

Open Joint Stock Company “HC “OZNA” and Subsidiaries

Consolidated Financial Statements
For the Year Ended 31 December 2010

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

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OPEN JOINT STOCK COMPANY "HC "OZNA" AND SUBSIDIARIES

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010

Management is responsible for the preparation of the consolidated financial statements that present fairly the consolidated financial position of the Open Joint Stock Company "HC "OZNA" and its subsidiaries (the "Group") as at 31 December 2010, and the results of its operations, cash flows and changes in shareholders' equity for the year then ended, in compliance with International Financial Reporting Standards ("IFRS").

In preparing the consolidated financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's consolidated financial position and financial performance;
- Making an assessment of the Group's ability to continue as a going concern.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls throughout the Group;
- Maintaining adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the consolidated financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with IFRS;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2010 were approved by management on 8 July 2011:


M.V. Kravtsov
General Director


M.N. Sultanbekova
Finance & Economics Deputy Manager

8 July 2011



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Independent Auditors' Report

To the Board of Directors of Open Joint Stock Company
"Holding Company "OZNA"

We have audited the accompanying consolidated financial statements of Open Joint Stock Company "Holding Company "OZNA" (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2010, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.



ZAO KPMG

8 July 2011

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

	Note	Year ended 31 December 2010	Year ended 31 December 2009
REVENUE	6	5,096,278	5,853,550
COST OF SALES	7	(3,764,844)	(4,425,656)
GROSS PROFIT		1,331,434	1,427,894
Selling, general and administrative expenses	8	(887,320)	(964,732)
Other income		29,462	13,741
Other expenses	11	(69,463)	(26,788)
OPERATING PROFIT		404,113	450,115
Finance income	9	24,874	31,698
Finance costs	10	(20,322)	(61,585)
Loss on disposal of associate		-	(2,958)
Share in (loss)/profit of associate	15	(18)	38
PROFIT BEFORE INCOME TAX		408,647	417,308
INCOME TAX EXPENSE	22	(97,221)	(109,900)
PROFIT FOR THE YEAR		311,426	307,408
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		311,426	307,408
Comprehensive income attributable to:			
Owners of the Company		314,493	311,292
Non-controlling interest		(3,067)	(3,884)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		311,426	307,408
Basic and diluted earnings per share (Russian Rubles)	5	0.558	0.568

The consolidated statement of comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 10-44.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2010

(in thousands of Russian Rubles, unless otherwise stated)

	Note	As at 31 December 2010	As at 31 December 2009
ASSETS			
NON-CURRENT ASSETS:			
Property, plant and equipment	12	829,362	850,357
Goodwill	13	8,799	13,840
Intangible assets	14	9,575	11,156
Investments in associates	15	44	62
Deferred tax assets	22	15,745	13,045
Long-term trade and other receivable	17	3,271	38,789
Other long-term assets		1,175	1,175
Total non-current assets		867,971	928,424
CURRENT ASSETS:			
Inventories	16	1,026,596	1,159,677
Trade and other receivables	17	1,856,871	1,740,761
Value-added tax and other taxes receivable	18	251,778	129,962
Income tax receivable		8,260	14,451
Short-term investments in securities and other financial assets	19	379,312	86,071
Cash and cash equivalents	20	207,154	55,258
Total current assets		3,729,971	3,186,180
TOTAL ASSETS		4,597,942	4,114,604
SHAREHOLDERS' EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY:			
Share capital	21	563,598	563,598
Share premium		254,682	254,682
Retained earnings		1,464,764	1,262,764
Equity attributable to equity holders of the parent		2,283,044	2,081,044
Non-controlling interest		7,909	10,976
Total shareholders' equity		2,290,953	2,092,020
NON-CURRENT LIABILITIES:			
Deferred tax liability	22	53,195	41,871
Total non-current liabilities		53,195	41,871
CURRENT LIABILITIES:			
Non-controlling interest in limited liability companies		47,756	50,362
Trade payables	23	454,287	878,351
Advances received	23	1,290,152	338,260
Taxes payable	24	141,727	215,830
Current income tax		26,595	34,093
Short-term borrowings	25	116,185	213,919
Accruals and other payables	26	177,092	249,898
Total current liabilities		2,253,794	1,980,713
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		4,597,942	4,114,604

The consolidated statement of financial position is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 10-44.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2010

(in thousands of Russian Rubles, unless otherwise stated)

	Attributable to equity holders of the parent				Non-controlling interest	Total shareholder's equity
	Share capital	Share premium	Retained earnings	Total		
Balance as at 1 January 2009	504,369	-	951,427	1,455,796	14,455	1,470,251
Total comprehensive income for the year						
Profit for the year	-	-	311,292	311,292	(3,884)	307,408
Total comprehensive income for the year	-	-	311,292	311,292	(3,884)	307,408
Transactions with owners, recorded directly in equity						
Share issue	59,229	254,682	-	313,911	-	313,911
Changes in ownership interests in subsidiaries that do not result in a loss of control	-	-	45	45	405	450
Total transactions with owners	59,229	254,682	45	313,956	405	314,361
Balance as at 31 December 2009	563,598	254,682	1,262,764	2,081,044	10,976	2,092,020
Total comprehensive income for the year						
Profit for the year	-	-	314,493	314,493	(3,067)	311,426
Total comprehensive income for the year	-	-	314,493	314,493	(3,067)	311,426
Transactions with owners, recorded directly in equity						
Dividends	-	-	(112,493)	(112,493)	-	(112,493)
Total transactions with owners	-	-	(112,493)	(112,493)	-	(112,493)
Balance as at 31 December 2010	563,598	254,682	1,464,764	2,283,044	7,909	2,290,953

The consolidated statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 10-44.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2010

(in thousands of Russian Rubles, unless otherwise stated)

	Note	Year ended 31 December 2010	Year ended 31 December 2009
OPERATING ACTIVITIES:			
Profit before income tax		408,647	417,308
Adjustments for:			
Depreciation of property, plant and equipment		76,137	66,193
Amortisation of intangible assets	14	12,134	14,166
Finance income	9	(24,874)	(31,698)
Finance costs	10	20,322	61,585
Share in loss/(profit) of associates	15	18	(38)
Loss on disposal of investments in associate		-	2,958
Change in provision for doubtful receivables	17	27,245	4,198
Change in provision for slow-moving inventories		11,165	(5,371)
Loss on disposal of property, plant and equipment	12	8,283	4,660
Other adjustments		6,864	19,042
Operating cash flow before working capital changes		545,941	553,003
Decrease in inventories		117,882	218,073
(Increase) in trade and other receivables		(186,551)	(988,802)
(Increase) in value-added tax and other taxes receivable		(121,816)	(25,668)
Increase/(Decrease) in trade payables and advances received		600,746	(141,339)
(Decrease)/Increase in short-term accruals and other payables		(72,806)	120,327
(Decrease)/Increase in taxes payable		(74,103)	70,874
Cash flows from/(used in) operating activities		809,293	(193,532)
Interest paid		(15,776)	(62,193)
Income tax paid		(89,904)	(106,060)
Net cash from/(used in) operating activities		703,613	(361,785)
INVESTING ACTIVITIES:			
Interest received		15,751	28,567
Purchase of property, plant and equipment		(59,391)	(31,581)
Purchase of a group of assets		-	(41,269)
Purchase of investments in subsidiary		-	(18,969)
Purchase of investments in associate		-	(24)
Purchase of intangible assets		(11,890)	(10,519)
Purchase of securities and other financial assets		(381,754)	(80,586)
Proceeds from disposal of securities and other financial assets		95,030	93,380
Net cash used in investing activities		(342,254)	(61,001)
FINANCING ACTIVITIES:			
Proceeds from borrowings		938,810	1,420,130
Repayment of borrowings		(1,035,780)	(1,620,103)
Proceeds from issue of share capital		-	313,911
Dividends paid		(112,493)	-
Other		-	450
Net cash (used in)/from financing activities		(209,463)	114,388
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS		151,896	(308,398)
CASH AND CASH EQUIVALENTS, beginning of year	20	55,258	363,656
CASH AND CASH EQUIVALENTS, end of year	20	207,154	55,258

The consolidated statement of cash flows is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 10-44.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

1. GENERAL INFORMATION

Russian business environment

The Group's operations are primarily located in the Russian Federation. Consequently, the Group is exposed to the economic and financial markets of the Russian Federation which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in the Russian Federation. The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

Organisation and operations

Hereinafter the Group includes the parent company, Open Joint Stock Company “Holding Company “OZNA” (the “Company” or “HC “OZNA”) and its subsidiaries (together referred to as the “Group” or “OZNA Group”).

