruspetro plc

We have audited the parent company financial statements of Ruspetro plc for the period ended 31 December 2012 which comprise the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flow, the significant accounting policies and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006.

### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on financial statements

In our opinion the parent company financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2012 and of its cash flows for the period then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and

- the information given in the Directors' Report for the financial year for which the parent company financial statements are prepared is consistent with the parent company financial statements.

### Emphasis of matter

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of the disclosure made in note 2 to the financial statements concerning the Company's ability to continue as a going concern. This ability is dependent whether the Group can obtain additional financing and an extension of the maturities of the existing debt facilities from the respective lenders and shareholders. This condition, along with the other matters explained in note 2 to the financial statements, indicate the existence of a material uncertainty which may cast significant doubt about the Group's and Company's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Group and Company was unable to continue as a going concern.

### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

### Other matter

We have reported separately on the group financial statements of Ruspetro plc for the year ended 31 December 2012. That report includes an emphasis of matter.



**Kevin Reynard (Senior Statutory Auditor)**  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Aberdeen  
20 March 2013

### Notes:

- a) The maintenance and integrity of the Ruspetro plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## Parent Company financial statements

## Statement of financial position

as at 31 December 2012 (presented in US\$ thousands, except otherwise stated)

	Note	31 December 2012
<b>Assets</b>		
<b>Non-current assets</b>		
Property, plant and equipment		615
Investments in subsidiaries	7	237,882
		<b>238,497</b>
<b>Current assets</b>		
Loans issued to Ruspetro LLC		6,800
Trade and other receivables		306
VAT recoverable		77
Other current assets	8	24
Cash and cash equivalents	9	23,877
		<b>31,084</b>
<b>Total assets</b>		<b>269,581</b>
<b>Shareholders' equity</b>		
Share capital	10	51,226
Share premium	10	220,506
Retained loss		(22,240)
Other reserves		2,341
<b>Total equity</b>		<b>251,833</b>
<b>Liabilities</b>		
<b>Non-current liabilities</b>		
Other non-current liabilities	8	15,365
		<b>15,365</b>
<b>Current liabilities</b>		
Payables to Ruspetro LLC		1,788
Trade and other payables		595
		<b>2,383</b>
<b>Total liabilities</b>		<b>17,748</b>
<b>Total equity and liabilities</b>		<b>269,581</b>

The financial statements on pages 88 to 94 were approved by the Board of Directors on 20 March 2013.

The accompanying notes on pages 90 to 94 are an integral part of these financial statements.



**Don Wolcott**  
Chief executive officer



**Tom Reed**  
Chief financial officer

## Parent Company financial statements

# Statement of changes in equity

for the period from 20 October 2011 to 31 December 2012 (presented in US\$ thousands, except otherwise noted)

	Note	Share capital	Share premium	Retained loss	Other reserves	Total equity
<b>Balance as at 20 October 2011</b>		–	–	–	–	–
Issue of share capital upon incorporation	10	79	–	–	–	79
Loss for the period		–	–	(22,240)	–	(22,240)
Other comprehensive income for the period		–	–	–	–	–
<b>Total comprehensive expense for the period</b>		–	–	(22,240)	–	(22,240)
Issue of share capital		51,147	220,506	–	–	271,653
Share options of shareholders	8	–	–	–	(9,694)	(9,694)
Share-based payment compensation	8	–	–	–	12,035	12,035
<b>Balance as at 31 December 2012</b>		<b>51,226</b>	<b>220,506</b>	<b>(22,240)</b>	<b>2,341</b>	<b>251,833</b>

## Parent Company financial statements

# Statement of cash flows

for the period from 20 October 2011 to 31 December 2012 (presented in US\$ thousands, except otherwise noted)

