ALWAYS MOVING FORWARD

LUKOIL

Annual Report 2009

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EVENTS IN 2009

MAIN OPERATING AND FINANCIAL INDICATORS

CORPORATE GOVERNANCE

ALWAYS MOVING FORWARD

LUKOIL LUBRICANTS

Annual Report 2009

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Concepts and Terms Used in this Report

Mentions of “OAO LUKOIL”, “LUKOIL Group”, “the Group”, “LUKOIL”, “the Company”, “we” and “our” are equivalent for the purposes of this Report and refer to LUKOIL Group of companies, to LUKOIL and/or its subsidiary enterprises, depending upon the context, in which the terms are used.

The average rouble/dollar exchange rate for 2009 (31.72 roubles/dollar) is used in conversion of rouble figures for expression in dollars, unless otherwise indicated.

Figures for reserves and production of oil include oil, gas condensate and gas liquids.

“Regions” with a capital “R” refers to administrative divisions of the Russian Federation, ”regions” with a small “r” refers to general geographical divisions.

“Reference fuel” is a rough measure to enable comparisons between different types of fuel, based on their energy content. 1 tonne of reference fuel = one tonne of crude oil = 1,000 cubic meters of natural gas.

Percentage change of operating figures in 2009 (million tones) is calculated using the same figures in thousand tonnes.

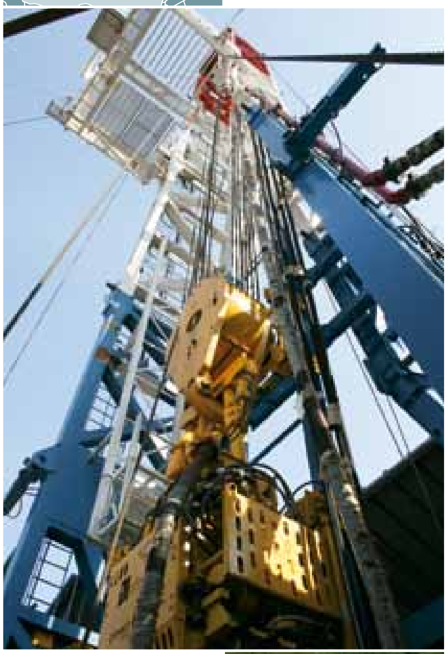
Abbreviations
boe – barrels of oil equivalent (1 boe = 6,000 cubic feet of gas)
km – kilometer
ppm – parts per million
PSA – production sharing agreement
RTS – Russian Trading System
MICEX – Moscow Interbank Currency Exchange

LUKOIL Reports

Electronic versions of the following reports are available on the Company web site:
- Report on Company Business.
- Consolidated Financial Accounts.
- Quarterly Consolidated Financial Accounts.
- Management Discussion and Analysis of Financial Condition and Results of Operations.
- Analyst DataBook.
- Fact book.

LUKOIL

Annual Report 2009



Contents

Letter to Shareholders

Dear Shareholders,

We are pleased to report that LUKOIL Group achieved positive results in the difficult and unstable environment of 2009, which saw the acute stage of the world economic crisis and abrupt decline in prices for oil and petroleum products. The Company showed its ability to withstand difficulties, react flexibly in unfavourable macroeconomic conditions, achieve sustained and progressive business development, and increase potential for growth of Company value. Prompted by sudden negative change in the macroeconomic climate, we focused our efforts on reduction of capital expenditures, tightening of financial discipline and strengthening of the Company's financial position. At the same time, we continued to fully finance key development projects. As a result, the Group was able to achieve strong results and lay a firm foundation for further growth.

Net profit of the Group in the reporting year was $7,011 million, and return on average capital employed was 11.8%. Free cash flow reached $2,360 million, which is a high level in view of the crisis situation in the economy. It should be noted that year-on-year decline of LUKOIL's net income in 2009 was significantly less than decline in oil prices: the price for Urals fell by 35.5%, while Company net profit was 23.3% lower than in 2008. Refining margins in Russia and abroad also fell faster than LUKOIL results in the segment. Better-than-average performance reflected Company efforts to raise business efficiency, reduce costs across the board and increase oil production and refining volumes.

The Company continues to prove its commitment to a long-term policy of increasing shareholders returns. Dividend payments for 2009 will not be reduced in comparison with 2008, despite lower net profits: on 20 April the Board of Directors recommended the Annual Meeting of Shareholders to approve 2009 dividends of 52 roubles per share ($1.72 at the exchange rate on December 31, 2009), which corresponds to the last

Chairman of the Board of Directors of LUKOIL
Valery Grayfer

year's level. So dividends will exceed 20% of net profit for 2009, compared with 15% for 2008. Dividend yield will be 3.6%.

We improved the balance between various sources of financing in 2009. In particular, the Group placed a $1.5-billion Eurobond issue, and obtained yield level equal to that before the crisis, which is an unprecedented achievement for a privately owned Russian company.

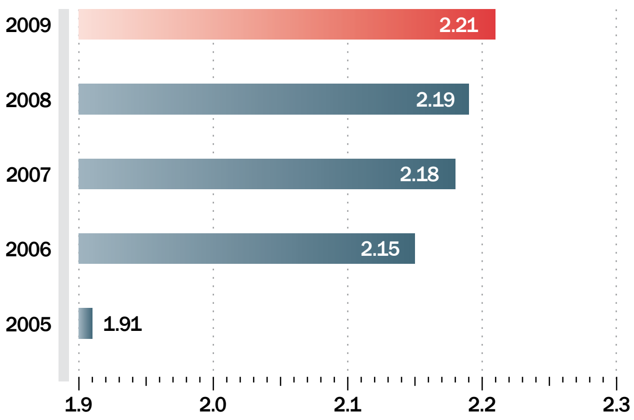
In the **Exploration & Production segment** the Company continued rapid growth and development of the resource base using the latest E&P technologies. The Group made a point of ensuring stabilization of production in traditional regions and rapid growth in new regions.

LUKOIL showed positive trends in hydrocarbon production in the accounting year thanks to investments in development made earlier. Average daily production of hydrocarbons by the Group rose by nearly 1% in 2009 to 2.21 million boe. Growth of average daily oil output was particularly strong (2.7%) thanks to the contribution of the Yuzhnaya Khylchuya field in Timan-Pechora, which was commissioned in 2008. The field was already producing at full capacity by the middle of 2009, helping to achieve the Company's aim of production increase in new regions. Oil production also grew in international projects. However, production of marketable gas fell by 12.5% in 2009 due to lower demand and resulting limits on volumes taken by Gazprom.

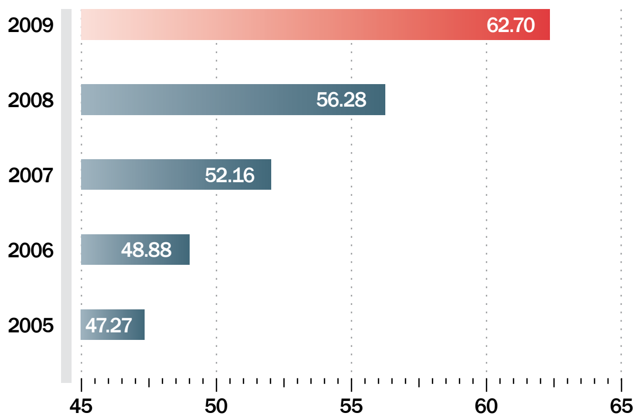
Success in 2009 of the bid by LUKOIL Group and Norwegian Statoil in the tendering competition for development of the West Qurna-2 field in Iraq was of great significance. With recoverable reserves of about 13 billion barrels, West Qurna-2 is one of the world's biggest fields that are not currently in production. The contract is for 20 years with possibility of extension for 5 years. We maintained constant pressure throughout the last decade to secure the Iraqi project, remaining true to the promise, which we made to shareholders,

President of LUKOIL
Vagit Alekperov

PRODUCTION OF MARKETABLE HYDROCARBONS, MILLION BOE PER DAY



REFINERY THROUGHPUTS AT OWN AND AFFILIATED REFINERIES, MILLION TONNES



and we finally achieved our goal in 2009. This project has strategic importance for the Company and will improve the quality of our business as well as increasing shareholder value.

We made every effort in 2009 to commence production in the Northern Caspian as quickly as possible. A fixed ice-resistant offshore platform with drilling unit, as well as living quarters and transport infrastructure were installed at the **Yu. Korchagin** field, and production drilling began. The first oil was produced at the field in the second quarter of 2010. The Yu. Korchagin field is the first of several promising Caspian projects, which will be developed by the Company and will be mainstays of long-term, high-quality production growth.

In the **Refining & Marketing segment** the Company achieved optimal balance in 2009 between levels of refining and production (capacity at Group refineries is equal to 75% of the Group's oil production). Total throughputs at Company refineries in 2009, including the share in the ISAB and TRN refineries, was 62.7 million tonnes, which is 11.4% more than in 2008. Retail sales of petroleum products were 14.1 million tonnes, which is close to the figure in 2008. The Company managed to keep sales volumes relatively stable, despite the recessionary economic environment, thanks to increase in the number of highly efficient filling stations and their growing popularity among consumers.

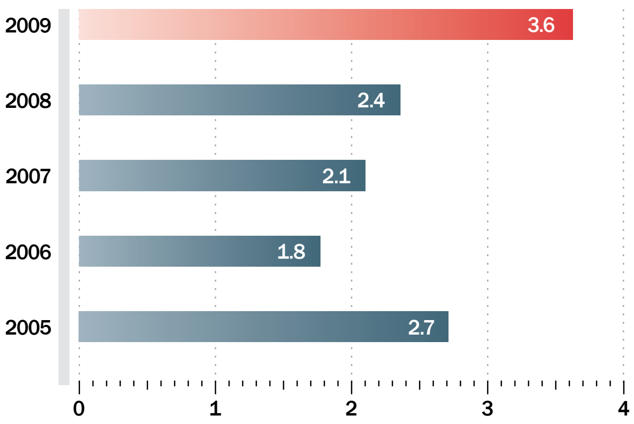
LUKOIL moved ahead in 2009 with rapid development of its **Power Generation segment**, which was created in 2008. This new business has considerable importance in the Group's strategy for 2010–2019: it should create substantial cash flows during the period, becoming an important factor for growth of shareholder value in the long term. Restructuring of the power generation business and its integration into the structure of the Group was mainly completed in 2009.

The Company is always aware of its responsibility for **protecting the environment and public health.** Our refineries are moving quickly to introduce new quality standards and start production of better-quality products. The Ukhta Refinery began production of gasoline meeting Euro-3 and Euro-4 standards thanks to installation of an isomerisation unit. A new sulphuric acid alkylation unit at the Burgas refinery will raise the quality of gasoline outputs. The unit has been designed using the latest industrial safety and environmental protection technologies. Despite overall lowering of capital expenditures across the Group, levels of spending on industrial safety and environmental protection were kept almost intact, and there was no increase in the rate of incidents at Group facilities.

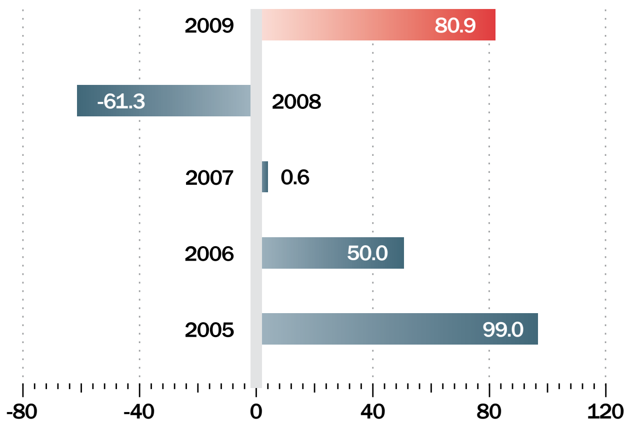
Achievement of strong results is helped by application of **modern technologies** in all spheres of our business. We recognize the prime importance of R&D work and its application for ensuring LUKOIL's competitiveness. The Company began cooperation in 2009 with the state corporation, RUSNANO, for commercialisation of nanotechnologies and their application in the oil & gas sector. It is already clear from progress to date that the cooperation will be rewarding.

Our successes would not be possible without the efforts of thousands of our talented employees in Russia and abroad, whose daily labour enables dynamic and rapid development by LUKOIL Group. It is natural, therefore, that our corporate social policy is fully geared to enhancing the motivation, qualification and social guarantees of our employees. We are particularly pleased to have avoided major cuts in employment and social payments in the crisis

DIVIDEND YIELD, %



TOTAL SHAREHOLDER RETURN, %



conditions of 2009 thanks to reduction of costs and business optimization in other areas. We thus remained true to our fundamental principle, that **people are the Company's most valuable asset**.

LUKOIL Group made every effort in the accounting year to increase shareholder value. Operating indicators were improved, new efficient assets were acquired, and a tough policy was in place for limiting capital expenditures. This enabled the Company to remain attractive as an object for investment despite the unstable international financial environment. The LUKOIL share price rose substantially by 75.6% in 2009, although the result was somewhat less than overall growth of the Russian share market. Total shareholder return (including dividends paid) exceeded 80% in 2009.

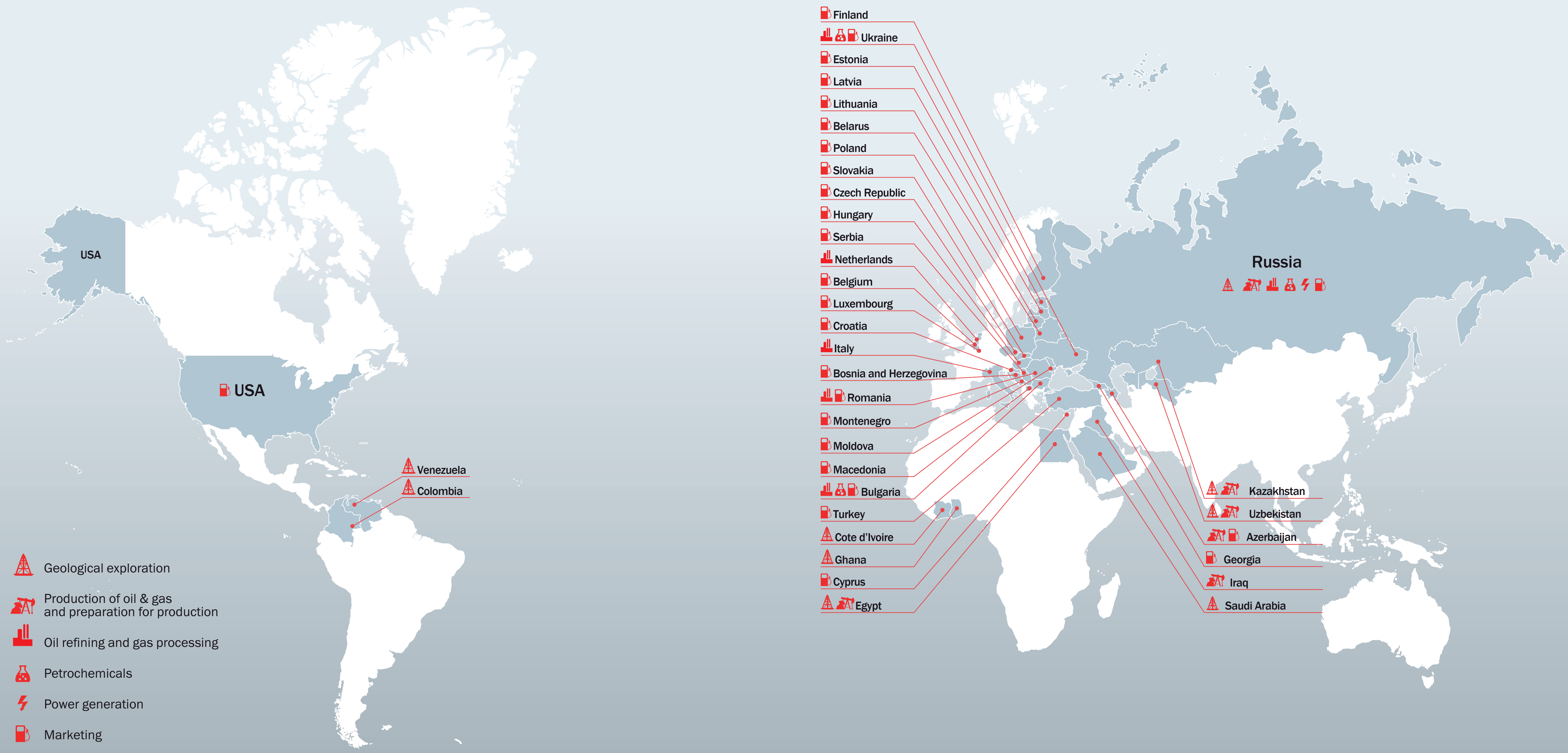
In the crisis year of 2009 LUKOIL once again showed its strength and ability to deal flexibly with difficult macroeconomic circumstances, while making its business more competitive, generating sufficient free cash flows and achieving our principal goal of raising the income of LUKOIL's shareholders.

Chairman of the Board
of Directors of LUKOIL
Valery Grayfer

President of LUKOIL
Vagit Alekperov

LUKOIL IN THE WORLD

LUKOIL IS ONE OF THE MAJOR INTERNATIONAL VERTICALLY INTEGRATED ENERGY COMPANIES



Main Operating and Financial Indicators

Main financial indicators

	2009	2008	Change, %
Sales, $ million	**81,083**	107,680	**-24.7%**
EBITDA, $ million	**13,475**	15,797	**-14.7%**
Net income, $ million	**7,011**	9,144	**-23.3%**
Basic EPS, $	**8.28**	10.88	**-23.9%**
ROACE, %	**11.8**	17.3	
Capital expenditures, $ million	**6,534**	10,589	**-38.3%**
Investments (acquisition of subsidiaries and minority stakes), $ million	**2,945**	5,398	**-45.4%**
Share price (end of year), $	**56.2**	32.0	**+75.6%**
Dividend per share, roubles	**52**	50	**+4.0%**

Main operating indicators

	2009	2008	Change, %
Oil reserves, million barrels	**13,696**	14,458	**-5.3%**
Gas reserves, billion cubic feet	**22,850**	29,253	**-21.9%**
Hydrocarbon reserves, million boe	**17,504**	19,334	**-9.5%**
Crude oil production, million barrels	**719.6**	702.9	**+2.4%**
Production of marketable natural gas, million cubic meters	**10,218**	12,671	**-19.4%**
Production of marketable associated gas, million cubic meters	**4,680**	4,349	**+7.6%**
Production of marketable hydrocarbons, thousand boe per day	**2,212**	2,194	**+0.8%**
Throughputs at own refineries and at ISAB and TRN, million tonnes	**62.70**	56.28	**+11.4%**
Throughputs at third-party refineries, million tonnes	**3.78**	5.48	**-31.0%**
Gas processing, million cubic meters	**2,962**	3,249	**-8.8%**
Production of petrochemicals, million tonnes	**0.90**	1.46	**-38.4%**
Crude oil exports, million tonnes	**42.02**	39.30	**+6.9%**
Petroleum product exports, million tonnes	**27.8**	25.8	**+7.7%**
Crude oil sales, million tonnes	**49.97**	39.54	**+26.4%**
Wholesale sales of petroleum products, million tonnes	**86.68**	80.98	**+7.0%**
Retail sales of petroleum products, million tonnes	**14.08**	14.16	**-0.6%**
Number of filling stations (owned, leased and franchises)	**6,620**	6,748	**-1.9%**
Average number of employees, thousand	**143.4**	152.5	**-5.9%**

Hydrocarbon reserves and production data include Group share in equity affiliates.

Events in 2009

FEBRUARY

LUKOIL obtains an unsecured credit of €1 billion from Gazprombank with three year maturity, as well as two credits, for $500 million and 17 billion roubles (about $500 million), with one year maturity from Sberbank. The money will be used for general corporate purposes, including provision of loans to Company subsidiaries and affiliates, refinancing of outstanding debt and replenishment of working capital.

LUKOIL approves an R&D coordination program for 2009, a medium-term R&D development program for 2010–2011, and a standardization program for 2009–2011. The program for 2009 includes execution of more than 800 scientific-research, design-and-testing, and technology tasks in the sphere of field exploration and development, as well as provision of scientific and technical services. A total of 3 billion roubles (about $100 million) have been allocated for the program. Financing of the medium-term R&D development program, the first such program ever prepared by the Group, is in excess of 7 billion roubles (over $200 million). About 90% of all spending as part of the one-year and medium-term programs will be on the Exploration & Production segment.

MARCH

LUKOIL and the Russian steel maker, Novolipetsk Steel (NLMK), sign a three-year agreement on cooperation and technical partnership. In accordance with the agreement, the companies will conduct a unified technical policy in development of lubricants and special-purpose liquids to achieve their full compliance with international requirements for performance and environmental safety. The companies also plan to work together on a program for substitution of lubricants and special-purpose liquids, which NLMK now imports, by LUKOIL-branded products, which have permits and approvals from leading international manufacturers of industrial equipment and vehicles.

APRIL

LUKOIL begins drilling of the first production well at the Pyakyakhinskoye gas-condensate field. The Company plans to drill 55 production wells at the field in the medium term, and commercial launch is scheduled in the fourth quarter of 2011. Hydrocarbons produced at the Pyakyakhinskoye field will be transported via a 126 km pipeline, which will be built to the Nakhodkinskoye field and a 160 km pipeline to the Vankor field. Proved reserves at the Pyakyakhinskoye field at the end of 2009 were 70 million barrels of oil and condensate and 1.9 trillion cubic feet of gas.

Pyakyakhinskoye gas-condensate field in Yamal-Nenets Autonomous District

The LUKOIL Management Committee approves the Company's environmental program for 2009–2013. The program includes 483 measures at total cost of 58 billion roubles (about $1.8 billion). The aim of the program is to improve the Company's environmental management system and minimize negative impact of the Company's production operations on the environment. The program includes measures to minimize formation of waste in the process of production and to utilize that waste, as well as greater utilization of associated gas and implementation of projects using mechanisms of the Kyoto Protocol, aiming to achieve environmental impact levels, which match requirements of national and international legislation.

LUKOIL and the Russian carmaker, AvtoVAZ, sign a general cooperation and technical partnership agreement for 2009–2012. The agreement includes provisions for supplies of gasoline, diesel fuel, and LUKOIL-branded engine and transmission oils for first filling of AvtoVAZ cars. The document also envisages a unified technical policy for raising quality of fuel and lubricants to ensure their compliance with modern international requirements for performance and environmental safety.

LUKOIL and AvtoVAZ sign a cooperation and technical partnership agreement

MAY

LUKOIL ranks among the Top-5 European oil & gas companies for loyalty to shareholders as a result of research by the authoritative magazine, Institutional Investor. The publication carries out an annual assessment of the standard of companies' shareholder relations through a survey of more than 300 analysts and portfolio investors, representing more than 200 financial groups with total investments in European assets in excess of $2.4 trillion.

JUNE

LUKOIL Group signs an agreement to acquire 45% of TOTAL Raffinaderij Nederland N.V. (TRN), a refinery in the Netherlands, from TOTAL S.A. The deal was completed in September 2009 and its final value was about $700 million. The refinery is managed on a processing-service basis. The Company will supply crude oil and other raw materials in proportion to its ownership stake and receive petroleum products. The refinery has access to transport infrastructure, including the Maasvlakte Olie terminal, also in the Netherlands, in which TRN has a 22% stake.

LUKOIL acquires 45% of TOTAL Raffinaderij Nederland N.V. (TRN)

LUKOIL successfully completes placement on the MICEX of a bond issue with value of 15 billion roubles (about $500 million) and maturity of 364 days. Total demand was 35 billion roubles (over $1.1 billion). After the order book had been completed, the coupon was set at 13.5% per annum. Funds from the placement were used for replenishment of working capital.

LUKOIL holds its Annual General Meeting of Shareholders, at which the Annual Report for 2008 and annual financial statements, including the statement of income, are approved. Shareholders approved payment of dividends for 2008 at a level of 50 roubles per common share (compared with 42 roubles per share for 2007). The AGM confirmed levels of remuneration and compensation of costs for members of the Board of Directors and Internal Audit Commission, elected members of the Board of Directors and Internal Audit Commission, and approved a transaction with interest.

AUGUST

LUKOIL places bonds to the value of 25 billion roubles (about $800 million) on the MICEX. The bonds have maturity of 1,092 days and a coupon period of 182 days with 13.35% annualized coupon. There were 126 investor offerings for coupons in the book-building period, varying between 12.3% and 14.5% per annum. Total demand was over 65 billion roubles (over $2 billion). The placement is the largest ever by LUKOIL on the rouble debt market.

LUKOIL obtains a $1.2 billion credit from a syndicate of international banks. The credit is for 3 years at LIBOR + 4% annualized, and is secured by oil export contracts. The borrowing was used by the Company for general corporate purposes, refinancing of existing financial debt, and financing of operations associated with oil exports.

LUKOIL and Bashneft sign a basic agreement on cooperation for the period until August 1, 2010. The document provides for long-term and mutually beneficial relations between the parties, their subsidiaries and authorized operators in delivery of oil produced by LUKOIL for processing at the Ufa group of refineries, and reciprocal deliveries of petroleum products and petrochemicals for export and sale on the Russian domestic market.

SEPTEMBER

LUKOIL publishes its Sustainable Development Report for 2007–2008. The document provides information on main trends and indicators reflecting operating, social and environmental activities by the Company in the regions of its presence: Western Siberia, Perm Territory, Kaliningrad, Volgograd, Astrakhan and Nizhny Novgorod regions, the Komi Republic and Nenets Autonomous District. International documents used in preparation of the Report include the AA1000 standard (1999), the Guide to Sustainable Development Reporting (produced by the Global Reporting Initiative) and the Global Compact, as well as the Social Charter of Russian Business.

LUKOIL publishes Sustainable Development Report for 2007-2008

LUKOIL Group commissions an isomerisation unit at the Ukhta Refinery. The unit, which is for production of the high-octane component in gasoline (free from sulphur compounds, benzol and aromatics), enabled the Ukhta Refinery to commence production of automotive gasolines, which comply with the Euro-3 and Euro-4 environmental standards. The unit has input capacity of 120,000 tonnes per year. Investments for its construction were about $40 million.

LUKOIL takes first place in a ranking of the country's 75 biggest companies by criteria of social responsibility, prepared by Trud newspaper, the Agency for Political and Economic Communications, and the Russian Anti-crisis Forum. For purposes of the ranking 'social responsibility' is understood to mean creation and preservation of jobs, tax discipline, delivering on commitments to employees, and helping to maintain social infrastructure in Russian regions. The ranking is based on results of a survey of 26 experts, including representatives of trade unions and business associations, economists, sociologists, political scientists and publicists.

LUKOIL and the Ministry of Economic Development of Russia sign a cooperation agreement. The document calls for mutual assistance in the field of cooperation with international fuel & energy organizations and foreign oil & gas companies, and participation in energy conferences, forums and other international public events. In accordance with the agreement, the Ministry of Economic Development of Russia will help the Company to protect its lawful interests in conduct of foreign business, and will include Company specialists in expert groups as part of inter-governmental commissions. LUKOIL will reciprocate by providing consulting support to the Ministry of Economic Development of Russia in preparation of government proposals concerning development of relationships with foreign countries and international organizations in the fuel & energy sector.

Six senior managers of LUKOIL Group organizations are included in a rating of the 1,000 most professional managers in Russia, compiled by the Association of Russian Managers and Kommersant newspaper. The rating identifies the most professional managers and leaders in specific sectors of the economy and specific roles.

OCTOBER

LUKOIL and the Russian Corporation of Nano-technologies (RUSNANO) sign a general agreement on strategic partnership. In accordance with the document, the sides will develop cooperation in commercialization of nanotechnologies and their use in the oil & gas sector, including LUKOIL Group enterprises, and will define priority projects and regions for conduct of industrial testing of promising nanotechnologies at Company production sites.

The authoritative international publication, Business Insurance, rates LUKOIL's business insurance and risk management arrangements as the best in the business. The magazine found that western underwriters view LUKOIL's approach to risk management and organization of insurance protection as exemplary and recommend it to other energy companies.

The Company launches new premium-class fuel brands, EKTO Plus (octane number 95) and EKTO Sport (octane number 98). A multi-functional package of additives in the new gasolines gives extra engine power and lower fuel consumption, as well as extending engine life and reducing CO_2 emissions. High standard and improved performance qualities of EKTO Plus and EKTO Sport have been attested by the independent UK test centre, Tickford Power Train Test.

LUKOIL launches new fuel brands, EKTO Plus and EKTO Sport

NOVEMBER

LUKOIL launches a new sulphuric acid alkylation unit with capacity of 300,000 tonnes per year at the Burgas Refinery. Commissioning of the new unit enables complete decommissioning of the Refinery's old sulphuric acid alkylation unit with 215,000 tonnes annual capacity. Investments in the new equipment were over $90 million. The unit was designed using the latest technologies, enabling substantial increase of the alkylate octane number and improvement in quality of gasoline output, as well as reducing atmospheric pollution and consumption of energy, materials and reagents in the production process.

LUKOIL places two Eurobond tranches with total value of $1.5 billion. The first tranche of $900 million is placed at 6.375% per annum, maturing in 2014; the second tranche of $600 million is placed at 7.250% per annum, maturing in 2019. Money raised in the placement is used for general corporate purposes, including settlement of outstanding debt.

The Company takes 8th place among oil & gas companies in Europe, the Middle East and Africa, and 12th place among worldwide industry leaders in the 'Top 250 Global Energy Companies' rating by the American energy agency, Platts. Companies were assessed by four main indicators: scale of assets, sales, net income and return on capital employed. LUKOIL's rankings in previous years were: 8th and 11th in 2008; 6th and 11th in 2007; and 6th and 15th in 2006.

LUKOIL wins the competition for corporate annual reports, held by the RTS stock exchange. The company took first prize in three nominations: 'Best presentation of investment attractiveness in an annual report', 'Best annual report in the Central Federal District', and 'Best information disclosure in an annual report by a company with capitalization over 100 billion roubles'. Competition participants were 125 companies from nearly all sectors of the economy. LUKOIL also won nominations at the federal competition for annual reports and internet sites, held by Securities Market magazine and the MICEX stock exchange: LUKOIL was recognized for 'Best level of information disclosure for investors on a corporate internet site' and 'Best level of information disclosure in an annual report in English'.

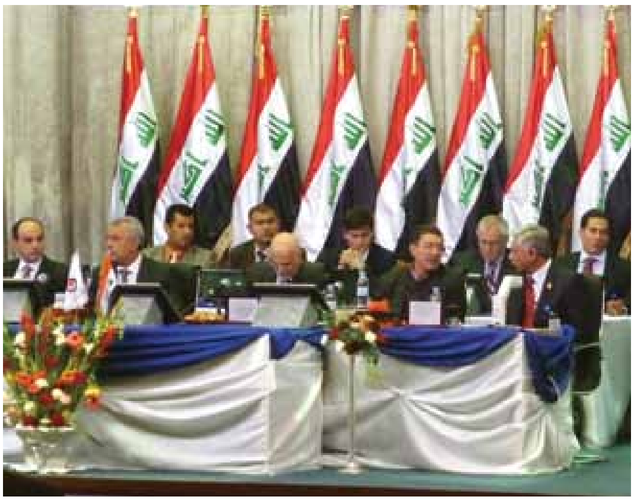
LUKOIL wins a nomination for 'Best petroleum products supplied to Russian consumers', based on research into the Russian retail market in 2008, carried out by the company InfoTEK-Consult. The Company was commended for its major contribution to improving the quality of Russian petroleum products.

The Board of Directors of LUKOIL approves the Program for Strategic Development of LUKOIL Group for 2010–2019. The Program sets the following priorities for LUKOIL Group: sustainable growth of free cash flow; growth of hydrocarbon production; full replacement of production by new reserves at lower cost than competitors; and geographical diversification of hydrocarbon production. The main tools for achieving these tasks are to be improved labour productivity, greater energy efficiency, control of capital expenditures, simplification of organizational structure, and divestment of non-core businesses.

DECEMBER

LUKOIL completes purchase from BP's subsidiary of a 46% stake in the joint venture, LUKARCO B.V., which is developing the Tengiz and Korolevskoye fields in Kazakhstan. The acquisition raises the Company's share in LUKARCO B.V. to 100%. Total value of the deal is $1.6 billion. The first payment of $300 million was made in December 2009, the rest is to be paid in next two years. The acquisition increases the Company's proved reserves by 102 million barrels of oil and 130 billion cubic feet of gas, and gives an increase of daily oil production by more than 13,000 barrels.

A consortium of LUKOIL and the Norwegian company Statoil wins the tendering competition for rights to develop the West Qurna-2 field in Iraq. LUKOIL and Statoil made the most attractive tender, including a remuneration fee of $1.15 per barrel produced above an agreed production level of 1.8 million barrels per day. Terms of the tender require 25% of shares in the consortium to be transferred to an Iraqi state company, so the LUKOIL stake will be 56.25% and the Statoil stake will be 18.75%. Recoverable reserves of oil at the field are estimated at 13 billion barrels.



LUKOIL and Statoil win the tendering competition for rights to develop the West Qurna-2 field in Iraq

LUKOIL begins production drilling at the Yu. Korchagin field in the Caspian Sea. The Company began field construction at sea in April 2009, towing the jacket for a fixed ice-resistant offshore platform from the port of Astrakhan. Living quarters were built onto the jacket in May. In August work was completed on a jetty for loading of oil from an underwater pipeline into a floating reservoir and onto shuttle tankers. In September a floating reservoir was installed at the field for loading of shuttle tankers and transportation of oil produced at the field. A fixed ice-resistant offshore platform with drilling unit was built for drilling of wells to a depth of 7,400 meters. A total of 33 production wells, 3 water injection wells and 1 gas injection well will be drilled at the field. The first oil was obtained at the field in the second quarter of 2010. Maximum annual output levels will be 2.5 million tonnes of oil and 1 billion cubic meters of gas. 3P hydrocarbon reserves are estimated at 274 million boe.

Yu. Korchagin field in the Caspian Sea

LUKOIL places bonds to the value of 10 billion roubles (more than $300 million). The bonds have maturity of 1,092 days, a 182-day coupon period and coupon rate of 9.2% per annum. 52 investor offerings were received during book building at coupon rates from 9% to 9.7%, and total demand was in excess of 17 billion roubles (over $500 million).

Exploration & Production

Strategy

Creating potential for long-term Company growth through reserve replacement in traditional production regions and accelerated development of new production regions in Russia and abroad.

Improving efficiency of geological exploration by careful selection of projects and use of the latest technologies.

Steady increase of hydrocarbon production in the medium term.

Improvement of production indicators and efficient control over lifting costs through application of the latest technologies, and through optimization of the well stock and field development systems.

Application of financial criteria to assess projects and business results, and to optimize the asset portfolio.

LUKOIL maintained its focus on efficient development of the Exploration & Production segment in 2009 and achieved substantial results.

We significantly raised the average daily level of oil production (by 2.7%), thanks mainly to rapid development of the Yuzhnaya Khylchuya field. Total daily production of hydrocarbons was 2.212 million boe. The Company maintained tight financial discipline, reducing capital expenditures in the E&P segment by more than 40% compared with 2008 to 4,687 million dollars as part of an anti-crisis program. Operating expenses were also lowered: hydrocarbon lifting costs fell by 14% to $3.56 per boe.

Thanks to the Company's efforts at business optimization, net profit in the E&P segment was $5,456 million.

The Company obtained development rights for the West Qurna-2 field in Iraq in 2009. This is an important event, which we worked for many years to achieve. West Qurna-2 is a strategic project for the Company and supports growth of its shareholder value.

Price and Tax Environment

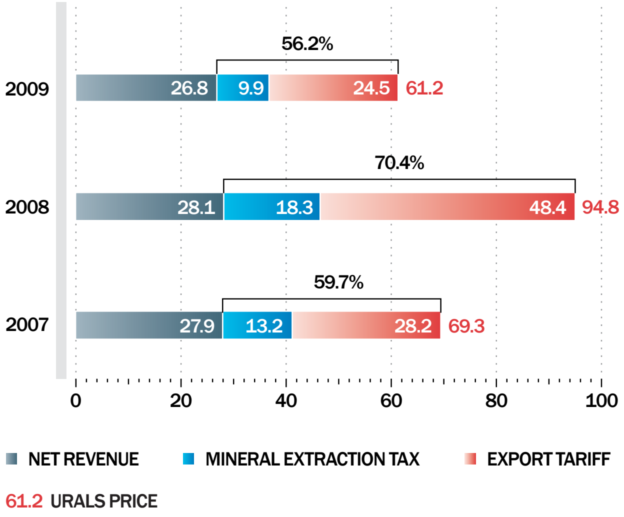
Crude Oil Market

Oil prices fluctuated in a corridor between $40 and $50 per barrel in January-April 2009 after falling below $35 per barrel at the end of 2008. Main supportive factors were coordinated actions by OPEC to cut production, the gas conflict between Russia and Ukraine, and the military operation by Israel in the Gaza Strip. High levels of commercial oil stocks worldwide, weak demand, and fears of further worsening of the economic situation exerted negative pressure on oil prices. Prices for oil began to grow from May, supported by better economic statistics. US commercial stocks, which had peaked in April, began to decline. Measures taken by several developed and developing countries to stimulate their economies (including the USA and China) began to bear fruit, and rates of economic decline slowed down. The more optimistic mood encouraged investors to move out of dollar assets into higher-risk assets, causing decline in value of the US currency and nominal increase of oil prices. As a result, oil prices stayed in a range of $60–80 per barrel until the end of the year. Any move towards higher price levels was held back by lack of confidence among market participants about rapid recovery of the world economy and strengthening of energy demand. But price falls were also due averted thanks to efforts by OPEC to hold back growth of output. Macroeconomic indicators, particularly in China, also helped to support the market.

The average price for Brent crude in 2009 was $61.7 per barrel, 36.6% lower than in 2008.

About 94% of production by LUKOIL Group in 2009 was in Russia, so prices for Russian Urals export blend had decisive impact on the Company's financial results. Due to lack of a quality bank in the Transneft pipeline system, oil of any quality delivered through that system is sold at the Urals price, so that Urals is the Company's main crude export. LUKOIL exported over 20% of its oil by-passing the Transneft system in 2009 compared with 8% in 2008. Growth in the share of deliveries by alternative routes was due to rapid development of the Yuzhnaya Khylchuya field in Timan-Pechora: oil from this field is shipped through the Varandey terminal, which was commissioned by the Company in 2008. These deliveries were valued by factual quality of the oil, giving a premium to the Urals price.

REVENUE STRUCTURE OF A RUSSIAN CRUDE OIL EXPORTER, $ PER BARREL



The average price for Urals blend in 2009 was $61.2 per barrel, which was 35.5% less than in 2008. The average price gap between Urals and Brent in 2009 was $0.5 per barrel, compared with $2.5 per barrel a year earlier. The much stronger position of Urals on the world market in 2009 was due to substantial reduction in output of competing crude varieties by OPEC countries. Shortage of semi-heavy sulphurous crude forced refiners to compete for available oil. Narrowing of the price differential was also due to adaptation of the world refining industry to a new level of demand for petroleum products (levels of demand for heavier and lighter crude types are evening out), and increase of margins on fuel oil production. Narrowing of the price gap between types of crude is a positive factor for the Company, enabling it to obtain substantial additional revenue.

For objective assessment of the market environment, in which the Company operated in 2009, it is important to take account of the tax burden on Russian oil exporters and how it changed in comparison with 2008.

The Company pays mineral extraction tax on its crude production inside Russia. Mineral extraction tax on oil was reduced by 45.8% in dollar terms in 2009, due to lower oil prices and steps taken by the Russian Government in 2008 to lower the tax rate, and the average tax level for the year was $9.9 per barrel.

The Company pays export tariffs on crude oil exports from Russia calculated using a progressive scale based on Urals prices. Export tariffs on crude oil decreased by 49.3% in 2009 and the average rate for the year was $24.5 per barrel. It should be noted that changes made by the Russian Government at the end of 2008 to the system for calculating export tariffs rendered the mechanism more efficient and timely (the time lag in calculation of duties was reduced).

The price of Urals oil for a Russian exporter net of taxes (the international market price without export tariffs and mineral extraction tax) was $26.8 per barrel in 2009. The share of mineral extraction tax and export tariffs in the average annual oil price was 56.2%, which is roughly equal to the average level in the last five years.

LUKOIL pays taxes in international projects based on production sharing agreements (PSAs), concession agreements and current legislation in respective countries. For example, the concession agreement in Egypt makes the Company liable only for income tax and a tax on personnel, with exemption from other taxes, tariffs and duties. Income tax is paid for LUKOIL by the Egyptian General Petroleum Corporation from LUKOIL's share of production. In Kazakhstan a new Tax Code came into force from January 1, 2009. It includes several significant changes with respect to Company projects: taxes paid by the Company are to be governed by current legislation (without possibility of fixing the tax regime as of the date of the legislation becoming effective), making LUKOIL liable for payment of income tax, a tax on super profits, a mineral extraction tax and a progressive rent tax. Taxation of projects regulated by PSAs remains as stated in the agreements. The changes in taxation regimes and lower oil prices led to decline of tax payments in international projects in 2009.

Gas Market

LUKOIL produces most of its gas inside Russia, and as part of the Kandym – Khauzak – Shady project in Uzbekistan, the Karachaganak project in Kazakhstan, and the Shakh Deniz project in Azerbaijan.

Marketable gas produced in Russia is sold to Gazprom and directly to Russian consumers. The Company cannot export the gas, which it produces, since Gazprom has a monopoly on gas exports and owns the gas transport system. Gazprom greatly reduced its purchases from independent producers in Russia in 2009 due to lower international demand for gas. The Company therefore reduced production of marketable gas in Russia by 16.9%. There was some recovery of demand towards the end of the year, which led to an increase in production.

The price environment on the Russian gas market was relatively favourable in 2009. Domestic prices for gas remained unchanged despite the sharp fall in oil prices, reflecting Government strategy. As a result the Company's average-weighted price for gas sales to Gazprom and other customers was the same as in the previous year (1,152 roubles per 1,000 cubic meters). However, the domestic gas price was naturally lower than in 2008 in dollar terms.

The Company pays mineral extraction tax for gas in its Russian gas production business. The tax rate for gas remained unchanged in 2009 compared with 2008 at 147 roubles per 1,000 cubic meters.

Production of marketable gas by LUKOIL in international projects rose by 1% in 2009. More than 50% of gas production outside Russia is at the Khauzak-Shady project in Uzbekistan. Gas from Khauzak-Shady is sold at an official price, fixed by agreements between Russia and Uzbekistan. The price in 2009 exceeded $190 per 1,000 cubic meters. Royalty is paid on production at a rate of 30% as part of the agreement. LUKOIL has a seven-year holiday from income tax, beginning from the start of production, at the end of which income tax will be payable at a preferential rate. The Uzbek Government share in profit production varies depending on the project's internal rate of return for LUKOIL Group, so the effective tax scale is progressive.

Natural gas produced as part of the Karachaganak project in Kazakhstan is supplied to the Orenburg Gas-processing Plant. Taxation in this project is specified by terms of the PSA (see above, 'Price and Tax Environment. Crude Oil Market' on page 18).

Gas produced at the Shakh Deniz field is supplied to the domestic market in Azerbaijan and also via the Southern Caucasus pipeline to Georgia and Turkey, where it is sold at market prices. Under terms of the PSA in Azerbaijan, LUKOIL is exempt from payment of taxes in cash on production and export of gas. The only significant tax paid by the Company is income tax at a fixed rate (the tax is withheld as a share of production).

Inflation and Exchange Rate

LUKOIL Group produces most of its hydrocarbons inside Russia, so a significant part of Company costs are in roubles and change in value of the rouble against the dollar, both nominal and real (taking account of inflation), changes the level of Company costs in dollars. The rouble weakened against the dollar by 12.4% in real terms in 2009, and this was one of the main reasons for reduction in unit costs of hydrocarbon production in Russia, which fell from $4.11 to $3.53 per boe, or by 14.1%. The fact that decline of production costs was greater than depreciation of the national currency shows that production optimization, work with suppliers and contractors, and use of the latest technologies enabled the Company to achieve high-quality cost savings in 2009.

Weakening of the rouble in real terms and an anti-crisis program for cost reduction in 2009 were the main reasons for lowering of capital expenditures in the E&P segment in Russia by 42.5%.

Capital expenditures in the international E&P segment declined by 28.3%. The decline was less than in Russia, due to growing scale of Company operations abroad. LUKOIL was also successful in controlling hydrocarbon lifting costs, which decreased by 7.6% in 2009.

Lifting costs declined by 13.6% on average across the Group, from $4.12 to $3.56 per boe. Capital expenditures in the E&P segment declined by 40.6% to $4,687 million.

The Company maintained tight financial discipline in 2009. Work with suppliers and contractors together with weakening of the national currency enabled substantial cost savings in dollar terms.

Acquisition of Assets

The Company continued dynamic increase of its resource potential and production capacities through acquisition of highly efficient assets. Expenditures on asset restructuring and acquisition of new assets in the E&P segment were $544 million in 2009.

The main acquisition by the Group was of a 46% stake in the joint venture LUKARCO B.V. from a subsidiary of BP. As a result, LUKOIL now owns 100% of LUKARCO B.V. Value of the transaction was $1.6 billion, to be paid over the next two years (the first tranche of $300 million was paid in December 2009).

LUKARCO B.V. owns 5% of the joint venture, Tengizchevroil, which develops the Tegniz and Korolevskoye fields in Kazakhstan. The transaction increased proved reserves of LUKOIL by 102 million barrels of oil and 130 billion cubic feet of gas, while the increase in production was more than 13,000 barrels per day.

LUKARCO B.V. also owns 12.5% of the Caspian Pipeline Consortium (CPC), which transports oil from Kazakh and Russian fields to the oil terminal at Novorossiysk. Physical throughput capacity of the CPC is currently 28.2 million tonnes per year and will be increased to 67 million tonnes per year in the future.

Consolidation of 100% in LUKARCO B.V. is of great importance, since it strengthens Company positions in the strategically important Caspian region.

Also in 2009 a consortium between LUKOIL and Statoil won a tender for development rights for the huge West Qurna-2 field in Iraq. Recoverable reserves at the field are estimated at 13 billion barrels of oil (see details on page 40).

Optimization of Corporate Structure and Consolidation

LUKOIL pursued optimization of its corporate structure in 2009 in order to improve efficiency of business management at its subsidiaries and to reduce administrative expenses.

The Group consolidated 100% of its subsidiary, OJSC RITEK, by purchase of about 25% of shares in the subsidiary. RITEK specializes in oil production in the European part of Russia and in Western Siberia and also has major R&D activities.

The Group made cost savings and reduced the headcount by disposal of 10 service companies, which were previously part of LUKOIL-Western Siberia. The disposal is part of Group strategy for withdrawal of non-core assets.

LUKOIL carried out a major restructuring of its electricity generating assets. The Group's stake in UGK TGK-8 was increased from 95.53% to 100% by purchase of shares from minorities and UGK TGK-8 itself was converted from an open joint-stock company into a limited liability company. Stakes in the generator, which had previously belonged to companies within the Group, were transferred to the parent company, OJSC LUKOIL.

Licensing

The Company successfully addressed a number of tasks associated with licensing during 2009: obtaining new licenses for mineral resource exploitation; securing reissue of licenses to reflect reorganization of subsidiary companies; changing and adding to conditions of use of mineral resources; extending the duration of licenses up to full field depletion; and optimizing the license portfolio.

There were 413 licenses on the balance of LUKOIL Group companies at the end of 2009, of which 337 were for exploration and production of hydrocarbons, 56 were for geological studies, exploration and production, and 20 were for geological study, including prospecting and evaluation of mineral fields.

The Company obtained 9 new licenses for use of mineral resources in 2009, of which 4 were based on proof of a field discovery, and 5 were obtained through auctions and competitions. Spending on license acquisitions was $40 million.

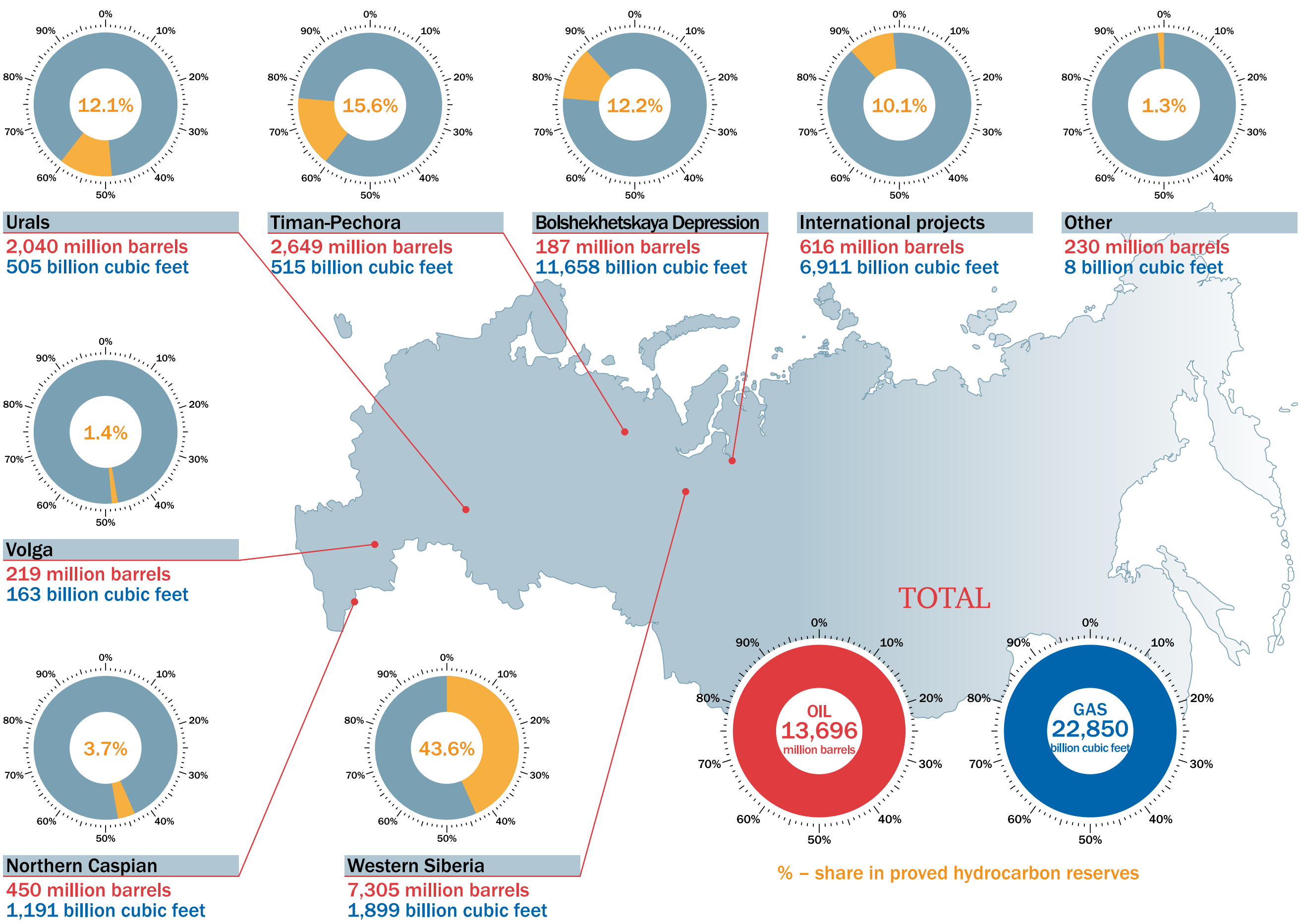
A total of 6 licenses for use of mineral resources were reissued during 2009 in connection with ongoing optimization of corporate structure of LUKOIL Group.

The Group registered 33 additions to licenses in 2009 in order to extend their period of validity. Work also continued on amendments and additions to current license agreements. A total of 54 additions were obtained to reflect changes in geological exploration schedules, clarification of borders of license areas, confirmation of ownership rights to production from license areas, and clarifications concerning obligations to achieve specific production levels in accordance with project documentation, as well as other issues.

Oil and Gas Reserves

Reserve replacement is fundamental to long-term, sustainable development of the Company. LUKOIL Group carries out extensive geological exploration work in Russia and abroad in order to increase its reserves, and also monitors new projects and assets, which could represent acquisition targets, on a constant basis.

PROVED OIL & GAS RESERVES OF LUKOIL GROUP BY REGIONS IN 2009



According to data audited by Miller and Lents (USA), the Company's proved reserves of hydrocarbons as of January 1, 2010 were 17.504 billion boe, consisting of 13.696 billion barrels of oil and 22.850 trillion cubic feet of gas.

The audit was carried out to the standards of the US Securities and Exchange Commission (SEC). The Company decided to adopt SEC standards for measurement of reserves in order to ensure greater transparency and comparability with respect to competitors.

The greater part of the Company's proved reserves of oil are in Western Siberia, Timan-Pechora and the Urals region. The main part of proved gas reserves are in the Bolshekhetskaya Depression, Uzbekistan and the Caspian region. 58% of Company proved reserves are in development (64% of oil reserves and 34% of gas reserves). This reserve structure reflects large potential of the Company to increase production in the medium term, particularly production of gas.

Most of the Company's proved hydrocarbon reserves are conventional. Only about 4% of the total represent high-viscosity oil and 4% are at offshore fields. This reserve structure enables the Company to ensure efficient control of development costs and to bring new fields into production rapidly.

Reserve appraisal was carried out with due account for changes to field development plans, as set out in the LUKOIL Group Program for Strategic Development in 2010–2019.

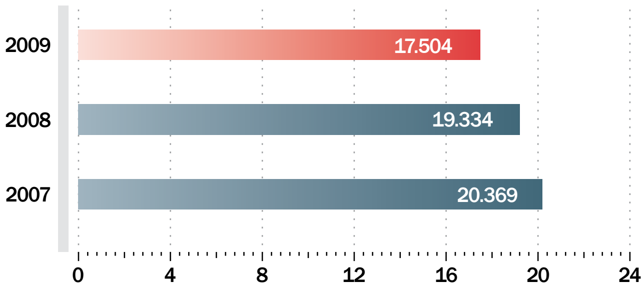
In accordance with SEC requirements, proved reserves that are not in development can only be recognized if there is an approved development plan. The plan must stipulate that development of the relevant reserves will start within five years, unless specific circumstances justify a longer period

OIL & GAS RESERVES OF LUKOIL GROUP

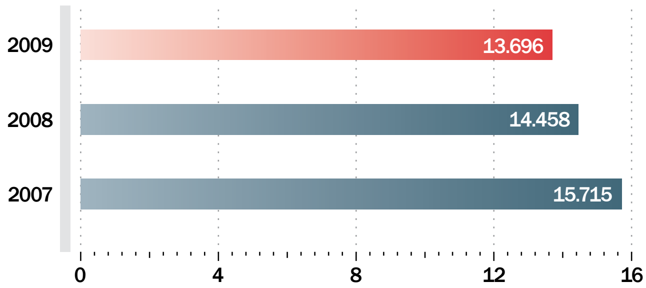
January 1, 2010	Oil (million barrels)	Gas (billion cubic feet)	Hydrocarbons* (million boe)
PROVED RESERVES	13,696	22,850	17,504
of which:			
Developed	8,827	7,795	10,126
Undeveloped	4,868	15,055	7,377
PROBABLE RESERVES	7,293	15,163	9,820
POSSIBLE RESERVES	3,683	8,226	5,054

* The ratio used for recalculation of cubic feet as barrels of oil equivalent (boe) is: 1 boe = 6,000 cubic feet.

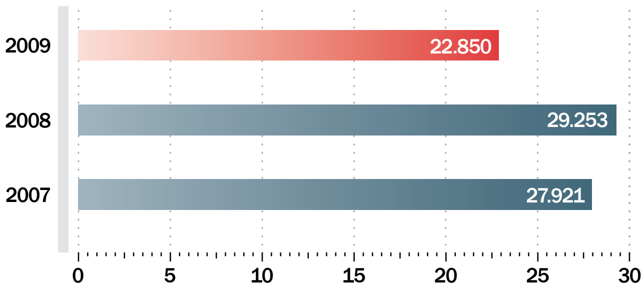
PROVED HYDROCARBON RESERVES, BILLION BOE



PROVED OIL RESERVES, BILLION BARRELS



PROVED GAS RESERVES, TRILLION CUBIC FEET



before the start of development. In order to take account of changes to development plans and launch schedules for several fields, the Company reclassified 1.8 billion boe of proved reserves as lower-category reserves and as conditional resources (most of the reclassified reserves are gas, reflecting changes to launch schedules for a number of Caspian projects). The Company believes that these volumes may be transferred back to the proved reserve category as development launch times approach.

Growth of proved reserves in 2009 due to geological exploration work, production drilling and acquisitions was 782 million boe, representing 95% of production during the year. Growth due to geological exploration work and production drilling was 617 million boe, and 165 million boe were added as a result of acquisitions. So organic growth of hydrocarbon reserves compensated about 75% of production (75% for oil and 73% for gas). Most of the organic growth of proved oil reserves was obtained in Western Siberia (55% of the total) and the Caspian region (24% of the total). Most of organic growth in proved gas reserves was obtained in the Caspian region (16% of the total) and in two international projects: Kandym – Khauzak – Shady and Shakh Deniz (63% of the total).

The main acquisition in 2009 was 46% of LUKARCO B.V., owner of a 5% stake in the joint venture, Tengizchevroil, which is developing the Tengiz and Korolevskoye fields in Kazakhstan. The transaction increased the Company's proved reserves by 102 million barrels of oil and 130 billion cubic feet of gas.

Reserves at the West Qurna-2 field were not included in reserve appraisal because the contract for development and production at that field was signed after the appraisal date. The Company plans to include its share of reserves at West Qurna-2 in the next appraisal and audit of hydrocarbon reserves.

As can be seen, LUKOIL remains one of the Russian and international leaders by volume of proved hydrocarbon reserves. The Company's ratio of proved hydrocarbon reserves to production is 21 years (19 years for oil and 37 years for gas).

Geological Exploration

The chief objective of LUKOIL's geological exploration work is to replace production with new commercial reserves of hydrocarbons, and to prepare reserves for rapid launch and expansion of production in promising regions (Timan-Pechora, the Northern Caspian and the Bolshekhetskaya Depression). The Company maximizes efficiency of its geological exploration work by use of the latest technologies.

Most of the Company's geological oil & gas exploration work in 2009 was concentrated in Western Siberia, Perm territory, Volgograd Region and Timan-Pechora. The Company's largest prospecting projects in 2009 were further exploration work at the Tsentralno-Astrakhanskoye gas and condensate field, study of geological structure and oil & gas potential at the Denisovskaya Depression in Timan-Pechora, and study of oil & gas potential at sites, which are part of the Riyadh (Block A) project in Saudi Arabia.

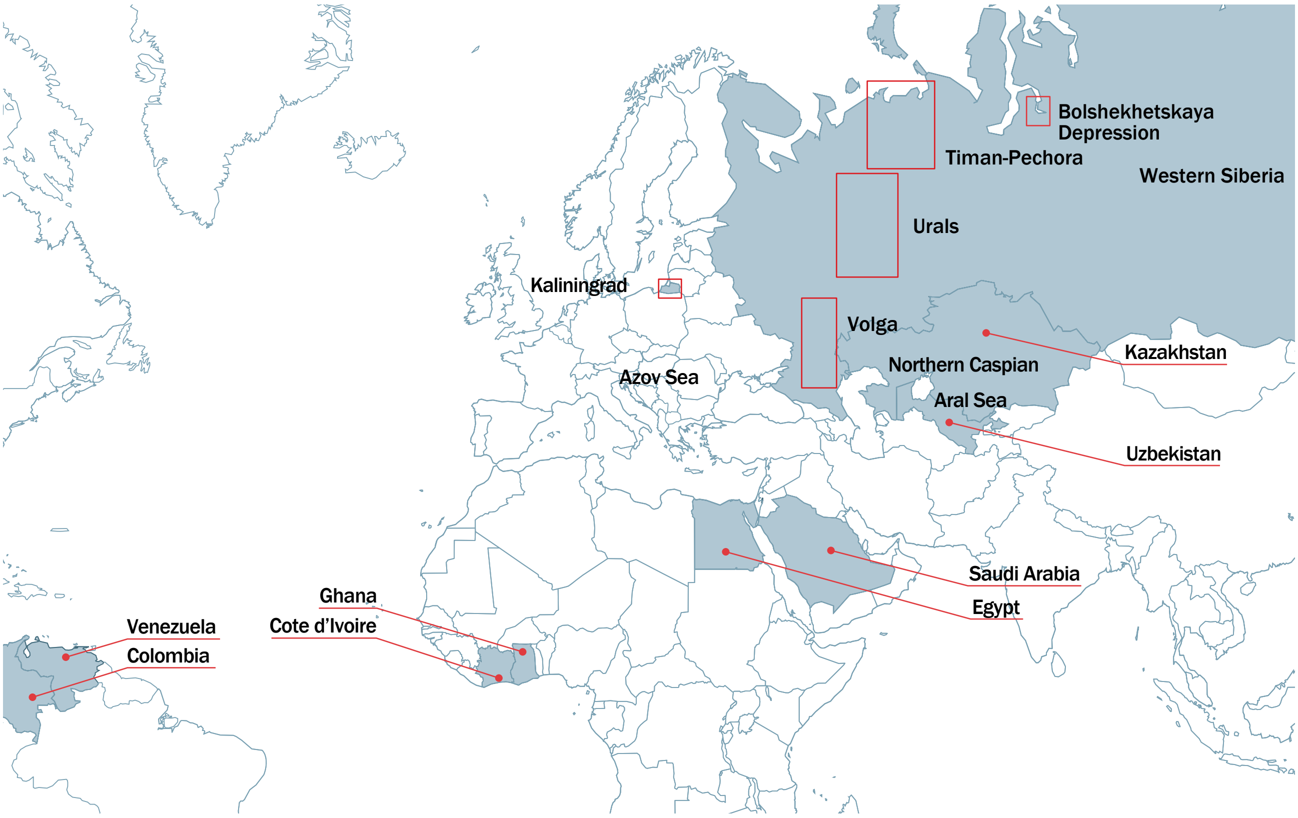
The Company carried out 2,446 km of 2D seismic and 4,548 km^2 of 3D seismic during 2009 in order to locate and detail geological structures and to prepare for drilling of prospecting and exploration wells at promising sites. In recent years the Company has improved quality of its seismic exploration work and speeded up processing and interpretation of data, mainly thanks to use of the latest IT solutions. High quality of seismic exploration keeps the average success rate of exploration drilling across the Group at a level above 70%.

Geoelectric exploration totalled 2,267 km in 2009. Vertical seismic profiling, which details the geological structure around a drilled well, was carried out at 9 wells. Total exploration drilling in 2009 was 79,600 meters and efficiency of exploration work rose from 929 to 1,612 tonnes of reference fuel per meter drilled. LUKOIL completed 33 prospecting and exploration wells in 2009, of which 24 were productive. The success rate of prospecting and exploration drilling was 73%.

One new field was discovered in 2009 (the Timerovskoye field in Tatarstan) as well as 17 new deposits at previously discovered fields.

Increase of proved reserves under international classification during 2009 through geological exploration and additional information obtained in the course of production drilling amounted to 617 million boe. Most of the growth of liquid hydrocarbon reserves as a result of geological exploration work was in Western Siberia. Spending by LUKOIL Group on geological exploration work totalled $394 million in 2009.

MAIN GEOLOGICAL EXPLORATION REGIONS OF LUKOIL GROUP



Russia

Exploration drilling in Russia in 2009 totalled 62,900 meters, 2D seismic exploration was 2,325 km and 3D seismic was 2,375 km^2. Spending on geological exploration in Russia was $172 million.

Western Siberia

Khanty-Mansiysk Autonomous District-Yugra

The Khanty-Mansiysk Autonomous District-Yugra is the main oil production base of LUKOIL Group. The chief aim of geological exploration work there is replacement of reserves in order to maintain the Group's current production levels in the region. Although reserves in the region have been extensively explored, geological exploration work there is highly efficient and successful.

Exploration drilling in the District totalled 29,400 meters in 2009 and 17 wells were completed, of which 11 were productive. The success rate of exploration drilling was 65%. The main task in the reporting year was study of oil & gas potential of Neocomian, Achimian and Jurassic sediments in the vicinity of earlier discoveries. The Company carried out 503 km of 2D seismic and 1,577 km^2 of 3D seismic. Most of the work was in peripheral areas of large fields, and was aimed at detailing oil & gas contours and identifying oil saturation in strata ahead of production drilling. A total of 12 new oil deposits were found at previously discovered fields in the District during 2009. Reserve growth was mainly due to 3D seismic work and exploration drilling at the Urevskoye, Vostochno-Perevalnoye, Mortymya-Teterevskoye, Tevlinsko-Russkinskoye, Kochevskoye, Klyuchevoye and Pokachevskoye fields. The Company's proved hydrocarbon reserves to SEC standards in Khanty-Mansiysk Autonomous District-Yugra were 7.5 billion boe by the end of 2009. Strong flows of oil were obtained at several fields.

A gushing flow of oil (1,200 barrels per day) was obtained from testing of a well at the Severo-Pokamasovskoye field. Proved reserves of oil at the field were increased by 2.7 million barrels.

An oil flow of 400 barrels per day was obtained from the Tyumen strata as a result of testing of a well drilled in the north-western section of the Potanay-Kartopinsky license area. A daily oil flow of 300 barrels per day was obtained from testing of a well at the Yuzhno-Vyintoiskoye field. A well was drilled at the Gribnoye field for further exploration of the eastern part of the field, and testing gave a daily flow of 400 barrels. Testing of Achimian sediments at the Vostochno-Perevalnoye field gave a gushing flow of 700 barrels per day. A directional exploration well was drilled at the same license area, and testing gave a gushing oil flow of 300 barrels per day from Achimian sediments.

Work was also carried out to demothball, retest and raise flow rates from previously drilled prospecting and exploration wells at the Bolshoy and Olkhovsky areas. Well flows of about 100 barrels per day were obtained.

Yamal-Nenets Autonomous District

LUKOIL is developing gas reserves at the Bolshekhetskaya Depression in Yamal-Nenets Autonomous District as part of its program for accelerated growth of gas production. The Company is also working at the Severo-Gubkinskoye, Prisklonovoye, Yuzhno-Tarasovskoye oil, gas and condensate fields, as well as the Urabor-Yakhinsky and Vansko-Namyssky areas.

The Company continued testing of a well drilled in 2008 at the Khalmerpayutinskoye field and obtained a gas and condensate flow. Daily flow rates from the well were 131,000 cubic meters of separator gas and 100 barrels of stable condensate. Testing of a well also continued at the Severo-Khalmerpayutinskoye field, where a gas and condensate mix was obtained, consisting of 324,000 cubic meters of gas and 100 barrels of condensate per day.

Proved gas reserves at Company fields in the Bolshekhetskaya Depression were 11.7 trillion cubic feet by the end of 2009, representing over 50% of LUKOIL's total gas reserves.