“HC OZNA” was incorporated in 2008 as a part of reorganization of the Group structure to consolidate the ownership of the Group companies under “HK OZNA”. The Company is located at 5/2 Lenina Street, Ufa, Republic of Bashkortostan, 450077 Russian Federation.

The principal activities of the Group are design, production and installation of equipment and infrastructure for oil and gas industry, as well as related services, including engineering and research works.

The significant subsidiaries are:

Company name	Place of incorporation and operation	Activity	Share of ownership as at:	
			31 December 2010	31 December 2009
LLC “OZNA-Management”	Ufa	Management services	100.00%	100.00%
OJSC “AK OZNA”	Oktyabrski	Production and sales of oil and gas equipment	100.00%	100.00%
LLC “OZNA- Engineering”	Ufa	Production and sale of hi-tech oil and gas equipment	100.00%	100.00%
LLC “OZNA –West Siberia”	Moscow	Sales of oil and gas equipment in North-West region	49.00%	49.00%
CJSC “OZNA-Project”	Nizhnevartovsk	Services in development works for new oil fields	74.80%	74.80%
LLC “Service company “OZNA ”	Ufa, Oktyabrski, Nizhnevartovsk, Surgut	Servicing and installation of equipment	100.00%	100.00%
LLC Hotel “Tonus”	Oktyabrski	Hotel	100.00%	100.00%
LLC “OZNA-Finance”	Oktyabrski	Special purpose entity for issuing bonds	100.00%	100.00%
LLC “Industrial systems”	Surgut	Maintenance of equipment services	100.00%	100.00%

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

LLC “OZNA-Neftegazmash”	Oktyabrski	Rent of real estate	60.74%	60.74%
LLC “OZNA-Metering Systems”	Oktyabrski	Production and sales of measuring stations	100.00%	-

All the above companies are registered in the Russian Federation.

The Group determined that the substance of relationship between the Group and LLC “OZNA-West Siberia”, with a 49% share belonging to the Group, indicated that LLC “OZNA-West Siberia” is controlled by the Group. As a result, this entity has been included into the Group’s consolidated financial statements as at 31 December 2010, because this is special purpose entity.

On 30 April 2010 the Group established a new subsidiary “OZNA – Metering Systems” with a share capital of 200 thousand of Russian Rubles. This company is engaged in production of measuring equipment.

2. BASIS OF PREPARATION

Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (the “IFRS”).

Basis of measurement

The consolidated financial statements of the Group have been prepared on the historical cost basis, except that at the date of transition to IFRS property, plant and equipment was revalued to fair value, as determined by independent appraisers.

Reclassification of comparable data

Certain reclassifications of comparative information in the consolidated financial statements have been made to conform to the current year presentation.

Functional and presentational currency

The national currency of the Russian Federation is the Russian Rouble, which is the Company’s functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in Russian Roubles has been rounded to the nearest thousand.

Changes in accounting policies and presentation

With effect from 1 January 2010, the Group changed its accounting policies in the following areas:

- accounting for business combinations
- accounting for acquisitions of non-controlling interests
- accounting for leases of land

Accounting for business combinations

From 1 January 2010 the Group has applied IFRS 3 *Business Combinations* (2008) in accounting for business combinations. The change in accounting policy has been applied prospectively and has had no material impact on earnings per share.

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that currently are exercisable.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

Acquisitions on or after 1 January 2010

For acquisitions on or after 1 January 2010, the Group measures goodwill at the acquisition date as:

- the fair value of the consideration transferred; plus
the recognised amount of any non-controlling interests in the acquiree; plus, if the business combination is achieved in stages, the fair value of the existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Costs related to the acquisition, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination, are expensed as incurred.

Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in profit or loss.

Accounting for acquisitions of non-controlling interests

From 1 January 2010 the Group has applied IAS 27 *Consolidated and Separate Financial Statements* (2008) in accounting for acquisitions of non-controlling interests. The change in accounting policy has been applied prospectively and has had no impact on earnings per share.

Under the new accounting policy, acquisitions of non-controlling interests are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognised as a result of such transactions. The adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary.

Accounting for leases of land

The amendment to IAS 17 *Leases* regarding the leases of land became effective from 1 January 2010. The amendment removed the earlier exemption which allowed leases of land to be classified as operating leases regardless of the length of the lease term. The amended guidance requires all existing leases of land to be reassessed and reclassified if necessary as finance leases if the finance lease classification criteria are met. At 1 January 2010, the Group reassessed all existing land lease contracts and as a result it was assessed that existing land lease contracts do not qualify as finance lease contracts and therefore, the classification was not changed.

Use of estimates and judgments

In the process of applying 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 recognised 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 of the revision affects both current and future periods.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 *(in thousands of Russian Rubles, unless otherwise stated)*

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Allowance for trade and other receivables

The allowance for trade and other receivables is based on management's evaluation of the volume of the receivables outstanding, past experience and general economic conditions.

Useful lives of assets

The useful economic lives of the Group's assets are determined by management at the time the asset is acquired and are regularly reviewed for appropriateness. The Group defines useful lives of its assets in terms of the assets' expected utility to the Group. This judgment is based on the experience of the Group with similar assets. In determining the useful life of an asset, the Group also considers technical and/or commercial obsolescence, appearing in consequence of changes or improvements of the market situation.

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the entity to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value.

Income tax

The Group is subject to income taxes and other taxes. Significant judgment is required in determining the provision for income taxes due to the complexity of the tax legislation of the Russian Federation. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. The estimation of that probability includes judgments based on the expected performance. Various factors are considered to assess the probability of the future utilisation of deferred tax assets, including past operating results, operational plan, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from that estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 *(in thousands of Russian Rubles, unless otherwise stated)*

Allowance for slow-moving inventory

Allowances for slow-moving inventories are made to reduce excess inventories to their estimated net realizable values, as necessary. A change in customer demand for inventory is the primary indicator for reductions in inventory carrying values. The Group records inventory allowances based on historical experiences with customers, the ability to utilise inventory in other programs, the ability to redistribute inventory back to the suppliers and current and forecasted demand for the inventory.

3. SIGNIFICANT ACCOUNTING POLICIES

Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Group. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

Special purpose entities

The Group has established a number of special purpose entities (“SPE”s) for trading and investment purposes. A SPE is consolidated if, based on an evaluation of the substance of its relationship with the Group and the SPE’s risks and rewards, the Group concludes that it controls the SPE. SPEs controlled by the Group were established under terms that impose strict limitations on the decision-making powers of the SPEs’ management and that result in the Group receiving the majority of the benefits related to the SPEs’ operations and net assets, being exposed to majority of risks incident to the SPE’s activities, and retaining the majority of the residual or ownership risks related to the SPE or its assets.

Loss of control

Upon the loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in profit or loss. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or as an available-for-sale financial asset depending on the level of influence retained.

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 *(in thousands of Russian Rubles, unless otherwise stated)*

Investments in associates (equity accounted investees)

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity. Investments in associates are accounted for using the equity method and are recognised initially at cost. The cost of investment includes transaction costs. The consolidated financial statements include the Group's share of the income and expenses and equity movements of equity accounted investees, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases.