	Note	Period from 20 October 2011 to 31 December 2012
<b>Cash flows from operating activities</b>		
Loss before income tax		(22,240)
Adjustments for:		
Depreciation, depletion and amortization		96
Foreign exchange gain		2,049
Finance costs		1,058
Change in fair value of call option	8	3,240
Gain on settlement of Makayla debt	5	(21,282)
Other operating expenses	6	21,385
Share-based compensation expense	8	12,035
<b>Operating cash flow before working capital adjustments</b>		<b>(3,659)</b>
Working capital adjustments:		
Change in trade and other receivables		(304)
Change in trade and other payables		1,671
Change in other taxes receivable/payable		(77)
<b>Net cash flows used in operating activities</b>		<b>(2,369)</b>
<b>Cash flows from investing activities</b>		
Purchase of property, plant and equipment		(699)
Investments in Ruspetro LLC	7	(186,833)
<b>Net cash used in investing activities</b>		<b>(187,532)</b>
<b>Cash flows from financing activities</b>		
Proceeds from issue of share capital on incorporation	10	79
Proceeds from issue of share capital on IPO (net of expenses)	10	213,699
<b>Net cash generated from financing activities</b>		<b>213,778</b>
<b>Net increase in cash and cash equivalents</b>		<b>23,877</b>
Cash and cash equivalents at the beginning of the period		–
Cash and cash equivalents at the end of the period	9	23,877



# Parent Company financial statements

## Notes

for the period from 20 October 2011 to 31 December 2012 (presented in US\$ thousands, except otherwise noted)

### 1. Corporate information

The financial statements of Ruspetro plc (the 'Company' or 'Ruspetro') for the 15 months period ended 31 December 2012 were approved by its Board of Directors on 20 March 2013.

The Company was incorporated in the United Kingdom on 20 October 2011 as a public company under the provisions of the Companies Act 2006 of England and Wales. The Company's registered office is 57–59 St James's Street, London, SW1A 1LD England.

On 18 January 2012, the Company became a Company of Ruspetro Group through a series of shares exchanges (see Note 10).

Details of subsidiaries of the Company are as follows:

Company	Business activity	Country of incorporation	Effective Ownership	
			Year of incorporation	31 December 2012
Ruspetro Holding Limited	Holding company	Republic of Cyprus	2007	100%
Ruspetro LLC ('Ruspetro Russia')	Crude oil sale	Russian Federation	2005	100%
INGA	Exploration and production of crude oil	Russian Federation	1998	100%
Trans-oil	Exploration and production of crude oil	Russian Federation	2001	100%

On 19 January 2012, LLC Sberbank Capital transferred its 5% participating interest in Ruspetro Russia to the Company in consideration for a pro rata number of shares in the Company. As of this date, all of the Company's subsidiaries were 100% owned.

### 2. Basis of preparation

The financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted by the European Union. The financial statements are prepared under the historical cost convention, modified for fair values under IFRS.

These financial statements are presented in US dollars ('US\$') and all values are rounded to the nearest thousand unless otherwise indicated.

As permitted by Section 408 of the Companies Act 2006, the Statement of Comprehensive Income of the Parent Company is not presented as part of these financial statements. The loss dealt with in the financial statements of the Company is US\$22,240 thousand.

### Going concern

These financial statements are prepared on a going concern basis, which presumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business in the foreseeable future.

At 31 December 2012, the Company had net current assets of \$28,701 thousand, which included cash in hand of \$23,877 thousand.

Management consider that the continued operational existence of the Company is dependent upon the ability to make further investment in field development of the subsidiaries in order to increase hydrocarbon production and sales. In response to these circumstances, management are in discussions with existing lenders of the subsidiaries with regard to the provision of additional long-term debt financing and the extension of the maturity of the existing long-term loans.

Management consider the additional financing and the maturity extension of existing debt of the subsidiaries will provide sufficient financial resources such that the subsidiaries can further invest in field development with the intention of raising production. Management further consider that the additional cash flows to be generated from production would allow the subsidiaries to service debt, further increase production and fund other activities. In developing their cash flow forecasts, management have a number of significant assumptions. These include assumptions as to future hydrocarbon prices, taxes, production volumes, and inflation and are further discussed in Note 4 of the notes to the consolidated financial statements.

Agreements with the existing lenders as to additional financing and maturity extension have not been entered into as of the date of these financial statements. In the event that such additional financing and maturity extension is not obtained, the subsidiaries may be unable to realize its assets and discharge its liabilities in the normal course of business. These circumstances represent a material uncertainty that may cast significant doubt on the subsidiaries and Company's ability to continue as a going concern.

