

**Urals Energy Public Company Limited**

**Consolidated Financial Statements**

**As of and for the Year Ended 31 December 2017**

**Urals Energy Public Company Limited**  
**Consolidated Financial Statements**

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## **Independent Auditor's Report** **To the Members of Urals Energy Public Company Limited**

### **Report on the Audit of the Consolidated Financial Statements**

#### **Opinion**

We have audited the consolidated financial statements of Urals Energy Public Company Limited (the "Company"), and its subsidiaries (together, the "Group"), which are presented in pages 8 to 50 and comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2017, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union.

#### **Basis for Opinion**

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the consolidated financial statements in Cyprus, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Key audit matters**

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

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*Key audit matter*

*How our audit addressed the key audit matter*

*Finalisation of purchase price allocation related to acquisition of 100% interest in OOO Arctic Oil Company*

*Refer to Note 27 to the consolidated financial statements*

In August 2016, the Group acquired a 100% interest in OOO Arctic Oil Company (hereafter - "Arctic Oil Company") from a third party for a total cash consideration of US \$1.8 million. The share purchase agreement also stipulated an additional payment (contingent consideration) should the Group merge Arctic Oil Company with its existing subsidiary and sell the combined company to a third party within two years from the acquisition of Arctic Oil Company. This new subsidiary is engaged in oil production in the central part of the Peschanoozerskoe oil field on Kolguyev Island. Management assessed that the acquisition qualifies as a business combination and applied IFRS 3 "Business Combinations". In accordance with IFRS 3, in its 2016 IFRS consolidated financial statements the Group recognised the acquired assets and liabilities based upon their provisional fair values at the date when the Group obtained control over Arctic Oil Company. Within 12 months from the acquisition date, the Group has finalised its assessment of the fair values of the assets and liabilities acquired and retrospectively adjusted the provisional amounts recognised at the acquisition date.

This was a significant focus area for our audit due to the significance of management's judgements and estimates involved in accounting for this acquisition.

We involved our valuation specialists to review the valuation report of the independent appraiser engaged by management for the finalisation of the purchase price allocation of OOO Arctic Oil Company.

We re-assessed that assumptions used in prior year are still valid and performed reconciliation of the purchase price consideration to the share purchase agreement and the amount of actual cash paid as per bank orders. We have re-confirmed management's assessment that the acquisition should be accounted for as a business combination in accordance with IFRS 3. We re-confirmed appropriateness of the identification of assets and liabilities assumed at acquisition date. We inquired management in relation to subsequent disposal of combined company and confirmed and corroborated that there were no such plans. Consequently, we concurred with management's estimate that the fair value of the contingent consideration was nil.

We assessed the final purchase price allocation, including an assessment of the final fair value of acquired assets and liabilities and the final assumptions and methodology used by the Group's management for the final fair value measurement of the assets and liabilities acquired.

We have not identified any significant issues in determination of the final fair values.

We considered whether the bargain gain from acquisition of subsidiary recognised by the Group as a result of finalisation of purchase



*Key audit matter*

*How our audit addressed the key audit matter*

price allocation is appropriately determined. We evaluated the completeness of the disclosures made in Note 27 of the financial statements to comply with the requirements of IFRS 3 “Business Combinations”. In particular, we assessed that retrospective adjustments made to preliminary purchase price allocation are appropriately reflected and disclosed in the notes to consolidated financial statements.

*Going concern*

*Refer to Note 3 to the consolidated financial statements*

The Group has a significant balance of undeveloped oil reserves that require significant additional investment. The Group is dependent on external debt to fully develop these oil reserves and realise the value attributed to such assets.

The Group had net current liabilities of USD 1.8 million as of 31 December 2017.

Based on the cash flow projections, management has concluded that the application of the going concern assumption for the preparation of the consolidated financial statements is appropriate.

Management applied its judgement and estimates primarily to the forecasts of oil production levels and oil prices.

We focused on this area of audit due to pervasiveness of the matter for the consolidated financial statements as a whole and the significant management estimates and judgements involved.

We evaluated and critically assessed the composition of future cash flows in management’s cash flow projections to ensure completeness of all operating expenses included in the cash flow projections.

Management’s key assumptions were evaluated as follows:

- the forecast for the oil price, the USD/RR exchange rate and mineral extraction tax rates were compared to independent forecasts by widely known information agencies and/or government economic and statistical bodies;
- major cash flow items were reconciled to management’s budgets and historical data;
- management’s sales volumes forecasts were compared to historical data and prices for oil products were reconciled to approved price lists for available periods (up to May 2018);
- expected proceeds from debt were reconciled to amounts of credit limits available to the Group as of 31 December 2017 or credit limits under loan agreements concluded in early 2018;

*Key audit matter*

*How our audit addressed the key audit matter*

- budgeted debt repayments were reconciled to repayment schedules stipulated by the contractual terms of respective loan agreements;
- reviewed compliance with debt covenant terms, included in relevant loan agreements.
- analysed subsequent events (after reporting date and up to date of this report) to consider whether there were any significant events that could cast doubt over the Group's going concern status.

We also compared actual financial results for the first quarter of 2018 to the respective projections included in the model to assess whether the assumptions included in the model were reasonable.

*Oil and gas reserves estimation*

*Refer to Notes 6, 10 and 27 to the consolidated financial statements*

For the purposes of 2017 consolidated financial statements, oil and gas reserves of the Group were determined in accordance with Society of Petroleum Engineers definitions and were estimated by Blackwatch Petroleum Services Limited, the Group's independent reservoir engineers who issued their report in June 2018. The estimate included oil reserves at AO Arcticneft, OOO Arctic Oil Company, AO Petrosakh, OOO RK-Oil and OOO BVN-Oil.

We focused on this area due to the significance of the impact that oil and gas reserves estimation renders on the results of the property, plant and equipment impairment tests, depreciation and depletion rates and dismantlement provision, which are material to the consolidated financial statements.

We assessed professional competence, experience and objectivity of management's external experts involved in the reserves estimation process and concluded that the management's experts had sufficient professional competence, experience and objectivity for the purpose of our audit.

In accordance with the report issued by Blackwatch Petroleum Services Limited, total proved reserves for Okruzhnoe field of AO Petrosakh decreased comparing to management's prior estimates.

We analysed the decrease of total proved reserves for Okruzhnoe field of AO Petrosakh and assessed that appropriate volumes were used for the purposes of depreciation calculation by management and appropriate estimates were used for the calculation of asset retirement obligation.



*Key audit matter*

*How our audit addressed the key audit matter*

Since decrease in total proved reserves for Okruzhnoe field triggered an impairment assessment for property, plant and equipment of AO Petrosakh, management prepared an impairment test model for the cash generating unit. We reviewed the model and assessed major assumptions used by management, such as discount rate, inflation rate, average oil price, estimated productions volumes and other inputs to the impairment model. We agreed with the Company's conclusion that no impairment should be recognised.

We evaluated the completeness of the disclosures made in the notes to the consolidated financial statements to comply with the requirements of IFRS.

### **Responsibilities of the Board of Directors and those charged with governance for the Consolidated Financial Statements**

The Board of Directors is responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union, and for such internal control as the Board of Directors determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

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



## **Auditor's Responsibilities for the Audit of the Consolidated Financial Statements**

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

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

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



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

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

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

#### **Other Matter**

This report, including the opinion, has been prepared for and only for the Company's members as a body and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whose knowledge this report may come to.

A handwritten signature in blue ink, appearing to read 'Constantinos Taliotis', is positioned above the printed name.

Constantinos Taliotis  
Certified Public Accountant and Registered Auditor  
for and on behalf of

PricewaterhouseCoopers Limited  
Certified Public Accountants and Registered Auditors

Nicosia, 29 June 2018

**Urals Energy Public Company Limited**  
**Consolidated Statement of Financial Position**  
(presented in US\$ thousands)

	Note	31 December	
		2017	2016 Restated
<b>Assets</b>			
<b>Current assets</b>			
Cash and cash equivalents	7	683	1,202
Accounts receivable and prepayments	8	6,982	3,998
Inventories	9	13,814	13,527
Current income tax prepayments		384	-
<b>Total current assets</b>		<b>21,863</b>	<b>18,727</b>
<b>Non-current assets</b>			
Property, plant and equipment	10, 27	72,672	65,653
Supplies and materials for capital construction		2,025	1,668
Deferred income tax assets	14	8,365	265
Other non-current assets	11	544	192
<b>Total non-current assets</b>		<b>83,606</b>	<b>67,778</b>
<b>Total assets</b>		<b>105,469</b>	<b>86,505</b>
<b>Liabilities and equity</b>			
<b>Current liabilities</b>			
Accounts payable and accrued expenses	12	5,037	1,703
Provisions	13	-	266
Income tax payable		1,789	2,009
Other taxes payable	14	6,388	5,897
Short-term borrowings and current portion of long-term borrowings	15	8,818	2,549
Advances from customers		1,588	712
<b>Total current liabilities</b>		<b>23,620</b>	<b>13,136</b>
<b>Long-term liabilities</b>			
Long-term borrowings	15	1,116	4,243
Long-term finance lease obligations	10	702	714
Dismantlement provision	16, 27	2,802	1,892
Long-term accounts payable		144	120
Deferred income tax liabilities	14	-	4,651
<b>Total long-term liabilities</b>		<b>4,764</b>	<b>11,620</b>
<b>Total liabilities</b>		<b>28,384</b>	<b>24,756</b>
<b>Equity</b>			
Share capital	17	1,589	1,589
Conversion difference/Share premium	17	(113)	656,855
Translation difference	27	(60,172)	(62,222)
Retained earnings/(Accumulated deficit)	27	135,155	(535,239)
<b>Equity attributable to shareholders of Urals Energy Public Company Limited</b>		<b>76,459</b>	<b>60,983</b>
<b>Non-controlling interest</b>	18	<b>626</b>	<b>766</b>
<b>Total equity</b>		<b>77,085</b>	<b>61,749</b>
<b>Total liabilities and equity</b>		<b>105,469</b>	<b>86,505</b>

Approved on behalf of the Board of Directors on 29 June 2018

  
L.Y. Dyachenko  
CEO

  
S. E. Uzornikov  
Chief Financial Officer

The accompanying notes on pages 12 to 50 are an integral part of these consolidated financial statements

**Urals Energy Public Company Limited**  
**Consolidated Statement of Profit or Loss and Other Comprehensive Income**  
(presented in US\$ thousands)

	Note	Year ended 31 December	
		2017	2016 Restated
Revenues after excise taxes and export duties	19	44,176	29,052
Cost of sales	21	(35,661)	(21,795)
<b>Gross profit</b>		<b>8,515</b>	<b>7,257</b>
Selling, general and administrative expenses	22	(6,080)	(4,358)
Bargain gain from acquisition of subsidiary	27	-	259
Other operating loss	8, 12, 13, 14	(47)	(853)
<b>Operating profit</b>		<b>2,388</b>	<b>2,305</b>
Interest income	15	72	50
Interest expense	15, 27	(1,626)	(1,078)
Net foreign exchange gain	23	988	4,914
<b>Total net finance (expense)/income</b>		<b>(566)</b>	<b>3,886</b>
<b>Profit before income tax</b>		<b>1,822</b>	<b>6,191</b>
Income tax benefit	14, 27	12,226	2,125
<b>Profit for the year</b>		<b>14,048</b>	<b>8,316</b>
Profit/(loss) for the year attributable to:			
- Non-controlling interest		(161)	91
- Shareholders of Urals Energy Public Company Limited		14,209	8,225
<b>Profit per share from profit attributable to shareholders of Urals Energy Public Company Limited:</b>	<b>17, 27</b>		
- Basic profit per share (in US dollar per share)		1.13	0.65
- Diluted profit per share (in US dollar per share)		1.13	0.65
Weighted average shares outstanding attributable to:			
- Basic shares		12,622,303	12,622,303
- Diluted shares		12,622,303	12,622,303
<b>Profit for the year</b>		<b>14,048</b>	<b>8,316</b>
<b>Other comprehensive profit/(loss) that may be reclassified subsequently to profit (loss), net of income tax:</b>			
- Effect of currency translation	27	2,071	5,573
<b>Total comprehensive income/(loss) for the year</b>		<b>16,119</b>	<b>13,889</b>
Attributable to:			
- Non-controlling interest	18	(140)	219
- Shareholders of Urals Energy Public Company Limited	27	16,259	13,670

The accompanying notes on pages 12 to 50 are an integral part of these consolidated financial statements

**Urals Energy Public Company Limited**  
**Consolidated Statement of Cash Flows**  
(presented in US\$ thousands)

	Note	Year ended 31 December	
		2017	2016 Restated
<b>Cash flows from operating activities</b>			
Profit before income tax		1,822	6,191
Adjustments for:			
Depreciation, amortization and depletion	21	4,288	5,331
Interest income	15	(72)	(50)
Interest expense	15, 27	1,626	1,078
Loss on disposal of property, plant and equipment		-	53
Charge for provision on claims	13	-	138
Foreign currency gain, net	23	(988)	(4,914)
Bargain gain from acquisition of subsidiary	27	-	(259)
Other non-cash transactions	8, 10, 12, 14	(89)	566
<b>Operating cash flows before changes in working capital</b>		<b>6,587</b>	<b>8,134</b>
Decrease/(increase) in inventories		165	(3,574)
Increase in accounts receivables and prepayments		(11,599)	(7,217)
Increase/(decrease) in accounts payable and accrued expenses		60	(244)
Increase/(decrease) in advances from customers		843	(12)
Increase in other taxes payable		192	1,880
<b>Cash used in operations</b>		<b>(3,752)</b>	<b>(1,033)</b>
Interest received		26	24
Interest paid		(1,087)	(779)
Income tax paid		(1,506)	(350)
<b>Net cash used in operating activities</b>		<b>(6,319)</b>	<b>(2,138)</b>
<b>Cash flows from investing activities</b>			
Purchase of property, plant and equipment and intangible assets		(5,483)	(4,391)
Acquisition of subsidiaries, net of cash acquired and indemnification asset received	27	-	(757)
Loans given		(1,683)	(354)
<b>Net cash used in investing activities</b>		<b>(7,166)</b>	<b>(5,502)</b>
<b>Cash flows from financing activities</b>			
Proceeds from borrowings	15	18,151	13,636
Repayment of borrowings	15	(4,284)	(6,459)
Finance lease principal payments		(246)	(55)
Dividends paid to the Company's shareholders	17	(783)	-
<b>Net cash generated from financing activities</b>		<b>12,838</b>	<b>7,122</b>
Effect of exchange rate changes on cash and cash equivalents		129	25
<b>Net decrease in cash and cash equivalents</b>		<b>(518)</b>	<b>(493)</b>
Cash and cash equivalents at the beginning of the year		1,202	1,695
<b>Cash and cash equivalents at the end of the year</b>		<b>683</b>	<b>1,202</b>