When the Group's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest including any long-term investments is reduced to zero and the recognition of further losses is discontinued, except to the extent that the Group has an obligation or has made payments on behalf of the investee.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Goodwill

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

The consideration transferred for the acquiree is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed, including fair value of assets or liabilities from contingent consideration arrangements but excludes acquisition related costs such as advisory, legal, valuation and similar professional services. Transaction costs incurred for issuing equity instruments are deducted from equity; transaction costs incurred for issuing debt are deducted from its carrying amount and all other transaction costs associated with the acquisition are expensed.

Goodwill is carried at cost less accumulated impairment losses, if any. The Group tests goodwill for impairment at least annually and whenever there are indications that goodwill may be impaired.

Goodwill is allocated to the cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the business combination. Such units or groups of units represent the lowest level at which the Group monitors goodwill and are not larger than an operating segment.

Non-current assets held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification. Non-current assets (and disposal groups) classified as held for sale are measured at the lower of their previous carrying amount and fair value less costs to sell.

OPEN JOINT STOCK COMPANY "HC "OZNA" AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 *(in thousands of Russian Rubles, unless otherwise stated)*

Foreign currencies

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the exchange rates prevailing on the dates of the transactions. At each reporting date, monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates prevailing at the reporting date. Non-monetary items carried at historical cost are translated at the exchange rate prevailing on the date of the transaction.

Exchange differences are recognised in profit or loss in the period in which they arise, except for exchange differences which relate to assets under construction for future productive use, which are included in the cost of those assets, where they are regarded as an adjustment to interest costs on foreign currency borrowings.

Revenue

Components and allocation of consideration

For each single arrangement the Group performs analysis whether it comprises separately identifiable components. In particular, the Group considers:

- whether the component has stand-alone value to the customer; and
- the fair value of the component can be measured reliably.

When a contract includes more than one component, revenue is allocated to components using relative fair values.

Recognition of sale of goods

Revenue from the sale of goods in the course of ordinary activities is measured at the fair value of the consideration received or receivable, net of returns, trade discounts, volume rebates and value-added tax. Revenue is recognised when persuasive evidence exists, usually in the form of an executed sales agreement, that the significant risks and rewards of ownership have been transferred to the customer, recovery of the consideration is probable, the associated costs can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably.

Recognition of provision of services

Revenue from services rendered is recognised in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed.

Supply of goods and installation services under single arrangements

In case two separate and distinct performance obligations are integrated in one contract, revenue is recognized once all significant performance obligations have been met.

In case both supply of goods and installation services are envisaged by a single arrangement:

- revenue from sale of goods and provision of installation services is recognised once installation is complete if installation is a significant part of the contract;
- revenue from sale of goods is recognised at the point of delivery as envisaged by agreement if installation is routine and could be performed by third party. Revenue from installation services is recognized by reference to stage of completion of installation.

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Interest income and dividends

Interest income is accrued on timely basis, by reference to the principal outstanding and at the effective interest rate applicable.

Dividend income from investments is recognised when the shareholders' rights to receive payments have been established.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Transaction costs associated with the issuance of a debt instrument are recorded as a reduction of the debt liability, and are amortised to interest expense over the term of the related debt. In any period in which the debt is redeemed, the unamortised costs relating to the debt being redeemed are expensed.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Property, plant and equipment

The date of initial application of IFRS for the Group was 1 January 2005. The Group elected to utilize exemptions available for first-time adopters under IFRS 1 and recorded property, plant and equipment at fair value. The valuations were performed by an independent appraiser. The difference between the fair value of the property, plant and equipment and its cost in Russian GAAP at 1 January 2005 was recorded as retained earnings at that date, net of effect of deferred tax.

Property, plant and equipment acquired through acquisitions of subsidiaries are recorded at fair value on the date of the acquisition, as determined by an independent appraiser.

Additions to property, plant and equipment are recorded at cost. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs, including overhaul expenses, are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably.

Capitalised cost includes major expenditures for improvements and replacements. Repairs and maintenance expenditures that do not meet the foregoing criteria for capitalisation are charged to profit or loss as incurred.

Depreciation is charged so as to write off the cost or valuation of assets, other than land and property under construction, over their estimated useful lives, using the straight-line method. Land is not depreciated.

The estimated useful lives of the various classes of assets are as follows:

	Useful lives (in years)
Buildings	10-50
Machinery and equipment	3-20
Other assets	3-10

Construction in progress comprises costs directly related to the construction of property, plant and equipment including an appropriate allocation of directly attributable variable overheads that are incurred in construction as well as costs of purchase of other assets that require installation or preparation for their use. Cost includes, for qualifying assets, borrowing costs capitalized in accordance with the Group's

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accounting policy. Depreciation of these assets, on the same basis as for other property assets, commences when the assets are put into operation. Construction in progress is reviewed regularly to determine whether its carrying value is fairly stated and whether appropriate provision for impairment is made.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

Intangible assets, other than goodwill

Intangible assets acquired separately are reported at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged on a straight-line basis over their estimated useful lives. The estimated useful life and amortisation method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets include capitalized development costs, software, licenses and patents and are amortized over their respective useful lives of 3 to 10 years.

Impairment of tangible and intangible assets excluding goodwill

At each reporting date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is an indication that the asset may be impaired.

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

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the first-in-first-out (“FIFO”) method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Financial assets

Investments are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

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Financial assets are classified into the following specified categories:

- * Available-for-sale ("AFS") financial assets; and
- * Loans and receivables.

The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest rate basis for debt instruments other than those financial assets designated as at FVTPL.

AFS financial assets

Listed shares and listed redeemable notes held by the Group that are traded in an active market are classified as being AFS and are stated at fair value. Fair value of AFS is determined as follows:

- * The fair value of AFS financial assets with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices; and
- * The fair value of other AFS financial assets are determined in accordance with generally accepted pricing model based on discounted cash flow analysis using prices from observable current market transactions.

Gains and losses arising from changes in fair value are recognised directly in equity in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest rate method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the investments revaluation reserve is included in profit or loss for the period.

Dividends on AFS equity instruments are recognised in profit or loss when the Group's right to receive payments is established.

The fair value of AFS monetary assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the reporting date. The change in fair value attributable to translation differences that result from a change in amortised cost of the asset is recognised in profit or loss, and other changes are recognised in equity.

Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances, cash deposits and highly liquid investments with maturities of three months or less, those are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

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Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each reporting date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognised directly in equity.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Financial liabilities and equity instruments issued by the Group

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the asset of an entity deducting all of its liabilities. Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- * The amount of the obligation under the contract, as determined in accordance with *IAS 37 Provisions, Contingent Liabilities and Contingent Assets*; and
- * The amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies set out above.

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Financial liabilities

Financial liabilities can be classified as financial liabilities at FVTPL or as other financial liabilities.

Other financial liabilities

Other financial liabilities, including loans and borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Employee benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans, including Russia's State pension fund, are recognised as an employee benefit expense in profit or loss in the periods during which services are rendered by employees. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available. Contributions to a defined contribution plan that are due more than 12 months after the end of the period in which the employees render the service are discounted to their present value.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

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Current income tax

Current income tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the profit or loss because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted at the reporting date.

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary differences arise from goodwill or from initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred taxes are recognised as an expense or income in profit or loss, except when they relate to items credited or debited directly to other comprehensive income or equity, in which case the tax is also recognised in other comprehensive income or directly in equity, or they arise from the initial accounting for a business combination. In case of a business combination, the tax effect is taken into account in calculating goodwill or determining the excess of the acquirer's interest in the net fair value of the acquirer's identifiable assets, liabilities and contingent liabilities over the cost.

Dividends declared

Dividends paid to shareholders are determined by the board of directors and declared and approved at the annual shareholders' meeting.

Dividends and related taxation thereon are recognised as a liability in the period in which they have been declared and become legally payable.