Timan-Pechora

Timan-Pechora (the Nenets Autonomous District and Komi Republic) is a promising region for oil production by the Company. The region is little studied, with high potential for new discoveries, and the Company carried out extensive geological exploration work there during 2009. Volumes of 2D and 3D seismic work during 2009, for clarification of geological models, were 1,349 km and 391 km^2, respectively, and exploration drilling was 9,800 meters. Most of the growth of oil reserves including production was at the Bayandyskoye and Oshskoye fields.

In the **Komi Republic** the Company carried out geological exploration work at the Denisovskaya and Khoreiverskaya depressions and also at the Kolvinsky Rise. Two wells were completed and both of them were productive, so drilling was 100% successful.

The Company carried out 999 km of 2D seismic at the Yuzhno-Khoreiversky and Severo-Denisovsky areas and 391 km^2 of 3D seismic at the Vostochno-Bayandyskaya and Vostochno-Lambeishorskaya areas.

Prospecting and exploration drilling totalled 10,000 meters. Drilling of a prospecting well at the Bayandyskoye field continued, penetrating Riphean sediments of the Upper Devonian sediment. Well testing gave daily oil flows of 400 barrels. Proved oil reserves at the field including production increased by 15%.

Growth of oil reserves including production thanks to 3D seismic work and exploration drilling was 6.4%.

Testing of a prospecting well was completed at the Oshskoye field in **Nenets Autonomous District**, and a daily flow of 1,100 barrels of oil was obtained. Proved oil reserves at the field including production increased by 35.1%.

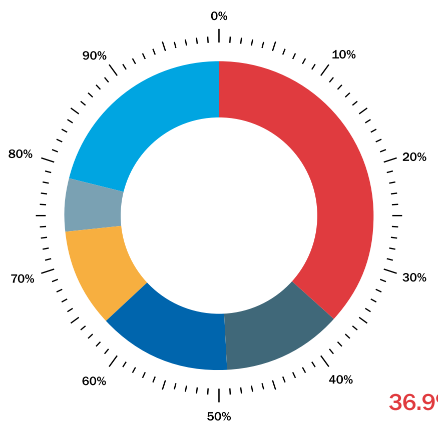
Naryanmarneftegaz, the joint venture between LUKOIL Group and ConocoPhillips carried out 350 km of 2D seismic exploration at the Vostochno-Perevoznaya area in the region of Khaipudyrskaya Bay.

Urals region

The Urals is a traditional production region for the Company, and reserves in the region have been extensively explored. Total 158 km^2 of 3D seismic exploration was carried out in the region in 2009 for general geological purposes, of which 77 km^2 at the Volimskaya area. The purpose of the work was to obtain data on hydrocarbon presence at the Urtsevskaya and Semisosninskaya structures, and also to determine best locations for appraisal wells at the Maltsevskoye field. The work is scheduled for completion in 2010. Exploration drilling totalled 8,000 meters, and most of it was in the vicinity of sites with established commercial oil presence.

Three wells were completed and all of them were productive. Commercial oil flows of 100–200 barrels per day were obtained from testing of Tulskoye, Bobrikovskoye and Famenskoye sediments. Four deposits were found at previously discovered fields (Mokhovskoye, Vinnikovskoye and Gabyshevskoye). Overall reserve growth including production in the region was 2.4%.

EXPLORATION DRILLING BY REGIONS (2009)



36.9%	Western Siberia
12.3%	Timan-Pechora
14.0%	Volga
10.2%	Urals
5.7%	Other
20.9%	International projects

Volga (onshore)

The Volga is also a traditional hydrocarbon production region for LUKOIL. Geology of the region has been extensively studied. Total 170 km of 2D seismic was carried out in **Volgograd and Astrakhan Regions** during 2009 at the Potemkinsky, Berezovsky and Zhuravsky license areas. The results will be used to plan future prospecting work. Exploration drilling totalled 9,400 meters.

Exploration drilling was carried out at the Stepnoye field, where a well, begun in 2008, was completed with bottomhole at depth of 3,300 meters in the Mosolovsky horizon. Testing in the process of drilling confirmed forecast presence of oil deposits in the upper sandstone stratum of the Pashiysky horizon on a north-eastern axis. A daily oil flow of 100 barrels was obtained, and an oil deposit was discovered in the sediments of the Vorobievsky horizon.

Drilling of 71 meters in 2009 completed an exploration well Tsentralno-Astrakhanskaya №2 at the Poimenny license area with bottomhole at depth of 4,390 meters. Purpose of the well was to define structure of the Tsentralno-Astrakhanskoye field and enable transfer of reserve to commercial categories. Testing at an interval of 4,248–4,282.5 meters gave daily flow of 210,000 cubic meters of gas. Reserves are now being estimated. As of the start of 2010 probable and possible reserves at the Tsentralno-Astrakhanskoye field were estimated at 10.2 trillion cubic feet of gas and 1.2 billion barrels of condensate, which is comparable with reserves at the Karachaganak field in Kazakhstan. Gas at the Tsentralno-Astrakhanskoye field contains very high levels of hydrogen sulphide. However, this problem can be solved by application of modern technologies, as shown by Gazprom during development of the adjacent Astrakhanskoye field.

In the **Republic of Tatarstan** the Timerovskoye oil field was discovered in the central part of the Nizhnekamskoye reservoir at the Menzelinsky license area. Testing of Carbonaceous sediments (Turneisko-Famensky strata) gave a commercial oil flow of 1,100 barrels per day. Initial estimates suggest that C1 oil reserves (Russian classification) are 3 million tonnes. 260 km of 2D seismic was carried out in Tatarstan to determine geological structure of areas, and to discover and prepare sites for deep drilling.

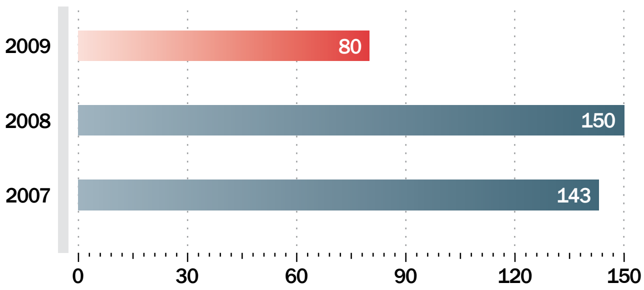
Northern Caspian

The Northern Caspian is one of the key regions for increase of oil & gas production by LUKOIL in the medium term and the Company attaches great importance to development of resource potential in the region.

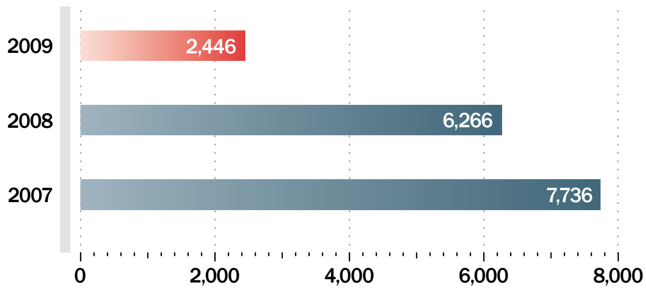
Rakushechnaya well № 5 at the V.Filanovsky field was completed with bottomhole at depth of 1,650 meters in Mid-Jurassic sediments. Testing of Neocomian sediments gave a gushing flow of water-free oil at maximum daily rate of 600 barrels. Rakushechnaya well № 5 confirmed the structural plan of deposits and determined location of the water-oil contact of deposits in Aptskian and Neocomian sediments. Appraisal of hydrocarbon reserves is now being carried out.

The Caspian Oil Company, in which a subsidiary of LUKOIL owns 49.89% (another 49.89% is owned by a subsidiary of Rosneft and remaining shares belong

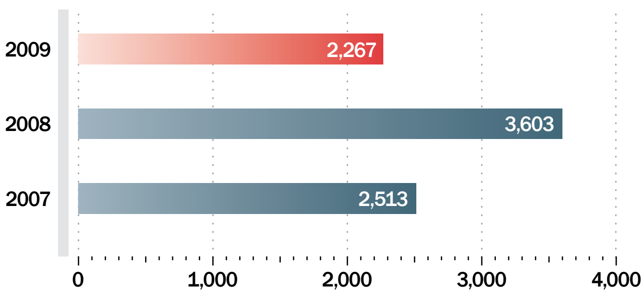
EXPLORATION DRILLING, THOUSAND METERS



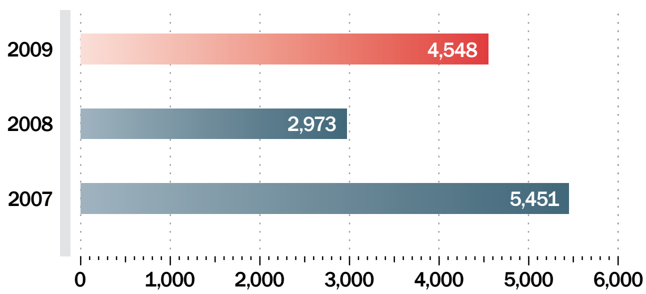
2D SEISMIC, KM



GEOELECTRICS, KM



3D SEISMIC, KM²



to Gazprom), completed 3D seismic exploration work at the Zapadno-Rakushechnoye field, which was discovered in 2008. A total of 106 km^2 of 3D seismic was carried out at the field over two years, of which the Company share in 2009 was 21 km^2. Equipment was bought and work was carried out on design and receipt of approvals ahead of prospecting drilling at the Ukatnaya structure in 2010.

TsentrCaspneftegaz, in which LUKOIL owns a 50% stake (50% is owned by Gazprom), completed 567 km^2 of 3D seismic exploration work that was begun in 2008 at the Tsentralnoye field. The Company's share of the work in 2009 was 228 km^2. These materials are now being processed. The Agreement (and Protocol to the same Agreement) between Russia and Kazakhstan on demarcation of the seabed in the northern part of the Caspian Sea for purposes of mineral use gives the Russian Federation rights of mineral use at the Tsentralnaya structure. However, the Agreement also stipulates that, in case of discovery of commercial reserves, development is to be carried out by Russia and Kazakhstan on parity basis.

Azov Sea

Priazovneft, in which LUKOIL Group has a 42.5% stake (42.5% is owned by a subsidiary of Rosneft and 15% belongs to the State Property Fund of Krasnodar Territory) carried out 2D seismic work during 2009, in which the Group's share was 42 km. In 2007 Priazovneft discovered the Novoye offshore field in the Azov Sea, offering the first confirmation of oil & gas promise of the Azov shelf. A joint meeting of geologists was held with Rosneft to review the outcome of work to date, and it was decided to carry out additional geological exploration work for study of the central part of the license area. The Tizdar-more structure was confirmed as promising, and a feasibility study will be carried out in order to assess viability of development, after which a program for additional study of the structure will be drawn up.

Kaliningrad Region

LUKOIL carried out geological work in 2009 in Kaliningrad Region both onshore and in the offshore Baltic Sea.

A prospecting well was completed at the Severny license area with bottomhole at depth of 2,217 meters in Mid-Cambrian sediments (drilling in 2009 was 7 meters). The drilling did not find oil-bearing deposits and the well was closed down.

The Company also reinterpreted 3D seismic work at the Kravtsovskoye and Druzhbinskoye fields.

International Projects

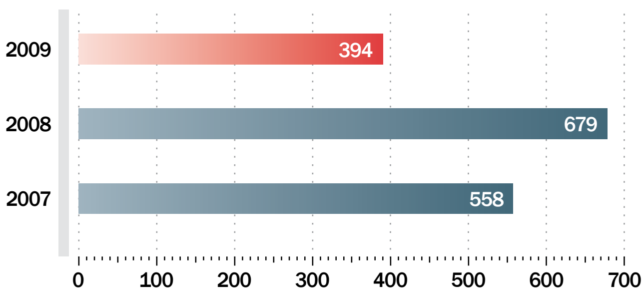
In accordance with LUKOIL's strategy for intensive development of its international business in the E&P segment, the main task of geological exploration by the Company outside Russia is to prepare the resource base for rapid launch of production. Exploration drilling in international projects in which LUKOIL participates was 16,600 meters in 2009. The Group's share of 2D seismic work in international projects in 2009 totalled 121 km and its share of 3D work was 2,173 km^2. Spending on geological exploration outside Russia was $222 million.

LUKOIL was involved in 13 geological exploration projects outside Russia in 2009: in Colombia, Kazakhstan, Saudi Arabia, Uzbekistan, Cote d'Ivoire and Ghana.

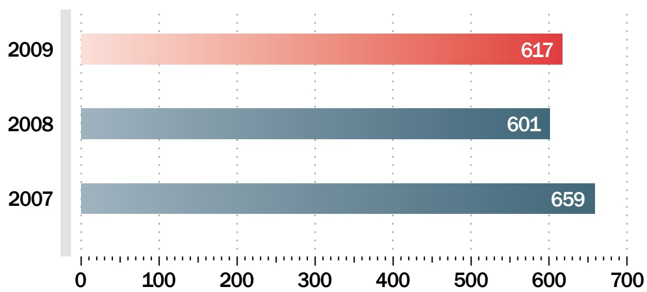
LUKOIL Group has a 56.66% stake in the **Cape Three Points Deep Water block in the Republic of Ghana** where drilling of the Dzata-1 well was begun in 2009. Bottomhole at the end of 2009 was at 4,175 meters and at the start of 2010 the well penetrated a 94-meter column of hydrocarbon saturation containing a multi-deposit oil & gas accumulation with effective capacity of 25 meters. The main sandstone collector contains gas and light oil. Drilling has now been completed and the well has been sealed and suspended so that additional reserve estimates can be carried out.

In the **Riyadh (Block A) project in Saudi Arabia** two prospecting wells were drilled, Abu-Nasr-1 and

EXPLORATION COSTS, $ MILLION



HYDROCARBON RESERVE EXTENSIONS AND DISCOVERIES, MILLION BOE



Faidakh-2, and drilling of an appraisal well, Tukhman-4, was begun. Open-hole testing of Faidakh-2 as part of joint development of the Sara section gave a steady flow of gas at average 81,000 cubic meters per day. The well was mothballed so that it can be cleaned and studied in order to obtain maximum possible flows. Geological exploration work in 2009 at the Mushaib field gave an increase of reserves by 10.3 million tonnes of reference fuel under Russian classification (this project is not included in reserve appraisal to SEC standards).

The geological exploration stage was completed in 2009 at the **Condor project in Colombia**. All contractual obligations have now been completed in full. LUKOIL agreed a program of test production for commercialization of the Medina field, which was discovered in 2006, and obtained a two-year extension for that purpose. R&D work carried out in 2008–2009 led to creation of a new tectonic model of the Condor block based on 2D and 3D seismic. In the eastern part of the block work was carried out to detail the Amarilo structure, which consists of a number of structural-tectonic groupings at different depths in close proximity to one another. Six groupings were identified in total. The first stage of preparatory work for drilling of the Amarilo-1 well began at the end of 2009, as well as work on an environmental impact assessment and application for an environmental license.

An investment consortium, in which LUKOIL has a 20% stake, carried out 606 km of 2D seismic as part of the **Aral project in the Uzbek sector of the Aral Sea**. All 2D seismic obtained since 2007 was processed and interpreted, as a result of which four structures were selected for drilling: the Western Aral, Umid, Ak-Tepe (Northern Umid) and Shagala structures. Drilling of prospecting well WAEx (Western Aral) was begun and continued into 2010.

Processing and interpretation of seismic exploration materials from 2008 was completed at the **Kungrad block in Uzbekistan** in 2009, as well as environmental monitoring of the area. The work confirmed presence of commercial gas reserves at the Shege field. Geological structure and development history of the block was also clarified and it was established that new hydrocarbon accumulations could be found. A site was chosen and technical design work was carried out for Shege prospecting well №3.

Drilling of an exploration well was begun and will be continued in 2010 as part of the **South-West Gissar project in Uzbekistan**. Reprocessing and re-interpretation of seismic materials from previous years was also completed and structural-geomorphological analysis of relief at South-West Gissar was carried out. Preparatory and project work was completed ahead of 2D seismic surveying. The first stage of work for digitalization, reprocessing and reinterpretation of seismic materials from previous years was carried out at the Ustyurt block. A plan for 2D seismic surveying in 2010 was prepared, based on study of geological structure of the blocks.

Intensive studies were carried out in 2007–2009 as part of the **Tyub-Karagan** project in the **Kazakh sector of the Caspian Sea** in order to reduce geological risks. 2D seismic data were reprocessed and reinterpreted taking account of data from drilling of exploration wells, further geochemical studies and analysis were carried out (as well as other forms of analysis), basin modelling was completed, as was a structural-tectonic model of the block. As a result of this work, further priorities for geological exploration at Tyub-Karagan have been defined, and are mainly focused on the South Tyub-Karagan structure. A certificate for this structure was prepared and approved by the Company in 2009. Geological resources of the structure were 317.6 million tonnes of reference fuel under Russian classification.

The main task in 2009 as part of the **Atash** project was conduct of geological and geophysical studies following construction of a first exploration well in 2008 (the well failed to discover hydrocarbons and was closed down).

The exploration period at the **South Zhambai** and **South Zaburunye** blocks was extended to the end of 2011, and design work was carried out for construction of a first exploration well with planned depth of 1,850 meters. Work on the well will begin in 2010.

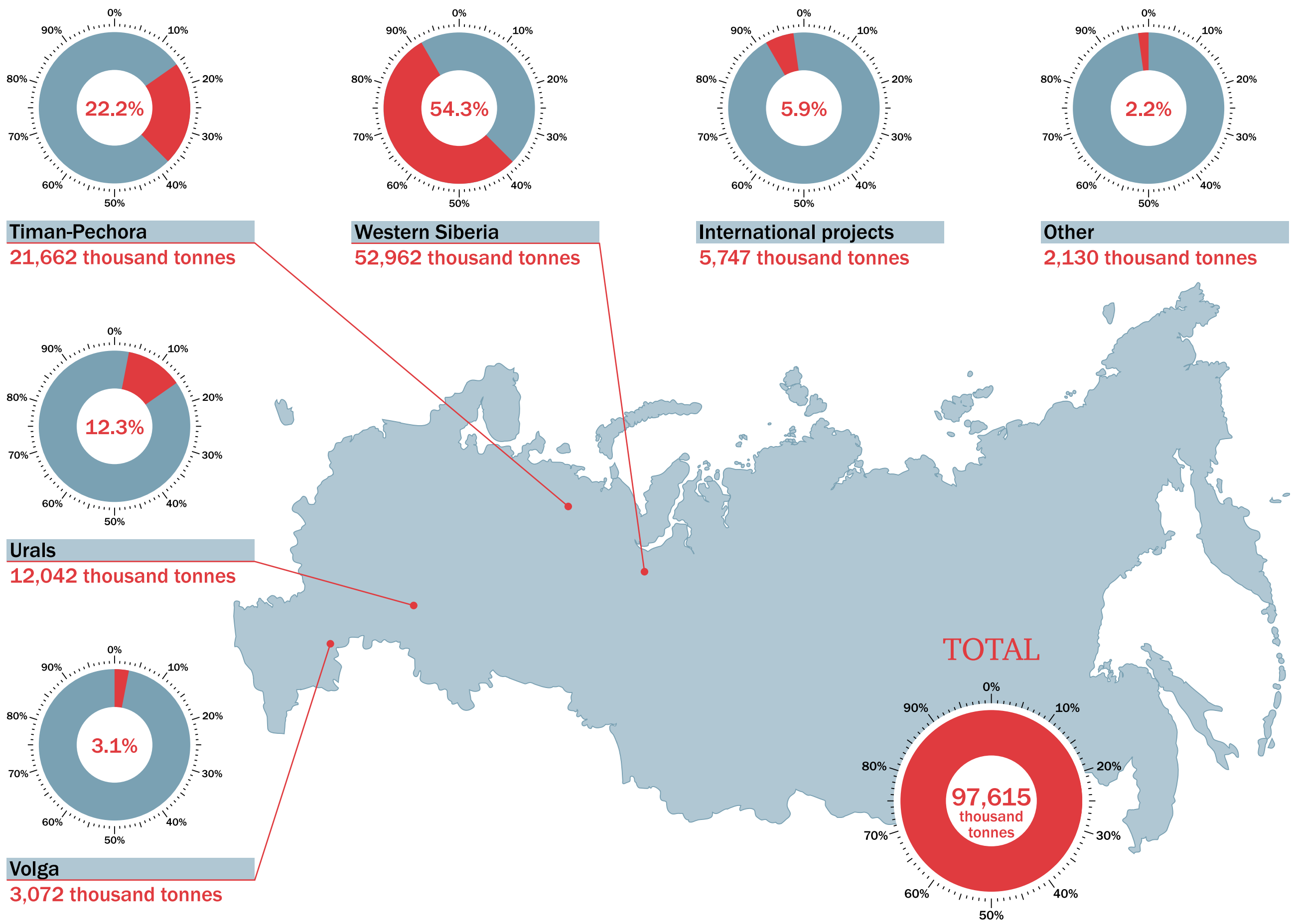
In **Cote d'Ivoire** 3D survey work totalling 1,658 km^2, 383 km^2 and 608 km^2 was carried out as part of the CI-101, CI-401 and CI-205 projects, respectively. Interpretation of all data will be completed in 2010. Three promising geological targets were mapped using 2D seismic in the eastern part of block **CI-205**. The drilling target will be chosen based on a ranking of all promising sites. An inversion was carried out on the Basam structure at block **CI-101**.

The Group became operator of the **WEEM Extension**, adjacent to the WEEM block in **Egypt**, in February 2009. Over 60% of the WEEM Extension was already covered by high-resolution 3D seismic carried out by the Group as part of the WEEM project in 2006. One well has been drilled at the area and has discovered 30 meters of oil-saturated formations. Two more wells will be drilled during the first phase of exploration work (by 2011).

Oil Field Development and Production

Total crude oil production by LUKOIL Group in 2009 (including share of production by equity affiliates) was 97.615 million tonnes (1.972 million barrels per day). Average daily output was 2.7% higher than in 2008.

LUKOIL GROUP OIL PRODUCTION BY REGIONS

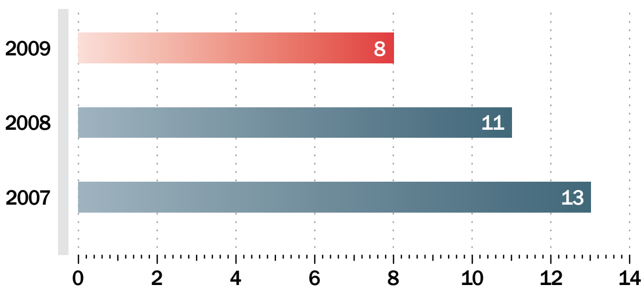


Growth of output was due mainly to operations at the Yuzhnaya Khylchuya field, which was commissioned in mid-2008 and also to international projects. Lower production at fields in Western Siberia had negative impact on the output trend and was due primarily to objective changes in the structure of recoverable reserves. The Company intends to reduce negative impact of these factors on production in Western Siberia by use of the latest enhanced recovery technologies. Meanwhile, LUKOIL has successfully addressed the problem of electricity supply shortages in Western Siberia. The Company is steadily building and commissioning its own power generating capacities at fields, and electricity supply shortages have now been almost completely overcome.

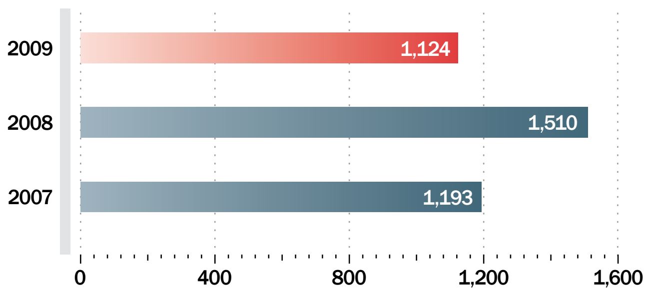
The Company expended much effort in the reporting year on preparation and construction of field facilities in the Northern Caspian. A fixed ice-resistant offshore platform with drilling unit was built at the Yu. Korchagin field, together with living quarters and transport infrastructure. The field will be developed using extra-long horizontal production wells (up to 5 km in length). This will be the first time that such technology has been used in Russia. **First oil at the Yu. Korchagin field was obtained in the second quarter of 2010.** Peak annual output at the field will be about 2.5 million tonnes of oil and 1 billion cubic meters of gas. Yu. Korchagin is the first field to have been brought into operation by the Company out of a whole group of fields in Russian territorial waters of the Caspian Sea.

Abrupt decline of oil prices in 2008–2009 encouraged the Company to work on improvement of field development efficiency and reduction of

COMISSIONING OF NEW FIELDS, FIELDS



OIL PRODUCTION WELL LAUNCHES, WELLS



operating costs. LUKOIL production companies carried out a range of measures to raise well productivity and oil recovery rates in order to achieve oil production targets for 2009. Spending on field development in 2009 was $4,421 million, which is about 40% less than in 2008.

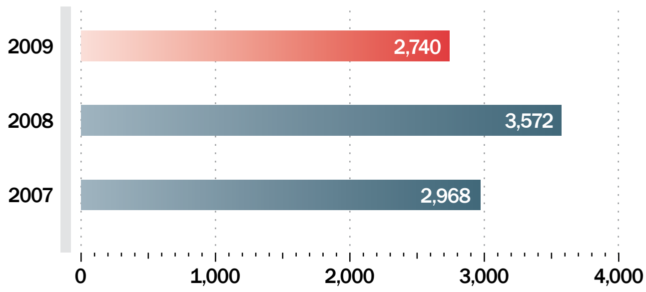
LUKOIL subsidiaries and equity affiliates produced hydrocarbons at 375 fields in 2009, and there were 8 new field launches: Aprelskoye, Bolshoye, Olkhovskoye and Longyuganskoye (Western Siberia), Nirmalinskoye and Pyzhelskoye (Timan-Pechora), Viktorinskoye and Bortomskoye (Urals). Peak annual production of liquid hydrocarbons from new fields launched in 2009 will be nearly 1 million tonnes. There were production increases of more than 50,000 tonnes of oil at 14 Group fields in 2009. The biggest increases (in excess of 200,000 tonnes) were achieved at 3 fields, which accounted for more than 6 million tonnes of oil production growth. These were the Yuzhnaya Khylchuya field in Timan-Pechora and the Kechimovskoye and Urevskoye fields in Western Siberia.

The Company had 29,760 oil production wells as of January 1, 2010, of which 25,380 were actually in use, and the number of water injection wells was 9,910, of which 7,630 were under pressure. The number of oil production wells was 3.7% higher than in 2008. The share of idle wells was almost unchanged in comparison with the end of 2008 at 14.7% of the total. Average daily oil flow from wells in projects with Company participation was 14.7 tonnes, which is 3.5% more than in 2008, due mainly to launch of the Yuzhnaya Khylchuya field.

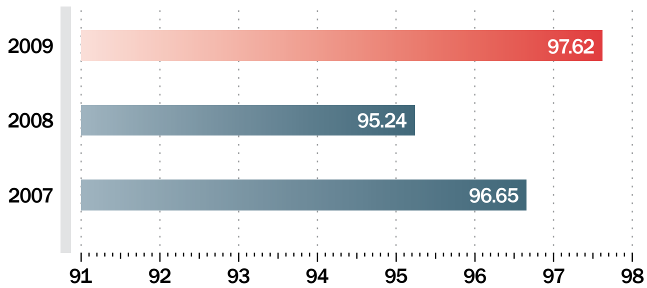
Amounts of production drilling declined in the reporting year, because a large part of drilling was in regions where difficult geological conditions slowed progress. Also LUKOIL decided to reduce financing of its drilling program in the context of the economic crisis and low prices for oil. As a result, production drilling in 2009 was 2,740 thousand meters, which is 23% less than in 2008. The number of new production wells brought into operation was 1,124, of which 91 were horizontal. High efficiency of horizontal well drilling has persuaded the Company to increase numbers of such wells in the medium term. Average daily flow from new wells in projects, in which the Group is a participant, was 34.8 tonnes, including 78.2 tonnes from horizontal wells. Flow rates at new wells were slightly lower than in 2008, reflecting overall lowering in quality of extracted reserves. However, flow rates at horizontal wells rose substantially (by a third). Progress reflected improving quality of geological and hydrodynamic models and extensive use of such models in organization of production drilling, as well as further work to improve technologies in well completion and initial and secondary penetration of productive formations.

The Company further increased drilling of sidetracks in 2009: a total of 264 wells with sidetracks were drilled and they gave average daily flow increase of 16.8 tonnes. Increase of flow rates at some fields was significantly higher than the average for the Company. For example, a multiple-bore well (two boreholes), drilled at the Kechimovskoye field in Western Siberia gave a flow rate of 103 tonnes per day.

OIL PRODUCTION DRILLING, THOUSAND METERS



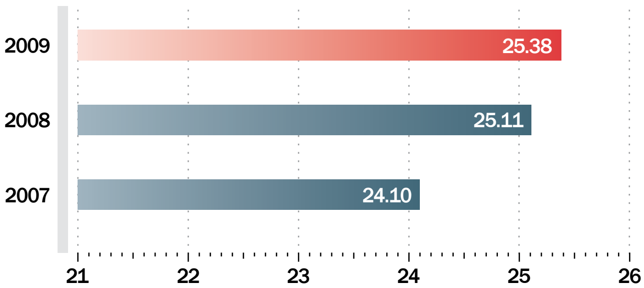
OIL PRODUCTION, MILLION TONNES



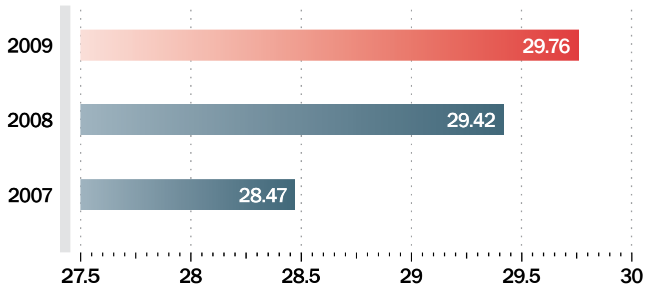
A total of 604 new injection wells were put under pressure in 2009 to optimize field development systems and maintain reservoir pressure. Injection wells pumped 510 million cubic meters of water into productive formations, which is 5% more than in 2008. The Company was able to halt growth in the water cut, which had been growing at an average rate of 1.5 percentage points annually for the previous five years. This was thanks to production of almost water-free oil at the Yuzhnaya Khylchuya field and measures to limit associated water and unproductive pumping at other Company fields in Russia. The Company plans further improvement of its systems for maintaining reservoir pressure at fields under development. The Company also continued the program, which it has been pursuing for several years, to install small power generation units at fields in order to achieve independence from electricity suppliers (see ‘Power Generation’ on page 64).

The Company took further action in 2009 to increase well productivity. In Russia a total of 1,141 operations were carried out to optimize functioning of mechanized wells, 57 wells were transferred to mechanized production, and 567 idle wells were brought into production. The Company continued to make extensive use of enhanced oil recovery techniques at oilfields. A total of 5,098 operations were carried out on productive

OIL PRODUCTION WELLS IN USE, THOUSAND WELLS



OIL PRODUCTION WELLS, THOUSAND WELLS



formations using physical, chemical, hydrodynamic and heat techniques (see 'Exploration and Production Technologies' on page 80). Additional oil output in Russia thanks to application of enhanced oil recovery techniques was 23 million tonnes, or 25% of total oil production by the Group in Russia.

Russia

Oil production by LUKOIL in Russia during 2009 was 91.868 million tonnes, of which 91.560 million tonnes were produced by Group subsidiaries. Production in Russia rose by 2.1% compared with 2008.

Subsidiaries and equity affiliates of LUKOIL produced hydrocarbons at 348 fields in Russia in 2009. Production drilling was 2,385 thousand meters, which is 20% less than in 2008. The number of production wells at the end of 2009 was 28,240, of which 24,040 were actually in use. There were 854 new wells brought into operation in 2009.

Fields in **Western Siberia** accounted for 57.7% of LUKOIL's Russian oil production in 2009. Production in the region was somewhat lower than in 2008 at 52.96 million tonnes. Stabilization of output levels in Western Siberia is one of the main challenges for the Company. It is complicated by gradual natural exhaustion of the resource base, due to the long period of production at most Company fields in Western Siberia, which has depleted their reserves. LUKOIL is combating output decline by use of the latest technologies, which enable substantial increase of the oil recovery rate and production of oil from reservoirs with difficult access. Another problem is shortage of electric power supply in the region, which leads to losses in the production process and makes it difficult to pump in sufficient

Opinion Column

Matta Maya Alberto Jose, Specialist of technological equipment repair division of central oil treatment office at the Vateganskoe field, LUKOIL-Kogalym-neftegaz.

Alberto came to Russia from Spain. He has been working in LUKOIL-Western Siberia since 2007 after graduating from Gubkin Russian State University of Oil & Gas.

– What made you decide to leave warm Spain for a cold land with about 40 degrees of frost?

– As with the others, my affection for oil & gas industry. I wanted to work for a big company where I could successfully put my knowledge to practice and gain priceless experience. And it's well known that companies of LUKOIL Group located in Western Siberia are a forge for the best oil & gas specialists, and the experience gained here is highly valued both in Russia and all over the world.

– Are you pleased with the results of your decision?

– I see the result of my work and feel that I get to know something new every day. That's why I cannot but be glad. I highly appreciate the help and experience my friends and colleagues share with me and in my turn try to work even better.

– What are your plans for the future?

– I'd like to gain experience so that I could be helpful to the Company. Another cherished wish of mine is to have six children and two dogs. I think I won't be truly happy without them.

volumes of water to maintain reservoir pressure. The Company is successfully dealing with power shortages at its own fields by construction of small power stations, fuelled mainly by associated gas (see 'Power Generation' on page 64).

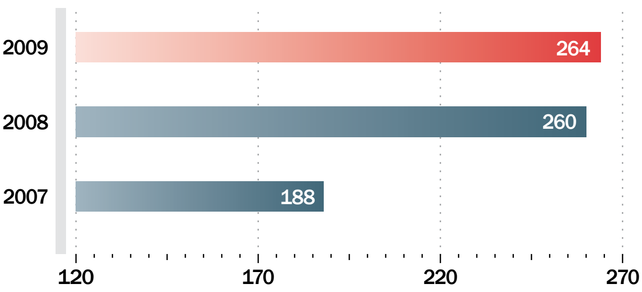
Despite long periods of exploitation, some of the Company's fields in Western Siberia have significant potential for production growth. In particular, the Kechimovskoye and Urevskoye fields showed strong oil production growth in 2009.

Oil production at the Kechimovskoye field, which was launched in 1995, grew by 63.9% in 2009 compared with 2008 to 1.59 million tonnes thanks to new production drilling: a total of 92 new wells were brought into production with average daily flow rates of 28.6 tonnes, including 27 horizontal wells with average daily flow rate of 42.9 tonnes. A multi-bore well (two boreholes) was also drilled at the field in 2009 and gave daily flow rate of 103 tonnes. High flow rates from wells that were launched in 2008 and were in operation throughout 2009 also had positive effect (79 wells with average daily flow of 28.8 tonnes). A total of 5 sidetracks were drilled at the field in 2009 and each gave average increase of daily flow rates by 27.2 tonnes. Work continued on a system to maintain reservoir pressure: 36 new injection wells were put under pressure during the reporting year. The Kechimovskoye field is one of the Company's biggest investment projects in Western Siberia. As of January 1, 2010, a further 512 wells remained to be drilled in accordance with the field development plan (402 oil wells and 110 injection wells). LUKOIL will maintain high rates of production drilling at the field in the immediate future in order to further increase levels of oil production.

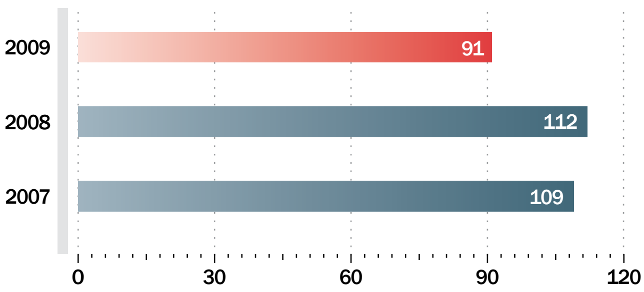
Oil production at the Urevskoye field, which was brought into production in 1978, rose by 9.4% to 2.62 million tonnes in 2009. The increase was achieved thanks to production drilling: 83 new wells were launched with average daily output of 28 tonnes, including 4 horizontal wells with daily flow of 75.5 tonnes. A total of 19 sidetracks were drilled at the field in 2009 in order to maintain output levels at wells, and 48 injection wells were put under pressure in order to optimize the reservoir pressure system and to compensate fluid extraction by water injection. A further 1,161 wells remained to be drilled in accordance with the field development scheme as of January 1, 2010. LUKOIL's development program for the Exploration & Production segment includes maintenance of high production drilling rates at the Urevskoye field and achievement of higher oil output rates.

The **Timan-Pechora** oil & gas province contributed 5 million tonnes to the Company's oil production growth in 2009. Oil output in the region was 21.66 million tonnes. As a result, the share of the region in total oil production by the Company in Russia rose from 19% to 24%. Growth of the share continued thanks to rapid development of the Yuzhnaya Khylchuya field, which was commissioned in mid-2008 jointly with

DRILLING OF SIDETRACKS, SIDETRACKS



DRILLING OF HORIZONTAL WELLS, WELLS



ConocoPhillips. Output at the field in 2009 rose by 3.5 times compared with 2008 to reach 7 million tonnes (about 140,000 barrels per day). The field reached its planned long-term oil output level of 7.5 million tonnes per year in July 2009. A total of 10 new production wells with average daily output of 602 tonnes were commissioned at the field in 2009, bringing the number of production wells in operation to 30 by the start of 2010. A system for maintenance of reservoir pressure is being developed, with 7 new injection wells put under pressure during 2009 (19 injection wells were in place by the start of 2010). Peak production should be achieved in 2010 with completion of production drilling (2 production and 3 injection wells will be brought into production during the year).

Timan-Pechora will be the main area of oil production growth by LUKOIL in the medium term, and the Company is making every effort to ensure rapid development of main reserves in the region (production started at 2 new fields in 2009). This progress will help to compensate natural decline of output in the Company's traditional operating regions.

Production of oil by LUKOIL in the **Urals region** increased to 12.04 million tonnes in 2009, or by 3.6%, thanks to use of new technologies, such as sidetracks, radial drilling and acid hydro-fracturing.

The Company started production at a new group of fields in Perm Territory during 2009, attached to the unique Verkhnekamskoye potash-magnesium salt field. Development rights at this area were obtained by the Company in 2008. This license area has several specific features: hydrocarbon fields are located underneath potash-magnesium salt deposits, which are already in the process of industrial development, and there are various environmental constraints (nature conservation zones, protected water spaces, settlements, etc.). Oil field development will therefore use a multi-column well-construction technique, unique in Perm Territory, in order to address all of these industrial and environmental safety issues:

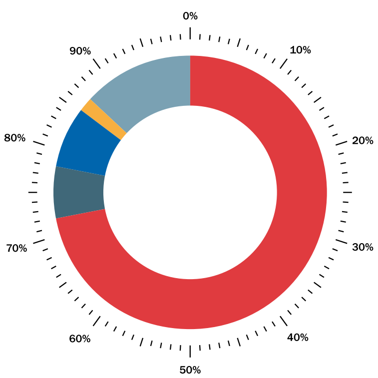
displacement from vertical will be up to 2 km, salt formations will be separated off using magnesium-phosphate tamping material with an expansion cement bond, and a system for constant monitoring of surface deformation. Forecast annual output of oil at the fields is 1.3 million tonnes.

Oil production in the **Volga** region in 2009 was 3.07 million tonnes, representing a slight decline compared with 2008. The Company is working to improve field development efficiency in the region in order to increase the oil recovery rate and maintain output at current levels, despite considerable depletion of reserves.

The Company put much emphasis in 2009 on preparation for development of fields on the **Caspian Sea shelf**. Development of these fields will be the main factor in oil production growth by the Company in the mid-term. The Yu. Korchagin and V. Filanovsky fields will be the first to be commissioned and will be the main sources of increase in oil output.

Following preparatory work in 2009, first oil was obtained in the second quarter of 2010 at the Yu. Korchagin field. Peak annual output at the field will be 2.5 million tonnes of oil and 1 billion cubic meters of gas. The Company began operations at sea for construction of the Yu. Korchagin field in April 2009, when the main block of a fixed ice-resistant offshore platform was towed to the site from the port of Astrakhan. Living quarters were built onto the block in May. In August work was completed on a jetty for loading of oil from an underwater pipeline into a floating reservoir and onto shuttle tankers. In September a floating reservoir was installed at the field for loading of shuttle tankers and transportation of oil produced at the field. A fixed ice-resistant offshore platform with drilling unit has thus been installed for drilling of wells with maximum borehole length of 7,400 meters. The field will be developed using exceptionally long horizontal wells (in excess of 5 km), which is a unique approach in Russia. The Yu. Korchagin field is the first of a whole group of fields in Russian territorial waters of the Caspian Sea to be brought into production by the Company. Development is on a zero-discharge basis, which ensures minimal impact on the natural environment of the Caspian Sea.

PRODUCTION DRILLING BY REGIONS (2009)



72.2% Western Siberia (including Bolshekhetskaya Depression)
5.9% Urals
7.3% Timan-Pechora
1.6% Other
13.0% International projects

International Projects

LUKOIL's share of production in international projects was 5.747 million tonnes, which is 8.5% more than in 2008. The growth was mainly due to the Tengiz, KarakudukMunai and Karachaganak projects in Kazakhstan.

Production drilling in the Company's international projects was 355,000 meters, which is 40% less than in 2008. The reduction is explained by lower levels of financing for drilling programs, but rates of progress were maintained in priority development projects (Karachaganak, Kumkol and Condor). The number of oil production wells was 1,522, of which 1,345 were actually in use. A total of 270 new production wells were commissioned as part of international projects, in which the Company is a participant. Average daily oil flow from these wells was 43.4 tonnes.

The largest increase in oil production growth was from the **Tengiz** project in **Kazakhstan**. Crude oil production from the project (Company share) grew by 37.8% to 642,000 tonnes. The expansion was due to organic growth and also to purchase in December 2009 from a BP subsidiary of a 46% stake in the LUKARCO B.V. joint venture, which is developing the Tengiz and Korolevskoye fields in Kazakhstan.

The Group share in production of oil and gas condensate as part of the **Karachaganak** project in **Kazakhstan** rose by 4.1% to 1.63 million tonnes in 2009. A further 10 production wells (of which 8 had horizontal end sections) were drilled and connected to the main collector system as part of implementation of the investment program in the reporting year, and gave an average daily flow of 572.9 tonnes. Work continued to expand capacity at the Karachaganak refining complex.

Rapid development work continued at the **Kumkol** field in **Kazakhstan** during the reporting year. LUKOIL's share in crude production in this project during 2009 was 1.59 million tonnes. 66 wells were drilled with penetration of the productive horizon using polymer agents with overlapping of the production liner pipe. This technology enables maximum preservation of reservoir qualities of formations. Average flow from new wells was 36.7 tonnes per day, and 11 sidetracks were drilled. A project for further field development was designed and approved. The first stage of the gas utilization program was carried out in 2009 and a unit for complex gas preparation, with 150 million cubic meters annual capacity, was put into operation.

The Company's share in production from the **KarakudukMunai** project in **Kazakhstan** grew by

12.3% to 714,000 tonnes. A central oil preparation unit with 1.8 million tonnes annual capacity was brought into operation during the reporting year, as well as 33 new production wells with average daily flow rates of 20.8 tonnes. Pilot test work was also carried out on large-scale hydrofracturing of formations: two operations were executed and gave average increase of flow by 58 tonnes per day using a free-flow production method.

Intensive development work continued at the **North Buzachi** field in **Kazakhstan**, where LUKOIL's share of production grew by 11.9% to 479,000 tonnes, and 130 new production wells were commissioned giving average daily flows of 10.6 tonnes. Work began on drilling of horizontal wells, technological scheme for gas utilization was designed and approved, and gas utilization program was implemented. The program for expansion of capacity of the oil preparation and pumping facility to 40,000 barrels per day was completed.

A total of 8 new production wells with average daily flow rates of 44.4 tonnes were brought into operation at the **Alibekmola and Kozhasai** fields (the **Kazakhoil Aktobe** project in **Kazakhstan**). The Group share in production at the fields was 234,000 tonnes, which is 23.2% more than in 2008. A geological and hydrodynamic models of the Alibekmola field were created in the reporting year, and recommendations were prepared for further development of the field. A contractor was chosen for construction of gas utilization facilities as part of the program for gas utilization. The project is in the planning stage now and should be completed by June 1, 2011.

Production in the **Shakh Deniz** project in **Azerbaijan**, which was launched in December 2006, declined by 2% in 2009 following rapid growth in 2007–2008, due to limited demand from Azerbaijani and Turkish customers. The Group share in gas condensate output was 139,000 tonnes, compared with 147,000 tonnes in 2008. A new well was completed and launched, giving daily flows of 1,450 tonnes of condensate and 6.2 million cubic meters of natural gas, supporting future growth of output in the project.

The Company's share of gas condensate production at the **Khauzak-Shady** area in Uzbekistan (developed as part of the **Kandym – Khauzak – Shady** project), which was commissioned in 2007, remained unchanged from 2008 at 12,000 tonnes. A further 5 production wells were commissioned in the course of the year. An integrated health, safety and environment system was installed at the field in 2009 and certified in compliance with the ISO 14001 international standard and the OHSAS 18001 specification.

Production at the **South-West Gissar** project in **Uzbekistan**, acquired in 2008, rose by over 5 times to 38,000 tonnes (the Group share). A further 12 production wells were put into operation in the reporting year and their average daily flow rates were 22.7 tonnes.

Substantial increase of output (+68.1%) was obtained in **Egypt** as part of the **Meleiha** project thanks to efficient drilling and commissioning of 18 new production wells with average daily flows of 67.6 tonnes. One new production well was launched in the Egyptian **WEEM** project and gave average daily flow of 53.6 tonnes. A sidetrack was also drilled at one well in order to maintain production efficiency. LUKOIL's share in production as part of the Egyptian projects rose by 30% compared with 2008 to a level of 247,000 tonnes.

The West Qurna-2 Project in Iraq

In 2009 a Consortium of LUKOIL and the Norwegian company Statoil won a tendering competition for rights to develop the West Qurna-2 field. The field is one of the largest in the world, which are not currently being developed, and is located in the southern Iraq, 65 km north-west of the large port city of Basrah.

Recoverable reserves at the field are close to 13 billion barrels. The main productive horizons are Mishrif, Yamamah, Hasib, Maudud, and Zubair. More than 90% of reserves are concentrated in Mishrif and Yamamah reservoirs. The field was discovered in 1973. Geological exploration (2D seismic and drilling of exploration wells) was carried out by Soviet geologists and service organizations.

Project History

The Company initially obtained a 68.5% share in the project through a production sharing agreement, which was signed in 1997. However, commercial development of the field was not possible at that time due to sanctions, which the UN had imposed on Iraq. Subsequently, after the conflict between the USA and Iraq, LUKOIL entered talks with the new Iraqi government about commencement of the project.

In 2009 LUKOIL and Statoil presented the best tender offerings and won field development rights at West Qurna-2. The remuneration fee per barrel will be $1.15 at a daily production level of 1.8 million barrels. In January 2010 the President of LUKOIL, Vagit Alekperov, signed a service contract for development and production at West Qurna-2, and the contract was ratified by the Iraqi Cabinet of Ministers.

Features of the Project

The contract is for 20 years with the possibility of 5-year extension. The contract parties are the Iraqi state oil company, South Oil Company, and the Contractors Consortium consisting of North Oil Company (an Iraqi state company, 25%), LUKOIL (56.25%) and Norwegian Statoil (18.75%).

The agreement calls for drilling to begin at West Qurna-2 in 2011. Within three years from the date of approval of the Initial Development Plan the Consortium must carry out a specified minimum geological exploration program, consisting of 450 km^2 of 3D seismic, and drilling of 2 appraisal wells to the Najmah formation and of one exploration well to the Khuff formation.

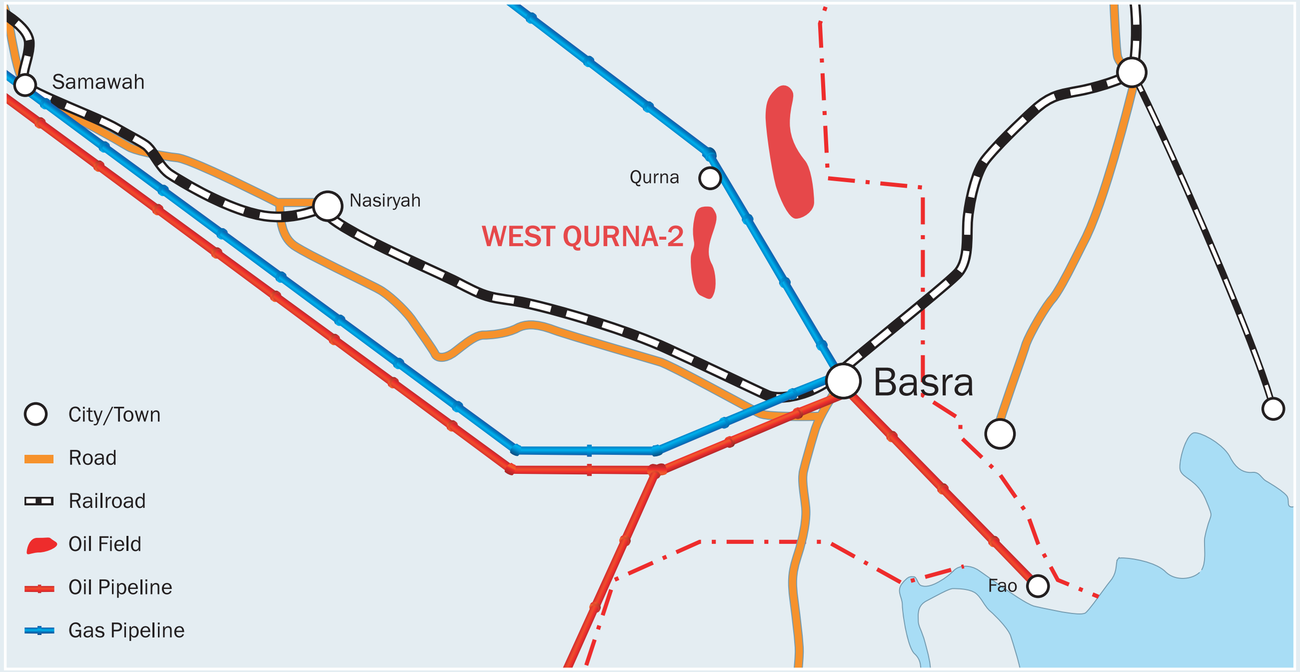
Production should begin at the end of 2012 at a minimum daily rate of 120,000 barrels. Target production level of 1.8 million barrels per day is to be achieved in 2017. The field is to be developed using over 500 wells, of which 120 will be injection wells.

According to preliminary estimates, investments by LUKOIL at West Qurna-2 in 2010 will be about $300 million and will total $4.5 billion dollars over the next 4–5 years.

The mechanism for return of investments will be based on distinction of two oil streams in the project: one of them owned and sold by the Iraqi marketing company, SOMO, and the other transferred to ownership of the Consortium as profit oil. Profit oil can be substituted by cash payment. It is seen as reasonable that costs will be reimbursed in the form of profit oil, intended for sale.

Pricing of export oil will be based on a market principle using FOB at point of delivery.

PROJECT GEOGRAPHICAL POSITION



« We have continued to fight for the Iraqi project over a number of years, delivering on the promise, made by us to shareholders. Today we have won a well-earned victory and intend to carry out, together with our Norwegian partners, all of the obligations, which we have assumed for development of the West Qurna-2 field in the interests of the Iraqi people and our shareholders. This project has strategic importance for our Company. »

VAGIT ALEKPEROV
President of LUKOIL

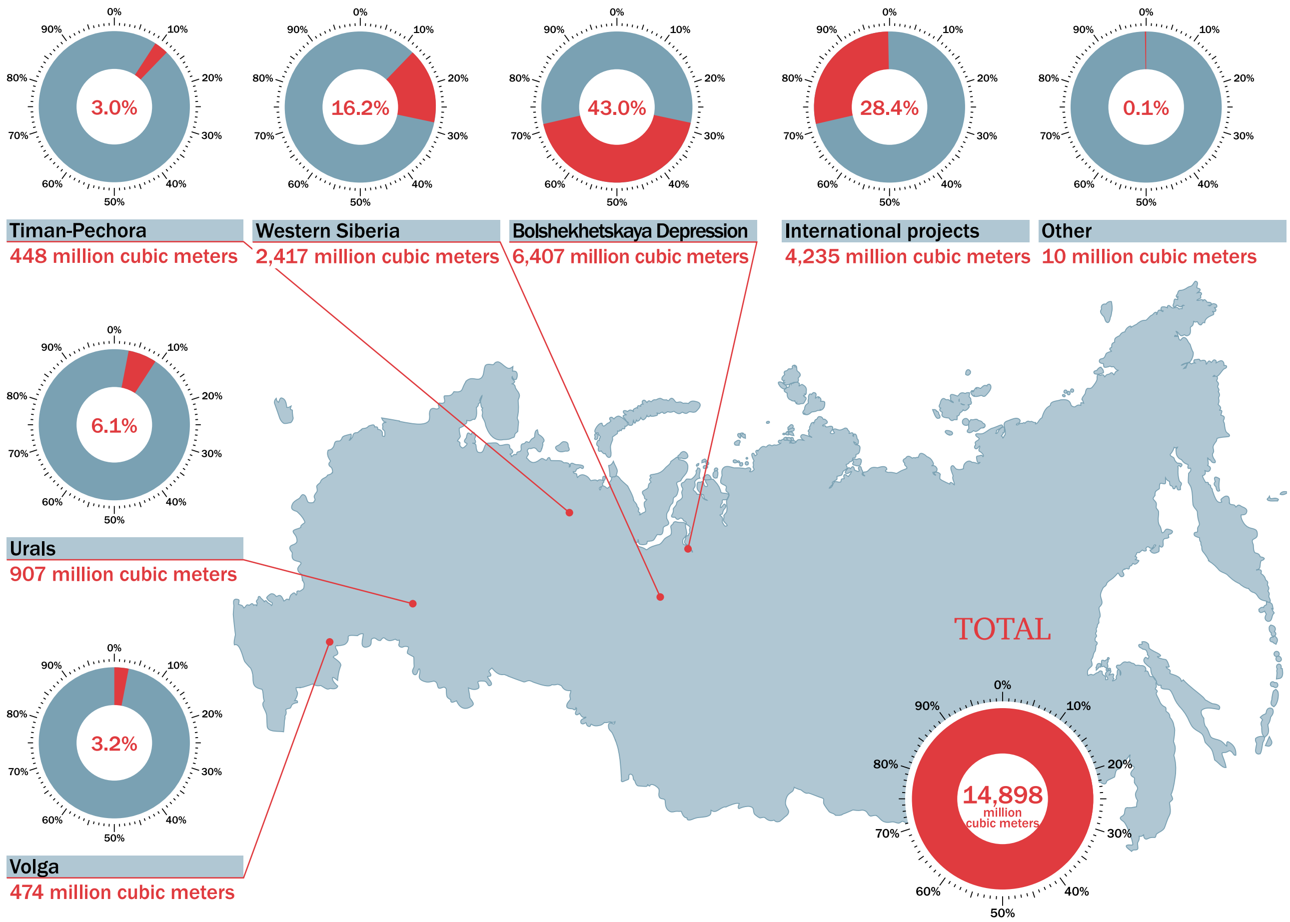
KEY FACTS ABOUT IRAQ:

- Iraq is a federal parliamentary republic, based on consensus between the three main ethno-religious communities, which constitute the Iraqi people: Shiite Arabs, Sunni Arabs and Kurds.
- The armed conflict, which began in March 2003, brought an end to the rule of Saddam Hussein. The country's economy was destroyed in the course of the conflict.
- Export of hydrocarbons accounts for 95% of central government budget revenues.
- The Iraqi state oil companies, North Oil Company (NOC) and South Oil Company (SOC), have a monopoly right to develop oil fields in the country.
- Iraq's proved oil reserves are 115 billion barrels (3rd largest in the world after Saudi Arabia and Iran).
- Current oil production is 2.5 million barrels per day.
- Less than a third of the country's 80 explored oil fields are in development.
- Combined peak production of fields allocated by auction in 2009 is about 10 million barrels per day.

Gas Field Development and Production

LUKOIL's gas program is focused on accelerated growth of gas production both in Russia and abroad and increase in the share of gas to a third of total hydrocarbon production by the Group. The main aim of this strategy is to commercialize gas reserves and reduce the Company's exposure to major price volatility on the international oil market.

LUKOIL GROUP MARKETABLE GAS PRODUCTION BY REGIONS



Total gas production by LUKOIL Group in 2009 (including the share of production by equity affiliates) was 17.717 billion cubic meters (1.714 billion cubic feet per day). Output of marketable gas (net of own use, reinjection into reservoir formations and transport losses) was 14.898 billion cubic meters (1.441 billion cubic feet per day). Average daily production of marketable gas declined by 12.5% compared with 2008, including a decline of 16.9% in Russia due to limitation of volumes of gas taken by Gazprom. Despite substantial reduction of output, LUKOIL Group achieved net income of $56 million from gas projects in Russia during 2009.

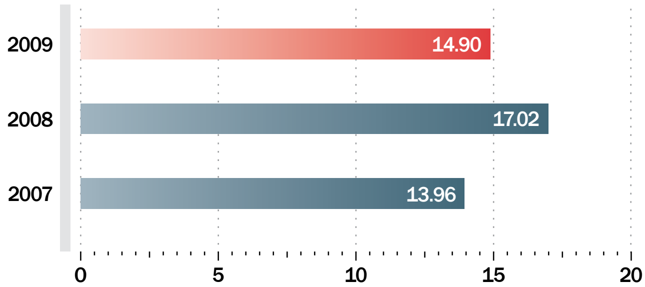
The Company had 394 gas production wells at the end of 2009, of which 274 were actually in use.

Production of natural gas in 2009 was 11.444 billion cubic meters, of which 10.218 billion cubic meters was marketable gas. Reduction in output of marketable natural gas was 19.4%, including 27.2% decline in Russia and 2.1% decline abroad. The share of production from international projects increased from 31% in 2008 to 38% in 2009. The large fall in Russian output is explained by lowering of production at the Nakhodkinskoye field (by almost 30%) due to reduction of demand for gas and limitation of volumes accepted by Gazprom.

Production of associated gas was 6.273 billion cubic meters, of which 4.680 billion cubic meters was marketable associated gas. Growth in production of marketable associated gas was 7.6%, reflecting growth of oil production and development of the system for associated gas utilization at Company fields. Associated gas is used at fields for injection into formations to maintain reservoir pressure, for production of electrical energy at gas-fired power stations, and for other production needs. Marketable associated gas is delivered to gas-processing plants and to local consumers.

The utilization rate for associated gas[1] was 71.1% in 2009, compared with 70.4% in 2008 and 69% in 2007, thanks to development of systems for utilization of associated gas at Company fields including construction of compressor stations and gas pipelines. The level of utilization of associated gas at main Company fields in Western Siberia is around 95%.

PRODUCTION OF MARKETABLE GAS, BILLION CUBIC METERS



[1] Share of produced gas in total gas extracted from formations. The remainder is flared off.

The Company is pursuing construction of gas-fired power stations at fields as part of a small-scale generating program in order to further increase utilization of associated gas. This reduces gas flaring and gives cost savings on electricity, lowering oil lifting costs. LUKOIL is implementing a program, approved in 2009 for the years 2009-2011, which aims to increase rates of associated gas utilization by organizations in the Group. The program target is to raise the utilization rate to 95% by 2012.

Russia

Production of marketable gas in Russia in 2009 was 10.663 billion cubic meters, which is 16.9% less than in 2008. The share of natural gas was 59%, which is 9 percentage points less than in 2008. The Company had 304 gas production wells in Russia at the end of 2009, of which 211 were actually in use.

Most of the Company's natural gas production in 2009 in Russia (more than 90%) came from the Nakhodkinskoye field in the Bolshekhetskaya Depression. Gas production there in 2009 was 6 billion cubic meters, which is nearly a third less than in 2008, due to limitations on the amount of gas bought by Gazprom.

Work continued in 2009 to prepare for development of other fields in the Bolshekhetskaya Depression. As prescribed by the investment program, construction of facilities began in 2009 at the Pyakyakhinskoye field, one well was brought into production, and natural gas output was used for the Company's own needs. Work was carried out on construction of roads, well pads and industrial installations, as well as production drilling to gas condensate accumulations, and the field should come on stream in 2013. Marketable gas will be transported along an inter-field pipeline to a gas compressor station near the Nakhodkinskoye field and from there along the existing trunk gas pipeline to Yamburg Gas Compression Stations-1 and -2. Gas production at the Yuzhno-Messoyakhskoye gas condensate field is due to start in 2019, and the Khalmerpayutinskoye gas condensate field should be launched in 2020.

Under an agreement with Rosneft, starting from autumn 2013, LUKOIL will accept up to 5.6 billion cubic meters of gas per year from the Vankor group of fields for input to its gas transportation system in the Bolshekhetskaya Depression and will transport the gas as far as the Yamburg Gas Compressor Station, which is part of Gazprom's gas transportation network. In return, starting from 2013, Rosneft will accept annual inputs of up to 3 million tonnes per year of stable oil and condensate mixture from LUKOIL's Pyakyakhinskoye field to the Vankor – Purpe oil pipeline and transport them to Transneft's trunk oil pipeline system. In order for these objectives to be achieved, LUKOIL will construct a 160-km gas pipeline from the Pyakyakhinskoye field to the Vankor central collection point, a 60-km gas pipeline from Pyakyakhinskoye to the Khalmerpayutinskoye field, and the first stage of a gas compressor station adjacent to the Nakhodkinskoye field.

Achievement of target production levels at all fields in the Bolshekhetskaya Depression will bring overall production of natural gas by the Company in the region to 20 billion cubic meters.

International Projects

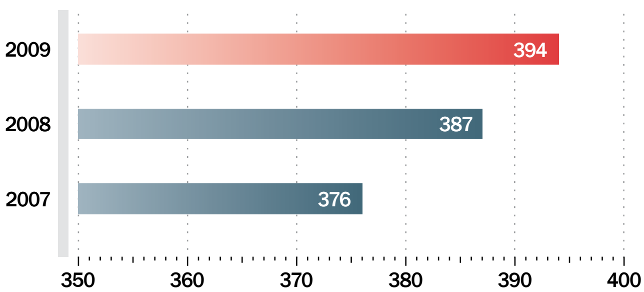
Production of marketable gas in 2009 as part of international projects was 4.235 billion cubic meters, which is 1.0% more than in 2008. The share of natural gas was 92%, representing a decline of 2 percentage points. The Company had 90 gas production wells in international projects at the end of 2009, of which 63 were actually in use.

Most of marketable gas production outside Russia (53%) was at the **Khauzak-Shady** area, which was brought into production at the end of 2007 and is being developed as part of the Kandym – Khauzak – Shady project in **Uzbekistan.** Production of marketable gas at the Khauzak-Shady area was 2.23 billion cubic meters in 2009. Production drilling at the area continued in 2009 and totalled 19,000 meters, and 5 new wells were commissioned giving average additional gas flow of 361 cubic meters per day. Intensive work has also started in Uzbekistan on drilling of gas wells at the Adamtash field as part of the Gissar project, where production of natural gas is due to start in 2012.

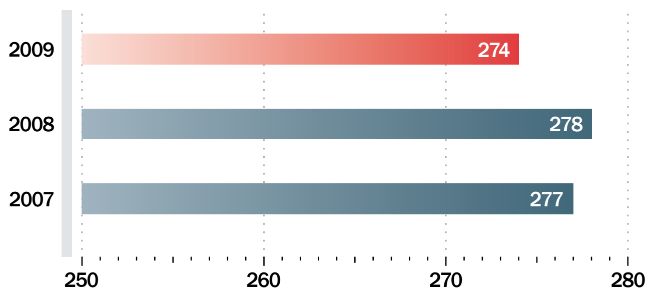
The Group share in production of marketable gas at the **Karachaganak** field in **Kazakhstan** was 1.13 billion cubic meters in 2009, representing an increase of 6.0% compared with 2008. The results were achieved thanks to commissioning of new wells with high flow rates.

Marketable gas production in 2009 at the **Shakh Deniz** project in **Azerbaijan**, which was brought into production in December 2006, was 518 million cubic meters (Company share), which is 6.1% less than in 2008, reflecting limited consumer demand. A new well was completed and commissioned, and gave daily production of 1,450 tonnes of condensate and 6.2 million cubic meters of natural gas, which will support future growth of output in the project. Drilling of a further 2 wells is planned in 2010.

GAS PRODUCTION WELLS, WELLS



GAS PRODUCTION WELLS IN USE, WELLS



Annual Report 2009

Oil Refining, Gas Processing and Petrochemicals

Strategy

Maximizing refinery throughputs

Production of high-quality, environmentally friendly petroleum products with high value added

Use of the latest technologies

Control over production costs

Net income in 2009 in the Refining & Marketing segment was $2,263 million. The net income decline was less than the decline of oil refining margin both in Russia and abroad, which is a reflection of improving efficiency in this segment of LUKOIL's business. Increase of operating indicators (mainly, throughput volumes) also contributed to the good financial results in spite of the economic downturn.

Oil Refining

LUKOIL Group continued rapid development of its oil refining business in 2009 through modernization and expansion of refining capacities, and participation in new promising projects.

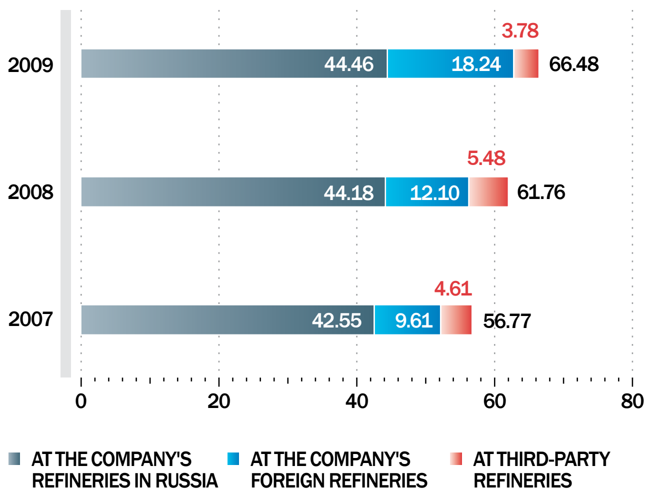
The volume of refinery throughputs, including processing at third-party refineries, increased by 7.6% in 2009 compared with 2008 to 66.48 million tonnes, of which 62.7 million tonnes were refined at Group Refineries (including Company shares of refining at the ISAB and TRN complexes), representing an increase of 11.4% over 2008.

In the reporting year LUKOIL continued implementation of the program for modernization and reconstruction of its refineries, making capital expenditures of $827 million (compared with $1,023 million in 2008).