The accompanying notes on pages 12 to 50 are an integral part of these consolidated financial statements

**Urals Energy Public Company Limited**  
**Consolidated Statement of Changes in Equity**  
 (presented in US\$ thousands)

	Notes	Share capital	Share premium	Difference from conversion of share capital into US\$	Cumulative Translation Difference	Retained earnings/(Accumulated deficit)	Equity attributable to Shareholders of Urals Energy Public Company Limited	Non-controlling interest	Total equity
<b>Balance at 31 December 2015</b>	<b>17, 18</b>	<b>1,589</b>	<b>656,968</b>	<b>(113)</b>	<b>(67,667)</b>	<b>(543,464)</b>	<b>47,313</b>	<b>547</b>	<b>47,860</b>
Effect of currency translation Profit for the year		-	-	-	5,445	-	5,445	128	5,573
<b>Total comprehensive income</b>		-	-	-	<b>5,445</b>	<b>8,225</b>	<b>8,225</b>	<b>91</b>	<b>8,316</b>
<b>Balance at 31 December 2016 Restated</b>	<b>17, 18</b>	<b>1,589</b>	<b>656,968</b>	<b>(113)</b>	<b>(62,222)</b>	<b>(535,239)</b>	<b>60,983</b>	<b>766</b>	<b>61,749</b>
Effect of currency translation Profit/(loss) for the year		-	-	-	2,050	-	2,050	21	2,071
<b>Total comprehensive income/(loss)</b>		-	-	-	<b>2,050</b>	<b>14,209</b>	<b>14,209</b>	<b>(161)</b>	<b>14,048</b>
Share premium reduction	17	-	(656,968)	-	-	656,968	-	-	-
Dividends declared	17	-	-	-	-	(783)	(783)	-	(783)
<b>Balance at 31 December 2017</b>	<b>17, 18</b>	<b>1,589</b>	-	<b>(113)</b>	<b>(60,172)</b>	<b>135,155</b>	<b>76,459</b>	<b>626</b>	<b>77,085</b>

The accompanying notes on pages 12 to 50 are an integral part of these consolidated financial statements

**Urals Energy Public Company Limited**  
**Notes to the Consolidated Financial Statements**  

(presented in US\$ thousands)

**1 Activities**

Urals Energy Public Company Limited ("Urals Energy" or the "Company" or "UEPCL") was incorporated as a limited liability company in Cyprus on 10 November 2003. Urals Energy and its subsidiaries (the "Group") are primarily engaged in oil and gas exploration and production in the Russian Federation and processing of crude oil for distribution on both the Russian and international markets.

The Group's average number of employees employed for year ended 31 December 2017 was 455 (for year ended 31 December 2016: 461).

The registered office of Urals Energy is at Glafkos Tower, Office 501, 5th Floor, 3 Menandrou Street, 1066 Nicosia, Cyprus. UEPCL's shares are traded on the AIM Market operated by the London Stock Exchange.

As at 31 December 2017 major shareholder with 44.59% ownership interest was Adler Impex S.A. which is beneficially owned by Mrs. Anastasia Kononova. Other shares belong to management (3.35%), Petraco Oil Company ("Petraco") (3.44%) and other insignificant shareholders.

As at 31 December 2016 the Group's major shareholder with 44.59% ownership interest was Adler Impex S.A. which is beneficially owned by Mr. Roman Shvets. Other shares belong to management (6.01%), Petraco Oil Company ("Petraco") (3.44%) and other insignificant shareholders.

The Group comprises UEPCL and the following main subsidiaries:

Entity	Jurisdiction	Effective ownership interest at 31 December	
		2017	2016
<i>Exploration and production</i>			
AO Petrosakh ("Petrosakh") (Note 18)	Sakhalin Region	98.56%	97.2%
AO Arcticneft ("Arcticneft")	Nenetsky Region	100%	100%
OOO Arctic Oil Company ("Arctic Oil Company") (Note 27)	Nenetsky Region	100%	100%
OOO BVN-Oil ("BVN-Oil")	Komi Republic	100%	100%
OOO RK-Oil ("RK-Oil")	Komi Republic	100%	100%
<i>Management company</i>			
OOO Urals Energy <sup>1</sup>	Moscow	-	100%

<sup>1</sup> In April 2017 the Group completed an internal reorganisation of its subsidiaries, which is intended to streamline the management of the Group and cut administrative expenses. As part of the internal reorganisation, AO Petrosakh, the Group's operating company on Sakhalin Island and principal profit and cash generator, was merged with OOO Urals Energy, the Russia-incorporated management company for all of the Group's operations, which was essentially a cost centre (Note 6 and 14).

**2 Significant Accounting Policies**

**Basis of preparation.** The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) under the historical cost convention as modified by the initial recognition of financial instruments based on fair value.

These policies have been consistently applied to all the periods presented, unless otherwise stated.

The preparation of consolidated financial statements in conformity with IFRS as adopted by the EU requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the reporting date and the reported amounts of revenues and expenses during the reporting period. Critical accounting estimates and judgements are disclosed in Note 6. Actual results could differ from the estimates.

**Functional and presentation currency.** The United States dollar ("US dollar or US\$ or \$") is the presentation currency for the Group's operations as management have used the US dollar accounts to manage the Group's financial risks and exposures, and to measure its performance. Financial statements of the Russian subsidiaries are measured in Russian Roubles, their functional currency.

The functional currency of the Company is the US Dollar as substantially all the cash flows affecting the Company are in US Dollars.

**2 Significant Accounting Policies (Continued)**

**Translation to functional currency.** Monetary assets and liabilities denominated in foreign currencies are retranslated into the functional currency at the rate of exchange ruling at the reporting date. Any resulting exchange differences are included in the profit or loss component of the consolidated Statement of profit or loss and other comprehensive income. Non-monetary assets and liabilities that are measured at historical cost and denominated in a foreign currency are translated into the functional currency using the rates of exchange as at the dates of the initial transactions. The US dollar to Russian Rouble exchange rates were 57.60 and 60.66 as of 31 December 2017 and 2016, respectively.

**Translation to presentation currency.** The Group's consolidated financial statements are presented in US dollars in accordance with IAS 21, *The Effects of Changes in Foreign Exchange Rates*. The results and financial position of each group entity having a functional currency different from the presentation currency are translated into the presentation currency as follows:

- (i) Assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position. Goodwill and fair value adjustments arising on the acquisitions are treated as assets and liabilities of the acquired entity.
- (ii) Income and expenses for each Statement of profit or loss and other comprehensive income are translated to the presentation currency of the Company at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions).
- (iii) All resulting exchange differences are recognised as a separate component of equity.

When a subsidiary is disposed of through sale, liquidation, repayment of share capital or abandonment of all, or part of, that entity, the exchange differences deferred in other comprehensive income are reclassified to the profit and loss.

**Consolidated financial statements.** Subsidiaries are those investees, including structured entities, that the Group controls because the Group (i) has power to direct the relevant activities of the investees that significantly affect their returns, (ii) has exposure, or rights, to variable returns from its involvement with the investees, and (iii) has the ability to use its power over the investees to affect the amount of the investor's returns. The existence and effect of substantive rights, including substantive potential voting rights, are considered when assessing whether the Group has power over another entity. For a right to be substantive, the holder must have a practical ability to exercise that right when decisions about the direction of the relevant activities of the investee need to be made. The Group may have power over an investee even when it holds less than the majority of the voting power in an investee. In such a case, the Group assesses the size of its voting rights relative to the size and dispersion of holdings of the other vote holders to determine if it has de-facto power over the investee. Protective rights of other investors, such as those that relate to fundamental changes of the investee's activities or apply only in exceptional circumstances, do not prevent the Group from controlling an investee. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date on which control ceases.

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

The Group measures non-controlling interest that represents present ownership interest and entitles the holder to a proportionate share of net assets in the event of liquidation on a transaction by transaction basis, either at: (a) fair value, or (b) the non-controlling interest's proportionate share of net assets of the acquiree. Non-controlling interests that are not present ownership interests are measured at fair value.

Non-controlling interest is that part of the net results and of the equity of a subsidiary attributable to interests which are not owned, directly or indirectly, by the Company. Non-controlling interest forms a separate component of the Group's equity.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Company and all of its subsidiaries use uniform accounting policies consistent with the Group's policies. When necessary amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

**Purchases and sales of non-controlling interests.** The Group applies the economic entity model to account for transactions with owners of non-controlling interest. Any difference between the purchase consideration and the carrying amount of non-controlling interest acquired is recorded as a capital transaction directly in equity. The

## **2 Significant Accounting Policies (Continued)**

Group recognises the difference between sales consideration and carrying amount of non-controlling interest sold as a capital transaction in the consolidated statement of changes in equity.

*Financial instruments - key measurement terms.* Depending on their classification financial instruments are carried at fair value or amortised cost as described below.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

A portfolio of financial derivatives or other financial assets and liabilities that are not traded in an active market is measured at the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (i.e. an asset) for a particular risk exposure or paid to transfer a net short position (i.e. a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date. This is applicable for assets carried at fair value on a recurring basis if the Group: (a) manages the group of financial assets and financial liabilities on the basis of the entity's net exposure to a particular market risk (or risks) or to the credit risk of a particular counterparty in accordance with the entity's documented risk management or investment strategy; (b) it provides information on that basis about the group of assets and liabilities to the entity's key management personnel; and (c) the market risks, including duration of the entity's exposure to a particular market risk (or risks) arising from the financial assets and financial liabilities is substantially the same.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) Level 1 are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) Level 2 measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is prices) or indirectly (that is, derived from prices), and (iii) Level 3 measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs).

*Amortised cost* is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the consolidated statement of financial position.

*The effective interest method* is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

*Classification of financial assets.* Financial assets have the following categories: (a) loans and receivables; (b) available-for-sale financial assets; (c) financial assets held to maturity and (d) financial assets at fair value through profit or loss. Financial assets at fair value through profit or loss have two sub-categories: (i) assets designated as such upon initial recognition, and (ii) those classified as held for trading.

Financial assets that would meet the definition of loans and receivables may be reclassified if the Group has the intention and ability to hold these financial assets for the foreseeable future or until maturity.

**2 Significant Accounting Policies (Continued)**

*Loans and receivables* are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Group intends to sell in the near term.

In 2017 and 2016 all financial assets of the Group related to loans and receivables.

*Classification of financial liabilities.* Financial liabilities have the following measurement categories: (a) held for trading which also includes financial derivatives and (b) other financial liabilities. Liabilities held for trading are carried at fair value with changes in value recognised in profit or loss for the year (as finance income or finance costs) in the period in which they arise. Other financial liabilities are carried at amortised cost.

*Initial recognition of financial instruments.* Trading investments, derivatives and other financial instruments at fair value through profit or loss are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

*Derecognition of financial assets.* The Group derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expire or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control.

Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

*Property, plant and equipment.* Property, plant and equipment acquired as part of a business combination is recorded at fair value at the acquisition date and adjusted for accumulated depreciation, depletion and impairment. All subsequent additions are recorded at historical cost of acquisition or construction and adjusted for accumulated depreciation, depletion and impairment.

Oil and gas exploration and production activities are accounted for in a manner similar to the successful efforts method. Costs of successful development and exploratory wells are capitalised. The cost of property, plant and equipment includes provisions for dismantlement, abandonment and site restoration (refer to Provisions below).

The Group accounts for exploration and evaluation activities in accordance with IFRS 6, *Exploration for and Evaluation of Mineral Resources*. The costs incurred in finding, acquiring, and developing reserves are capitalised on a 'field by field' basis.

Exploration and evaluation assets are measured at cost less provision for impairment, where required. Costs directly associated with an exploration well are initially capitalised in exploration and evaluation assets, which are presented within Property, plant and equipment. These costs include employee remuneration, materials and fuel used, rig costs, delay rentals and payments made to contractors. Geological and geophysical exploration costs are expensed as incurred. Amounts paid for the acquisition of exploration and development licenses are also capitalised as exploration and evaluation assets.

If hydrocarbons are not found, the exploration expenditure is written off as a dry hole. If hydrocarbons are found and, subject to further appraisal activity, which may include the drilling of further wells (exploration or exploratory-type stratigraphic test wells), are likely to be capable of commercial development, the costs continue to be carried as an asset. All such carried costs are subject to technical, commercial and management review at least once a year to confirm the continued intent to develop or otherwise extract value from the discovery. When this is no longer the case, the costs are written off.

An exploration and evaluation asset is reclassified from special category of exploration and evaluation assets presented within Oil and gas properties to ordinary Oil and gas properties when the technical feasibility and commercial viability of extracting a mineral resource are demonstrable. Exploration and evaluation assets are assessed for impairment, and any impairment loss is recognised, before reclassification.

Development and production assets are accumulated generally on a field-by-field basis and represent the cost of

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**2 Significant Accounting Policies (Continued)**

developing the commercial reserves discovered and bringing them to production together with Exploration and Evaluation (E&E) expenditures incurred in finding commercial reserves and transferred from the intangible E&E assets described above. The cost of development and production assets also include the costs of acquisitions and purchases of such assets, directly attributable overheads, finance costs capitalised and the costs of recognising provisions for future restoration and decommissioning.

Depletion of capitalized costs of proved oil and gas properties is calculated using the unit-of-production method for each field based upon proved reserves for property acquisitions and proved developed reserves for exploration and development costs. Oil and gas reserves for this purpose are determined in accordance with Society of Petroleum Engineers definitions and were last estimated by Blackwatch Petroleum Services Limited, the Group's independent reservoir engineers in June 2018 with the estimate of reserve as at 31 December 2017. As of 31 December 2017 management had preliminary results supporting the changes in reserves reflected in the Blackwatch Petroleum Services Report.

Depreciation of non-oil and gas property, plant and equipment is calculated using the straight-line method over their estimated remaining useful lives, as follows:

	Estimated useful life
Refinery and related equipment	19
Buildings	20
Other assets	6 to 20

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'Other operating (loss)/profit' in the profit and loss section of consolidated Statement of profit or loss and other comprehensive income.

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

Provisions, including those related to dismantlement, abandonment and site restoration, are evaluated and re-estimated annually, and are included in the consolidated financial statements at each reporting date at the present value of the expenditures expected to be required to settle the obligation using pre – tax discount rates which reflect the current market assessment of the time value of money and the risks specific to the liability.

Changes in provisions resulting from the passage of time are reflected in the profit and loss section of consolidated Statement of profit or loss and other comprehensive income each year. Other changes in provisions, relating to a change in the expected pattern of settlement of the obligation, changes in the discount rate or in the estimated amount of the obligation, are treated as a change in accounting estimate in the period of the change. Changes in provisions relating to dismantlement, abandonment and site restoration are added to, or deducted from, the cost of the related asset in the current period. The amount deducted from the cost of the asset should not exceed its carrying amount. If a decrease in the liability exceeds the carrying amount of the asset, the excess is recognised immediately in profit or loss.