However, on the basis of the assumptions and cash flow forecasts prepared, management have assumed that the Company will continue to operate within both available and prospective facilities. Accordingly, the Company's financial statements are prepared on the going concern basis and do not include any adjustments that would be required in the event that the loan holders do request repayment and alternative finance is not available.

### 3. Summary of significant accounting policies

#### Investments

Investments in subsidiary undertakings are included in the balance sheet of the Company at cost less any provision for impairment.

#### Impairment of non-financial assets

The Company performs impairment reviews in respect of fixed asset investments whenever events or changes in circumstance indicate that the carrying amount may not be recoverable. An impairment loss is recognized when the recoverable amount of an asset, which is the higher of the asset's net realizable value and its value in use, is less than its carrying amount.

#### Financial instruments

The accounting policy for financial instruments is consistent with the Group accounting policy as presented in the notes to the Group financial statements. The Company's financial risk management policy is consistent with the Group's financial risk management policy outlined in the Group financial statements.

#### Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are subsequently carried at amortized cost using the effective interest method less any provision for impairment.

A provision for impairment is recognized when there is an objective evidence that the Company will not be able to collect all amounts due according to the original terms of the loans and receivables. The amount of provision is the difference between the assets' carrying value and the present value of the estimated future cash flows, discounted at the original effective interest rate. The change in the amount of the loan or receivable is recognized in profit or loss. Interest income is recognized in profit or loss by applying the effective interest rate.

#### Cash and cash equivalents

Cash and cash equivalents in the statement of financial position comprise cash at banks and on hand and short term deposits with an original maturity of three months or less.

For the purpose of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts if any.

#### Borrowings and accounts payable

The Company's financial liabilities are represented by trade and other payables.

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the profit or loss.

#### Impairment of financial assets

The Company assesses at the end of each reporting period whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is an objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

#### Taxes

##### Income tax

The income tax expense comprises current and deferred taxes calculated based on the tax rates that have been enacted or substantively enacted at the end of the reporting period. Current and deferred taxes are charged or credited to profit or loss except where they are attributable to items which are charged or credited directly to equity, in which case the corresponding tax is also taken to equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods.

# Parent Company financial statements

## Notes *continued*

for the period from 20 October 2011 to 31 December 2012 (presented in US\$ thousands, except otherwise noted)

### 3. Summary of significant accounting policies *continued*

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred taxes provide for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred tax arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recognized for all deductible temporary differences and carry forward of unused tax credits and unused tax losses only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences or carry forward can be utilized.

Unrecognized deferred tax assets are reassessed at the end of each reporting period and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are offset when the Company has a legally enforceable right to set off current tax assets and liabilities, when deferred tax balances are referred to the same governmental body (i.e. federal, regional or local) and the same subject of taxation and when the Company intends to perform an offset of its current tax assets and liabilities.

### Equity

#### Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares and options are shown in equity as a deduction, net of tax, from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium.

#### Foreign currency translation

Foreign currency transactions are initially recognized in the functional currency at the exchange rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange in effect at the end of the reporting period.

The US dollar ('US\$') is the presentation currency of the Company. The functional currency of the Company is the pound sterling ('GBP'). The assets and liabilities are translated into the presentation currency at the rate of exchange ruling at the end of each of the reporting period. Income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions). All the resulting exchange differences are recorded in other comprehensive income.

The US\$ to GBP exchange rates were 0.62 and 0.65 as at 31 December 2012 and 31 December 2011, respectively and the average rates for the year ended 31 December 2012 and 2011 were 0.63 and 0.62 respectively.

#### Share option plan

The share option plan, under which the Group has the ability to choose whether to settle it in cash or equity instruments at the discretion of the Board of Directors is accounted for as an equity settled transaction. The fair value of the options granted by the Parent to employees is measured at the grant date and calculated using the Trinomial option pricing model and recognized in the financial statements as a component of equity with a corresponding amount recognised in selling, general and administrative expenses over the time share reward vest to the employee.

Modifications of the terms or conditions of the equity instruments granted in a manner that reduces the total fair value of the share based payment arrangement or is not otherwise beneficial to the employee, are accounted for as services received in consideration for the equity instruments granted as if the modification had not occurred.