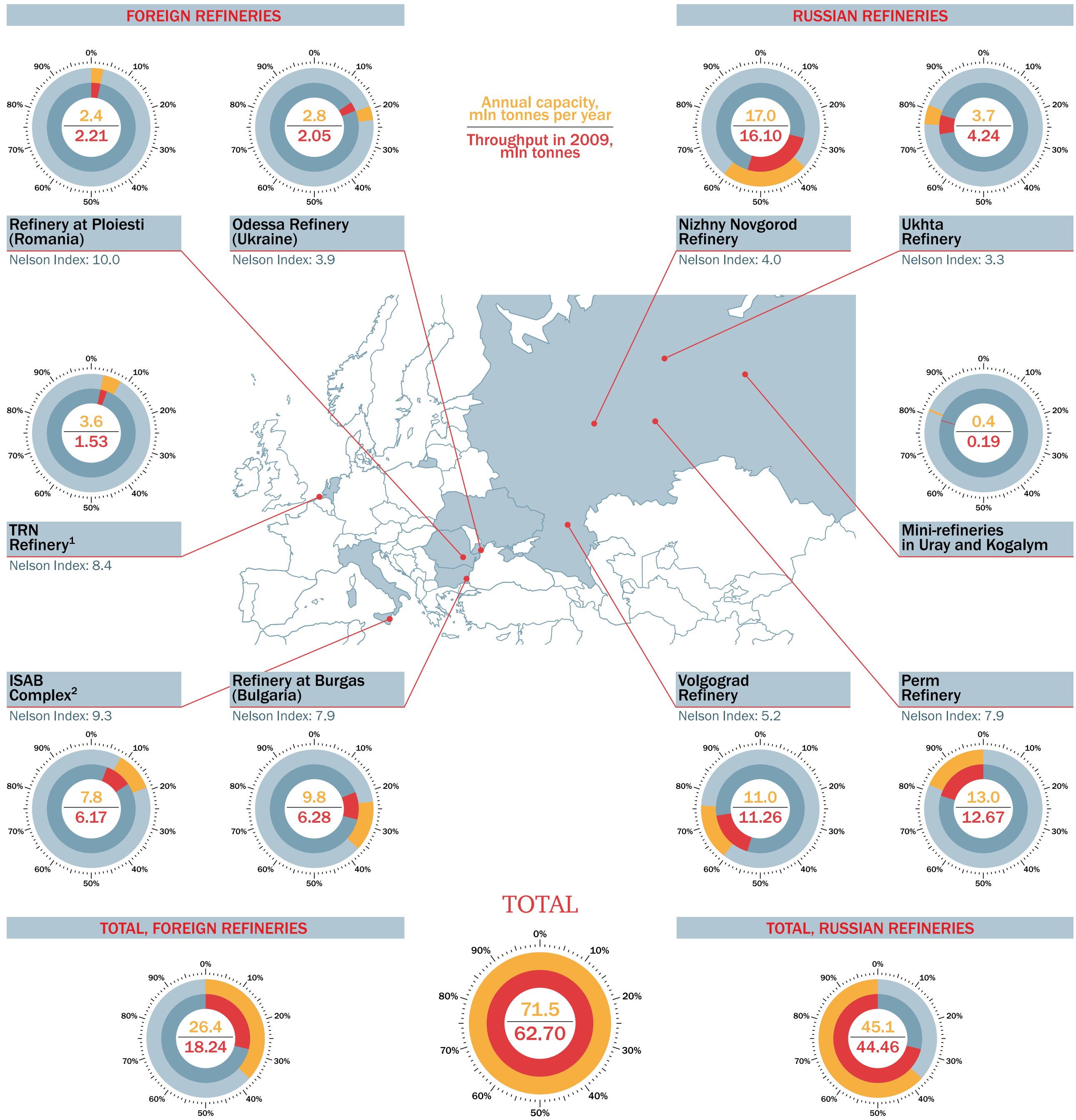
In September 2009 LUKOIL completed a transaction with the French company TOTAL S.A. for acquisition of 45% of the TRN Refinery in the Netherlands. The transaction price was about $700 million. Acquisition of the TRN stake fits into the Company strategy of increasing its refining capacities at locations adjacent to product markets, which offer large value added. The Refinery is located by the port of Vlissingen Oost in the south-west of Holland, in one of the world's largest centers for trading of oil and petroleum products (the Amsterdam – Rotterdam – Antwerp region). The Refinery is integrated with adjacent petrochemical production facilities and connected by pipeline with one of Europe's largest oil terminals, Maasvlakte Olie (Rotterdam), in which the Refinery has a 22% stake. The Refinery also has its own port with several jetties for sea and river transshipment.

Company refineries took a number of steps in 2009 to reduce costs and raise efficiency of their operations. A total of 156 measures were implemented during the year to optimize production capacities, increase capacity load of refining units, raise energy efficiency and reliability of equipment (increasing the period in operation between overhauls), as well as to optimize personnel numbers and rotation. Financial impact from implementation of these measures was about $88 million (net effect was $18 million), including $70 million from optimization of production capacities. The biggest effect was achieved at the Perm Refinery ($28 million).

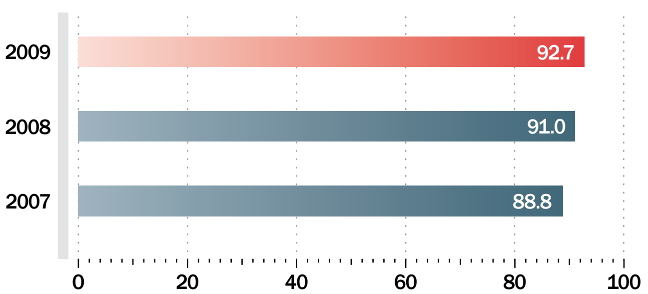
REFINERY THROUGHPUTS BY LUKOIL, MILLION TONNES



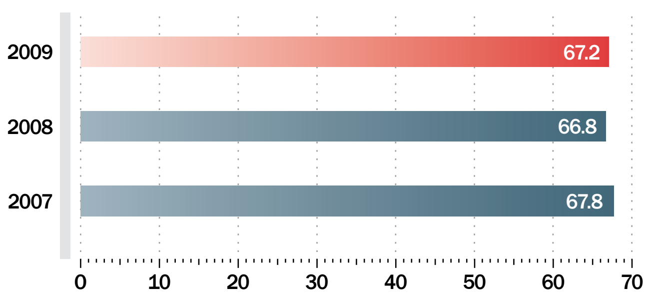
LUKOIL GROUP REFINERIES



SHARE OF HIGH OCTANE GASOLINE IN TOTAL GASOLINE PRODUCTION, %[3]



SHARE OF DIESEL FUEL WITH SULPHUR CONTENT BELOW 50 PPM IN TOTAL DIESEL PRODUCTION, %[3]



[1] Capacity of the TRN Refinery is shown as the Company share (45%). The throughput figure is the Company's share during September-December 2009.

[2] Capacity of the ISAB complex is shown as the Company share (49%).

[3] Excluding mini-refineries and the ISAB and TRN complexes.

Russian Refineries

Refinery throughputs in 2009 at LUKOIL Group's Russian refineries were 44.46 million tonnes, which is 0.6% more than in 2008. Capacity utilization was 99.5%, which represents a new record in the history of the Company.

LUKOIL also processed 2.05 million tonnes of crude oil at third-party refineries in Ufa, in order to maximize profits in the specific market environment.

The share of high-octane gasoline in total output of gasoline at Group refineries in Russia (not including mini-refineries) rose to 89.7% in 2009 (from 87.0% in 2008). Refining depth was 74.8% which is 1.2 percentage points lower than in 2008 mainly due to increase in oil throughput, decrease in sales of bitumen and unplanned maintenance. Light-product yield was 50.1% (virtually unchanged from 2008).

The most significant output increases compared with 2008 were of vacuum gas oil (by 8%), fuel oil (by 5.8%) and motor gasoline (by 5.4%).

Measures were implemented during the year to reduce operating costs and raise production efficiency at Russian refineries. This enabled reduction of irretrievable losses at refineries from 0.58% to 0.54% to (against the Russian average of 0.85%). Average personnel numbers at Russian refineries were reduced by 5.0%. Capital expenditures for modernization of the Company's refineries in Russia in the reporting year were $519 million (against $688 million in 2008).

At the **Ukhta Refinery** construction work was completed on an isomerization block. The block enables production of high-octane gasoline, free from sulphur compounds, benzol and aromatics. As a result, the Ukhta refinery has started production of motor gasolines that meet Euro-3 and Euro-4 environmental requirements. Target annual input capacity for the block is 120,000 tonnes, and cost of installation was about $40 million.

Work was carried out in 2009 to prepare the **Nizhny Novgorod Refinery** for production of the high-performance EKTO-98 motor gasoline. Project implementation will increase refining depth at the Refinery, raising efficiency and profits.

A unit for production of inert gas was brought into operation in 2009 at the **Volgograd Refinery** and a steam recuperation unit was commissioned at the oil loading rack. The Refinery also completed a project for modernization of the heat exchanger on one of its catalytic reforming units.

The Company's **Perm Refinery** commissioned pipe stills on its atmospheric distillation blocks and stills for hydrotreatment of diesel fuel as part of an ongoing modernization program, as well as launching an automated lubricant packaging line.

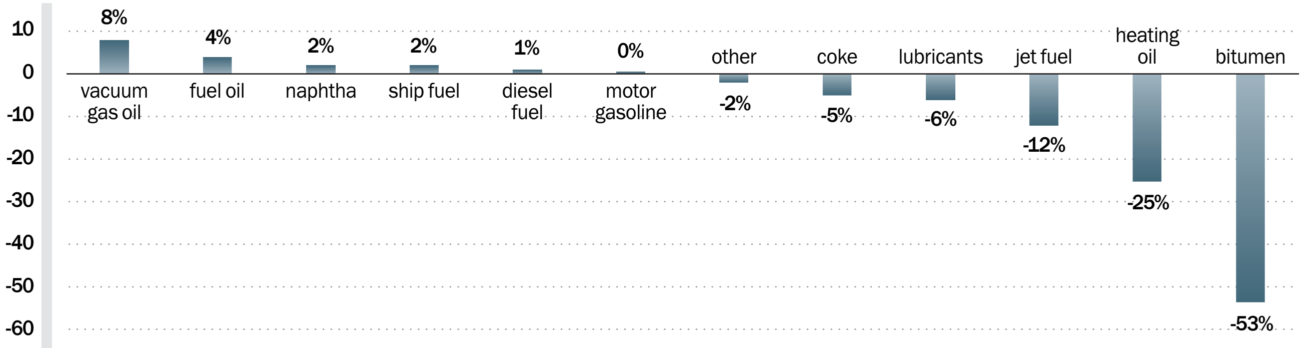
International Refineries

Refinery throughputs in 2009 at LUKOIL Group's international refineries, including the Group share of refining at the ISAB and TRN complexes, were 18.24 million tonnes, which is 50.8% more than in 2008. The large increase is explained by acquisition of stakes in the ISAB and TRN complexes as well as re-commissioning of the Odessa Refinery in April 2008, following modernization. Delivery of large quantities of oil to the ISAB and TRN refineries led to a decline in throughput of Group oil at third-party refineries outside Russia in the reporting year (to 1.73 million tonnes from 2.29 million tonnes in 2008).

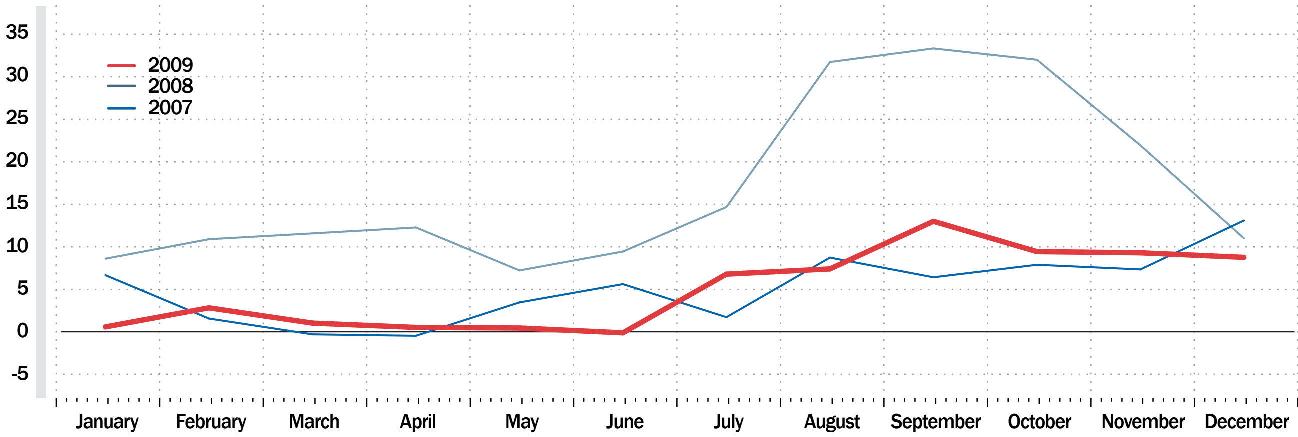
Total refining volumes outside Russia in 2009 including processing at third-party refineries were 19.97 million tonnes, which is 38.8% more than in 2008. Capacity utilization at the Group's own refineries outside Russia in 2009 was 75.3%.

Average refining depth at the Company's foreign refineries (not including ISAB and TRN) was 79.9%, which is slightly higher than in 2008. Light product yield

CHANGE IN OUTPUT LEVELS OF PETROLEUM PRODUCTS AT COMPANY REFINERIES IN 2009 COMPARED WITH 2008, %[1]



REFINING MARGIN IN RUSSIA (AVERAGE REFINERY IN EUROPEAN RUSSIA WITHOUT CATALYTIC CRACKING), $ PER BARREL



(not including ISAB and TRN) was 65.2% (as against 62.2% in 2008). Irretrievable losses at refineries outside Russia fell from to 0.93% to 0.86% in 2009.

Capital expenditures in modernization of the Group's foreign refineries were $308 million in 2009 ($335 million in 2008) and investments were $1,666 million.

Reconstruction work was completed in 2009 at the **Odessa Refinery (Ukraine)** on equipment for hydrotreatment of kerosene-gas oil fractions, enabling the Refinery to produce diesel fuel with sulphur content that meets the Euro-4 and Euro-5 standards.

A new unit for sulphuric acid alkylation with 300,000 tonnes annual capacity was commissioned at the **Burgas Refinery (Bulgaria)**. The launch will enable complete withdrawal from production of the existing sulphuric acid alkylation unit, with 215,000 tonnes annual capacity. Investments in the new unit were more than $90 million and it was designed using the latest technologies, which substantially increase the alkylate octane number and raise quality of gasoline production, as well as reducing atmospheric pollution and consumption of energy, materials and reagents required in production.

Modernization of a diesel hydrotreatment unit for production of Euro-5 fuel was completed in the reporting year. Outline projects were prepared for installation of bitumen and vacuum gas oil hydrocracking units. These projects are being developed as part of construction of a complex for refining of heavy residues.

The Petrotel-LUKOIL Refinery (Romania) completed upgrading of units for hydrotreatment of diesel fuel, catalytic cracking, hydrotreatment of gasoline produced by catalytic cracking, and production of MTBE and TAME, as well as a vacuum unit for the Atmospheric Distillation Block-1. Work on a hydrogen unit was also completed. These projects made the Refinery capable of producing fuels to Euro-5 standards in the reporting year and raised standards of environmental safety.

The Group share in refinery throughput at the ISAB Refining Complex (Sicily, Italy), in which the Group bought 49% stake in 2008, was 6.17 million tonnes in 2009.

In September 2009 the Group began refining of oil at the TRN Refinery in the Netherlands after completing a transaction for acquisition of a 45% stake. The Group share in refining of oil and petroleum products in September to December 2009 was 1.53 million tonnes.

[1] Excluding mini-refineries and the ISAB and TRN complexes.

Acquisition of the TRN Refinery

As part of Group strategy for development in the oil refining segment in Western Europe LUKOIL signed an agreement in June 2009 with the French company, TOTAL S.A. (hereinafter referred to as Total), for acquisition of a 45% stake in the TOTAL Raffinaderij Nederland N.V. refining complex at Vlissingen in the Netherlands.

TRN is among the biggest and most technologically advanced refineries in Western Europe. Acquisition of the stake increased LUKOIL's overall refining capacity by 5% and increased its refining capacities abroad by 16%.

The Group completed the acquisition of 45% of shares in TRN on September 1, 2009. Transaction value was close to $700 million. Management of the JV is now carried out by LUKOIL and Total on parity basis.

Acquisition of a share in the refinery improves the balance between oil production and refining in the Company's asset portfolio, bringing it closer to that of other vertically integrated oil companies. The TRN stake brings the Group's ratio of refining capacity to crude oil production to nearly 75% (at the end of 2009), which is the optimal level for the Group.

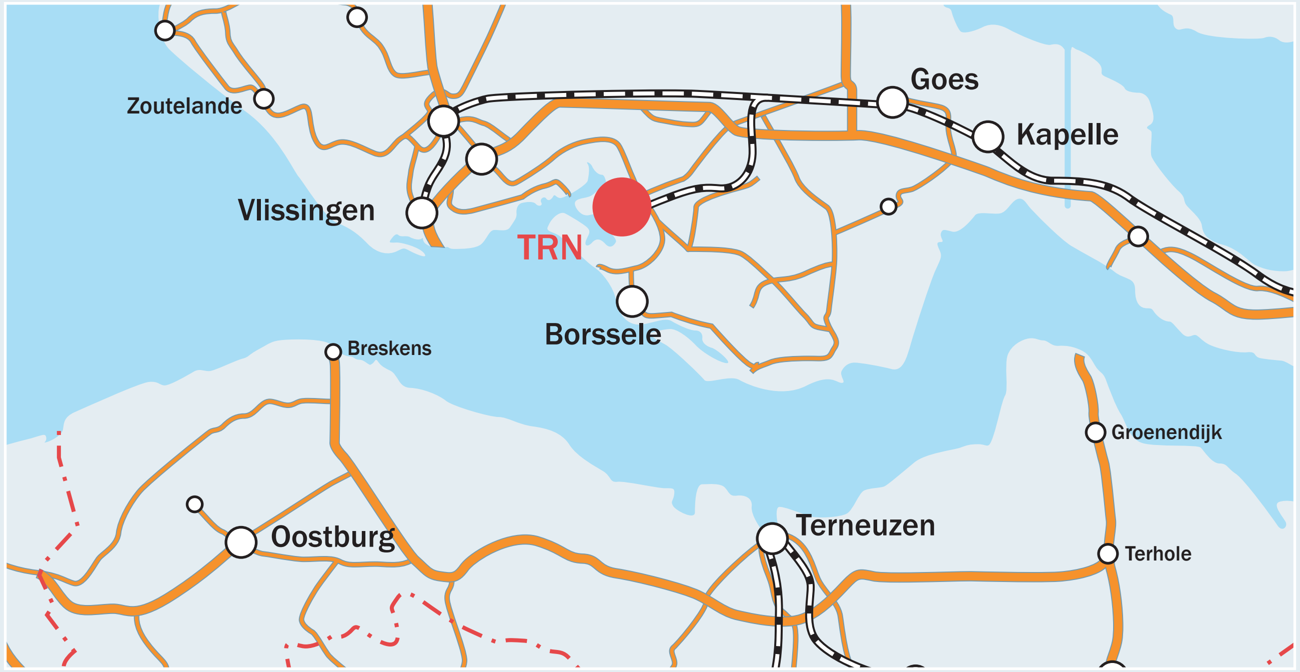
TRN is located in the biggest oil refining and trading hub in north-west Europe (the Amsterdam – Rotterdam – Antwerp region, often referred to as 'ARA'), adjacent to product markets with high value added. About 90% of Refinery output is sold in Belgium, the Netherlands, Germany and Switzerland. Acquisition of the TRN stake strengthens LUKOIL's trading position and enables larger petroleum product supply volumes to the Group's filling station network in Western Europe.

TRN Refinery Profile

The TRN refinery was commissioned by Total in 1973, and is now one of the most advanced refineries in Western Europe with Nelson Index of 9.8 and annual refining capacity of 7.9 million tonnes.

TRN is operated on a 'processing' basis: LUKOIL supplies crude oil and other inputs to the Refinery and receives petroleum products in proportion to its equity stake.

- The Netherlands has one of the largest oil refining segments in the European Union. Its 5 refineries are owned by 6 different companies and have combined daily throughput capacity of 1.3 million barrels. TRN represents 13% of this capacity.



PROJECT GEOGRAPHICAL POSITION

LUKOIL has a 45% stake in all TRN refining units (and 100% in the second hydrogen production unit), except for gasoline production units, which remain in full ownership of Total. The Group expects to obtain benefits from the Refinery's capacity for production of medium distillates (mainly diesel fuel), demand for which in Europe will increase, while gasoline demand in European countries is steadily declining.

TRN has an exceptionally large hydrocracking unit (annual capacity is 3.5 million tonnes) and the refinery is capable of processing various types of crude oil, including oil with high sulphur content.

Refining depth at TRN in 2009 was 71% and light product yield was 65% (the Group's stake in September–December). Diesel and bunker fuel are the largest products at the Refinery (respectively 30% and 23% of marketable outputs in September-December 2009).

The Refinery has unique logistical and infrastructure advantages. It owns 22% of the Maasvlakte Olie oil terminal (Rotterdam), which has 4 million tonnes capacity. It also has access to the Borsele sea terminal, the Van Cittershaven loading wharf and a loading rack for road tankers. TRN owns a naphtha pipeline and 54 reservoirs for storage of crude oil and petroleum products.

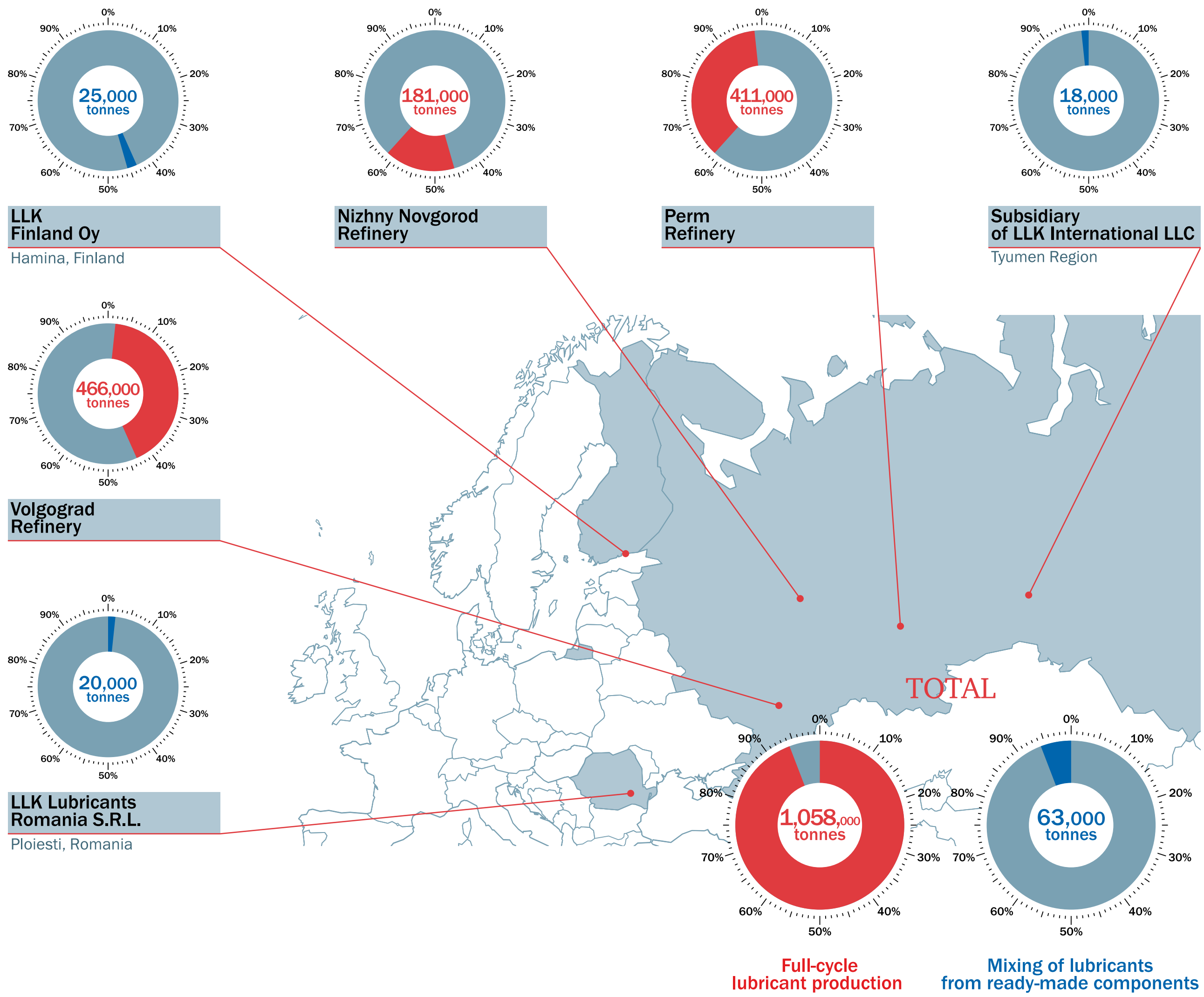
HISTORY OF THE TRN REFINERY

- The TRN refinery was commissioned by Total in 1973.
- In 1980 the company Dow acquired 20% of the refinery.
- Modernization was carried out in the early 1980s and a hydrocracking unit was commissioned in 1986. Dow increased its stake in share capital to 45%.
- The Refinery has carried out a series of modernizations since 1990 to remain one of the most advanced facilities in Europe: units have been installed for purification of kerosene fractions and production of sulphur, and the reactor for hydrotreatment of medium distillates has been expanded to enable production of diesel fuel with sulphur content below 50 ppm. One of the most recent large modernization projects at the refinery was reconstruction of the hydrocracking unit to increase its capacity (completed in 2004).

Production of Oils and Lubricants

Production and sale of oils and lubricants is an important part of LUKOIL's business. The Group is constantly improving the quality of products and expanding their range, as well as raising efficiency of the sales system and diversifying business geography.

LUBRICANT PRODUCTION AT LUKOIL GROUP REFINERIES



LUKOIL is the leader on the Russian oils and lubricants market, accounting for about 44% of domestic production. Oils and lubricants are produced at Group refineries in Perm, Volgograd and Nizhny Novgorod. The Company also mixes lubricants from ready-made components (both produced by the Company and bought from third parties) at facilities in Russia, Finland and Romania.

Group refineries produced 1.06 million tonnes of oils and lubricants in 2009, and mixing of oils and lubricants was 63,000 tonnes. Output of packaged oils was 205,000 tonnes (231,000 tonnes in 2008).

LUKOIL produces about 190 brands of oils and lubricants to the latest international standards. They include motor and transmission oils for all types of transport, base oils (used as inputs for production of ready-to-use oils, lubricants and additives), and lubricants for industrial equipment. In addition to oils and lubricants the Group also makes over 20 brands of other oil-based products as well as over 10 brands of coolants.

The Group worked hard in 2009 to improve efficiency in sales of oils and lubricants, including further development of an import substitution program, which helped to increase sales of industrial lubricants by 26% compared with 2008. The Company launched production of various vehicle-care products in the reporting year, including coolants, anti-freeze, and screen wash. Preparations were made in 2009 for restructuring of the dealer network, and unified systems of credit, price formation and motivation were introduced for dealers in 2010.

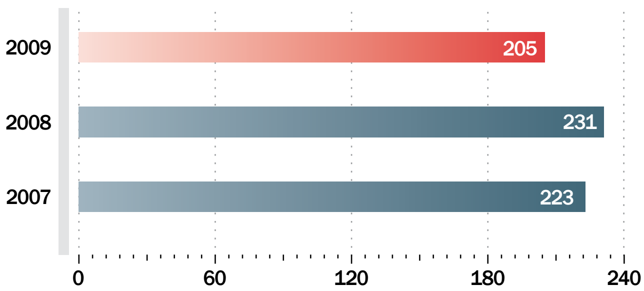
The Company started to make 43 new products in the course of the year and obtained 25 approvals from vehicle and machine-building companies.

LUKOIL MOTOR OILS

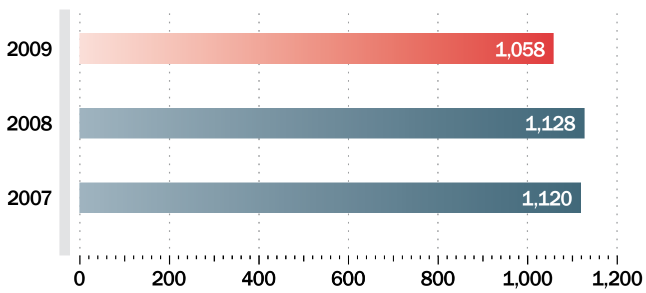
LUKOIL motor oils match international requirements of the Society of Automotive Engineers (SAE), the American Petroleum Institute (API), the European Automobile Manufacturers Association (ACEA) and the Russian Association of Automobile Engineers (AAE). Our oils are produced using the latest technologies and contain high-quality additives supplied by Russian and foreign producers.

High performance qualities of LUKOIL lubricants have been acknowledged by major automotive manufacturers in Russia and abroad. Company motor oils have passed tests at western certification centers on engines made by DaimlerChrysler, BMW, Volkswagen, MAN, Porsche, Volvo, Renault trucks and Cummins, and have been approved for use in these engines. In 2009 a total of 25 product approvals were obtained from vehicle and machine builders.

PRODUCTION OF PACKAGED OILS, THOUSAND TONNES



OILS AND LUBRICANTS PRODUCTION AT COMPANY REFINERIES, THOUSAND TONNES



LLK-Naftan, the joint venture between LUKOIL and the Naftan refinery (Belarus), met 34% of LUKOIL's requirements for additives used in lubricant production in 2009, and the share will increase to 80% in the medium term. The JV has increased output almost by 7 times, from 3,000 to 20,000 tonnes, since its creation in 2006.

The Company carries out sales of oils and lubricants in more than 40 countries worldwide and sales geography is constantly expanding. In 2009 LUKOIL began lubricant sales on the following new markets: Lebanon, Algeria, Israel, India, Vietnam, Turkmenistan, Taiwan, Pakistan, Iraq and Jordan.

The Company rapidly expanded lubricant sales in Turkey in 2009, where agreements were signed for lubricant deliveries to over 500 service centers of leading international car makers, such as Mercedes, Ford, Mitsubishi, Renault, Man, Toyota, Opel, Iveco, Skoda and others.

Constant expansion of the product range and improvement in the quality of Company oils and lubricants supports growth of sales volumes. Sales of LUKOIL branded lubricants were over 190,000 tonnes in 2009, which is 6% more than in 2008. Main markets for branded lubricants were Russia, Kazakhstan and Finland. The biggest increase compared with 2008 was in sales of packaged lubricants in Belarus (by 12%, including 39% increase in sales of branded lubricants).

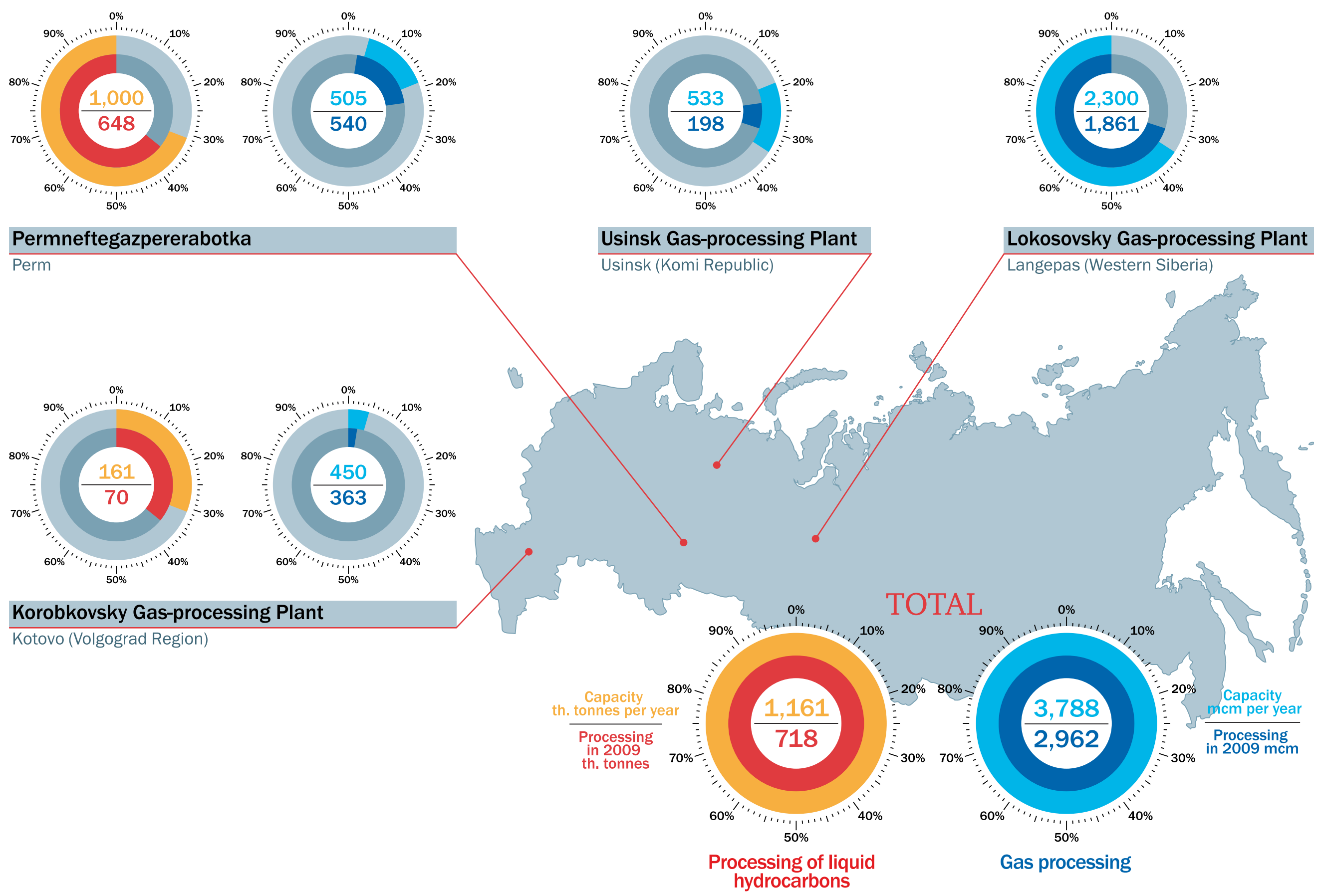
In an important breakthrough, LUKOIL began sale of its own lubricants for ship engines in 2009. In June and August the Group obtained approvals for use of its new generation of lubricants, LUKOIL NAVIGO, in the most up-to-date maritime engines (including those of MAN, B&W and Wartsila). By the end of 2009 the Group's ship lubricants were available for sale in 122 ports in 24 countries in Europe, America, Asia and the Middle East.

The Company has done much work to develop customer relations in its lubricant business. LUKOIL was among the first companies in the industry to offer comprehensive service with full product support, from placement of client orders to delivery of the product and, ultimately, disposal of used lubricants. Thanks to this policy the Company now sells more than 80% of its lubricant output directly to end-users.

Gas Processing

Gas-processing plants of LUKOIL Group process associated gas from fields in Russia into marketable gas (fed into the Gazprom gas pipeline system) and liquid hydrocarbons.

GAS-PROCESSING PLANTS OF LUKOIL GROUP



In 2009 the Company's gas-processing plants processed 2.962 billion cubic meters of gas feedstock and 718,000 tonnes of natural gas liquids (9% and 17% less than in 2008, respectively). The reduction was due to lower demand for products as well as to overhaul of an associated gas compressor unit at the Korobkovsky Gas-processing Plant (completed in November 2009).

During 2009 company plants produced 2.346 billion cubic meters of stripped gas, 785,000 tonnes of LPG and 838,000 tonnes of liquid hydrocarbons (stable gas naphtha, isopentane and hexane-heptane fractions, and natural gas liquids).

Work proceeded in the reporting year at the Company's **Usinsk Gas-processing Plant** on construction of an associated gas compressor unit with annual capacity of 500 million cubic meters, and on installation of a desulphurization unit with annual capacity of 100 million cubic metres.

The **Permneftegazpererabotka** Plant carried out various projects to help achieve the Company's target of 95% utilization of associated gas. Work to reduce costs in all areas and increase profitability was carried on.

There were no major modernization projects at the **Lokosovsky Gas-processing Plant** in 2009, but 2 cylindrical vertical flare furnaces were brought into operation, which helped to ensure more reliable operation of other technical equipment. Deliveries of gas liquids were optimized, including increase of deliveries to Stavrolen by 7 times.

Work was carried out at the **Korobkovsky Gas-processing Plant** on upgrading of a boosting compressor station and installation of a propane cooling unit, as well as work to ensure that the Plant meets current industrial and environmental standards.

Opinion Column

Rauf Gafarov, CEO of Korobkovsky gas processing plant

There is only one company in Rauf Gafarov's service record – Korobkovsky gas processing plant, however, the record contains a lot of entries reflecting 33 years of hard working experience starting from an operator of process installation to a CEO.

— What period of your working experience do you remember most vividly?

— My first position – an operator of processing installation. Everything was interesting to me as what we'd been taught at university differed from practice. And it was also the period when I realized that a lot in life depends on a man himself. The matter is not only in knowledge you get at university – everyone is equal after the graduation. The main thing is not to skid and go on learning and advancing forward.

— Korobkovsky gas processing plant has been actively modernized; a lot of modern units have been put in operation. What are your plans for the future?

— Launch of propane refrigeration unit is expected sometime soon within the scope of the modernization program. The program will be fully completed in 2012. Korobkovskiy plant will become a totally different enterprise furnished with the latest highly technological equipment and latest gas processing technologies. The next step is to increase the profitability of operations. I think we'll manage: we have trusted staff at the plant.

Petrochemicals

LUKOIL's petrochemical business is one of the biggest in Russia, CIS and Eastern Europe. Company plants in Russia, Ukraine and Bulgaria make pyrolysis and organic synthesis products, fuel fractions and polymer materials. LUKOIL meets a major share of Russian domestic demand for various chemicals and is a major exporter of chemicals to more than 30 countries worldwide.

In accordance with its development strategy in the petrochemicals sector, LUKOIL is steadily increasing production of chemicals with high value added (polymers, monomers and organic synthesis products) and reducing production of chemicals with low value added (secondary pyrolysis products and fuel fractions).

LUKOIL petrochemical plants produced 902,000 tonnes of petrochemicals in 2009, which is 38% less than in 2008. The reduction was due to suspension of production at Karpatneftekhim in May 2008 for upgrading work as well as reduction of demand for petroleum products.

Markets for petrochemical products were highly volatile in 2009. A sharp decline of prices in the first half of the year (continuing from the end of 2008) was followed by a modest recovery in the second half of the year. As a result, the sale price for polyethylene in Russia declined by 11.7% in the course of the year, polypropylene prices fell by 18.4%, and prices for benzol fell by 16.9%. Price declines for all three products were even more marked in Europe, where prices dropped by 27.4% for polyethylene, 27.6% for polypropylene and 32.8% for benzol.

LUKOIL moved ahead with modernization of existing production and installation of new production in 2009 as part of its strategy for development in the petrochemical sector. Capital expenditures in the sector were $113 million in 2009.

Production was halted at the **Karpatneftekhim** plant in May 2008 so that a large-scale upgrade could be carried out. Construction and assembly work was completed in 2009 on a new chlorine and caustic soda production unit using membrane electrolysis technology. Annual capacity of the new unit is 182,000 tonnes of gaseous chlorine and 200,000 tonnes of caustic soda. Completion of the project will enable Karpatneftekhim to produce caustic soda, which meets international quality standards, and to fully cover the plant's own chlorine needs. Commissioning of the unit is scheduled in mid-2010.

Karpatneftekhim also continued work on construction of a suspended polyvinylchloride unit with annual capacity of 300,000 tonnes. Its integration with the plant's capacities for production of vinylchloride monomer will greatly increase overall efficiency. Commissioning of the unit is scheduled at the end of 2010.

Routine repair work was carried out at **Saratovorgsintez** in 2009 and the sodium cyanide unit, which was installed in 2008, reached its target production level of 15,000 tonnes per year. The plant achieved input and energy savings in the reporting year.

At **Stavrolen** reconstruction of the storage facility for liquefied hydrocarbon gases continued in 2009 in order to increase gas feedstock handling and processing from 200,000 to 400,000 tonnes per

LUKOIL GROUP PETROCHEMICAL PLANTS

PETROCHEMICAL PLANTS

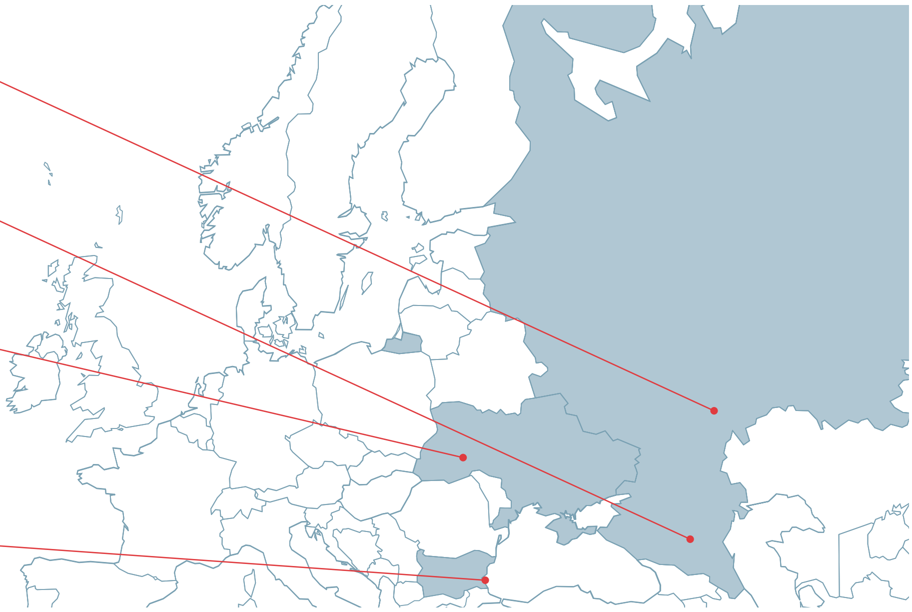
Saratovorgsintez
Saratov (Russia)
- Acrylonitrile and other organic synthesis products

Stavrolen
Budennovsk (Stavropol Region, Russia)
- Polyethylene and other products

Karpatneftekhim
Kalush (Ukraine)
- Polyethylene, vinyl chloride and other products

REFINERIES WITH PETROCHEMICAL UNITS

LUKOIL Neftokhim Burgas AD
Burgas (Bulgaria)
- Polymers and organic synthesis products



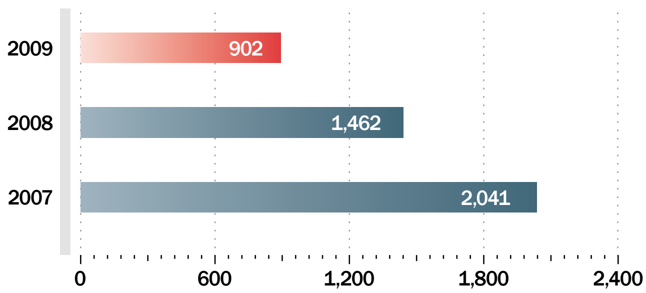
year. Commissioning of the facility is scheduled in 2010. Polypropylene output reached the target level of 360 tonnes per day in the fourth quarter of 2009, producing new high-index grades with high value added. A new polyethylene compounding line was also commissioned in the reporting year, and the plant reduced unit consumption of electrical energy in production of polyethylene and polypropylene, as well as reducing consumption of natural gas in olefin production.

One of the main projects scheduled by LUKOIL for implementation in the next few years is construction of the **Caspian Gas-chemical Complex**. The Complex will use natural gas and condensate produced by LUKOIL Group in the Caspian region and will have annual capacity of at least 600,000 tonnes of ethylene.

The purpose of the project is to increase value added through deeper processing of gas feedstocks (ethane and natural gas liquids). The Caspian Complex will carry out refining of ethylene and its derivatives into polyethylene, polypropylene and other petrochemical products.

Pre-project work for the Complex was completed in 2009 including preliminary analysis of proposals by licensor firms and engineering companies, as well as further cooperation with the Stavropol regional government aimed at increasing production and sales volumes of petrochemical products.

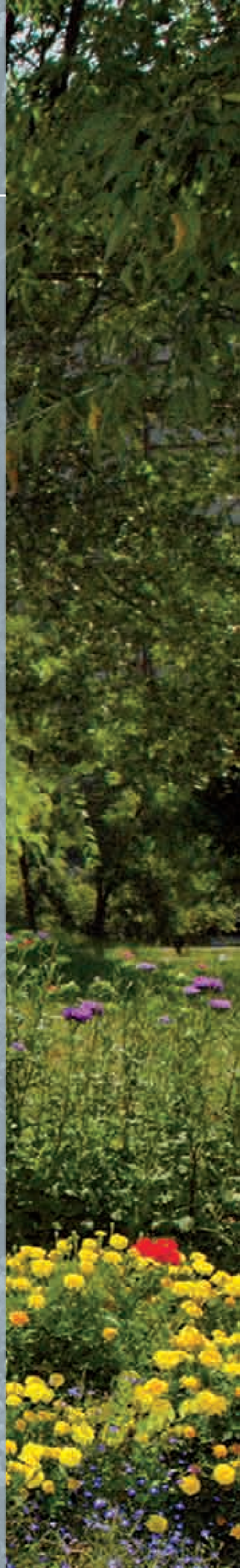
PETROCHEMICAL PRODUCTION, THOUSAND TONNES



Work in 2010 will include definition of production configuration at the Complex and development of a master plan, choice of licensor firms for petrochemical technologies to be used at the Complex, making of licensing agreements and start of design work on base projects (particularly for processing of associated gas).

Power Generation

LUKOIL created a new business sector in 2008: Power Generation. The new segment has a special role in the revised Company's Strategic development program for 2010–2019 and Power Generation will be an important factor for growth of Company cash flows and shareholder value in the long term.



Power Generation

The new sector includes all aspects of power business, from generation to transmission and sale of heat and electrical power, ensuring reliable supplies for the Company's own needs and for external customers.

As well as UGK TGK-8, which was acquired at the end of 2008, and the Company's own power generating facilities at oil & gas fields in Russia, the sector also includes a number of power generators in Bulgaria, Romania and Ukraine.

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Structural Transformations

Restructuring of LUKOIL's power business entered its final stage in the reporting year. The intended final structuring of the sector was achieved, consisting of 7 organizations, which began operations in 2009, including 4 generating companies: LUKOIL-Astrakhanenergo, LUKOIL-Volgogradenergo, LUKOIL-Kubanenergo and LUKOIL-Rostovenergo.

The generating companies manage assets of UGK TGK-8, which was acquired in 2008. The LUKOIL stake in UGK TGK-8 was increased to 100% in 2009 and the company was transformed from a public to a private limited company.

Power Generation

Total production of electrical energy in 2009 by organizations in LUKOIL's power generation business was 14.7 billion kilowatt-hours. Total heat production by generators was 16.9 million Gcal.

Reduction in output of heat energy was due to lower demand and delayed start of the heating season as a result of unusually warm weather in Russia's Southern Federal District.

LUKOIL works constantly to optimize production costs of its electricity enterprises, and applies strict control over implementation of anti-crisis programs for reduction of non-operating expenses.

Small-scale Generating

LUKOIL is continuing rapid development of its own power generating at fields. This enables substantial savings on electricity purchases and raises the level of utilization of associated gas, which is used as fuel for gas-fired generating. The Group generated 1,152 million kilowatt-hours of electricity at its own power generating units in 2009, representing 8.2% of total consumption of electricity by the Group in its production activities.

LUKOIL applies the latest technologies in its investment projects for construction and upgrade of generating facilities. This will ensure increasing reliability of power supplies to LUKOIL enterprises. Use

of new technologies also enables the Company to limit spending on its electricity needs thanks to improvement of energy efficiency and use of the Company's own refined products as fuel for power generation.

Energy-saving Technologies

LUKOIL works constantly to improve reliability of its electricity supply arrangements and to reduce spending on energy. The efforts have been coordinated through corporate programs (being implemented in 2006–2010) for energy saving and improvement of reliability of power supplies.

Savings of fuel and energy resources in 2009 as a result of the energy-saving program were more than $100 million, which is more than double the amount saved in 2008.

Spending on measures as part of the program for improving reliability of electricity supplies was over $100 million in 2009, which is about 20% less than in 2008 (real expenditures adjusted for rouble depreciation remained at the level of 2008). Implementation of the program reduced power cuts and resulting underproduction of crude oil by nearly 30%.

The Company approved an energy audit schedule for its oil & gas production subsidiaries in the period from 2006 to 2010. Purpose of the audit is to identify potential for energy-saving and enhancing energy efficiency and to devise energy-saving measures. In 2009 energy audits were carried out as scheduled at Uraineftegaz (LUKOIL-Western Siberia), the Perm Refinery, Permneftegazpererabotka and Saratovorgsintez.

Company specialists recognize the huge potential for resource and energy saving, offered by alternative sources of energy. Priority alternative sustainable forms of energy supply include hydro- and wind-power, solar energy and geothermal energy. Alternative energy projects by the Company have been on a small scale to date, and have been focused on resolution of local energy-saving tasks. For example, the company installed photoelectric units at two filling stations in 2009 (one in Serbia and the other at Krasnaya Polyana in southern Russia).

Rational use of electricity considerably reduces Group spending on purchase of energy resources. An automated system for measurement of electricity use has been installed at all Company subsidiaries. The system makes it possible to take advantage of tariffs in force at different times of the day, to increase accuracy in measurement of electricity consumption, and to purchase electrical energy and generating capacity on the wholesale market.

Product Deliveries and Marketing

Strategy

Optimizing logistics: reduction of transportation expenses

Prompt management of trade flows

Increasing efficiency of trading operations

Increase of retail sales of petroleum products and of related goods and services

Retail network optimization

Crude Oil Deliveries

Total crude oil deliveries by the Company in 2009 were 115 million tonnes, which is 13% more than in 2008. Oil exports from Russia grew substantially in the reporting year (by 7%) due to supplies of oil from the Yuzhnaya Khylchuya field via the Varandey terminal. Oil refinery throughputs inside Russia remained high (capacity utilization was close to 100%).

The Company sold 3.0 million tonnes of crude oil in **Russia** during the year, which is 42% more than in 2008. LUKOIL used mechanisms of substitution in deliveries of Company crude to refineries at Yaroslavl and Ryazan. This enabled logistics savings compared with the alternative of exporting oil via the port of Primorsk.

The Company **bought** 606,000 tonnes of oil **in Russia** during 2009, compared with 236,000 tonnes bought in 2008.

Refining at the Company's own refineries inside Russia was 44.46 million tonnes, which is 0.6% more than in 2008. Work was carried out to optimize deliveries to Company refineries. Direct contracts were made between LUKOIL-Komi and the Ukhta refinery, and between LUKOIL-Volgogradneftegaz and the Volgograd Refinery (crude oil, which was previously supplied to the Caspian Pipeline Consortium system was supplied instead to the refineries, with positive economic effect). The Company also delivered 2.05 million tonnes of crude oil for processing to third-party refineries in Russia in order to obtain additional profit. An important event was signing in August 2009 of an agreement for supplies of crude oil to refineries in Bashkortostan. This contract gives LUKOIL a guaranteed market for crude oil inside the country on export terms.

Crude oil exports from Russia by LUKOIL subsidiaries (including oil purchased from other producers) grew by 6.9% in comparison with 2008 to 42.02 million tonnes thanks to large deliveries via the Varandey terminal. The Company exported 33.66 million tonnes to the far-abroad countries and 8.36 million tonnes to the near-abroad countries. The Company managed its export deliveries efficiently in 2009, selecting the most profitable export routes.

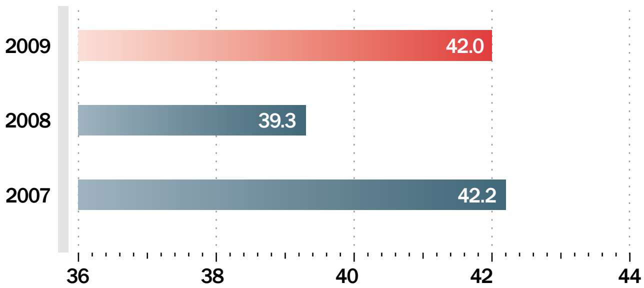
Most export in 2009 was via the Transneft pipeline system. Deliveries via Transneft were 33.00 million tonnes (8.5% less than in 2008) and their share in overall exports was 79%. The volume of export deliveries by-passing the Transneft system almost doubled in 2009 to 9.02 million tonnes of crude oil, due to commissioning of the Company's Varandey terminal in 2008. Deliveries through Varandey were valued on the basis of actual quality of the crude oil, at a premium to the Urals price. (There is no oil quality bank in the Transneft system, so crude oil of any quality supplied through this system is sold at the price for Urals blend crude, making Urals blend the Company's main export commodity).

The Company exported 8.7 million tonnes of crude oil via its own transport terminals in 2009 compared with 2.8 million tonnes in 2008. Use of the Company's own terminals reduces transportation costs and makes transport arrangements more flexible.

An important achievement in 2009 was design and implementation of a new logistics scheme for deliveries of oil by the company RITEK via the northern sea route. Lowering of freight prices and demurrage rates enabled a more financially attractive export scheme for RITEK using LUKOIL Group infrastructure (direct deliveries to Europe and use of LITASCO buffer storage facility in Murmansk).

The Company continued to apply a new approach to price formation as part of work to improve efficiency of crude oil deliveries in 2009. The new approach takes account of developments on the international

CRUDE OIL EXPORTS, MILLION TONNES



market for purposes of oil sales in Russia and the near-abroad countries. This has positive impact on quality of commercial decisions, which are better founded, since financial outcomes are more predictable at the time when deliveries are planned.

Feedstock deliveries to foreign refineries of LUKOIL Group and to the ISAB and TRN refining complexes were 18.24 million tonnes, representing a record 50.7% increase compared with 2008. This was achieved thanks to acquisition of stakes in Western European refineries. The Company also delivered oil for processing to third-party refineries (Naftan and the Mozyr refinery in Belarus and the Panchevo refinery in Serbia). Volumes of these deliveries in the accounting year were 1.73 million tonnes, which is nearly 25% less than in 2008.

LUKOIL sold 46.98 million tonnes of crude oil on the international market in 2009, including 5.33 million tonnes in the near-abroad countries and 41.65 million tonnes in countries of the far-abroad.

VARANDEY OIL TERMINAL

In 2008 LUKOIL Group commissioned the Varandey oil loading terminal with crude oil throughput capacity of up to 12 million tonnes per year (240,000 barrels per day). Crude oil deliveries to the terminal are mainly from the Timan-Pechora oil & gas province, primarily from the Yuzhnaya Khylchuya field, which was brought into operation in the summer of 2008.

Facilities built and commissioned at Varandey include a stationary, ice-resistant loading terminal at sea, a shore tank farm with capacity of 325,000 cubic metres, two stretches of underwater pipeline, and also an oil accounting facility, auxiliary reservoirs, a pumping station, energy supply facilities, a shift camp for duty personnel and other infrastructure. Capital expenditures during the whole period of construction were $1.1 billion.

The terminal operates as follows: ice-class shuttle tankers with deadweight tonnage of 70,000 tonnes transport oil to a floating reservoir in the ice-free waters off Murmansk, then long-distance tankers with deadweight tonnage of 150,000 tonnes deliver the oil to Western Europe and the USA. About 7.7 million tonnes of crude oil were shipped through the terminal in 2009.

Gas Deliveries

The gas segment is a new and rapidly developing business segment for LUKOIL Group. Expansion in the gas segment is one of our strategic tasks, emphasizing commercialization of gas reserves to boost Company value.

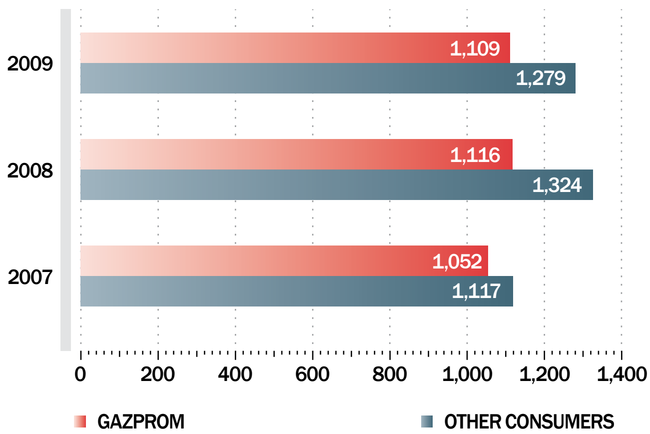
Sales of natural, associated, stripped and dry gas by the Group's Russian organizations totalled 10.947 billion cubic meters in 2009. Of this total, 7.584 billion cubic meters of gas were sold to Gazprom (including 6 billion cubic meters of natural gas from the Company's Nakhodkinskoye field) and 3.363 billion cubic meters of gas were sold to other consumers. Decrease in sales volumes was due to lowering of global demand for gas and corresponding limitations of the volumes bought by Gazprom.

Thanks to share increase of price-efficient deliveries to end-users, the average sale price for gas stayed at the level of 2008 (1,152 roubles per thousand cubic meters), consisting of 1,109 roubles per thousand cubic meters for Gazprom and 1,279 roubles per thousand cubic meters for end-users.

In order to increase profit from sales and simplify arrangements for gas supply to end-users, the Company made large deliveries in 2009 through Gaz-Oil Trading (a parity joint venture between LUKOIL and Gazprom subsidiaries). Creation of the joint venture has enabled a unified approach to pricing and has simplified gas supplies through the Gazprom gas-transportation system.

In order to minimize costs the Company carried out preparatory work in the accounting year, which will enable contracts to be made for direct gas supplies to end-users (specifically, the generating company, UGK TGK-8), cutting out intermediaries.

LUKOIL SELLING PRICE FOR GAS, ROUBLES PER THOUSAND CUBIC METRES



Gas Balance


ASSOCIATED GAS
NATURAL GAS
RUSSIA
Own consumption 1.50 bcm
Gas production 5.82 bcm
Marketable gas 4.32 bcm
Processing at gas-processing plants 2.96 bcm
Other sales 1.36 bcm
Own consumption 0.21 bcm
Gas production 6.55 bcm
Marketable gas 6.34 bcm
Total sales 6.34 bcm
Gazprom 5.95 bcm
Other 0.39 bcm
INTERNATIONAL
Own consumption 0.09 bcm
Gas production 0.45 bcm
Marketable gas 0.36 bcm
Sales 0.36 bcm
Own consumption 1.01 bcm
Gas production 4.89 bcm
Marketable gas 3.88 bcm
Sales 3.88 bcm

Petroleum Product Marketing

Wholesale Trading in Petroleum Products

LUKOIL's petroleum product wholesale business in **Russia** is carried out by its refineries and by 7 petroleum product organizations inside the Group, operating in 62 regions of the country. Volume of petroleum product wholesale in Russia in the accounting year was 9.80 million tonnes, which is 26.4% less than in 2008. Gradual increase of world oil prices in 2009 had an effect on prices for main petroleum products on the domestic market, which remained 10–20% higher than export prices, taking account of transport expenses and duties.

Company organizations **exported** 27.8 million tonnes of petroleum products to the near- and far-abroad countries in the reporting year, which is 7.7% more than in 2008. Exports were dominated by heating oil, diesel fuel/gas oil and vacuum gas oil, which accounted for 89.4% of total export volumes. The Company's petroleum product export structure mainly corresponds to the structure of exports from Russia as a whole. The Company maintained efficient management of product deliveries from Group oil refineries during 2009.

Railway remained the main means of transport for Group exports of petroleum products (over 80% of the total in 2009). Optimization of petroleum product deliveries by rail continued in 2009: LUKOIL used its own rail cars and cars provided by other private companies, tariff rates were lowered and the Company obtained discounts on main export routes. This enabled the Company to successfully limit growth in the cost of rail shipments.

The 2007 agreement with Russian Railways on development of rail infrastructure for shipment of up to 12 million tonnes of petroleum products per year to the Vysotsk terminal continued to be implemented in 2009. It was decided in 2008 to examine the possibility of increasing shipment volumes to 14 million tonnes. A total 13.7 million tonnes of petroleum products were shipped through Vysotsk in the reporting year, helping to optimize efficiency of petroleum product deliveries by the Company.

Petroleum products are also exported by sea and river transport. In order to minimize transport costs and diversify routes, the Company mainly used Russian ports for petroleum product transshipment in 2009. LUKOIL made no use of Ukrainian ports for deliveries of fuel oil in 2009 thereby optimizing deliveries of dark petroleum products and making savings of $14 million. Redirection of more fuel oil volumes (up to 1 million tonnes) from St. Petersburg port to the Vysotsk terminal gave further savings of $16 million. Also the Company benefited from introduction at the end of the year of a zero VAT rate for transportation of petroleum products through Primorsk, which reduced the amount of working capital that was diverted for tax payment by about $1 million each month.

The Company is working continually to optimize delivery routes for exports of petroleum products. In 2009 exports of diesel fuel EN 590 with sulphur content of 10 ppm were partly reoriented from Vysotsk to Primorsk, which gave a cost saving of more than $13 million.

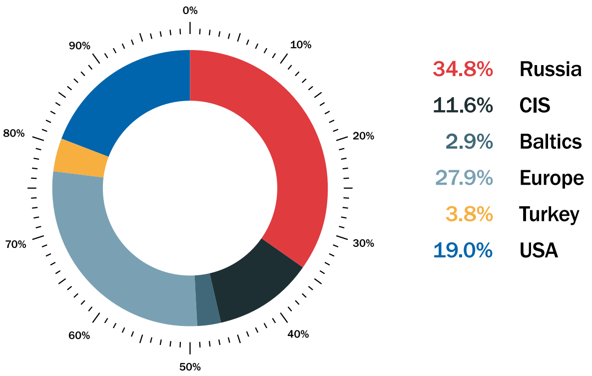
From the start of the navigation season, petroleum products are delivered for export by tankers from the Company's river terminals, enabling significant reduction of transportation costs. LUKOIL also succeeded in reducing river freight costs as a result of negotiations with ship owners, which gave a saving of $8 million in the 2009 river transport season compared with 2008.

About 9% of petroleum product exports in 2009 were by pipeline. LUKOIL increased the volume of such exports by more than 10% in 2009, thanks to commissioning in September 2008 of the Sever Pipeline System, connecting Kstovo Pumping Station and the port of Primorsk.

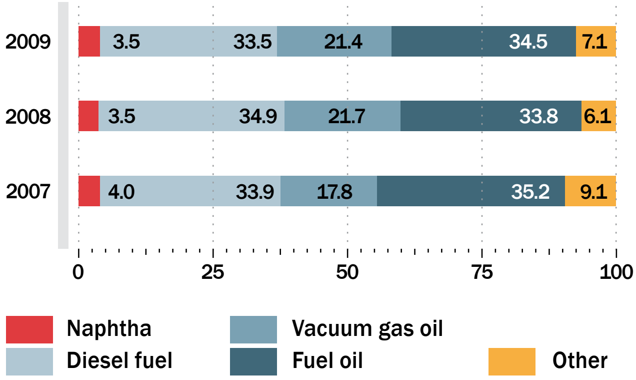
LUKOIL is rapidly developing its **international trading business** in petroleum products by increase of scale and geographical diversification of the business. The objective of LUKOIL's international trade is to place Company resources as efficiently as possible, including direct sale to end-users (by-passing third-party traders). Volume of the Group's wholesale petroleum product sales on the international market in 2009 was 76.89 million tonnes, which is 13.6% more than in 2008.

LUKOIL has trading offices in 9 countries worldwide and makes deliveries of crude oil and petroleum

STRUCTURE OF PETROLEUM PRODUCT SALES IN 2009 (WHOLESALE AND RETAIL)



PETROLEUM PRODUCT EXPORT STRUCTURE, %



products to markets in Europe, the USA and the Asia-Pacific region, as well as increasing its sales volumes in new regions (Africa, Latin America and the Middle East). The Company had trading business in 86 countries worldwide during the reporting year.

LUKOIL constantly monitors global hydrocarbon markets when planning placement of its products. This gives opportunities for arbitrage deliveries, using both the Company's own resources and third-party resources. The Company also blends petroleum products, including biofuels, on its main sales markets in order to achieve the best-possible match with consumer preferences and quality demands.

Petroleum Product Retail

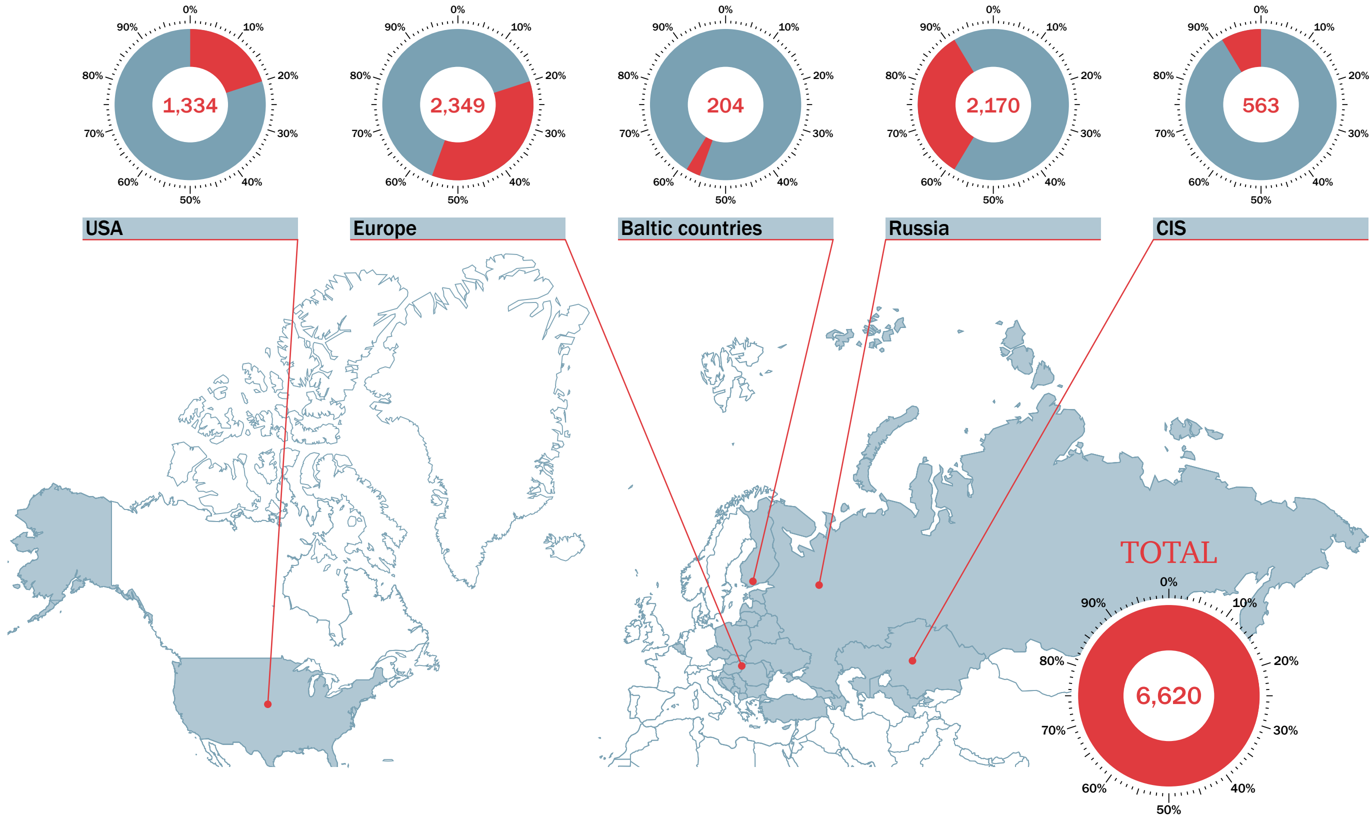
The Company's retail network extends to 26 countries, including Russia, the near-abroad countries and European countries (Azerbaijan, Belarus, Georgia, Moldova, Ukraine, Bulgaria, Hungary, Finland, Estonia, Latvia, Lithuania, Poland, Serbia, Montenegro, Romania, Macedonia, Cyprus, Turkey, Belgium, Luxembourg, Czech Republic, Slovakia, Croatia, and Bosnia and Herzegovina) as well as the USA. The network includes 199 tank farm facilities with total capacity of 3.13 million cubic meters and 6,620 filling stations (including franchises).