The provision for dismantlement liability is recorded on the consolidated statement of financial position, with a corresponding amount being recorded as part of property, plant and equipment in accordance with IAS 16.

**Leases.** Leases of property, plant and equipment where the Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the commencement of the lease at the lower of the fair value of the leased property or the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are presented as finance lease obligations on the consolidated statement of financial position. The interest element of the finance cost is charged to the profit or loss in the consolidated Statement of profit or loss and other comprehensive income over the lease period. Property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life of the asset or the lease term.

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the consolidated Statement of profit or loss and other comprehensive income on a straight-line basis over the period of the lease.

**Impairment of assets.** Assets that are subject to depreciation and depletion are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is

## **2 Significant Accounting Policies (Continued)**

recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell or value in use. For the purposes of assessing impairment, assets are grouped by license areas, which are the lowest levels for which there are separately identifiable cash flows (cash-generating units).

**Reversal of impairment.** Non-financial assets other than goodwill that suffered an impairment are reviewed for indications of possible reversal of impairment at each reporting date.

**Inventories.** Inventories of extracted crude oil, oil products, materials and supplies and construction materials are valued at the lower of the weighted-average cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated cost of completion and selling expenses. General and administrative expenditure is excluded from inventory costs and expensed in the period incurred.

**Trade receivables.** Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, net of provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Such objective evidence may include significant financial difficulties of the debtor, an increase in the probability that the debtor will enter bankruptcy or financial reorganization, and actual default or delinquency in payments. The amount of the provision 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 change in the amount of the provision is recognised in the profit and loss section of consolidated Statement of profit or loss and other comprehensive income.

**Cash and cash equivalents.** Cash and cash equivalents includes cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at amortised cost using the effective interest method. Restricted balances are excluded from cash and cash equivalents for the purposes of the consolidated statement of cash flow. Balances restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date are included in other non-current assets. Restricted cash balances are segregated from cash available for the business to use until such time as restrictions are removed.

**Value added tax.** Output value added tax related to sales is payable to tax authorities on the earlier of (a) collection of receivables from customers or (b) delivery of goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is recognised in the consolidated statement of financial position on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

**Borrowings.** Borrowings are recognised initially at the fair value of the liability, net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective interest method; any difference between amount at initial recognition and the redemption amount is recognised as interest expense over the period of the borrowings. Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

**Capitalisation of borrowing costs.** Borrowing costs directly attributable to the acquisition, construction or production of assets that necessarily take a substantial time to get ready for intended use or sale (qualifying assets) are capitalised as part of the costs of those assets.

The commencement date for capitalisation is when (a) the Group incurs expenditures for the qualifying asset; (b) it incurs borrowing costs; and (c) it undertakes activities that are necessary to prepare the asset for its intended use or sale.

Capitalisation of borrowing costs continues up to the date when the assets are substantially ready for their use or sale.

The Group capitalises borrowing costs that could have been avoided if it had not made capital expenditure on qualifying assets. Borrowing costs capitalised are calculated at the group's average funding cost (the weighted average interest cost is applied to the expenditures on the qualifying assets), except to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset. Where this occurs, actual borrowing costs incurred less any investment income on the temporary investment of those borrowings are capitalised.

## 2 Significant Accounting Policies (Continued)

**Loans receivable.** The loans advanced by the Group are classified as "loans and receivables" in accordance with IAS 39 and stated at amortised cost using the effective interest method. These loans are individually tested for impairment at each reporting date.

**Income taxes.** Income taxes have been provided for in the consolidated financial statements in accordance with legislation enacted or substantively enacted by the end of the reporting period. The income tax charge or benefit comprises current tax and deferred tax and is recognised in profit or loss for the year except if it is recognised in other comprehensive income or directly in equity because it relates to transactions that are also recognised, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes other than on income are recorded within operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

**Uncertain tax positions.** The Group's uncertain tax positions are reassessed by management at the end of each reporting period. Liabilities are recorded for income tax positions that are determined by management as more likely than not to result in additional taxes being levied if the positions were to be challenged by the tax authorities. The assessment is based on the interpretation of tax laws that have been enacted or substantively enacted by the end of the reporting period, and any known court or other rulings on such issues. Liabilities for penalties, interest and taxes other than on income are recognised based on management's best estimate of the expenditure required to settle the obligations at the end of the reporting period.

**Employee benefits.** Wages, salaries, contributions to the Russian Federation state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits (such as health services and kindergarten services) are accrued in the year in which the associated services are rendered by the employees of the Group. The Group has no legal or constructive obligation to make pension or similar benefit payments beyond the payments to the statutory defined contribution scheme.

**Social costs.** The Group incurs employee costs related to the provision of benefits such as health insurance. These amounts principally represent an implicit cost of employing production workers and, accordingly, are included in the cost of sales.

**Prepayments.** Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group. Other prepayments are written off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying value of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss.

**Revenue recognition.** Revenues from sales of goods are recognised at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped. If the Group agrees to transport goods to a specified location, revenue is recognised when the goods are passed to the customer at the destination point.

Sales of services are recognised in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Sales are shown net of VAT and discounts.

## **2 Significant Accounting Policies (Continued)**

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of goods received in a barter transaction cannot be measured reliably, the revenue is measured at the fair value of the goods or service given up.

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

**Segments.** The Group operates in one business segment which is crude oil exploration and production. The Group assesses its results of operations and makes its strategic and investment decisions based on the analysis of its profitability as a whole. The Group operates within geographic segments as disclosed in Note 20.

**Share capital.** Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is presented as a share premium.

**Share-based payments.** The fair value of the employee services received in exchange for the grant of options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, using market prices, taking into account the terms and vesting conditions upon which those equity instruments were granted.

**Earnings per share.** Earnings per share are determined by dividing the profit or loss attributable to equity holders of the Group by the weighted average number of participating shares outstanding during the reporting year.

## **3 Going Concern**

A significant portion of the Group's consolidated net assets of \$ 77.1 million (31 December 2016: \$61.7 million) comprises undeveloped oil reserves requiring significant additional investment. The Group is dependent upon external debt to fully develop the oil reserves and realise the value attributed to such assets.

The Group had net current liabilities of \$ 1.8 million as of 31 December 2017 (31 December 2016: net current assets of \$5.6 million).

Management have prepared monthly cash flow projections for 2018 and for 6 months 2019. Judgements, which are significant to management's conclusion that no material uncertainty exists about the Group's ability to continue as a going concern, include future oil prices and planned production, which were required for the preparation of the cash flow projections and model. Positive overall cash flows are dependent on future oil prices (a price of \$45 per barrel was used for 2018 and \$70 per barrel for six months ended 30 June 2019). Despite the uncertainties, based on the cash flow projections performed and taking into account financing received from Petraco (Note 28), management considers that the application of the going concern assumption for the preparation of these consolidated financial statements is appropriate.

## **4 Adoption of New or Revised standards and interpretations**

The following standards or amended standards and interpretations, relevant to the Group, became effective for the Group from 1 January 2017, but did not have any material impact on the Group:

- Disclosure Initiative – Amendments to IAS 7 (issued on 29 January 2016 and effective for annual periods beginning on or after 1 January 2017). The Group has provided the required disclosure in Note 15.
- Recognition of Deferred Tax Assets for Unrealised Losses – Amendment to IAS 12 (issued on 19 January 2016 and effective for annual periods beginning on or after 1 January 2017).
- Amendments to IFRS 12 included in Annual Improvements to IFRSs 2014-2016 Cycle (issued on 8 December 2016 and effective for annual periods beginning on or after 1 January 2017).

## **5 New Accounting Pronouncements**

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2018 or later, and which the Group has not early adopted. Only those amendments that are relevant to the Group are discussed below.

*IFRS 9 "Financial Instruments" (issued in 24 July 2014 and effective for annual periods beginning on or after 1 January 2018).* Key features of the new standard are:

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
- Classification for debt instruments is driven by the entity's business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets' cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.
- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.
- IFRS 9 introduces a new model for the recognition of impairment losses – the expected credit losses (ECL) model. There is a 'three stage' approach which is based on the change in credit quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.
- Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

Based on an analysis of the Group's financial assets and financial liabilities as at 31 December 2017 and on the basis of the facts and circumstances those exist at that date, as well as forecast information, the main changes expected from adoption of IFRS 9 since 1 January 2018 are the following:

- Current classification of the Group's financial assets will be changed.
- Current model for recognition of impairment losses will be changed into the expected credit losses (ECL) model. However, the Group does not expect that the amount of the expected credit losses will differ significantly from the current impairment provisions.

No significant changes are expected to impact the measurement of financial liabilities.

The new standard also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and extent of the Group's disclosures about its financial instruments particularly in the year of the adoption of the new standard.

Overall, the management of the Group is not expecting a significant impact on its consolidated financial statements from the adoption of the new standard on 1 January 2018.

*IFRS 15, Revenue from Contracts with Customers (issued on 28 May 2014 and effective for the periods beginning on or after 1 January 2018).* The new standard introduces the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must

## **5 New Accounting Pronouncements (Continued)**

generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed.

As the majority of the Group's revenue is derived from arrangements in which the transfer of risks and rewards coincides with the fulfilment of the performance obligations, the changes in respect of timing and amount of revenue currently recognised by the Group were assessed and have no material effect on the Group's consolidated financial statements.

*Amendments to IFRS 15, Revenue from Contracts with Customers (issued on 12 April 2016 and effective for annual periods beginning on or after 1 January 2018).* The amendments do not change the underlying principles of the Standard but clarify how those principles should be applied. The amendments clarify how to identify a performance obligation (the promise to transfer a good or a service to a customer) in a contract; how to determine whether a company is a principal (the provider of a good or service) or an agent (responsible for arranging for the good or service to be provided); and how to determine whether the revenue from granting a licence should be recognised at a point in time or over time. In addition to the clarifications, the amendments include two additional reliefs to reduce cost and complexity for a company when it first applies the new Standard.

The Group plans to apply the practical expedient available for simplified transition method: IFRS 15 is retrospectively applied only to the contracts that are not completed at the date of initial application (1 January 2018).

Based on the analysis of the Group's revenue streams for the year ended 31 December 2017 and individual contracts' terms and on the basis of the facts and circumstances that exist at that date, an impact on the consolidated financial statements from the adoption of the new standard on 1 January 2018 is not significant.

*IFRS 16 "Leases" (issued on 13 January 2016 and effective for annual periods beginning on or after 1 January 2019).* The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Group is currently assessing the impact of the amendments on its consolidated financial statements.

*IFRIC 22 - Foreign Currency Transactions and Advance Consideration (issued on 8 December 2016 and not yet endorsed in EU).* The interpretation addresses how to determine the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part thereof) on the derecognition of a non-monetary asset or non-monetary liability arising from an advance consideration in a foreign currency. Under IAS 21, the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part thereof) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine the date of the transaction for each payment or receipt of advance consideration. IFRIC 22 only applies in circumstances in which an entity recognises a non-monetary asset or non-monetary liability arising from an advance consideration. IFRIC 22 does not provide application guidance on the definition of monetary and non-monetary items. An advance payment or receipt of consideration generally gives rise to the recognition of a non-monetary asset or non-monetary liability, however, it may also give rise to a monetary asset or liability. An entity may need to apply judgment in determining whether an item is monetary or non-monetary. The Group is currently assessing the impact of the amendments on its consolidated financial statements.

*IFRIC 23 "Uncertainty over Income Tax Treatments" (issued on 7 June 2017 and not yet endorsed in EU).* IAS 12 specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. The interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. An entity should determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments based on which approach better predicts the resolution of the uncertainty. An entity should assume that a taxation authority will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations. If an entity concludes it is not probable that the taxation authority will accept an uncertain tax treatment, the effect of

## 5 New Accounting Pronouncements (Continued)

uncertainty will be reflected in determining the related taxable profit or loss, tax bases, unused tax losses, unused tax credits or tax rates, by using either the most likely amount or the expected value, depending on which method the entity expects to better predict the resolution of the uncertainty. An entity will reflect the effect of a change in facts and circumstances or of new information that affects the judgments or estimates required by the interpretation as a change in accounting estimate. Examples of changes in facts and circumstances or new information that can result in the reassessment of a judgment or estimate include, but are not limited to, examinations or actions by a taxation authority, changes in rules established by a taxation authority or the expiry of a taxation authority's right to examine or re-examine a tax treatment. The absence of agreement or disagreement by a taxation authority with a tax treatment, in isolation, is unlikely to constitute a change in facts and circumstances or new information that affects the judgments and estimates required by the Interpretation. The Group is currently assessing the impact of the amendments on its consolidated financial statements.

The following other new standards are not expected to have any material impact on the Group when adopted:

- Amendments to IFRS 15 - Revenue from Contracts with Customers (issued on 12 April 2016 and effective for annual periods beginning on or after 1 January 2018).
- Amendments to IFRS 2 - Share-based Payment (issued in 20 June 2016 and not yet endorsed in EU).
- IFRS 17 "Insurance Contracts" (issued on 18 May 2017 and not yet endorsed in EU).
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – Amendments to IFRS 10 and IAS 28 (issued on 11 September 2014 and not yet endorsed in EU).
- Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts - Amendments to IFRS 4 (issued on 12 September 2016 and effective, depending on the approach, for annual periods beginning on or after 1 January 2018 for entities that choose to apply temporary exemption option, or when the entity first applies IFRS 9 for entities that choose to apply the overlay approach).
- Transfers of Investment Property - Amendments to IAS 40 (issued on 8 December 2016 and not yet endorsed in EU).
- Annual Improvements to IFRSs 2014-2016 cycle – Amendments to IFRS 1 and IAS 28 (issued on 8 December 2016 and not yet endorsed in EU).
- Prepayment Features with Negative Compensation - Amendments to IFRS 9 (issued on 12 October 2017 and not yet endorsed in EU).
- Long-term Interests in Associates and Joint Ventures - Amendments to IAS 28 (issued on 12 October 2017 and not yet endorsed in EU).
- Annual Improvements to IFRSs 2015-2017 cycle - Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23 (issued on 12 December 2017 and not yet endorsed in EU).

Unless otherwise described above, the new standards and interpretations are not expected to affect significantly the Group's consolidated financial statements.

## 6 Critical Accounting Estimates and Judgements in Applying Accounting Policies

The Group makes estimates and assumptions that affect the amounts recognised in the consolidated financial statements and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

**Tax legislation.** Russian tax and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant authorities. Please see Note 24 for more details.