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Accumulated profits distributable by the Group's entities are based on the amounts available for distribution in accordance with the applicable legislation of the jurisdictions where each entity operates and as reflected in the statutory financial statements of the individual entities of the Group based on calendar reporting years (years ending 31 December). These amounts may differ significantly from the amounts calculated on the basis of IFRSs.

Related parties

Related parties are those counterparties that represent:

- (a) Enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under the common control of, the Group. This includes, but is not limited to, holding companies, subsidiaries and fellow subsidiaries;
- (b) Enterprises over which the Group has significant influence and which are neither subsidiaries nor joint ventures of the investor. This includes associates;
- (c) Individuals owning, directly or indirectly, an interest in the voting power of the Group, which gives them significant influence over the Group, and anyone expected to influence, or be influenced by, that person in their dealings with the Group;
- (d) Key management personnel, namely persons with authority and responsibility for planning, directing and controlling the activities of the Group, including directors and officers of the Group and close family members of such individuals; and
- (e) Enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in (c) or (d) or over which such a person is able to exercise significant influence. This includes enterprises owned by directors, partners or shareholders of the Group and enterprises that have a member of key management in common with the Group.

In considering each possible related-party relationship, attention is paid to the substance of the relationship, and not merely the legal form.

4. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2010, and have not been applied in preparing these consolidated financial statements. The assessment of the potential impact of these pronouncements on the Group's operations is given below. The Group plans to adopt some of these pronouncements when they become effective.

IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments (issued in November 2009, effective for annual periods beginning on or after 1 July 2010). This IFRIC clarifies the accounting when an entity settles its debt by issuing its own equity instruments. A gain or loss is recognized in profit or loss based on the fair value of the equity instruments compared to the carrying amount of the debt. The Group does not expect the interpretation to have any material effect on its financial statements.

Classification of Rights Issues - Amendment to IAS 32, Financial Instruments: Presentation (issued in October 2009; effective for annual periods beginning on or after 1 February 2010). The amendment exempts certain rights issues of shares with proceeds denominated in foreign currencies from classification as financial derivatives. The Group does not expect the amendment to have any material effect on its financial statements.

Amendment to IAS 24, Related Party Disclosures (issued in November 2009 and effective for annual periods beginning on or after 1 January 2011). IAS 24 was revised in 2009 by: (a) simplifying the definition of a related party, clarifying its intended meaning and eliminating inconsistencies; and by (b) providing a partial exemption from the disclosure requirements for government-related entities. The Group does not expect the interpretation to have any material effect on its financial statements.

IFRS 9, Financial Instruments, Classification and Measurement. IFRS 9 Financial Instruments will be effective for annual periods beginning on or after 1 January 2013. The new standard is to be

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issued in phases and is intended ultimately to replace International Financial Reporting Standard IAS 39 Financial Instruments: Recognition and Measurement. The first phase of IFRS 9 was issued in November 2009 and relates to the classification and measurement of financial assets. The second phase regarding classification and measurement of financial liabilities was published in October 2010. The remaining parts of the standard are expected to be issued during the first half of 2011. The Group recognises that the new standard introduces many changes to the accounting for financial instruments and is likely to have a significant impact on Group's consolidated financial statements. The impact of these changes will be analysed during the course of the project as further phases of the standard are issued. The Group does not intend to adopt this standard early.

Improvements to International Financial Reporting Standards (issued in May 2010). Amendments IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34 and IFRIC 13 issued by the IASB in 2010 are generally applicable for annual periods beginning after 1 January 2011. The Group is currently assessing the effect on those amendments on future financial statements.

Prepayments of a Minimum Funding Requirement – Amendment to IFRIC 14 (effective for annual periods beginning on or after 1 January 2011). This amendment will have a limited impact as it applies only to companies that are required to make minimum funding contributions to a defined benefit pension plan. It removes an unintended consequence of IFRIC 14 related to voluntary pension prepayment when there is a minimum funding requirement. The Group does not expect the amendments to have any material effect on its financial statements.

Limited exemption from comparative IFRS 7 disclosures for first-time adopters - Amendment to IFRS 1 (effective for annual periods beginning on or after 1 July 2010). Existing IFRS preparers were granted relief from presenting comparative information for the new disclosures required by the March 2009 amendments to IFRS 7, *Financial Instruments: Disclosures*. This amendment to IFRS 1 provides first-time adopters with the same transition provisions as included in the amendment to IFRS 7. The revised standard is not relevant to the Group's operations.

Disclosures—Transfers of Financial Assets – Amendment to IFRS 7 (issued in October 2010 and effective for annual periods beginning on or after 1 July 2011). The amendment requires additional disclosures in respect of risk exposures arising from transferred financial assets. The amendment includes a requirement to disclose by class of asset the nature, carrying amount and a description of the risks and rewards of financial assets that have been transferred to another party yet remain on the entity's balance sheet. Disclosures are also required to enable a user to understand the amount of any associated liabilities, and the relationship between the financial assets and associated liabilities. Where financial assets have been derecognised but the entity is still exposed to certain risks and rewards associated with the transferred asset, additional disclosure is required to enable the effects of those risks to be understood. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

Recovery of Underlying Assets – Amendment to IAS 12 (issued in December 2010 and effective for annual periods beginning on or after 1 January 2012). The amendment introduced a rebuttable presumption that an investment property carried at fair value is recovered entirely through sale. This presumption is rebutted if the investment property is held within a business model whose objective is to consume substantial all of the economic benefits embodied in the investment property over time, rather than through sale. SIC-21, *Income Taxes – Recovery of Revalued Non-Depreciable Assets*, which addresses similar issues involving non-depreciable assets measured using the revaluation model in IAS 16, *Property, Plant and Equipment*, was incorporated into IAS 12 after excluding from its scope investment properties measured at fair value. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters – Amendments to IFRS 1 (issued in December 2010 and effective for annual periods beginning on or after 1 July 2011). The amendment regarding severe hyperinflation creates an additional exemption when an entity that has been subject to severe hyperinflation resumes presenting or presents for the first time, financial statements in accordance with IFRS. The exemption allows an entity to elect to measure certain assets and liabilities at fair value; and to use that fair value as the deemed cost in the opening IFRS

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statement of financial position. The IASB has also amended IFRS 1 to eliminate references to fixed dates for one exception and one exemption, both dealing with financial assets and liabilities. The first change requires first-time adopters to apply the derecognition requirements of IFRS prospectively from the date of transition, rather than from 1 January 2004. The second amendment relates to financial assets or liabilities where the fair value is established through valuation techniques at initial recognition and allows the guidance to be applied prospectively from the date of transition to IFRS rather than from 25 October 2002 or 1 January 2004. This means that a first-time adopter may not need to determine the fair value of certain financial assets and liabilities at initial recognition for periods prior to the date of transition. IFRS 9 has also been amended to reflect these changes. The revised standard is not relevant to the Group's operations.

New standards issued in May 2011 that are effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted.

IFRS 10 Consolidated financial statements. The standard replaces all of the guidance on control and consolidation in IAS 27 “Consolidated and separate financial statements” and SIC-12 “Consolidation special purpose entities”. IFRS 10 changes the definition of control so that the same criteria are applied to all entities to determine control. This definition is supported by extensive application guidance.

IFRS 11 Joint arrangements. The standard replaces IAS 31 “Interests in Joint Ventures” and SIC-13 “Jointly Controlled Entities – Non-Monetary Contributions by Ventures”. Changes in the definitions have reduced the “types” of joint arrangements to two: joint operations and joint ventures. The existing policy choice of proportionate consolidation for jointly controlled entities has been eliminated. Equity accounting is mandatory for participants in joint ventures.

IFRS 12 Disclosure of interest in other entities. The standard applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity; it replaces the disclosure requirements currently found in IAS 28 “Investments in associates”. IFRS 12 requires entities to disclose information that helps financial statement readers to evaluate the nature, risks and financial effects associated with the entity's interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities. To meet this objective, there is a new requirement to disclose significant judgments and assumptions in determining whether an entity controls, jointly controls or significantly influences its interests in other entities.