Retail sales of the Company's petroleum products were almost unchanged in the reporting year: 14.08 million tonnes of petroleum products were sold through our own filling stations, which is 0.6% less than in 2008. However, average Group sales per filling station (owned or leased) rose from 7.3 to 7.8 tonnes per day thanks to optimization of the retail network and reduction in numbers of stations with low efficiency (particularly in the USA).

Good results were achieved mainly due to increase of sales volume on the Russian market and efficiency improvements in the segment. Retail sales outside Russia fell by 4.1% due to lower demand (reduction of transport volumes). The Company's new strategy is to focus on optimization of the existing filling station network rather than acquisition of new assets. Investments in the retail segment in 2009 were $506 million.

The Company continued optimization of its filling station network in 2009, upgrading or disposing of stations and tank farms with low-efficiency: 7 low-efficiency filling stations were withdrawn from the Group in Europe, while in Russia 10 filling stations and 5 tank farm facilities were withdrawn and 16 filling stations and 8 tank farms were sold. The retail network in the USA shed nearly 200 low-efficiency stations. However, construction and acquisition of highly-efficient stations continued, and upgrading was carried out at existing stations. In Europe 35 filling stations were built and

LUKOIL FILLING STATION NETWORK



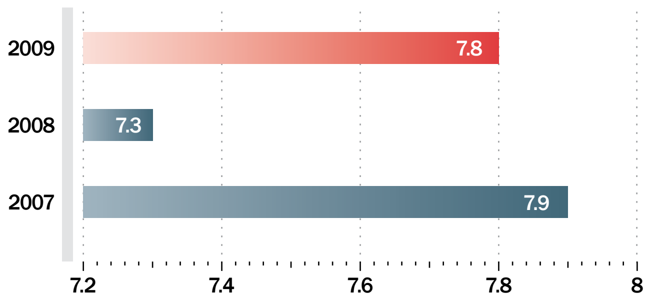
38 were upgraded. In Russia 40 filling stations were built and 39 upgraded. Capital expenditures in the retail sector in 2009 were $313 million.

The Company continued to implement its program for development of a marketing and sales network for liquefied and compressed gas. The program envisages increase in sales volumes of these products in Russia to 530,000 tonnes per year in the period up to 2014. Sales of liquefied and compressed gas by Group organizations in Russia were 120,000 tonnes in 2009.

At the end of 2009 the Group had 111 multi-fuel and gas filling stations in Russia. The Company's strategy in the Refining & Marketing segment targets increase in the number of stations to 318 in 2013 and 345 in 2017.

The Company launched Russia's first dual-use (water – shore) filling station in 2009 in St. Petersburg. The station can serve both vehicles (up to 500 refuellings per day), and small boats during the navigation period on the River Neva (up to 60 refuellings per day). The station was built to meet strict environmental standards applicable to ordinary filling stations and to sea terminals for petroleum product transshipment.

AVERAGE DAILY SALES OF PETROLEUM PRODUCTS PER FILLING STATION, TONNES



The Group's multi-fuel and gas retail network abroad consisted of nearly 1,000 stations at the end of 2009. Total volume of liquefied and compressed gas sales by Company organizations outside Russia in the accounting year were 612,000 tonnes (622,000 tonnes in 2008), including retail sales of 369,000 tonnes.

Russia

LUKOIL's retail network in Russia consists of 2,170 filling stations (including franchises) and 118 tank farm facilities with reservoir capacity of 1.37 million cubic meters. The filling stations and tank farms are operated by 7 petroleum product supply organizations, which do business in 62 of Russia's administrative regions.

Volume of retail sales of petroleum products on the domestic market in 2009 was 6.22 million tonnes, which is 4.2% more than in 2008. Capital expenditures in the Russian retail sector were $157 million ($357 million in 2008), and investments were $202 million. The Company withdrew 10 filling stations and 5 tank farm facilities in 2009 as part of its program for optimization of the sales network, and also sold 16 filling stations and 8 tank farms, leased out 45 filling stations and mothballed 3 tank farm facilities. The Group acquired and built 61 filling stations, and rebuilt 39.

Decline of demand associated with lower transport volumes in the context of the world economic crisis led to reduction in average daily sales of petroleum products per Company filling station in Russia from 9.8 tonnes in 2008 to 9.3 tonnes in 2009.

There was steady growth through 2009 in sales of EKTO branded motor fuels, which the Company launched in 2006. Sales of EKTO gasolines in December 2009 were 132,000 tonnes, which is 83% more than in January. Total sales of EKTO gasoline in 2009 were 1.3 million tonnes, which is 77% more than in 2008, and sales of EKTO diesel fuel were 869,000 tonnes, which is 23% more than in 2008. The Company also expanded sales geography of the new fuels. EKTO fuels fully meet European environmental standards (Euro-3 for gasolines and Euro-4 for diesel), and they offer improved performance features, which justify a price premium for quality. In October 2009 LUKOIL began sales of new premium EKTO gasolines, EKTO Plus (octane number 95) and EKTO Sport (octane number 98), which offer further engine power and fuel economy gains compared with the previous generation.

In November 2009 LUKOIL won a nomination for 'Best petroleum products supplied to Russian consumers', based on research into the Russian retail market in 2008, carried out by the company InfoTEK-Consult. The Company was commended for its major contribution to improving the quality of Russian petroleum products.

Development of the system of payment for petroleum products at filling stations using LICard fuel cards continued in 2009. The number of filling stations where these cards can be used grew by 1% to 2,814 stations, of which 1,886 belong to LUKOIL Group. The number of cards in circulation increased by 34% to 2.72 million. A total of 3.2 million tonnes of petroleum products were sold using LICards, which is 8% more than in 2008.

The program for development of retail sales of non-fuel products and services by LUKOIL Group's Russian petroleum product organizations in the period up to 2014 continued to be implemented in 2009. More than 2,000 of our filling stations in Russia had their own shops by the end of 2009. Revenue from sales of non-fuel products and services through the Group's retail network in 2009 was over $155 million (41% of revenue was from sales of food goods, 29% represented packaged products, 22% came from accessories and 8% from sale of services). The revenue increase reflects improvement in service quality at filling stations and expansion of the range of goods and services on offer. The program target for revenue by 2014 is about $300 million. Development of non-fuel business is an important factor for positioning of LUKOIL Group as a customer-oriented company with European standards of service.

International

LUKOIL's retail network in Europe, the near-abroad countries and the USA consists of 4,450 filling stations (including franchises) and 81 tank farms with reservoir capacity of 1.75 million cubic meters. The Company built 35 new filling stations outside Russia in the reporting year, acquired 12 and upgraded 38. LUKOIL also withdrew 7 stations outside Russia from service in the reporting year.

Capital expenditures in international retail in 2009 were $156 million ($369 million in 2008), and investments were $304 million.

Retail sales of petroleum products on international markets in 2009 were 7.86 million tonnes (8.20 million tonnes in 2008). Average daily sales of petroleum products per filling station in Europe and countries of the near-abroad were 7.0 tonnes, which is 5% less than in 2008. Daily sales per station in the USA were 6.8 tonnes. Thanks to withdrawal from the Group of inefficient stations, sales volumes per filling station in the USA were unchanged compared with 2008, despite reduction of demand.

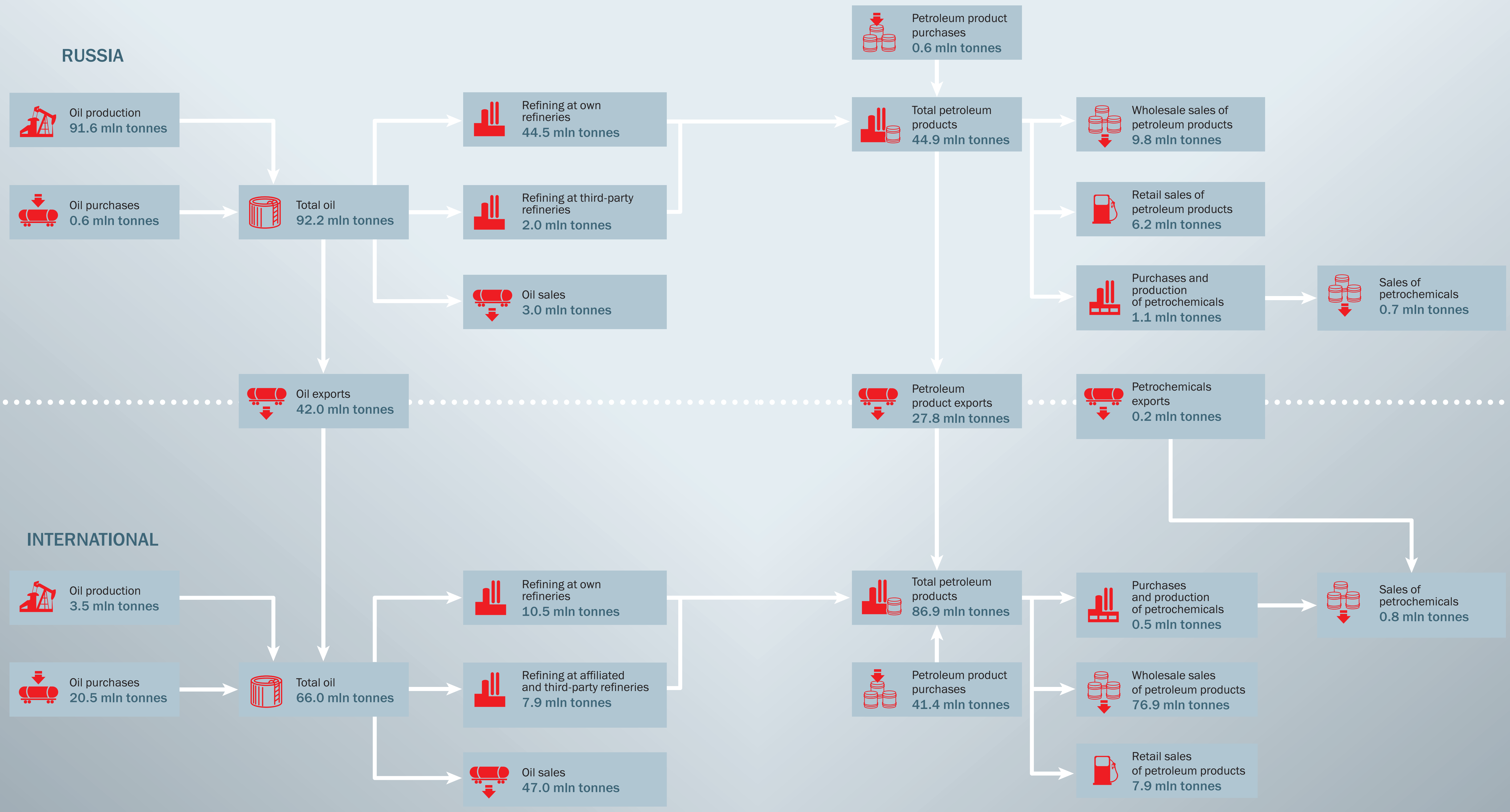
The Company continued rebranding of acquired sales assets in the accounting year. Rebranding of 376 filling stations purchased from ConocoPhillips at the end of 2006 in Hungary, Poland, the Czech Republic, Belgium and Slovakia was almost completed (52 of the stations were rebranded in 2009). The Company also completed rebranding of 82 Akpet filling stations (Akpet was acquired in 2008).

Abroad, as in Russia, LUKOIL is working hard to increase profitability of its filling stations, particularly through development of retail sales of non-fuel products and services. Revenue from sales of non-fuel products and services at filling stations abroad increased to over $500 million in 2009. The Company plans to further increase non-fuel revenues from filling stations abroad through increase in numbers of filling stations, broadening of the product range, improvement in customer service quality, optimization of work with suppliers and intensive marketing activity.

The LICard system was in use at 667 filling stations outside Russia by the end of 2009 (the figure at the end of 2008 was 642 stations).

TRADE BALANCE

Trade Balance



Technology and Innovation

New technologies and innovation are among LUKOIL's competitive strengths. The Company's specialists are engaged both in development of new technologies and modernization of existing ones.

The Group began intensive cooperation in 2009 with The Russian Corporation of Nanotechnologies (RUSNANO) on commercialization of nanotechnologies and their application in the oil & gas industry. The companies are considering joint development work and implementation of various projects, including creation of large-scale (multi-tonne) production of a unique nano-reagent, RITIN, which enables major improvement of oil recovery from formations, as well as development and production of permanent-magnet electric motors using highly efficient, nano-built magnets. The partners are also considering potential for testing of nanotechnologies, developed with RUSNANO's participation, at Group enterprises. Such technologies include multi-functional nano-coatings, sulphur purification units that use nano-catalyzers, and various other nanotechnologies.

LUKOIL Group spent more than $80 million on research & development in 2009 ($95 million in 2008). Institutes in the Company's R&D complex carried out project and research tasks and other work with total value of $200 million.

Exploration & Production Technologies

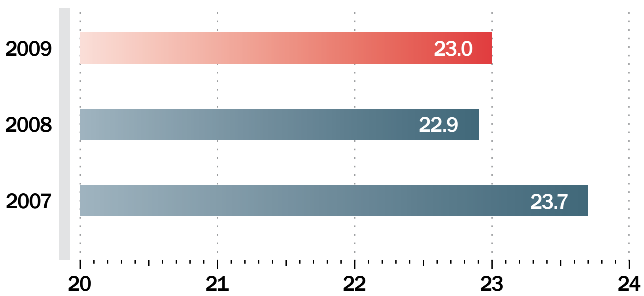
LUKOIL fully recognizes the vital role of technology in supporting competitiveness of the Exploration and Production segment.

Most R&D work in the segment in 2009 was focused on development of geological and geophysical study techniques, improvement of reserve assessment methods (work continued on a methodology to assess hydrocarbon reserves in reservoirs with complex structure), as well as design and improvement of methods for increasing oil recovery and optimizing technological solutions used for development of new areas and accumulations. The Company is particularly keen to develop technologies that ensure environmental safety during field development, most notably during development of offshore fields.

Production of oil began in 2010 at the Yu. Korchagin field, where development will use a system of extra-long horizontal wells (more than 5 km). This is a unique project solution in Russia. In addition all works at the field are to be carried out on a 'zero-discharge' basis, which avoids negative environmental impacts.

One of the most important outcomes of the Company's technology development efforts is increasingly widespread application of methods for intensifying oil production and of enhanced oil recovery (EOR) techniques. These methods offer significant increase of recoverable reserves and oil production, enabling commercial development of high-viscosity oil, oil in almost impenetrable collectors and hard-to-recover reserves at late stages of field development. In recent years the share of oil produced at LUKOIL fields using various EOR techniques has been over 20% of total oil production. The Company applies physical, chemical, hydrodynamic and heat methods to stimulate extraction.

ADDITIONAL PRODUCTION FROM EOR IN RUSSIA, MILLION TONNES

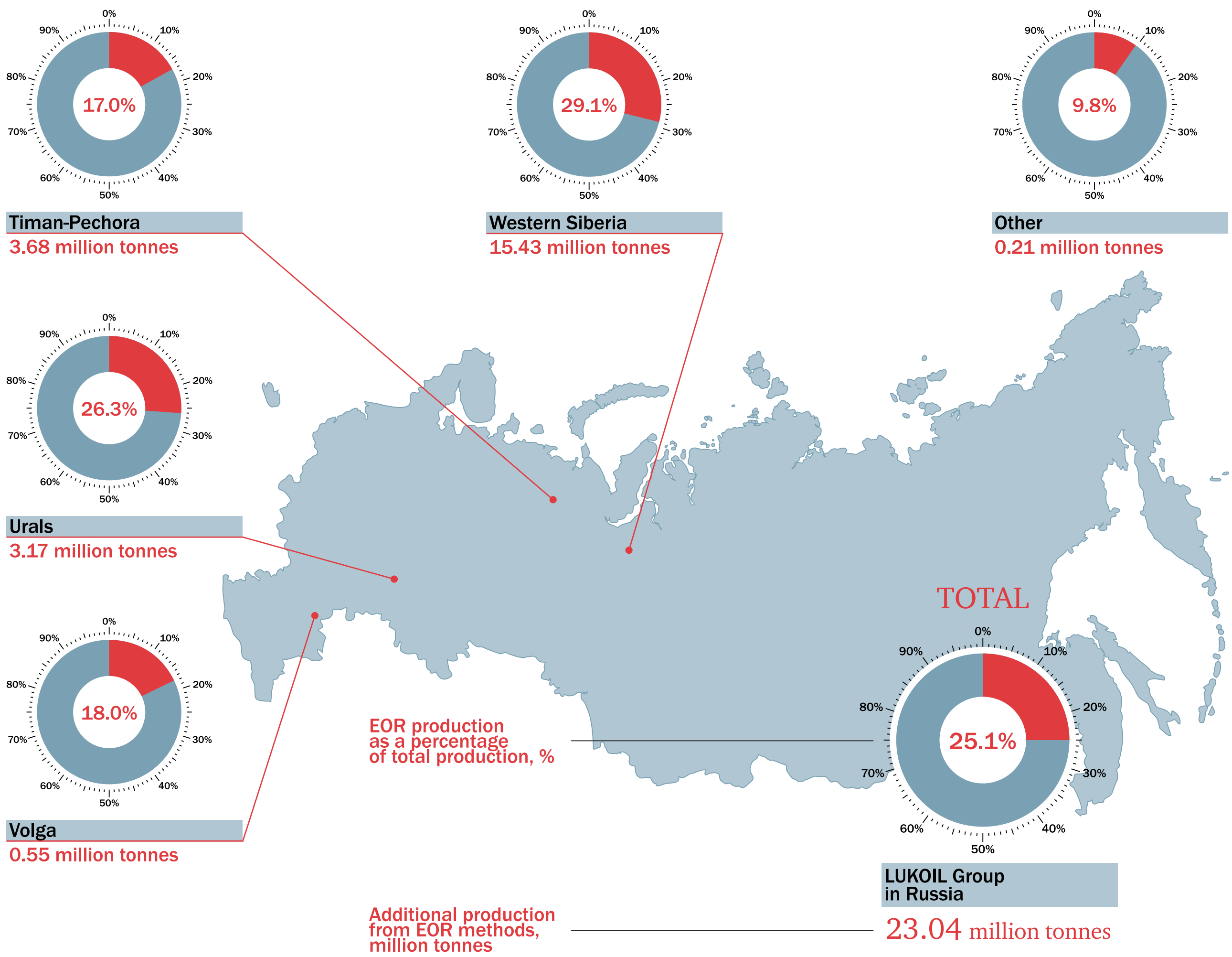


The Group carried out 5,098 EOR operations in 2009, which is 300 less than in 2008. However, additional production obtained as a result of EOR techniques (23 million tonnes, or 25% of total oil production by the Company in Russia) was slightly higher than in the previous year, thanks to higher efficiency in application of the techniques.

Most of the additional production volume (14 million tonnes, or 61%) was obtained using physical methods, primarily hydrofracturing.

The Group carried out 634 hydrofracturing operations at fields in 2009, achieving average growth in flow rate of 9.6 tonnes per day. The extent and the effectiveness of hydrofracturing operations in 2009 were comparable with analogous figures for 2008. Hydrofracturing was applied as a method of intensifying production mainly at fields that had been in development for a long period of time and had highly depleted reserves. LUKOIL succeeded in maintaining growth in oil flow from hydrofracturing operations at the 2008 level through improvement of hydrofracturing design, selection of wells using hydrodynamic models, and through tighter quality control over the materials and reagents, which were used by service companies.

EFFECT FROM EOR IN RUSSIA (2009)



Company specialists were awarded a diploma in 2009 by the Federal Service for Intellectual Property, Patents and Trademarks (Rospatent) in the nomination '100 best Russian inventions' for designing a method for locally directed hydrofracturing of formations at oil & gas fields. The method can be used for raising recovery at oil, gas and gas condensate fields, particularly at fields, which are in late stages of development and are characterized by high water cut in output, and by a large number of stagnant and blind zones, which are unproductive using traditional methods.

Use of other EOR methods (hydrodynamic, heat, chemical methods and oil production intensification) gave 9 million tonnes of production. The Company continued to make extensive use of chemical technologies in 2009. The number of chemical EOR interventions was almost unchanged (1,357 in 2009 compared with 1,324 in 2008) but additional output from such operations grew by 18% to 1.9 million tonnes.

Drilling of sidetracks at existing wells has also proved a highly-efficient form of EOR. The Company continued drilling of sidetracks in 2009, when 264 such operations were carried out (260 in 2008), giving average daily flow increase of 16.8 tonnes. The Company kept drilling of sidetracks at the same level in 2009 as in the previous year, despite overall reduction of the corporate investment program. Sidetracks are mainly used to extract residual reserves at inactive wells, which have been in production for a considerable period of time and are characterized by near exhaustion of active reserves and high levels of water cut. In the immediate future Company specialists will focus on increase of technical efficiency, primarily through improved accuracy in geological and reserve structure forecasts at areas where sidetracks are to be drilled.

Another way of raising efficiency of crude oil production is drilling of horizontal wells, which offers well productivity growth of 1.5–2 times. A total of 91 new horizontal wells were commissioned in 2009 with average daily flow rate of 78.2 tonnes (twice more than for ordinary wells).

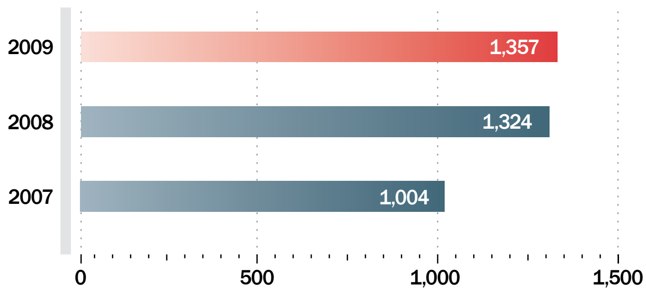
LUKOIL is rapidly developing and applying new technologies for production of high-viscosity oils. Experience of work with high-viscosity oil extraction in Russia is concentrated in the Komi Republic, where LUKOIL is developing the Yaregskoye and Usinskoye fields with initial geological reserves of heavy oil in excess of 1 billion tonnes under Russian classification. Thermal methods are used at both fields to increase oil recovery and annual production is about 2.2 million tonnes, representing about two thirds of total heavy oil production in Russia.

The Permocarbon deposit at the Usinskoye field is being developed using areal steam-heating and cyclic-steam stimulation. There has been successful work in recent years to improve efficiency of thermal applications at vertical wells (development of combined cyclic-steam stimulation (CSS) is being continued and trials have begun to increase oil flow through simultaneous injection of heat carriers and compositions for oil displacement). New thermal technologies are being introduced: steam-heat stimulation of rock formations in horizontal well systems; technology for perpendicular thermo-gravitational deposit draining; CCS technologies for horizontal wells, vertical wells with radial channels, and for an entire productive interval; and technologies for oil recovery by steam.

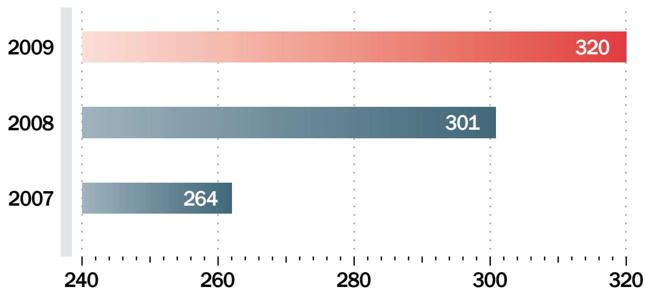
The Yaregskoye field is being developed using a thermo-shaft technology. Surface production is at the stage of industrial tests. Work on thermo-gravitational drainage of formations was carried out in 2009 at the test section of the Yaregskoye field in order to achieve efficient surface production of oil. Work in 2010 will make use of horizontal injection and production wells. Steam injection should begin in 2011.

Further introduction was made of assembled drive mechanisms using permanent-magnet motors for pump installations, developed and produced by

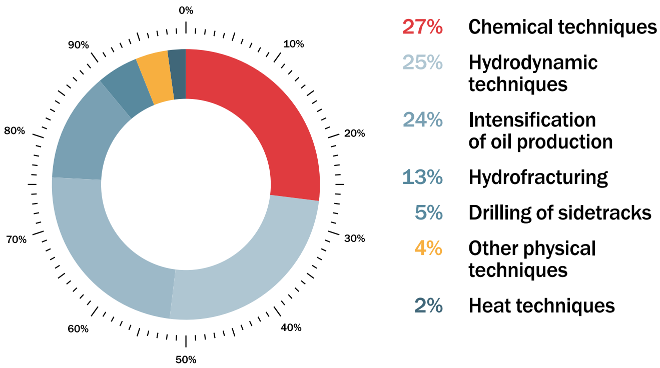
CHEMICAL EOR OPERATIONS, WELLS



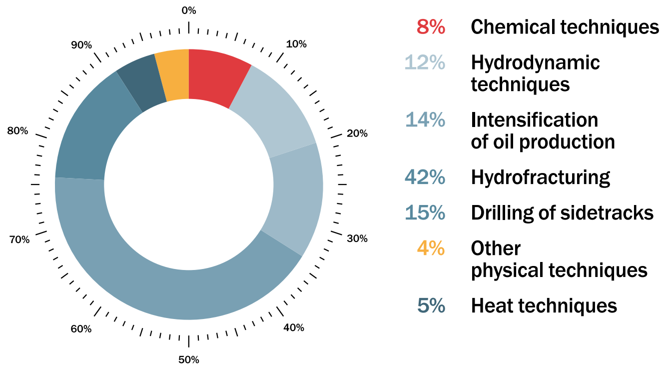
NUMBER OF GEOLOGICAL AND HYDRODYNAMIC MODELS OF FIELDS, FIELDS



EOR TECHNIQUES USED BY LUKOIL GROUP IN 2009



SHARES OF VARIOUS TECHNIQUES IN OVERALL EOR PRODUCTION IN 2009



LUKOIL Group. New types of cavity pumps are being used in Timan-Pechora for production of high-viscosity oil using permanent-magnet-motor drives. Metal carcases for oil production equipment with various new protective coatings, including coatings obtained using gas thermal deposition and nanotechnologies, will be field tested in 2010.

By the end of 2009 a total of 320 Group fields had been included in the multi-level system for monitoring of field development using geological and hydrodynamic models. The system developed rapidly in the reporting year, when about 20 fields were modelled. Use of geological and hydrodynamic models allows optimal technological solutions to be put into effect during field development, conforming to peculiarities of geological structure and composition of available reserves. Modelling enables improvement of oil recovery rates and reduction of expenditures on field development. Models are widely used by the Company when drilling over fields and applying EOR methods. The number of geological and hydrodynamic models of Group fields in Russia has been increasing as planned towards the target level of 85% of all fields, and such modelling will cover all fields in Western Siberia, Timan-Pechora and Kaliningrad Region. Although reserves in traditional production regions have been in development for long periods of time, the Company has been able to keep output levels steady and in some cases to increase output. This result reflects improved quality of geological and hydrodynamic models and increasing use of such models during production drilling, as well as continued work to improve well completion technologies, and widespread use of primary and secondary drilling into productive formations.

Refining Technologies

LUKOIL places much emphasis on development, modernization and construction of high-tech equipment that reduces costs in refining operations and enables production of new, high-quality product types.

Constant improvement of quality serves the interests of customers and protects the environment, and sale of products with a large share of value added generates additional profit for the Group.

LUKOIL carried out large-scale work in 2009 to modernize existing units and launch new units at Company refineries in order to increase yield of high-quality products. Achievements include the launch of an isomerization block with 120,000 tonnes annual capacity at the Ukhta Refinery, enabling changeover to production of motor gasolines, which meet the Euro-3 standard.

The Company's Volgograd Refinery brought inert gas and steam recuperation units into operation during 2009, and modernization of pipe stills was carried out at the Perm Refinery in the reporting year.

The Burgas Refinery in Bulgaria commissioned a sulphuric acid alkylation unit in 2009 including a block for sulphuric acid regeneration. The unit was designed using the latest technologies, enabling substantial increase in the alkylate octane number and improving quality of the Refinery's motor gasoline output, as well as lowering environmental pollution and reducing consumption of energy, materials and reagents for production purposes.

LUKOIL is also devoting much attention to development of up-to-date production technologies for oils, lubricants and additives. The focus is on developing and bringing to market new, high-quality products suited to modern machinery, as well as creating new technologies and blends. This work is being carried out by Company specialists in close association with scientific centers in Russia.

The Group carried out studies in 2009 for development of new-generation technologies for turbine lubricants. Company specialists also developed techniques for cleansing compressor lubricants of hydrogen sulphide.

The Company worked hard in the accounting year to optimize technological processes at production units and to improve the quality of its oils and lubricants. Steps were taken to improve yield of priority products, reduce energy consumption and raise base oil quality. The Company began production of 43 new lubricant types during the reporting year.

Information Technologies

We apply the latest information technologies to optimize business processes in various spheres.

LUKOIL continues to develop and install automated systems for management of production and technology processes, as well as IT systems to help run Group companies. The Company is also working to improve quality of its telecommunication systems, information security, IT hardware and office equipment.

IT technologies can be of great value for enhancing the efficiency of both management and operations. LUKOIL has expanded functionality of all software programs and applied them in an ever increasing number of Group organizations. Progressive creation and development of the Integrated Management System with SAP architecture had enabled installation of 15 modules at nearly 100 Group organizations by the end of 2009.

An integrated management system (IMS) using SAP R/3 architecture has been installed in order to optimize management decision-making systems and automate management accounting inside the Company. LUKOIL completed extension of the IMS system throughout the Company in the reporting year, and software programs created as part of the project were brought into industrial use.

Work continued in 2009 to prepare for implementation of the IMS Global Solution and Information Infrastructure Monitoring System. These innovations will allow Company employees to work in a unified IT space, supporting proper balance and efficiency of the LUKOIL management system.

Elements of the IMS are thus being developed and applied in ever-greater spheres of Company business.

Social Responsibility

The Company is guided in its work by the principles of sustainable development and tries to attain equilibrium between socio-economic and ecological development. LUKOIL shares the principles of the UN Global Compact and the Social Charter of Russian Business, which reflects in the Company's activities aimed at supporting sustainable economic development and increasing social responsibility.

Protecting the Environment

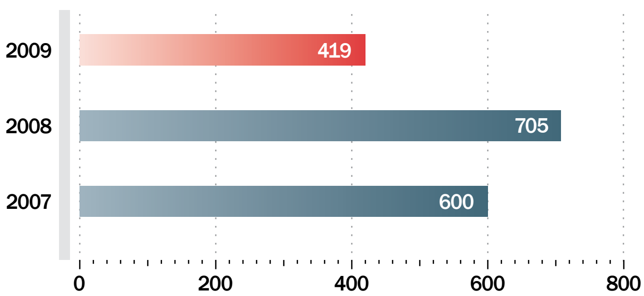
LUKOIL acknowledges its responsibility to society for protection of the environment and rational use of resources, and the Company is guided in its work by the highest standards of care for the environmental and industrial safety.

Group organizations work constantly to raise the level of environmental safety at production facilities, reduce environmental impacts and to optimize use of natural resources. Environmental safety is a key consideration at all stages of project implementation, from the investment idea to disposal of production assets and equipment at the end of the project.

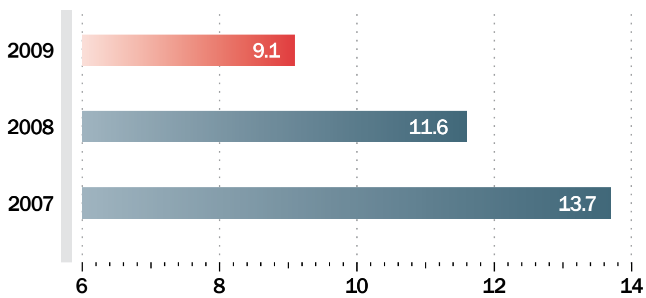
We ensure that Company activity is in full compliance with national legislation and international standards of environmental protection, and that quality of our products matches the latest environmental requirements.

In March 2009 the LUKOIL Management Committee approved a new version of the Group's Policy on Industrial Safety, Labour and Environment Protection in the 21st century. The document was originally designed in compliance with the ISO 14001 international standard and the OHSAS 18001 specification, and was enacted in 2002. The need for amendments to the Policy Document was dictated by development of new measures for energy efficiency and environmental action on the part of the Company (mostly on a voluntary basis). These measures include: application of a zero-discharge principle for development of offshore fields; production of environmentally friendly fuels, which match European standards; and implementation of requirements of the Kyoto Protocol for reduction of greenhouse gases. Updating of the Policy was also made necessary by changes to Russian legislation and legislation in countries where LUKOIL has operations, as well as requirements set out in new versions of the ISO 14001:2004 and OHSAS 18001:2007 standards.

ENVIRONMENTAL SPENDING, $ MILLION



WASTE WATER DISCHARGE, MILLION CUBIC METERS



The Environmental Safety Program for LUKOIL Group Organizations in 2009–2013 was approved in April 2009. The new Program includes 483 measures with overall cost of $1.8 billion.

Aims of the Program are to ensure that the Group's environmental impact indicators comply with current and future requirements of national and international legislation, including: further recycling of accumulated and newly generated waste; raising the level of utilization of associated gas to 95% by 2012; implementing the mechanisms of the Kyoto Protocol; and raising output of environmentally friendly fuel, which meets Euro-4 and Euro-5 standards.

Organizations in LUKOIL Group spent about $420 million in 2009 on measures to ensure environmental safety (spending in 2008 was over $700 million).

Most specific Company indices for impact on the environment in 2009 were unchanged or better than in 2008 and still remain considerably better than the average for the oil & gas sector in the Russian Federation. There were substantial reductions in volume of atmospheric emissions (by 8%), polluted water discharge (by more than 20%), and volumes of accumulated waste (by 4%). However, certain indicators worsened to some extent in 2009. In particular, there was an increase in the number

The Company operates in conditions of strict environmental control by government and society, and must also take account of ongoing reform of natural resource and conservation legislation in Russia and other countries. The following changes to Russian and international legislation on protection of the environment had impact on environmental activity by LUKOIL organizations in 2009:

- Federal Law № 261, dated November 23, 2009, defined government strategy for energy saving and energy efficiency improvement.
- Russian Government Resolution № 53, dated January 27, 2009, defined principles for state control over environmental protection (state environmental control), and Resolution № 285, dated March 31, 2009, stipulated new criteria for facilities, which are subject to state environmental control.
- Russian Government Resolution № 843, dated October 28, 2009, changed the procedure for approval and monitoring of execution of projects, carried out in compliance with Article 6 of the Kyoto Protocol and the UN Framework Convention on Climate Change, as well as receipt, transfer and acquisition of emission reduction units for greenhouse gases.
- The Russian Ministry of Natural Resources approved a new version of the Guide for Measurement of damage to natural water resources due to violation of laws on water use. LUKOIL specialists took part in discussion of various aspects of the draft.
- Rospotrebnadzor (the Russian Government body with responsibility for consumer rights) changed the procedure for deciding the extent of required buffer zones around facilities and plants that have impact on habitat and human health.

The Company took account in a timely fashion of changes to Russian environmental legislation, and LUKOIL was not subject to criticism or claims from control and supervisory bodies in the course of 2009.

Work to ensure industrial safety, labour and environmental protection is carried out in accordance with LUKOIL's Policy on Industrial Safety, Labour and Environmental Protection in the 21st Century.

In 2001 LUKOIL became the first Russian oil company to undergo certification for compliance with the requirements of the ISO 14001 International standard and the OHSAS 18001 specification. In 2008 and 2009 the Company successfully passed its first and second external audit by the supervisory authority of the Company's Industrial Safety, Labour and Environmental Protection Management (for compliance with standards).

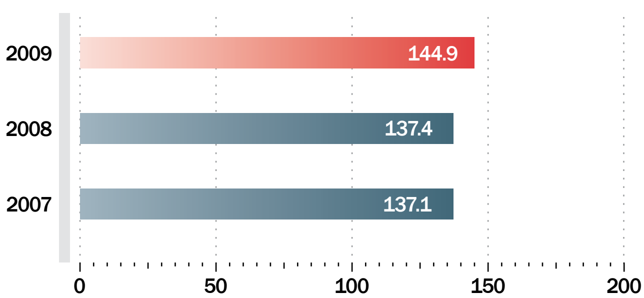
The **ISO 14001** standard attests that the Company has put an environmental policy in place, adheres to it in its operations, makes constant improvements to the environmental management system, and takes all necessary measures to prevent negative environmental impact.

The **OHSAS 18001** specification is intended to assist organizations in management of their project risks associated with protecting health and safety of employees and the general public. Key elements of the specification are identification, assessment and control over risk factors, as well as observance of legal requirements and consistent improvement of safety in the work place.

of incidents with environmental impact, explained by greater frequency of pipeline incidents due to corrosion and ageing of pipeline systems and also by the fact that liquids, transported through pipelines, became more corrosive due to increase of the water cut in extracted crude.

During 2009 the Company continued implementation of its Corporate concept (approved in 2007) for production planning by LUKOIL Group in compliance with provisions of the Kyoto Protocol, and of the Action Plan for implementation of the Concept in 2007–2008. The Company's Management Committee took stock of outcomes of Plan execution. Inventory of greenhouse gas emissions by LUKOIL Group was carried out (with independent review of the inventory), and a portfolio of carbon projects was prepared. Independent review of three pilot projects for reduction of greenhouse gases was carried out and a plan was approved for design of specialized carbon documentation for potential projects. Company

POLLUTED LAND, HECTARES

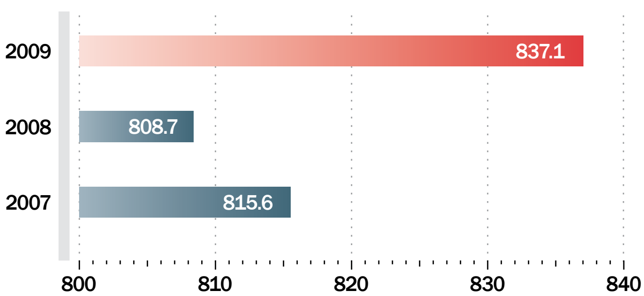


standards regulating the procedure for execution by LUKOIL of projects for reducing greenhouse gas emissions have been designed and are in the process of approval.

LUKOIL is aware of the environmental benefits, which can be obtained by expanding output of high-quality products. Accordingly, more than 20% of total capital expenditure in 2009 was in the Refining & Marketing segment. A significant part of these investments was spent on development of fuels with improved environmental characteristics: LUKOIL continued to produce gasoline and diesel fuels, which conform to the latest European standards. Gasoline sold under the EKTO ('Ecological Fuel') brand ensures a significant reduction in emissions of carcinogens, sulphur and nitrogen compounds, and other harmful substances. LUKOIL launched new brands of premium-class motor fuel in 2009: EKTO-Plus (octane number 95) and EKTO Sport (octane number 98). Multifunctional additive mixtures in the new fuels provide lower fuel consumption and reduction of carbon gas emissions.

Measures to protect the environment are also being applied in the transportation and marketing segment. The Company's new filling stations are equipped with systems for returning gasoline fumes from the reservoir to tankers during discharge of petroleum products, as well as systems for preventing spillages of petroleum products from reservoirs, and facilities for waste-water purification.

UTILIZATION AND BURIAL OF TOXIC WASTE, THOUSAND TONNES



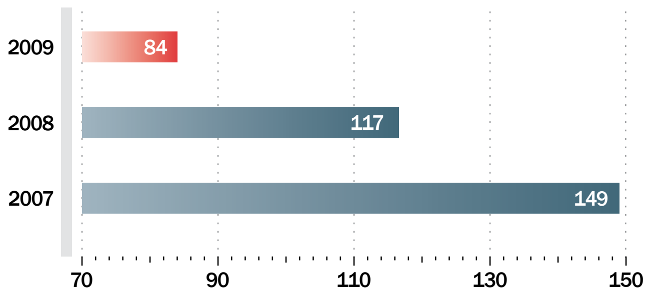
Industrial Safety and Labour Protection

Ensuring safe working conditions and caring for the health of employees is among the basic duties of the Company.

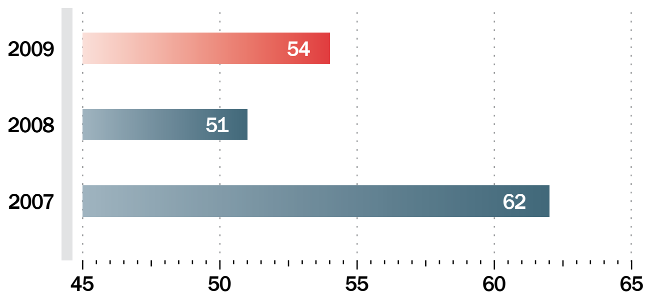
LUKOIL continued work in the reporting year on implementation of its Program for industrial and labour safety, improvement of working conditions, and prevention and resolution of emergency situations at organizations in LUKOIL Group for 2006–2010. Spending on measures as part of the Program was about $150 million. Work as part of the Program included construction of new and modernization of old equipment and facilities, installation of modern automated management and accident prevention systems at industrial sites, and certification of work places with respect to working conditions, as well as measures to ensure that employees are provided with protective clothing and equipment.

Internal health and safety inspections were carried out at 107 structural subdivisions of the Company and at 14 Group organizations in 2009. Scheduled checks were also carried out to ascertain knowledge of health and safety procedures among 76 employees in positions of responsibility and among members of standing workplace certification commissions at Group organizations.

LOST TIME INJURIES



NUMBER OF ACCIDENTS



Personnel and Social Programs

Each day thousands of employees worldwide help to advance the business of LUKOIL Group by their labour. Achievement by the Company of outstanding results is thanks to them. Our social policy is therefore designed to improve the labour efficiency and social protection of our employees. We also take issues of staff motivation very seriously and try to ensure that each employee takes a personal interest in achievement of the best possible results by the Company.

We are particularly pleased to have avoided reduction of the workforce and of social payments in 2009, despite the crisis environment, thanks to reduction of costs and business optimization in other areas. We continue to deliver on our social commitments, including those assumed voluntarily on the Company's own initiative as part of the LUKOIL Social Code. A sixth employer-trade union agreement, for 2009–2011, was agreed in September 2008 and came into force at the end of 2008. Social guarantees in the new agreement match those traditionally assumed by the Company and are in no way inferior to those in the previous agreement, despite being provided at a time of financial and economic crisis.

Work continued in the reporting year on restructuring of LUKOIL Group, including the Company's Corporate center, in order to increase efficiency of the Group's industrial and financial activities. Tasks included optimization of the organizational structure of existing subdivisions and standardization of organizational structure at subsidiaries. Withdrawal of non-core and low-margin assets from the Group was also continued. One result of these steps was reduction in personnel numbers in nearly all business segments. The only exception was substantial growth of average employee numbers in the Power Generation segment due to acquisition in 2008 of UGK TGK-8. Overall employee numbers at the Company declined by 5.9% in 2009.

Withdrawal from the Group of non-core subdivisions, optimization of costs and rouble depreciation enabled us to lower total payroll by more than 20%. However, wage levels remained attractive compared with the market average, despite reduction of total payroll, ensuring that highly qualified specialists continue to give preference to the Company as a place of employment. In order to ensure that payroll levels of our employees remain competitive, we constantly monitor payrolls in the respective market segment in regions where the Company has presence.

In addition to material incentives, LUKOIL uses moral encouragement as a way of developing personnel potential: 25 Company employees received national awards for professional excellence and for conscientious and successful work, while 673 were awarded sectoral marks of distinction for their work, and 779 employees and 39 groups of workers were presented with Company awards in 2009. The annual competition for the title of 'Best Employees and Organizations in LUKOIL Group' has become an established and popular tradition within the Company: the winners receive prizes and cash bonuses.

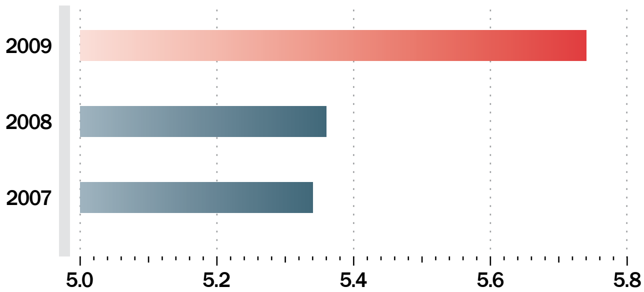
As well as material and moral incentives, LUKOIL is implementing a wide-ranging set of programs and measures, which constitute the Company's social package. Expenditure on this program in 2009 were $278 million. Main elements of the social package are:

- Health care and medical treatment for Company employees, including voluntary health insurance;
- Leisure and recreation provisions for employees and their families, organization of sport and fitness events;
- Help to employees in acquiring housing;
- Social support to women and families with children;
- Social support to young specialists;
- Non-state pension provision for employees, which has operated since 2004 on the principle of shared funding of non-state pensions by employee and employer. In 2009 contributions by employees in LUKOIL's Russian organizations alone were about to $13 million. The Company's total contributions under non-state pension provision programs in Russia and abroad for the reporting period were over $31 million.

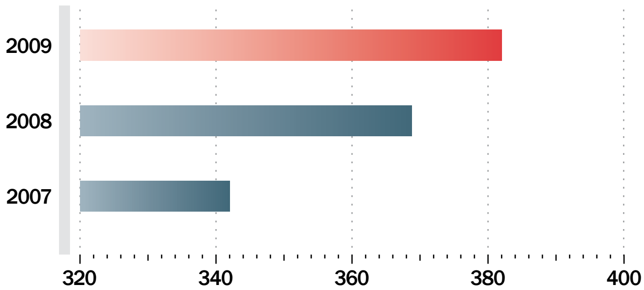
An efficient system of social protection helps to attract qualified specialists, reduces employee turnover, strengthens corporate morale and is the basis for successful industrial activity.

Training and professional study is a highly important part of HR management at LUKOIL, particularly for employees in positions of responsibility and reserve executives. Programs have therefore been designed and implemented at sector institutes and other

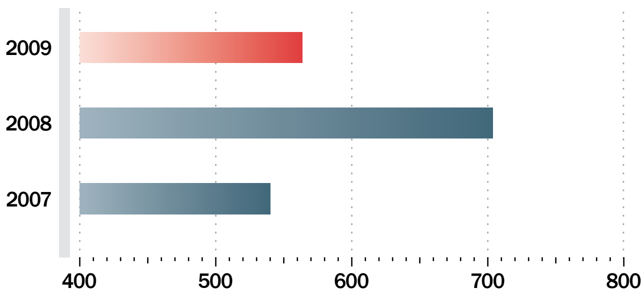
HYDROCARBON PRODUCTION PER EMPLOYEE, THOUSAND BOE



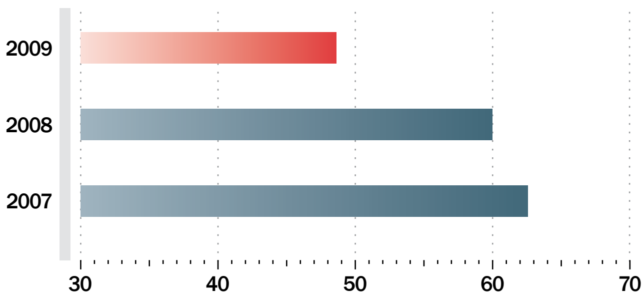
REFINERY THROUGHPUT AT OWN REFINERIES PER EMPLOYEE, TONNES



SALES PER EMPLOYEE, $ THOUSAND



NET INCOME PER EMPLOYEE, $ THOUSAND



Russian and foreign educational institutions for development of leadership potential and professional and management skills. LUKOIL uses the whole spectrum of modern training aids: workshops, seminars away from the work place, special training programs, work placements abroad, training sessions, courses to gain higher qualifications, professional training days, distance learning, MBA programs, etc. The Company is developing cooperation with leading institutions of higher education, including the Gubkin Russian State Oil & Gas University, the Russian Government Financial Academy, the Oil & Gas Business Institute, and the Higher School of Economics. The number of students who obtain work experience at LUKOIL production subdivisions through cooperation agreements between education institutions and the Company is increasing year by year. A total of 72 students obtained work experience at the parent Company and more than 1,000 students took temporary placements at Group organizations during 2009.

Work continued in 2009 on creation of a center for training of staff to work on offshore oil and gas facilities (in the city of Astrakhan). The Norwegian company Falck Nutec, a leader in training of personnel for work on offshore facilities, was selected as LUKOIL's main partner in the scheme.

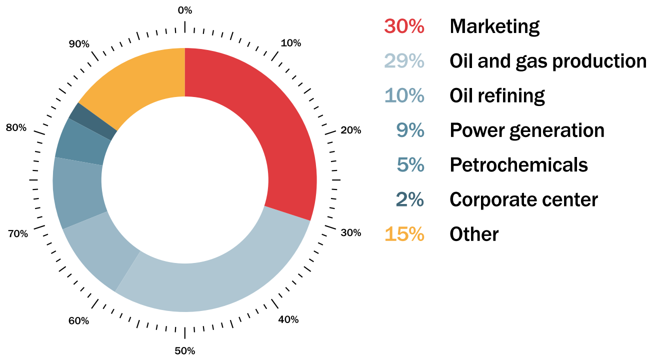
Improvement of the Company's Distance Learning System (DLS) is important for development of the professional training system for Company employees. Work continued in 2009 on creation of relevant study courses and over 60 new courses were designed. The System had almost 10,500 registered users by the end of the year, and a total of 3,500 Company employees carried out studies using the DLS in 2009. LUKOIL was acclaimed winner in the nomination, 'Best e-learning solution in the corporate sector' at a conference organized in Moscow in June 2009 with the support of the Ministry of Education and Science of the Russian Federation. The Company was awarded a diploma of the 6th eLearnExpo international exhibition.

The program for exchange of personnel was continued in 2009 as part of the strategic partnership between LUKOIL Group and ConocoPhillips. A group of 16 employees completed their period of work in the US company, and a meeting was organized in June 2009 with the President of LUKOIL, at which the exchange employees presented outcomes of their experience. A fifth group of 13 employees was seconded to ConocoPhillips as part of the exchange scheme in September 2009.

LUKOIL gives priority to work with young specialists as part of the Group's comprehensive target program for cooperation with young people and young specialists in the period from 2008 to 2017. Committees of young specialists operate at Company enterprises, and their functions include support to young specialists in adjustment to new working conditions, support for acquisition and improvement of skills by young employees, and work to encourage commitment to corporate values and corporate culture. As part of its efforts to encourage fulfilment of the creative and professional potential of young employees, the Company held a fourth competition in 2009 to find the Best Young Specialist of the Year: 103 competitors took part in 17 categories, and 25 young specialists won awards.

LUKOIL took first place in 2009 in a ranking of the country's 75 biggest companies by criteria of social responsibility, prepared by Trud newspaper, the Agency for Political and Economic Communications, and the Russian Anti-crisis Forum. For purposes of the ranking 'social responsibility' is understood to mean creation and preservation of jobs, tax discipline, delivering on commitments to employees, and helping to maintain social infrastructure in Russian regions. The ranking was based on results of a survey of 26 experts, including representatives of trade unions and business associations, economists, sociologists, political scientists and publicists.

EMPLOYEE STRUCTURE BY BUSINESS SEGMENTS (AS OF JANUARY 1, 2010)



Social Policy and Charity Activities

Social and charity programs are an integral part of the Company's corporate strategy and help to ensure constructive partnership with the state, business and society. Corporate programs have a targeted character and are based on professional experience and human potential in regions where the Company operates.

The Company continues to deliver on commitments, which it undertook voluntarily and on its own initiative under the LUKOIL Social Code. This Code is obligatory for all LUKOIL organizations and represents a set of principles and norms of socially responsible behaviour towards all parties whose interests are affected by Company business. Commitments under the Code are additional to commitments arising from collective negotiations with employees. These commitments apply to Company employees, non-working pensioners and shareholders, as well as to commercial partners, the state and society as a whole.

As well as traditional forms of charity, LUKOIL carries out strategic charity programs and social investment programs, which find synergies between approaches to social problems and the Company's strategic aims. Total spending by the Company in 2009 for charity and social partnership was about $150 million.

Support for Children's Homes and Schools

Helping children is a Company priority, and underlies all of the social programs, which we have built and which we pursue: charitable programs, sponsorship, sports development programs for children and young people, and cultural programs. Social investments in human capital are particularly valuable in the current environment. LUKOIL strives to achieve a balanced approach, providing support both to children, who by virtue of their family circumstances or health find themselves in a worse situation than their contemporaries, and to children with favourable family backgrounds by helping them to develop their natural abilities and talents.

LUKOIL provides support to children in more than 50 children's homes and boarding schools, ensuring that they remain in good health and obtain an education to acquire a profession and find their place in life. The Company provides financial support for various needs at the children's homes, schools and boarding schools, which it sponsors – from vacations for the children to major building repairs. Help was provided in 2009 for purchases and repairs of equipment and vehicles at children's homes in the cities and towns of Langepas, Kirov, St. Petersburg, Kstovo, Ishim and in Astrakan Region. Each year LUKOIL organizes summer vacations for children on the Black Sea as well as educational trips around Russia. LUKOIL has been providing grants since 2006 to students who continue their education in higher or vocational colleges after leaving children's homes. The Company maintained funding in 2009 for a study program, begun in 2008, at the Astrakhan College of Technology for 30 children from children's homes and underprivileged families, who will obtain jobs at Group organizations in the region after they graduate.

LUKOIL also provides support to educational establishments in regions outside the Russian Federation, where the Company has operations. In 2009 the Company carried out charity actions at four schools in Kashkadarinskaya Region in Uzbekistan, including repairs and disinfection of buildings, provision of equipment and textbooks, and organization of special events.

The Group gives special attention to children with special medical needs. One project, which LUKOIL has maintained over a number of years, is called 'An illustrated book for every blind child' and is part of the program, 'Illustrated Books for Blind Children'. Various publications were supplied to specialized children's institutions in Perm Territory during 2009 as part of this project.

Education Programs

LUKOIL attaches great importance to the training of young, qualified specialists, on whom the future success and prosperity of the Russian oil & gas industry depends.

LUKOIL provides financial support to a number of higher education institutions which train oil & gas specialists. These include specialized universities and institutions in Moscow, St. Petersburg, Perm, Ukhta, Tyumen, Ufa, Volgograd and Volgograd Region, Arkhangelsk and Astrakhan. Sector training institutes in the near-abroad countries, such as the State Oil Academy of Azerbaijan, also receive support from LUKOIL. As well as supporting oil & gas institutes, LUKOIL also helps the Russian Civil Service Academy, the State University–Higher School of Economics, the Financial Academy (attached to the Russian Federal Government), the Diplomatic Academy, the Mendeleyev Chemical Engineering University, the Moscow Physics and Technical Institute, the Khrulev Military Logistics and Transport Academy, and the Kstovo Oil Industry Technical College.

Since 2000 the Company has paid grants to particularly talented students at oil industry and technical institutes. Such corporate grants are currently paid to 180 students in various towns and cities across Russia. The Company also finances studies by foreign students at industry institutes in Russia. Financing continued in 2009 for Iraqi oil specialists at the Gubkin Russian State Oil & Gas University and Ufa Oil Industry University. A total of 77 Iraqi students completed masters and post-graduate studies in 2004–2009.

The Company also helps young teachers. About 70 talented young teachers at leading Russian oil & gas institutes receive grants from LUKOIL.

In addition, the Company helps institutions of higher education to improve their material and equipment provision, enabling them to keep the education process up to date. Significant amounts were allocated for this purpose in 2009 to the Tyumen State Oil & Gas University, Perm State Technical University, Ukhta State Technical University and the Suvorov and Nakhimov Institutes. New office equipment was supplied to the Bukhara Oil & Gas College in Uzbekistan, with which LUKOIL has been cooperating since 2007.

Support for Medical Institutions

Assistance to the health care system in regions where the Company has operations, as well as support to a number of major specialized medical research centers, is an integral part of the Company's social commitment. LUKOIL provides assistance to the Scientific Center for Obstetrics, Gynaecology and Perinatal Care, the Center for Haematology Research, and the Russian Cardiovascular Scientific and Production Complex. Regions of Company presence, where assistance was provided to healthcare in 2009 included Astrakhan, Penza, Saratov, Perm Territory, the Komi Republic, and Astrakhan and Nizhny Novgorod Regions.

Social Project Competition

Social project competitions have proved to be an efficient way of channelling financial assistance to help improve social and economic conditions in regions, where the Company has operations. Allocation of prize money is based on principles of transparency, competitiveness and public scrutiny.

The purpose of the competitions is to support projects and initiatives, which originate from and address urgent needs of specific regions.

The first LUKOIL competition for social and cultural projects was held by LUKOIL-PERM in 2002. The competitions were extended to Volgograd and Astrakhan Regions in 2004, to the Komi Republic and Western Siberia in 2005, to Nizhny Novgorod Region in 2007, and to Kaliningrad Region and the Republic of Kalmykia in 2008.

In 2009 the competitions were held in 10 of Russia's administrative regions. A total of 299 projects won grants in these regions, having been carefully selected from more than 1,200 applications. The competition budget has grown by nearly 20 times since it was first held in 2002 to a level of $1.3 million in 2009.

Social project competitions consist of several categories: 'Environment', 'Charity' 'Culture and Art', 'Physical Culture, Sport and Tourism', and 'My Region'. A special category was added in 2009 to mark Russia's National Year of Youth.

In the 8 years since they began, LUKOIL's social project competitions have proved their worth as a unique vehicle for nurturing social initiative. Experts have called attention to efficiency of the competition mechanism, which has a strong motivational element and is seen as a model for emulation in social programs of the Russian Federal Government. The mechanism enables project participants to develop their potential, set themselves goals and organize their progress towards achievement of those goals, helped by the informational and financial resources, which the Company puts at their disposal.

As well as its social project competitions, LUKOIL implements social partnership programs on a competitive basis, such as the ARAI program in Kazakhstan, which gives local people in Mangistau

Region the chance of obtaining grants up to $7,000 for development of small business, artisan skills and artistic projects. In the 3 years since the program began, it has enabled creation of 130 small businesses, as well as sports clubs, children's dance and art studios and leisure centers. In 2010 the program was replicated in rural regions of Aktobe Region (also in Kazakhstan).

Preserving Cultural and Spiritual Heritage

Support for cultural, historical and spiritual heritage is a traditional aspect of LUKOIL's charity activities. The Company does all it can to preserve and revive cultural, historical and religious values and traditions, whose loss would have inevitable negative impact on the lives of current and future generations, leading to spiritual degeneration and impoverishment of society as a whole.

LUKOIL provides support to a number of leading Russian museums. In 2009 the Company provided financial support to the Tretyakov Gallery for restoration of a panneau from the 'Far North' cycle by Konstantin Korovin, to the Russian Museum for holding of the international festival, 'Imperial Gardens of Russia', to the Pushkin Museum of Fine Art for the exhibition, 'Great Russian Victories in Medals and Engravings' (dedicated to the anniversary of the Battle of Poltava) and to the V.M. and A.M. Vasnetsov Regional Art Museum in Kirov for publication of an art album, 'The Collection of Western European Art at the Kirov Art Museum'. LUKOIL also helped to finance successful travelling exhibitions of the Moscow Kremlin Museums in Washington and the Tretyakov Gallery in Helsinki.

LUKOIL also has programs of assistance to theatres and performing art groups. The Company has worked for many years with the Tchaikovsky Symphony Orchestra, conducted by Vladimir Fedoseyev, and also supports the Perm State Theatre of Opera and Ballet, the Kaliningrad Regional Philharmonia and other live art groups in regions of Company operations.

LUKOIL makes significant contributions to restoration and preservation of religious traditions and spiritual heritage, and to revival and development of church and spiritual life in regions where the Company has operations. In 2009 LUKOIL continued its program of support for restoration work at the Optina Pustyn Monastery as well as providing significant funding for restoration of the Orthodox Cathedral of the Assumption in Budapest (Hungary).

Help for War Veterans and the Disabled

Oil workers and other veterans of the Great Patriotic War (World War II), as well as veterans of the labour front, have a special place in LUKOIL's social programs. Every year veterans of the Great Patriotic War who live in regions where the Company has operations receive special payments and gifts from the Company to coincide with Victory Day. The Company also provides assistance to families of members of law enforcement agencies, who have perished in armed conflicts.

LUKOIL provides financial assistance to people with disabilities, including support to help them to earn a living independently and thus to feel a part of society.

Support for Northern Peoples

Operations by Group companies in Siberia and the Far North of Russia can have significant impact on the living conditions of small indigenous peoples, creating various social and economic problems. LUKOIL respects the traditions and customs of these peoples and understands the importance of preserving their age-old way of life. The Company is therefore implementing special programs to help such indigenous groups, and LUKOIL's policy is to shift gradually from charity provision to economic partnership.

In the Komi Republic, the Nenets Autonomous District and Khanty-Mansiysk Autonomous District-Yugra LUKOIL has made agreements with local administrations, with heads of lands that are traditionally inhabited and exploited by indigenous groups, and with social organizations. The agreements guarantee money compensation to indigenous families for use of their traditional lands, provision of tools and equipment for reindeer herding and household purposes, construction of housing and communications, and health care. The Company organizes traditional celebrations and sports events, as well as holding competitions which offer financing for projects to support spiritual, historical and cultural values of indigenous peoples. LUKOIL understands that material support alone is not enough, and that northern peoples also need help to improve education levels and find employment. The Company therefore works hard to provide various special training to local people and to find them subsequent employment in LUKOIL organizations.

Sport

Company priorities in the sphere of fitness and sport include promotion of health and fitness pursuits among employees and their families, development of mass sport, support for professional sports teams in Russia, for national federations and for the national Olympic Movement, as well as assistance in development of children's sport in Russia.

LUKOIL's international amateur sports competitions ('Spartakiada') are among the biggest events for popularization of fitness and mass sport among Company employees. The first such competition was held in 2001 in Astrakhan, the second in Perm in 2003, and the third in Kaliningrad in June 2005. The fourth winter event, celebrating the Company's 15th anniversary, was held in Kogalym in 2007.

The Company gives much support to youth sport, both amateur and professional. In 2009 an all-Russian sports event 'Believe in yourself' was held with LUKOIL support in regions of Company activity, dedicated to Russian Year of Youth and intended to promote healthy lifestyle and orientation to sport and physical exercise among students and school children.

LUKOIL also supports leading Russian sports teams, including the Spartak water polo team in Volgograd, the Zarya Kaspiya handball team in Astrakhan, Spartak football team in Moscow, the Torpedo hockey team (Nizhny Novgorod), the Interior Ministry hockey club, and the Dinamo-Yantar volleyball team (Kaliningrad).

For many years the Company has been general sponsor of the national ski-racing team and partner of the Russian Ski-Racing Federation, in which LUKOIL President, Vagit Alekperov, heads the Board of Trustees. LUKOIL sponsorship helps in training of the national team as well as development of amateur

ski sport in Russia. LUKOIL is also official sponsor of the Russian Martial Arts Union and a partner of the Children's Football League, through which about 250 teams from all over Russia compete annually in regional and international championships. The Company also finances the Student Basketball Foundation, which holds a student championship for more than 100 teams from higher education institutions across the country.

LUKOIL has been an official partner of the Russian Olympic Committee for many years. Since 2005 the Company has supported the Russian Olympic Support Foundation, which was set up for the country's Olympic sport teams, young Russian sportsmen and veterans of sport.

In addition to its support for sports teams, LUKOIL also views sport as a way of testing the Company's own products to the limits. The victories and successes of LUKOIL Racing Team (Moscow) and Sura Motorcross Team (Penza) are testaments to the efficiency of LUKOIL fuels and motor oils.

The LUKOIL Museum

LUKOIL's corporate museum was created in 2005 and now stands at the head of a network of more than 20 museums in Group organizations in various regions of Russia, and also in Ukraine, Bulgaria and Romania.

More than 10 travelling exhibitions were held in 2009 including: 'His Homeland's Son' (dedicated to the 80th birthday of Valery Grayfer), 'LUKOIL as Stock Market Leader', 'Company Youth Policy', 'LUKOIL's Caspian Project', '80 years of the Oil Industry in Perm', '60 Years of Volgograd Oil', 'The Nobel Dynasty for Russia' (dedicated to the 130th anniversary of the Nobel Brothers' oil business), 'V.G. Shukhov, Russia's First Engineer', and 'D.I. Mendeleyev and the Russian Oil Industry'. The exhibitions were shown in the Company's central office, the Central State Museum of Modern Russian History, the Russian Academy of Sciences, the Gubkin Russian State Oil & Gas University, and Tyumen Technopark.

An offering by LUKOIL was also featured as part of the exhibition, 'We Are Russia's Future', held in the Central State Museum of Modern Russian History and dedicated to Russian Year of Youth.

Corporate Governance and Securities

LUKOIL's system of corporate governance is an effective tool for protecting the rights and observing the interests of Company shareholders. Efficient corporate governance lowers the weighted average cost of capital and reduces investment risks, making investments in LUKOIL more attractive and, as a consequence, raising shareholder value of the Company.

LUKOIL more attractive and, as a consequence, raising shareholder value of the Company. LUKOIL's corporate governance gives a special place to protecting the rights of minority shareholders. Amendments to the LUKOIL Charter, made in 2005, expanded the authority of the Board of Directors and established a principle of unanimous agreement on key matters, such as: inclusion in the AGM agenda of issues related to any increase of LUKOIL's charter capital above 10%; issue of securities which can be converted into more than 10% of the Company's outstanding shares within 12 months from the date of issue; and approval of a transaction or a number of interrelated transactions amounting to more than 7.5% of consolidated non-core asset value.