**Estimation of oil and gas reserves.** Engineering estimates of hydrocarbon reserves are inherently uncertain and are subject to future revisions. Accounting measures such as depreciation, depletion and amortization charges, impairment assessments and asset retirement obligations that are based on the estimates of proved reserves are subject to change based on future changes to estimates of oil and gas reserves.

Proved reserves are defined as the estimated quantities of hydrocarbons which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing

**6 Critical Accounting Estimates and Judgements in Applying Accounting Policies (Continued)**

economic conditions. Proved reserves are estimated by reference to available reservoir and well information, including production and pressure trends for producing reservoirs. Furthermore, estimates of proved reserves only include volumes for which access to market is assured with reasonable certainty. All proved reserves estimates are subject to revision, either upward or downward, based on new information, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As those fields are further developed, new information may lead to further revisions in reserve estimates. Reserves have a direct impact on certain amounts reported in the consolidated financial statements, most notably depreciation, depletion and amortization as well as impairment expenses. Depreciation rates on production assets using the units-of-production method for each field are based on proved developed reserves for development costs, and total proved reserves for costs associated with the acquisition of proved properties. Assuming all variables are held constant, an increase in proved developed reserves for each field decreases depreciation, depletion and amortization expenses. Conversely, a decrease in the estimated proved developed reserves increases depreciation, depletion and amortization expenses. Moreover, estimated proved reserves are used to calculate future cash flows from oil and gas properties, which serve as an indicator in determining whether or not property impairment is present. The possibility exists for changes or revisions in estimated reserves to have a significant effect on depreciation, depletion and amortization charges and, therefore, reported net profit/(loss) for the year.

The Group last obtained an independent reserve engineers report in June 2018 with the estimate of reserve as at 31 December 2017. As result, proved reserves estimates of the Okruzhnoye field determined by independent reserve engineers were revised significant downwards. Proved developed reserves estimates of the Okruzhnoye field were revised significant upwards. Petrosakh, that developed the Okruzhnoye field, earnings were affected by decrease in depreciation, depletion and amortization expense related to oil and gas properties in the amount of \$2.0 million and increase in depreciation, depletion and amortization expense related to costs associated with the acquisition of proved properties in the amount of \$0.7 million. Changes in proved reserves indicated the possibility of a impairment of Petrosakh properties' carrying values (Note 10).

**Deferred income tax asset recognition.** The recognised deferred tax asset represents income taxes recoverable through future deductions from taxable profits and is recorded in the consolidated statement of financial position. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. The future taxable profits and the amount of tax benefits that are probable in the future are based on the medium term business plan prepared by management and extrapolated results thereafter. The business plan is based on management expectations that are believed to be reasonable under the circumstances.

In April 2017 the Group completed an internal reorganisation of its subsidiaries. As part of the internal reorganisation, Petrosakh, the Group's operating company on Sakhalin Island and principal profit and cash generator, was merged with Urals Energy, the Russia-incorporated management company for all of the Group's operations, which is essentially a cost centre. As a result of this merger, the Group will be able to offset accumulated tax losses of Urals Energy against the future profits of Petrosakh for tax purposes. The accumulated tax losses transferred from Urals Energy to Petrosakh as a result of this reorganization amounted to \$65.4 million. Recognition of statutory tax loss carry forward in 2017 amounts to \$12.9 million (Note 14).

**Dismantlement provision.** Management makes provision for the future costs of decommissioning hydrocarbon production facilities, pipelines and related support equipment based on the best estimates of future cost and economic lives of those assets. Estimating future dismantlement provision is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future. Changes in the measurement of existing obligations can result from changes in estimated timing, future costs or discount rates used in valuation. Management believes that in 2016 and 2017 there were no reasonably possible change in any of the above key assumptions used that would have significant impact on the dismantlement provision recognised in these consolidated financial statements.

**Useful lives of non-oil and gas properties.** Items of non-oil and gas properties are stated at cost less accumulated depreciation. The estimation of the useful life of an asset is a matter of management judgement based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any of these conditions or estimates may result in adjustments to future depreciation rates.

**6 Critical Accounting Estimates and Judgements in Applying Accounting Policies (Continued)**

Useful lives applied to oil and gas properties may exceed the license term where management considers that licenses will be renewed. Assumptions related to renewal of licenses can involve significant judgment of management. Management believes that in 2016 and 2017 there were no reasonably possible changes in useful lives of non-oil and gas properties that would have significant impact on the depreciation charge recognised in these consolidated financial statements.

*Acquisition of companies.* Management applies judgements to determine whether the acquired entities represent business or assets. In making such judgements management considers whether the acquired entities are able to produce desired output, plan to produce outputs is being pursued, access to customers that will purchase the outputs can be obtained and employees, intellectual property, and other inputs and processes are present. Please refer to Note 27 for specific judgements applied in accounting of Arctic Oil Company acquisitions.

In accounting for business combinations, the purchase price paid to acquire a business is allocated to its assets and liabilities based on the fair values of the assets acquired and liabilities assumed as of the date of acquisition. A significant amount of judgment is involved in estimating the individual fair values of property, plant and equipment and identifiable intangible assets.

The Group hired external valuator to determine the fair values and economic useful lives of the acquired assets and liabilities. Fair value was calculated as the present value of projected future cash flows discounted by the rates reflecting the time value of money as at 29 August 2016 and the risk specific to the Arctic Oil Company. The external valuator applied discount rate 18.3%. Note 27 provides for the information on the finalization of 2016 business combination accounting.

The estimates used in determining fair values are based on projected cash flows believed to be reasonable but which are inherently uncertain. Accordingly, actual results may differ from the projected results used to determine fair value.

**7 Cash and cash equivalents**

	31 December	
	2017	2016
Cash at bank and on hand	683	465
Short-term bank deposits with maturities of 3 months or less	-	737
<b>Total cash and cash equivalents</b>	<b>683</b>	<b>1,202</b>

Based on Fitch's rating, the credit quality of Public Joint-Stock Company Sberbank of Russia in which the Group mostly held its cash and cash equivalents as at 31 December 2017 and 2016 is BBB-.

Based on Standard & Poor's rating, the credit quality of Public Joint-Stock Company Promsvyazbank in which the Group held its cash and cash equivalents as at 31 December 2017 and 2016 is B+ and BB-, accordingly.

**8 Accounts Receivable and Prepayments**

	31 December	
	2017	2016
Loans receivable	2,145	442
Trade and other accounts receivable	616	953
<b>Total financial assets</b>	<b>2,761</b>	<b>1,395</b>
Recoverable and prepaid taxes, including VAT	2,306	1,261
Advances to suppliers	1,533	933
Other	382	409
<b>Total accounts receivable and prepayments</b>	<b>6,982</b>	<b>3,998</b>

Included in total accounts receivable and prepayments are \$ 0.9 million and \$0.6 million at 31 December 2017 and 2016, respectively, denominated in US dollars and substantially all remaining amounts are denominated in Russian Roubles.

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**8 Accounts Receivable and Prepayments (Continued)**

As at 31 December 2017 advances to suppliers included advance in the amount \$1.0 million under the sale and lease back agreement of drilling rig. In April 2018 Petrosakh received the rig under the agreement. The Group intends using the rig for exploration South Dagi field.

In 2017 and 2016 the Group issued short-term loans to unrelated third parties at a market rate.

In 2016 the Group wrote-off prepaid expenses in the amount of \$0.5 million. The amount of this transaction was included in Other operating loss for the year ended 31 December 2016.

Trade accounts receivable arise primarily from sales to ongoing customers with standard payment terms. The category 'Other' primarily relates to prepaid amounts to customs and tax authorities, which will be returned to the Group either in cash or through an offset against future payments.

Changes in the provision for impairment of trade and other receivables were as follows:

	31 December	
	2017	2016
At 1 January	-	49
Use of provision	-	(59)
Effect of currency translation	-	10
<b>At 31 December</b>	<b>-</b>	<b>-</b>

The carrying values of trade and other receivables and loans issued approximate their fair value (Level 3 of fair value hierarchy). The maximum exposure to credit risk at the reporting date is the carrying value of each class of financial receivables mentioned above. The Group does not hold any collateral as security for trade and other receivables and loans issued (see Note 25 for credit risk disclosures).

As at 31 December 2017 and 2016 there were no past due, but not impaired accounts receivable.

**9 Inventories**

	31 December	
	2017	2016
Crude oil	5,132	6,718
Oil products	4,740	3,768
Materials and supplies	3,942	3,041
<b>Total inventories</b>	<b>13,814</b>	<b>13,527</b>

As at 31 December 2017 and 2016 the Group pledged its crude oil stored at Arcticneft's warehouse of \$1.5 million and \$2.0 million under loan agreements with Kamchatcomagroprombank (Note 15).

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**10 Property, Plant and Equipment**

<i>Cost at</i>	<b>Oil and gas properties</b>	<b>Refinery and related equipment</b>	<b>Buildings</b>	<b>Other Assets</b>	<b>Assets under construction</b>	<b>Total</b>
<b>1 January 2016</b>	77,893	3,827	388	3,219	3,020	88,347
Translation difference	16,308	792	78	732	400	18,310
Additions	2,250	198	-	463	1,539	4,450
Transfers	2,527	-	-	-	(2,527)	-
Capitalised borrowing costs (Note 15)	-	-	-	-	128	128
Acquisition of subsidiaries (Note 27)	1,734	-	-	1,208	-	2,942
Changes in estimates of dismantlement provision (Note 16)	(167)	-	-	-	-	(167)
Disposals	-	-	-	(437)	(33)	(470)
<b>31 December 2016</b>						
<b>Restated</b>	<b>100,545</b>	<b>4,817</b>	<b>466</b>	<b>5,185</b>	<b>2,527</b>	<b>113,540</b>
Translation difference	5,386	256	41	290	172	6,145
Additions	108	-	489	1,166	5,462	7,225
Transfers	1,921	-	713	-	(2,634)	-
Capitalised borrowing costs (Note 15)	-	-	-	-	108	108
Changes in estimates of dismantlement provision (Note 16)	584	(39)	-	-	-	545
Disposals	-	-	-	(117)	-	(117)
<b>31 December 2017</b>	<b>108,544</b>	<b>5,034</b>	<b>1,709</b>	<b>6,524</b>	<b>5,635</b>	<b>127,446</b>

In 2017 additions to assets under construction included purchase of drilling rig in the amount of \$2.2 million under the sale and lease back agreement (Note 11). The Group intends using the rig for exploration South Dagi field.

Additions to assets under construction included capitalised depreciation in the amount of \$100 thousand (for the year ended 31 December 2016: \$72 thousand).

The average capitalisation rate for the year ended 31 December 2017 is 13.68% (for the year ended 31 December 2016: 14.28%).

The Group recorded the change in estimate of dismantlement provision for oil and gas properties and for refinery and related equipment that was caused by revision of discount rate and its useful life in 2017 and by revision of discount and expected long-term inflation rates in 2016 (Note 16).

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**10 Property, Plant and Equipment (Continued)**

<i>Accumulated Depreciation, Amortisation and Depletion at</i>	<b>Oil and gas properties</b>	<b>Refinery and related equipment</b>	<b>Buildings</b>	<b>Other Assets</b>	<b>Assets under construction</b>	<b>Total</b>
<b>1 January 2016</b>	(31,099)	(1,927)	(326)	(1,885)	-	(35,237)
Translation difference	(6,796)	(411)	(68)	(348)	-	(7,623)
Depreciation	(4,857)	(214)	(22)	(310)	-	(5,403)
Disposals	-	-	-	376	-	376
<b>31 December 2016</b>						
<b>Restated</b>	(42,752)	(2,552)	(416)	(2,167)	-	(47,887)
Translation difference	(2,316)	(140)	(22)	(124)	-	(2,602)
Depreciation	(3,587)	(245)	(47)	(523)	-	(4,402)
Disposals	-	-	-	117	-	117
<b>31 December 2017</b>	(48,655)	(2,937)	(485)	(2,697)	-	(54,774)
<i>Net Book Value at</i>						
<b>31 December 2016</b>						
<b>Restated</b>	57,793	2,265	50	3,018	2,527	65,653
<b>31 December 2017</b>	59,889	2,097	1,224	3,827	5,635	72,672

As at 31 December 2017 and 2016 the Group pledged its property, plant and equipment in amount of \$3.6 million and \$3.0 million under loan agreements with PJSC Sberbank of Russia (Note 15).

Included within oil and gas properties at 31 December 2017 and 2016 were exploration and evaluation assets:

	<b>Cost at 31 December 2016 Restated</b>	<b>Additions</b>	<b>Translation difference</b>	<b>Cost at 31 December 2017</b>
<i>Exploration and evaluation assets</i>				
Petrosakh	17,783	101	945	18,829
Arcticneft	8,947	-	473	9,420
BVN-Oil	5,284	-	280	5,564
RK-Oil	474	-	26	500
<b>Total cost of exploration and evaluation assets</b>	<b>32,488</b>	<b>101</b>	<b>1,724</b>	<b>34,313</b>
	<b>Cost at 1 January 2016</b>	<b>Additions</b>	<b>Translation difference</b>	<b>Cost at 31 December 2016 Restated</b>
<i>Exploration and evaluation assets</i>				
Petrosakh	12,871	2,098	2,814	17,783
Arcticneft	7,448	-	1,499	8,947
BVN-Oil	4,257	152	875	5,284
RK-Oil	395	-	79	474
<b>Total cost of exploration and evaluation assets</b>	<b>24,971</b>	<b>2,250</b>	<b>5,267</b>	<b>32,488</b>

At the each reporting date management assess whether there is any indication that the recoverable value has declined below the carrying value of property, plant and equipment. As at 31 December 2017 management considered the result of the latest independent reserve engineers' report and noted a decrease of total proved reserves for Okruzhnoe field. This decrease was considered by management as impairment indicator and impairment test of Petrosakh assets was performed at as 31 December 2017. As at 31 December 2016 management considered continuing deterioration in economic environment and volatility of oil prices as impairment indicators.

The Group conducted impairment test assessing whether the carrying amount of cash-generating unit related to Okruzhnoe field exceeds its recoverable amount. The recoverable amount has been determined as value in use of respective assets. The value in use of cash-generating unit has been calculated as the present values of projected future cash flow discounted using the rate derived from the weighted average cost of capital of the Group, as

**10 Property, Plant and Equipment (Continued)**

adjusted, where applicable, to take into account any specific risks of business operations related to the cash-generating unit. Key assumptions for impairment test are a 14.5% discount rate, an average oil price of \$59 for 2018, \$61 for 2019, \$65 for 2020, \$71 for 2021, \$76 for 2022, \$80 for 2023, \$82 for 2024 and \$83 in real terms for future sales. Based on the results of the impairment test the Group did not identify impairment. Estimated production volumes are based on detailed data for the fields and take into account development plans for the fields agreed by management as part of the long-term planning process. Consequently, management believes no reasonably possible change in the production and discount rate assumption would cause the carrying amount of non-current assets to exceed their recoverable amount.