As a consequence of above changes IAS 27 is renamed “Separate financial statements”. It continues to be a standard dealing solely with separate financial statements. The existing guidance for separate financial statements is unchanged.

IFRS 13 Fair value measurement. The standard aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs.

The Group is currently assessing the impact of the new standards on the consolidated financial statements.

5. EARNINGS PER SHARE

Basic and diluted earnings per share for the years ended 31 December 2010 and 2009 have been calculated on the basis of the profit for the year and the weighted average number of ordinary shares in issue during the year.

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The calculation of basic and fully diluted earnings per share is based on the following information:

	Year ended	
	31 December 2010	31 December 2009
Profit for the year attributable to equity holders of the parent	314,493	311,292
Weighted average number of shares (in shares)	563,597,774	548,019,865
Basic and diluted earnings per share (Russian Rubles)	0.558	0.568

6. REVENUE

	Year ended	
	31 December 2010	31 December 2009
By product		
Measuring stations	1,714,653	1,620,134
Module-type installations	678,996	1,358,821
Oil, oil products, water and gas fiscal metering units	617,563	708,003
Blocks	521,082	422,968
Bush block pump stations	465,374	891,422
Spare parts	392,360	298,245
Building and assembly jobs	197,103	-
Maintenance of equipment	165,482	212,357
Concurrent engineering	126,223	119,166
Setup and commissioning services	83,502	57,596
Overhaul services	42,549	18,176
Hotel services	25,324	27,172
Other products	66,067	119,490
Total	5,096,278	5,853,550

The Group considers that single arrangements for supply of goods and provision of installation services include two separately identifiable components. This is because the installation is normally is routine and can be performed by the customer or another party.

Revenue from the goods sale component is recognized at the moment of transfer of risks and rewards to buyers in accordance with provisions of IAS 18 Revenue for sale of goods. Revenue from installation component is recognized by reference to stage of completion in accordance with provisions of IAS 18 Revenue for services.

	Year ended	
	31 December 2010	31 December 2009
By geographical location of the customers		
Russian Federation	5,062,725	5,743,901
Kazakhstan	-	106,929
Other	33,553	2,720
Total	5,096,278	5,853,550

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The following summary shows revenue from top five customers of the Group:

Customer location		% of total turnover, 2010	Revenue	
			2010	2009
OJSC "NK Rosneft"	Moscow	24%	1,247,210	2,212,236
OJSC "Surgutneftegaz"	Surgut	16%	804,287	968,321
OJSC "AK Transneft"	Moscow	11%	577,056	542,054
OJSC "Gazprom"	Moscow	9%	439,939	241,510
OJSC "LUKOIL"	Moscow	8%	419,947	130,587
OJSC "TNK-BP Holding"	Tyumen	7%	357,315	418,659
Total		75%	3,845,754	4,513,367

7. COST OF SALES

	Year ended	
	31 December 2010	31 December 2009
Cost of production		
Raw materials	2,384,522	3,429,377
Payroll and contributions to social funds	740,981	714,269
Subcontractors	225,616	103,955
Utilities	43,904	39,963
Depreciation of property, plant and equipment	47,606	43,038
Repairs and maintenance	19,857	16,807
Other	119,248	115,331
Change in inventories	86,561	(66,712)
Cost of goods resold	96,549	29,628
Total	3,764,844	4,425,656

8. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended	
	31 December 2010	31 December 2009
Payroll and contributions to social funds	513,839	615,424
Transportation expenses	98,361	70,969
Consulting, certification, advertising expenses and audit fee	46,780	43,176
Materials	32,706	39,284
Business trip expenses	30,594	32,232
Rent (Note 29)	24,641	31,375
Depreciation of property, plant and equipment	24,497	25,098
Security, repairs and maintenance	17,874	22,016
Taxes other than income tax	13,825	16,461
Insurance expenses	9,033	9,146
Utilities	9,026	8,228
Bank services	5,478	8,916
Other expenses	60,666	42,407
Total	887,320	964,732

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

9. FINANCE INCOME

	Year ended	
	31 December 2010	31 December 2009
Interest income	18,135	19,686
Net foreign exchange gain	-	8,302
Unwinding of discount on promissory notes	4,133	-
Income from non-controlling interest in limited liability companies	2,606	-
Other	-	3,710
Total	24,874	31,698

10. FINANCE COSTS

	Year ended	
	31 December 2010	31 December 2009
Interest expenses	15,016	61,585
Net foreign exchange loss	5,306	-
Total	20,322	61,585

11. OTHER EXPENSES

	Year ended	
	31 December 2010	31 December 2009
Change in allowances for doubtful receivables	27,245	4,198
Impairment of goodwill (Note 13)	5,041	-
Donations and social expenses	5,084	4,981
Other	32,093	17,609
Total	69,463	26,788

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

12. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings	Machinery and equipment	Other assets	Total
Cost				
As at 1 January 2009	459,929	346,996	105,710	912,635
Additions	656	25,633	7,261	33,550
Acquired on acquisition of subsidiary and group of assets	141,270	2,622	180	144,072
Disposals	(2,008)	(7,941)	(1,060)	(11,009)
As at 31 December 2009	599,847	367,310	112,091	1,079,248
Additions	6,687	44,081	8,623	59,391
Disposals	(4,929)	(8,408)	(1,344)	(14,681)
As at 31 December 2010	601,605	402,983	119,370	1,123,958
Accumulated depreciation				
As at 1 January 2009	(28,843)	(124,699)	(13,562)	(167,104)
Charge for the year	(15,351)	(42,461)	(10,324)	(68,136)
Disposals	7	5,851	491	6,349
As at 31 December 2009	(44,187)	(161,309)	(23,395)	(228,891)
Charge for the year	(16,730)	(43,130)	(12,243)	(72,103)
Disposals	295	5,442	661	6,398
As at 31 December 2010	(60,622)	(198,997)	(34,977)	(294,596)
As at 31 December 2009	555,660	206,001	88,696	850,357
As at 31 December 2010	540,983	203,986	84,393	829,362

As at 31 December 2010, no property, plant and equipment have been pledged as security for certain borrowings of the Group (2009: 85,287 thousand Russian Rubles).

13. GOODWILL

	31 December 2010	31 December 2009
Balance as at 1 January	13,840	8,799
Acquisition of LLC “Industrial systems”	-	5,041
Impairment loss recognized in the year (LLC “Industrial systems”)	(5,041)	-
Balance as at 31 December	8,799	13,840
Carrying amount	8,799	13,840

Goodwill was allocated to two cash generating units: CJSC “OZNA-Project” and LLC “Industrial Systems”. The Group performed impairment test of goodwill as at 31 December 2010.

The recoverable amount of goodwill of CJSC “OZNA-Project” was determined as not impaired.

The Group assessed the recoverable amount of goodwill associated with LLC “Industrial systems” and determined that goodwill was impaired by 5,041 thousand Russian Rubles.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

14. INTANGIBLE ASSETS

	<u>Licence and patents</u>	<u>Software</u>	<u>Total</u>
Cost			
As at 1 January 2009	3,929	21,331	25,260
Additions	5,402	5,117	10,519
Additions as a result of business combinations	-	48	48
Disposals	-	(378)	(378)
As at 31 December 2009	9,331	26,118	35,449
Additions	4,206	7,684	11,890
Disposals	(127)	(1,336)	(1,463)
As at 31 December 2010	13,410	32,466	45,876
Accumulated amortisation			
As at 1 January 2009	(1,695)	(8,432)	(10,127)
Charge for the year	(3,072)	(11,094)	(14,166)
As at 31 December 2009	(4,767)	(19,526)	(24,293)
Charge for the year	(5,667)	(6,467)	(12,134)
Disposals	11	115	126
As at 31 December 2010	(10,423)	(25,878)	(36,301)
Carrying amount			
As at 31 December 2009	<u>4,564</u>	<u>6,592</u>	<u>11,156</u>
As at 31 December 2010	<u>2,987</u>	<u>6,588</u>	<u>9,575</u>