Corporate Governance

Much has been done to make LUKOIL's management processes comply with best international practice and to enable further improvement of their efficiency and transparency. A modern system of corporate governance has been put in place: 6 out of 11 members of the Board of Directors are independent, and BoD committees (for Strategy and Investment, Audit, and HR and Compensation) have been operating successfully for a number of years.

In 2009 the Board of Directors held 9 face-to-face meetings and 21 meetings in absentia. Board members dealt with the following matters in their official capacity:

- defining overall priorities for Company business; strategic, medium-term and short-term planning; reviewing business results;
- in-depth study and design of specific steps for development of LUKOIL's various business segments;
- formation of the LUKOIL Management Committee; improvements to corporate governance in the Company (LUKOIL's Policy for Work with Shareholders was approved); preparation for holding of the Annual General Meeting of Shareholders;
- approval of transactions with interest, of debt securities issues, etc.

Company management maintains a high level of openness towards the investment community and the media, as confirmed by regular meetings of Company officials with investors and shareholders, organization of trips for representatives of the investment community to Company production regions, and conference calls and webcasts to accompany publication of financial results and for presentation of other important Company events.

Professionalism of LUKOIL management has been repeatedly attested by experts over the years: 6 senior managers of LUKOIL were placed near the top of the annual ranking by the Russian Association of Managers and Kommersant Publishing House, '1,000 Most Professional Russian Managers'.

Board of Directors of LUKOIL

Valery Grayfer

Chairman of the LUKOIL Board of Directors

CEO of RITEK (until 12 January 2010), Chairman of the RITEK Board of Directors (from 12 January 2010)

Born 1929

Graduated in 1952 from Gubkin Moscow Oil Institute. Doctoral Candidate in Technical Sciences. Awarded six orders, four medals, and a diploma of the Supreme Soviet of the Tatar ASSR. Awarded a diploma of the Russian Federation President in 2009. Deputy to the USSR Oil Industry Minister from 1985, Head of the Tyumen Main Office for the Oil & Gas Industry. From 1992 to 2009, CEO of RITEK, from 2010, Chairman of the Board of Directors of RITEK. Chairman of the Board of Directors of LUKOIL from 2000. Professor of Gubkin Russian State Oil & Gas University, Lenin Prize Winner and Russian Government Prize Winner.

Elected to the LUKOIL Board of Directors since 1996.

Vagit Alekperov

President of LUKOIL

Member of the LUKOIL Board of Directors

Chairman of the LUKOIL Management Committee

Born 1950

Graduated in 1974 from the Azizbekov Institute of Oil and Chemistry in Azerbaijan. Doctor of Economics, current Member of the Russian Academy of Natural Sciences. Awarded four orders and eight medals. Winner of two Russian Government Prizes. Worked from 1968 in the oil industry in Azerbaijan and Western Siberia. From 1987 to 1990 CEO of Kogalymneftegaz (oil production company), a division of Glavtyumenneftegaz within the Ministry of the Oil & Gas Industry of the USSR. From 1990 to 1991, Deputy, then First Deputy to the USSR Oil & Gas Industry Minister. From 1992 to 1993, President of Langepasuraykogalymneft (oil production group). Chairman of the Board of Directors of LUKOIL from 1993 to 2000. President of LUKOIL from 1993.

Elected to the LUKOIL Board of Directors since 1993.

Viktor Blajeev

Independent Member of the LUKOIL Board of Directors*

President of Kutafin Moscow State Academy of Law

Member of the LUKOIL BoD Audit Committee

Born 1961

Graduated from the evening department of the All-Union Extra-Mural Law Institute (AELI) in 1987; completed a post-graduate program at AELI/Moscow Law Institute in the department of civil litigation in 1990. Since 1994 he has combined work as a lecturer with various administrative posts at the Moscow State Academy of Law. Dean of the full-time day department of Moscow State Academy of Law in 1999–2001. Vice-Rector of Moscow State Academy of Law in charge of academic agenda in 2001–2002. First Vice-Rector of Moscow State Academy of Law in charge of academic agenda in 2002–2007. Rector of Kutafin Moscow State Academy of Law since 2007.

Elected to the LUKOIL Board of Directors since 2009.

Igor Ivanov

Independent Member of the LUKOIL Board of Directors*

Professor of Moscow State Institute of International Relations (University)

Chairman of the LUKOIL BoD Strategy and Investment Committee

Born 1945

Graduated from the Maurice Thorez Moscow State Institute of Foreign Languages in 1969. Doctor of History. Professor. Awarded Russian and foreign orders and medals. First Deputy Minister of Foreign Affairs of the Russian Federation in 1993–1998. Minister of Foreign Affairs of the Russian Federation in 1998–2004. Secretary of the Security Council of the Russian Federation in 2004–2007.

Elected to the LUKOIL Board of Directors since 2009.

Herman Gref

Independent Member of the LUKOIL Board of Directors*

President, Chairman of the Executive Board of SBERBANK (Savings Bank of the Russian Federation)

Chairman of the LUKOIL BoD Audit Committee

Born 1964

Graduated from Omsk State University in 1990, completed a post-graduate program at St. Petersburg State University in 1993. First Deputy Minister of Property Relations of the Russian Federation in 1998–2000. Minister of Economic Development and Trade of the Russian Federation in 2000–2007. President, Chairman of the Executive Board of SBERBANK (Savings Bank of the Russian Federation) since 2007.

Elected to the LUKOIL Board of Directors since 2009.

Ravil Maganov

Member of the LUKOIL Board of Directors

Member of the LUKOIL Management Committee

First Executive Vice-President of LUKOIL (Exploration & Production)

Member of the LUKOIL BoD Strategy and Investment Committee

Born 1954

Graduated in 1977 from Moscow Gubkin Petrochemical & Gas Institute. Honored Employee of the Oil and Gas Industry of the Russian Federation. Awarded three orders and three medals. Winner of three Russian Government Prizes in science and technology. Chief Engineer, Deputy CEO, CEO of Langepasneftegaz (oil production company) from 1988 to 1993. Vice-President of LUKOIL from 1993 to 1994. First Vice-President of LUKOIL from 1994 to 2006. First Executive Vice-President of LUKOIL from 2006.

Elected to the LUKOIL Board of Directors since 1993.

* According to provisions of the Code of Corporate Conduct whose application is recommended by an instruction of the Federal Financial Markets Service, dated April 4, 2002.

Richard Matzke

Member of the LUKOIL Board of Directors

Member of the LUKOIL BoD Strategy and Investment Committee

Born 1937

Graduated from Iowa State University (1959), Pennsylvania State University (1961), and St. Mary's College in California (1977). Masters in Geology, MBA. President of Chevron Overseas Petroleum and Member of the Board of Directors of Chevron Corporation from 1989 to 1999. Vice-Chairman of Chevron and Chevron-Texaco Corporation from 2000 until 2002. Awarded a non-Government (sectoral) medal 'For Development of the Russian Oil & Gas Industry' in 2006; winner of the national prize 'Director of the Year, 2006' (Russia) in the 'Independent Directors' nomination, organized by the Association of Independent Directors and PricewaterhouseCoopers.

Elected to the LUKOIL Board of Directors since 2002.

Sergei Mikhailov

Independent Member of the LUKOIL Board of Directors*

CEO of the company Management-Consulting

Member of the LUKOIL BoD Audit Committee

Member of the LUKOIL BoD HR and Compensation Committee

Born in 1957

Graduated in 1979 from Dzerzhinsky Military Academy, in 1981 from Moscow Aviation Institute (Further Qualification Faculty), and in 1998 from the Plekhanov Russian Economics Academy. Doctoral Candidate in Technical Sciences, Doctor of Economics, Professor. Awarded four medals. 1974–1992, service in armed forces. Head of Section, Deputy Chairman of the Russian Federal Property Fund from 1992 to 1996. Head of Restructuring and Investment Department of Ministry of Industry in 1996–1997. CEO of Management-Center (management company) from 1997 to 2003. CEO of the company Management-Consulting from 2001 to the present. From 2004, Chairman of the Board of Directors of Russian Mediagroup and of Capital Unit Investment Funds (Management Company), member of the Board of Directors of Spartak-Moscow Football Club and of Petrocommerce Commercial Bank. From 2005, member of the Board of Directors of IFD Capital and of Izvestiya Newspaper Editorial. From 2008 to 2009, Chairman of the Board of Directors of Capital Investment Group, from 2009 – Member of the Board of Directors of Capital Management Company.

Elected to the LUKOIL Board of Directors since 2003.

* According to provisions of the Code of Corporate Conduct whose application is recommended by an instruction of the Federal Financial Markets Service, dated April 4, 2002.

Alexander Shokhin

Independent Member of the LUKOIL Board of Directors*

President of the Russian Union of Industrialists and Entrepreneurs

President of the State University – Higher School of Economics

Chairman of the LUKOIL BoD HR and Compensation Committee

Born 1951

Graduated from Economics Faculty of Lomonosov Moscow State University in 1974, Doctor of Economics, Professor. Awarded an order for 'Services to Russia' (4th grade) and a medal of Russian Security Council for 'Services to national security'. Began working career in 1969. Deputy Chairman of the Government of the Russian Federation, Minister of the Economy, Minister for Labour and Employment (1991–1994). Deputy of the State Duma of the Russian Federation (1994–2002). First Deputy Chairman of the State Duma of the Russian Federation (1996–1997). Chairman of Duma Fraction 'Our Home is Russia' (1997–1998). Deputy Chairman of the Russian Government in 1998. Chairman of the Supervisory Council of Renaissance Capital Investment Group (2002–2005). In 2005–2009 member of the Public Chamber of the Russian Federation. President of the Russian Union of Industrialists and Entrepreneurs (from 2005). Member of the Presidential Council for Priority National Projects and Demographic Policy, member of the Competitiveness and Enterprise Council of the Prime Minister of Russia, member of the Government Commissions for administrative reform, legislature, investment projects of national importance.

Elected to the LUKOIL Board of Directors since 2005.

* According to provisions of the Code of Corporate Conduct whose application is recommended by an instruction of the Federal Financial Markets Service, dated April 4, 2002.

Nikolai Tsvetkov

Member of the LUKOIL Board of Directors

Chairman of the BoD of URALIB Financial Corporation

Member of the LUKOIL BoD HR and Compensation Committee

Born 1960

Graduated in 1980 from Dzerzhinsky Military Aviation Engineering School in Tambov, in 1988 from the Zhukovsky Air Force Engineer Academy and in 1996 from the Plekhanov Russian Economics Academy. Doctoral Candidate in Economics. President of NIKoil Oil Investment Company, Vice-President of LUKOIL – Director of Securities Department from 1994 to 1997. CEO of NIKoil investment bank from 1998 to 2003. Chairman of AVTOBANK–NIKOIL bank from 2003 to 2005. Chairman of the Management Committee of BANK URALSIB in 2005–2007. Chairman of BANK URALSIB Supervisory Council and Chairman of the Board of Directors of URALSIB Financial Corporation from 2007.

Elected to the LUKOIL Board of Directors since 1995 (excluding 1996 and 1997).

Donald Wallette Jr

Independent Member of the LUKOIL Board of Directors*

Russia/Caspian Region President of ConocoPhillips

Member of the LUKOIL BoD Strategy and Investment Committee

Born 1958

Graduated from the University of Southern California with a Degree in Chemical Engineering in 1981. ConocoPhillips Manager for Production Support and Optimization from 2002 to 2005. Vice-President for the Shtokman Project in the Russia/Caspian Region Division of ConocoPhillips in 2005 to 2006. Russia/Caspian Region President of ConocoPhillips from December 2006.

Elected to the LUKOIL Board of Directors since 2007.

Management Committee of LUKOIL

Vagit Alekperov

President of LUKOIL

Member of the LUKOIL Board of Directors

Chairman of the LUKOIL Management Committee

Born 1950

Graduated in 1974 from the Azizbekov Institute of Oil and Chemistry in Azerbaijan. Doctor of Economics, current Member of the Russian Academy of Natural Sciences. Awarded four orders and eight medals. Winner of two Russian Government Prizes. Worked from 1968 in the oil industry in Azerbaijan and Western Siberia. From 1987 to 1990 CEO of Kogalymneftegaz (oil production company), a division of Glavtyumenneftegaz within the Ministry of the Oil & Gas Industry of the USSR. From 1990 to 1991, Deputy, then First Deputy to the USSR Oil & Gas Industry Minister. From 1992 to 1993, President of Langepasuraykogalymneft (oil production group). Chairman of the Board of Directors of LUKOIL from 1993 to 2000. President of LUKOIL from 1993.

Elected to the LUKOIL Board of Directors since 1993.

Anatoly Barkov

Member of the LUKOIL Management Committee

Vice-President, Head of the Main Division of General Affairs, Corporate Security and Communications of LUKOIL

Born 1948

Graduated in 1992 from Ufa Oil Institute. Doctoral Candidate of Economics. Honored Employee of the Oil & Gas Industry of the Russian Federation. Awarded an order and 10 medals. Head of Operations, Head of Oil & Gas Production, Senior Engineer at Kogalymneftegaz from 1987 to 1992. Executive Director, then Director of the Department of Foreign Projects at Langepasuraykogalymneft in 1992–1993. Vice-President, Head of the Main Division of General Affairs, Corporate Security and Communications of LUKOIL from 1993.

Jevan Cheloyants

Member of the LUKOIL Management Committee

Vice-President, Head of the Main Technical Division of LUKOIL

Born 1959

Graduated in 1981 from Grozny Oil Institute. Honored Employee of the Oil & Gas Industry. Awarded a medal of the order for ‘Services to Russia’ (2nd grade) and 4 medals. Winner of a Russian Government Prize. Section Head, then Deputy CEO for Foreign Economic Affairs of Langepasneftegaz from 1990 to 1993. Vice-President of LUKoil for Foreign Market Trading from 1993 to 1995. Vice-President of LUKOIL and Head of the Main Department for Maritime and Foreign Projects from 1995 to 2001. Vice-President, Head of the Main Division of Oil & Gas Production from 2001 to 2007. Vice-President and Head of the Main Technical Division of LUKOIL since 2007.

Leonid Fedun

Member of the LUKOIL Management Committee

Vice-President, Head of Main Division of Strategic Development and Investment Analysis of LUKOIL

Born 1956

Graduated in 1977 from Rostov Nedelin Higher Military School. Doctoral Candidate in Philosophy. Awarded an order and 7 medals. CEO of LUKoil Consulting from 1993 to 1994. Vice-President and Head of Main Division of Strategic Development and Investment Analysis of LUKOIL from 1994.

Evgueny Khavkin

Member of the LUKOIL Management Committee

Secretary of the Board of Directors, Head of the BoD Office of LUKOIL

Born 1964

Graduated in 2003 from Moscow Institute of Economy, Management and Law. Awarded 2 medals. Worked in oil companies in Western Siberia from 1988. Deputy Head, then First Deputy Head of the BoD Office of LUKOIL from 1997 to 2003. BoD Secretary, Head of the BoD Office of LUKOIL from 2003.

Sergey Kukura

Member of the LUKOIL Management Committee

First Vice-President of LUKOIL (Economics and Finance)

Born 1953

Graduated in 1979 from the Ivano-Frankovsk Institute of Oil & Gas. Doctor of Economics. Honored Economist of the Russian Federation. Awarded an order and five medals. Vice-President of Langepasuraykogalymneft from 1992 to 1993. First Vice-President of LUKOIL from 1993.

Lyubov Khoba

Member of the LUKOIL Management Committee

Chief Accountant of LUKOIL (until 25.08.2009 inclusive)

Born 1957

Graduated in 1992 from Sverdlovsk Institute of National Economy. Doctoral Candidate of Economics. Honored Economist of the Russian Federation. Awarded 2 medals and an order. Chief Accountant at Kogalymneftegaz from 1991 to 1993. Chief Accountant at LUKOIL from 1993 to 2000. Vice-President of LUKOIL, Head of Financial Accounting from 2000 to 2003. Chief Accountant and Vice-President of LUKOIL from 2003 to 2004. Chief Accountant of LUKOIL from 2004 until 25.08.2009 inclusive.

Ravil Maganov

Member of the LUKOIL Board of Directors

Member of the LUKOIL Management Committee

First Executive Vice-President of LUKOIL (Exploration & Production)

Member of the LUKOIL BoD Strategy and Investment Committee

Born 1954

Graduated in 1977 from Moscow Gubkin Petrochemical & Gas Institute. Honored Employee of the Oil and Gas Industry of the Russian Federation. Awarded three orders and three medals. Winner of three Russian Government Prizes in science and technology. Chief Engineer, Deputy CEO, CEO of Langepasneftegaz (oil production company) from 1988 to 1993. Vice-President of LUKOIL from 1993 to 1994. First Vice-President of LUKOIL from 1994 to 2006. First Executive Vice-President of LUKOIL from 2006.

Elected to the LUKOIL Board of Directors since 1993.

Ivan Masliaev

Member of the LUKOIL Management Committee

Head of the Main Division of Legal Support of LUKOIL

Born 1958

Graduated in 1980 from Lomonosov Moscow State University. Doctoral Candidate in Law. Honored Lawyer of the Russian Federation. Awarded three medals. Head of the Legal Section of Langepasuraykogalymneft from 1992 to 1993. Head of the LUKOIL Legal Department from 1994 to 1999. Head of the Main Division of Legal Support at LUKOIL since 2000.

Anatoly Moskalenko

Member of the LUKOIL Management Committee

Head of the Main Division of Human Resources of LUKOIL

Born 1959

Graduated in 1980 from Moscow Higher School of the Armed Forces, from the Military-Diplomatic Academy in 1987, and from the Russian Presidential Civil Service Academy in 2005. Doctoral Candidate in Economics. Awarded five orders and 20 medals. Served in the Armed Forces from 1976 to 2001. Head of Human Resources Department of LUKOIL from 2001 to 2003. Head of the Main Division of Human Resources at LUKOIL from 2003.

Alexander Matytsyn

Member of the LUKOIL Management Committee

Vice-President, Head of the Main Division of Treasury and Corporate Finance of LUKOIL

Born 1961

Graduated in 1984 from Lomonosov Moscow State University. Doctoral Candidate in Economics. MBA from Bristol University (1997). Awarded a medal of the order for 'Services to Russia' (2nd grade). Director and CEO of international auditing firm KPMG from 1994 to 1997. Vice-President, Head of the Main Division of Treasury and Corporate Finance of LUKOIL from 1997.

Vladimir Mulyak

Member of the LUKOIL Management Committee

Vice-President, Head of the Main Division of Oil & Gas Production of LUKOIL

Born 1955

Graduated from Moscow Gubkin Petrochemical & Gas Institute in 1977. Doctoral Candidate in Geological and Mineralogical Sciences. Awarded a medal of the order for 'Services to Russia' (2^{nd} grade). Chief Engineer, Head of Lasyeganneft Oil & Gas production unit of LUKoil-Langepasneftegaz (1990–1996). First Deputy CEO for Production, CEO of production company Belorusneft (1996–2001). First Vice-President for Production of KomiTEK in 2001. Chief Engineer, First Deputy CEO, CEO of LUKOIL-Komi (2002–2007). Vice-President, Head of the Main Division of Oil & Gas Production of LUKOIL from 2007.

Vladimir Nekrasov

Member of the LUKOIL Management Committee

First Vice-President of LUKOIL (Refining & Marketing)

Born 1957

Graduated in 1978 from Tyumen Industrial Institute. Doctoral Candidate in Technical Science, Member of the Academy of Mining Sciences. Awarded an order and three medals. Winner of a Russian Government Prize. Chief Engineer, CEO of Kogalymneftegaz (part of LUKOIL-Western Siberia) from 1992 to 1999. Vice-President of LUKOIL and CEO of LUKOIL-Western Siberia from 1999 to 2005. First Vice-President of LUKOIL since 2005.

Valery Subbotin

Member of the LUKOIL Management Committee

Vice-President, Head of the Main Division of Supplies and Sales of LUKOIL

Born 1974

Graduated from Tyumen State University in 1996. From 1998 to 2003, worked at LUKOIL-Prague, LUKOIL-Bulgaria, and the Moscow Representative Office of the company LITASCO. From 2003 to 2005, First Deputy Head of the Office of the Board of Directors of LUKOIL. From 2005 to 2007, First Deputy Head of the Main Division of Supplies and Sales of LUKOIL. From 2007, Vice-President, Head of the Main Division of Supplies and Sales of LUKOIL.

Vagit Sharifov

Member of the LUKOIL Management Committee

Vice-President, Head of the Main Division of Control and Internal Audit of LUKOIL

Born 1945

Graduated in 1968 from Azizbekov Institute of Oil and Chemistry in Azerbaijan. Doctor of Economics. Honored Employee of the Oil and Gas Industry of the Russian Federation. Awarded 2 orders and 6 medals. Senior Engineer, CEO of Volgogradnefteprodukt, and LUKoil-Volgogradnefteprodukt from 1985 to 1994. CEO of a branch of LUKOIL Finance Company from 1994 to 1995. CEO of LUKOIL regional office in Volgograd from 1995 to 1996. Vice-President of LUKOIL for Petroleum Product Marketing from 1996 to 2002. Vice-President, Head of the Main Division of Control and Internal Audit of LUKOIL from 2002.

Shares of BoD and Management Committee members in Charter Capital, as of December 31, 2009[1]

BoD and Management Committee members	Stake, %	BoD and Management Committee members	Stake, %
Valery Grayfer	0.007	Jevan Cheloyants	0.10
Vagit Alekperov	20.60[2]	Leonid Fedun	9.27[2]
Viktor Blazheev	–	Evgueny Khavkin	0.01
Herman Gref	–	Lyubov Khoba	0.34
Igor Ivanov	–	Sergey Kukura	0.39
Ravil Maganov	0.37	Ivan Masliaev	0.02
Richard Matzke	–	Alexander Matytsyn	0.30
Sergei Mikhailov	0.05	Anatoly Moskalenko	0.01
Alexander Shokhin	–	Vladimir Mulyak	0.01
Nikolai Tsvetkov	1.03[2]	Vladimir Nekrasov	0.04
Donald Wallette, Jr	–	Vagit Sharifov	–
Anatoly Barkov	0.07	Valery Subbotin	0.005

[1] Share stakes of BoD and Management Committee members are shown in accordance with requirements of Russian law for disclosure of such information, and include shares held directly by Board/Management Committee members as well as shares held by nominee investors in their names.
[2] Including beneficiary ownership.

Remuneration paid to Management Committee and BoD members of LUKOIL[1]

	Paid in 2009, thousand roubles				
	Salary	Bonuses	Remuneration	Other payments	Total
BoD	–	–	55,974.5	12,306.1	68,280.6
Management Committee	421,187.6	402,903.0	29,386.0	22,013.6	875,490.2

[1] For members of the Board of Directors who were simultaneously members of the Management Committee, remuneration received for membership of the Board of Directors is shown only in the 'Board of Directors' line, while salary, bonuses and remuneration to members of the Management Committee, and other payments are shown only in the 'Management Committee' line.

Each member of the Board of Directors was paid a remuneration of 4.47 million roubles in 2009 for carrying out their duties. There were additional payments for the roles of Board Chairman (1.04 million roubles), Chairman of a BoD Committee (520,000 roubles), as well as some other types of payment associated with duties of Board members and members of BoD Committees. Each member of the Board of Directors was paid a compensation associated with duties of Board members in the amount of documentarily confirmed expenditures, established at AGM from 24 June 2004.

In the accounting year members of the Management Committee were paid remuneration equal to their monthly salary in their principle job. This payment is made in accordance with main conditions of contracts, drawn up with members of the Management Committee, subject to achievement of key corporate targets in the reporting period. Members of the Management Committee also received an annual base salary, annual bonus payments based on results of their work for 2008, additional compensations of a social nature, and annual long-term premium payments. Scale of annual long-term premium payments was calculated by multiplying the number of shares conditionally owned by a Company official by the dividend per share, which was decided at the Annual General Meeting of Shareholders.

Committees of the Board of Directors

Strategy and Investment Committee

The purpose of this Committee is to draw up proposals to the BoD concerning:

- design of strategic goals for Company development;
- analysis of strategic development concepts, programs and plans of the Company;
- dividend amounts and procedure for dividend payment;
- distribution of Company profit and loss for the financial year.

From 25 June, 2009 the Committee has consistsed of Igor Ivanov (Chairman), Donald Wallette Jr, Ravil Maganov, and Richard Matzke.

Audit Committee

The purpose of this Committee is to make proposals to the BoD concerning:

- assessment of quality of services provided by the auditor, and observance by the auditor of auditing independence;
- selection and assessment of performance of the auditor.

From 25 June 2009 the Committee has consisted of Herman Gref (Chairman), Viktor Blazheev, and Sergei Mikhailov.

HR and Compensation Committee

The purpose of this Committee is to make proposals to the BoD concerning:

- design of corporate personnel policy;
- policy and standards in selection of candidates to management positions in the Company, emphasizing importance of appointing the most highly qualified specialists.

From 25 June 2009 the Committee has consisted of Alexander Shokhin (Chairman), Sergei Mikhailov and Nikolai Tsvetkov.

Changes in Group Structure

LUKOIL has been implementing a restructuring program since 2002. The main aim of the program is to increase shareholder value through increased transparency and efficiency of management processes, consolidation of core subsidiaries and withdrawal from the Group of non-core and inefficient assets.

The value of shares and share stakes of subsidiaries and affiliates, which were sold by the Group in 2009, amounted to $92 million. A total of $2.945 billion were paid out by the Group for acquisitions and consolidations in 2009. The biggest acquisitions by the Company in the reporting year were of stakes in the TRN refining complex (Netherlands) and the joint venture LUKARCO B.V. as well as increase to 100% of stakes in RITEK and UGK TGK-8.

Main corporate transactions in 2009:

- In June 2009 LUKOIL signed an agreement for acquisition from the company TOTAL S.A. of a 45% stake in the TOTAL Raffinaderij Nederland (TRN) refinery in the Netherlands. The deal was completed in September 2009 and its final value was about $700 million. The refinery is operated on a processing basis. LUKOIL will supply crude oil and other inputs and receive refined products in proportion to its equity stake. The Refinery has access to transport infrastructure, including the Maasvlakte Olie terminal (Netherlands), in which TRN has a 22% stake.
- In December 2009 LUKOIL Group completed purchase from a BP subsidiary of a 46% stake in the joint venture, LUKARCO B.V., which is developing the Tengiz and Korolevskoye fields in Kazakhstan. The acquisition increased the Company share in LUKARCO B.V. to 100%. Total value of the deal was $1.6 billion. The first payment of $300 million was made in December 2009, and the rest is to be paid no later than two years after the acquisition. As a result of the acquisition the Company's proved reserves increased by 102 million barrels of oil and 130 billion cubic feet of gas, and daily oil production rose by over 13,000 barrels.
- In January-November 2009 the Group bought about 25% of shares in RITEK, increasing its stake in the company to 100%. RITEK produces oil in European Russia and Western Siberia and also has major R&D activities.
- In April-May 2009 the Group bought about 4.57% of shares in UGK TGK-8, increasing its stake to 100%.

Financial Management

The Company's global approach to financial management is dictated by growth of the scale and geographical diversification of Company business. A system for centralized management of treasury operations, created in 2006, ensures efficient distribution of capital between Group organizations.

There was a major shortage of liquidity on international financial markets in 2009, and a tightening of credit conditions. However, a centralized policy for raising credit and the Company's strong financial position kept the cost of consolidated debt at best market levels and ensured smooth, full and timely financing of Group business.

LUKOIL continued to use its system for pooling of cash balances and their efficient redistribution in Russia and abroad during the reporting year, which helped to increase return on investment of cash balances.

The Company also diversified its sources of financing in order to achieve optimal structure of the debt portfolio. As part of this policy LUKOIL issued bonds worth 40 billion roubles ($1.3 billion) in June and August of the reporting year.

Also in August the Company obtained a syndicated credit of $1.2 billion for 3 years, secured by oil deliveries. The credit was provided at the best available rates for Russian companies (LIBOR +4%).

In November of the reporting year the Company placed a $1.5 billion Eurobond issue in two tranches of $900 million (for 5 years) and $600 million (for 10 years). Yield was at the pre-crisis level, which is an unprecedented achievement for a Russian private company.

Overall economic effect from actions in 2009 for optimization of financial management was $1.2 billion, which is nearly double the amount in 2008.

Internal Control and Audit

The system of control and internal audit is an integral part of the Company's corporate governance structure, enabling the Company to function efficiently and the interests of its shareholders and investors to be protected. The Group has created an Internal Audit Service, which ensures that management receives objective and accurate information on the business of organizations in LUKOIL Group and of its structural subdivisions.

There were 22 control and internal audit checks at organizations and structural subdivisions of LUKOIL Group during 2009, spread over all business segments. The Internal Audit Service also participated in 3 audit checks of foreign organizations in the Refining & Marketing segment. Purpose of the checks is to ensure that business of Group organizations and structural subdivisions complies with current legal requirements, regional laws, and international norms and standards.

The main tasks of the checks were:

- analysis of business efficiency, including investment efficiency, of LUKOIL Group organizations;
- checking that business of Group organizations is in accordance with LUKOIL's strategic goals and monitoring compliance with Company management decisions, including decisions taken as a result of previous checks;
- identification of significant risks related to activity of Group organizations and working out recommendations on ways of minimizing risks;
- assessing measures by management of subsidiaries and structural subdivisions of the Company to ensure stable and efficient functioning of various components of the internal control system;
- assessing whether organization and conduct of financial accounting help to make operating and financial control more efficient, contribute to further growth of shareholder value and protect shareholder interests.

Audit recommendations and management decisions were designed based on outcome of the checks in order to raise efficiency of Company business, minimize any risks, which had been identified, and improve the system of internal control and risk management. The Internal Audit Service constantly monitored execution of decisions by the Company's managing bodies, which were taken based on results of previous control and audit checks, and also monitored execution of approved action plans designed on the basis of internal audit recommendations in order to ensure efficiency of the internal audit system. Results of the monitoring are presented quarterly to the Company President. The share of instructions arising from audit checks, which are executed to schedule, is constantly growing and reached 93.3% in 2009 compared with 90% in the previous year.

The Company works constantly to organize and coordinate audit activity at LUKOIL Group organizations. Audit checks of financial and operating results for 2008 were carried out at 64 Group organizations in 2009 in order to ensure coordination between members of audit commissions in various Group organizations.

The Company continued to develop and improve its system for conduct of tendering procedures in the reporting year. Tendering procedures are an important element in the internal control system. During 2009 LUKOIL Group organized 4,934 tendering procedures with overall value of $2.6 billion. Cost of procurement of goods, work and services by LUKOIL Group was reduced by $361 million thanks to tighter control over conduct of tendering procedures, and improvements in the quality of assessment of tendering documentation and of proposals by tender participants.

There was systematic control by the Company in 2009 over observance of established procedures and authorizations in conduct of transactions, which affect the interests of Company shareholders and investors.

During 2009, in compliance with the procedure approved by the Management Committee on decision-making concerning participation in other organizations, the Internal Audit Service prepared and submitted opinions to the Restructuring Commission of LUKOIL Group on 71 corporate transactions, of which 41 were approved. The Commission also reviewed materials and issued opinions on 37 investment projects.

Informational Openness

Since receiving a full secondary listing on the London Stock Exchange in 2002 the Company has set up and successfully operates a system of corporate information disclosure for the investment community. LUKOIL's level of informational openness and quality of information disclosure fully comply with internationally accepted standards and with standards of the UK Financial Services Authority.

LUKOIL won prizes in several annual report competitions in 2009, as in previous years.

Such prizes are testimony to the Company's efforts to enhance informational openness and ensure efficient disclosure of information about Company business to investors, shareholders and the general public.

The Company's policy of informational openness includes:

- quarterly publication of financial statements, prepared in accordance with US GAAP;
- annual publication of international audit of Company hydrocarbon reserves;
- conference calls and webcasts for the investment community to accompany publication of financial results and announcement of other important corporate events;
- trips for representatives of the investment community to Company operating regions;
- regular meetings with investors and shareholders;
- annual publication of an Analyst DataBook and Fact Book containing detailed industrial and financial statistics;
- publication every two years of a Company Sustainability Report on the Company's activities in the Russian Federation.

Company Securities

There was growth of LUKOIL capitalization in 2009 after its large fall in the previous year due to international financial crisis. LUKOIL's capitalization by the end of 2009 was $47.8 billion, compared with $27.2 billion at the end of 2008.

Prices for company shares were subject to much volatility during the reporting year, reflecting general trends in Russia and internationally.

Prices for shares throughout the reporting year were determined mainly by the Urals crude oil price, which rose to $77 per barrel by the end of 2009 (from $40 at the start) thanks mainly to OPEC policy of limiting output. Macroeconomic indicators, particulary in the USA and China, also had impact and they led to some recovery in demand for oil by the end of the year. The second half of the year also saw a return of substantial investment inflows to emerging markets, including Russia.

Besides macroeconomic environment prices for LUKOIL shares were also influenced by corporate news. The Company successfully implemented its anti-crisis program in 2009 for raising production efficiency and increasing free cash flow. LUKOIL increased production and refining of hydrocarbons, won rights to develop the West Qurna-2 field in Iraq, acquired a stake in the TRN refinery in the Netherlands, and pursued an energetic capital raising policy.

As a result the LUKOIL share price on the RTS Stock Exchange rose by 75.6% in the course of the year to $56.2 per share at the end of 2009. Growth in price of Company shares was somewhat slower than overall Russian market growth (the RTS Index rose by 128.6% and the MICEX Index by 121%). So current undervaluation offers potential for substantial growth in the future.

Despite the complex situation on the stock market and in the economy as a whole, LUKOIL shares were among the most liquid securities of Russian issuers during 2009 both domestically and abroad. Shares of LUKOIL represented 6.5% and 5.3% of total volumes on main trading floors, the MICEX and the RTS Stock Exchange, respectively, in 2009.

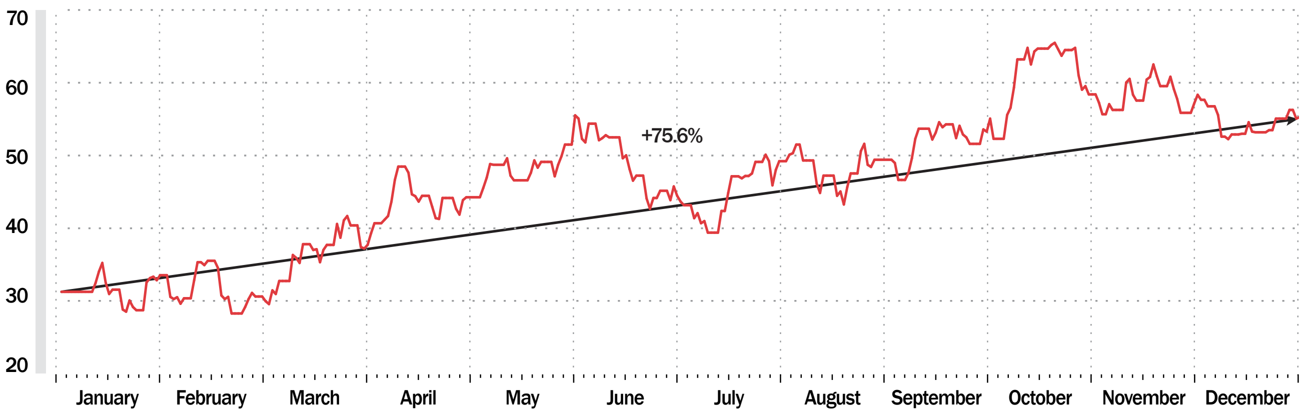
Programs of American Depositary Receipts (ADRs) on Company shares continued to operate in the reporting year. Company ADRs were traded on over-the-counter market in the USA and also on stock exchanges in London, Frankfurt, Munich, Stuttgart, etc.

The total number of ADRs issued on ordinary shares of the Company at the end of 2009 was 581 million (68.3% of Company charter capital). ADRs on LUKOIL shares took second place by volumes of trading among ADRs of foreign issuers listed on the IOB system of the London Stock Exchange in 2009 (they represented 18.7% of total average monthly trading volumes in the IOB system).

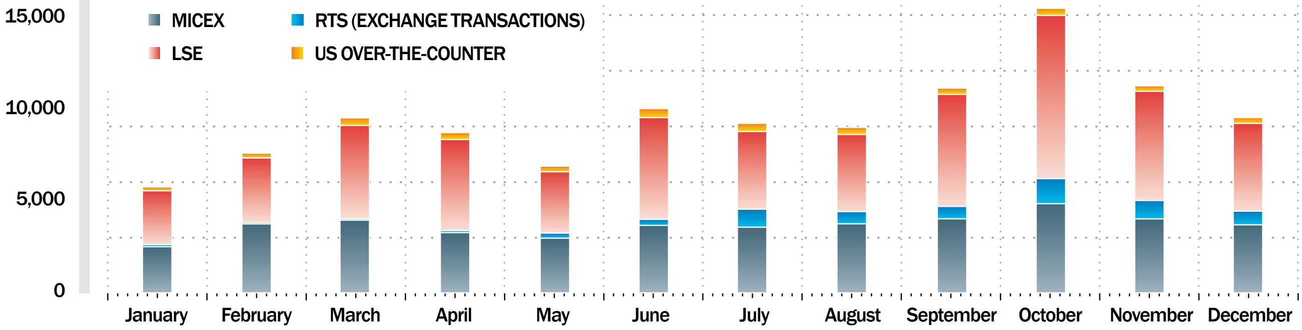
Trading turnover in LUKOIL shares and ADRs was much lower in 2009 than in 2008 both by volumes and money value. This trend was common to shares of most Russian issuers and not only Company shares. However, trading volumes recovered gradually in the second half of the year thanks to revival of international capital markets.

LUKOIL shares continued to be used as an underlying instrument for trading on the Russian stock futures market in the reporting year. Future

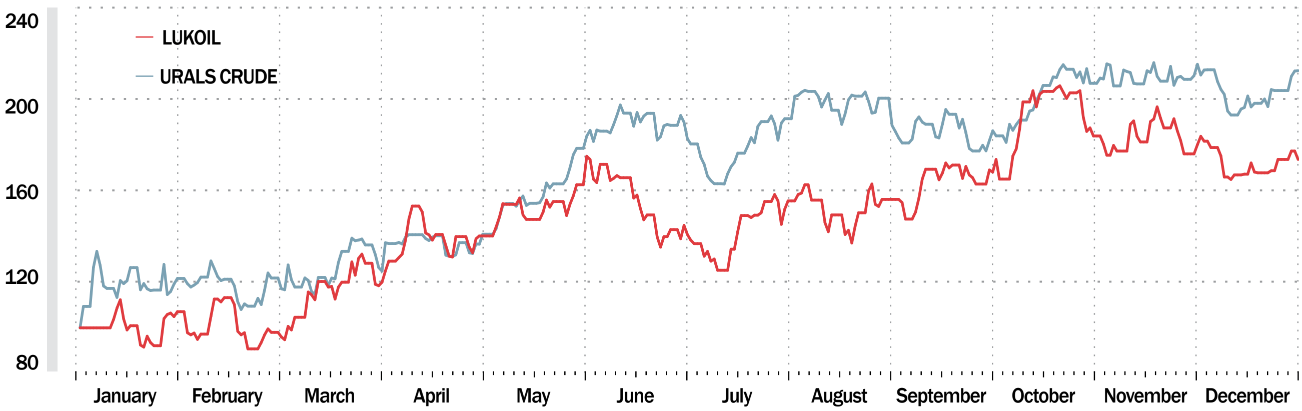
LUKOIL SHARE PRICE ON THE RTS EXCHANGE (2009), $



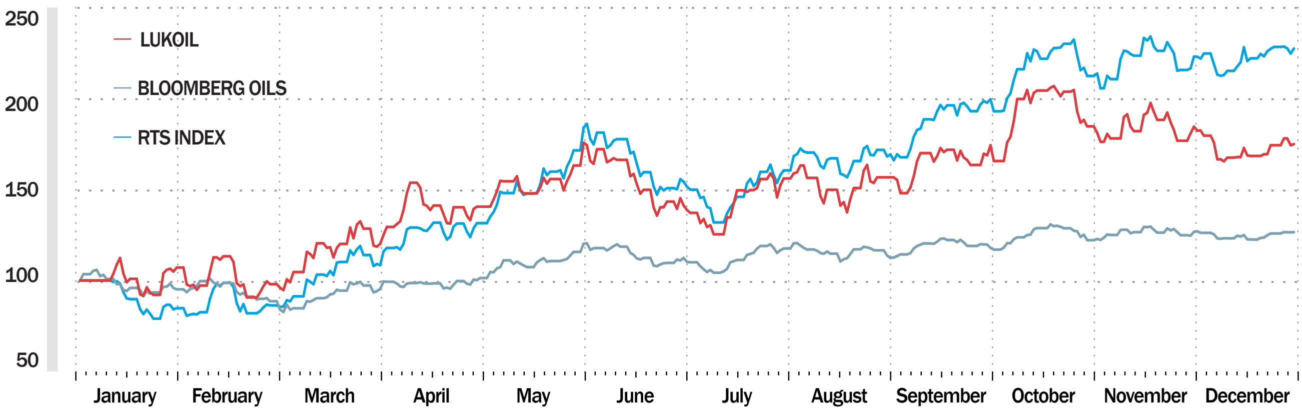
MONTHLY TRADING IN LUKOIL SHARES AND DEPOSITARY RECEIPTS (2009), $ MILLION



LUKOIL SHARE PRICE ON THE RTS EXCHANGE AND URALS OIL PRICE (2009), %



LUKOIL SHARE PRICE ON THE RTS EXCHANGE, BLOOMBERG OILS INDEX AND THE RTS INDEX (2009), %



MAIN LUKOIL SHAREHOLDERS[1] (> 1% OF ORDINARY SHARES)

	Number of shares on January 1, 2009	% of total shares on January 1, 2009	Number of shares on January 1, 2010	% of total shares on January 1, 2010
ING Bank (Eurasia) ZAO	585,245,353	68.81%	588,130,232	69.15%
Depositary-Clearing Company	67,184,973	7.90%	75,790,805	8.91%
KB Citibank ZAO	69,274,981	8.14%	66,536,986	7.82%
National Depositary Center	48,689,475	5.72%	38,176,573	4.49%
SDK Garant	31,028,284	3.65%	33,177,732	3.90%
DK URALSIB	19,627,533	2.31%	13,574,885	1.60%

[1] Nominees.

contracts for delivery of LUKOIL shares were among main instruments on the futures section of the RTS Stock Exchange.

In autumn 2009 the Group carried out an issue of Eurobonds. A first tranche of $900 million with redemption date in 2014 was placed at 6.375% and a second tranche of $600 million with redemption date in 2019 was placed at 7.250%. The 2014 bonds were placed at 99.474% of their face value, giving 6.5% yield to redemption. The 2019 bonds were placed at 99.127% of face value to give 7.375% yield to redemption. This was the first Eurobond placement by a Russian issuer for more than a year and the placement terms were highly favourable for the Company, thanks to strong demand from investors.

LUKOIL did its utmost in the reporting year to maintain and increase its shareholder value. Operating indicators were improved, new efficient assets were acquired and the Company implemented a tight policy to limit capital expenditures and increase cash flows. As a result, the Company was able to preserve its investment attractiveness in an environment of instability in the world financial system. During 2009 the Company devised and approved a 10-year program of strategic development, which emphasizes increase of free cash flow and shareholder income. Achievement of the goals, which LUKOIL has set itself, will ensure future growth in value of its shares and will overcome the current situation of undervaluation of the Company.

Dividends

LUKOIL bases its dividend policy on a balance of interests between the Company and its shareholders, aiming to increase the Company's investment attractiveness and shareholder value, and to respect and strictly observe the rights of shareholders, as set out in acting legislation of the Russian Federation, the Company Charter and its internal documents.

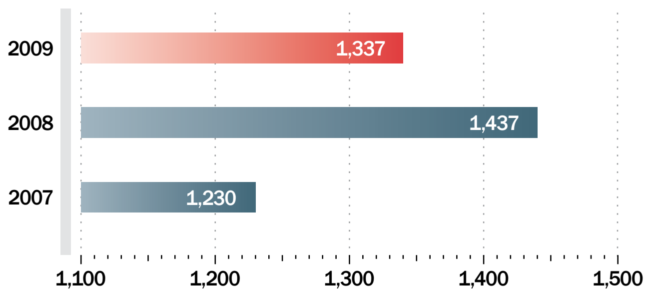
Dividends accrued in 2009 on results for 2008 were $1,360 million or 15% of consolidated net income of LUKOIL Group for 2008 under US GAAP.

The Company decided in 2009 to steadily increase the share of dividends in net income from previously approved 15% to 30%. Dividends for 2009 will not be lowered in comparison with 2008, despite reduction of net income: on April 20, 2010 the Board of Directors recommended the Annual General Meeting to approve dividends for 2009 at 52 roubles per share ($1.72 at the exchange rate as of December 31, 2009), which corresponds to the level for the previous year. So the ratio of dividends to net income will exceed 20%, which is significantly more than in 2008. Dividend yield will be 3.6%. Basic income per ordinary share in 2009 was $8.28, compared with $10.88 in 2008.

DIVIDEND PER COMMON SHARE (ROUBLES) AND DIVIDEND YIELD (%)

	Dividend, roubles	Dividend yield, %[2]
2005	33	2.71
2006	38	1.77
2007	42	2.10
2008	50	2.38
2009[1]	52	3.62

DIVIDENDS PAID ON COMPANY COMMON STOCK, $ MILLION



[1] Dividends recommended by the LUKOIL Board of Directors for approval at the Annual General Meeting of Shareholders.
[2] Dividend yield is calculated based on the average market price for LUKOIL shares and exchange rate as of the end of the year, for which the dividends are paid.

CONSOLIDATED FINANCIAL STATEMENTS

As of December 31, 2009 and 2008 and for each of the years in the three-year period ended December 31, 2009

(PREPARED IN ACCORDANCE WITH US GAAP)

Independent Auditors' Report

The Board of Directors
of OAO LUKOIL

We have audited the accompanying consolidated balance sheets of OAO LUKOIL and its subsidiaries as of December 31, 2009 and 2008, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2009. These consolidated financial statements are the responsibility of the management of OAO LUKOIL. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of OAO LUKOIL and its subsidiaries as of December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

ZAO KPMG

ZAO KPMG
Moscow, Russian Federation
March 19, 2010

OAO LUKOIL
Consolidated Balance Sheets

As of December 31, 2009 and 2008

(Millions of US dollars, unless otherwise noted)

	Note	2009	2008
ASSETS			
Current assets			
Cash and cash equivalents	3	2,274	2,239
Short-term investments		75	505
Accounts and notes receivable, net	5	5,935	5,069
Inventories	6	5,432	3.735
Prepaid taxes and other expenses		3,549	3.566
Other current assets		574	519
Total current assets		**17,839**	**15,633**
Investments	7	5,944	3,269
Property, plant and equipment	8	52,228	50,088
Deferred income tax assets	12	549	521
Goodwill and other intangible assets	9	1,653	1,159
Other non-current assets		806	791
TOTAL ASSETS		79,019	71,461
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities			
Accounts payable		4,906	5,029
Short-term borrowings and current portion of long-term debt	10	2,058	3,232
Taxes payable		1,828	1,564
Other current liabilities		902	750
Total current liabilities		**9,694**	**10,575**
Long-term debt	11,15	9,265	6,577
Deferred income tax liabilities	12	2,080	2,116
Asset retirement obligations	8	1,189	718
Other long-term liabilities		412	465
Total liabilities		**22,640**	**20,451**
Equity	14		
OAO LUKOIL stockholders' equity			
Common stock		15	15
Treasury stock, at cost		(282)	(282)
Additional paid-in capital		4,699	4,694
Retained earnings		51,634	45,983
Accumulated other comprehensive loss		(75)	(70)
Total OAO LUKOIL stockholders' equity		**55,991**	**50,340**
Non-controlling interests		388	670
Total equity		**56,379**	**51,010**
TOTAL LIABILITIES AND EQUITY		79,019	71,461

President of OAO LUKOIL
ALEKPEROV V.Y.

Chief accountant of OAO LUKOIL
KOZYREV I.A.

OAO LUKOIL
Consolidated Statements of Income

For the years ended December 31, 2009, 2008 and 2007

(Millions of US dollars, unless otherwise noted)

	Note	2009	2008	2007
REVENUES				
Sales (including excise and export tariffs)	22	81,083	107,680	81,891
COSTS AND OTHER DEDUCTIONS				
Operating expenses		(7,124)	(8,126)	(6,172)
Cost of purchased crude oil, gas and products		(31,977)	(37,851)	(27,982)
Transportation expenses		(4,830)	(5,460)	(4,457)
Selling, general and administrative expenses		(3,306)	(3,860)	(3,207)
Depreciation, depletion and amortization		(3,937)	(2,958)	(2,172)
Taxes other than income taxes	12	(6,474)	(13,464)	(9,367)
Excise and export tariffs		(13,058)	(21,340)	(15,033)
Exploration expenses		(218)	(487)	(307)
Loss on disposals and impairments of assets		(381)	(425)	(123)
INCOME FROM OPERATING ACTIVITIES		**9,778**	**13,709**	**13,071**
Interest expense		(667)	(391)	(333)
Interest and dividend income		134	163	135
Equity share in income of affiliates	7	351	375	347
Currency translation (loss) gain		(520)	(918)	35
Other non-operating expense		(13)	(244)	(240)
INCOME BEFORE INCOME TAX		**9,063**	**12,694**	**13,015**
Current income taxes		(1,922)	(4,167)	(3,410)
Deferred income taxes		(72)	700	(39)
TOTAL INCOME TAX EXPENSE	12	(1,994)	(3,467)	(3,449)
NET INCOME		**7,069**	**9,227**	**9,566**
Less: net income attributable to non-controlling interests		(58)	(83)	(55)
NET INCOME ATTRIBUTABLE TO OAO LUKOIL		**7,011**	**9,144**	**9,511**
Basic and diluted earnings per share of common stock (US dollars) attributable to OAO LUKOIL:	14	8.28	10.88	11.48

OAO LUKOIL
Consolidated Statements of Stockholders' Equity and Comprehensive Income
For the years ended December 31, 2009, 2008 and 2007

(Millions of US dollars, unless otherwise noted)

	2009		2008		2007	
	Stockholders' equity	Comprehensive income	Stockholders' equity	Comprehensive income	Stockholders' equity	Comprehensive income
Common stock						
Balance as of January 1	15		15		15	
BALANCE AS OF DECEMBER 31	**15**		**15**		**15**	
Treasury stock						
Balance as of January 1	(282)		(1,591)		(1,098)	
Stock purchased	–		(219)		(712)	
Stock disposed	–		1,528		219	
BALANCE AS OF DECEMBER 31	**(282)**		**(282)**		**(1,591)**	
Additional paid-in capital						
Balance as of January 1	4,694		4,499		3,943	
Premium on non-outstanding shares issued	–		20		–	
Effect of stock compensation plan	20		103		103	
Changes in non-controlling interests	(15)		–		–	
Proceeds from sale of treasury stock in excess of carrying amount	–		72		453	
BALANCE AS OF DECEMBER 31	**4,699**		**4,694**		**4, 499**	
Retained earnings						
Balance as of January 1	45,983		38,349		30,061	
Net income	7,011	7,011	9,144	9,144	9,511	9,511
Dividends on common stock	(1,360)		(1,510)		(1,223)	
BALANCE AS OF DECEMBER 31	**51,634**		**45,983**		**38,349**	
Accumulated other comprehensive loss, net of tax						
Balance as of January 1	(70)		(59)		(21)	
Pension benefits:						
Prior service cost	(4)	(4)	(5)	(5)	(16)	(16)
Actuarial gain (loss)	1	1	(6)	(6)	(22)	(22)
Unrecognized loss on available-for-sale securities	(2)	(2)	–	–	–	–
BALANCE AS OF DECEMBER 31	**(75)**		**(70)**		**(59)**	
Total comprehensive income for the year		7,006		9,133		9,473
TOTAL OAO LUKOIL STOCKHOLDERS' EQUITY AS OF DECEMBER 31	**55,991**		**50,340**		**41,213**	

	2009		2008		2007	
	Stockholders' equity	Comprehensive income	Stockholders' equity	Comprehensive income	Stockholders' equity	Comprehensive income
Non-controlling interests						
Balance as of January 1	670		577		523	
Net income attributable to non-controlling interests	58		83		55	
Changes in non-controlling interests	(340)		10		(1)	
BALANCE AS OF DECEMBER 31	**388**		**670**		**577**	
TOTAL EQUITY AS OF DECEMBER 31	**56,379**		**51,010**		**41,790**	

	Share activity (thousands of shares)		
	2009	2008	2007
Common stock, issued			
Balance as of January 1	850,563	850,563	850,563
BALANCE AS OF DECEMBER 31	**850,563**	**850,563**	**850,563**
Treasury stock			
Balance as of January 1	(3,836)	(23,321)	(23,632)
Purchase of treasury stock	–	(2,899)	(8,756)
Disposal of treasury stock	–	22,384	9,067
BALANCE AS OF DECEMBER 31	**(3,836)**	**(3,836)**	**(23,321)**

OAO LUKOIL
Consolidated Statements of Cash Flows
For the years ended December 31, 2009, 2008 and 2007

(Millions of US dollars)

	Note	2009	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income		**7,011**	**9,144**	**9,511**
Adjustments for non-cash items:				
Depreciation, depletion and amortization		3,937	2,958	2,172
Equity share in income of affiliates, net of dividends received		(213)	(238)	209
Dry hole write-offs		117	317	143
Loss on disposals and impairments of assets		381	425	123
Deferred income taxes		72	(700)	39
Non-cash currency translation (gain) loss		(57)	(668)	251
Non-cash investing activities		(20)	(29)	(36)
All other items – net		138	404	297
Changes in operating assets and liabilities:				
Accounts and notes receivable		(1,171)	2,647	(2,297)
Inventories		(1,719)	963	(1,148)
Accounts payable		96	(989)	1,599
Taxes payable		292	(521)	386
Other current assets and liabilities		19	599	(368)
NET CASH PROVIDED BY OPERATING ACTIVITIES		**8,883**	**14,312**	**10,881**
CASH FLOWS FROM INVESTING ACTIVITIES				
Acquisition of licenses		(40)	(12)	(255)
Capital expenditures		(6,483)	(10,525)	(9,071)
Proceeds from sale of property, plant and equipment		91	166	72
Purchases of investments		(216)	(398)	(206)
Proceeds from sale of investments		478	636	175
Sale of interests in subsidiaries and affiliated companies		92	3	1,136
Acquisitions of subsidiaries and non-controlling interests (including advances related to acquisitions), net of cash acquired		(2,845)	(3,429)	(1,566)
NET CASH USED IN INVESTING ACTIVITIES		**(8,923)**	**(13,559)**	**(9,715)**

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

	Note	2009	2008	2007
CASH FLOWS FROM FINANCING ACTIVITIES				
Net movements of short-term borrowings		(1,281)	974	(59)
Cash received under sales-leaseback transaction		–	235	–
Proceeds from issuance of long-term debt		5,467	2,884	2,307
Principal repayments of long-term debt		(2,697)	(1,547)	(1,632)
Dividends paid on company common stock		(1,337)	(1,437)	(1,230)
Dividends paid to non-controlling interest stockholders		(85)	(168)	(78)
Financing received from related and third party non-controlling interest stockholders		20	39	177
Purchase of Company's stock		–	(219)	(712)
Proceeds from sale of Company's stock		–	–	129
Other – net		–	2	-
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES		**87**	**763**	**(1,098)**
Effect of exchange rate changes on cash and cash equivalents		(12)	(118)	21
NET INCREASE IN CASH AND CASH EQUIVALENTS		**35**	**1,398**	**89**
Cash and cash equivalents at beginning of year		2,239	841	752
CASH AND CASH EQUIVALENTS AT END OF YEAR	3	**2,274**	**2 239**	**841**
Supplemental disclosures of cash flow information				
Interest paid		520	440	338
Income taxes paid		1,575	4,902	2,872

OAO LUKOIL
Notes to Consolidated Financial Statements

(Millions of US dollars, except as indicated)

Note 1. Organization and environment

The primary activities of OAO LUKOIL (the "Company") and its subsidiaries (together, the "Group") are oil exploration, production, refining, marketing and distribution. The Company is the ultimate parent entity of this vertically integrated group of companies.

The Group was established in accordance with Presidential Decree 1403, issued on November 17, 1992. Under this decree, on April 5, 1993, the Government of the Russian Federation transferred to the Company 51% of the voting shares of fifteen enterprises. Under Government Resolution 861 issued on September 1, 1995, a further nine enterprises were transferred to the Group during 1995. Since 1995, the Group has carried out a share exchange program to increase its shareholding in each of the twenty-four founding subsidiaries to 100%.

From formation, the Group has expanded substantially through consolidation of its interests, acquisition of new companies and establishment of new businesses.

Business and economic environment

The Russian Federation has been experiencing political and economic change, that has affected and will continue to affect the activities of enterprises operating in this environment. Consequently, operations in the Russian Federation involve risks, which do not typically exist in other markets. In addition, the recent contraction in the capital and credit markets has further increased the level of economic uncertainty in the environment.

The accompanying financial statements reflect management's assessment of the impact of the business environment in the countries in which the Group operates on the operations and the financial position of the Group. The future business environments may differ from management's assessment.

Basis of preparation

These consolidated financial statements have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

Note 2. Summary of significant accounting policies

Principles of consolidation

These consolidated financial statements include the financial position and results of the Company, controlled subsidiaries of which the Company directly or indirectly owns more than 50% of the voting interest, unless minority stockholders have substantive participating rights, and variable interest entities where the Group is determined to be the primary beneficiary. Other significant investments in companies of which the Company directly or indirectly owns between 20% and 50% of the voting interest and over which it exercises significant influence but not control, are accounted for using the equity method of accounting. Investments in companies of which the Company directly or indirectly owns more than 50% of the voting interest but where minority stockholders have substantive participating rights are accounted for using the equity method of accounting. Undivided interests in oil and gas joint ventures are accounted for using the proportionate consolidation method. Investments in other companies are recorded at cost. Equity investments and investments in other companies are included in "Investments" in the consolidated balance sheet.

Use of estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying value of oil and gas properties and other property, plant and equipment, goodwill impairment assessment, asset retirement obligations, deferred income taxes, valuation of financial instruments, and obligations related to employee benefits. Eventual actual amounts could differ from those estimates.

Revenue

Revenues from the production and sale of crude oil and petroleum products are recognized when title passes to customers at which point the risks and rewards of ownership are assumed by the customer and the price is fixed or determinable. Revenues include excise on petroleum products sales and duties on export sales of crude oil and petroleum products.

Revenues from non-cash sales are recognized at the fair market value of the crude oil and petroleum products sold.

Foreign currency translation

The Company maintains its accounting records in Russian rubles. The Company's functional currency is the US dollar and the Group's reporting currency is the US dollar.

For operations in the Russian Federation and for the majority of operations outside the Russian Federation, the US dollar is the functional currency. Where the US dollar is the functional currency, monetary assets and liabilities have been translated into US dollars at the rate prevailing at each balance sheet date. Non-monetary assets and liabilities have been translated into US dollars at historical rates. Revenues, expenses and cash flows have been translated into US dollars at rates, which approximate actual rates at the date of the transaction. Translation differences resulting from the use of these rates are included in the consolidated statement of income.

For certain other operations outside the Russian Federation, where the US dollar is not the functional currency and the economy is not hyperinflationary, assets and liabilities are translated into US dollars at year-end exchange rates and revenues and expenses are translated at average exchange rates for the year. Resulting translation adjustments are reflected as a separate component of comprehensive income.

In all cases, foreign currency transaction gains and losses are included in the consolidated statement of income.

As of December 31, 2009, 2008 and 2007, exchange rates of 30.24, 29.38 and 24.55 Russian rubles to the US dollar, respectively, have been used for translation purposes.

The Russian ruble and other currencies of republics of the former Soviet Union are not readily convertible outside of their countries. Accordingly, the translation of amounts recorded in these currencies into US dollars should not be construed as a representation that such currency amounts have been, could be or will in the future be converted into US dollars at the exchange rate shown or at any other exchange rate.

Cash and cash equivalents

Cash and cash equivalents include all highly liquid investments with an original maturity of three months or less.

Cash with restrictions on immediate use

Cash funds for which restrictions on immediate use exist are accounted for within other non-current assets.

Accounts and notes receivable

Accounts and notes receivable are recorded at their transaction amounts less provisions for doubtful debts. Provisions for doubtful debts are recorded to the extent that there is a likelihood that any of the amounts due will not be collected. Non-current receivables are discounted to the present value of expected cash flows in future periods using the original discount rate.

Inventories

Starting from January 1, 2009, the Group elected to change the inventory accounting method for finished goods and purchased products from the weighted average to the FIFO cost method. Management believes the FIFO cost method for these inventory categories is preferable because it reflects the results of the most recent business activity and allows a more rapid reflection of results of operations, and represents a better matching of cost of sales with related sales. The Group determined that it is impracticable to calculate the cumulative effect of applying this change retrospectively because of the lack of information available.

The cost of all other inventory categories is determined using an "average cost" method.

Investments

Debt and equity securities are classified into one of three categories: trading, available-for-sale, or held-to-maturity.

Trading securities are bought and held principally for the purpose of selling in the near term. Held-to-maturity securities are those securities in which a Group company has the ability and intent to hold until maturity. All securities not included in trading or held-to-maturity are classified as available-for-sale.

Trading and available-for-sale securities are recorded at fair value. Held-to-maturity securities are recorded at cost, adjusted for the amortization or accretion of premiums or discounts. Unrealized holding gains and losses on trading securities are included in the consolidated statement of income. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are reported as a separate component of comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific identification basis. Dividends and interest income are recognized in the consolidated statement of income when earned.

A permanent decline in the market value of any available-for-sale or held-to-maturity security below cost is accounted for as a reduction in the carrying amount to fair value. The impairment is charged to the consolidated statement of income and a new cost base for the security is established. Premiums and discounts are amortized or accreted over the life of the related held-to-maturity or available-for-sale security as an adjustment to yield using the effective interest rate method and such amortization and accretion is recorded in the consolidated statement of income.

Property, plant and equipment

Oil and gas properties are accounted for using the successful efforts method of accounting whereby property acquisitions, successful exploratory wells, all development costs, and support equipment and facilities are capitalized. Unsuccessful exploratory wells are expensed when a well is determined to be non-productive. Other exploratory expenditures, including geological and geophysical costs are expensed as incurred.

The Group continues to capitalize costs of exploratory wells and exploratory-type stratigraphic wells for more than one year after the completion of drilling if the well has found a sufficient quantity of reserves to justify its completion as a producing well and the company is making sufficient progress assessing the reserves and the economic and operating viability of the project. If these conditions are not met or if information that raises substantial doubt about the economic or operational viability of the project is obtained, the well would be assumed impaired, and its costs, net of any salvage value, would be charged to expense.

Depreciation, depletion and amortization of capitalized costs of oil and gas properties is calculated using the unit-of-production method based upon proved reserves for the cost of property acquisitions and proved developed reserves for exploration and development costs.

Production and related overhead costs are expensed as incurred.

Depreciation of assets not directly associated with oil production is calculated on a straight-line basis over the economic lives of such assets, estimated to be in the following ranges:

Buildings and constructions	5 – 40 Years
Machinery and equipment	5 – 20 Years

In addition to production assets, certain Group companies also maintain and construct social assets for the use of local communities. Such assets are capitalized only to the extent that they are expected to result in future economic benefits to the Group. If capitalized, they are depreciated over their estimated economic lives.

Significant unproved properties are assessed for impairment individually on a regular basis and any estimated impairment is charged to expense.

Asset retirement obligations

The Group records the fair value of liabilities related to its legal obligations to abandon, dismantle or otherwise retire tangible long-lived assets in the period in which the liability is incurred. A corresponding increase in the carrying amount of the related long-lived asset is also recorded. Subsequently, the liability is accreted for the passage of time and the related asset is depreciated using the unit-of-production method.

Goodwill and other intangible assets

Goodwill represents the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed. It is assigned to reporting units as of the acquisition date. Goodwill is not amortized, but is tested for impairment at least on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The impairment test requires estimating the fair value of a reporting unit and comparing it with its carrying amount, including goodwill assigned to the reporting unit. If the estimated fair value of the reporting unit is less than its net carrying amount, including goodwill, then the goodwill is written down to its implied fair value.

Intangible assets with indefinite useful lives are tested for impairment at least annually. Intangible assets that have limited useful lives are amortized on a straight-line basis over the shorter of their useful or legal lives.

Impairment of long-lived assets

Long-lived assets, such as oil and gas properties (other than unproved properties), other property, plant, and equipment, and purchased intangibles subject to amortization, are assessed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset group to the estimated undiscounted future cash flows expected to be generated by that group. If the carrying amount of an asset group exceeds its estimated undiscounted future cash flows, an impairment charge is recognized by writing down the carrying amount to the estimated fair value of the asset group, generally determined as discounted future net cash flows. Assets to be disposed of are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale are presented separately in the appropriate asset and liability sections of the balance sheet.

Income taxes

Deferred income tax assets and liabilities are recognized in respect of future tax consequences attributable to temporary differences between the carrying amounts of existing assets and liabilities for the purposes of the consolidated financial statements and their respective tax bases and in respect of operating loss and tax credit carryforwards. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse and the assets be recovered and liabilities settled. The effect on deferred income tax assets and liabilities of a change in tax rates is recognized in the consolidated statement of income in the reporting period which includes the enactment date.

The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income in the reporting periods in which the originating expenditure becomes deductible. In assessing the realizability of deferred income tax assets, management considers whether it is more likely than not that the deferred income tax assets will be realized. In making this assessment, management considers the scheduled reversal of deferred income tax liabilities, projected future taxable income, and tax planning strategies.

An income tax position is recognized only if the uncertain position is more likely than not of being sustained upon examination, based on its technical merits. A recognized income tax position is measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company records interest and penalties relating to income tax in income tax expense in the consolidated statements of income.

Interest-bearing borrowings

Interest-bearing borrowings are initially recorded at the value of net proceeds received. Any difference between the net proceeds and the redemption value is amortized at a constant rate over the term of the borrowing. Amortization is included in the consolidated statement of income each year and the carrying amounts are adjusted as amortization accumulates.

If borrowings are repurchased or settled before maturity, any difference between the amount paid and the carrying amount is recognized in the consolidated statement of income in the period in which the repurchase or settlement occurs.

Pension benefits

The expected costs in respect of pension obligations of Group companies are determined by an independent actuary. Obligations in respect of each employee are accrued over the reporting periods during which the employee renders service in the Group.

The Group recognizes the funded status of postretirement defined benefit plan in the balance sheet with corresponding adjustments to accumulated other comprehensive income. The adjustment to accumulated other comprehensive income represents the net unrecognized actuarial gains and unrecognized prior service costs. These amounts are subsequently recognized as net periodic benefit cost. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic benefit cost in the same periods are recognized as a component of other comprehensive income. These amounts are subsequently recognized as a component of net periodic benefit cost on the same basis as the amounts recognized in accumulated other comprehensive income.