No impairment was recognized in respect of property, plant and equipment in 2017 and 2016.

The Group's oil fields are located in the Russian Federation on land owned by the Russian government. The Group holds production licenses and pays production taxes to extract oil and gas from the fields. The licenses expire between 2018 and 2067 and may be extended. Management intends to renew the licenses as the properties are expected to remain productive subsequent to the license expiration date.

Estimated costs of dismantling oil and gas production facilities, including abandonment and site restoration costs, amount to \$1.3 million and \$0.3 million at 31 December 2017 and 2016, respectively, are included in the cost of oil and gas properties. The Group has estimated its liability based on current environmental legislation using estimated costs when the expenses are expected to be incurred.

In 2017 the Group paid \$101 thousand of capital expenditure related to additions to exploration and evaluation assets (for the year ended 31 December 2016: \$201 thousand).

On 15 June 2016 the Company was awarded a 25 year exploration and development licence for the South Dagi oil field on Sakhalin Island, following an auction by the Russian State Authorities. The licence, with an area of 27.8 sq. kms, was the subject of an earlier exploration and appraisal programme in the 1970s, followed by additional seismic work done in the middle of 1990s and 2007. During these periods two exploratory and six appraisal wells were drilled.

The auction bid price payable by the Company is Russian Roubles 134.6 million, equivalent to US\$2.1 million. The funding of this transaction was made from the Company's existing capital resources. The transaction was made as a part of the Company's strategy to acquire licences and defer significant development decisions until conditions (oil price, exchange rates and taxes) become more favourable.

The Group leases certain items within oil and gas properties under a number of finance lease agreements. The Group classified these leases as finance lease based on contract terms that include transfer of ownership rights at the end of contract.

As at 31 December 2017 cost of the leased assets amounted to \$1,807 thousand (2016: \$1,406 thousand). Accumulated depreciation for the leased assets as at 31 December 2017 amounted to \$904 thousand (2016: \$674 thousand). Additions of the leased assets amounted to \$322 thousand (for the year ended 31 December 2016: \$200 thousand).

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**10 Property, Plant and Equipment (Continued)**

Future minimum lease payments were as follows:

	31 December 2017		
	Minimum lease payments	Future finance charges	Present value of minimum lease payments
Financial lease obligations payable			
Less than one year	374	129	245
Between one year and five years	665	229	436
More than five years	389	123	266
<b>Total</b>	<b>1,428</b>	<b>481</b>	<b>947</b>

  

	31 December 2016		
	Minimum lease payments	Future finance charges	Present value of minimum lease payments
Financial lease obligations payable			
Less than one year	225	112	113
Between one year and five years	666	313	353
More than five years	469	108	361
<b>Total</b>	<b>1,360</b>	<b>533</b>	<b>827</b>

**11 Other Non-Current Assets**

	31 December	
	2017	2016
Advances to contractors and suppliers for construction in process	456	119
Intangible assets	88	73
<b>Total other non-current assets</b>	<b>544</b>	<b>192</b>

**12 Accounts Payable and Accrued Expenses**

	31 December	
	2017	2016
Accounts payable for non-current assets	2,804	15
Trade payables	280	478
Short-term finance lease obligations	245	113
Other payable and accrued expenses	665	162
<b>Total financial liabilities</b>	<b>3,994</b>	<b>768</b>
Wages and salaries	1,043	935
<b>Total accounts payable and accrued expenses</b>	<b>5,037</b>	<b>1,703</b>

Total accounts payable and accrued expenses in the amount of \$ 0.3 million and \$0.2 million at 31 December 2017 and 2016, respectively, are denominated in US dollars. Substantially all remaining amounts are denominated in Russian Roubles.

As at 31 December 2017 accounts payable for non-current assets included payables in the amount \$2.7 million under the sale and lease back agreement of drilling rig (Note 11).

In 2016 the Group wrote-off Trade payables and Accounts payable for non-current assets in the amount of \$112 thousand. The amount of these transactions were included in Other operating (loss)/profit for the year ended 31 December 2016.

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**13 Provisions**

	Provision on claims	Provision for severance	Total
<b>1 January 2016</b>	-	-	-
Addition due to acquisition of subsidiary (Note 27)	-	223	223
Accrual of provision for legal claims	138	-	138
Use of provision	-	(116)	(116)
Increase of provision due to exchange difference	14	7	21
<b>31 December 2016</b>	<b>152</b>	<b>114</b>	<b>266</b>
Use of provision	(152)	(114)	(266)
<b>31 December 2017</b>	-	-	-

In 2016 the Group accrued provision for legal claims amounting to \$0.1 million. The amount of this transaction in 2016 included in Other operating loss for the year.

In 2017 the Group acknowledged and accrued payables in the amount of provision accrued in 2016.

**14 Taxes**

Income taxes for the years ended 31 December 2017 and 2016 comprised the following:

	Year ended 31 December	
	2017	2016
Current tax expense/(benefit)	590	(2,103)
Deferred tax benefit	(12,816)	(22)
<b>Income tax benefit</b>	<b>(12,226)</b>	<b>(2,125)</b>

Below is a reconciliation of profit before tax to income tax charge:

	Year ended 31 December	
	2017	2016
<b>Profit before income tax</b>	<b>1,822</b>	<b>6,191</b>
Theoretical charge at the statutory rate of 20%	364	1,238
Recognition of statutory tax loss carry forward, net	(12,564)	(724)
Reversal of uncertain tax position provision	-	(2,684)
Effects of different tax rate	(116)	2
Unrecognised tax loss carry forward for the year	232	-
Other non-deductible (income)/ expenses, net of non-taxable (income)/expenses	(142)	43
<b>Income tax benefit</b>	<b>(12,226)</b>	<b>(2,125)</b>
<b>Effective tax rate</b>	<b>-671%</b>	<b>-34.3%</b>

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**14 Taxes (Continued)**

The movements in deferred tax assets and liabilities during the years ended 31 December 2017 were as follows:

	31 December 2017	Recognized in equity for translation differences	Credited/(charged) to the profit and loss section of consolidated Statement of profit or loss and other comprehensive income	31 December 2016
<i>Deferred income tax liabilities</i>				
Property, plant and equipment	(8,306)	(422)	93	(7,977)
Inventories	(1,247)	(65)	29	(1,211)
<i>Deferred income tax assets</i>				
Tax losses	17,200	390	12,564	4,246
Dismantlement provision	560	23	159	378
Payables	158	8	(7)	157
Provisions	-	1	(22)	21
<b>Net deferred income tax liabilities</b>	<b>-</b>	<b>(183)</b>	<b>4,834</b>	<b>(4,651)</b>
<b>Net deferred income tax assets</b>	<b>8,365</b>	<b>118</b>	<b>7,982</b>	<b>265</b>
<b>Net deferred income tax assets/(liabilities)</b>	<b>8,365</b>	<b>(65)</b>	<b>12,816</b>	<b>(4,386)</b>

The movements in deferred tax assets and liabilities during the years ended 31 December 2016 were as follows:

	31 December 2016	Recognized in equity for translation differences	Credited/(charged) to the profit and loss section of consolidated Statement of profit or loss and other comprehensive income	Acquisition of subsidiary (Note 27)	31 December 2015
<i>Deferred income tax liabilities</i>					
Property, plant and equipment	(7,977)	(1,319)	166	(310)	(6,514)
Inventories	(1,211)	(179)	(415)	146	(763)
<i>Deferred income tax assets</i>					
Dismantlement provision	378	49	4	131	194
Payables	157	27	243	(188)	75
Tax losses	4,246	708	49	-	3,489
Provisions	21	1	(25)	45	-
<b>Net deferred income tax liabilities</b>	<b>(4,651)</b>	<b>(735)</b>	<b>(124)</b>	<b>(273)</b>	<b>(3,519)</b>
<b>Net deferred income tax assets</b>	<b>265</b>	<b>22</b>	<b>146</b>	<b>97</b>	<b>-</b>
<b>Net deferred income tax liabilities</b>	<b>(4,386)</b>	<b>(713)</b>	<b>22</b>	<b>(176)</b>	<b>(3,519)</b>

The amount of deferred tax assets and liabilities that will be settled in 2018 is not significant.

Starting from 1 January 2017 the amendments to the Russian tax legislation became effective in respect of tax loss carry forwards. The amendments affect tax losses incurred and accumulated since 2007 that have not been utilised. The 10-year expiry period for tax loss carry-forwards no longer applies. The amendments also set limitation on utilisation of tax loss carry forwards that will apply during the period from 2017 to 2020. The amount of losses that can be utilised each year during that period is limited to 50% of annual taxable profit. The amendments have a positive effect on the Group's consolidated financial statements. The Group expects to utilise substantially all tax losses carried forward.

The Company is subject to corporation tax on taxable profits at the rate of 12.5%. Under certain conditions interest expense may be exempt from income tax and be subject only to special contribution for defense at the rate of 30%. In certain cases dividends received from abroad may be subject to defense contribution at the rate of 17%.

Most of the individual operating entities are taxed in the Russian Federation at the rate of 20%.

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**14 Taxes (Continued)**

In the context of the Group's current structure, tax losses and current tax assets of different group companies may not be offset against current tax liabilities and taxable profits of other group companies and, accordingly, taxes may accrue even where there is a consolidated tax loss. Therefore, deferred tax assets and liabilities are offset only when they relate to the same taxable entity. At 31 December 2017 and 2016, deferred tax assets of \$2.3 million and \$13.8 million, respectively, have not been recognized for deductible temporary differences for which it is not probable that sufficient taxable profit will be available to allow the benefit of that deferred tax assets to be utilised. Accumulated tax losses were \$97.1 million and \$90.1 million at 31 December 2017 and 2016, respectively.

Other taxes payable at 31 December 2017 and 2016 were as follows:

	31 December	
	2017	2016
Mineral extraction tax	3,373	2,324
VAT	1,990	2,060
Excise	759	1,103
Other taxes payable	266	410
<b>Total other taxes payable</b>	<b>6,388</b>	<b>5,897</b>

In 2016 the Group accrued penalties and fines related taxes amounting to \$0.1 million. The amount of these transactions in 2016 included in Other operating (loss)/profit for the period.

**15 Borrowings**

*Long-term and short-term borrowings.* Long-term and short-term borrowings were as follows at 31 December 2017 and 2016:

	31 December	
	2017	2016
<i>Long-term borrowings</i>		
Sberbank		
- Principal	4,236	4,121
- Interest	17	20
Transnational Bank		
- Principal	1,696	1,611
- Interest	767	456
Other	180	122
<b>Subtotal</b>	<b>6,896</b>	<b>6,330</b>
Less: current portion of long-term borrowings	(5,780)	(2,087)
<b>Total long-term borrowings</b>	<b>1,116</b>	<b>4,243</b>
<i>Short-term borrowings</i>		
Kamchatcomagroprombank	3,038	462
<b>Subtotal</b>	<b>3,038</b>	<b>462</b>
Plus: current portion of long-term borrowings	5,780	2,087
<b>Total short-term borrowings</b>	<b>8,818</b>	<b>2,549</b>
<b>Total borrowings</b>	<b>9,934</b>	<b>6,792</b>

On 19 November 2015, the Group acquired two private Russian companies, OOO RK-Oil and OOO BVN Oil that carried long-term and short-term borrowings in the amount of \$1.8 million including loans of Transnational Bank in the amount of \$1.7 million at an interest rate 15-20% per annum due for repayment from November 2018 to January 2019.

In April 2015, Transnational Bank lost its Central Bank of Russia license and started to be managed by The State Corporation Deposit Insurance Agency in accordance with established procedure in the Russian Federation. After this event legal owners of the bank cannot participate in the decision making process of the bank. Loss of the licence by

## **15 Borrowings (Continued)**

Transnational bank did not change the terms of long term loans of OOO RK-Oil and OOO BVN Oil, and such changes are not expected. The companies suspended loan interest payments in 2015, following the bank's license being revoked. In 2016, the State Corporation Deposit Insurance Agency filed a lawsuit against BVN-Oil for breach of the respective loan agreements' terms and claiming immediate repayment of the principal, accrued interest and penalties for non-payment of the loan interest. In 2016, the Group recorded a provision in relation to this lawsuit. In 2017, the provision was used in full (Note 13).

On 20 September 2016 Petrosakh entered into an 18 month revolving credit facility with the Sakhalin branch of PJSC Sberbank of Russia ("Sberbank") for a total amount of 300 million Roubles (representing approximately US\$4.6 million at prevailing exchange rates) to Petrosakh for working capital financing.

The key terms of the loan are as follow:

- it is repayable on 19 March 2018 (the agreement also provides for early repayment of the loan without incurring any penalties);
- interest is chargeable at the rate of 13% plus 1%. The lowest rate of 13% is subject to Petrosakh meeting monthly turnover targets and having average cash balances in its bank account;
- it is secured by way of a pledge over property (Note 10) and cash flows from Petrosakh.

On 14 February 2017 Petrosakh has entered into a new 24 month non-revolving credit facility with the Sakhalin branch of PJSC Sberbank of Russia. Under the loan agreement, Sberbank will provide, by way of several tranches, the amount of 50 million Roubles (representing approximately \$0.9 million at prevailing exchange rates) to Petrosakh. The interest rate under the loan agreement is 15.6% plus 1%. The lowest rate of 15.6% is subject to Petrosakh meeting certain conditions. The loan is secured by property, plant and equipment of Petrosakh.

On 26 September 2017 Petrosakh has entered into a new 36 month non-revolving credit facility with the Sakhalin branch of PJSC Sberbank of Russia. Under the loan agreement, Sberbank will provide, by way of several tranches, the amount of 70 million Roubles (representing approximately \$1.2 million at prevailing exchange rates) to Petrosakh. The interest rate under the loan agreement is 11% plus 1%. The lowest rate of 11% is subject to Petrosakh meeting certain conditions. The loan is secured by property, plant and equipment of Petrosakh.

On 30 October 2017 Petrosakh has entered into a new 36 month non-revolving credit facility with the Sakhalin branch of PJSC Sberbank of Russia. Under the loan agreement, Sberbank will provide, by way of several tranches, the amount of 30 million Roubles (representing approximately \$0.5 million at prevailing exchange rates) to Petrosakh. The interest rate under the loan agreement is 11% plus 1%. The lowest rate of 11% is subject to Petrosakh meeting certain conditions. The loan is secured by property, plant and equipment of Petrosakh.

On 26 December 2016 Arcticneft signed an agreement to raise a short-term non-revolving secured credit facility with Kamchatcomagroprombank. Total amount of the credit facility is 40 million Roubles (representing approximately US\$0.7 million at prevailing exchange rates). As of 31 December 2016 the company had drawn down US\$462 thousand. The loan is repayable on 31 August 2017. Interest is chargeable at 15%. The Company pledged its 7 thousand tons of crude oil stored at AO Arcticneft's warehouse under the loan agreement with Kamchatcomagroprombank.