15. INVESTMENTS IN ASSOCIATES

	<u>LCC “OZNA Imstalcon”</u>	<u>LLC “OZNA- Neftegazmash”</u>	<u>CJSC “TD OZNA”</u>	<u>Total</u>
Carrying value as at 1 January 2009	2,958	36,093	-	39,051
Acquisition of associate	-	-	24	24
Disposal of investments in associate	(2,958)	(36,093)	-	(39,051)
Group's share in profit for the year	-	-	38	38
Carrying value as at 31 December 2009	-	-	62	62
Group's share of loss for the year	-	-	(18)	(18)
Carrying value as at 31 December 2010	-	-	44	44

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

Details of the Group's significant associate as at 31 December 2010 is as follows:

Name of associate	Country	Date of acquisition	Principal activity	Ownership, %	
				31 December 2010	31 December 2009
CJSC “TD OZNA”	Russian Federation	29 January 2009	Wholesale trade	24%	24%

Summarised financial information in respect of CJSC “TD OZNA” is presented below:

	31 December 2010	31 December 2009
Total assets	144	195
Total liabilities	70	37
Net assets	74	158
Group's share of associate's net assets	18	38

16. INVENTORIES

	31 December 2010	31 December 2009
Raw materials, including:		
Components	229,536	274,980
Metal	92,187	83,869
Electronic parts	92,379	52,623
Construction materials	12,013	2,147
Armature parts	9,101	22,647
Other	60,135	39,434
Less: allowance for slow-moving inventories	(3,679)	(1,026)
Total raw materials	491,672	474,674
Work in progress	332,145	257,870
Less: allowance for slow-moving WIP	(4,347)	-
Total work in progress	327,798	257,870
Finished goods	149,183	235,346
Goods in transit	57,677	183,980
Goods for resale	266	7,807
Total	1,026,596	1,159,677

As at 31 December 2010, raw materials and finished goods with a carrying amount of 203,964 thousand Russian Rubles (2009: 228,078 thousand Russian Rubles) were pledged as security for short term borrowings granted to the Group by OJSC “Sberbank RF” (Note 25). As at 31 December 2010 no draw downs were made from these credit lines.

As at 31 December 2010, raw materials and finished goods with a carrying amount of 5,062 thousand Russian Rubles (2009: 50,351 thousand Russian Rubles) were pledged as security for bank guarantees to the Group customers (Note 25).

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

17. TRADE AND OTHER RECEIVABLES

	31 December 2010	31 December 2009
Long-term trade and other receivables	3,271	38,789
Trade accounts receivable from third parties	1,180,888	1,420,191
Trade accounts receivable from related parties	23,964	11,473
Advances paid to third parties	637,394	273,601
Advances paid to related parties	3,593	2,904
Other receivables and prepayments	30,376	24,867
Other receivables from related parties	21,560	21,960
Less: allowance for doubtful receivables	(40,904)	(14,235)
Total	1,860,142	1,779,550

Long term trade receivables are trade receivables from CJSC “Vankorneft”, major customer of the Group. Effective sales contracts with CJSC “Vankorneft” contain a provision that 5% of sales price of equipment is settled upon the fulfillment of start-up works required to put equipment in use. Thus long term trade receivables represent 5% of the sales price of equipment sold to CJSC “Vankorneft” in 2010 that is going to be put in use in 2012.

Before accepting any new customer, the Group uses an internal credit system to assess the potential customer's credit quality. Of the trade receivables balance at the end of the year, the Group's five largest customers represent 51.5% (2009: 74.3%) of the outstanding balance.

Included in the Group's receivable balance are debtors with a carrying amount of 169,501 thousand Russian Rubles (2009: 254,257 thousand Russian Rubles) which are past due at the respective reporting date and which the Group still considers recoverable (i.e. not impaired). The Group does not hold any collateral over these outstanding balances.

Ageing of past due but not impaired trade and other receivables:

	31 December 2010	31 December 2009
less than 30 days	86,838	17,745
30-90 days	38,443	53,922
90-180 days	6,294	161,732
180-360 days	4,696	16,459
Thereafter	33,230	4,399
Total	169,501	254,257

Movement in allowance for doubtful trade and other receivables:

	31 December 2010	31 December 2009
Balance at the beginning of the year	14,235	16,837
Recognised in profit or loss	30,839	4,198
Amounts written-off as uncollected	(576)	(6,800)
Amount recovered during the year	(3,594)	-
Balance at the end of the year	40,904	14,235

OPEN JOINT STOCK COMPANY "HC "OZNA" AND SUBSIDIARIES

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Ageing of impaired trade and other receivables:

	31 December 2010	31 December 2009
less than 30 days	17,190	-
30-90 days	-	-
90-180 days	-	-
180-360 days	-	4,409
Thereafter	23,714	9,826
Total	40,904	14,235

18. VALUE-ADDED TAX AND OTHER TAXES RECEIVABLE

	31 December 2010	31 December 2009
VAT recoverable	247,793	127,570
Other taxes receivable	3,985	2,392
Total	251,778	129,962

19. SHORT-TERM INVESTMENTS IN SECURITIES AND OTHER FINANCIAL ASSETS

	31 December 2010	31 December 2009
Redeemable notes from third parties	963	38,361
	963	38,361
Bank deposits, in RUB	170,000	-
Bank deposits, in EURO	201,665	-
Loans given to third parties	3,063	10,080
Loans given to related parties	3,621	37,630
Total	379,312	86,071

Short term bank deposits as at 31 December 2010 mature in 6 months since date of placement. Interest rate on deposits denominated in EURO is 3.75%; in Russian Roubles – 6.75%.

Amount of loans given to related parties are represented mainly by loan given to entity under control of shareholders. Interest rate on loan is 12% per annum.

20. CASH AND CASH EQUIVALENTS

	31 December 2010	31 December 2009
Bank deposits, in RUB	160,000	10,400
Cash in banks, in RUB	36,891	44,704
Cash in banks, in USD	10,142	92
Cash in hand	121	62
Total	207,154	55,258

Short-term bank deposits as at 31 December 2010 have maturity up to three months and can be withdrawn without any restrictions.

Cash and cash equivalents fair value is equal to their carrying value.

OPEN JOINT STOCK COMPANY "HC "OZNA" AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2010 (in thousands of Russian Rubles, unless otherwise stated)

21. SHAREHOLDERS' EQUITY

Share capital and share premium

The share capital of the Group as at 31 December 2010 consists of 563,597,774 (2009: 563,597,774) authorized, issued and fully paid ordinary shares with a par value of 1 Russian Ruble.

Number of shares unless otherwise stated	Ordinary shares	
	2010	2009
On issue at 1 January	563,597,774	504,369,264
Issued	-	59,228,510
On issue at 31 December	563,597,774	563,597,774

The shareholders of the Group are represented by:

Shareholder	Year ended 31 December 2010, %	% Year ended 31 December 2009, %
Marat Marsovich Akhmetshin	24.67	24.67
Marat Familyevich Fattakhov	24.67	24.67
Artur Valeryevich Khazigaleev	24.67	24.67
Yurals Holding BV	25.99	25.99
Total	100.00	100.00

Dividends

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

In accordance with Russian legislation the Company's distributable reserves are limited to the balance of retained earnings as recorded in the Company's statutory financial statements prepared in accordance with Russian Accounting Principles.

In 2010, the decision was made by the shareholders of the Group to pay dividends for the operating results of the 1st six months of the year of 2010 in the total amount of 99,530 thousand Russian Rubles (0.1766 Russian Rubles per share) and additional of 12,963 thousand Russian Rubles for 9 months operating results of the year 2010 (0.023 Russian Rubles per share). Dividends declared were paid during 2010.

22. INCOME TAX EXPENSE

The Group's applicable tax rate is the income tax rate of 20% for Russian companies effective from 1 January 2009.