### 4. Significant accounting judgments, estimates and assumptions

The significant accounting judgments, estimates and assumptions are consistent with the Group significant accounting judgments, estimates and assumptions as presented in the notes to the Group financial statements.

### 5. Other income

On 13 December 2011, Itera Group Limited agreed to sell a receivable from Ruspetro relating to deferred consideration arising from the acquisition of INGA and Trans-oil (the 'Itera debt') to Makayla Investments Limited ('Makayla'), a related party and shareholder of the Company.

Makayla negotiated the terms of settlement with Itera and agreed to buy the receivable at an amount lower than the carrying value. Makayla passed on this benefit to Ruspetro by entering into an agreement dated 13 December 2011 with Ruspetro, granting it the option to acquire the debt owing to Makayla (valued at US\$47,453 thousand at the date of transaction) by no later than 25 January 2012 for US\$26,171 thousand.

On 18 January 2012, the Company issued 12,707,584 Ordinary shares at £1.34 each to Makayla to acquire this debt for a total value of US\$26,171 thousand. Accordingly an amount of US\$21,282 thousand representing the difference between the nominal value of the debt and the fair value of the issued Ordinary shares was recognized as other income in the accompanying financial statements.

### 6. Other operating expense

Other operating expense include the impairment in the carrying amount of the investment in one of the Group's subsidiaries.

## 7. Investments in subsidiaries

	As at 31 December 2012
Ruspetro LLC	206,138
Ruspetro Holding Limited	31,744
<b>Total investments in subsidiaries</b>	<b>237,882</b>

## 8. Options on shares of the Company

On 2 December 2011, the Company and LLC 'Sberbank Capital' entered into an option agreement which became effective on 17 January 2012, pursuant to which LLC 'Sberbank Capital' granted the Company a call option to acquire the 10,362,632 Ordinary shares held by LLC 'Sberbank Capital'. The call option may be exercised once only at any time prior to the day (which is 15 months from the date of IPO), at an exercise price equal to the IPO Price (£1.34) per share less 10%.

The fair value of this call option amounted to originally valued at US\$4,059 thousand and valued at US\$24 thousand as at 31 December 2012. The fair value of this option was calculated using the Black-Scholes option pricing model and was recognised in these financial statements as a current asset.

The following table presents the changes of fair value of call option for the year ended 31 December 2012:

	Year ended 31 December 2012
<b>As at 1 January</b>	<b>—</b>
Initial recognition of the option	4,059
Change in fair value of call option	(3,240)
Foreign exchange loss related to put option	(795)
<b>As at 31 December</b>	<b>24</b>

The following assumptions were used in calculating the fair value of this call option:

	Year ended 31 December 2012
Market price	GBP0.79
Exercise price	GBP1.206
Expected volatility	37.1%
Expected life	0.3 years
Risk-free interest rate	1.0%
Expected dividend yield	Zero

Expected volatility was determined on the basis of the historic share price volatility of certain peer companies of the Group.

In addition, pursuant to this agreement LLC 'Sberbank Capital' may put the Ordinary shares issued back to the Company. The put option may be exercised once only at any time between the second and third anniversary of Admission, at an exercise price equal to the Offer Price (£1.34) less 20%. With respect to the put option, a liability of US\$15,365 thousand has been recorded as at 31 December 2012.

The following table presents the changes of value of put option for the year ended 31 December 2012:

	Year ended 31 December 2012
<b>As at 1 January</b>	<b>—</b>
Initial recognition of the option	13,753
Unwinding of discount	1,058
Foreign exchange loss related to put option	554
<b>As at 31 December</b>	<b>15,365</b>

## 9. Cash and cash equivalents

	Year ended 31 December 2012
Cash in bank denominated in US\$	13,081
Cash in bank denominated in GBP	10,796
<b>Total Cash and cash equivalents</b>	<b>23,877</b>

Cash balances generally bear no interest. The Company holds its cash with Bank of America (Moody's rating Baa2/P2 (Negative) at 31 December 2012).