On 2 March 2017 Arcticneft has entered into a new short-term non-revolving credit facility with Kamchatcomagroprombank. Under the loan agreement the bank will provide a total of 30 million Roubles (representing approximately \$0.5 million at prevailing exchange rates) to Arcticneft, via several tranches. Interest is chargeable at the rate 15%. Arcticneft pledged crude oil stored at its warehouse under the loan agreement with Kamchatcomagroprombank. The proceeds of this new loan will be used by Arcticneft for its general working capital financing. The loan is repayable in August 2017.

On 20 April 2017 Arcticneft has entered into a new short-term non-revolving credit facility with Kamchatcomagroprombank. Under the loan agreement the bank will provide a total of 30 million Roubles (representing approximately \$0.5 million at prevailing exchange rates) to Arcticneft, via several tranches. Interest is chargeable at the rate 15%. Arcticneft pledged crude oil stored at its warehouse under the loan agreement with Kamchatcomagroprombank. The proceeds of this new loan will be used by Arcticneft for its general working capital financing. The loan is repayable in August 2017.

On 10 August 2017 Arcticneft has entered into a new short-term non-revolving credit facility with Kamchatcomagroprombank. Under the loan agreement the bank will provide a total of 130 million Roubles (representing approximately \$2.3 million at prevailing exchange rates) to Arcticneft, via several tranches. Interest is

**15 Borrowings (Continued)**

chargeable at the rate 14%. Arcticneft pledged crude oil stored at its warehouse under the loan agreement with Kamchatcomagroprombank. The proceeds of this new loan will be used by Arcticneft for its general working capital financing. The loan is repayable in August 2018.

On 18 October 2017 Arcticneft has entered into a new short-term non-revolving credit facility with Kamchatcomagroprombank. Under the loan agreement the bank will provide a total of 10 million Roubles (representing approximately \$0.2 million at prevailing exchange rates) to Arcticneft, via several tranches. Interest is chargeable at the rate 14%. Arcticneft pledged crude oil stored at its warehouse under the loan agreement with Kamchatcomagroprombank. The proceeds of this new loan will be used by Arcticneft for its general working capital financing. The loan is repayable in August 2018.

On 25 October 2017 Arcticneft has entered into a new short-term non-revolving credit facility with Kamchatcomagroprombank. Under the loan agreement the bank will provide a total of 35 million Roubles (representing approximately \$0.6 million at prevailing exchange rates) to Arcticneft, via several tranches. Interest is chargeable at the rate 14%. Arcticneft pledged crude oil stored at its warehouse under the loan agreement with Kamchatcomagroprombank. The proceeds of this new loan will be used by Arcticneft for its general working capital financing. The loan is repayable in August 2018.

***Petraco***

In May 2016 the Company obtained a short-term secured loan from Petraco in the amount of US\$6.0 million at an interest rate of six months Libor plus 5% per annum due on the 30 day after the date of next tanker shipment. From the date of the next tanker shipment the interest rate is six month Libor plus 2% per annum. The Company pledged its 100% shares in its subsidiary AO Arcticneft and 22 thousand tons of crude oil stored at AO Arcticneft's warehouse under the loan agreement with Petraco. The loan including the accrued interest was fully paid as a result of the non-cash settlement transactions with trade receivables due to crude oil sales to Petraco in August 2016.

In April 2017 Company the Company entered into a pre-export short term loan finance arrangement with Petraco under which Petraco will advance the sum of \$5.9 million at an interest rate of three months Libor plus 5% per annum due on the 30 day after the date of next tanker shipment. From the date of the next tanker shipment the interest rate is three month Libor plus 2% per annum. Company pledged its 100% shares in its subsidiary AO Arcticneft under the loan agreement with Petraco.

On 7 September 2017, the Company entered into a pre-export short term loan finance arrangement with Petraco under which Petraco will advance the sum of US\$5.6 million to the Company ahead of the anticipated October 2017 tanker shipment from Kolguev Island.

The loans including the accrued interest was fully paid as a result of the non-cash settlement transactions with trade receivables due to crude oil sales to Petraco in July and in October 2017.

The carrying values of borrowings approximate their fair value.

Other than stated above, the Group is in compliance with the debt covenants under loan agreements as of 31 December 2017 and 2016.

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**15 Borrowings (Continued)**

*Interest income and expense.* Interest income and expense for the years ended 31 December 2017 and 2016, respectively, comprised the following:

	Year ended 31 December	
	2017	2016
<b>Interest income</b>		
Loans receivable	54	23
Interest on deposits	18	27
<b>Total interest income</b>	<b>72</b>	<b>50</b>
Interest on loan from Sberbank	(706)	(490)
Interest on loans from OOO KB Transnational Bank	(293)	(253)
Change in dismantlement provision due to unwinding of discount (Note 16)	(252)	(179)
Interest on loans from Kamchatcomagroprombank	(247)	(91)
Finance leases	(131)	(84)
Interest on loan from Petraco Oil Company Limited	(96)	(102)
Interest on other loans	(9)	(7)
Less: capitalised in PP&E (Note 10)	108	128
<b>Total interest expense</b>	<b>(1,626)</b>	<b>(1,078)</b>
<b>Net finance cost</b>	<b>(1,554)</b>	<b>(1,028)</b>

*Weighted average interest rate.* The Group's weighted average interest rates on borrowings was 13.68% and 14.28% at 31 December 2017 and 2016, respectively.

*Reconciliation of liabilities arising from financing activities.* The movements in the Group's liabilities arising from financing activities for the year ended 31 December 2017 are as follows:

	Short-term and long-term debt	Finance lease	Other liabilities from financing activities	Total
<b>As of 31 December 2016</b>	<b>6,792</b>	<b>827</b>	<b>-</b>	<b>7,619</b>
Cash flows, including:				
Proceeds from borrowings	18,151	-	-	18,151
Repayment of borrowings	(4,284)	-	-	(4,284)
Interest paid	(956)	(131)	-	(1,087)
Finance lease principal payments	-	(246)	-	(246)
Dividends paid to the Company's shareholders	-	-	(783)	(783)
Interest accrued	1,351	131	-	1,482
Assets received under finance lease	-	322	-	322
Non-cash settlement transactions with trade receivables	(11,546)	-	-	(11,546)
Dividends declared	-	-	783	783
Effect of currency translation	426	44	-	470
<b>Balance at 31 December 2017</b>	<b>9,934</b>	<b>947</b>	<b>-</b>	<b>10,881</b>

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**15 Borrowings (Continued)**

	Short-term and long-term debt	Finance lease	Total
<b>As of 1 January 2016</b>	<b>3,935</b>	<b>611</b>	<b>4,546</b>
Cash flows, including:			
<i>Proceeds from borrowings</i>	13,636	-	13,636
<i>Repayment of borrowings</i>	(6,459)	-	(6,459)
<i>Interest paid</i>	(695)	(84)	(779)
<i>Finance lease principal payments</i>	-	(55)	(55)
Interest accrued	943	84	1,027
Assets received under finance lease	-	200	200
Non-cash settlement transactions with trade receivables	(6,102)	-	(6,102)
Business combinations	482	-	482
Effect of currency translation	1,052	71	1,123
<b>As of 31 December 2016</b>	<b>6,792</b>	<b>827</b>	<b>7,619</b>

**16 Dismantlement Provision**

The dismantlement provision represents the net present value of the estimated future obligation for dismantlement, abandonment and site restoration costs which are expected to be incurred at the end of the production lives of the oil and gas fields, which vary from 10 to 52 years depending on the field and type of assets. Nominal discount rate was 9.3% and 14.5% as of 31 December 2017 and 2016, respectively. The revision of nominal discount rate was caused by improvements in current economic situation in Russia.

	Year ended 31 December	
	2017	2016 Restated
Opening dismantlement provision	1,892	971
Changes in estimates	545	(167)
Unwinding of discount (Note 15)	252	179
Translation difference	113	256
Addition due to acquisition of subsidiary (Note 27)	-	653
<b>Closing dismantlement provision</b>	<b>2,802</b>	<b>1,892</b>

As further discussed in Note 24, environmental regulations and their enforcement are being developed by governmental authorities. Consequently, the ultimate dismantlement, abandonment and site restoration obligation may differ from the estimated amounts, and this difference could be significant.

**17 Equity**

At 31 December 2017 and 2016 authorised share capital was \$1,890 thousand divided into 15 million shares of \$0.126 each.

	Number of shares (thousand of shares)	Share capital	Share premium	Difference from conversion of share capital to USD
<b>Balance at 1 January 2016</b>	<b>252,446</b>	<b>1,589</b>	<b>656,968</b>	<b>(113)</b>
<b>Balance at 31 December 2016</b>	<b>252,446</b>	<b>1,589</b>	<b>656,968</b>	<b>(113)</b>
<b>Balance at 31 December 2017</b>	<b>12,622</b>	<b>1,589</b>	<b>-</b>	<b>(113)</b>

**17 Equity (Continued)**

The Share premium is not available for distribution by way of dividend.

On 26 May 2017 shareholders approved a reduction of the Company's share premium account from \$656,968,491 to nil by writing off the losses of the Company equivalent to this reduction of share premium account.

On 9 November 2017 the Company's annual general meeting approved a dividend on the ordinary shares for the year ended 31 December 2016 in the amount of \$0.062 per ordinary share. Dividends were fully paid in November 2017.

**Profit/(loss) per share.** Basic profit/(loss) per share is calculated by dividing the profit/(loss) attributable to equity holders of the company by the weighted average number of ordinary shares in issue during the year.

On 26 May 2017 shareholders approved the Company's share consolidation: the 252,446,060 existing ordinary shares of nominal value \$0.0063 each in the issued share capital of the Company have been consolidated and divided into 12,622,303 new ordinary shares of nominal value \$0.126 each, effective on 30 May 2017. Basic and diluted earnings per share for year ended 31 December 2017 and 2016 were adjusted retrospectively.

**Performance Share Plan.** On 20 January 2017 the Company announced the granting of conditional share awards over a total of 656,360 new ordinary shares of \$0.126 each in the capital of the Company, pursuant to the Company's performance share plan.

Grants of Conditional Share Awards have been made to a total of seven employees, including members of the Company's Board and certain key employees within the Group's subsidiaries. In aggregate, the Performance Shares represent 5.2 per cent of the Company's current issued ordinary share capital. For the time being, the Board intends to retain the balance of a further 4.8 per cent of the Company's current issued ordinary share capital, which is approved under the Performance Share Plan.

The performance Share Plan is conditional on the establishment of certain KPI indicators. To date the KPI indicators have not been established, therefore the management is of the view that there is no service commencement date.

The Conditional Share Awards would only vest once the Board has determined that certain key performance indicators allocated to the individuals have been achieved. The KPIs in all cases will relate to performance in the underlying operations and developments achieved by the Group.

On 10 January 2018 the Remuneration committee of the Company passed a resolution to postpone the Plan.

The weighted average number of ordinary shares issued was calculated as following:

	Year ended 31 December	
	2017	2016
Balance at 1 January		
Weighted average number of ordinary shares in issue	12,622,303	12,622,303

	Year ended 31 December	
	2017	2016
Profit attributable to equity holders of the Company	14,209	8,225
Weighted average shares outstanding (thousands) attributable to:		
- Basic shares	12,622	12,622
- Diluted shares	12,622	12,622
Basic profit per share (in US dollar per share)	1.13	0.65
Diluted profit per share (in US dollar per share)	1.13	0.65

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**18 Non-controlling interest**

In April 2017 the Group completed an internal reorganisation of its subsidiaries: Petrosakh merged Urals Energy, the Russia-incorporated management company for all of the Group's operations. As a result of reorganization a share of non-controlling interest decrease from 2.8% to 1.44%.

The following table summarises the consolidated information relating to the significant Group's subsidiary, AO Petrosakh, with a non-controlling interest that is material to the Group:

	Year ended 31 December	
	2017	2016
Share of non-controlling interest*	1.44%	2.8%
(Loss)/profit attributable to non-controlling interest	(161)	91
Effect of currency translation	21	128
Accumulated non-controlling interest in the subsidiary	626	766

\* Share of non-controlling interest is equal to the proportion of voting rights held by the non-controlling interest.

Country of primary operation of AO Petrosakh is Russia.

	As of and for the year ended	
	31 December 2017	31 December 2016
Current assets	20,900	16,301
Non-current assets	48,959	35,750
Current liabilities	10,862	6,946
Non-current liabilities	15,520	18,139
Revenue	28,144	21,501
Profit for the year	15,241	3,280
Total comprehensive income/(loss) for the year	16,699	7,787
Net cash from/(used in):		
operating activities	6,171	4,619
investing activities	(6,630)	(5,564)
financing activities	(185)	585

AO Petrosakh did not distribute dividends during the years ended 31 December 2017 and 2016.

**19 Revenues**

	Year ended 31 December	
	2017	2016
Crude oil		
Export sales	21,567	9,831
Domestic sales (Russian Federation)	1,806	1,986
Petroleum (refined) products – domestic sales	30,797	23,349
Other sales	84	143
<b>Total proceeds from sales</b>	<b>54,254</b>	<b>35,309</b>
Less: excise taxes	(5,336)	(3,754)
Less: export duties	(4,742)	(2,503)
<b>Revenues after excise taxes and export duties</b>	<b>44,176</b>	<b>29,052</b>

All of the Group's export crude oil sales are made to one customer – Petraco, with whom the Group was trading for the past several years. The customer is a trader, sales are made purely on market terms, the title over the oil sold passes upon tanker loading and, accordingly, management does not monitor the ultimate consumers of its export sales.

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**20 Segment information**

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

The CODM receives monthly IFRS based financial information for its production entities. There were three production entities in 2017 and in 2016. Management has determined that the operations of these production entities are sufficiently homogenous, operating segments display similar economic characteristics and, therefore, they can be aggregated for the purpose of IFRS 8. CODM does not review performance of RK oil and BVN oil on regular basis as production on these entities has not started. Therefore, these entities do not represent operating or reportable segments. The Group has other entities that engage as either head office / corporate or as holding companies. Consequently, management has concluded that due to the above aggregation criteria there is only one reportable segment.

**Geographical information.** The Group operates in two major geographical areas of the world. In the Russian Federation, its home country, the Group is mainly engaged in the exploration, development, extraction and sales of crude oil, and refining and sale of oil products. Activities outside the Russian Federation are restricted to sales activities where title passes upon tanker loading. Sales are made to Europe (sales of crude oil). Information on the geographical location of the Group's revenues is set out below.