Income tax recognized in profit or loss

	Year ended 31 December 2010	Year ended 31 December 2009
Current income tax	88,597	113,634
Deferred tax expense/(benefit)	8,624	(3,734)
Income tax expense	97,221	109,900

OPEN JOINT STOCK COMPANY “HC “OZNA” AND SUBSIDIARIES

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Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

Deferred tax assets and liabilities

The tax effect of the major temporary differences that gave rise to the deferred tax assets and liabilities as at 31 December 2010 and 2009 is presented below:

	31 December 2010	31 December 2009
Deferred tax assets		
Accrual and other payables	16,872	30,442
Inventories	21,703	9,769
Property, plant and equipment	2,596	7,817
Prepaid expenses	5,637	5,676
Trade and other receivables	2,174	2,842
Other adjustments	619	2,321
Set off of tax	(33,856)	(45,822)
Total	15,745	13,045
Deferred tax liabilities		
Property, plant and equipment	80,686	86,266
Trade and other receivables	4,875	-
Other adjustments	1,490	1,427
Set off of tax	(33,856)	(45,822)
Total	53,195	41,871

All movements in temporary differences were recognized in profit or loss, except for the amount recognized in 2009 as part of business combination (2,219 thousand Russian Rubles).

A temporary difference of 1,471,404 thousand Russian Rubles relating to investments in subsidiaries has not been recognized as a Group is able to control the timing of reversal of the difference, and reversal is not expected in the foreseeable future.

Reconciliation of effective tax rate

	Year ended			
	31 December 2010	%	31 December 2009	%
Profit before income tax	408,647	100	417,308	100
Income tax at applicable tax rate	81,729	20	83,462	20
Adjustments due to:				
Tax effect of expenses that are not deductible for taxation purposes	15,492	4	26,438	6
Income tax expense	97,221	24	109,900	26

23. TRADE PAYABLES AND ADVANCES RECEIVED

	31 December 2010	31 December 2009
Trade payables to third parties	451,887	871,740
Trade payables to associates	322	-
Trade payables to other related parties	2,078	6,611
Total	454,287	878,351

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	31 December 2010	31 December 2009
Advances received from third parties	1,290,152	338,260
Total	1,290,152	338,260

The Group received advances mainly from customers OJSC “ULPIK” and JSC “Kaspiyskiy Truboprovodniy Kosorcium” for the supply of equipment.

24. TAXES PAYABLE

	31 December 2010	31 December 2009
Value-added tax	99,323	172,701
Contributions to social funds	18,645	18,140
Personal income tax	20,230	21,369
Property tax	1,660	2,542
Other	1,869	1,078
	141,727	215,830

25. SHORT-TERM BORROWINGS

	Denominated in currency	Interest rate, 2010	Interest rate, 2009	31 December 2010	31 December 2009
OJSC “Sberbank RF”	RUB	6.00%- 15.5%	11.75% - 18%	54,037	211,020
CJSC “UniCredit Bank”	RUB	5.55%-9.8%	-	54,025	-
	RUB	7.75%- 8.25%	-	5,030	-
CJSC “BSGV”				3,093	2,899
OJSC “Neftegazmash”	RUB	10%	10%		
Total				116,185	213,919

The Group may enjoy credit lines of 98,000 thousand Russian Rubles provided by OJSC “Sberbank RF” (Note 16). These lines are secured by inventory with a carrying amount of 203,964 thousand Russian Rubles. As at 31 December 2010 no draw downs were made from these credit lines.

As at 31 December 2010 the Group also contracted banks to issue bank guarantees to Group’s customers against the advances to the Group for the future delivery of the goods and services to the total amount of 697,702 thousand Russian Rubles. Bank guarantees are secured by inventory with a carrying amount of 5,062 thousand Russian Rubles (Note 16).

26. ACCRUALS AND OTHER PAYABLES

Short-term accruals as at 31 December 2010 and 2009 consisted of the following:

	31 December 2010	31 December 2009
Payroll and bonus accrual	104,178	162,409
Unused vacation accrual	48,911	48,309
Warranty provision	6,200	6,858
Other accruals and payables	17,803	32,322
Total	177,092	249,898

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27. RELATED PARTIES

Control relationship

The Company does not have a parent company. The Company's ultimate shareholders are disclosed in Note 21.

Management remuneration

Key management received the following remuneration during the year, which is included in personnel costs:

	Year ended	
	31 December 2010	31 December 2009
Salaries	21,290	11,552
Bonuses	64,220	87,648
Contributions to social funds	2,241	3,068
Other short-term benefits provided	397	370
Termination benefits	431	-
Total	88,579	102,638

Other transactions

As at 31 December 2010 loans to directors amounted to 314 thousand Russian Rubles including interest receivable (2009: 3,340 thousand Russian Rubles).

Transactions with other related parties

The Group had the following significant transactions with associates and other related parties:

	Year ended	
	31 December 2010	31 December 2009
Revenue from other related parties*	152,021	60,214
Purchases from associate parties	-	8,639
Purchases from other related parties	105,392	50,459
Interest income from other related parties	2,356	4,482
Interest expense to associate parties	196	-
Interest expense to other related parties	-	250

The Group had the following significant balances with associates and other related parties:

	Year ended	
	31 December 2010	31 December 2009
Loans given to other related parties	3,621	37,630
Loans received from other related parties	3,093	2,899
Trade accounts receivable from other related parties	23,964	11,473
Advances paid to other related parties	3,593	2,904
Other receivables from other related parties	21,560	21,960
Trade payables to associate parties	322	-
Trade payables to other related parties	2,078	6,611
Other current payables from other related parties	-	16,170

* Other related parties mostly include entities under control of Group shareholders.

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Transactions with related parties are performed on terms that would not necessarily be available to unrelated parties. Interest rate on loans given to related parties as at 31 December 2010 are from 13.75% to 15%.

The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received. No provision has been made for doubtful debts in respect of the amounts owed by related parties.

28. DETERMINATION OF FAIR VALUES

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and for disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

Property, plant and equipment - The fair value of property, plant and equipment recognised as a result of a business combination is based on market values. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably and willingly. The fair value of items of plant, equipment, fixtures and fittings is based on market approach and cost approaches using quoted market prices for similar items when available.

When no quoted market prices are available, the fair value of property, plant and equipment is primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

Intangible assets - The fair value of intangible assets is based on the discounted cash flows expected to be derived from the use and eventual sale of the assets.

Inventories - The fair value of inventories acquired in a business combination is determined based on its estimated selling price in the ordinary course of business less the estimated costs of completion and sale, and a reasonable profit margin based on the effort required to complete and sell the inventories.

Investments in equity and debt securities - The fair value of financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets is determined by reference to their quoted closing bid price at the reporting date. The fair value of held-to-maturity investments is determined for disclosure purposes only.

Trade and other receivables - The fair value of trade and other receivables, excluding construction work in progress, is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes.

Non-derivative financial liabilities - Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. In respect of the liability component of convertible notes, the market rate of interest is determined by reference to similar liabilities that do not have a conversion option. For finance leases the market rate of interest is determined by reference to similar lease agreements.

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29. OPERATING LEASES

The Group leases land plots, office facilities and other assets owned by local authorities and the private companies under operating lease agreements.

Non-cancellable operating lease rentals are payable as follows:

	Year ended	
	31 December 2010	31 December 2009
Less than 1 year	12,950	23,432
1-5 years	5,063	41,954
More than 5 years	76	-
Total	18,089	65,386

Land plots leased by the Group represent areas on which industrial buildings are located. The duration of the operating leases contracts are as follows: minimum period makes 11 month, maximum – 6-7 years.

During the current year 24,641 thousand Russian Rubles was recognized in profit or loss in respect of operating leases (2009: 31,375 thousand Russian Rubles).

30. RISK MANAGEMENT

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

- credit risk
- liquidity risk
- market risk

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

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

Major categories of financial instruments

The Group's principle financial liabilities comprise loans and borrowings, trade payables and other payables and accruals. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various financial assets such as trade receivables, investments in securities and cash and cash equivalents.