Treasury stock

Purchases by Group companies of the Company's outstanding stock are recorded at cost and classified as treasury stock within Stockholders' equity. Shares shown as Authorized and Issued include treasury stock. Shares shown as Outstanding do not include treasury stock.

Earnings per share

Basic earnings per share is computed by dividing net income available to common stockholders of the Company by the weighted-average number of shares of common stock outstanding during the reporting period. A calculation is carried out to establish if there is potential dilution in earnings per share if convertible securities were to be converted into shares of common stock or contracts to issue shares of common stock were to be exercised. If there is such dilution, diluted earnings per share is presented.

Contingencies

Certain conditions may exist as of the balance sheet date, which may result in losses to the Group but the impact of which will only be resolved when one or more future events occur or fail to occur.

If a Group company's assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability is accrued and charged to the consolidated statement of income. If the assessment indicates that a potentially material loss is not probable, but is reasonably possible, or is probable, but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss, is disclosed in the notes to the consolidated financial statements. Loss contingencies considered remote or related to unasserted claims are generally not disclosed unless they involve guarantees, in which case the nature of the guarantee is disclosed.

Environmental expenditures

Estimated losses from environmental remediation obligations are generally recognized no later than completion of remedial feasibility studies. Group companies accrue for losses associated with environmental remediation obligations when such losses are probable and reasonably estimable. Such accruals are adjusted as further information becomes available or circumstances change. Costs of expected future expenditures for environmental remediation obligations are not discounted to their present value.

Use of derivative instruments

The Group's derivative activity is limited to certain petroleum products marketing and trading outside of its physical crude oil and petroleum products businesses and hedging of commodity price risks. Currently this activity involves the use of futures and swaps contracts together with purchase and sale contracts that qualify as derivative instruments. The Group accounts for these activities under the mark-to-market methodology in which the derivatives are revalued each accounting period. Resulting realized and unrealized gains or losses are presented in the consolidated statement of income on a net basis. Unrealized gains and losses are carried as assets or liabilities on the consolidated balance sheet.

Share-based payments

The Group accounts for liability classified share-based payment awards to employees at fair value on the date of grant and as of each reporting date. Expenses are recognized over the vesting period. Equity classified share-based payment awards to employees are valued at fair value on the date of grant and expensed over the vesting period.

Comparative amounts

Certain prior period amounts have been reclassified to conform with the current period's presentation.

Recent accounting pronouncements

In February 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-09, *"Subsequent events"* which amends Accounting Standards Codification (ASC) No. 855 (former SFAS No. 165, *"Subsequent events"*), issued in May 2009. The Group adopted ASC No. 855 starting from the second quarter of 2009. These standards address accounting and disclosure requirements related to subsequent events and require management of an entity which is an SEC filer or is a conduit bond obligator for conduit securities that are traded in a public market to evaluate subsequent event through the date that the financial statements are issued. Entities that do not meet these criteria should evaluate subsequent events through the date the financial statements are available to be issued and are required to disclose the date through which subsequent events have been evaluated. The Group determined that it should evaluate subsequent events through the date the financial statements are available to be issued and applied the requirements of ASU No. 2010-09 starting from the financial statements for 2009.

In January 2010, the FASB issued ASU No. 2010-01, *"Accounting for Distributions to Shareholders with Components of Stock and Cash"* which addresses how an entity should account for the stock portion of a dividend in certain arrangements when a shareholder makes an election to receive cash or stock, subject to limitations on the amount of the dividend to be issued in cash. The stock portion of the dividend should be accounted for as a stock issuance upon distribution, resulting in basic earnings per share being adjusted prospectively. Prior to distribution, the entity's obligation to issue shares would be reflected in diluted earnings-per-share based on the guidance in ASC No. 260, which addresses contracts that may be settled in shares. This ASU is effective for interim and annual periods ending after December 15, 2009. The Group adopted ASU No. 2010-01 for the 2009 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In January 2010, the FASB issued ASU No. 2010-02, *"Accounting and Reporting for Decreases in Ownership of a Subsidiary - A Scope Clarification"* to clarify the scope of ASC Subtopic No. 810-10, *"Consolidation – Overall."* This ASU specifies that the guidance in ASC Subtopic No. 810-10 on accounting for decreases in ownership of a subsidiary applies to: (1) a subsidiary or group of assets that constitutes a business or nonprofit activity; (2) a subsidiary that is a business or a nonprofit activity that is transferred to an equity method investee or a joint venture; and (3) an exchange of a group of assets that constitute a business or nonprofit activity for a noncontrolling interest in an entity. If a company's ownership interest in a subsidiary that is not a business or nonprofit activity decreases, then other accounting guidance generally would be applied based on the nature of the transaction. The new pronouncement also clarifies that the recent guidance on accounting for decreases in ownership of a subsidiary does not apply if the transaction is a sale of in-substance real estate or a conveyance of oil and gas properties. This ASU is effective for interim and annual periods ending after December 15, 2009 and the guidance should be applied on a retrospective basis to the first period in which the company adopted ASC No. 810. The Group adopted ASU No. 2010-02 for the 2009 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In January 2010, the FASB issued ASU No. 2010-03, *"Extractive activities — Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures"*. The main provisions of ASU No. 2010-03 are the following: (1) expanding the definition of oil- and gas-producing activities to include the extraction of saleable hydrocarbons, in solid, liquid, or gaseous state, from oil sands, shale, coalbeds, or other nonrenewable resources that are intended to be upgraded into synthetic oil or gas, and activities undertaken with a view to such extraction; (2) entities should use first-day-of-the-month price during the 12-month period (the 12-months average price) in calculating proved oil and gas reserves and estimating related standardized measure of discounted net cash flows; (3) requiring entities to disclose separately information about reserves quantities and financial statement amounts for geographic areas that represent 15 percent or more of proved reserves; (4) separate disclosure for consolidated entities and equity method investments. ASU No. 2010-03 is effective for annual reporting periods ending on or after December 31, 2009. The Group adopted ASU No. 2010-03 for the 2009 annual financial statements. This adoption did not have a material impact on the Group's reported reserves evaluation, results of operations, financial position or cash flows.

In June 2009, the FASB issued amendments to ASC No. 810 (former FASB Interpretation No. 46(R), *"Consolidation of Variable Interest Entities"*) to address the effects of the elimination of the qualifying special purpose entity concept. More specifically, it requires a qualitative rather than a quantitative approach to determine the primary beneficiary of a variable interest entity, it amends certain guidance pertaining to the determination of the primary beneficiary when related parties are involved, and it amends certain guidance for determining whether an entity is a variable interest entity. Additionally, these amendments require continuous assessment of whether an enterprise is the primary beneficiary of a variable interest entity. Amendments are effective on January 1, 2010, and the Group does not expect any material impact on its results of operations, financial position or cash flows upon adoption.

In June 2009, the FASB issued ASC No. 105 (former SFAS No. 168, *"The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles"*). The FASB Accounting Standards Codification ("Codification") is the exclusive authoritative reference for US GAAP recognized by the FASB and applied by nongovernmental entities, except for SEC rules and interpretive releases, which are also authoritative US GAAP for SEC registrants. The change established by ASC No. 105 divides nongovernmental US GAAP into authoritative Codification and guidance that is not authoritative. The contents of the Codification carry the same level of authority, eliminating the four-level US GAAP hierarchy previously set forth in SFAS No. 162. The Codification supersedes all non-SEC accounting and reporting standards. All other non-grandfathered, non-SEC accounting literature not included in the Codification became nonauthoritative. This Statement is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Group adopted ASC No. 105 starting from the third quarter of 2009. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In December 2008, the FASB amended ASC Nos. 310, 320, 323, 405, 460, 470, 712, 715, 810, 815, 860, 954 and 958 (former FSP FAS 140-4 and FIN 46(R)-8, *"Disclosures about Transfers of Financial Assets and Interest in Variable Interest Entities"*). It requires additional disclosures about transfers of financial assets and requires public entities, including sponsors that have a variable interest in a variable interest entity, to provide additional disclosures about their involvement with variable interest entities. The Group adopted new provisions starting from the fourth quarter of 2008. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In March 2008, the FASB issued ASC No. 815 (former SFAS No. 161, *"Disclosures about Derivative Instruments and Hedging Activities"*). This ASC improves financial reporting about derivative instruments and hedging activities by enhanced disclosures of their effects on an entity's financial position, financial performance and cash flows. The Group adopted the provisions of ASC No. 815 starting from the first quarter of 2009. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In December 2007, the FASB issued ASC No. 805 (former SFAS No. 141 (Revised), *"Business combinations"*). This ASC applies to all transactions in which an entity obtains control of one or more businesses. In April 2009, this ASC was amended and requires an entity to recognize the total fair value of assets acquired and liabilities assumed in a business combination; to recognize and measure the goodwill acquired in the business combination or gain from a bargain purchase and modifies the disclosure requirements. The Group adopted the provisions of ASC No. 805 for business combinations for which the acquisition date is after December 31, 2008. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In December 2007, the FASB issued ASC No. 810 (former SFAS No. 160, *"Noncontrolling Interests in Consolidated Financial Statements – an amendment of*

ARB No. 51"). This ASC applies to all entities that prepare consolidated financial statements (except not-for-profit organizations) and affects those which have an outstanding noncontrolling interest (or minority interest) in their subsidiaries or which have to deconsolidate a subsidiary. This ASC changes the classification of a non-controlling interest; establishing a single method of accounting for changes in the parent company's ownership interest that does not result in deconsolidation and requires a parent company to recognize a gain or loss when a subsidiary is deconsolidated. The Group prospectively adopted the provisions of ASC No. 810 in the first quarter of 2009, except for the presentation and disclosure requirements which were applied retrospectively. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In February 2007, the FASB issued ASC Nos. 470, 825 and 954 (former SFAS No. 159, *"The Fair Value Option for Financial Assets and Financial Liabilities"*). These ASC expands the possibility of using fair value measurements and permits enterprises to choose to measure certain financial assets and financial liabilities at fair value. Enterprises shall report unrealized gains and losses on items for which the fair value option has been elected in earnings in each subsequent period. The Group adopted the provisions of ASC Nos. 470, 825 and 954 in the first quarter of 2008 and elected not to use the fair value option for its financial assets and financial liabilities not already carried at fair value in accordance with other standards. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In September 2006, the FASB issued ASC No. 820 (former SFAS No. 157, *"Fair Value Measurements"*), which establishes a single authoritative definition of fair value, sets out a framework for measuring fair value and requires additional disclosures about fair value measurements. Effective January 1, 2009, the Group fully adopted ASC No. 820. Because there usually is a lack of quoted market prices for long-lived assets, the Group determines fair value using the present value of estimated future net cash flows from using these assets or by using historical data of market transactions with similar assets where possible. Fair value used in the initial recognition of asset retirement obligations is determined using the present value of expected future dismantlement costs, which are estimated based on the costs for dismantlement services for similar assets providing by third parties. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

Note 3. Cash and cash equivalents

	As of December 31	
	2009	2008
Cash held in Russian rubles	557	444
Cash held in other currencies	1,384	1,425
Cash of a banking subsidiary in other currencies	131	132
Cash held in related party banks in Russian rubles	174	182
Cash held in related party banks in other currencies	28	56
TOTAL CASH AND CASH EQUIVALENTS	2,274	2,239

Note 4. Non-cash transactions

The consolidated statement of cash flows excludes the effect of non-cash transactions, which are described in the following table:

	2009	2008	2007
Non-cash investing activity	20	29	36
Non-cash acquisitions	100	1,969	–
Settlement of stock-based compensation plan liability	–	–	537
TOTAL NON-CASH TRANSACTIONS	120	1,998	573

The following table shows the effect of non-cash transactions on investing activity:

	2009	2008	2007
Net cash used in investing activity	8,923	13,559	9,715
Non-cash acquisitions	100	1,969	–
Non-cash investing activity	20	29	36
TOTAL INVESTING ACTIVITY	9,043	15,557	9,751

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Note 5. Accounts and notes receivable, net

	As of December 31	
	2009	2008
Trade accounts and notes receivable (net of provisions of $191 million and $133 million as of December 31, 2009 and 2008, respectively)	4,389	3,466
Current VAT and excise recoverable	1,205	855
Other current accounts receivable (net of provisions of $41 million and $38 million as of December 31, 2009 and 2008, respectively)	341	748
TOTAL ACCOUNTS AND NOTES RECEIVABLE	5,935	5,069

Note 6. Inventories

	As of December 31	
	2009	2008
Crude oil and petroleum products	4,391	2,693
Materials for extraction and drilling	387	439
Materials and supplies for refining	37	35
Other goods, materials and supplies	617	568
TOTAL INVENTORIES	5,432	3,735

Note 7. Investments

	As of December 31	
	2009	2008
Investments in equity method affiliates and joint ventures	4,754	2,988
Long-term loans given by non-banking subsidiaries	1,176	251
Other long-term investments	14	30
TOTAL LONG-TERM INVESTMENTS	5,944	3,269

Investments in "equity method" affiliates and corporate joint ventures

The summarized financial information below is in respect of equity method affiliates and corporate joint ventures. The companies are primarily engaged in crude oil exploration, production, marketing and distribution operations in the Russian Federation, crude oil production and marketing in Kazakhstan, and refining operations in Europe.

	2009		2008		2007	
	Total	Group's share	Total	Group's share	Total	Group's share
Revenues	5,139	2,275	4,590	2,144	2,930	1,382
Income before income taxes	1,305	478	1,602	807	1,398	650
Less income taxes	(407)	(127)	(869)	(432)	(605)	(303)
NET INCOME	898	351	733	375	793	347

	As of December 31 2009		As of December 31 2008	
	Total	Group's share	Total	Group's share
Current assets	6,796	1,524	2,023	982
Property, plant and equipment	18,877	5,284	5,872	2,841
Other non-current assets	607	240	544	269
Total assets	**26,280**	**7,048**	**8,439**	**4,092**
Short-term debt	442	274	158	47
Other current liabilities	3,982	817	1,188	557
Long-term debt	7,769	732	890	392
Other non-current liabilities	1,633	471	220	108
NET ASSETS	12,454	4,754	5,983	2,988

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

In December 2009, the Group acquired the remaining a 46.0% interest in its equity affiliate LUKARCO B.V. for $1.6 billion, thereby increasing the ownership stake to 100%. LUKARCO B.V. is a holding company, which owns a 5% share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, and a 12.5% share in the Caspian Pipeline Consortium (CPC), which carries Kazakhstani and Russian oil to Novorossiysk marine terminal. Therefore the Group increased the ownership in Tengizchevroil from 2.7% to 5% and the ownership in CPC from 6.75% to 12.5%. The first installment in the amount of $300 million was paid in December 2009; the remaining amount should be paid no later than two years after the acquisition. The Group is using the equity method of accounting for investments in Tengizchevroil and CPC.

In June 2009, a Group company entered into an agreement with Total to acquire a 45% interest in the TRN refinery in the Netherlands. The transaction was finalized in September 2009 in the amount of approximately $700 million. The Group supplies crude oil and market refined products in line with its equity stake in the refinery. The refinery has the flexibility to process Urals blend crude oil as well as significant volumes of straight-run fuel oil and vacuum gasoil, which will allow the Group to integrate the plant into its crude oil supply and refined products marketing operations. This plant with a Nelson complexity index of 9.8 has an annual topping capacity of 7.9 million tonnes and an annual capacity of a hydro-cracking unit of approximately 3.4 million tonnes. This acquisition was made in accordance with the Group's plans to develop its refining capacity in Europe.

In June 2008, a Group company signed an agreement with ERG S.p.A. to establish a joint venture to operate the ISAB refinery complex in Priolo, Italy. In December 2008, the Group completed the acquisition of a 49% stake in the joint venture for €1.45 billion (approximately $1.83 billion) and paid €600 million (approximately $762 million) as a first installment. The remaining amount was paid in February 2009. The seller has a put option, the effect of which would be to increase the Group's stake in the company operating the ISAB refinery complex up to 100%. As of December 31, 2009, the fair value of this option for the Group is zero. The agreement states that each partner is responsible for procuring crude oil and marketing refined products in line with its equity stake in the joint venture. The ISAB refinery complex has the flexibility to process Urals blend crude oil, and the Group integrated its share of the ISAB refinery complex capacity into its crude oil supply and refined products marketing operations. The ISAB refinery complex includes three jetties and storage tanks totaling 3,700 thousand cubic meters and has an annual refining capacity of 16 million tonnes.

Note 8. Property, plant and equipment and asset retirement obligations

	At cost		Net	
	As of December 31, 2009	As of December 31, 2008	As of December 31, 2009	As of December 31, 2008
Exploration and Production:				
Western Siberia	23,465	21,663	13,878	12,784
European Russia	24,908	23,111	17,761	17,103
International	6,371	5,910	5,170	5,009
Total	**54,744**	**50,684**	**36,809**	**34,896**
Refining, Marketing, Distribution and Chemicals:				
Western Siberia	6	122	5	107
European Russia	10,228	9,752	6,923	6,829
International	6,849	6,462	4,783	4,633
Total	**17,083**	**16,336**	**11,711**	**11,569**
Other:				
Western Siberia	186	178	94	89
European Russia	3,951	3,618	3,491	3,385
International	189	200	123	149
Total	**4,326**	**3,996**	**3,708**	**3,623**
TOTAL PROPERTY, PLANT AND EQUIPMENT	76,153	71,016	52,228	50,088

In December 2009, the Company performed a regular annual impairment test of its exploration and production assets. The test was based on geological models and development programs, which are revised on a regular basis. As a result of the test, the Company recognized an impairment loss of $238 million for certain properties in the Timan-Pechora and Central European regions of Russia. The fair value of these assets was determined using the present value of the expected cash flows. The Group also recognized an impairment loss of $63 million related to the project in Iran due to incapability of undertaking further works because of the threat of economic sanctions of the US Government.

In June 2008, the Company performed an impairment test of certain exploration and production assets located in oil fields in the Timan-Pechora region of Russia, due to a revision of geological models. The revision resulted in a reduction of planned development activities on these oil fields. The fair value of these assets was determined using the present value of the expected cash flows. As a result, the Company recognized an impairment loss of $156 million. In December 2008, the Group recognized an impairment loss of $58 million relating to retail petrol stations in the USA.

As of December 31, 2009 and 2008, the asset retirement obligations amounted to $1,199 million and $728 million, respectively, of which $10 million was included in "Other current liabilities" in the consolidated balance sheets as of each balance sheet date.

During 2009 and 2008, asset retirement obligations changed as follows:

	2009	2008
Asset retirement obligations as of January 1	728	821
Accretion expense	63	78
New obligations	146	54
Changes in estimates of existing obligations	311	(88)
Spending on existing obligations	(7)	(8)
Property dispositions	(13)	(3)
Foreign currency translation and other adjustments	(29)	(126)
ASSET RETIREMENT OBLIGATIONS AS OF DECEMBER 31	1,199	728

The asset retirement obligations incurred during 2009 and 2008 were Level 3 (unobservable inputs) fair value measurements.

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Note 9. Goodwill and other intangible assets

The carrying value of goodwill and other intangible assets as of December 31, 2009 and 2008 was as follows:

	As of December 31	
	2009	2008
Amortized intangible assets		
Software	419	500
Licenses and other assets	465	335
Goodwill	769	324
TOTAL GOODWILL AND OTHER INTANGIBLE ASSETS	1,653	1,159

All goodwill amounts relate to the refining, marketing and distribution segment.

In the fourth quarter of 2009, the Group recognized goodwill related to acquisitions of a 100% interest in the Akpet group, 100% interests in OOO Smolenskneftesnab, OOO IRT Investment, OOO PM Invest and OOO Retailer House and 100% interests in ZAO Association Grand and OOO Mega Oil M in the amount of $114 million, $165 million and $196 million, respectively (refer to Note 16. Business combinations).

In December 2008, the Group recognized an impairment loss of $100 million relating to goodwill on the acquisition of Beopetrol due to the change in the economic environment. Beopetrol is a marketing and distribution company operating a chain of retail petrol stations in Serbia. The fair value of Beopetrol was determined using the present value of the expected cash flows.

Note 10. Short-term borrowings and current portion of long-term debt

	As of December 31	
	2009	2008
Short-term borrowings from third parties	442	2,301
Short-term borrowings from related parties	77	–
13,50% Russian ruble bonds	496	–
Current portion of long-term debt	1,043	931
TOTAL SHORT-TERM BORROWINGS AND CURRENT PORTION OF LONG-TERM DEBT	2,058	3,232

Short-term borrowings from third parties are unsecured and include amounts repayable in US dollars of $282 million and $1,529 million, amounts repayable in Euro of $76 million and $676 million and amounts repayable in Russian rubles of $18 million and $70 million as of December 31, 2009 and 2008, respectively. The weighted-average interest rate on short-term borrowings from third parties was 2.02% and 5.15% per annum as of December 31, 2009 and 2008, respectively.

Russian ruble bonds

In June 2009, the Company issued 15 million short-term stock exchange bonds with a face value of 1,000 Russian rubles each. Bonds were placed at the face value with a maturity of 364 days. The coupon yield is 13.5% per annum and is paid at the maturity date.

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Note 11. Long-term debt

	As of December 31	
	2009	2008
Long-term loans and borrowings from third parties (including loans from banks in the amount of $3,967 million and $3,333 million as of December 31, 2009 and 2008, respectively)	4,043	3,384
Long-term loans and borrowings from related parties	1,939	2,165
6.375% US dollar bonds, maturing 2014	895	-
6.356% US dollar bonds, maturing 2017	500	500
7.250% US dollar bonds, maturing 2019	595	-
6.656% US dollar bonds, maturing 2022	500	500
7.25% Russian ruble bonds, maturing 2009	-	204
7.10% Russian ruble bonds, maturing 2011	265	272
8.00% Russian ruble bonds, maturing 2012	-	8
13.35% Russian ruble bonds, maturing 2012	827	-
9.20% Russian ruble bonds, maturing 2012	331	-
7.40% Russian ruble bonds, maturing 2013	198	204
Capital lease obligations	215	271
Total long-term debt	10,308	7,508
Current portion of long-term debt	(1,043)	(931)
TOTAL NON-CURRENT PORTION OF LONG-TERM DEBT	**9,265**	**6,577**

Long-term loans and borrowings

Long-term loans and borrowings from third parties include amounts repayable in US dollars of $3,493 million and $2,844 million, amounts repayable in Euro of $487 million and $375 million and amounts repayable in Russian rubles of $42 million and $112 million as of December 31, 2009 and 2008, respectively. This debt has maturity dates from 2010 through 2021. The weighted-average interest rate on long-term loans and borrowings from third parties was 2.77% and 4.09% per annum as of December 31, 2009 and 2008, respectively. A number of long-term loan agreements contain certain financial covenants due levels of which are being met by the Group. Approximately 15% of total long-term debt is secured by export sales and property, plant and equipment.

The Company has a secured loan agreement with Deutche Bank AG with an outstanding amount of $1,200 million as of December 31, 2009, maturing up to 2012. Borrowings under this agreement bear interest at three month LIBOR plus 4.0% per annum.

A Group company has an unsecured syndicated loan agreement with an outstanding amount of $860 million as of December 31, 2009, with maturity dates up to 2013. The loan was arranged by ABN AMRO Bank, Banco Bilbao Vizcaya Argentaria, BNP Paribas, The Bank of Tokyo-Mitsubishi UFJ, ING Bank, Mizuho Corporate Bank and WestLB. Borrowings under this agreement bear interest from three month LIBOR plus 0.85% to three month LIBOR plus 0.95% per annum.

Two Group companies have unsecured loan agreements with an outstanding amount of $424 million as of December 31, 2009, maturing up to 2011. The loans were arranged by ABN AMRO Bank, The Bank of Tokyo-Mitsubishi UFJ, Barclays Capital, BNP Paribas, Citibank, Dresdner Kleinwort, ING Bank and WestLB. Borrowings under these agreements bear interest at three month LIBOR plus 3.25% per annum.

The Company has an unsecured syndicated loan agreement with the European Bank for Reconstruction and Development with an outstanding amount of $258 million as of December 31, 2009, maturing up to 2017. Borrowings under this agreement bear interest from six month LIBOR plus 0.45% to six month LIBOR plus 0.65% per annum.

A Group company has a secured loan agreement, arranged by Credit Suisse, supported by an Overseas Private Investment Corporation guarantee, with an outstanding amount of $175 million as of December 31, 2009. Borrowings under this agreement bear interest at six month LIBOR plus 4.8% per annum and have maturity dates up to 2015.

A Group company has an unsecured loan agreement with Citibank with an outstanding amount of $129 million as of December 31, 2009, maturing up to 2019. Borrowings under this agreement bear interest at euribor plus 0.125% per annum.

The Company has an unsecured syndicated loan agreement, arranged by ABN AMRO Bank and CALYON with an outstanding amount of $125 million as of December 31, 2009, maturing up to 2012. Borrowings under this agreement bear interest at three month LIBOR plus 0.40% per annum.

A Group company has an unsecured loan agreement with BNP Paribas with an outstanding amount of $119 million as of December 31, 2009, maturing up to 2018. Borrowings under this agreement bear interest at six month euribor plus 0.15% per annum.

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

A Group company has an unsecured loan agreement with Citibank with an outstanding amount of $100 million as of December 31, 2009, maturing in 2011. Borrowings under this agreement bear interest at one month LIBOR plus 0.90% per annum.

As of December 31, 2009, the Group has a number of other loan agreements with fixed rates with a number of banks and other organizations totaling $239 million, maturing from 2010 to 2021. The weighted average interest rate under these loans was 4.12% per annum.

As of December 31, 2009, the Group has a number of other floating rate loan agreements with a number of banks and other organizations totaling $414 million, maturing from 2010 to 2017. The weighted average interest rate under these loans was 2.16% per annum.

A Group company has a number of loan agreements nominated in Russian rubles with ConocoPhillips, the Group's related party, with an outstanding amount of $1,939 million as of December 31, 2009. This amount includes $1,660 million loaned by ConocoPhillips to a joint venture OOO Narianmarneftegaz ("NMNG") (refer to Note 17. Consolidation of Variable Interest Entity). Borrowings under these agreements bear interest at fixed rates ranging from 6.8% to 8.2% per annum and have maturity dates up to 2038. These agreements are a part of the Company's broad-based strategic alliance with ConocoPhillips and this financing is used to develop oil production and the distribution infrastructure in the Timan-Pechora region of the Russian Federation.

US dollar bonds

In November 2009, a Group company issued two tranches of non-convertible bonds totaling $1.5 billion. The first tranche totaling $900 million with a coupon yield of 6.375% per annum was placed with a maturity of 5 years at a price of 99.474% of the bond's face value. The resulting yield to maturity for the first tranche is 6.500%. The second tranche totaling $600 million with a coupon yield of 7.250% per annum was placed with a maturity of 10 years at a price of 99.127% of the bond's face value. The resulting yield to maturity for the second tranche is 7.375%. These tranches have a half year coupon period.

In June 2007, a Group company issued non-convertible bonds totaling $1 billion. $500 million were placed with a maturity of 10 years and a coupon yield of 6.356% per annum. Another $500 million were placed with a maturity of 15 years and a coupon yield of 6.656% per annum. All bonds were placed at the face value and have a half year coupon period.

Russian ruble bonds

In December 2009, the Company issued 10 million stock exchange bonds with a face value of 1,000 Russian rubles each. Bonds were placed at the face value with a maturity of 1,092 days. The bonds have a 182 days' coupon period and bear interest at 9.20% per annum.

In August 2009, the Company issued 25 million stock exchange bonds with a face value of 1,000 Russian rubles each. Bonds were placed at the face value with a maturity of 1,092 days. The bonds have a 182 days' coupon period and bear interest at 13.35% per annum.

In January 2007, OAO UGK TGK-8 ("TGK-8"), a subsidiary acquired in 2008 (refer to Note 16. Business combinations) issued 3.5 million non-convertible bonds with a face value of 1,000 Russian rubles each. These bonds were placed at the face value with a maturity of 5 years, with a coupon yield of 8.0% per annum and a half year coupon period. By the end of May 2009, TGK-8 redeemed all issued bonds in accordance with the conditions of the bond issue.

In December 2006, the Company issued 14 million non-convertible bonds with a face value of 1,000 Russian rubles each. Eight million bonds were placed with a maturity of 5 years and a coupon yield of 7.10% per annum and six million bonds were placed with a maturity of 7 years and a coupon yield of 7.40% per annum. All bonds were placed at the face value and have a half year coupon period.

In November 2004, the Company issued 6 million non-convertible bonds with a face value of 1,000 Russian rubles each, maturing on November 23, 2009. The bonds had a half year coupon period and beard interest at 7.25% per annum. In November 2009, the Company redeemed all issued bonds in accordance with the conditions of the bond issue.

Maturities of long-term debt

Annual maturities of total long-term debt during the next five years, including the portion classified as current, are $1,043 million in 2010, $1,890 million in 2011, $2,105 million in 2012, $524 million in 2013, $1,094 million in 2014 and $3,652 million thereafter.

Note 12. Taxes

The Group is taxable in a number of jurisdictions within and outside of the Russian Federation and, as a result, is subject to a variety of taxes as established under the statutory provisions of each jurisdiction.

The total cost of taxation to the Group is reported in the consolidated statement of income as "Total income tax expense" for income taxes, as "Excise and export tariffs" for excise taxes, export tariffs and petroleum products sales taxes and as "Taxes other than income taxes" for other types of taxation. In each category taxation is made up of taxes levied at various rates in different jurisdictions.

Until January 1, 2009, operations in the Russian Federation were subject to a Federal income tax rate of 6.5% and a regional income tax rate that varied from 13.5% to 17.5% at the discretion of the individual regional administration. Starting on January 1, 2009, the Federal income tax rate is 2.0% and regional income tax rate varies from 13.5% to 18.0%. The Group's foreign operations are subject to taxes at the tax rates applicable to the jurisdictions in which they operate.

As of January 1, 2009 and 2008, and during 2009, 2008 and 2007, the Group did not have any unrecognized tax benefits and thus, no interest and penalties related to unrecognized tax benefits were accrued. The Group's policy is to record interest and penalties related to unrecognized tax benefits as components of income tax expense. In addition, the Group does not expect that the amount of unrecognized tax benefits will change significantly within the next 12 months.

The Company and its Russian subsidiaries file standalone income tax returns in Russia. With a few exceptions, income tax returns in Russia are open to examination by the Russian tax authorities for the tax years beginning in 2007.

There are not currently, and have not been during the three years ended December 31, 2009, any provisions in the taxation legislation of the Russian Federation to permit the Group to reduce taxable profits in a Group company by offsetting tax losses in another Group company against such profits. Tax losses of a Group company in the Russian Federation may, however, be used fully or partially to offset taxable profits in the same company in any of the ten years following the year of loss.

Domestic and foreign components of income before income taxes were:

	2009	2008	2007
Domestic	9,013	12,767	11,699
Foreign	50	(73)	1,316
INCOME BEFORE INCOME TAXES	9,063	12,694	13,015

Domestic and foreign components of income taxes were:

	2009	2008	2007
Current			
Domestic	1,677	3,614	2,940
Foreign	245	553	470
Current income tax expense	**1,922**	**4,167**	**3,410**
Deferred			
Domestic	98	(523)	77
Foreign	(26)	(177)	(38)
Deferred income tax expense (benefit)	**72**	**(700)**	**39**
TOTAL INCOME TAX EXPENSE	1,994	3,467	3,449

The following table is a reconciliation of the amount of income tax expense that would result from applying the Russian combined statutory income tax rate to income before income taxes to total income taxes:

	2009	2008	2007
Income before income taxes	**9,063**	**12,694**	**13,015**
Notional income tax at Russian statutory rate	1,813	3,047	3,123
Increase (reduction) in income tax due to:			
Non-deductible items, net	252	792	372
Foreign rate differences	68	159	84
Effect of enacted tax rate changes	–	(299)	–
Domestic regional rate differences	(251)	(261)	(237)
Change in valuation allowance	112	29	107
TOTAL INCOME TAX EXPENSE	1,994	3,467	3,449

Taxes other than income taxes were:

	2009	2008	2007
Mineral extraction tax	5,452	12,267	8,482
Social taxes and contributions	399	512	442
Property tax	470	405	313
Other taxes and contributions	153	280	130
TAXES OTHER THAN INCOME TAXES	6,474	13,464	9,367

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Deferred income taxes are included in the consolidated balance sheets as follows:

	As of December 31	
	2009	2008
Other current assets	66	92
Deferred income tax assets – non-current	549	521
Other current liabilities	(50)	(49)
Deferred income tax liabilities – non-current	(2,080)	(2,116)
NET DEFERRED INCOME TAX LIABILITY	(1,515)	(1,552)

The following tables set out the tax effects of each type of temporary differences which give rise to deferred income tax assets and liabilities:

	As of December 31	
	2009	2008
Accounts receivable	42	50
Long-term liabilities	295	208
Inventories	5	17
Property, plant and equipment	209	226
Accounts payable	28	10
Operating loss carry forwards	555	578
Other	132	166
Total gross deferred income tax assets	1,266	1,255
Less valuation allowance	(397)	(285)
Deferred income tax assets	**869**	**970**
Property, plant and equipment	(2,189)	(2,226)
Accounts payable	(6)	(4)
Accounts receivable	(7)	(21)
Long-term liabilities	(58)	(118)
Inventories	(68)	(57)
Investments	(16)	–
Other	(40)	(96)
Deferred income tax liabilities	**(2,384)**	**(2,522)**
NET DEFERRED INCOME TAX LIABILITY	(1,515)	(1,552)

As a result of acquisitions and business combinations during 2009 and 2008 the Group recognized a net deferred tax liability of $35 million and $891 million, respectively. Also, in 2009, the Group finalized purchase price allocation related to prior year acquisitions which resulted in a $140 million decrease of deferred tax liability.

As of December 31, 2009, retained earnings of foreign subsidiaries included $17,261 million for which deferred taxation has not been provided because remittance of the earnings has been indefinitely postponed through reinvestment and, as a result, such amounts are considered to be indefinitely invested. It is not practicable to estimate the amount of additional taxes that might be payable on such undistributed earnings.

In accordance with ASC No. 830 (former SFAS No. 52, *"Foreign currency translation"*) and ASC No. 740 (former SFAS No. 109, *"Accounting for Income Taxes"*) deferred tax assets and liabilities are not recognized for the changes in exchange rate effects resulting from the translation of transactions and balances from the Russian rubles to the US dollar using historical exchange rates. Also, in accordance with ASC No. 740, no deferred tax assets or liabilities are recognized for the effects of the related statutory indexation of property, plant and equipment.

Based upon the levels of historical taxable income and projections for future taxable income over the periods in which the deferred income tax assets are deductible, management believes it is more likely than not that Group companies will realize the benefits of the deductible temporary differences and loss carry forwards, net of existing valuation allowances as of December 31, 2009 and 2008.

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

As of December 31, 2009, the Group had operating loss carry forwards of $2,273 million of which $757 million expire during 2010, $82 million expire during 2011, $196 million expire during 2012, $322 million expire during 2013, $58 million expire during 2014, $58 million expire during 2015, $9 million expire during 2016, $2 million expire during 2017, $12 million expire during 2018, $31 million expire during 2019, $1 million expire during 2020, $67 million expire during 2026, $77 million expire during 2027, $202 million expire during 2028, $2 million expire during 2035 and $397 million have an indefinite carry forward.

Note 13. Pension benefits

The Company sponsors a postretirement benefits program. The primary component of the post employment and post retirement benefits program is a defined benefit pension plan that covers the majority of the Group's employees. This plan is administered by a non-state pension fund, LUKOIL-GARANT, and provides pension benefits primarily based on years of service and final remuneration levels. The Company also provides several long-term employee benefits such as death-in-service benefit and lump-sum payments upon retirement of a defined benefit nature and other defined benefits to certain old age and disabled pensioners who have not vested any pensions under the pension plan.

The Company's pension plan primarily consists of a defined benefit plan enabling employees to contribute a portion of their salary to the plan and at retirement to receive a lump sum amount from the Company equal to all past contributions made by the employee up to 2% (prior to 2009 – 7%) of their annual salary. Employees also have the right to receive upon retirement the benefits accumulated under the previous pension plan that was replaced in December 2003. These benefits have been fixed and included in the benefit obligation as of December 31, 2009 and 2008. The amount was determined primarily based on a formula including past pensionable service and relative salaries as of December 31, 2003.

The Company uses December 31 as the measurement date for its post employment and post retirement benefits program. An independent actuary has assessed the benefit obligations as of December 31, 2009 and 2008.

The following table provides information about the benefit obligations and plan assets as of December 31, 2009 and 2008. The benefit obligations below represent the projected benefit obligation of the pension plan.

	2009	2008
Benefit obligations		
Benefit obligations as of January 1	288	328
Effect of exchange rate changes	(7)	(56)
Service cost	17	22
Interest cost	23	19
Plan amendments	6	21
Actuarial gain	(3)	(5)
Acquisitions	8	1
Benefits paid	(30)	(42)
Curtailment gain	(11)	–
BENEFIT OBLIGATIONS AS OF DECEMBER 31	291	288
Plan assets		
Fair value of plan assets as of January 1	88	108
Effect of exchange rate changes	(1)	(18)
Return on plan assets	12	6
Employer contributions	45	35
Divestiture	(6)	(1)
Benefits paid	(30)	(42)
FAIR VALUE OF PLAN ASSETS AS OF DECEMBER 31	108	88
Funded status	(183)	(200)
Amounts recognized in the consolidated balance sheet as of December 31, 2009 and 2008		
Accrued benefit liabilities included in "Other long-term liabilities"	(143)	(164)
Accrued benefit liabilities included in "Other current liabilities"	(40)	(36)

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Weighted average assumptions used to determine benefit obligations as of December 31, 2009 and 2008:

	2009	2008
Discount rate	8.70%	9.00%
Rate of compensation increase	8.10%	8.61%

Weighted average assumptions used to determine net periodic benefit costs for the year ended December 31, 2009 and 2008:

	2009	2008
Discount rate	9.00%	6.34%
Rate of compensation increase	8.61%	8.12%
Expected rate of return on plan assets	10.89%	10.49%

Included in accumulated other comprehensive loss as of December 31, 2009 and 2008, are the following before-tax amounts that have not yet been recognized in net periodic benefit cost:

	2009	2008
Unamortized prior service cost	96	92
Unrecognized actuarial gain	(10)	(5)
TOTAL COSTS	86	87

Amounts recognized in other comprehensive loss during the year ended December 31, 2009 and 2008:

	2009	2008
Additional gain arising during the period	(5)	(1)
Additional prior service cost from plan amendment	6	21
Re-classified prior service cost amortization	(2)	(11)
NET AMOUNT RECOGNIZED FOR THE PERIOD	(1)	9

The real returns on bonds and equities are based on what is observed in the international markets over extended periods of time. In the calculation of the expected return on assets no use is made of the historical returns LUKOIL-GARANT has achieved.

In addition to the plan assets, LUKOIL-GARANT holds assets in the form of an insurance reserve. The purpose of this insurance reserve is to satisfy pension obligations should the plan assets not be sufficient to meet pension obligations. The Group's contributions to the pension plan are determined without considering the assets in the insurance reserve.

The plans are funded on a discretionary basis through a solidarity account, which is held in trust with LUKOIL-GARANT. LUKOIL-GARANT does not allocate separately identifiable assets to the Group or its other third party clients. All funds of plan assets and other individual pension accounts are managed as a pool of investments.

The asset allocation of the investment portfolio maintained by LUKOIL-GARANT for the Group and its clients was as follows:

Type of assets	As of December 31	
	2009	2008
Promissory notes of Russian issuers	3%	6%
Russian corporate bonds	25%	36%
Russian municipal bonds	4%	2%
Bank deposits	42%	22%
Equity securities of Russian issuers	8%	10%
Shares of OAO LUKOIL	2%	2%
Shares in investment funds	14%	20%
Other assets	2%	2%
	100%	100%

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

The investment strategy employed by LUKOIL-GARANT includes an overall goal to attain a maximum investment return, while guaranteeing the principal amount invested. The strategy is to invest with a medium-term perspective while maintaining a level of liquidity through proper allocation of investment assets. Investment policies include rules and limitations to avoid concentrations of investments.

The investment portfolio is primarily comprised of investments: bank deposits, securities with fixed yield and equity securities. The securities with fixed yield include mainly high yield corporate bonds and promissory notes of banks with low and medium risk ratings. Maturities range from one to three years.

Components of net periodic benefit cost were as follows:

	2009	2008	2007
Service cost	17	22	15
Interest cost	23	19	16
Less expected return on plan assets	(10)	(11)	(9)
Amortization of prior service cost	2	11	8
Actuarial gain	–	–	(1)
Curtailment gain	(11)	–	–
TOTAL NET PERIODIC BENEFIT COST	21	41	29

Total employer contributions for 2010 are expected to be $40 million. An amount of $13 million before-tax is included in other comprehensive income and expected to be recognized in the net periodic benefit cost in 2010.

The following benefit payments, which reflect expected future services, as appropriate, are expected to be paid:

	2010	2011	2012	2013	2014	5-year period 2010-2014	5-year period 2015-2019
Pension benefits	54	13	14	13	13	107	49
Other long-term employee benefits	40	19	19	19	20	117	106
TOTAL EXPECTED BENEFITS TO BE PAID	94	32	33	32	33	224	155

Note 14. Stockholders' equity

Common stock

	As of December 31, 2009 (thousands of shares)	As of December 31, 2008 (thousands of shares)
Authorized and issued common stock, par value of 0.025 Russian rubles each	850,563	850,563
Common stock held by subsidiaries, not considered as outstanding	(82)	(82)
Treasury stock	(3,836)	(3,836)
OUTSTANDING COMMON STOCK	846,645	846,645

Dividends and dividend limitations

Profits available for distribution to common stockholders in respect of any reporting period are determined by reference to the statutory financial statements of the Company prepared in accordance with the laws of the Russian Federation and denominated in Russian rubles. Under Russian Law, dividends are limited to the net profits of the reporting year as set out in the statutory financial statements of the Company. These laws and other legislative acts governing the rights of shareholders to receive dividends are subject to various interpretations.

The Company's net profits were 45,148 million Russian rubles, 66,926 million Russian rubles and 64,917 million Russian rubles respectively for 2009, 2008 and 2007, pursuant to the statutory financial statements, which at the US dollar exchange rates as of December 31, 2009, 2008 and 2007, amounted to $1,493 million, $2,278 million and $2,645 million, respectively.

At the annual stockholders' meeting on June 25, 2009, dividends were declared for 2008 in the amount of 50.00 Russian rubles per common share, which at the date of the meeting was equivalent to $1.61.

At the annual stockholders' meeting on June 26, 2008, dividends were declared for 2007 in the amount of 42.00 Russian rubles per common share, which at the date of the meeting was equivalent to $1.78.

At the annual stockholders' meeting on June 28, 2007, dividends were declared for 2006, in the amount of 38 Russian rubles per common share, which at the date of the decision was equivalent to $1.47.

Earnings per share

The weighted average number of outstanding common shares was 846,646 thousand shares, 840,108 thousand shares and 828,501 thousand shares for years ended December 31, 2009, 2008 and 2007, respectively. There is no potential dilution in earnings available to common stockholders and as such diluted earnings per share are not disclosed.

Note 15. Financial and derivative instruments

Fair value

The fair values of cash and cash equivalents, current accounts and notes receivable, long-term receivables and liquid securities are approximately equal to their value as disclosed in the consolidated financial statements. The fair value of long-term receivables was determined by discounting with estimated market interest rates for similar financing arrangements.

The fair value of long-term debt differs from the amount disclosed in the consolidated financial statements. The estimated fair value of long-term debt as of December 31, 2009 and 2008 was $9,976 million and $5,425 million, respectively, as a result of discounting using estimated market interest rates for similar financing arrangements. These amounts include all future cash outflows associated with the long-term debt repayments, including the current portion and interest. Market interest rates mean the rates of raising long-term debt by companies with a similar credit rating for similar tenors, repayment schedules and similar other main terms. During the year ended December 31, 2009, the Group did not have significant transactions or events that would result in nonfinancial assets and liabilities measured at fair value on a nonrecurring basis.

Derivative instruments

The Group uses financial and commodity-based derivative contracts to manage exposures to fluctuations in foreign currency exchange rates, commodity prices, or to exploit market opportunities. Since the Group is not currently using ASC Nos. 220, 310, 440 and 815 (former SFAS No. 133, *"Accounting for Derivative Instruments and Hedging Activity"*) hedge accounting, all gains and losses, realized or unrealized, from derivative contracts have been recognized in the consolidated income statement.

ASC No. 815 requires purchase and sales contracts for commodities that are readily convertible to cash (e.g., crude oil, natural gas and gasoline) to be recorded on the balance sheet as derivatives unless the contracts are for quantities the Group expects to use or sell over a reasonable period in the normal course of business (i.e., contracts eligible for the normal purchases and normal sales exception). The Group does apply the normal purchases and normal sales exception to certain long-term contracts to sell oil products. This normal purchases and normal sales exception is applied to eligible crude oil and refined product commodity purchase and sales contracts; however, the Group may elect not to apply this exception (e.g., when another derivative instrument will be used to mitigate the risk of the purchase or sale contract but hedge accounting will not be applied, in which case both the purchase or sales contract and the derivative contract mitigating the resulting risk will be recorded on the balance sheet at fair value).

The fair value hierarchy for the Group's derivative assets and liabilities accounted for at fair value on a recurring basis was:

	As of December 31, 2009				As of December 31, 2008			
	Level				Level			
	1	2	3	Total	1	2	3	Total
Assets								
Commodity derivatives	–	1,065	–	1,065	–	1,995	–	1,995
Total assets	**–**	**1,065**	**–**	**1,065**	**–**	**1,995**	**–**	**1,995**
Liabilities								
Commodity derivatives	–	(1,110)	–	(1,110)	–	(1,655)	–	(1,655)
Total liabilities	**–**	**(1,110)**	**–**	**(1,110)**	**–**	**(1,655)**	**–**	**(1,655)**
NET (LIABILITIES) ASSETS	–	(45)	–	(45)	–	340	–	340

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

The derivative values above are based on an analysis of each contract as the fundamental unit of account as required by ASC No. 820; therefore, derivative assets and liabilities with the same counterparty are not reflected net where the legal right of offset exists. Gains or losses from contracts in one level may be offset by gains or losses on contracts in another level or by changes in values of physical contracts or positions that are not reflected in the table above.

Commodity derivative contracts

The Group operates in the worldwide crude oil, refined product, natural gas and natural gas liquids markets and is exposed to fluctuations in the prices for these commodities. These fluctuations can affect the Group's revenues as well as the cost of operating, investing and financing activities. Generally, the Group's policy is to remain exposed to the market prices of commodities. However, the Group uses futures, forwards, swaps and options in various markets to balance physical systems, meet customer needs, manage price exposures on specific transactions, and do a limited, immaterial amount of trading not directly related to the Group's physical business. These activities may move the Group's profile away from market average prices.

The fair value of commodity derivative assets and liabilities as of December 31, 2009 was:

	As of December 31, 2009
Assets	
Accounts receivable	1,065
Liabilities	
Accounts payable	1,110

Hedge accounting has not been used for items in the table.

As required under ASC No. 815 the amounts shown in the preceding table are presented gross (i.e., without netting assets and liabilities with the same counterparty where the right of offset and intent to net exist). Derivative assets and liabilities resulting from eligible commodity contracts have been netted in the consolidated balance sheet and are recorded as accounts receivable in the amount of $59 million and accounts payable in the amount of $104 million.

The gains and losses from commodity derivatives were included in the consolidated income statements in "Cost of purchased crude oil, gas and products" and for the years ended December 31, 2009 and 2008 were in total amount of net loss of $781 million (of which realized losses were $406 million and unrealized losses were $375 million) and net income of $902 million (of which realized gain was $502 million and unrealized gain was $400 million), respectively.

As of December 31, 2009, the net position of outstanding commodity derivative contracts, primarily to manage price exposure on underlying operations, was not significant.

Currency exchange rate derivative contracts

The Group has foreign currency exchange rate risk resulting from its international operations. The Group does not comprehensively hedge the exposure to currency rate changes, although the Group selectively hedges certain foreign currency exchange rate exposures, such as firm commitments for capital projects or local currency tax payments and dividends.

The fair value of foreign currency derivatives assets and liabilities open at December 31, 2009 was not significant.

The impact from foreign currency derivatives during the year ended December 31, 2009 on the consolidated income statement was not significant. The net position of outstanding foreign currency swap contracts as of December 31, 2009 also was not significant.

Credit risk

The Group's financial instruments that are potentially exposed to concentrations of credit risk consist primarily of cash equivalents, over-the-counter derivative contracts and trade receivables. Cash equivalents are placed in high-quality commercial paper, money market funds and time deposits with major international banks and financial institutions.

The credit risk from the Group's over-the-counter derivative contracts, such as forwards and swaps, derives from the counterparty to the transaction, typically a major bank or financial institution. Individual counterparty exposure is managed within predetermined credit limits and includes the use of cash-call margins when appropriate, thereby reducing the risk of significant non-performance. The Group also uses futures contracts, but futures have a negligible credit risk because they are traded on the New York Mercantile Exchange or the ICE Futures.

Certain of the Group's derivative instruments contain provisions that require the Group to post collateral if the derivative exposure exceeds a threshold amount. The Group has contracts with fixed threshold amounts and other contracts with variable threshold amounts that are contingent on the Group's credit rating. The variable threshold amounts typically decline for lower credit ratings, while both the variable and fixed threshold amounts typically revert to zero if the Group falls below investment grade. Cash is the primary collateral in all contracts; however, many contracts also permit the Group to post letters of credit as collateral.

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There were no derivative instruments with such credit-risk-related contingent features that were in a liability position on December 31, 2009. The Group posted $21 million in collateral in the normal course of business for the over-the-counter derivatives. If the Group's credit rating were lowered one level from its «BBB-» rating (per Standard and Poors) on December 31, 2009, and it would be below investment grade, the Group would be required to post additional collateral of $5 million to the Group's counterparties for the over-the-counter derivatives, either with cash or letters of credit. The maximum additional collateral based on the lowest downgrade would be $14 million in total.

Note 16. Business combinations

During 2009, a Group company acquired the remaining 25.2% of share capital of OAO RITEK ("RITEK") for $235 million, thereby increasing the Group's share to 100%. RITEK is a crude oil producing company operating in European Russia and Western Siberia.

In the first quarter of 2009, the Group acquired 100% interests in OOO Smolenskneftesnab, OOO IRT Investment, OOO PM Invest and OOO Retailer House for $238 million. These are holding companies, which between them own 96 petrol stations and plots of land in Moscow, the Moscow region and other regions of central European Russia. This acquisition was made in order to expand the Group's presence on the most advantageous retail market in the Russian Federation. The Group allocated $165 million to goodwill, $113 million to property, plant and equipment, $15 million to other assets, $8 million to deferred tax liability and $47 million to other liabilities. The value of property, plant and equipment was determined by an independent appraiser.

In the fourth quarter of 2008, the Group acquired 100% interests in ZAO Association Grand and OOO Mega Oil M for $493 million. ZAO Association Grand and OOO Mega Oil M are holding companies, owning 181 petrol stations in Moscow, the Moscow region and other regions of central European Russia. This acquisition was made in order to expand the Group's presence on the most advantageous retail market in the Russian Federation. The Group allocated $196 million to goodwill, $334 million to property, plant and equipment, $46 million to other assets, $14 million to deferred tax liability and $69 million to other liabilities. The value of property, plant and equipment was determined by an independent appraiser.

In March 2008, a Group company entered into an agreement with a related party, whose management and directors include members of the Group's management and Board of Directors, to acquire a 64.31% interest in TGK-8 for approximately $2,117 million. The purchase consideration partly consists of 23.55 million shares of common stock of the Company (at a market value of approximately $1,620 million). The transaction was finalized in May 2008. The following table summarizes the determined fair value of the assets acquired and liabilities assumed of TGK-8 at the date of acquisition. The value of property, plant and equipment was determined by an independent appraiser.

Cash and short-term investments	724
Other current assets	266
Property, plant and equipment	2,092
Other non-current assets	319
Total assets acquired	**3,401**
Current liabilities	(196)
Non-current deferred tax liabilities	(357)
Long-term debt	(149)
Minority interest	(582)
Total liabilities assumed	**(1,284)**
NET ASSETS ACQUIRED	2,117

From May to December 2008, a Group company acquired additional interests in TGK-8 for a total of $1,075 million. These acquisitions increased the Group's ownership to 95.53%. As a result of this additional acquisition the Group recognized property, plant and equipment and a deferred tax liability amounting to $802 million and $192 million, respectively. From January to June 2009, a Group company acquired the remaining 4.47% of share capital of TGK-8 for approximately $127 million. The acquisition increased the Group's ownership to 100%. TGK-8 is a power generating company which owns power plants located in the Astrakhan, Volgograd and Rostov regions, the Krasnodar and Stavropol Districts, and the Republic of Dagestan of the Russian Federation. This acquisition is made in accordance with the Company's plans to develop its electric power business.

In July 2008, a Group company signed an agreement to acquire a 100% interest in the Akpet group for $555 million. The transaction was finalized in November 2008. Based on the agreement there were three payments of purchase consideration: the first payment in the amount of $250 million was paid at the date of finalization; second and third deferred payments were paid in April and October 2009. The Akpet group operated 689 petrol filling stations on the basis of dealer agreements and owned eight refined product terminals, five LNG storage tanks, three jet fuel terminals and a lubricant production plant in Turkey. The Group allocated $114 million to goodwill, $271 million to intangible assets and $241 million to property, plant and equipment. The value of intangible assets and property, plant and equipment was determined by an independent appraiser.

In March 2008, a Group company entered into an agreement to acquire 75 petrol stations and storage facilities in Bulgaria for approximately $367 million. The transaction was finalized in the second quarter of 2008. The Group determined the fair value of assets acquired and as a result recognized property, plant and equipment of $367 million.

These business combinations did not have a material impact on the Group's consolidated operations for the years ended December 31, 2009 and 2008. Therefore, no pro-forma income statement information has been provided.

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Note 17. Consolidation of Variable Interest Entity

The Group and ConocoPhillips have a joint venture NMNG which develops oil reserves in the Timan-Pechora region of the Russian Federation. The Group and ConocoPhillips have equal voting rights over the joint venture's activity and effective ownership interests of 70% and 30%, respectively.

The Group determined that NMNG is a variable interest entity as the Group's voting rights are not proportionate to its ownership rights and all of NMNG's activities are conducted on behalf of the Group and ConocoPhillips, its related party. The Group is considered to be the primary beneficiary and has consolidated NMNG.

NMNG's total assets were approximately $5.9 billion and $7.1 billion as of December 31, 2009 and 2008, respectively.

The Group and ConocoPhillips agreed to provide financing to NMNG by means of long-term loans in proportion to their effective ownership interests. These loans mature from 2035 to 2038, with the option to be extended for a further 35 years with the agreement of both parties. As of December 31, 2009, borrowings under these agreements bear fixed interest in the range of 6.8% to 8.2% per annum.

As of December 31, 2009, the amount outstanding to ConocoPhillips from NMNG was $1,660 million, which consists of a number of loans with a weighted-average interest rate of 7.79% per annum. This amount is presented within "Long-term loans and borrowings from related parties".

Note 18. Financial guarantees

The Group has entered into various guarantee arrangements. These arrangements were entered into in order to optimize affiliated companies' financing terms. The undiscounted maximum amount of potential future payments for the guarantees issued in favour of equity companies was $50 million and $161 million as of December 31, 2009 and 2008, respectively.

Note 19. Commitments and contingencies

Capital expenditure, exploration and investment programs

The Group owns and operates refineries in Bulgaria (LUKOIL Neftochim Bourgas AD) and Romania (Petrotel-LUKOIL S.A.). As a result of Bulgaria and Romania joining the European Union in 2007, LUKOIL Neftochim Bourgas AD and Petrotel-LUKOIL S.A. are required to upgrade their refining plants to comply with the requirements of European Union legislation in relation to the quality of produced petroleum products and environmental protection. These requirements are stricter than those which previously existed under Bulgarian and Romanian legislation. The Group estimates the amount of future capital commitment required to upgrade LUKOIL Neftochim Bourgas AD and Petrotel-LUKOIL S.A. to be approximately $49 million and $44 million, respectively.

Under the terms of existing exploration and production license agreements in Russia the Group has to fulfill certain operations: oil and gas exploration, wells drilling, fields development, etc., and the Group also has commitments to reach a defined level of extraction on the fields. Management believes that the Group's approved annual capital expenditure budgets fully cover all the requirements of the described license obligations.

Group companies have commitments for capital expenditure contributions in the amount of $565 million related to various production sharing agreements over the next 28 years.

The Company has signed a three-year agreement for drilling services with OOO Eurasia Drilling Company. The volume of these services is based on the Group's capital construction program, which is re-evaluated on an annual basis. The Group estimates the amount of capital commitment under this agreement for 2010 to be approximately $610 million.

The Company has signed a strategic agreement for the ongoing provision of construction, engineering and technical services with ZAO Globalstroy-Engineering. The volume of these services is based on the Group's capital construction program, which is re-evaluated on an annual basis. The Group estimates the amount of capital commitment under this agreement for 2010 to be approximately $126 million.

The Group has a commitment to purchase equipment for modernization of its petrochemical refinery Karpatnaftochim Ltd., located in Ukraine, during next two years in the amount of $55 million.

The Group has a commitment to execute the capital construction program of TGK-8 (refer to Note 16. Business combinations) and under the terms of this program power plants with total capacity of 890 MW should be constructed. Currently the Group is approving certain amendments to the capital construction program, which included its extension by the end of 2013. As of December 31, 2009, the Group estimates the amount of this commitment to be approximately $944 million.

Operating lease obligations

Group companies have commitments of $974 million primarily for the lease of vessels and petroleum distribution outlets. Operating lease expenses were $185 million and $170 million during the years ended December 31, 2009 and 2008, respectively. Commitments for minimum rentals under these leases as of December 31, 2009 are as follows:

	As of December 31, 2009
2010	276
2011	172
2012	135
2013	104
2014	93
beyond	194

Insurance

The insurance industry in the Russian Federation and certain other areas where the Group has operations is in the course of development. Management believes that the Group has adequate property damage coverage for its main production assets. In respect of third party liability for property and environmental damage arising from accidents on Group property or relating to Group operations, the Group has insurance coverage that is generally higher than insurance limits set by the local legal requirements. Management believes that the Group has adequate insurance coverage of the risks, which could have a material effect on the Group's operations and financial position.

Environmental liabilities

Group companies and their predecessor entities have operated in the Russian Federation and other countries for many years and, within certain parts of the operations, environmental related problems have developed. Environmental regulations are currently under consideration in the Russian Federation and other areas where the Group has operations. Group companies routinely assess and evaluate their obligations in response to new and changing legislation.

As liabilities in respect of the Group's environmental obligations are able to be determined, they are charged against income. The likelihood and amount of liabilities relating to environmental obligations under proposed or any future legislation cannot be reasonably estimated at present and could become material. Under existing legislation, however, management believes that there are no significant unrecorded liabilities or contingencies, which could have a materially adverse effect on the operating results or financial position of the Group.

Social assets

Certain Group companies contribute to Government sponsored programs, the maintenance of local infrastructure and the welfare of their employees within the Russian Federation and elsewhere. Such contributions include assistance with the construction, development and maintenance of housing, hospitals and transport services, recreation and other social needs. The funding of such assistance is periodically determined by management and is appropriately capitalized or expensed as incurred.

Taxation environment

The taxation systems in the Russian Federation and other emerging markets where Group companies operate are relatively new and are characterized by numerous taxes and frequently changing legislation, which is often unclear, contradictory, and subject to interpretation. Often, differing interpretations exist among different tax authorities within the same jurisdictions and among taxing authorities in different jurisdictions. Taxes are subject to review and investigation by a number of authorities, which are enabled by law to impose severe fines, penalties and interest charges. In the Russian Federation a tax year remains open for review by the tax authorities during the three subsequent calendar years.

However, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation. Such factors may create taxation risks in the Russian Federation and other emerging markets where Group companies operate substantially more significant than those in other countries where taxation regimes have been subject to development and clarification over long periods.

The tax authorities in each region may have a different interpretation of similar taxation issues which may result in taxation issues successfully defended by the Group in one region being unsuccessful in another region. There is some direction provided from the central authority based in Moscow on particular taxation issues.

The Group has implemented tax planning and management strategies based on existing legislation at the time of implementation. The Group is subject to tax authority audits on an ongoing basis, as is normal in the Russian environment and other republics of the former Soviet Union, and, at times, the authorities have attempted to impose additional significant taxes on the Group. Management believes that it has adequately met and provided for tax liabilities based on its interpretation of existing tax legislation. However, the relevant tax authorities may have differing interpretations and the effects on the financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

Litigation and claims

On November 27, 2001, Archangel Diamond Corporation ("ADC"), a Canadian diamond development company, filed a lawsuit in the District Court of Denver, Colorado against OAO Archangelskgeoldobycha ("AGD"), a Group company, and the Company (together the "Defendants"). ADC alleged that the Defendants interfered with the transfer of a diamond exploration license to Almazny Bereg, a joint venture between ADC and AGD. ADC claimed total damages of approximately

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$4.8 billion, including compensatory damages of $1.2 billion and punitive damages of $3.6 billion. On October 15, 2002, the District Court dismissed the lawsuit for lack of personal jurisdiction. This ruling was upheld by the Colorado Court of Appeals on March 25, 2004. On November 21, 2005, the Colorado Supreme Court affirmed the lower courts' ruling that no specific jurisdiction exists over the Defendants. By virtue of this finding, AGD (the holder of the diamond exploration license) was dismissed from the lawsuit. The Supreme Court found, however, that the trial court made a procedural error by failing to hold an evidentiary hearing before making its ruling concerning general jurisdiction regarding the Company, which is whether the Company had systematic and continuous contacts in the State of Colorado at the time the lawsuit was filed. In a modified opinion dated December 19, 2005, the Colorado Supreme Court remanded the case to the Colorado Court of Appeals (instead of the District Court) to consider whether the lawsuit should have been dismissed on alternative grounds (i.e., forum non conveniens). On June 29, 2006, the Colorado Court of Appeals declined to dismiss the case based on forum non conveniens. The Company filed a petition for certiorari on August 28, 2006, asking the Colorado Supreme Court to review this decision. On March 5, 2007, the Colorado Supreme Court remanded the case to the District Court. On June 11, 2007, the District Court ruled it would conduct an evidentiary hearing on the issue of whether the Company is subject to general personal jurisdiction in the State of Colorado. Discovery regarding jurisdiction was commenced. On June 26, 2009, three creditors of ADC filed an Involuntary Bankruptcy Petition putting ADC into bankruptcy. ADC ultimately confirmed entry of an Order For Relief and the matter was converted to a Chapter 11 Case by order dated September 29, 2009. On November 25, 2009, after adding a claim, ADC removed the case from the Colorado District Court to the US Bankruptcy Court. On December 22, 2009, the Company filed a motion seeking to have the case remanded to the Colorado District Court. On December 31, 2009, before there was a ruling on the motion seeking remand ADC filed a motion seeking withdrawal of the reference from the bankruptcy and the case be heard by US District Court. On February 3, 2010, the US Bankruptcy Court ordered the Motion For Withdrawal Of The Reference be transferred to the US District Court for further action. All pending motions as well as discovery are stayed pending further order of the Court. Management plans to vigorously defend the matter. Management does not believe that the ultimate resolution of this matter will have a material adverse effect on the Group's financial condition.

In 2008 and 2009, the Federal Anti-monopoly Service of the Russian Federation ("FAS of Russia") issued two decisions against major Russian oil companies, including the Company and the Group's refinery plants alleging abuse of their dominant position in the oil products wholesale market of the Russian Federation.

The Moscow Arbitration Court combined all refinery plants' appeals against the first decision. The next appeal hearing was scheduled for April 8, 2010.

The second decision of FAS of Russia was appealed by the refinery plants in their local courts. On February 8, 2010, the Arbitration Court of Nizhni Novgorod Region satisfied the request of OOO LUKOIL-Nizhnegorodnefteorgsintez to recognize as illegal the decisions of FAS of Russia dated September 10, 2009 and the resolution to impose fines in the amount of $80 million. The appeals of the other refinery plants are currently suspended.

In the second half of 2008 and first half of 2009, the FAS of Russia filed claims against several Group companies in relation to violation of the anti-monopoly regulation. The companies were accused of violations primarily involving abuse of their dominant market position via setting monopolistically high retail prices in coordination with other market participants. These claims are being appealed in the courts.

The total amount of penalties assessed under the administrative law for the violation of anti-monopoly regulation by the Group in 2008-2009 is $290 million. Management believes that the Group complied with all regulatory and legal requirements and, consequently, believes that the ultimate resolution of the antimonopoly claims will lead to cancellation or significant reduction of these penalties and will not have a material adverse impact on the Group's operating results or financial condition.

The Group is involved in various other claims and legal proceedings arising in the normal course of business. While these claims may seek substantial damages against the Group and are subject to uncertainty inherent in any litigation, management does not believe that the ultimate resolution of such matters will have a material adverse impact on the Group's operating results or financial condition.

Note 20. Related party transactions

In the rapidly developing business environment in the Russian Federation, companies and individuals have frequently used nominees and other forms of intermediary companies in transactions. The senior management of the Company believes that the Group has appropriate procedures in place to identify and properly disclose transactions with related parties in this environment and has disclosed all of the relationships identified which it deemed to be significant. Related party sales and purchases of oil and oil products were primarily to and from affiliated companies and the Company's shareholder ConocoPhillips. Related party processing services were provided by affiliated refineries. Insurance services were provided by the related parties, whose management and directors include members of the Group's management.

Below are related party transactions not disclosed elsewhere in the financial statements. Refer also to Notes 3, 4, 7, 10, 11, 13, 16, 17, 18 and 21 for other transactions with related parties.

Sales of oil and oil products to related parties were $1,152 million, $436 million and $652 million for the years ended December 31, 2009, 2008 and 2007, respectively.

Other sales to related parties were $69 million, $86 million and $77 million for the years ended December 31, 2009, 2008 and 2007, respectively.

Purchases of oil and oil products from related parties were $862 million, $1,891 million and $1,363 million for the years ended December 31, 2009, 2008 and 2007, respectively.

Purchases of processing services from related parties were $539 million, nil and nil for the years ended December 31, 2009, 2008 and 2007, respectively.

Purchases of insurance services from related parties were nil, $93 million and $143 million during the years ended December 31, 2009, 2008 and 2007, respectively.

Other purchases from related parties were $28 million, $33 million and $26 million for the years ended December 31, 2009, 2008 and 2007, respectively.

Amounts receivable from related parties, including loans and advances, were $591 million and $248 million as of December 31, 2009 and 2008, respectively. Amounts payable to related parties were $97 million and $36 million as of December 31, 2009 and 2008, respectively.

Note 21. Compensation plan

During the period from 2007 to 2009, the Company had a compensation plan available to certain members of management, which is based on assigned shares and provides compensation consisting of two parts.

The first part represented annual bonuses that are based on the number of assigned shares and amount of dividend per share. The payment of these bonuses is contingent on the Group meeting certain financial KPIs in each financial year. The second is based upon the Company's common stock appreciation from 2007 to 2009, with rights vested in December 2009. The number of assigned shares is approximately 15.5 million shares. For the first part of the share plan the Group recognizes a liability based on expected dividends and number of assigned shares.