For the year ended 31 December 2017:

	Russian Federation	Europe	Total
Crude oil	1,806	21,567	23,373
Petroleum (refined) products	30,797	-	30,797
Other sales	84	-	84
<b>Total proceeds from sales</b>	<b>32,687</b>	<b>21,567</b>	<b>54,254</b>
Less: excise taxes	(5,336)	-	(5,336)
Less: export duties	-	(4,742)	(4,742)
<b>Revenues after excise taxes and export duties</b>	<b>27,351</b>	<b>16,825</b>	<b>44,176</b>

For the year ended 31 December 2016:

	Russian Federation	Europe	Total
Crude oil	1,986	9,831	11,817
Petroleum (refined) products	23,349	-	23,349
Other sales	143	-	143
<b>Total proceeds from sales</b>	<b>25,478</b>	<b>9,831</b>	<b>35,309</b>
Less: excise taxes	(3,754)	-	(3,754)
Less: export duties	-	(2,503)	(2,503)
<b>Revenues after excise taxes and export duties</b>	<b>21,724</b>	<b>7,328</b>	<b>29,052</b>

Revenue from external customers is based on the geographical location of customers although all revenues are generated by assets in the Russian Federation. Substantially all of the Group's assets are located in the Russian Federation. Excise taxes relate to petroleum products, export duties – to crude oil.

**Major customers.** For the year 2017, the Group has one major customer to whom individual revenues represent 38 percent of total external revenues (2016: one major customer that represented 28 percent).

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**21 Cost of Sales**

	Year ended 31 December	
	2017	2016
Mineral extraction tax	13,401	8,563
Materials	7,446	4,500
Wages and salaries (including payroll taxes of \$1.4 million and \$1.2 million for the years ended 31 December 2017 and 2016, respectively)	7,360	5,408
Depreciation, depletion and amortisation	4,288	5,331
Oil treating, storage and other services	1,306	982
Other taxes	365	282
Utilities and repair services	78	143
Rent	74	120
Other	186	261
Change in finished goods	1,157	(3,795)
<b>Total cost of sales</b>	<b>35,661</b>	<b>21,795</b>

**22 Selling, General and Administrative Expenses**

	Year ended 31 December	
	2017	2016
Wages and salaries (including payroll taxes of \$0.3 million and \$0.2 million for the years ended 31 December 2017 and 2016, respectively)	2,403	1,697
Transport and shipment services	1,065	878
Loading services	637	215
Office rent	429	359
Professional consultancy fees	410	272
Materials	313	205
Office expenses	197	102
Audit fees	184	151
Trip expenses and communication services	169	166
Insurance	74	55
Other expenses	199	258
<b>Total selling, general and administrative expenses</b>	<b>6,080</b>	<b>4,358</b>

The audit fee stated above include \$41 thousand (2016: \$40 thousand) charged by the Company's statutory audit firm. The professional services stated above include fees of \$18 thousand (2016: \$1 thousand) for tax consultancy services and \$7 thousand (2016: \$6 thousand) for other non-assurance services charged by the Company's statutory audit firm.

**23 Foreign currency gain/(loss)**

	Year ended 31 December	
	2017	2016
Net foreign exchange gain on financing activities, including:		
- foreign exchange gain	904	4,763
- foreign exchange loss	2,307	8,175
	(1,403)	(3,412)
Net foreign exchange gain on operating activities, including:		
- foreign exchange gain	84	151
- foreign exchange loss	809	569
	(725)	(418)
<b>Total foreign currency gain</b>	<b>988</b>	<b>4,914</b>

Net foreign exchange gain/(loss) on financing activities is related to loans between the Group entities. Loans between the Group entities and related foreign exchange gains or losses are eliminated upon consolidation. However, where the loan is between the Group entities that have different functional currencies, the foreign exchange gain or loss cannot be eliminated in full and is recognized in the consolidated profit or loss.

**24 Contingencies, Commitments and Operating Risks**

**Operating Environment. Russian Federation.** The Russian Federation displays certain characteristics of an emerging market. Its economy is particularly sensitive to oil and gas prices. The legal, tax and regulatory frameworks continue to develop and are subject to frequent changes and varying interpretations. The Russian economy was growing in 2017, after overcoming the economic recession of 2015 and 2016. The economy is negatively impacted by low oil prices, ongoing political tension in the region and international sanctions against certain Russian companies and individuals. The financial markets continue to be volatile. This operating environment has a significant impact on the Group's operations and financial position. Management is taking necessary measures to ensure sustainability of the Group's operations. However, the future effects of the current economic situation are difficult to predict and management's current expectations and estimates could differ from actual results.

**Operating Environment. Cyprus.** The Cypriot economy has recorded positive growth in 2016 and 2017 after overcoming the economic recession of recent years. The overall economic outlook of the economy remains favorable, however there are still downside risks emanating from the still high levels of non-performing loans, the public debt ratio, as well as possible deterioration of the external environment for Cyprus.

This operating environment may have a significant impact on the Group's operations and financial position. Management is taking necessary measures to ensure sustainability of the Group's operations. However, the future effects of the current economic situation are difficult to predict and management's current expectations and estimates could differ from actual results.

Economic recovery in Cyprus accelerated in 2017 and the medium term outlook is favourable driven by an improving labour market, broadening investments and increasing resilience. Cyprus continues to face challenges primarily in relation to public and private indebtedness and NPEs, but while more remains to be done, considerable progress has been achieved.

The Company's management is unable to predict all developments which could have an impact on the Cyprus economy and consequently, what effect, if any, they could have on the future financial performance, cash flows and financial position of the Company.

On the basis of the evaluation performed, the Company's management has concluded that no provisions or impairment charges are necessary.

The Company's management believes that it is taking all the necessary measures to maintain the viability of the Company and the development of its business in the current business and economic environment.

**Oilfield licenses.** The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its oil field licenses. Management of the Group correspond with governmental authorities to agree on remedial actions, if necessary, to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties or license limitations, suspension or revocations. Management believes any issues of non-compliance will be resolved through negotiations or corrective actions without any materially adverse effect on the financial position or the operating results of the Group. Management believes that proved reserves should include quantities that are expected to be produced after the expiry dates of the Group's production licenses. These licenses expire between 2019 and 2067.

The principal licenses of the Group and their expiry dates are:

Field	License holder	License expiry date
Okruzhnoye	Petrosakh	December 2037
Yuzhno-Daginsky area	Petrosakh	December 2041
Peschanozerskoye (eastern and western parts)	Arcticneft	December 2067
Peschanozerskoye (central part)	Arcticneft	August 2019
Ordynsky area	RK-Oil	January 2040
Babayevsky area (exploration and production)	BVN-Oil	August 2036
Babayevsky area (geological study)	BVN-Oil	October 2021

Management believes the licenses may be extended at the initiative of the Group and management intends to extend such licenses for properties expected to produce subsequent to their license expiry dates.

**24 Contingencies, Commitments and Operating Risks (Continued)**

**Tax contingencies.** Russian tax and customs legislation which was enacted or substantively enacted at the end of the reporting period, is subject to varying interpretations when being applied to the transactions and activities of the Group. Consequently, tax positions taken by management and the formal documentation supporting the tax positions may be successfully challenged by relevant authorities. Russian tax administration is gradually strengthening, including the fact that there is a higher risk of review of tax transactions without a clear business purpose or with tax non-compliant counterparties. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

The Russian transfer pricing legislation is generally aligned with the international transfer pricing principles developed by the Organisation for Economic Cooperation and Development (OECD), with certain specific features. The transfer pricing legislation provides for the possibility of additional tax assessment for controlled transactions (transactions between related parties and certain transactions between unrelated parties) if such transactions are not on an arm's length basis. Management has implemented internal controls to be in compliance with current transfer pricing legislation.

Tax liabilities arising from intercompany transactions are determined using actual transaction prices. It is possible, with the evolution of the interpretation of the transfer pricing rules, that such prices could be challenged. The impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial position and/or the Company's operations.

The Group includes companies incorporated outside of Russia. The tax liabilities of the Group are determined on the assumption that these companies are not subject to Russian profits tax, because they do not have a permanent establishment in Russia. This interpretation of relevant legislation may be challenged but the impact of any such challenge cannot be reliably estimated currently; however, it may be significant to the financial position and/or the overall operations of the Group.

As Russian tax legislation does not provide definitive guidance in certain areas, the Group adopts, from time to time, interpretations of such uncertain areas that reduce the overall tax rate of the Group. While management currently estimates that the tax positions and interpretations that it has taken can probably be sustained, there is a possible risk that outflow of resources will be required should such tax positions and interpretations be challenged by the relevant authorities. The impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the Group.

Management regularly reviews the Group's taxation compliance with applicable legislation, laws and decrees as well as interpretations published by the authorities in the jurisdictions in which the Group has operations. However, from time to time potential exposures and contingencies are identified and at any point in time a number of open matters exist, management believes that its tax positions are sustainable. Management estimates possible tax exposures that probability is higher than remote but for which no liability is required to be recognised under IFRS, could be up to \$0.4 million. These exposures primarily relate to the fact that tax authorities may challenge deductibility of certain expenses and application of certain tax regimes. This estimation is provided for the IFRS requirement for disclosure of possible taxes and should not be considered as an estimate of the Group's future tax liability.

**Restoration, rehabilitation and environmental costs.** The Group companies have operated in the upstream and refining oil industry in the Russian Federation for many years, and their activities have had an impact on the environment. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations related thereto. The outcome of environmental liabilities under proposed or future legislation, or as a result of stricter enforcement of existing legislation, cannot reasonably be estimated at present, but could be material. Under the current levels of enforcement of existing legislation, management believes there are no significant liabilities in addition to amounts which are already accrued and which would have a material adverse effect on the financial position of the Group.

**Legal proceedings.** From time to time and in the normal course of business, claims against the Group may be received. On the basis of its own estimates and both internal and external professional advice, management is of the opinion that no material losses will be incurred in respect of claims in excess of provisions that have been made in these consolidated financial statements.

**Other capital commitments.** At 31 December 2017 and 2016 the Group had no significant contractual commitments for capital expenditures.

**Urals Energy Public Company Limited**  
**Notes to the Consolidated Financial Statements**  
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**25 Financial Risk Management**

The accounting policies for financial instruments have been applied to the line items below:

	At 31 December	
	2017	2016
<i>Financial assets</i>		
<i>Loans and receivables: current assets</i>		
Loan receivable	2,145	442
Cash and cash equivalents	683	1,202
Trade and other accounts receivable	616	953
<b>Total loans and receivables: current assets</b>	<b>3,444</b>	<b>2,597</b>
<i>Financial liabilities</i>		
<i>Measured at amortized cost: current liabilities</i>		
Short-term borrowings and current portion of long-term borrowings	8,818	2,549
Trade and other payables (excluding short-term portion of finance lease obligations)	3,749	655
Short-term portion of finance lease obligations	245	113
<b>Total current liabilities measured at amortized cost</b>	<b>12,812</b>	<b>3,317</b>
<i>Measured at amortized cost: non-current liabilities</i>		
Long-term borrowings	1,116	4,243
Long-term finance lease obligations	702	714
Long-term accounts payable	144	120
<b>Total long-term liabilities measured at amortized cost</b>	<b>1,962</b>	<b>5,077</b>

**Financial risk management objectives and policies.** In the ordinary course of business, the Group is exposed to market risks from fluctuating prices on commodities purchased and sold, credit risk, liquidity risk, currency exchange rates and interest rates. Depending on the degree of price volatility, such fluctuations in market price may create volatility in the Group's financial results. As an entity focused upon the exploration and development of oil and gas properties, the Group's overriding strategy is to maintain a strong financial position by securing access to capital to meet its capital investment needs.

The Group's principal risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to these limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

**Market risk.** Market risk is the risk that changes in market prices and rates, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Group's financial results or the value of its holdings of financial instruments. The primary objective of mitigating these market risks is to manage and control market risk exposures. The Group is exposed to market price movements relating to changes in commodity prices such as crude oil, gas condensate, petroleum products and natural gas (commodity price risk), foreign currency exchange rates, interest rates, equity prices and other indices that could adversely affect the value of the Group's financial assets, liabilities or expected future cash flows.

*(a) Foreign exchange risk*

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to the US dollar. Foreign exchange risk arises primarily from commercial transactions, and recognized assets and liabilities when such transactions, assets and liabilities are denominated in a currency other than the functional currency. The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble or the US dollar. The carrying amounts of the Group's financial instruments are denominated in the following currencies (all amounts expressed in thousands of US dollars at the appropriate 31 December 2017 and 2016 exchange rates):

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**25 Financial Risk Management (Continued)**

At 31 December 2017	Russian rouble	US dollar	Total
<b>Financial assets</b>			
<i>Current</i>			
Loans issued	2,145	-	2,145
Cash and cash equivalents	629	54	683
Accounts receivable	616	-	616
<b>Financial liabilities</b>			
<i>Non-current</i>			
Long-term borrowings	(1,116)	-	(1,116)
Long-term finance lease obligations	(702)	-	(702)
Long-term accounts payable	(144)	-	(144)
<i>Current</i>			
Accounts payable and accrued expenses (excluding short-term portion of finance lease obligations)	(3,430)	(319)	(3,749)
Short-term finance lease obligations	(245)	-	(245)
Short-term borrowings and current portion of long-term borrowings	(8,818)	-	(8,818)
<b>Net exposure at 31 December 2017</b>	<b>(11,065)</b>	<b>(265)</b>	<b>(11,330)</b>
<hr/>			
At 31 December 2016	Russian rouble	US dollar	Total
<b>Financial assets</b>			
<i>Current</i>			
Loans issued	58	384	442
Cash and cash equivalents	1,177	25	1,202
Accounts receivable	953	-	953
<b>Financial liabilities</b>			
<i>Non-current</i>			
Long-term borrowings	(4,243)	-	(4,243)
Long-term finance lease obligations	(714)	-	(714)
Long-term accounts payable	(120)	-	(120)
<i>Current</i>			
Accounts payable and accrued expenses (excluding short-term portion of finance lease obligations)	(516)	(139)	(655)
Short-term finance lease obligations	(113)	-	(113)
Short-term borrowings and current portion of long-term borrowings	(2,549)	-	(2,549)
<b>Net exposure at 31 December 2016</b>	<b>(6,067)</b>	<b>270</b>	<b>(5,797)</b>

In accordance with IFRS requirements, the Group has provided information about market risk and potential exposure to hypothetical loss from its use of financial instruments through sensitivity analysis disclosures. The sensitivity analysis depicted in the table below reflects the hypothetical income (loss) that would occur assuming a 10% change in exchange rates and no changes in the portfolio of instruments and other variables held at 31 December 2017 and 2016, respectively.

Effect on pre-tax profit	Increase in exchange rate	Year ended 31 December	
		2017	2016
\$/RUS	10%	(27)	27

The effect of a corresponding 10% decrease in exchange rate is approximately equal and opposite.