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	Year ended	
	31 December 2010	31 December 2009
Financial assets		
<i>Loans and receivables (including cash and cash equivalents)</i>		
Cash and cash equivalents	47,154	44,858
Bank deposits	531,665	10,400
Redeemable notes	963	38,361
Loans given	6,684	47,710
Trade receivables	1,208,123	1,470,453
Total financial assets	1,794,589	1,611,782
Financial liabilities		
<i>Measured at amortised cost</i>		
Loans and borrowings	116,185	213,919
Trade payables	454,287	878,351
Total financial liabilities	570,472	1,092,270

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

Currency risk

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the functional currency of Group entities, which is Russian Rouble. The currencies in which these transactions primarily are denominated are euro and USD.

In respect of other monetary assets and liabilities denominated in foreign currencies, the Group's policy is to ensure that its net exposure is kept to an acceptable level by buying or selling foreign currencies at spot rates when necessary to address short-term imbalances.

Exposure to currency risk

The Group's exposure to foreign currency risk was as follows based on notional amounts:

	USD- denominated 2010	Euro- denominated 2010	USD- denominated 2009	Euro- denominated 2009
Bank deposits	10,142	201,665	92	-
Trade receivables	102	-	-	-
Gross exposure	10,244	201,665	92	-
Net exposure	10,244	201,665	92	-

The following significant exchange rates applied during the year:

	Average rate		Reporting date spot rate	
	2010	2009	2010	2009
USD	30.37	31.75	30.48	30.24
EUR	40.30	44.14	40.33	43.39

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Sensitivity analysis

A strengthening of the Russian Rouble, as indicated below, against the following currencies at 31 December would have increased (decreased) profit or loss net of taxes by the amounts shown below. This analysis is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2009, albeit that the reasonably possible foreign exchange changes rate variances were different, as indicated below.

	Strengthening	Weakening
	Profit or loss	Profit or loss
31 December 2010		
USD (10% movement)	(820)	820
EUR (10% movement)	(16,133)	16,133
31 December 2009		
USD (10% movement)	(7)	7
EUR (10% movement)	-	-

Interest rate risk

Interest risk is the risk that changes in floating interest rates will adversely impact financial results of the Group.

Group profit and cash flows from the operating activity do not depend on the interest rate risks changes. The Group does not use any derivatives to manage interest rate risk exposure, at the same time the majority of the Group's financial assets and liabilities are at fixed rates.

	Carrying amount	
	2010	2009
Fixed rate instruments		
Financial assets	539,312	96,471
Financial liabilities	(116,185)	(213,919)
	423,127	(117,448)

Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial instruments as fair value through profit or loss or as available-for-sale. Therefore a change in interest rates at the reporting date would not have an effect in profit or loss or in equity.

Price risk

Management considers the Group not to be influenced by security price risk as it does not have ready for sale investments. The Group does not commit transactions concerning financial instruments with the value depending on the good quotation in the open market that is why the risk considered as distant.

Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Group financial assets, having potential credit

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risk, are represented by accounts receivable, cash and bank deposits. The aim of the credit risk management is the prevention of liquid assets loss, lodged or invested in financial institutes or receivables' cost lowering.

Cash and cash equivalents. Cash and cash equivalents are placed in major Russian and multinational banks, having independent credit rating. All account balances haven't exceeded the time limit and aren't devalued.

Buyers and customers debts. The Group has a credit policy under which each new customer is analysed individually for creditworthiness before the Group's standard payment and delivery terms and conditions are offered.

The summary below shows the outstanding balances of top five debtors of the Group:

		31 December 2010		31 December 2009	
	Customer location	% in total receivables	Outstanding balance	% in total receivables	Outstanding balance
OJSC "NK Rosneft"	Moscow	29.4%	545,705	56.8%	988,265
OJSC "LUKOIL"	Moscow	10.9%	202,491	0.1%	2,376
OJSC "TNK-BP Holding"	Moscow	5.4%	100,908	2.7%	47,405
OJSC "Uraltechnoneftegas Group"	Ufa				
		3.8%	70,978	0.0%	-
OJSC "Surgutneftegaz"	Surgut	3.4%	63,768	3.4%	59,895
Total		52.9%	983,850	63%	1,097,941

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The above mentioned minimal cash levels are held on cash account balances, bank deposits, short-term investments, cash and other financial instruments that can be classified as cash equivalents.

The table below summarizes the maturity profile of the Group's trade payables and payables for operational activity as at 31 December 2010 and 2009, based on contractual undiscounted payments:

	31 December 2010	31 December 2009
On demand	314,064	664,062
Due within three months	127,654	152,993
Due from three to six months	2,618	55,292
Due from six months to twelve months	7,998	1,262
Due within more than twelve months	1,953	4,742
Total	454,287	878,351

The Group short-term borrowings are repayable as follows:

	31 December 2010	31 December 2009
Due within three months	89,173	113,452
Due from three to twelve months	27,012	100,467
Total	116,185	213,919

	31 December 2009	31 December 2009
Interest expense	15,016	61,585
Interest paid	15,776	62,193

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Capital risk management

The Group manages its capital to ensure that entities of the Group will be able to continue as a going concern while maximizing the return to the equity holder through the optimization of the debt and equity balance. The management of the Group reviews the capital structure on a regular basis. Based on the results of this review, the Group takes steps to balance its overall capital structure through the payment of dividends, new share issues and share buy-backs as well as the issue of new debt or the redemption of existing debt. The Group monitors capital on the capitalization ratio basis as well as direct ratio of net debt (difference between short-term borrowings and cash and cash equivalents) to earnings before interest, tax, depreciation and amortization (EBITDA).

Gearing ratio

The Group's capital structure as determined by gearing ratio at the year end was as follows:

	31 December 2010	31 December 2009
Debt (i)	116,185	213,919
Cash and cash equivalents (Note 20)	207,154	55,258
Net debt	(90,969)	158,661
Equity (ii)	2,283,044	2,081,044
Net debt to equity ratio	(0.04)	0.08

(i) Debt is defined as short-term borrowings, as detailed in Note 25;

(ii) Equity includes share capital and all reserves of the Group.

Net debt /EBITDA

Net debt /EBITDA as at 31 December 2010 and 2009:

	31 December 2010	31 December 2009
Profit before income tax	408,647	417,308
Plus depreciation and amortisation	88,271	80,359
Plus interest expense	15,016	61,585
Minus interest income	18,135	19,686
EBITDA	493,799	539,566
Net debt	(90,969)	158,661
Net debt/EBITDA	(0.18)	0.29

31. COMMITMENTS AND CONTINGENCIES

Litigation

The Group has been and continues to be the subject of legal proceedings and adjudications from time to time, none of which has had, individually or in the aggregate, a material adverse impact on the Group. Management believes that the resolution of all such matters will not have a material impact on the Group's consolidated financial position or operating results.

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Taxation contingencies in the Russian Federation

The taxation system in the Russian Federation is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

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

Environmental matters

The Group is subject to extensive federal and local environmental controls and regulations. The Group's management believes that the Group operations are in compliance with all current existing environmental legislation in the Russian Federation. However, environmental laws and regulations continue to evolve. The Group is unable to predict the timing or extent to which those laws and regulations may change, or the cost thereby.

Insurance

In 2010 management has determined the following main insurance types according to the Group insurance policy:

- * Property insurance;
- * Fire dangerous objects insurance;
- * Third parties liability insurance of risks associated with start-up and installation works;
- * Accident insurance;
- * Cargo insurance.

Management believes that the Group has an adequate insurance coverage of the risks that could have a material adverse effect on the Group's operations and consolidated financial position.

Capital commitments

The Group does not have capital commitments as at 31 December 2010. The Group did not have capital commitments as at 31 December 2009.

32. EVENTS AFTER THE REPORTING DATE

On 10 June 2011 the decision was made to dispose of 100% shares of LLC “Industrial Systems”.