The second part of the share plan is classified as equity and the grant date fair value of the plan is estimated using the Black-Scholes-Merton option-pricing model. Related to this plan the Group recorded $105 million, $134 million and $125 million of compensation expense during the years ended December 31, 2009, 2008 and 2007, respectively, of which $20 million, $103 million and $103 million are recognized as an increase in additional paid-in capital in respective periods. Because of unfavorable market situation the conditions for exercising the second part of this share plan were not met therefore no payments or share transfers to employees took place.

In December 2009, the Company introduced a new compensation plan to certain members of management for the period from 2010 to 2012. Its conditions are similar to the conditions of the previous compensation plan. The number of assigned shares is approximately 17.3 million shares. The Group is currently finalizing the calculation of the grant date fair value of the new plan.

Note 22. Segment information

Presented below is information about the Group's operating and geographical segments for the years ended December 31, 2009, 2008 and 2007, in accordance with ASC No. 280 (former SFAS No. 131, *"Disclosures about Segments of an Enterprise and Related Information"*).

The Group has four operating segments – exploration and production; refining, marketing and distribution; chemicals and other business segments. These segments have been determined based on the nature of their operations. Management on a regular basis assesses the performance of these operating segments. The exploration and production segment explores for, develops and produces primarily crude oil. The refining, marketing and distribution segment processes crude oil into refined products and purchases, sells and transports crude oil and refined petroleum products. The chemicals segment refines and sells chemical products. Activities of the other business operating segment include power generation business and development of businesses beyond the Group's traditional operations.

Geographical segments have been determined based on the area of operations and include three segments. They are Western Siberia, European Russia and International.

Operating segments

2009	Exploration and production	Refining, marketing and distribution	Chemicals	Other	Elimination	Consolidated
Sales						
Third parties	2,257	76,650	1,022	1,154	–	81,083
Inter-segment	22,096	784	162	1,765	(24,807)	–
Total sales	**24,353**	**77,434**	**1,184**	**2,919**	**(24,807)**	**81,083**
Operating expenses and total cost of purchases	3,668	55,943	812	2,346	(23,668)	39,101
Depreciation, depletion and amortization	2,613	936	41	347	–	3,937
Interest expense	886	1,205	14	407	(1,845)	667
Income tax expense	1,221	821	12	(1)	(59)	1,994
Net income	5,456	2,263	(69)	(310)	(329)	7,011
Total assets	54,924	56,299	1,371	18,091	(51,666)	79,019
Capital expenditures	4,687	1,391	113	343	–	6,534

2008	Exploration and production	Refining, marketing and distribution	Chemicals	Other	Elimination	Consolidated
Sales						
Third parties	1,753	103,132	2,067	728	–	107,680
Inter-segment	25,854	1,582	28	2,057	(29,521)	–
Total sales	**27,607**	**104,714**	**2,095**	**2,785**	**(29,521)**	**107,680**
Operating expenses and total cost of purchases	3,779	67,061	1,934	2,361	(29,158)	45,977
Depreciation, depletion and amortization	1,938	817	34	169	–	2,958
Interest expense	870	570	4	295	(1,348)	391
Income tax expense	955	2,510	14	(66)	54	3,467
Net income	4,234	5,130	(117)	(160)	57	9,144
Total assets	47,130	45,039	940	12,751	(34,399)	71,461
Capital expenditures	7,889	2,150	121	429	–	10,589

2007	Exploration and production	Refining, marketing and distribution	Chemicals	Other	Elimination	Consolidated
Sales						
Third parties	1,527	77,960	2,348	56	–	81,891
Inter-segment	22,331	2,191	19	325	(24,866)	–
Total sales	**23,858**	**80,151**	**2,367**	**381**	**(24,866)**	**81,891**
Operating expenses and total cost of purchases	3,813	52,032	1,904	206	(23,801)	34,154
Depreciation, depletion and amortization	1,427	663	28	54	–	2,172
Interest expense	611	621	4	218	(1,21)	333
Income tax expense	1,783	1,639	23	4	–	3,449
Net income	4,686	4,770	148	243	(336)	9,511
Total assets	43,395	41,091	1,004	8,412	(34,270)	59,632
Capital expenditures	7 262	1 822	171	117	–	9,372

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

Geographical segments

	2009	2008	2007
Sales of crude oil within Russia	735	600	440
Export of crude oil and sales of crude oil by foreign subsidiaries	19,914	24,007	19,258
Sales of petroleum products within Russia	8,101	13,872	9,583
Export of petroleum products and sales of petroleum products by foreign subsidiaries	46,888	62,542	47,154
Sales of chemicals within Russia	514	880	733
Export of chemicals and sales of chemicals by foreign subsidiaries	574	1,232	1,569
Other sales within Russia	2,235	2,335	1,644
Other export sales and other sales by foreign subsidiaries	2,122	2,212	1,510
TOTAL SALES	81,083	107,680	81,891

2009	Western Siberia	European Russia	International	Elimination	Consolidated
Sales					
Third parties	130	13,750	67,203	–	81,083
Inter-segment	11,035	26,918	18	(37,971)	–
Total sales	**11,165**	**40,668**	**67,221**	**(37,971)**	**81,083**
Operating expenses and total cost of purchases	2,035	15,151	59,061	(37,146)	39,101
Depletion, depreciation and amortization	963	2,223	751	–	3,937
Interest expense	62	643	406	(444)	667
Income taxes	624	1,210	219	(59)	1,994
Net income	2,873	4,638	(168)	(332)	7,011
Total assets	20,418	43,890	28,038	(13,327)	79,019
Capital expenditures	1,878	3,186	1,470	–	6,534

2008	Western Siberia	European Russia	International	Elimination	Consolidated
Sales					
Third parties	138	19,905	87,637	–	107,680
Inter-segment	15,436	38,808	40	(54,284)	–
Total sales	**15,574**	**58,713**	**87,677**	**(54,284)**	**107,680**
Operating expenses and total cost of purchases	2,011	19,789	78,220	(54,043)	45,977
Depletion, depreciation and amortization	832	1,499	627	–	2,958
Interest expense	37	196	260	(102)	391
Income taxes	640	2,397	376	54	3,467
Net income	1,848	7,615	(449)	130	9,144
Total assets	17,136	37,598	23,577	(6,850)	71,461
Capital expenditures	2,915	5,660	2,014	–	10,589

2007	Western Siberia	European Russia	International	Elimination	Consolidated
Sales					
Third parties	118	13,226	68,547	–	81,891
Inter-segment	14,045	31,781	30	(45,856)	–
Total sales	**14,163**	**45,007**	**68,577**	**(45,856)**	**81,891**
Operating expenses and total cost of purchases	1,995	17,323	59,692	(44,856)	34,154
Depletion, depreciation and amortization	649	969	554	–	2,172
Interest expense	22	244	239	(172)	333
Income taxes	973	2,044	432	–	3,449
Net income	3,587	5,341	884	(301)	9,511
Total assets	16,227	32,764	20,805	(10,164)	59,632
Capital expenditures	2,253	5,448	1,671	–	9,372

The accompanying notes are an integral part of these consolidated financial statements (millions of US dollars, unless otherwise noted)

The Group's international sales to third parties include sales in Switzerland of $37,724 million, $47,066 million and $35,868 million for the years ended December 31, 2009, 2008 and 2007, respectively. The Group's international sales to third parties include sales in the USA of $8,144 million, $12,171 million and $11,481 million for the years ended December 31, 2009, 2008 and 2007, respectively. These amounts are attributed to individual countries based on the jurisdiction of subsidiaries making the sale.

Note 23. Subsequent events

In accordance with the requirements of ASC No. 855, *"Subsequent events,"* the Group evaluated subsequent events through the date the financial statements were available to be issued. Therefore subsequent events were evaluated by the Group up to March 19, 2010.

In January 2010, the Company signed a development and production agreement at West Qurna-2 field located in the south of Iraq. The parties to the agreement are: Iraq's state-owned South Oil Company and the contracting consortium formed by the Iraqi state-owned North Oil Company, the Company and Norway's Statoil ASA. The Company's share in the project is 56.25%. As at the day of the agreement the Group has a commitment in the amount of approximately $281 million. The West Qurna-2 field has recoverable reserves of about 12.9 billion barrels.

Supplementary Information on Oil and Gas Exploration and Production Activities (Unaudited)

(Millions of US dollars, except as indicated)

This section provides unaudited supplemental information on oil and gas exploration and production activities in accordance with ASC No. 932 (former SFAS No. 69, *"Disclosures About Oil and Gas Producing Activities"*) in six separate tables:

I. Capitalized costs relating to oil and gas producing activities

II. Costs incurred in oil and gas property acquisition, exploration, and development activities

III. Results of operations for oil and gas producing activities

IV. Reserve quantity information

V. Standardized measure of discounted future net cash flows

VI. Principal sources of changes in the standardized measure of discounted future net cash flows

Amounts shown for equity companies represent the Group's share in its exploration and production affiliates, which are accounted for using the equity method of accounting.

I. Capitalized costs relating to oil and gas producing activities

As of December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Unproved oil and gas properties	545	305	850	285	1 135
Proved oil and gas properties	5,826	47,237	53,063	1,998	55,061
Accumulated depreciation, depletion, and amortization	(1,201)	(16,460)	(17,661)	(454)	(18,115)
NET CAPITALIZED COSTS	**5,170**	**31,082**	**36,252**	**1,829**	**38,081**

Net capitalized costs related to asset retirement obligations in the amount of $815 million, as of December 31, 2009, was included in net capitalized costs.

As of December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Unproved oil and gas properties	519	507	1,026	158	1 184
Proved oil and gas properties	5,391	42,248	47,639	855	48,494
Accumulated depreciation, depletion, and amortization	(901)	(14,649)	(15,550)	(209)	(15,759)
NET CAPITALIZED COSTS	**5,009**	**28,106**	**33,115**	**804**	**33,919**

Net capitalized costs related to asset retirement obligations in the amount of $439 million, as of December 31, 2008, was included in net capitalized costs.

As of December 31, 2007	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Unproved oil and gas properties	454	446	900	20	920
Proved oil and gas properties	3,906	36,664	40,570	677	41,247
Accumulated depreciation, depletion, and amortization	(644)	(13,813)	(14,457)	(164)	(14,621)
NET CAPITALIZED COSTS	3,716	23,297	27,013	533	27,546

Net capitalized costs related to asset retirement obligations in the amount of $406 million, as of December 31, 2007, was included in net capitalized costs.

II. Costs incurred in oil and gas property acquisition, exploration, and development activities

Year ended December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Acquisition of properties - proved	–	17	17	1,154	1,171
Acquisition of properties - unproved	–	23	23	97	120
Exploration costs	221	162	383	11	394
Development costs	549	3,726	4,275	146	4,421
TOTAL COSTS INCURRED	770	3,928	4,698	1,408	6,106

Year ended December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Acquisition of properties - proved	806	6	812	–	812
Acquisition of properties - unproved	49	5	54	6	60
Exploration costs	357	313	670	9	679
Development costs	719	6,430	7,149	139	7,288
TOTAL COSTS INCURRED	1,931	6,754	8,685	154	8,839

Year ended December 31, 2007	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Acquisition of properties - proved	-	393	393	-	393
Acquisition of properties - unproved	27	486	513	-	513
Exploration costs	180	366	546	12	558
Development costs	670	5,887	6,557	103	6,660
TOTAL COSTS INCURRED	877	7,132	8,009	115	8,124

(Millions of US dollars, except as indicated)

III. Results of operations for oil and gas producing activities

The Group's results of operations for oil and gas producing activities are presented below. In accordance with ASC No. 932, sales and transfers to Group companies are based on market prices. Income taxes are based on statutory rates. The results of operations exclude corporate overhead and interest costs.

Year ended December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Revenue					
Sales	1,472	13,870	15,342	824	16,166
Transfers	–	11,850	11,850	17	11,867
Total revenues	**1,472**	**25,720**	**27,192**	**841**	**28,033**
Production costs (excluding production taxes)	(195)	(2,592)	(2,787)	(98)	(2,885)
Exploration expense	(147)	(71)	(218)	(10)	(228)
Depreciation, depletion, and amortization	(323)	(2,235)	(2,558)	(105)	(2,663)
Accretion expense	–	(43)	(43)	–	(43)
Taxes other than income taxes	(206)	(12,830)	(13,036)	(186)	(13,222)
Related income taxes	(198)	(1,399)	(1,597)	(203)	(1,800)
TOTAL RESULTS OF OPERATIONS FOR PRODUCING ACTIVITIES	**403**	**6,550**	**6,953**	**239**	**7,192**

Year ended December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Revenue					
Sales	1,839	24,307	26,146	1,112	27,258
Transfers	–	17,941	17,941	11	17,952
Total revenues	**1,839**	**42,248**	**44,087**	**1,123**	**45,210**
Production costs (excluding production taxes)	(202)	(3,006)	(3,208)	(74)	(3,282)
Exploration expense	(356)	(131)	(487)	(7)	(494)
Depreciation, depletion, and amortization	(313)	(1,572)	(1,885)	(52)	(1,937)
Accretion expense	–	(25)	(25)	–	(25)
Taxes other than income taxes	(61)	(24,668)	(24,729)	(170)	(24,899)
Related income taxes	(294)	(3,272)	(3,566)	(481)	(4,047)
TOTAL RESULTS OF OPERATIONS FOR PRODUCING ACTIVITIES	**613**	**9,574**	**10,187**	**339**	**10,526**

Year ended December 31, 2007	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Revenue					
Sales	1,351	15,232	16,583	883	17,466
Transfers	–	15,444	15,444	79	15,523
Total revenues	**1,351**	**30,676**	**32,027**	**962**	**32,989**
Production costs (excluding production taxes)	(140)	(2,638)	(2,778)	(76)	(2, 854)
Exploration expense	(158)	(149)	(307)	(13)	(320)
Depreciation, depletion, and amortization	(259)	(1,130)	(1,389)	(33)	(1,422)
Accretion expense	–	(21)	(21)	–	(21)
Taxes other than income taxes	(7)	(17,087)	(17,094)	(134)	(17,228)
Related income taxes	(384)	(2,378)	(2,762)	(336)	(3,098)
TOTAL RESULTS OF OPERATIONS FOR PRODUCING ACTIVITIES	**403**	**7,273**	**7,676**	**370**	**8,046**

(Millions of US dollars, except as indicated)

IV. Reserve quantity information

Proved reserves are the estimated quantities of oil and gas reserves which geological and engineering data demonstrate will be recoverable with reasonable certainty in future years from known reservoirs under existing economic and operating conditions. In accordance with ASC No. 932 existing economic and operating conditions are based on the 12-months average price (for the year 2009) or year-end price (for the periods before 2009) and the year-end costs. Proved reserves do not include additional quantities of oil and gas reserves that may result from applying secondary or tertiary recovery techniques not yet tested and determined to be economic.

Proved developed reserves are the quantities of proved reserves expected to be recovered through existing wells with existing equipment and operating methods.

Due to the inherent uncertainties and the necessarily limited nature of reservoir data, estimates of reserves are inherently imprecise, require the application of judgment and are subject to change as additional information becomes available.

Management has included within proved reserves significant quantities which the Group expects to produce after the expiry dates of certain of its current production licenses in the Russian Federation. The Subsoil Law of the Russian Federation states that, upon expiration, a license is subject to renewal at the initiative of the license holder provided that further exploration, appraisal, production or remediation activities are necessary and provided that the license holder has not violated the terms of the license. Since the law applies both to newly issued and old licenses and the Group has currently renewed nearly 50% of its licenses, management believes that licenses will be renewed upon their expiration for the remainder of the economic life of each respective field.

In January 2010, the FASB issued ASU No. 2010-03, *"Extractive activities Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures."* The adoption of ASU No. 2010-03 did not have a significant impact on the Group's proved reserves and standardized measure of discounted future net cash flows.

Estimated net proved oil and gas reserves and changes thereto for the years ended December 31, 2009, 2008 and 2007, are shown in the tables set out below.

Millions of barrels	Consolidated subsidiaries			Group's share in equity companies	Total
	International	Russia	Total		
CRUDE OIL					
January 1, 2007	**410**	**15,183**	**15,593**	**334**	**15,927**
Revisions of previous estimates	2	35	37	(23)	14
Purchase of hydrocarbons in place*	–	178	178	(104)	74
Extensions and discoveries	20	463	483	35	518
Production	(26)	(668)	(694)	(19)	(713)
Sales of reserves	(105)	–	(105)	–	(105)
December 31, 2007	**301**	**15,191**	**15,492**	**223**	**15,715**
Revisions of previous estimates	80	(1,205)	(1,125)	1	(1,124)
Purchase of hydrocarbons in place	17	19	36	5	41
Extensions and discoveries	30	493	523	6	529
Production	(24)	(660)	(684)	(19)	(703)
December 31, 2008	**404**	**13,838**	**14,242**	**216**	**14,458**
Revisions of previous estimates	(85)	(636)	(721)	15	(706)
Purchase of hydrocarbons in place	–	39	39	102	141
Extensions and discoveries	37	503	540	–	540
Production	(27)	(673)	(700)	(20)	(720)
Sales of reserves	–	(17)	(17)	–	(17)
DECEMBER 31, 2009	**329**	**13,054**	**13,383**	**313**	**13,696**
Proved developed reserves					
December 31, 2007	164	9,715	9,879	180	10,059
December 31, 2008	208	8,806	9,014	156	9,170
DECEMBER 31, 2009	**186**	**8,442**	**8,628**	**199**	**8,827**

* Purchase of hydrocarbons in place for equity companies includes transfers of reserves to the consolidated group upon those equity companies becoming subject to consolidation.

(Millions of US dollars, except as indicated)

The minority interest share included in the above total proved reserves was 242 million barrels, 426 million barrels and 559 million barrels as of December 31, 2009, 2008 and 2007, respectively. The minority interest share included in the above proved developed reserves was 135 million barrels, 203 million barrels and 228 million barrels as of December 31, 2009, 2008 and 2007, respectively. Substantially all minority interests relate to the reserves in the Russian Federation.

Billions of cubic feet	Consolidated subsidiaries			Group's share in equity companies	Total
	International	Russia	Total		
NATURAL GAS					
January 1, 2007	**4,276**	**22,128**	**26,404**	**193**	**26,597**
Revisions of previous estimates	506	550	1,056	(2)	1,054
Purchase of hydrocarbons in place*	–	19	19	(14)	5
Extensions and discoveries	207	630	837	7	844
Production	(87)	(482)	(569)	(10)	(579)
December 31, 2007	**4,902**	**22,845**	**27,747**	**174**	**27,921**
Revisions of previous estimates	566	(386)	180	4	184
Purchase of hydrocarbons in place	1,395	4	1,399	-	1,399
Extensions and discoveries	118	310	428	7	435
Production	(175)	(500)	(675)	(11)	(686)
December 31, 2008	**6,806**	**22,273**	**29,079**	**174**	**29,253**
Revisions of previous estimates	(294)	(6 081)	(6,375)	(3)	(6,378)
Purchase of hydrocarbons in place	-	13	13	130	143
Extensions and discoveries	294	164	458	-	458
Production	(175)	(436)	(611)	(15)	(626)
DECEMBER 31, 2009	**6,631**	**15,933**	**22,564**	**286**	**22,850**
Proved developed reserves:					
December 31, 2007	1,369	6,553	7,922	133	8,055
December 31, 2008	1,912	5,893	7,805	114	7,919
DECEMBER 31, 2009	**2,002**	**5,636**	**7,638**	**157**	**7,795**

* Purchase of hydrocarbons in place for equity companies includes transfers of reserves to the consolidated group upon those equity companies becoming subject to consolidation.

The minority interest share included in the above total proved reserves was 36 billion cubic feet, 34 billion cubic feet and 49 billion cubic feet as of December 31, 2009, 2008 and 2007, respectively. The minority interest share included in the above proved developed reserves was 23 billion cubic feet, 24 billion cubic feet and 30 billion cubic feet as of December 31, 2009, 2008 and 2007, respectively. Substantially all minority interests relate to the reserves in the Russian Federation.

As a result of changes to development plans and commissioning dates, the Company transferred part of its gas reserves from the category of proved reserves into lower reserve categories and into resources. Management believes that these volumes will be returned into the proved reserves category as their development start date draws nearer or some new technologies are applied.

V. Standardized measure of discounted future net cash flows

The standardized measure of discounted future net cash flows, related to the above oil and gas reserves, is calculated in accordance with the requirements of ASC No. 932. Estimated future cash inflows from production are computed by applying the 12-months average price (for the year 2009) or year-end price (for the periods before 2009) for oil and gas to year-end quantities of estimated net proved reserves. Adjustment in this calculation for future price changes is limited to those required by contractual arrangements in existence at the end of each reporting year. Future development and production costs are those estimated future expenditures necessary to develop and produce year-end estimated proved reserves based on year-end cost indices, assuming continuation of year-end economic conditions. Estimated future income taxes are calculated by applying appropriate year-end statutory tax rates. These rates reflect allowable deductions and tax credits and are applied to estimated future pre-tax net cash flows, less the tax bases of related assets. Discounted future net cash flows have been calculated using a ten percent discount factor. Discounting requires a year-by-year estimate of when future expenditures will be incurred and when reserves will be produced.

(Millions of US dollars, except as indicated)

The information provided in the tables set out below does not represent management's estimate of the Group's expected future cash flows or of the value of the Group's proved oil and gas reserves. Estimates of proved reserve quantities are imprecise and change over time as new information becomes available. Moreover, probable and possible reserves, which may become proved in the future, are excluded from the calculations. The arbitrary valuation prescribed under ASC No. 932 requires assumptions as to the timing and amount of future development and production costs. The calculations should not be relied upon as an indication of the Group's future cash flows or of the value of its oil and gas reserves.

As of December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Future cash inflows	31,025	385,266	416,291	14,816	431,107
Future production and development costs	(18,778)	(254,811)	(273,589)	(7,692)	(281,281)
Future income tax expenses	(2,337)	(22,285)	(24,622)	(1,489)	(26,111)
Future net cash flows	9,910	108,170	118,080	5,635	123,715
Discount for estimated timing of cash flows (10% p.a.)	(6,468)	(66,015)	(72,483)	(3,013)	(75,496)
Discounted future net cash flows	3,442	42,155	45,597	2,622	48,219
Minority share in discounted future net cash flows	–	1,370	1,370	–	1,370

Included as a part of the $281 billion of future production and development costs are $6.5 billion of future dismantlement, abandonment and rehabilitation costs.

As of December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Future cash inflows	26,612	312,334	338,946	5,546	344,492
Future production and development costs	(18,647)	(185,733)	(204,380)	(3,074)	(207,454)
Future income tax expenses	(318)	(21,250)	(21,568)	(516)	(22,084)
Future net cash flows	7,647	105,351	112,998	1,956	114,954
Discount for estimated timing of cash flows (10% p.a.)	(6,132)	(64,296)	(70,428)	(950)	(71,378)
Discounted future net cash flows	1,515	41,055	42,570	1,006	43,576
Minority share in discounted future net cash flows	–	1,333	1,333	–	1,333

Included as a part of the $207 billion of future production and development costs are $6.4 billion of future dismantlement, abandonment and rehabilitation costs.

As of December 31, 2007	International	Russia	Total consolidated companies	Group's share in equity companies	Total
Future cash inflows	34,051	660,363	694,414	17,892	712,306
Future production and development costs	(13,015)	(442,801)	(455,816)	(4,639)	(460,455)
Future income tax expenses	(2,414)	(48,552)	(50,966)	(3,568)	(54,534)
Future net cash flows	18,622	169,010	187,632	9,685	197,317
Discount for estimated timing of cash flows (10% p.a.)	(9,576)	(106,185)	(115,761)	(4,857)	(120,618)
Discounted future net cash flows	9,046	62,825	71,871	4,828	76,699
Minority share in discounted future net cash flows	–	1,379	1,379	–	1,379

Included as a part of the $460 billion of future production and development costs are $7.8 billion of future dismantlement, abandonment and rehabilitation costs.

(Millions of US dollars, except as indicated)

VI. Principal sources of changes in the standardized measure of discounted future net cash flows

	2009	2008	2007
CONSOLIDATED COMPANIES			
Discounted present value as at January 1	**42,570**	**71 871**	**45 568**
Net changes due to purchases and sales of minerals in place	86	(279)	(46)
Sales and transfers of oil and gas produced, net of production costs	(11,151)	(15,663)	(11,848)
Net changes in prices and production costs estimates	36,633	(113,710)	75,908
Net changes in mineral extraction taxes	(27,376)	79,317	(43,384)
Extensions and discoveries, less related costs	1,878	1,423	2,947
Development costs incurred during the period	3,201	3,528	2,308
Revisions of previous quantity estimates	(4,495)	(3,520)	980
Net change in income taxes	(1,104)	11,054	(6,562)
Other changes	70	123	185
Accretion of discount	5,285	8,426	5,815
Discounted present value at December 31	**45,597**	**42,570**	**71,871**

	2009	2008	2007
GROUP'S SHARE IN EQUITY COMPANIES			
Discounted present value as at January 1	**1,006**	**4,828**	**2,888**
Net changes due to purchases and sales of minerals in place	1,182	17	(367)
Sales and transfers of oil and gas produced, net of production costs	(547)	(872)	(739)
Net changes in prices and production costs estimates	2,129	(6,343)	3,622
Net changes in mineral extraction taxes	(1,086)	901	(643)
Extensions and discoveries, less related costs	3	38	1,020
Development costs incurred during the period	31	51	74
Revisions of previous quantity estimates	137	13	(716)
Net change in income taxes	(442)	1,553	(629)
Other changes	95	239	(38)
Accretion of discount	114	581	356
Discounted present value at December 31	**2,622**	**1,006**	**4,828**

	2009	2008	2007
TOTAL			
Discounted present value as at January 1	**43,576**	**76,699**	**48,456**
Net changes due to purchases and sales of minerals in place	1,268	(262)	(413)
Sales and transfers of oil and gas produced, net of production costs	(11,698)	(16,535)	(12,587)
Net changes in prices and production costs estimates	38,762	(120,053)	79,530
Net changes in mineral extraction taxes	(28,462)	80,218	(44,027)
Extensions and discoveries, less related costs	1,881	1,461	3,967
Development costs incurred during the period	3,232	3,579	2,382
Revisions of previous quantity estimates	(4,358)	(3,507)	264
Net change in income taxes	(1,546)	12,607	(7,191)
Other changes	165	362	147
Accretion of discount	5,399	9,007	6,171
Discounted present value at December 31	**48,219**	**43,576**	**76,699**

(Millions of US dollars, except as indicated)

Management's discussion and analysis of financial condition and results of operations

The following report represents management's discussion and analysis of the financial condition and results of operations of OAO LUKOIL as of December 31, 2009, and each of the years ended December 31, 2009, 2008 and 2007, and significant trends that may affect its future performance. It should be read in conjunction with our US GAAP consolidated financial statements and notes and supplemental oil and gas disclosure.

References to "LUKOIL," "the Company," "the Group," "we" or "us" are references to OAO LUKOIL and its subsidiaries and equity affiliates. All dollar amounts are in millions of US dollars, unless otherwise indicated. Tonnes of crude oil produced are translated into barrels using conversion rates characterizing the density of oil from each of our oilfields. Tonnes of crude oil purchased as well as other operational indicators expressed in barrels were translated into barrels using an average conversion rate of 7.33 barrels per tonne. Translations of cubic meters to cubic feet were made at the rate of 35.31 cubic feet per cubic meter. Translations of barrels of crude oil into barrels of oil equivalent ("BOE") were made at the rate of 1 barrel per BOE and of cubic feet into BOE at the rate of 6 thousand cubic feet per BOE.

This report includes forward-looking statements – words such as "believes," "anticipates," "expects," "estimates," "intends," "plans," etc. – that reflect management's current estimates and beliefs, but are not guarantees of future results. Please see "Forward-looking statement" on page 194 for a discussion of some of the factors that could cause actual results to differ materially.

Key financial and operational results

	2009	Change to 2008, %	2008	Change to 2007, %	2007
Sales (millions of US dollars)	81,083	(24.7)	107,680	31.5	81,891
Net income attributable to OAO LUKOIL (millions of US dollars)	7,011	(23.3)	9,144	(3.9)	9,511
Net income before one-off impairment losses (millions of US dollars)[1]	7,352	(22.4)	9,471	(0.4)	9,511
EBITDA (millions of US dollars)	13,475	(14.7)	15,797	3.0	15,330
Taxes other than income taxes, excise and export tariffs (millions of US dollars)	19,532	(43.9)	(34,804)	42.6	(24,400)
Basic and diluted earning per share of common stock attributable to OAO LUKOIL (US dollars)	8.28	(23.9)	10.88	(5.2)	11.48
Hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE)	807,301	0.5	803,109	1.0	795,099
Crude oil production by the Group including our share in equity affiliates (thousands of tonnes)	97,615	2.5	95,240	(1.5)	96,645
Gas produced by the Group including our share in equity affiliates (millions of cubic meters)[2]	14,898	(12.5)	17,020	22.0	13,955
Refined products produced by the Group including our share in equity affiliates (thousands of tonnes)	59,879	12.9	53,033	8.6	48,819
Hydrocarbon proved reserves including our share in equity affiliates (millions of BOE)	17,504	(9.5)	19,334	(5.1)	20,369

[1] One-off impairment losses are discussed in details on page 183.
[2] Gas available for sale.

In 2009, our net income was $7,011 million, which is $2,133 million, or 23.3%, less than in 2008.

Such decrease in our net income is mainly explained by a sharp decrease in prices for hydrocarbons in 2009, compared to 2008.

Business overview

The primary activities of OAO LUKOIL and its subsidiaries are oil exploration, production, refining, marketing and distribution. The Company is the ultimate parent entity of a vertically integrated group of companies.

The Group was established in accordance with Presidential Decree 1403, issued on November 17, 1992. Under this decree, on April 5, 1993, the Government of the Russian Federation transferred to the Company 51% of the voting shares of fifteen enterprises. Under Government Resolution 861 issued on September 1, 1995, a further nine enterprises were transferred to the Group during 1995. Since 1995, the Group has carried out a share exchange program to increase its shareholding in each of 24 founding subsidiaries to 100%. From formation, the Group has expanded substantially through consolidation of interests, acquisition of new companies and establishment of new businesses. Now LUKOIL is a global energy company operating through its subsidiaries in 37 countries on four continents.

LUKOIL is one of the world's largest energy companies in terms of hydrocarbon reserves. The Company's proved reserves as of January 1, 2010 amounted to 17.5 billion BOE and comprised of 13.7 billion BOE of crude oil and 22.9 trillion cubic feet of gas.

Our operations are divided into three main business segments:

- **Exploration and Production** – which includes our exploration, development and production operations relating to crude oil and natural gas. These activities are primarily located within Russia, with additional activities in Azerbaijan, Kazakhstan, Uzbekistan, the Middle East, South America, and Northern and Western Africa.
- **Refining, Marketing and Distribution** – which includes refining and transport operations, marketing and trading of crude oil, natural gas and refined products.
- **Chemicals** – which includes processing and trading of petrochemical products.

Other businesses include a power generation business, banking, finance and other activities. Each of our three main segments is dependent on the other, with a portion of the revenues of one segment being a part of the costs of the other. In particular, our Refining, Marketing and Distribution segment purchases crude oil from our Exploration and Production segment. As a result of certain factors considered in the "Domestic crude oil and refined products prices" section on page 169 benchmarking crude oil market prices in Russia cannot be determined with certainty. Therefore, the prices set for inter-segment purchases of crude oil reflect a combination of market factors, primarily international crude oil market prices, transportation costs, regional market conditions, the cost of refining crude oil and other factors. Accordingly, an analysis of either of these segments on a stand-alone basis could give a misleading impression of those segments' underlying financial position and results of operations. For this reason, we do not analyze either of our main segments separately in the discussion that follows. However, we present the financial data for each in Note 22 "Segment information" to our consolidated financial statements.

Recent developments and outlook

The following has been achieved in 2009:

Exploration and production

- 8 new oil and gas fields were brought on line (2008: 11 oil and gas fields).
- Within the consortium with Norway's Statoil we won the tender to develop the major West Qurna-2 oilfield, which has estimated recoverable reserves of 12.9 billion barrels of crude oil.
- We started production drilling at Yu. Korchagin field in the Caspian Sea, where we plan to begin commercial production in the second quarter of 2010.
- We acquired the remaining 46% interest and so became an owner of full stake in LUKARCO B.V. ("LUKARCO"), thus increasing our reserves by 102.3 million barrels of oil and 129.8 billion cubic feet of gas, and oil production by approximately 13 thousand barrels per day. LUKARCO is a holding company, which owns a 5% share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, and a 12.5% share in the Caspian Pipeline Consortium (CPC), which carries Kazakhstani and Russian oil to Novorossiysk marine terminal.

Refining

- We acquired 45% interest in TRN refinery in the Netherlands ("TRN"). TRN has an annual topping capacity of 7.9 million tonnes and a hydro-cracking unit with an annual capacity of approximately 3.4 million tonnes. Our share of production at TRN amounted to 1,528 thousand tonnes.

Marketing

- In the Russian Federation we acquired petrol stations networks of companies, OOO Smolensknefteprodukt, OOO IRT Investment, OOO PM Invest and OOO Retaier House. Thus, we increased our network by 96 stations and plots of land.
- As a result of our activity for development of retail segment our retail sales in Russia increased by 252 thousand tonnes.

Other

- In 2009, we continued our pursuit to improve the Group structure by divesting our non-core businesses. We spun off and sold outside the Group several transportation and service assets in Western Siberia and a group of security agencies.
- We continued to develop our power generating and distribution business. We successfully fulfil investment program of OAO UGK TGK-8 ("TGK-8"), we invested $202 million and plan to invest further $944 million within next 4 years. The revenue of power generating sector in 2009 amounted to $804 million.

Other achievements in 2009 are described in detail further in this report.

Changes in the Group structure

In December 2009, the Group acquired the remaining 46.0% interests in its equity affiliate LUKARCO for $1.6 billion, thereby increasing the ownership stake to 100%. LUKARCO is a holding company, which owners a 5% share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, and a 12.5% share in CPC, which carries Kazakhstani and Russian oil to Novorossiysk marine terminal. Therefore the Group increased the ownership in Tengizchevroil from 2.7% to 5% and the ownership in CPC from 6.75% to 12.5%. The first installment in amount of $300 million was paid in December 2009; the remaining amount should be paid no later than two years after the acquisition. The Group is using equity method of accounting for investments in Tengizchevroil and CPC.

During 2009, a Group company acquired the remaining 25.2% of share capital of OAO RITEK ("RITEK") for $235 million, thereby increasing the Group's share to 100%. RITEK is a crude oil producing company operating in European Russia and Western Siberia.

In June 2009, a Group company entered into an agreement with Total to acquire a 45% interest in TRN refinery in the Netherlands. The transaction was finalized in September 2009 in the amount of approximately $700 million. The Group provides crude oil and market refined products in line with its equity stake in the refinery. The refinery has the flexibility to process Urals blend crude oil as well as significant volumes of straight-run fuel oil and vacuum gasoil, which allows to integrate the plant into the Group's crude oil supply and refined products marketing operations. This plant with a Nelson complexity index of 9.8 has an annual topping capacity of 7.9 million tonnes and an annual capacity of a hydro-cracking unit of approximately 3.4 million tonnes. This acquisition was made in accordance with the Group's plans to develop its refining capacity in Europe.

In the first quarter of 2009, the Group acquired 100% interests in OOO Smolenskneftesnab, OOO IRT Investment, OOO PM Invest and OOO Retaier House for $238 million. These are holding companies, which between them own 96 petrol stations and plots of land in Moscow, the Moscow region and other regions of central European Russia. This acquisition was made in order to expand the Group's presence on the most advantageous retail market in the Russian Federation.

In the fourth quarter of 2008, the Group acquired 100% interests in ZAO Association Grand and OOO Mega Oil M for $493 million. ZAO Association Grand and OOO Mega Oil M are holding companies, owning 181 petrol stations in Moscow, the Moscow region and other regions of central European Russia. This acquisition was made in order to expand the Group's presence on the most advantageous retail markets in the Russian Federation.

In July 2008, a Group company signed an agreement to acquire a 100% interest in the Akpet group for $555 million. The transaction was finalized in November 2008. The amended agreement provided for three payments of purchase consideration: the first payment in amount of $250 million was paid at the date of finalization, the second payment in amount of $150 million was paid in April 2009, and the remaining amount was paid in October 2009. The Akpet group operated 689 petrol filling stations on the basis of dealer agreements and owned eight refined product terminals, five LNG storage tanks, three jet fuel terminals and a lubricant production plant in Turkey.

In June 2008, a Group company signed an agreement with ERG S.p.A. to establish a joint venture to operate the ISAB refinery complex ("ISAB") in Priolo, Italy. In December 2008, the Group completed the acquisition of a 49% stake in the joint venture for €1.45 billion (approximately $1.83 billion) and paid €600 million (approximately $762 million) as a first installment. The remaining amount was paid in February 2009. The seller has a put option, the effect of which would be to increase the Group's stake in the company operating ISAB up to 100%. As of December 31, 2009, the fair value of this option for the Group is zero. The agreement states that each partner is responsible for procuring crude oil and marketing refined products in line with its equity stake in the joint venture. ISAB has the flexibility to process Urals blend crude oil, and the Group integrated its share of ISAB capacity into its crude oil supply and refined products marketing operations. ISAB includes three jetties and storage tanks totaling 3,700 thousand cubic meters and has an annual refining capacity of 16 million tonnes.

In March 2008, a Group company entered into an agreement to acquire 75 petrol stations and storage facilities in Bulgaria for approximately $367 million. The transaction was finalized in the second quarter of 2008.

In March 2008, a Group company acquired 100% of the share capital of the SNG Holdings Ltd. group for $578 million. The purchase agreement provided for two additional components of contingent purchase consideration in amount of $100 million each. During 2008, all conditions for contingent purchase consideration were met and a Group company completely settled its obligation under the purchase agreement. The SNG Holdings Ltd. group holds a 100% interest in a production sharing agreement in oil and gas condensate fields located in the South-Western Gissar and Ustyurt regions of Uzbekistan. The purpose of the acquisition was to increase the Group's presence in the Uzbekistan oil and gas sector.

In March 2008, a Group company entered into an agreement with a related party, whose management and directors include members of the Group's management and Board of Directors, acquire a 64.31% interest in TGK-8 for approximately $2,117 million. The purchase consideration partly consisted of 23.55 million shares of common stock of the Company (at a market value of approximately $1,620 million). The transaction was finalized in May 2008. From May 2008 to June 2009, a Group company acquired the remaining interest in TGK-8 for a total of $1,202 million, increasing the Group's ownership to 100%. TGK-8 is one of the major gas consumers in the Southern Federal District with an annual consumption of 6 billion cubic meters per year. Its power plants are located in Astrakhan, Volgograd and Rostov regions, Krasnodar and Stavropol Districts, and the Republic of Dagestan of the Russian Federation with total productive capacity of 3.6 GW. By purchasing TGK-8 LUKOIL expects significant synergies through natural gas supplies from the Company's gas fields located in the Northern Caspian and in Astrakhan region, which will allow the Company to reach efficient gas price. This acquisition is made in accordance with the Company's plans to develop its electric power business.

In 2008, the Group acquired the remaining 3.09% of the share capital of OAO LUKOIL-Nizhegorodnefteorgsintez ("Nizhegorodnefteorgsintez") for $64 million increasing the Group's ownership in Nizhegorodnefteorgsintez to 100%. Nizhegorodnefteorgsintez is a refinery plant located in European Russia.

Resource base

The table below summarizes the net oil-equivalent proved reserves of consolidated subsidiaries and our share in equity affiliates that have been derived or extracted from the reports of Miller and Lents, Ltd. ("Miller and Lents"), our independent reservoir engineers, dated as at January 1, 2009 and 2010.

(millions of BOE)	January 1, 2010	Changes in 2009: Production[1]	Changes in 2009: Extensions, discoveries and changes in structure	Changes in 2009: Revision of previous estimates	January 1, 2009
Western Siberia	9,751	(450)	332	(625)	10,494
Timan-Pechora	2,735	(163)	38	(157)	3,017
Ural region	2,124	(94)	30	23	2,165
Volga region	895	(26)	142	(891)	1,670
Other in Russia	231	(16)	12	1	234
Outside Russia	1,768	(75)	210	(121)	1,754
Proved oil and gas reserves	**17,504**	**(824)**	**764**	**(1,770)**	**19,334**
Probable oil and gas reserves	**9,820**				**11,767**
Possible oil and gas reserves	**5,054**				**5,282**

[1] Gas production shown before own consumption.

The Company's proved reserves as at January 1, 2010 amount to 17.5 billion BOE and comprise of 13.7 billion BOE of crude oil and 22.9 trillion cubic feet of gas.

In 2009, the increase in Company's proved reserves due to geological exploration and production drilling amounted to 617 million BOE.

Acquisitions increased our proved reserves by 124 million BOE, due to the increase of our share in Tengizchevroil to 5% as a result of increasing our share in LUKARCO to 100%.

Changes in our licences portfolio led to a net increase of our reserves by 23 million BOE.

Operational highlights

Hydrocarbon production

We undertake exploration for, and production of, crude oil and natural gas in Russia and internationally. In Russia our major oil producing subsidiaries are LUKOIL-Western Siberia, LUKOIL-Komi and LUKOIL-Perm. Also we have a consolidated joint venture with ConocoPhillips, Narianmarneftegaz, in the Northern Timan-Pechora region. Exploration and production outside of Russia is performed by our 100% subsidiary LUKOIL-Overseas, that has stakes in PSA's and other projects in Kazakhstan, Azerbaijan, Uzbekistan, Saudi Arabia, Columbia, Ghana and Cote d'Ivoire.

The table below summarizes the results of our exploration and production activities.

	2009	2008	2007
Daily production of hydrocarbons, including the Company's share in equity affiliates (thousand BOE per day), including:	**2,212**	**2,194**	**2,178**
- crude oil	1,972	1,921	1,953
- natural and petroleum gas[1]	240	273	225
Hydrocarbon extraction expenses (US dollar per BOE)	**3.56**	**4.12**	**3.58**
	(millions of US dollars)		
Hydrocarbon extraction expenses	**2,787**	**3,208**	**2,757**
- in Russia	2,592	3,006	2,616
- outside Russia	195	202	141
Exploration expenses	**218**	**487**	**307**
- in Russia	71	131	149
- outside Russia	147	356	158
Mineral extraction tax	**5,452**	**12,267**	**8,482**
- in Russia	5,399	12,267	8,482
- outside Russia	53	–	–

[1] Gas available for sale (excluding gas produced for our own consumption).

Crude oil production. In 2009, we increased our daily crude oil production by 2.7%, compared to 2008. We produced (including the Company's share in equity affiliates) 719.6 million barrels, or 97.6 million tonnes.
The following table represents our crude oil production in 2009 and 2008 by major regions.

		Change to 2008			
(thousands of tonnes)	2009	Total, %	Change in structure	Organic change	2008
Western Siberia	52,962	(5.7)	–	(3,225)	56,187
Timan-Pechora	21,662	29.8	–	4,977	16,685
Ural region	11,958	3.6	–	410	11,548
Volga region	2,848	(6.3)	–	(193)	3,041
Other in Russia	2,130	(2.5)	–	(55)	2,185
Crude oil produced in Russia	91,560	2.1	–	1,914	89,646
Crude oil produced internationally	3,515	9.8	–	315	3,200
Total crude oil produced by consolidated subsidiaries	**95,075**	**2.4**	**–**	**2,229**	**92,846**
Our share in crude oil produced by equity affiliates:					
in Russia	308	3.0	–	9	299
outside Russia	2,232	6.5	26	111	2,095
TOTAL CRUDE OIL PRODUCED	97,615	2.5	26	2,349	95,240

The main oil producing region of the Company is Western Siberia where we produced 55.7% of our crude oil in 2009 (60.5% in 2008 and 63.6% in 2007). In 2009, the Western Siberian producing assets continued to mature resulting in a production decline and water cut increase. A significant impact on our production in the period was caused by a lack of sufficient power generating capacities to meet the growing demand for extra power from a wide range of oil producers in Western Siberia as they faced the need to scale up pumping operations supporting crude oil production. In order to overcome this problem, which arose in the region several years ago, the Group is continuously increasing its own power capacity by construction power plants in the oil fields.

In line with our strategy the Company is developing new oil fields in the Northern Timan-Pechora and Caspian regions in order to compensate for the decrease in crude oil production in the traditional regions. In August 2008, we began commercial production on the Yuzhnoye Khylchuyu oil field, located in the Timan-Pechora region. We produced 7.0 million tonnes from this field in 2009. This oil field is developed within our strategic partnership with ConocoPhillips.

The structural growth of our share in equity affiliates' production outside of Russia is explained by the increase of our effective share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, to 5% as a result of acquiring the remaining 46% interest in LUKARCO.

In December 2009, we started production drilling on the Yu. Korchagin field in the Caspian Sea. The maximum annual production from this field is expected to be 2.5 million tonnes of oil and gas condensate, and 1.0 billion cubic meters of gas.

In addition to our production, we purchase crude oil in Russia and on international markets. In Russia we primarily purchase crude oil from affiliated producing companies and other producers. Then we either refine or export purchased crude oil. Crude oil purchased on international markets is used for trading activities, for supplying our international refineries or for processing at third party refineries.

	2009		2008		2007	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Crude oil purchases in Russia	4,442	606	1,730	236	345	47
Crude oil purchases internationally	150,258	20,499	76,078	10,379	32,802	4,475
TOTAL CRUDE OIL PURCHASED	**154,700**	**21,105**	**77,808**	**10,615**	**33,147**	**4,522**

The increase in volumes of crude oil purchased internationally resulted from increased refining and trading. In 2009, we purchased 11,313 thousand tonnes of crude oil to process at our and at third party refineries (including 5,116 thousand tonnes at ISAB and 698 thousand tonnes at TRN), compared to 5,029 thousand tonnes in 2008.

Gas production. In 2009, we produced 14,898 million cubic meters of gas available for sale (including our share in equity affiliates), a decrease of 12.5%, compared to 2008.

Our major gas production field is the Nakhodkinskoe gas field, where we produced 5,936 million cubic meters of natural gas in 2009, compared to 8,313 million cubic meters in 2008. The 28.6% decrease in gas production from this field resulted from the decrease of purchases of our gas by OAO Gazprom ("Gazprom"), the Russian gas monopoly.

In 2009, our share in production from the Shakh-Deniz field in Azerbaijan was 518 million cubic meters, compared to 552 million cubic meters in 2008. Our production from the Khauzak gas field in Uzbekistan was 2,227 million cubic meters of natural gas, compared to 2,340 million cubic meters in 2008.

Refining, marketing and trading

Refining. We own and operate four refineries located in European Russia and three refineries located outside of Russia – in Bulgaria, Ukraine and Romania. In August 2005, we closed our refinery in Odessa, Ukraine to commence a wide-scale upgrade. In April 2008, we put it back into operation after the completion of the upgrade. The annual capacity of the Odessa refinery amounts to 2.8 million tonnes. At the end of 2008, we acquired 49% interest in ISAB, which has an annual refining capacity of 16 million tonnes. In September 2009, we acquired 45% interest in TRN refinery, which has an annual capacity of 7.9 million tonnes.

Compared to 2008, production at our consolidated and affiliated refineries increased in 2009 by 12.9%. Russian refineries increased their production by 0.8%. Production of our international refineries including our share of production at ISAB and TRN increased by 59.3%, notwithstanding the fact that the production at our Romanian refinery was 7.4% lower due to overhaul performed at the refinery in January-February 2009 and decreased production at our Bulgarian refinery, which was 7.1% lower than in 2008 as a result of revision of 2009 production plan due to low refining margins.

In 2009, our share of refined products produced at ISAB amounted to 6,153 thousand tonnes (578 thousand tonnes in 2008) and our share in production of TRN amounted to 1,528 thousand tonnes.

In Russia LUKOIL holds the leading position in production of European standards motor fuel before the official terms of their obligatory implementation in the country. At our Russian refineries we produced 7,266, 7,224 and 7,218 thousand tonnes of Euro 4 and Euro 5 diesel fuel in 2009, 2008 and 2007, respectively. In 2009, 2008 and 2007 our production of Euro 3 gasoline amounted to 4,746, 4,191 and 852 thousand tonnes, respectively.

Along with our own production of refined products we refined crude oil at third party refineries. In Russia we processed crude oil at third party refineries primarily to supply our network in the Ural region and for export sales. To supply our retail networks in Eastern Europe we refined crude oil in Belarus and Serbia. Refined products processed in Belarus are used for supplying our local retail network and for wholesale export.

The following table summarizes key figures for our refining activities.

	2009	2008	2007
	(millions of US dollars)		
Own refining expenses	923	1,115	880
- in Russia	671	780	651
- outside Russia	252	335	229
Refining expenses at ISAB and TRN	543	39	–
Refining expenses at third party refineries	170	400	242
- in Russia	126	341	214
- outside Russia	44	59	28
Capital expenditures	828	1,023	830
- in Russia	520	688	606
- outside Russia	308	335	224
	(thousand barrels per day)		
Refinery throughput at the Group refineries in Russia	889	881	851
Refinery throughput at the Group refineries outside Russia	210	231	193
Refinery throughput at the Group refineries	**1,099**	**1,112**	**1,044**
Refinery throughput at ISAB and TRN[1]	123	11	–
Refinery throughput at the Group and affiliated refineries	**1,222**	**1,123**	**1,044**
Refinery throughput at third party refineries in Russia	41	64	72
Refinery throughput at third party refineries outside Russia	36	46	21
Refinery throughput at third party refineries	**77**	**110**	**93**
TOTAL REFINERY THROUGHPUT	1,299	1,233	1,137
	(thousand of tonnes)		
Refined products produced at the Group refineries in Russia[2]	42,408	42,067	40,381
Refined products produced at the Group refineries outside Russia	9,790	10,388	8,438
Total refined products produced at the Group refineries	**52,198**	**52,455**	**48,819**
The Group's share of the production of ISAB and TRN	7,681	578	–
Total refined products produced at the Group and affiliated refineries	**59,879**	**53,033**	**48,819**
Refined products produced at third party refineries in Russia	1,873	2,881	3,270
Refined products produced at third party refineries outside Russia	1,612	2,123	945
Total refined products produced at third party refineries	**3,485**	**5,004**	**4,215**

[1] Group's share.
[2] Excluding mini refineries.

Marketing and trading. Our marketing and trading activities mainly include wholesale and bunkering operations in Western Europe, South-East Asia, Central America and retail operations in the USA, Central and Eastern Europe, the Baltic States and other regions. In Russia we purchase refined products on occasion, primarily to manage supply chain bottlenecks.

The Group retails its refined products in 26 countries through 6.2 thousand petrol stations. Most of the stations operate under the LUKOIL brand. We continuously develop our retail business and LUKOIL brand by expanding our retail network.

The table below summarizes figures for our trading activities.

	2009	2008	2007
	(millions of US dollars)		
Retail sales	13,146	17,812	12,904
Wholesale sales	41,843	58,602	43,833
TOTAL REFINED PRODUCTS SALES	54,989	76,414	56,737
	(thousand of tonnes)		
Refined products purchased in Russia	625	1,635	1,543
Refined products purchased internationally	41,445	38,743	38,745
TOTAL REFINED PRODUCTS PURCHASED	42,070	40,378	40,288

Exports of crude oil and refined products from Russia. In 2009, our export of crude oil from Russia was 6.9% more than in 2008, and we exported 45.9% of our total domestic crude oil production (43.8% in 2008 and 46.5% in 2007). This increase resulted from the commencement of production on the Yuzhnoye Khylchuyu oil field by our joint venture with ConocoPhillips, crude oil from which we export from Russia.

The volumes of crude oil exported from Russia by our subsidiaries are summarized as follows:

	2009		2008		2007	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Exports of crude oil using Transneft export routes	241,890	33,000	264,393	36,070	293,163	39,995
Exports of crude oil bypassing Transneft	66,109	9,019	23,639	3,225	15,818	2,158
TOTAL CRUDE OIL EXPORTS	307,999	42,019	288,032	39,295	308,981	42,153

In 2009, the crude oil exported through our own export infrastructure was 8,712 thousand tonnes or over three times more than in 2008. This was due to export of crude oil produced from the Yuzhnoye Khylchuyu oil field (7.0 million tonnes in 2009) through our export terminal in Varandey.

In 2009, we exported from Russia 27.8 million tonnes of refined products, an increase of 7.7%, compared to 2008. We export from Russia primarily diesel fuel, fuel oil and gasoil. These products account for approximately 89.4% of our refined products export volumes.

In 2009, our revenue from export from Russia both to the Group companies and third parties amounted to $17,485 million for crude oil and $11,414 million for refined products.

Main macroeconomic factors affecting our results of operations

Changes in the price of crude oil and refined products

The price at which we sell crude oil and refined products is the primary driver of our revenues. During 2009, the Brent crude oil price fluctuated between $39 and $78 per barrel and reached its peak of $78.86 in mid-November of 2009.

In 2008, the crude oil prices were the highest ever in real terms. Starting from July 2008, crude oil prices began to descend and by the end of the year crude oil price dropped by more than $100 per barrel down to $37 per barrel driven by the world economic downturn. During the second half of 2009, the crude oil price stabilized around $70 per barrel. Expectations for economic recovery help to resist the negative impact of fundamental factors. According to IEA, global oil demand for 2010 is forecasted at 86.5 million barrels daily, which is 1.8% higher than in 2009.

Substantially all crude oil we export is Urals blend. The following table shows the average crude oil and refined product prices for 2009, 2008 and 2007.

	2009	Change to 2008, %	2008	Change to 2007, %	2007
	(in US dollars per barrel, except for figures in percent)				
Brent crude	61.67	(36.6)	97.26	34.4	72.39
Urals crude (CIF Mediterranean)[1]	61.22	(35.4)	94.76	36.6	69.38
Urals crude (CIF Rotterdam)[1]	61.15	(35.5)	94.83	37.1	69.16
	(in US dollars per metric tonne, except for figures in percent)				
Fuel oil 3.5% (FOB Rotterdam)	345.72	(24.8)	459.74	35.6	339.00
Diesel fuel 10 ppm (FOB Rotterdam)	534.84	(40.7)	901.53	42.2	634.09
High-octane gasoline (FOB Rotterdam)	579.01	(30.8)	836.79	20.2	695.97

Source: Platts.

[1] The Company sells crude oil on foreign markets on various delivery terms. Thus, our average realized sale price of oil on international markets differs from the average prices of Urals blend on Mediterranean and Northern Europe markets.

Domestic crude oil and refined products prices

Substantially all crude oil produced in Russia is produced by vertically integrated oil companies such as ours. As a result, most transactions are between affiliated entities within vertically integrated groups. Thus, there is no concept of a benchmark domestic market price for crude oil. The price of crude oil that is produced but not refined or exported by one of the vertically integrated oil companies is generally determined on a transaction-by-transaction basis against a background of world market prices, but with no direct reference or correlation. At any time there may exist significant price differences between regions for similar quality crude oil as a result of the competition and economic conditions in those regions.

Domestic prices for refined products are determined to some extent by world market prices, but they are also directly affected by local demand and competition.

The table below represents average domestic wholesale prices of refined products in 2009, 2008 and 2007.

	2009	Change from 2008, %	2008	Change from 2007, %	2007
	(in US dollars per metric tonne, except for figures in percent)				
Fuel oil	162.12	(32.1)	238.87	42.2	167.93
Diesel fuel	462.65	(37.8)	744.07	39.0	535.32
High-octane gasoline (Regular)	584.87	(22.2)	751.95	19.9	626.95
High-octane gasoline (Premium)	636.24	(26.0)	860.07	20.3	714.72

Source: InfoTEK (excluding VAT).

Changes in the US dollar-ruble exchange rate and inflation

A substantial part of our revenue is either denominated in US dollars or is correlated to some extent with US dollar crude oil prices, while most of our costs in the Russian Federation are settled in Russian rubles. Therefore, ruble inflation and movements of exchange rates can significantly affect the results of our operations. In particular, the real devaluation of the ruble against the US dollar generally causes our costs to decrease in US dollar terms, and vice versa. The appreciation of the purchasing power of the US dollar in the Russian Federation calculated on the basis of the ruble-dollar exchange rates and the level of inflation in Russia was 12.4% in 2009, compared to 2008. The year-end ruble-dollar exchange rate exceeded the opening rate by 2.9%.

The following table gives data on inflation in Russia and the change in the ruble-dollar exchange rate.

	2009	2008	2007
Ruble inflation (CPI), %	8.9	13.3	11.9
Change of the ruble-dollar exchange rate, %	(2.9)	(19.7)	6.8
Average exchange rate for the period (ruble to US dollar)	31.72	24.86	25.58
Exchange rate at the end of the period (ruble to US dollar)	30.24	29.38	24.55

Tax burden

Given the relative size of our activities in Russia, our tax profile is largely determined by the taxes payable in Russia (based on records maintained under Russian legislation – not US GAAP). In 2009, 2008 and 2007, the tax charge on the operations in Russia was approximately 81%, 86% and 86% of our total tax charge, respectively.

Apart of income tax, fundamental taxes specific to the oil industry in Russia are mineral extraction tax, excise and export tariffs. In addition to above mentioned taxes, we are subject to a number of other taxes in Russia, including:

- social taxes;
- VAT;
- property tax;
- other local and regional taxes.

The effective rates of total taxes and tariffs (total taxes, including income taxes, taxes other than on income and excise and export tariffs, divided by income before taxes and tariffs) for 2009, 2008 and 2007, respectively, were 75%, 81% and 75%. In 2009, tax expenses in Russia were about 43% of the domestic and export sales revenue of Russian companies of the Group.

The measures that we use for tax planning and management strategies have been based on our understanding of tax legislation existing at the time of implementation of these measures. We are subject to tax authority audits on an ongoing basis, as is normal in the Russian environment, and, at times, the authorities have attempted to impose significant additional taxes on us. We believe that we have adequately met and provided for tax liabilities based on our interpretation of existing tax legislation. However, the relevant authorities may have differing interpretations and the effects could be significant.

The following table represents average enacted rates for taxes specific to the oil industry in Russia for the respective periods.

		2009[1]	Change to 2008, %	2008[1]	Change to 2007, %	2007[1]
Export tariffs on crude oil	$/tonne	179.93	(49.3)	355.08	71.8	206.70
Export tariffs on refined products						
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	$/tonne	133.54	(46.9)	251.53	65.9	151.59
Liquid fuels (fuel oil)	$/tonne	71.93	(46.9)	135.51	66.0	81.64
Excise on refined products						
Straight-run gasoline	RUR/tonne	3,900.00	46.8	2,657.00	–	2,657.00
High-octane gasoline	RUR/tonne	3,629.00	–	3,629.00	–	3,629.00
Low-octane gasoline	RUR/tonne	2,657.00	–	2,657.00	–	2,657.00
Diesel fuel	RUR/tonne	1,080.00	–	1,080.00	–	1,080.00
Motor oils	RUR/tonne	2,951.00	–	2,951.00	–	2,951.00
Mineral extraction tax						
Crude oil	RUR/tonne	2,302.85	(30.8)	3,328.35	34.6	2,472.67
Natural gas	RUR/1,000 m^3	147.00	–	147.00	–	147.00

[1] Average values.

Tax rates set in rubles and translated at the average exchange rates are as follows:

		2009[1]	Change to 2008, %	2008[1]	Change to 2007, %	2007[1]
Excise on refined products						
Straight-run gasoline	$/tonne	122.94	15.0	106.90	2.9	103.88
High-octane gasoline	$/tonne	114.40	(21.7)	146.01	2.9	141.89
Low-octane gasoline	$/tonne	83.76	(21.7)	106.90	2.9	103.88
Diesel fuel	$/tonne	34.04	(21.7)	43.45	2.9	42.23
Motor oils	$/tonne	93.02	(21.7)	118.73	2.9	115.38
Mineral extraction tax						
Crude oil	$/tonne	72.59	(45.8)	133.91	38.5	96.68
Natural gas	$/1,000 m^3	4.63	(21.7)	5.91	2.9	5.75

[1] Average values.

The rates of taxes specific to the oil industry in Russia are linked to international crude oil prices and are changed in line with them. The methods to determine the rates for such taxes are presented below.

Crude oil extraction tax rate. During 2005-2008, the base rate was 419 rubles per metric tonne extracted and it was adjusted depending on the international market price of Urals blend and the ruble exchange rate. The tax rate was zero when the average Urals blend international market price for a tax period was less than or equal to $9.00 per barrel. Each $1.00 per barrel increase in the international Urals blend price over the threshold ($9.00 per barrel) resulted in an increase of the tax rate by $1.61 per tonne extracted (or $0.22 per barrel extracted using a conversion factor of 7.33).

Effective from January 1, 2009, the tax rate calculation was changed. The base rate remained the same, while the threshold crude oil price up to which the tax rate is zero was raised from $9.00 to $15.00 per barrel. This leads to a $1.3 per barrel decrease in crude oil extraction tax expenses in Russia. Also, the list of regions where, depending on the period and volume of production, the zero crude oil extraction tax rate applies was extended. In particular, it now includes Caspian offshore and the Nenetsky Autonomous District, where the Group explores and produces hydrocarbons.

Effective from January 1, 2007, the crude oil extraction tax rate varies depending on the development and depletion of a particular oilfield. The tax rate is zero for extra-heavy crude oil and for crude oil produced in certain regions of Eastern Siberia, depending on the period and volume of production. For crude oil produced in other regions the tax rate calculation described above should be multiplied by a coefficient characterizing the depletion of a particular oilfield. The coefficient is equal to 1.0 for oilfields with depletion below 80%. Each 1% increase of depletion of a particular oilfield above 80% results in a decrease of the coefficient by 0.035. The minimum value of the coefficient is 0.3. The depletion level assessment is based on crude oil production and reserves information reported to the Russian government.

Natural gas extraction tax rate. The mineral extraction tax on natural gas production is calculated using a flat rate. The current rate of 147 rubles per thousand cubic meters of natural gas extracted has been in effect since January 1, 2006.

Crude oil export duty rate is calculated on a progressive scale. The rate is zero when the average Urals blend international market price is less than or equal to approximately $15.00 per barrel ($109.50 per metric tonne). If the Urals blend price is between $15.00 and $20.00 per barrel ($146.00 per metric tonne), each $1.00 per barrel increase in the Urals blend price over $15.00 results in an increase of the crude oil export duty rate by $0.35 per barrel exported. If the Urals blend price is between $20.00 and $25.00 per barrel ($182.50 per metric tonne), each $1.00 per barrel increase in the Urals blend price over $20.00 results in an increase of the crude oil export duty rate by $0.45 per barrel exported. Each $1.00 per barrel increase in the Urals blend price over $25.00 per barrel results in an increase of the crude oil export duty rate by $0.65 per barrel exported.

Prior to October 1, 2008, the Russian government set export tariff rates for two-month periods. The rates in a specific two-month period were based on Urals blend international market prices in the preceding two months. Thus, the calculation method that the Russian government employed to determine export tariff rates resulted in a two-month gap between movements in crude oil prices and the revision of the export duty rate based on those crude oil prices.

This method of calculation was amended in September 2008. The Russian government set the specific crude oil export duty rate for October, November and December 2008 at $372.20, $287.30 and $192.10 per tonne, respectively, in order to compensate oil companies the negative effect of sharply decreased crude oil prices. Effective from December 2008, the crude oil export duty rate is revised monthly on the basis of the immediately preceding one-month period of crude oil price monitoring.

Export duty rates on refined products are set by the Russian government. The rate of export duty depends on internal demand for refined products and international crude oil market conditions.

Crude oil and refined products exported to CIS countries, other than Ukraine and Belarus, are not subject to export duties. Crude oil exported from Russia to Belarus was subject to export duties calculated in 2009 with the application of a coefficient 0.356 (0.335 in 2008) to the regular export duty rate set by the Russian government.

In 2010, under the agreement between the Russian Federation and Belarus, crude oil exported from Russia to Belarus up to total amount of 6.3 million tonnes will not be subject to export duty. Volumes of crude oil above this limit will be taxed at a regular export duty rate.

Excise on refined products. The responsibility to pay excises on refined products in Russia is imposed on refined product producers (except for straight-run gasoline). In other countries where the Group operates, excises are paid either by producers or retailers depending on the local legislation.

Income tax. Before 2009, operations in the Russian Federation were subject to an income tax rate up to 24%. The Federal income tax rate was 6.5% and the regional income tax rate varied from 13.5% to 17.5% at the discretion of the individual regional administrations. Starting on January 1, 2009, the Federal income tax rate was decreased to 2.0% and the regional income tax rate varies between 13.5% and 18.0%. The Group's foreign operations are subject to taxes at the tax rates applicable to the jurisdictions in which they operate.

Transportation of crude oil and refined products in Russia

The main Russian crude oil production regions are remote from the main crude oil and refined products markets. Therefore, access of crude oil production companies to the markets is dependent on the extent of diversification of the transport infrastructure and access to it. As a result, transportation cost is an important macroeconomic factor affecting our net income.

Transportation of crude oil produced in Russia to refineries and export destinations is performed primarily through the trunk oil pipeline system of state-owned OAO AK Transneft ("Transneft"). Access to the Transneft crude oil export pipeline network is allocated quarterly, based on recent volumes produced and delivered through the pipeline and proposed export destinations. The crude oil transported by Transneft is Urals blend – a mix of crude oils of various qualities. Therefore Russian companies that produce crude oil of a higher quality, cannot obtain benefits from selling it using Transneft's pipeline. Alternative access to international markets bypassing Transneft's export routes can be obtained through railroad transport, by tankers, and by the export infrastructure of oil producing companies. Our own export infrastructure includes the Vysotsk terminal in the Leningrad region, the Varandey terminal in the Nenetsky Autonomous District and the Svetly terminal in the Kaliningrad region. We use the offshore ice-resistant terminal in Varandey with annual capacity of 12 million tonnes to export crude oil produced by our joint venture with ConocoPhillips located in Northern Timan-Pechora. Through the Svetly terminal we export crude oil primarily produced by OOO LUKOIL-Kaliningradmorneft, our subsidiary operating in the Kaliningrad region, and refined products. Its annual capacity is 6 million tonnes. We use the Vysotsk terminal to export refined products. In the future we expect to use the terminal to export both crude oil and refined products, depending on market conditions. Currently it has a capacity of 12 million tonnes per year and it can be expanded up to 15 million tonnes per year.

Transportation of refined products in Russia is performed by railway transport and the pipeline system of OAO AK Transnefteproduct. The Russian railway infrastructure is owned and operated by OAO Russian Railways. Both these companies are state-owned. Besides transportation of refined products, OAO Russian Railways provides oil companies with crude oil transportation services. We transport the major part of our refined products by railway transport.