**25 Financial Risk Management (Continued)**

*(b) Commodity price risk*

The Group's overall commercial trading strategy in crude oil and related products is centrally managed. Changes in commodity prices could negatively or positively affect the Group's results of operations.

The Group sells all its crude oil and petroleum products under spot contracts. Crude oil sold internationally is based on benchmark reference crude oil prices of Brent dated, plus or minus a discount for quality and on a transaction-by-transaction basis for volumes sold domestically. As a result, the Group's revenues from the sales of liquid hydrocarbons are subject to commodity price volatility based on fluctuations or changes in the crude oil benchmark reference prices. Presently, the Group does not use commodity derivative instruments for trading purposes to mitigate price volatility.

*(c) Cash flow and fair value interest rate risk*

To the degree possible, the Group centralizes the cash requirements and surpluses of controlled subsidiaries and the majority of their external financing requirements, and applies, on its consolidated net debt position, a funding policy to optimize its financing costs and manage the impact of interest-rate changes on its financial results in line with market conditions. Fixed rate borrowings expose the Group to fair value interest rate risk. The carrying value of fixed rate borrowings approximate their fair value.

**Credit risk.** Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if a counterparty defaults on its contractual obligations.

Credit risk is managed on a Group level and arises from cash and cash equivalents, including short-term deposits with banks, loans issued as well as credit exposures to customers, including outstanding trade receivables and committed transactions. Cash and cash equivalents are deposited only with banks that are considered by the Group at the time of deposit to minimal risk of default. Based on Fitch's rating, the credit quality of Public Joint-Stock Company Sberbank of Russia in which the Group mostly held its cash and cash equivalents as at 31 December 2017 and 2016 was BBB-. Based on Standard & Poor's rating, the credit quality of Public Joint-Stock Company Promsvyazbank in which the Group held its cash and cash equivalents as at 31 December 2017 and 2016 is B+ and BB-, accordingly.

The Group's domestic trade and other receivables consist of a large number of customers, spread across diverse industries mainly on Sakhalin Island. All of the Group's export crude oil sales are made to one customer, Petraco, with whom the Group was trading for the past several years (see Note 19). A majority of domestic sales of petroleum products are made on a prepayment basis. Although the Group does not require collateral in respect of trade and other receivables, it has developed standard credit payment terms and constantly monitors the status of trade receivables and the creditworthiness of the customers. The maximum exposure to credit risk is represented by the carrying amount of each financial asset exposed to credit risk. As the majority of customers pay in advance (including Petraco currently) credit risk related to trade debtors is not considered to be significant.

**Liquidity risk.** Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity has been to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group prepares various financial and operational plans (monthly, quarterly and annually) to ensure that the Group has sufficient cash on demand to meet expected operational and administrative expenses (Note 3).

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**25 Financial Risk Management (Continued)**

The following tables summarize the maturity profile of the Group's financial liabilities based on contractual undiscounted payments, including interest payments:

At 31 December 2017	On demand	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	After 5 years	Total
Debt at fixed rate						
Principal	1,697	6,535	667	229	-	9,128
Interest	817	532	41	24	-	1,414
Debt at fixed rate – Leasing obligations	-	374	328	337	389	1,428
Accounts payable and accrued expenses	-	3,749	-	-	-	3,749
<b>Total financial liabilities</b>	<b>2,514</b>	<b>11,190</b>	<b>1,036</b>	<b>590</b>	<b>389</b>	<b>15,719</b>
At 31 December 2016	On demand	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	After 5 years	Total
Debt at fixed rate						
Principal	1,611	461	4,122	99	-	6,293
Interest	456	602	88	44	-	1,190
Debt at fixed rate – Leasing obligations	-	225	223	443	469	1,360
Accounts payable and accrued expenses	-	655	-	-	-	655
<b>Total financial liabilities</b>	<b>2,067</b>	<b>1,943</b>	<b>4,433</b>	<b>586</b>	<b>469</b>	<b>9,498</b>

**Capital management.** The primary objectives of the Group's capital management policy is to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain investor, market and creditor confidence to support its business activities.

The capital as defined by management at 31 December 2017 and 2016 was as follows:

	2017	2016
Total borrowings	9,934	6,792
Less cash and cash equivalents	(683)	(1,202)
Net debt	9,251	5,590
Total equity	77,085	61,749
Debt to equity ratio	0.12	0.09

Management considers capital to represent net debt and total equity. Management does not use a specific target debt to equity or gearing ratio when managing the business.

For the capital management, the Group manages and monitors its liquidity on a corporate-wide basis to ensure adequate funding to sufficiently meet group operational requirements. The Group controls all external debts at the Parent level, and all financing to Group entities for the operating and investing activity is facilitated through inter-company loan arrangements, except for the specific project financing, which are taken on the subsidiary level.

There were no changes to the Group's approach to capital management during the year.

**26 Balances and transactions with Related Parties**

Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24 Related Party Disclosures. Key management personnel are considered to be related parties. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

**Compensation to senior management.** The Group's senior management team compensation, including salary, social tax, and bonuses, totaled \$0.6 million and \$0.6 million for the years ended 31 December 2017 and 31 December 2016, respectively. In 2017 and in 2016 senior management team stock compensation was nil.

**26 Balances and transactions with Related Parties (Continued)**

*Directors' fees.* Directors' fees for the years ended 31 December 2017 and 2016 were \$68 thousand and \$37 thousand, respectively. During the years ended 31 December 2017 and 2016 no non-cash benefits were received by the directors, no payments to the directors were made under share options or other long-term incentive plans and there were no share option schemes or other long-term incentive plans in effect during the periods, and no contributions were made to pension schemes, other than social insurance payments required by the Russian legislation.

	Year ended 31 December	
	2017	2016
<b>Senior management</b>		
L. Dyachenko	305	258
A. Ogarev	176	218
S. Uzornikov	166	171
<b>Directors fees</b>		
A. Shragar	55	37
S. Buscher	13	-
<b>Total compensation to senior management and directors' fees</b>	<b>715</b>	<b>684</b>

**27 Acquisition of Controlling Interest in Subsidiaries**

*Acquisition of Arctic Oil Company.* On 29 August 2016 the Group acquired 100% interest of OOO Arctic Oil Company (Russia) from an unrelated third party for a total consideration of \$1.8 million paid in cash. Arctic Oil Company's asset is the central part of the Peschanoozerskoe oil field on Kolguyev Island. The eastern and western parts of the Peschanoozerskoe field are already owned by Arcticneft. By acquiring Arctic Oil Company, Group will be able to achieve significant economies of scale through combining the operations of Arctic Oil Company with its existing operations on Kolguyev Island.

The share purchase agreement also stipulated an additional payment (contingent consideration) should the Group merge Arctic Oil Company with its existing subsidiary and sell the combined company to a third party within two years since the acquisition of Arctic Oil Company. The Group has no intention to sell combined operations within the next two years. Consequently, the fair value of the contingent consideration was estimated as nil.

The acquisition of Arctic Oil Company was partly financed by a short-term secured loan provided by Kamchatcomagroprombank. Total amount of the loan is 100 million Roubles (representing approximately US\$1.6 million at prevailing exchange rates). The loan was repaid before the end of 2016. Interest was chargeable at the rate 17%. Company pledged its crude oil stored at AO Arcticneft's warehouse under the loan agreement with Kamchatcomagroprombank.

In accordance with IFRS 3 "Business Combinations", the Group recognized the acquired assets and liabilities based upon their provisional fair values at the date when control of Arctic Oil Company was obtained. As of 31 December 2016 the Group did not finalize their assessment of the estimated fair values of assets and liabilities acquired due to the fact that the subsidiary was recently acquired. Management was required to finalise the accounting within 12 months from the date of acquisition.

The Group hired external valuator to determine the final fair values and economic useful lives of the acquired assets and liabilities. In 2017 revisions to the provisional values was reflected as of the acquisition date.

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**27 Acquisition of Controlling Interest in Subsidiaries (Continued)**

The following assets and liabilities were acquired with Arctic Oil Company:

	Provisional value	Adjustments	Fair value
Property, plant and equipment (Note 10)	2,245	697	2,942
Cash and cash equivalents	482	-	482
Inventories	383	-	383
Accounts receivable and prepayments	148	-	148
Deferred income tax assets (Note 14)	33	64	97
<b>Total assets</b>	<b>3,291</b>	<b>761</b>	<b>4,052</b>
Trade and other payables	678	-	678
Borrowings	482	-	482
Dismantlement provision (Note 16)	291	362	653
Provisions (Note 13)	223	-	223
Taxes payable	221	-	221
Deferred income tax liabilities (Note 14)	133	140	273
<b>Total liabilities</b>	<b>2,028</b>	<b>502</b>	<b>2,530</b>
Net assets at acquisition date	1,263	259	1,522
Bargain gain from acquisition of subsidiary	-	(259)	(259)
Indemnification asset	515	-	515
<b>Total consideration paid</b>	<b>1,778</b>	<b>-</b>	<b>1,778</b>

The sales and purchase agreement included an indemnification clause in which the seller of Arctic Oil Company agreed to reimburse the Group for any liabilities that had not been repaid or accrued for at acquisition date. The Group has recognised such liabilities in full at acquisition date. As a result, the Group recognised an indemnification asset in the amount of \$515 thousand. The indemnification asset was repaid by cash before the year end.

Recognised bargain gain is assignable to several causes including loss from operating activities for some time before acquisition Arctic Oil Company and fact that acquisition of Arctic Oil Company by any other buyers could not be financial viable.

The acquired subsidiary contributed revenue of nil and loss of \$0.1 million to the Group for the period from the date of acquisition to 31 December 2016. If the acquisition had occurred on 1 January 2016, Group revenue for 2016 would have been higher by \$6.1 million, and loss for 2016 would have been lower by \$1.5 million.

As result of revisions to the provisional values as of the acquisition date, the following effects of the restatement on the previously reported amounts are set out below.

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**27 Acquisition of controlling interest in subsidiaries (Continued)**

*Consolidated Statement of Financial Position*

	31 December 2016		
	As previously reported	Adjustments	Restated
<b>Assets</b>			
Property, plant and equipment	65,089	564	65,653
<b>Total non-current assets</b>	<b>67,214</b>	<b>564</b>	<b>67,778</b>
<b>Total assets</b>	<b>85,941</b>	<b>564</b>	<b>86,505</b>
<b>Liabilities and equity</b>			
Dismantlement provision	1,673	219	1,892
<b>Total long-term liabilities</b>	<b>11,401</b>	<b>219</b>	<b>11,620</b>
<b>Total liabilities</b>	<b>24,537</b>	<b>219</b>	<b>24,756</b>
<b>Equity</b>			
Translation difference	(62,252)	30	(62,222)
Accumulated deficit	(535,554)	315	(535,239)
<b>Equity attributable to shareholders of Urals Energy Public Company Limited</b>	<b>60,638</b>	<b>345</b>	<b>60,983</b>
<b>Total equity</b>	<b>61,404</b>	<b>345</b>	<b>61,749</b>
<b>Total liabilities and equity</b>	<b>85,941</b>	<b>564</b>	<b>86,505</b>

*Consolidated Statement of Profit or Loss and Other Comprehensive Income*

	Year ended 31 December 2016		
	As previously reported	Adjustments	Restated
Bargain gain from acquisition of subsidiary	-	259	259
<b>Operating profit</b>	<b>2,046</b>	<b>259</b>	<b>2,305</b>
Interest expense	(1,066)	(12)	(1,078)
<b>Total net finance income/(expense)</b>	<b>3,898</b>	<b>(12)</b>	<b>3,886</b>
<b>Profit before income tax</b>	<b>5,944</b>	<b>247</b>	<b>6,191</b>
Income tax benefit	2,057	68	2,125
<b>Profit for the year</b>	<b>8,001</b>	<b>315</b>	<b>8,316</b>
Profit for the year attributable to:			
- Non-controlling interest	91	-	91
- Shareholders of Urals Energy Public Company Limited	7,910	315	8,225
<b>Profit per share from profit attributable to shareholders of Urals Energy Public Company Limited:</b>			
- Basic profit per share (in US dollar per share)	0.63	0.02	0.65
- Diluted profit per share (in US dollar per share)	0.63	0.02	0.65
Weighted average shares outstanding attributable to:			
- Basic shares	12,622,303	-	12,622,303
- Diluted shares	12,622,303	-	12,622,303
<b>Profit for the year</b>	<b>8,001</b>	<b>315</b>	<b>8,316</b>

**27 Acquisition of controlling interest in subsidiaries (Continued)**

<b>Other comprehensive profit that may be reclassified subsequently to profit, net of income tax:</b>			
- Effect of currency translation	5,543	30	5,573
<b>Total comprehensive income for the year</b>	<b>13,544</b>	<b>345</b>	<b>13,889</b>
<b>Attributable to:</b>			
- Non-controlling interest	219		219
- Shareholders of Urals Energy Public Company Limited	13,325	345	13,670

*Consolidated Statement of Changes in Equity*

	31 December 2016		
	As previously reported	Adjustments	Restated
Effect of currency translation	5,415	30	5,445
Profit for the year	7,910	315	8,225

**28 Events after the reporting period**

On 31 January 2018 Petrosakh entered into an 12 month revolving credit facility with the Sakhalin branch of PJSC Sberbank of Russia ("Sberbank") for a total amount of 300 million Roubles (representing approximately US\$5.2 million at prevailing exchange rates) to Petrosakh for working capital financing.

The key terms of the Loan are that:

- it is repayable on 30 January 2019 (the agreement also provides for early repayment of the loan by Petrosakh without incurring any penalties);
- interest is chargeable at the rate of 9.6% plus 1%. The lowest rate of 9.6% is subject to Petrosakh meeting monthly turnover targets and volume of salary transferred to Sberbank accounts of employees;
- it is secured by way of a pledge over property and cash flows from Petrosakh;
- the agreement provides for a parent company guarantee from Urals Energy and a guarantee from Arcticneft.

In May 2018 Company obtained a short-term secured loan from Petraco in the amount of \$5.0 million at an interest rate of three months Libor plus 5% per annum due on the 30 day after the date of next tanker shipment. From the date of the next tanker shipment the interest rate is three month Libor plus 2% per annum. Company pledged its 100% shares in its subsidiary AO Arcticneft under the loan agreement with Petraco. Loan is repayable immediately following the loading of the tanker shipment of approximately 20,000 tonnes of crude oil, scheduled for July 2018. The proceeds of the Loan will be used by the Company for general working capital financing.

In the beginning of 2018 the Group has initiated the merger of Arctic Oil Company to Arcticneft, which is intended to simplify and streamline the operational structure.

There were no other material events after the balance sheet date, which have a bearing on the understanding of the financial statements.

Independent auditor's report on pages 1 to 7.