# Parent Company financial statements

## Notes *continued*

for the period from 20 October 2011 to 31 December 2012 (presented in US\$ thousands, except otherwise noted)

### 10. Shareholders' equity

#### Share Capital

	Year ended 31 December 2012
Ordinary share capital	51,226

#### Incorporation of the Company

The Company was incorporated on 20 October 2011 as a public company under the provisions of the Companies Act 2006 of England and Wales. Upon incorporation the Company issued 506,640 of its ordinary shares with a nominal value of 10 pence each, for a consideration of US\$79 thousand.

#### Initial Public Offering ('IPO')

On 18 January 2012, a new holding structure became effective. The reorganization was effected through a series of shares exchanges as described below.

On 18 January 2012, the existing shareholders of the Previous Holding Company transferred their shares in the Previous Holding Company to the Company in consideration for the issue of 196,890,000 Ordinary shares in the Company, representing 95% of the issued share capital of the Company at the date of transfer with nominal value of £0.10 each.

On 19 January 2012, LLC Sberbank Capital transferred its 5% participating interest in Ruspetro Russia to the Company in consideration for the issue of 10,362,632 Ordinary shares in the Company, representing approximately 5% of the issued share capital of the Company at the date of transfer with nominal value of £0.10 each.

Also on 19 January 2012, the Company completed an Initial Public Offering (IPO) on the London Stock Exchange. As a result of the IPO, 126,128,848 Ordinary Shares were issued with nominal value of £0.10 each at a price of £1.34 per Ordinary Share, including 12,707,584 Ordinary Shares to the value of \$26.2 million in settlement of the debt owing to Makayla, related to the original Itera debt (Note 5). The IPO related transaction costs amounted to US\$19 million and net proceeds from the IPO amounted to US\$214 million.

	Number of shares (pcs.)	Share capital	Share premium
As at 20 October 2011	—	—	—
Issue of share capital upon incorporation	506,640	79	—
Conversion of shares of Previous Holding Company to shares of Company	206,745,992	31,746	—
Initial Public Offering (IPO)	126,128,848	19,401	220,506
Including to acquire Makayla debt	12,707,584	1,955	24,216
As at 31 December 2012	333,381,480	51,226	220,506

#### Directors' options

On 17 January 2012, the Company granted two executive directors the options to acquire 10,362,632 Ordinary shares with an exercise price of £1.34. These options are outstanding as at the balance sheet date. At grant date the options were not subject to service and performance conditions, therefore the value of these options was expensed immediately. In February 2013 the terms of the options were amended by introduction of vesting periods which are as follows: the options vest in three equal instalments on 17 January 2013, 17 January 2014 and 17 January 2015. After those dates the options are exercisable anytime up to 16 January 2022.

The fair value of the options amounted to US\$12,035 thousand and was calculated using the Trinomial option pricing model and recognized in these financial statements as a component of equity, with a corresponding amount recognized in selling, general and administrative expenses.

The following assumptions were used in calculating the fair value:

	As at the grant date
Offer price	£1.34
Exercise price	£1.34
Volatility	38.45%
Expected life	10 years
Risk-free interest rate	4.65%
Expected dividend yield	Zero

Expected volatility was determined on the basis of the historic share price volatility of the certain peer companies of the Group.



# Shareholder information

## Significant shareholders

Number of shares in issue	333,381,480	28 February 2013
Shareholder:	Holding	% shareholding
Limolines Transport Limited	99,150,000	29.74%
Nervent Limited	46,479,833	13.94%
Schroder Investment Management	29,206,088	8.76%
Makayla Investments Limited	28,819,017	8.64%
Wind River Management Limited	22,860,000	6.86%
Henderson Global Investors	21,913,089	6.57%
Crossmead Holding Limited	12,270,000	3.68%
LLC Sberbank Capital	10,362,632	3.11%

# Contact information

## Annual General Meeting

The Company's Annual General Meeting will be held at 11am on Wednesday, 17 April 2013 at the offices of White & Case LLP, 5 Old Broad Street, London, EC2N 1DW.

## Company website

The Company's annual report and results announcements are available on our website, [www.ruspetro.com](http://www.ruspetro.com).

The website can also be used to access the latest information about the Company, press announcements and future events as they are released as well as who to contact for further information.

## Registrars

For information about the AGM, shareholdings and to report changes in details, shareholders should contact:

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