As the activities of the above mentioned companies fall under the scope of natural monopolies, the fundamentals of their tariff policies are defined by the state authorities to ensure the balance of interests of the state and all participants in the transportation process. Transportation tariffs of natural monopolies are set by the Federal Service for Tariffs of the Russian Federation ("FST"). The tariffs are dependent on transport destination, delivery volume, distance of transportation, and several other factors. Changes in the tariffs depend on inflation forecasts by the Ministry of Economic Development of the Russian Federation, the investment needs of owners of the transport infrastructure, other macroeconomic factors, and compensation of economically reasonable expense, incurred by entities of the natural monopolies. Tariffs are revised by the FST at least annually.

Year ended December 31, 2009, compared to years ended December 31, 2008 and December 31, 2007

The table below details certain income and expense items from our consolidated statements of income for the periods indicated.

	2009	2008	2007
	(millions of US dollars)		
REVENUES			
Sales (including excise and export tariffs)	81,083	107,680	81,891
COSTS AND OTHER DEDUCTIONS			
Operating expenses	(7,124)	(8,126)	(6,172)
Cost of purchased crude oil, gas and products	(31,977)	(37,851)	(27,982)
Transportation expenses	(4,830)	(5,460)	(4,457)
Selling, general and administrative expenses	(3,306)	(3,860)	(3,207)
Depreciation, depletion and amortization	(3,937)	(2,958)	(2,172)
Taxes other than income taxes	(6,474)	(13,464)	(9,367)
Excise and export tariffs	(13,058)	(21,340)	(15,033)
Exploration expense	(218)	(487)	(307)
Loss on disposals and impairments of assets	(381)	(425)	(123)
INCOME FROM OPERATING ACTIVITIES	**9,778**	**13,709**	**13,071**
Interest expense	(667)	(391)	(333)
Interest and dividend income	134	163	135
Equity share in income of affiliates	351	375	347
Currency translation (loss) gain	(520)	(918)	35
Other non-operating expense	(13)	(244)	(240)
INCOME BEFORE INCOME TAXES	**9,063**	**12,694**	**13,015**
Current income taxes	(1,922)	(4,167)	(3,410)
Deferred income taxes	(72)	700	(39)
TOTAL INCOME TAX EXPENSE	**(1,994)**	**(3,467)**	**(3,449)**
NET INCOME	**7,069**	**9,227**	**9,566**
Less: net income attributable to noncontrolling interests	(58)	(83)	(55)
NET INCOME ATTRIBUTABLE TO OAO LUKOIL	**7,011**	**9,144**	**9,511**
Basic and diluted earning per share of common stock attributable to OAO LUKOIL (in US dollars)	8.28	10.88	11.48

The analysis of the main financial indicators of the financial statements is provided below.

Sales revenues

Sales breakdown	2009	2008	2007
	(millions of US dollars)		
Crude oil			
Export and sales on international markets other than CIS	18,276	22,382	18,346
Export and sales to CIS	1,638	1,625	912
Domestic sales	735	600	440
	20,649	**24,607**	**19,698**
Refined products			
Export and sales on international markets			
Wholesale	38,023	50,553	37,971
Retail	8,865	11,989	9,183
Domestic sales			
Wholesale	3,820	8,049	5,862
Retail	4,281	5,823	3,721
	54,989	**76,414**	**56,737**
Petrochemicals			
Export and sales on international markets	574	1,232	1,569
Domestic sales	514	880	733
	1,088	**2,112**	**2,302**
Gas and gas products			
Export and sales on international markets	1,091	926	562
Domestic sales	548	985	831
	1,639	**1,911**	**1,393**
Other			
Export and sales on international markets	1,031	1,286	947
Domestic sales	1,687	1,350	814
	2,718	**2,636**	**1,761**
TOTAL SALES	81,083	107,680	81,891

Sales volumes	2009	2008	2007
	(thousands of barrels)		
Crude oil			
Export and sales on international markets other than CIS	305,273	242,784	268,974
Export and sales to CIS	39,106	31,629	19,879
Domestic sales	21,909	15,408	11,757
	366,288	**289,821**	**300,610**
	(thousands of tonnes)		
Crude oil			
Export and sales on international markets other than CIS	41,647	33,122	36,695
Export and sales to CIS	5,335	4,315	2,712
Domestic sales	2,989	2,102	1,604
	49,971	**39,539**	**41,011**
	(thousands of tonnes)		
Refined products			
Export and sales on international markets			
Wholesale	76,885	67,669	64,394
Retail	7,863	8,200	7,910
Domestic sales			
Wholesale	9,796	13,314	13,704
Retail	6,216	5,964	4,853
	100,760	**95,147**	**90,861**
TOTAL SALES VOLUME OF CRUDE OIL AND REFINED PRODUCTS	150,731	134,686	131,872

Realized average sales prices	2009		2008		2007	
	($/barrel)	($/tonne)	($/barrel)	($/tonne)	($/barrel)	($/tonne)
Average realized price international						
Oil (excluding CIS)	59.87	438.84	92.19	675.76	68.21	499.96
Oil (CIS)	41.89	307.05	51.38	376.58	45.86	336.15
Refined products						
Wholesale		494.55		747.06		589.66
Retail		1,127.44		1,462.14		1,160.90
Average realized price within Russia						
Crude oil	33.56	245.97	38.97	285.66	37.43	274.37
Refined products						
Wholesale		389.92		604.55		427.74
Retail		688.74		976.40		766.67

During 2009, our revenues decreased by $26,597 million, or by 24.7%, compared to 2008 (in 2008 increased by $25,789 million, or by 31.5%, compared to 2007). Our revenues from crude oil sales decreased by $3,958 million, or by 16.1% (in 2008 increased by $4,909 million, or by 24.9%, compared to 2007). Our revenues from sales of refined products decreased by $21,425 million, or by 28.0% (in 2008 increased by $19,677 million, or by 34.7%, compared to 2007). In 2009, the decrease in sales revenue was due to sharp decrease in hydrocarbon prices, compared to 2008. Moreover, the devaluation of the ruble against the US dollar also seriously affected our average realized prices in Russia.

At the same time, we increased crude oil production and trading, which raised our crude oil sales by 26.4% in terms of volumes. The increase in crude oil production was a result of commencement of production on the Yuzhnoye Khylchuyu oil field in August 2008, from which we produced about 7.0 million tonnes in 2009, compared to 1.5 million tonnes in 2008.

We also increased our refined product sales outside of Russia in terms of volumes by 11.7%, mainly due to commencement of processing at ISAB and TRN. In 2009, our share of production at these refineries amounted to 6.2 million tonnes and 1.5 million tonnes, respectively. In 2008, we produced 0.6 million tonnes at ISAB.

Sales of crude oil and refined products on international markets, including the CIS, accounted for 87.4% of the total sales volume in 2009 (84.1% in 2008 and 84.7% in 2007).

Sales of crude oil

2009 vs. 2008

Our total crude oil sales revenues decreased by 16.1%. We sell crude oil to third parties mostly outside Russia and CIS, the international sales revenue, which accounted for approximately 88.5% of our total crude oil sales revenue in 2009 and 91.0% in 2008, decreased by 18.3% due to a decrease in sales prices by 35.1%. At the same time, the volume of international crude oil sales increased by 25.7% due to increased crude oil trading and export from Russia.

In 2009, we increased the volume of domestic sales to benefit from current market conditions.

In 2009, our revenue from export of crude oil from Russia both to the Group companies and third parties amounted to $17,485 million.

2008 vs. 2007

The 24.9% increase in our total crude oil sales from 2007 to 2008 was attributable primarily to an increase in our international crude oil sales revenues (excluding CIS). This sales revenue, which accounted for approximately 91.0% of our total crude oil sales revenue in 2008 and 93.1% in 2007, increased by 22.0% primarily due to an increase in sales prices by 35.2%. At the same time the volume of international crude oil sales decreased by 9.7%, compared to 2007 as a result of decreased crude oil production and increased crude oil refining in Russia.

Sales of refined products

2009 vs. 2008.

In 2009, our revenue from the wholesale of refined products outside of Russia decreased by $12,530 million, or by 24.8%, compared to 2008, due to decreased average realized price by 33.8%. At the same time, commencement of crude oil refining at ISAB and TRN and expansion of trading activities led to an increase in volumes sold by 13.6%.

In 2009, our revenue from international retail sales decreased by $3,124 million, or by 26.1%, compared to 2008, mainly due to a decrease in average retail prices by 22.9%. Sales volumes also decreased following the negative economic situation.

In 2009, our revenue from the wholesale of refined products on the domestic market decreased by $4,229 million, or by 52.5%, compared to the previous year, due to a decrease in the average realized price by 35.5%, and a decrease in volumes sold by 3,518 thousand tonnes, or by 26.4%. The decrease in volume sold was a result of decreased domestic purchases and increased refined product exports from Russia by 7.7%.

In 2009, our revenue from retail sales in Russia decreased by $1,542 million, or by 26.5%, compared to the 2008, due to a decrease in prices. In 2009, our retail sales revenue was 52.8% of total refined products sales in Russia (in 2008 – 42.0%).

In 2009, our revenue from export of refined products from Russia both to Group companies and third parties amounted to $11,414 million.

2008 vs. 2007

In 2008, our revenue from the wholesale of refined products outside Russia increased by $12,582 million, or by 33.1%, compared to 2007, mainly due to an increase in the average realized price.

In 2008, our revenue from international retail sales increased by $2,806 million, or by 30.6%, compared to 2007, mainly due to an increase in average retail prices by 25.9%. The increase of retail sales volumes outside Russia amounted to 290 thousand tonnes, or 3.7%. This increase was attributable to the expansion of our retail network. In 2008, we acquired petrol stations in Turkey, petrol stations and storage facilities in Bulgaria, besides, in the second quarter of 2007, we acquired petrol stations in seven European countries. Our international retail sales include supplies of refined products to third party retail networks under long-term contracts with pricing similar to retail pricing.

In 2008, our revenue from the wholesale of refined products on the domestic market increased by $2,187 million, or by 37.3%, compared to the previous year, due to an increase in the average realized price by 41.3%.

In 2008, our revenue from retail sales in Russia increased by $2,102 million, or by 56.5%, compared to 2007, due to an increase both in sales volumes and prices. Revenue from retail sales was 42.0% of total refined products sales in Russia in 2008 (in 2007 – 38.8%).

Sales of petrochemical products

2009 vs. 2008

In 2009, our revenue from sales of petrochemical products decreased by $1,024 million, or by 48.5%, compared to 2008. This resulted from a decrease in prices by 35.8% and a decrease in sales volumes by 19.7%. The decrease in volumes resulted from general overhauls at our Russian plants and a temporary shutdown of our petrochemical plant Karpatnaftochim Ltd. in Ukraine, which was stopped for modernization and construction of a chlorine and caustic production line in May 2008. Besides, the overall negative situation on the world petrochemical markets led to a decrease in sales volumes.

2008 vs. 2007

In 2008, our revenue from sales of petrochemical products decreased by $190 million, or by 8.3%, compared to 2007. This resulted from the decrease in sales volumes by 15.5%. At the same time the prices increased by 8.6%. The decrease in volumes resulted from a temporary shutdown of our Ukrainian petrochemical plant Karpatnaftochim Ltd. In May 2008, this plant was stopped for modernization and construction of chlorine and caustic production line. Moreover, overall negative situation on the world petrochemical markets led to decrease of the sales volumes.

Sales of gas and gas products

2009 vs. 2008

In 2009, sales of gas and gas refined products decreased by $272 million, or by 14.2%, compared to 2008. Gas products sales revenue decreased by $158 million, or by 13.2%, primarily as a result of decrease in prices. Natural gas sales revenue amounted to $571 million – a decrease of 17.2%, compared to 2008. Decrease in domestic sales volumes and selling prices were partly compensated by an increase in realized selling price in Uzbekistan.

Our major purchaser of natural gas produced in the Russian Federation is Gazprom. In 2009, we sold 5,936 million cubic meters of natural gas to Gazprom (7,856 million cubic meters in 2008). The average realized price decreased by 21.6% to $33.4 per 1,000 cubic meters as a result of the ruble devaluation.

2008 vs. 2007

In 2008, sales of gas and gas refined products amounted to $1,911 million, which is 37.2% more than in 2007. This was due to an increase in gas products and natural gas sales revenues. Gas products sales revenue increased by $215 million, or by 21.9%, compared to 2007, mainly as a result of an increase in prices for gas products both in Russia and abroad. Natural gas sales revenue amounted to $690 million (an increase of 77.4%, compared to 2007). This increase was a result of the commencement of natural gas production in Uzbekistan and Azerbaijan, and an increase in average realized prices in Russia.

Sales of other products

Other sales include revenue of our electric power generating companies, non-petroleum sales through our retail network, and other services provided and goods not related to our primary activities (such as electricity, heat, transportation, etc.) sold by our production and marketing companies.

2009 vs. 2008

In 2009, our other sales increased by $82 million, or by 3.1%. The increase was a result of scaling up our power generating and distribution sector, which emerged in the Group with the acquisition of TGK-8 in May 2008. At the same time, this was partially offset by decrease in other sales outside of Russia primarily through retail stations and transportation services, and effect of devaluation of the ruble in Russia.

During 2009, sales of goods and other products from our retail stations amounted to $568 million, a decrease of $45 million from the level of 2008. This was mainly because of an overall decrease of such sales outside of Russia as a result of the adverse macroeconomic environment.

2008 vs. 2007

In 2008, other sales increased by $875 million, or by 49.7%.

During 2008, sales of goods and other products from our retail outlets amounted to $613 million, an increase of $188 million above the level of 2007. This was mainly attributable to the expansion of our retail network.

The Group develops its electric power business. Related sales increased by $528 million, compared to 2007, mainly as a result of the acquisition of TGK-8.

Operating expenses

Operating expenses include the following:

	2009	2008	2007
	(millions of US dollars)		
Hydrocarbon extraction expenses	2,787	3,208	2,757
Own refining expenses	923	1,115	880
Refining expenses at third parties and affiliated refineries	713	439	242
Excise included in processing fee paid to third parties refineries	54	116	158
Petrochemical expenses	127	235	272
Expenses on crude oil transportation to refineries	955	1,072	848
Other operating expenses	1,781	1,691	1,271
	7,340	**7,876**	**6,428**
Change in operating expenses in crude oil and refined products inventory originated within the Group[1]	(216)	250	(256)
TOTAL OPERATING EXPENSES	**7,124**	**8,126**	**6,172**

[1] The change in operating expenses in crude oil and refined products inventory originating within the Group includes extraction and refining expenses related to crude oil and refined products produced by the Group during the reporting period, but not sold to third party.

Compared to 2008, operating expenses decreased by $1,002 million, or by 12.3%, which is mainly explained by general decrease in operating expenses in Russia due to the ruble devaluation. At the same time, refining expenses at third party and affiliated refineries increased significantly due to the commencement of refining crude oil at ISAB at the end of 2008 and at TRN in September 2009.

Hydrocarbon extraction expenses

Our extraction expenses include expenditures related to repairs of extraction equipment, labor costs, expenses on artificial stimulation of reservoirs, fuel and electricity costs, property insurance of extraction equipment and other similar costs.

2009 vs. 2008

In 2009, our extraction expenses decreased by $421 million, or by 13.1%, compared to 2008, despite increased crude oil production by 2.5% and an increase in expenses for power supply. The decrease was mainly a result of the effect of the real ruble devaluation against the US dollar. Our average hydrocarbon extraction cost decreased from $4.12 to $3.56 per BOE, or by 13.6%, compared to 2008.

2008 vs. 2007

In 2008, our extraction expenses increased by $451 million, or by 16.4%, compared to 2007. The increase resulted from the effect of the real ruble appreciation against the US dollar, increased expenses for energy supply, materials, artificial stimulation of reservoirs and labor. Our average hydrocarbon extraction cost per BOE increased from $3.58 to $4.12, or by 15.1%, compared to 2007. At the same time in the forth quarter of 2008 our extraction cost decreased to $4.01 per barrel, compared to $4.29 per barrel in the third quarter of 2008 due to the ruble devaluation.

Own refining expenses

2009 vs. 2008

In 2009, our refining expenses decreased by $192 million, or by 17.2%, compared to 2008.

Refining expenses at our domestic refineries decreased by 14.2%, or by $111 million, mainly as a result of the devaluation of the ruble against the US dollar and cost cutting program implemented since the fourth quarter of 2008. This was despite an increase in power supply and overhaul costs.

Refining expenses at our international refineries decreased by 24.3%, or by $81 million. This resulted mainly from a decrease in the cost of power supply at our refinery in Bulgaria. In 2009, we produced energy from our own resources, while, in 2008, we purchased gas for this purpose from third party. Besides, decreased production and changes of the exchange rates of local currencies to the US dollar additionally decreased our refining expenses abroad.

2008 vs. 2007

In 2008, refining expenses increased by $235 million, or by 26.7%, compared to 2007.

Refining expenses at our domestic refineries increased by 19.8%, or by $129 million, mainly as a result of increased expenses for power supply, real ruble appreciation against the US dollar and increased production volumes.

Refining expenses at our international refineries increased by 46.5%, or by $106 million. This resulted mainly from increased expenses for power supply, the effect of appreciation of the exchange rates of the Romanian and Bulgarian currencies to the US dollar, and an increase in production volumes mainly as a result of commencement of operations of Odessa refinery after a wide-scale upgrade.

Refining expenses at third party and affiliated refineries

Along with our own production of refined products we refine crude oil at third party and affiliated refineries both in Russia and abroad.

2009 vs. 2008

Due to commencement of crude oil refining at ISAB and TRN we doubled the processing volumes compared to 2008. However, this was partially compensated by a decrease of processing costs and decreased volumes in Russia and Belarus. Thus, in 2009 refining expenses at third party and affiliated refineries increased by 62.4%, compared to 2008.

2008 vs. 2007

In 2008, refining expenses at third party and affiliated refineries increased by 81.4%, compared to 2007, as a result of increased refining costs in Russia that are linked to crude oil prices. Also, we increased refining volumes in Belarus, and, in December 2008, we commenced crude oil refining at ISAB.

Petrochemical operating expenses

2009 vs. 2008

In 2009, operating expenses of our petrochemical companies decreased by $108 million, or by 46.0%, compared to 2008, due to a general decrease of production volumes. In May 2008, we stopped our Ukrainian petrochemical plant Karpatnaftochim Ltd. for modernization and construction of a chlorine and caustic production line.

2008 vs. 2007

In 2008, operating expenses of our petrochemical companies decreased by $37 million, or by 13.6%, compared to 2007, due to decrease of production volumes. The decrease resulted from a temporary shutdown of our petrochemical plant Karpatnaftochim Ltd. in Ukraine. In May 2008, this plant was stopped for modernization and construction of chlorine and caustic production line.

Expenses for crude oil transportation to refineries

2009 vs. 2008

Expenses for crude oil transportation to refineries decreased in 2009 by $117 million, or by 10.9%, compared to 2008, due to a decrease in transportation tariffs as a result of a real ruble devaluation in Russia (see Transportation expenses below), and change in crude oil supply structure – an increase in the proportion of crude oil we purchased from third parties. The price of purchased crude oil typically includes transportation costs, and the crude oil is purchased from a source geographically closer to the destination refinery than crude oil from our own production.

2008 vs. 2007

Expenses on crude oil transportation to refineries increased in 2008 by $224 million, or by 26.4%, compared to 2007, due to an increase in transportation tariffs and volumes transported.

Other operating expenses

Other operating expenses include expenses of the Group's upstream and downstream enterprises that do not relate to their core activities, namely sales of electricity, heat, transportation services, other goods, etc., operating expenses of our gas processing plants, the costs of other services provided and goods sold by our marketing companies, operating expenses of our power generating companies and of other non-core businesses of the Group.

2009 vs. 2008

In 2009, our other operating expenses increased by $90 million, or by 5.3%, compared to 2008. The increase was a result of scaling up our power generating and distribution sector, which emerged in the Group with the acquisition of TGK-8 in May 2008. However, this was partially compensated by the ruble devaluation, decrease in expenses related to other sales through petrol stations and transportation services outside of Russia.

2008 vs. 2007

In 2008, our other operating expenses increased by $420 million, or by 33.0%, compared to 2007. This was due to a general increase in other sales including growth of transportation and other services provided by the Group in the international segment. Half of the increase of other operating expenses was attributable to changes in the Group structure, mainly to the acquisition of TGK-8 in May 2008.

Cost of purchased crude oil, gas and products

2009 vs. 2008

Cost of purchased crude oil, gas and products decreased by $5,874 million in 2009, or by 15.5%, compared to 2008, due to a decrease in international crude oil and refined products prices. The effect of decreased prices was partly compensated by an increase in purchases due to scaling up trading operations outside of Russia, especially in the fourth quarter of 2009.

Cost of purchased crude oil, gas and products includes the result of hedging of international crude oil and refined products sales. In 2009, we recognized a $781 million expense from hedging, compared to a $902 million gain in 2008.

2008 vs. 2007

Cost of purchased crude oil, gas and products increased by $9,869 million in 2008, or by 35.3%, compared to 2007, due to increases in international crude oil and refined products prices and in volumes of crude oil purchases.

Cost of purchased crude oil, gas and products includes the result of hedging of international crude oil and refined products sales. In 2008, we recognized a $902 million gain from hedging, compared to an expense of $575 million in 2007.

Cost of purchased crude oil, gas and products included purchases of natural gas and fuel oil to supply TGK-8.

Transportation expenses

2009 vs. 2008

In 2009, our transportation expenses decreased by $630 million, or by 11.5%, compared to 2008. This was primarily due to a decrease in freight rates and railway transportation tariffs in Russia. It should be noted that ruble denominated transportation tariffs in Russia increased in 2009, but this increase was offset by the ruble devaluation.

Our actual transportation expenses related to crude oil and refined products deliveries to various export destinations, weighted by volumes transported, changed in 2009, compared to the previous year, as follows: crude oil pipeline tariffs increased by 8.9%, railway tariffs for refined products transportation decreased by 10.9%, crude oil and refined products freight rates decreased by 42.3% and 50.1%, respectively.

2008 vs. 2007

In 2008, our transportation expenses increased by $1,003 million, or by 22.5%, compared to 2007. This was due to an increase in transportation tariffs and an overall increase in refined products sales volumes in Russia and internationally.

Our actual transportation expenses related to crude oil and refined products deliveries to various export destinations, weighted by volumes transported, changed in 2008, compared to the previous year, as follows: crude oil and refined products freight rates increased by 15.7% and 20.4%, respectively; crude oil pipeline tariffs increased by 15.9%; railway tariffs for refined products transportation increased by 13.6%.

Selling, general and administrative expenses

Selling, general and administrative expenses include general business expenses, payroll costs (excluding extraction entities' and refineries' production staff costs), insurance costs (except for property insurance related to extraction and refinery equipment), costs of maintenance of social infrastructure, movement in bad debt provision and other expenses.

2009 vs. 2008

In 2009, our selling, general and administrative expenses decreased by $554 million, or by 14.4%, compared to 2008. The decrease was primarily due to the devaluation of the ruble. Nevertheless, this was partially offset by the increase of expenses for creation of allowance for bad debts and the effect of changes in the Group's structure.

2008 vs. 2007

In 2008, our selling, general and administrative expenses increased by $653 million, or by 20.4%, compared to 2007. The growth was mainly due to real ruble appreciation, expansion of our activities both in Russia and internationally, and an overall increase in selling expenses.

Depreciation, depletion and amortization

Depreciation, depletion and amortization expenses include depletion of assets fundamental to production, depreciation of other productive and non-productive assets and certain intangible assets.

2009 vs. 2008

Our depreciation, depletion and amortization expenses increased by $979 million, or by 33.1%, compared to 2008. The increase was a result of the Company's capital expenditures and the corresponding increase in depreciable assets, in particular due to putting in production the Yuzhnoye Khylchuyu oil field.

2008 vs. 2007

Our depreciation, depletion and amortization expenses increased by $786 million, or by 36.2%, compared to 2007. The increase was a result of the

Company's capital expenditures and the corresponding increase in depreciable assets, in particular due to putting in production the Yuzhnoe Khylchuyu oil field. Besides, the decrease of our proved reserves resulted in an increase in depreciation of our oil and gas producing assets.

Exploration expenses

2009 vs. 2008

During 2009, exploration expense decreased by $269 million, or by 55.2%, compared to 2008. Dry hole costs decreased by $200 million to $117 million.

In 2009, we charged to expense the cost of a dry well in Saudi Arabia totaling $56 million. Also, we expensed dry hole costs related to our project in Azerbaijan in the amount of $9 million.

In 2009, we charged to expense $30 million as idle costs related to first phase of drilling an exploratory well in Ghana.

Dry hole costs in Russia amounted to $22 million, primarily relating to Western Siberia.

2008 vs. 2007

During 2008, exploration expense increased by $180 million, or by 58.6%, compared to 2007. Dry hole costs increased by $174 million to $317 million.

In 2008, we charged to expense the costs of three dry wells in Saudi Arabia totaling $122 million. Also, we expensed dry hole costs related to our projects in Kazakhstan and Columbia in amount of $20 million and $45 million, respectively. The amount of $93 million was charged to expense in the fourth quarter of 2008 in regard of our project Yalama in Azerbaijan.

Interest expense

2009 vs. 2008

In 2009, interest expense amounted to $667 million, which is 70.6% more than in the previous year. This was a result of the termination of interest capitalization related to assets in Timan-Pechora after completion of their construction and a general increase in our indebtedness and cost of borrowings due to unfavorable situation on capital markets (see Liquidity and capital resources – Financing activities).

2008 vs. 2007

In 2008, interest expense amounted to $391 million, which is $58 million, or 17.4%, more than in previous year. In 2008, interest expense was affected by termination of interest capitalization related to certain assets in Timan-Pechora due to completion of their construction and general increase in our indebtedness.

Equity share in income of affiliates

The Group has investments in equity method affiliates and corporate joint ventures. These companies are primarily engaged in crude oil exploration, production, marketing and distribution operations in the Russian Federation, crude oil production and marketing in Kazakhstan and refining operations in Europe. Our largest affiliates are Turgai Petroleum, an exploration and production company operating in Kazakhstan, and ISAB and TRN refineries. In the end of 2009, we increased our share in LUKARCO from 54% to 100%, thus increasing our stake in Tengizchevroil, an exploration and production joint-venture in Kazakhstan, to 5%.

2009 vs. 2008

Compared to 2008, our share in income of affiliates decreased by $24 million, or by 6.4%.

2008 vs. 2007

Compared to 2007, our share in income of affiliates increased by $28 million, or by 8.1%.

Currency translation (loss) gain

2009 vs. 2008

In 2009, currency translation loss amounted to $520 million, of which $437 million refer to the Russian segment of the Group, and $83 million – to the international segment.

2008 vs. 2007

In 2008, currency translation loss amounted to $918 million, of which $631 million refer to the Russian segment of the Group, and $287 million – to the international segment. Those losses mostly refer to the fourth quarter results.

The main reasons for those losses were decrease in the US dollar value of the ruble-nominated accounts receivables, advances, VAT recoverable, other taxes prepaid (less value of ruble-nominated liabilities), and fluctuations of euro-dollar exchange rate, which affected results of some operations performed by the Group outside of Russia.

Taxes other than income taxes

	2009	2008	2007
	(millions of US dollars)		
In Russia			
Mineral extraction taxes	5,399	12,267	8,482
Social security taxes and contributions	330	435	385
Property tax	438	374	284
Other taxes	92	180	105
Total in Russia	**6,259**	**13,256**	**9,256**
International			
Mineral extraction taxes	53	–	–
Social security taxes and contributions	69	77	57
Property tax	32	31	29
Other taxes	61	100	25
Total internationally	**215**	**208**	**111**
TOTAL	6,474	13,464	9,367

2009 vs. 2008

In 2009, taxes other than income taxes decreased by 51.9%, or by $6,990 million, compared to 2008, mainly due to a decrease in mineral extraction taxes in Russia. This is explained by a decrease in the tax rate resulting from the low level of crude oil prices. Moreover, the change in the tax rate calculation effective from January 1, 2009 led to approximately $754 million decrease in the extraction taxes. Effect from the application of the zero tax rate for crude oil produced mainly in Timan-Pechora and Western Siberia and decreased rate for depleted oilfields led to approximately $961 million tax reduction.

2008 vs. 2007

In 2008, taxes other than income taxes increased by 43.7%, or by $4,097 million, compared to 2007, mainly due to an increase in mineral extraction tax resulting from an increase in the crude oil extraction tax rate.

Excise and export tariffs

Our excise and export tariffs include taxes on sales of refined products and export tariffs on the export of crude oil and refined products.

	2009	2008	2007
	(millions of US dollars)		
In Russia			
Excise tax and sales taxes on refined products	763	956	734
Crude oil export tariffs	6,251	11,911	8,160
Refined products export tariffs	2,306	4,119	2,654
Total in Russia	**9,320**	**16,986**	**11,548**
International			
Excise tax and sales taxes on refined products	3,524	3,984	3,468
Crude oil export tariffs	107	143	–
Refined products export tariffs	107	227	17
Total internationally	**3,738**	**4,354**	**3,485**
TOTAL	13,058	21,340	15,033

2009 vs. 2008

In spite of an increase in crude oil and refined products export volumes, export tariffs decreased by $7,629 million, or by 46.5%, compared to 2008, due to the decrease in tariff rates in Russia because of the crude oil prices decline. The decrease in excises in Russia was due to the ruble devaluation. Despite the fact that the changes in the Group structure contributed $101 million to the excise increase, our international excises decreased by $460 million, or by 11.5%, compared to 2008. Such a fall was a result of a decrease in sales volumes of refined products subject to excise taxes and decrease in excise rates, caused mainly by the changes of the exchange rates of local currencies to the US dollar.

2008 vs. 2007

In spite of a decrease in crude oil export volumes, export tariffs increased by $5,569 million, or by 51.4%, compared to 2007, due to the increase in tariff rates.

The growth in international excises was mainly due to the increase in volumes sold as a result of expansion of our retail network in Europe, the appreciation of the Euro against the US dollar, as the excise rates in most European countries we operate in are either denominated in Euro or tied to it.

Loss on disposals and impairments of assets

2009 vs. 2008

In 2009, loss on disposals and impairments of assets amounted to $381 million, compared to $425 million in 2008.

As a result of an impairment test of exploration and production assets performed in December 2009, the Company recognized an impairment loss of $238 million for certain properties in the Timan-Pechora and Central European regions of Russia. The Group also recognized an impairment loss in amount of $63 million related to our project in Iran due to incapability of undertaking further works because of the threat of economic sanctions of the US Government. Besides, we charged to expense $33 million related to realization of Atashsky project in Kazakhstan.

2008 vs. 2007

In 2008, loss on disposals and impairments of assets amounted to $425 million, compared to $123 million in 2007.

In 2008, the loss included $156 million related to impairment of certain oil and gas assets located in the Timan-Pechora region. The impairment resulted from a decrease in crude oil reserves due to revision of geological models. The loss also included $171 million related to impairment of goodwill and certain retail assets in the United States and Serbia due to the change in the economic environment.

The losses also include the financial result from disposals of a number of non-core assets and individually insignificant impairments of non-performing business units.

Income taxes

2009 vs. 2008

In 2009, our total income tax expense decreased by $1,473 million, or by 42.5%, compared to 2008, due to the decrease in income before income tax by $3,631 million, or by 28.6%.

In 2009, our effective income tax rate was 22.0%, compared to 27.3% in 2008, which is higher than the maximum statutory rate for the Russian Federation (20% in 2009 and 24% in 2008).

2008 vs. 2007

In 2008, our total income tax expense increased by $18 million, or by 0.5%, compared to 2007.

In 2008, our effective income tax rate was 27.3%, compared to 26.5% in 2007, which is higher than the maximum statutory rate for the Russian Federation (24%).

Starting from January 1, 2009, the income tax rate in the Russian Federation was decreased from 24.0% to 20.0%. Moreover, starting from 2009, the tax burden is reduced in Kazakhstan. As a result of this amendment we recalculated the deferred tax assets and liabilities as of December 31, 2008 at reduced income tax rates, which resulted in $299 million of income tax benefit in 2008.

Reconciliation of net income to EBITDA (earnings before interest, income taxes, depreciation and amortization)

	2009	2008	2007
	(millions of US dollars)		
Net income	**7,011**	**9,144**	**9,511**
Add back:			
Income tax expense	1,994	3,467	3,449
Depreciation and amortization	3,937	2,958	2,172
Interest expense	667	391	333
Interest and dividend income	(134)	(163)	(135)
EBITDA	**13,475**	**15,797**	**15,330**

EBITDA is a non-US GAAP financial measure. EBITDA is defined as net income before interest, taxes and depreciation and amortization. The Company believes that EBITDA provides useful information to investors because it is an indicator of the strength and performance of our business operations, including our ability to finance capital expenditures, acquisitions and other investments and our ability to incur and service debt. While depreciation and amortization are considered as operating costs under US GAAP, these expenses primarily represent the non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods. The EBITDA calculation is commonly used as a basis for some investors, analysts and credit rating agencies to evaluate and compare the periodic and future operating performance and value of companies within the oil and gas industry. EBITDA should not be considered in isolation as an alternative to net income, operating income or any other measure of performance under US GAAP. EBITDA does not include our need to replace our capital equipment over time.

Liquidity and capital resources

	2009	2008	2007
	(millions of US dollars)		
Net cash provided by operating activities	8,883	14,312	10,881
Net cash used in investing activities	(8,923)	(13,559)	(9,715)
Net cash provided by (used in) financing activities	87	763	(1,098)

Operating activities

Our primary source of cash flow is funds generated from our operations. During 2009, cash generated by operating activities was $8,883 million, or 37.9% less than in 2008, mainly due to the decrease in sales revenues. Besides, in 2009, our operating cash inflows were affected by an increase of working capital by $2,483 million, compared to January 1, 2009. This was mainly caused by:

- a $897 million net increase in trade accounts receivable and payable;
- an increase in inventory of $1,719 million, resulting mainly from increased hydrocarbons prices;
- a $141 million net increase in tax accounts receivable and payable.

At the same time, the negative effect from the above mentioned factors was partly offset by a $274 million net decrease in other assets and liabilities.

Investing activities

The decrease in cash used in investing activities resulted from a decrease in cash spent on capital expenditures. In 2009, our capital expenditures decreased by $4,042 million, or by 38.4%, compared to 2008 (for a detailed analysis of capital expenditures see a later section).

In 2009, we paid the remaining amount of $1,066 million for the acquisition of a 49% stake in ISAB, we paid $127 million for the remaining interests in TGK-8. We also made a payment of approximately $600 million within the acquisition of 45% interest in TRN, settled a $305 million liability within the acquisition of Akpet group and paid $244 million for increasing our share in RITEK. We also paid $300 million as a first installment of the acquisition of the remaining 46% interest in LUKARCO. Other payments for acquisitions refer to advances for downstream assets in Russia.

In 2008, we made a final payment of $157 million and two contingent payments of $200 million in total for the acquisition of upstream assets in Uzbekistan (SNG Holdings Ltd.). During 2008, we paid $64 million for the increase in our share of the share capital of our refinery in Nizhny Novgorod and $1,222 million as the cash part of the consideration for the TGK-8 acquisition. As first installments for the acquisitions of the 49% stake in ISAB and petrol stations in Turkey we paid $762 million and $250 million, respectively. We also paid $343 million and $221 million for acquisitions of petrol stations in Bulgaria and petrol station networks in Russia. The other payments were primarily advances related to acquisitions of marketing assets in Russia and abroad.

Financing activities

In 2009, net movements of short-term and long-term debt generated an inflow of $1,489 million, compared to an inflow of $2,311 million in 2008.

In December 2009, the Company issued stock exchange bonds worth 10 billion rubles. The bonds will mature after 1,092 days and have a coupon period of 182 days. The coupon rate is set at 9.20% per annum.

In November 2009, a Group company issued two-tranche non-convertible bonds totaling $1.5 billion. The first tranche totaling $900 million with a coupon yield of 6.375% per annum was placed with a maturity of 5 years at a price of 99.474% of the bond's face value. The resulting yield to maturity for the first tranche is 6.500%. The second tranche totaling $600 million with a coupon yield of 7.250% per annum was placed with a maturity of 10 years at a price of 99.127% of the bond's face value. The resulting yield to maturity for the second tranche is 7.375%. These tranches have a half year coupon period.

In August 2009, we raised a $1.2 billion syndicated term loan facility. This three-year loan bears interest at LIBOR plus 4% per annum and is secured by proceeds from our oil export contracts. The proceeds from this loan were used to repay a €1,000 million loan from Gazprombank, which we borrowed in February 2009.

In August 2009, we issued stock exchange bonds in the amount of 25 billion rubles with a coupon rate of 13.35% per annum. The bonds will mature in three years. The proceeds from the issuance were used to repay the majority of our $500 million and 17 billion ruble loans from Sberbank, which we borrowed in February 2009.

In June 2009, we completed offering of three series of issued stock exchange bonds, altogether worth 15 billion rubles. Coupon rate for each of the issues was set at 13.5%. The bonds will mature in 364 days.

In February 2009, we received short-term loans of $500 million and 17 billion rubles from Sberbank to finance our working capital. Also, in the first quarter of 2009, we received a long-term loan of €1,000 million from Gazprombank. We have since repaid these loans.

Credit rating

In 2009, Standard & Poor's Ratings Services affirmed its long-term corporate credit rating and all debt ratings on the Company at BBB- with stable outlook.

In 2009, Moody's affirmed the Company's long-term corporate family rating and long-term issuer rating of Baa2 with stable outlook.

In 2009, Fitch Ratings affirmed the Company's long-term issuer default rating of BBB- and short-term issuer default rating of F3 and changed Company's outlook from positive to stable.

A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organization. Similar ratings on the Company and/or on different types of securities do not necessarily mean the same thing. The ratings do not address the marketability of any of our securities or their market price.

Any change in the credit ratings of the Company or our securities could adversely affect the price that a subsequent purchaser will be willing to pay for our securities. We recommend that you analyze the significance of each rating independently from any other rating.

Analysis of capital expenditures

	2009	2008	2007
	(millions of US dollars)		
Capital expenditures[1]			
Exploration and production			
Russia	3,916	6,813	6,391
International	771	1,076	871
Total exploration and production	4,687	7,889	7,262
Refining, marketing and distribution	832	1,377	1,177
Russia	559	773	645
International	1,391	2,150	1,822
Total refining, marketing and distribution			
Chemicals			
Russia	13	23	73
International	100	98	98
Total chemicals	113	121	171
Other	343	429	117
TOTAL CAPITAL EXPENDITURES	6,534	10,589	9,372
Acquisitions of subsidiaries and minority shareholding interest[2]			
Exploration and production			
Russia	244	4	77
International	300	357	357
Total exploration and production	544	361	434
Refining, marketing and distribution			
Russia	213	636	685
International	2,069[3]	1,397	511
Total refining, marketing and distribution	2,282	2,033	1,196
Other	138	3,194[4]	38
Less cash acquired	(19)	(190)	(102)
TOTAL ACQUISITIONS	2,945	5,398	1,566

[1] Including non-cash transactions and prepayments.
[2] Including prepayments related to acquisitions of subsidiaries and minority shareholding interests and non-cash transactions.
[3] Including $100 million of non-cash part of consideration for acquisition of TRN.
[4] Including $1,969 million of non-cash part of consideration for acquisition of TGK-8.

During 2009, our capital expenditures, including non-cash transactions, amounted to $6,534 million, which is 38.3% less than in 2008. The decrease was in compliance with our plan to reduce capital expenditures in 2009 because of the economic downturn. Capital expenditures in our exploration and production segment decreased by $3,202 million, or by 40.6%, compared to 2008. The exploration and production capital expenditures in new regions decreased by $1,411 million mainly due to commencement of commercial production on the Yuzhnoye Khylchuyu oil field. In the traditional exploration and production regions of Western Siberia and European Russia capital expenditures decreased by $1,004 million and $555 million, respectively. The decrease in the capital expenditures in our international exploration projects (excluding the Caspian region) amounted to $232 million and was primarily related to our projects in Kazakhstan and Saudi Arabia.

The table below shows our exploration and production capital expenditures in promising new production regions. In 2010, we plan to begin production on the Yu. Korchagin field in the Caspian Sea. The maximum annual production from the field is expected to be 2.5 million tonnes of oil and gas condensate, and 1.0 billion cubic meters of gas.

	2009	2008	2007
	(millions of US dollars)		
Northern Timan-Pechora	385	1,878	2,357
Yamal	131	161	75
Caspian region[1]	532	420	441
TOTAL	**1,048**	**2,459**	**2,873**

[1] Russian and international projects.

Following negative trends on international hydrocarbon markets the Company optimized its capital expenditure program for 2009, shifting it from originally expected $11.2 billion down to $6.5 billion. In case of continuing decline in crude oil prices the Company is flexible enough to further reduce capital expenditures and maintain its solid financial health.

Contractual obligations, other contingencies and off balance sheet arrangements

Capital commitments and contractual obligations

The Group owns and operates refineries in Bulgaria (LUKOIL Neftochim Bourgas AD) and Romania (Petrotel-LUKOIL S.A.). As a result of Bulgaria and Romania joining the European Union in 2007, LUKOIL Neftochim Bourgas AD and Petrotel-LUKOIL S.A. are required to upgrade their refining plants to comply with the requirements of European Union legislation in relation to the quality of produced petroleum products and environmental protection. These requirements are stricter than those which previously existed under Bulgarian and Romanian legislation. The Group estimates the amount of future capital commitment required to upgrade LUKOIL Neftochim Bourgas AD and Petrotel-LUKOIL S.A. to be approximately $49 million and $44 million, respectively.

Under the terms of existing exploration and production license agreements in Russia the Group has to fulfill certain operations: oil and gas exploration, wells drilling, fields development, etc., and the Group also has commitments to reach a defined level of extraction on the fields. Management believes that the Group's approved annual capital expenditure budgets fully cover all the requirements of the described license obligations.

Group companies have commitments for capital expenditure contributions in the amount of $565 million related to various production sharing agreements over the next 28 years.

The Company has signed a three-year agreement for drilling services with OOO Eurasia Drilling Company. The volume of these services is based on the Group's capital construction program, which is re-evaluated on an annual basis. The Group estimates the amount of capital commitment under this agreement for 2010 to be approximately $610 million.

The Company has signed a strategic agreement for the ongoing provision of construction, engineering and technical services with ZAO Globalstroy-Engineering. The volume of these services is based on the Group's capital construction program, which is re-evaluated on an annual basis. The Group estimates the amount of capital commitment under this agreement for 2010 to be approximately $126 million.

The Group has a commitment to purchase equipment for modernization of its petrochemical refinery Karpatnaftochim Ltd., located in Ukraine, during next two years in the amount of $55 million.

The Group has a commitment to execute the capital construction program of TGK-8 and under the terms of this program power plants with total capacity of 890 MW should be constructed. Currently the Group is approving certain amendments to the capital construction program, which included its extension by the end of 2013. As of December 31, 2009, the Group estimates the amount of this commitment to be approximately $944 million.

The following table displays our total contractual obligations and other commitments:

(millions of US dollars)	Total	2010	2011	2012	2013	2014	After
ON BALANCE SHEET							
Short term debt	519	519	–	–	–	–	–
Long-term bank loans and borrowings	3,967	911	1,515	881	268	134	258
Long-term non-bank loans and borrowings	76	11	16	4	6	21	18
Long-term loans and borrowings from related parties	1,939	45	53	42	32	24	1,743
6.375% Non-convertible US dollar bonds, maturing 2014	895	–	–	–	–	895	–
6.356% Non-convertible US dollar bonds, maturing 2017	500	–	–	–	–	–	500
7.250% Non-convertible US dollar bonds, maturing 2019	595	–	–	–	–	–	595
6.656% Non-convertible US dollar bonds, maturing 2022	500	–	–	–	–	–	500
13,50% Russian ruble bonds	496	496	–	–	–	–	–
7.10% Russian ruble bonds, maturing 2011	265	–	265	–	–	–	–
13.35% Russian ruble bonds, maturing 2012	827	–	–	827	–	–	–
9.20% Russian ruble bonds, maturing 2012	331	–	–	331	–	–	–
7.40% Russian ruble bonds, maturing 2013	198	–	–	–	198	–	–
Capital lease obligations	215	76	41	20	20	20	38
TOTAL	11,323	2,058	1,890	2,105	524	1,094	3,652
OFF BALANCE SHEET							
Operating lease obligations	974	276	172	135	104	93	194
Capital commitment in LUKOIL-Neftochim Bourgas AD	49	49	–	–	–	–	–
Capital commitment in LUKOIL-Petrotel	44	1	17	1	12	13	–
Commitment for modernization of the petrochemical refinery in Ukraine	55	52	3	–	–	–	–
Capital commitments in PSAs	565	399	102	27	2	2	33
Capital commitments in TGK-8	944	307	339	184	114	–	–
Obligation under contract with Eurasia Drilling Company	610	610	–	–	–	–	–
Obligation under contract with ZAO Globalstroy-Engineering	126	126	–	–	–	–	–

Litigation and claims

On November 27, 2001, Archangel Diamond Corporation ("ADC"), a Canadian diamond development company, filed a lawsuit in the District Court of Denver, Colorado against OAO Archangelskgeoldobycha ("AGD"), a Group company, and the Company (together the "Defendants"). ADC alleged that the Defendants interfered with the transfer of a diamond exploration license to Almazny Bereg, a joint venture between ADC and AGD. ADC claimed total damages of approximately \$4.8 billion, including compensatory damages of \$1.2 billion and punitive damages of \$3.6 billion. On October 15, 2002, the District Court dismissed the lawsuit for lack of personal jurisdiction. This ruling was upheld by the Colorado Court of Appeals on March 25, 2004. On November 21, 2005, the Colorado Supreme Court affirmed the lower courts' ruling that no specific jurisdiction exists over the Defendants. By virtue of this finding, AGD (the holder of the diamond exploration license) was dismissed from the lawsuit. The Supreme Court found, however, that the trial court made a procedural error by failing to hold an evidentiary hearing before making its ruling concerning general jurisdiction regarding the Company, which is whether the Company had systematic and continuous contacts in the State of Colorado at the time the lawsuit was filed. In a modified opinion dated December 19, 2005, the Colorado Supreme Court remanded the case to the Colorado Court of Appeals (instead of the District Court) to consider whether the lawsuit should have been dismissed on alternative grounds (i.e., forum non conveniens). On June 29, 2006, the Colorado Court of Appeals declined to dismiss the case based on forum non conveniens. The Company filed a petition for certiorari on August 28, 2006, asking the Colorado Supreme Court to review this decision. On March 5, 2007, the Colorado Supreme Court remanded the case to the District Court. On June 11, 2007, the District Court ruled it would conduct an evidentiary hearing on the issue of whether the Company is subject to general personal jurisdiction in the State of Colorado. Discovery regarding jurisdiction was commenced. On June 26, 2009, three creditors of ADC filed an Involuntary Bankruptcy Petition putting ADC into bankruptcy. ADC ultimately confirmed entry of an Order

For Relief and the matter was converted to a Chapter 11 Case by order dated September 29, 2009. On November 25, 2009, after adding a claim, ADC removed the case from the Colorado District Court to the US Bankruptcy Court. On December 22, 2009, the Company filed a motion seeking to have the case remanded to the Colorado District Court. On December 31, 2009, before there was a ruling on the motion seeking remand ADC filed a motion seeking withdrawal of the reference from the bankruptcy and the case be heard by US District Court. On February 3, 2010, the US Bankruptcy Court ordered the Motion For Withdrawal Of The Reference be transferred to the US District Court for further action. All pending motions as well as discovery are stayed pending further order of the Court. Management plans to vigorously defend the matter. Management does not believe that the ultimate resolution of this matter will have a material adverse effect on the Group's financial condition.

In 2008 and 2009, the Federal Anti-monopoly Service of the Russian Federation ("FAS of Russia") issued two decisions against major Russian oil companies, including the Company and the Group's refinery plants alleging abuse of their dominant position in the oil products wholesale market of the Russian Federation.

The Moscow Arbitration Court combined all refinery plants' appeals against the first decision. The next appeal hearing was scheduled for April 8, 2010.

The second decision of FAS of Russia was appealed by the refinery plants in their local courts. On February 8, 2010, the Arbitration Court of Nizhni Novgorod Region satisfied the request of OOO LUKOIL-Nizhnegorodnefteorgsintez to recognize as illegal the decisions of FAS of Russia dated September 10, 2009 and the resolution to impose fines in the amount of $80 million. The appeals of the other refinery plants are currently suspended.

In the second half of 2008 and first half of 2009, the FAS of Russia filed claims against several Group companies in relation to violation of the anti-monopoly regulation. The companies were accused of violations primarily involving abuse of their dominant market position via setting monopolistically high retail prices in coordination with other market participants. These claims are being appealed in the courts.

The total amount of penalties assessed under the administrative law for the violation of anti-monopoly regulation by the Group in 2008-2009 is $290 million. Management believes that the Group complied with all regulatory and legal requirements and, consequently, believes that the ultimate resolution of the antimonopoly claims will lead to cancellation or significant reduction of these penalties and will not have a material adverse impact on the Group's operating results or financial condition.

The Group is involved in various other claims and legal proceedings arising in the normal course of business. While these claims may seek substantial damages against the Group and are subject to uncertainty inherent in any litigation, management does not believe that the ultimate resolution of such matters will have a material adverse impact on the Group's operating results or financial condition.

Critical accounting policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to select appropriate accounting policies and to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. See Note 2 "Summary of significant accounting policies" to our consolidated financial statements for descriptions of the Company's major accounting policies. Certain of these accounting policies involve judgments and uncertainties to such an extent that there is a reasonable likelihood that materially different amounts would have been reported under different conditions, or if different assumptions had been used.

Business combinations

Purchase price allocation

Accounting for the acquisition of a business requires the allocation of the purchase price to the various assets and liabilities of the acquired business. For most assets and liabilities, purchase price allocation is accomplished by recording the asset or liability at its estimated fair value. The most difficult estimations of individual fair values are those involving property, plant and equipment and identifiable intangible assets. We use all available information to make these fair value determinations and, for major business acquisitions, typically engage an outside appraisal firm to assist in the fair value determination of the acquired long-lived assets. We have, if necessary, up to one year after the acquisition closing date to finish these fair value determinations and finalize the purchase price allocation.

Principles of consolidation

Our consolidated financial statements include the financial position and results of the Company, controlled subsidiaries of which the Company directly or indirectly owns more than 50% of the voting interest, unless minority interest shareholders have substantive participating rights, and variable interest entities where the Group is determined to be the primary beneficiary. Other significant investments in companies of which the Company directly or indirectly owns between 20% and 50% of the voting interest and over which it exercises significant influence but not control, are accounted for using the equity method of accounting. Investments in companies of which the Company directly or indirectly owns more than 50% of the voting interest but where minority interest shareholders have substantive participating rights are accounted for using the equity method of accounting. Undivided interests in oil and gas joint ventures are accounted for using the proportionate consolidation method. Investments in other companies are recorded at cost.

Revenue recognition

Revenues from the production and sale of crude oil and petroleum products are recognized when title passes to customers at which point the risks and rewards of ownership are assumed by the customer and the price is fixed or determinable. Revenues include excise on petroleum products sales and duties on export sales of crude oil and petroleum products.

Revenues from non-cash sales are recognized at the fair market value of the crude oil and petroleum products sold.

Successful efforts accounting for oil and gas activities

Accounting for oil and gas activities is subject to special accounting rules that are unique to the oil and gas industry. Property acquisitions, successful exploratory wells, all development costs and support equipment and facilities are capitalized. Artificial stimulation and well work-over costs are included in operating expenses as incurred.

Property acquisition costs

For individually significant undeveloped properties, management periodically performs impairment test based on exploration and drilling efforts to date. For undeveloped properties that individually are relatively small, management exercises judgment and determines a periodic property impairment charge as required that is reported in loss on disposals and impairments of assets.

Exploratory costs

For exploratory wells, drilling costs are temporarily capitalized, or "suspended", on the balance sheet, pending a judgmental determination of whether potentially economic oil and gas reserves have been discovered by the drilling effort. If a judgment is made that the well did not encounter potentially economic oil and gas quantities, the well costs are expensed as a dry hole and are reported in exploration expense. Exploratory wells that are judged to have discovered potentially economic quantities of oil and gas and that are in areas where a major capital expenditure would be required before production could begin, remain capitalized on the balance sheet as long as additional exploratory appraisal work is under way or firmly planned. There is no periodic impairment assessment of suspended exploratory well costs. Management continuously monitors the results of the additional appraisal drilling and seismic work and expenses the suspended well costs as dry holes when it judges that the potential field does not warrant further exploratory efforts in the near term.

Other exploratory expenditures, including geological and geophysical costs are expensed as incurred.

Proved oil and gas reserves

Due to the inherent uncertainties and the necessarily limited nature of reservoir data, estimates of reserves are inherently imprecise, require the application of judgment and are subject to change as additional information becomes available. The estimates are made using all available geological and reservoir data as well as historical production data. Estimates are reviewed and revised as appropriate. Revisions occur as a result of changes in prices, costs, fiscal regimes, reservoir performance or a change in the Company's plans.

Proved oil and gas reserves are the estimated quantities of crude oil, natural gas liquids including condensate and natural gas that geological and engineering data demonstrate with reasonable certainty can be recovered in future years from known reservoirs under existing economic and operating conditions. Reserves are considered proved if they can be produced economically as demonstrated by either actual production or conclusive formation tests. Proved reserves do not include additional quantities of oil and gas reserves that may result from applying secondary or tertiary recovery techniques not yet tested and determined to be economic. The proved reserves include volumes which are recoverable up to and after license expiry dates. Proved developed reserves are the quantities of proved reserves expected to be recovered through existing wells with existing equipment and operating methods.

Management has included within proved reserves significant quantities which the Group expects to produce after the expiry dates of certain of its current production licenses in the Russian Federation. The Subsoil Law of the Russian Federation states that, upon expiration, a license is subject to renewal at the initiative of the license holder provided that further exploration, appraisal, production or remediation activities are necessary and provided that the license holder has not violated the terms of the license. Since the law applies both to newly issued and old licenses and the Group has currently renewed nearly 50% of its licenses, management believes that licenses will be renewed upon their expiration for the remainder of the economic life of each respective field.

Impairment of long-lived assets

Long-lived assets, such as oil and gas properties (other than unproved properties), other property, plant, and equipment, and purchased intangibles subject to amortization, are assessed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset group may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset group to the estimated undiscounted future cash flows expected to be generated by that group. If the carrying amount of an asset group exceeds its estimated undiscounted future cash flows, an impairment charge is recognized by writing down the carrying amount to the estimated fair value of the asset group, generally determined as discounted future net cash flows. Assets to be disposed of are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale are presented separately in the appropriate asset and liability sections of the balance sheet.

Deferred income taxes

Deferred income tax assets and liabilities are recognized in respect of future tax consequences attributable to temporary differences between the carrying amounts of existing assets and liabilities for the purposes of the consolidated financial statements and their respective tax bases and in respect of operating loss and tax credit carryforwards. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse and the assets be recovered and liabilities settled. The effect on deferred income tax assets and liabilities of a change in tax rates is recognized in the consolidated statement of income in the reporting period which includes the enactment date.

The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income in the reporting periods in which the originating expenditure becomes deductible. In assessing the realizability of deferred income tax assets, management considers whether it is more likely than not that the deferred income tax assets will be realized. In making this assessment, management considers the scheduled reversal of deferred income tax liabilities, projected future taxable income, and tax planning strategies.

Asset retirement obligations

Under various laws, contracts, permits and regulations, the Group has legal obligations to remove tangible equipment and restore the land or seabed at the end of operations at production sites. The largest asset retirement obligations of the Group relate to wells and oil and gas production facilities and pipelines. The Group records the fair value of liabilities associated with such obligations when incurred. Estimating the future asset retirement obligations costs necessary for this accounting calculation involves significant estimates and judgments by management. Most of these obligations are many years in the future and the contracts and regulations often have vague descriptions of what removal practices and criteria will have to be met when the removal event actually occurs. Asset removal technologies and costs are constantly changing, as well as political, environmental, safety and public relations considerations.

Contingencies

Certain conditions may exist as of balance sheet dates that may result in losses, but the impact of which will only be resolved when one or more future events occur or fail to occur. The Group is required to both determine whether a loss is probable based on judgment and interpretation of laws and regulations and determine whether the loss can be reasonably estimated. If our assessment of a contingency indicates that it is probable that a material loss will arise, and the amount of the liability can be estimated, then the estimated liability is accrued and charged to the consolidated statement of income. If our assessment indicates that a potentially material loss is not probable, but is only reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability is disclosed in the notes to our consolidated financial statements. Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the nature of the guarantee is disclosed. The Company's management continually monitor known and potential contingent matters and make appropriate charges to the consolidated statement of income when warranted by circumstance.

Use of derivative instruments

The Group's derivative activity is limited to certain petroleum products marketing and trading outside of its physical crude oil and petroleum products businesses and hedging of commodity price risks. Currently this activity involves the use of futures and swaps contracts together with purchase and sale contracts that qualify as derivative instruments. The Group accounts for these activities under the mark-to-market methodology in which the derivatives are revalued each accounting period. Resulting realized and unrealized gains or losses are presented in the consolidated statement of income on a net basis. Unrealized gains and losses are carried as assets or liabilities on the consolidated balance sheet.

Recent accounting pronouncements

In February 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-09, *"Subsequent events"* which amends Accounting Standards Codification (ASC) No. 855 (former SFAS No. 165, *"Subsequent events"*), issued in May 2009. The Group adopted ASC No. 855 starting from the second quarter of 2009. These standards address accounting and disclosure requirements related to subsequent events and require management of an entity which is an SEC filer or is a conduit bond obligator for conduit securities that are traded in a public market to evaluate subsequent event through the date that the financial statements are issued. Entities that do not meet these criteria should evaluate subsequent events through the date the financial statements are available to be issued and are required to disclose the date through which subsequent events have been evaluated. The Group determined that it should evaluate subsequent events through the date the financial statements are available to be issued and applied the requirements of ASU No. 2010-09 starting from the financial statements for 2009.

In January 2010, the FASB issued ASU No. 2010-01, *"Accounting for Distributions to Shareholders with Components of Stock and Cash"* which addresses how an entity should account for the stock portion of a dividend in certain arrangements when a shareholder makes an election to receive cash or stock, subject to limitations on the amount of the dividend to be issued in cash. The stock portion of the dividend should be accounted for as a stock issuance upon distribution, resulting in basic earnings per share being adjusted prospectively. Prior to distribution, the entity's obligation to issue shares would be reflected in diluted earnings-per-share based on the guidance in ASC No. 260, which addresses contracts that may be settled in shares. This ASU is effective for interim and annual periods ending after December 15, 2009. The Group adopted ASU No. 2010-01 for the 2009 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In January 2010, the FASB issued ASU No. 2010-02, *"Accounting and Reporting for Decreases in Ownership of a Subsidiary - A Scope Clarification"* to clarify the scope of ASC Subtopic No. 810-10, *"Consolidation – Overall."* This ASU specifies that the guidance in ASC Subtopic No. 810-10 on accounting for decreases in ownership of a subsidiary applies to: (1) a subsidiary or group of assets that constitutes a business or nonprofit activity; (2) a subsidiary that is a business or a nonprofit activity that is transferred to an equity method investee or a joint venture; and (3) an exchange of a group of assets that constitute a business or nonprofit activity for a noncontrolling interest in an entity. If a company's ownership interest in a subsidiary that is not a business or nonprofit activity decreases, then other accounting guidance generally would be applied based on the nature of the transaction. The new pronouncement also clarifies that the recent guidance on accounting for decreases in ownership of a subsidiary does not apply if the transaction is a sale of in-substance real estate or a conveyance of oil and gas properties. This ASU is effective for interim and annual periods ending after December 15, 2009 and the guidance should be applied on a retrospective basis to the first period in which the company adopted ASC No. 810. The Group adopted ASU No. 2010-02 for the 2009 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In January 2010, the FASB issued ASU No. 2010-03, *"Extractive activities Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures"*. The main provisions of ASU No. 2010-03 are the following: (1) expanding the definition of oil- and gas-producing activities to include the extraction of saleable hydrocarbons, in solid, liquid, or gaseous state, from oil sands, shale, coalbeds, or other nonrenewable resources that are intended to be upgraded into synthetic oil or gas, and activities undertaken with a view to such extraction; (2) entities should use first-day-of-the-month price during the 12-month period (the 12-months average price) in calculating proved oil and gas reserves and estimating related standardized measure of discounted net cash flows; (3) requiring entities to disclosure separately information about reserves quantities and financial statement amounts for geographic areas that represent 15 percent or more of proved reserves; (4) separate disclosure for consolidated entities and equity method investments. ASU No. 2010-03 is effective for annual reporting periods ending on or after December 31, 2009. The Group adopted ASU No. 2010-03 for the 2009 annual financial statements. This adoption did not have a material impact on the Group's reported reserves evaluation, results of operations, financial position or cash flows.

In June 2009, the FASB issued amendments to ASC No. 810 (former FASB Interpretation No. 46(R), *"Consolidation of Variable Interest Entities"*) to address the effects of the elimination of the qualifying special purpose entity concept. More specifically, it requires a qualitative rather than a quantitative approach to determine the primary beneficiary of a variable interest entity, it amends certain guidance pertaining to the determination of the primary beneficiary when related parties are involved, and it amends certain guidance for determining whether an entity is a variable interest entity. Additionally, these amendments require continuous assessment of whether an enterprise is the primary beneficiary of a variable interest entity. Amendments are effective on January 1, 2010, and the Group does not expect any material impact on its results of operations, financial position or cash flows upon adoption.

In June 2009, the FASB issued ASC No. 105 (former SFAS No. 168, *"The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles"*). The FASB Accounting Standards Codification ("Codification") is the exclusive authoritative reference for US GAAP recognized by the FASB and applied by nongovernmental entities, except for SEC rules and interpretive releases, which are also authoritative US GAAP for SEC registrants. The change established by ASC No. 105 divides nongovernmental US GAAP into authoritative Codification and guidance that is not authoritative. The contents of the Codification carry the same level of authority, eliminating the four-level US GAAP hierarchy previously set forth in SFAS No. 162. The Codification supersedes all non-SEC accounting and reporting standards. All other non-grandfathered, non-SEC accounting literature not included in the Codification became nonauthoritative. This Statement is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Group adopted ASC No. 105 starting from the third quarter of 2009. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In December 2008, the FASB amended ASC Nos. 310, 320, 323, 405, 460, 470, 712, 715, 810, 815, 860, 954 and 958 (former FSP FAS 140-4 and FIN 46(R)-8, *"Disclosures about Transfers of Financial Assets and Interest in Variable Interest Entities"*). It requires additional disclosures about transfers of financial assets and requires public entities, including sponsors that have a variable interest in a variable interest entity, to provide additional disclosures about their involvement with variable interest entities. The Group adopted new provisions starting from the fourth quarter of 2008. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In March 2008, the FASB issued ASC No. 815 (former SFAS No. 161, *"Disclosures about Derivative Instruments and Hedging Activities"*). This ASC improves financial reporting about derivative instruments and hedging activities by enhanced disclosures of their effects on an entity's financial position, financial performance and cash flows. The Group adopted the provisions of ASC No. 815 starting from the first quarter of 2009. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In December 2007, the FASB issued ASC No. 805 (former SFAS No. 141 (Revised), *"Business combinations"*). This ASC applies to all transactions in which an entity obtains control of one or more businesses. In April 2009, this ASC was amended and requires an entity to recognize the total fair value of assets acquired and liabilities assumed in a business combination; to recognize and measure the goodwill acquired in the business combination or gain from a bargain purchase and modifies the disclosure requirements. The Group adopted the provisions of ASC No. 805 for business combinations for which the acquisition date is after December 31, 2008. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In December 2007, the FASB issued ASC No. 810 (former SFAS No. 160, *"Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51"*). This ASC applies to all entities that prepare consolidated financial statements (except not-for-profit organizations) and affects those which have an outstanding noncontrolling interest (or minority interest) in their subsidiaries or which have to deconsolidate a subsidiary. This ASC changes the classification of a non-controlling interest; establishing a single method of accounting for changes in the parent company's ownership interest that does not result in deconsolidation and requires a parent company to recognize a gain or loss when a subsidiary is deconsolidated. The Group prospectively adopted the provisions of ASC No. 810 in the first quarter of 2009, except for the presentation and disclosure requirements which were applied retrospectively. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In February 2007, the FASB issued ASC Nos. 470, 825 and 954 (former SFAS No. 159, *"The Fair Value Option for Financial Assets and Financial Liabilities"*). These ASC expands the possibility of using fair value measurements and permits enterprises to choose to measure certain financial assets and financial liabilities at fair value. Enterprises shall report unrealized gains and losses on items for which the fair value option has been elected in earnings in each subsequent period. The Group adopted the provisions of ASC Nos. 470, 825 and 954 in the first quarter of 2008 and elected not to use the fair value option for its financial assets and financial liabilities not already carried at fair value in accordance with other standards. This adoption did not have any impact on the Group's results of operations, financial position or cash flows.

In September 2006, the FASB issued ASC No. 820 (former SFAS No. 157, *"Fair Value Measurements"*), which establishes a single authoritative definition of fair value, sets out a framework for measuring fair value and requires additional disclosures about fair value measurements. Effective January 1, 2009, the Group fully adopted ASC No. 820. Because there usually is a lack of quoted market prices for long-lived assets, the Group determines fair value using the present value of estimated future net cash flows from using these assets or by using historical data of market transactions with similar assets where possible. Fair value used in the initial recognition of asset retirement obligations is determined using the present value of expected future dismantlement costs, which are estimated based on the costs for dismantlement services for similar assets providing by third parties. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

Forward-looking statements

Certain statements in this document are not historical facts and are "forward-looking". We may from time to time make written or oral forward-looking statements in reports to shareholders and in other communications. Examples of such forward-looking statements include, but are not limited to:

- statements of our plans, objectives or goals, including those related to products or services;
- statements of future economic performance;
- statements of assumptions underlying such statements.

Forward looking statements that may be made by us from time to time (but that are not included in this document) may also include projections or expectations of revenues, income (or loss), earnings (or loss) per share, dividends, capital structure or other financial items or ratios. Words such as "believes", "anticipates", "expects", "estimates", "intends" and "plans" and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that the predictions, forecasts, projections and other forward-looking statements will not be achieved. You should be aware that a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements.

These factors include:

- inflation, interest rate and exchange rate fluctuations;
- the price of oil;
- the effects of, and changes in, Russian government policy;
- the effects of competition in the geographic and business areas in which we conduct operations;
- the effects of changes in laws, regulations, taxation or accounting standards or practices;
- our ability to increase market share for our products and control expenses;
- acquisitions or divestitures;
- technological changes;
- our success at managing the risks of the aforementioned factors.

This list of important factors is not exhaustive. When relying on forward-looking statements, you should carefully consider the foregoing factors and other uncertainties and events, especially in light of the political, economic, social and legal environment in which we operate. Such forward-looking statements speak only as of the date on which they are made, and, subject to any continuing obligations under the Listing Rules of the U.K. Listing Authority, we do not undertake any obligation to update or revise any of them, whether as a result of new information, future events or otherwise. We do not make any representation, warranty or prediction that the results anticipated by such forward-looking statements will be achieved, and such forward-looking statements represent, in each case, only one of many possible scenarios and should not be viewed as the most likely or standard scenario.