



LUKOIL

ANNUAL REPORT
2010

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LETTER TO SHAREHOLDERS

Dear Shareholders,

LUKOIL is celebrating its 20th anniversary this year. Over the past twenty years we have achieved substantial results. We have grown from a few production assets in Russia into a global energy company with operations in 37 countries on four continents. We have worked consistently for two decades to make all aspects of our business more efficient and to maximize income to our shareholders.

We have entered our third decade with confidence, and we are starting a new age which reflects the reality of today's global business environment. In the fall of 2011 we are going to present a new business development strategy. Taking into account the shrinkage of traditional hydrocarbon deposits, we will particularly focus on new technologies to make the best use of our reserve base in the future. This approach will give us new competitive advantages and increase our shareholder value.

The business of LUKOIL Group developed well in 2010 as the world economy made a gradual recovery after the global financial crisis. Ability of our Company to adapt quickly to a changing environment brought strong financial results, and we remained in the vanguard of the Russian oil & gas industry. Tight financial discipline, good decision-making, and efficient management gave a record level of free cash flow in the reporting year. We focused our efforts on priority projects and on improvement of the business efficiency, including a strong emphasis on innovation policy and business structure optimization.

Net income of LUKOIL Group increased by 28.5% in 2010 to \$9,006 million, and return on average capital employed was 14.0%. Free cash flow reached \$6,930 million. LUKOIL remains one of the most financially efficient oil companies in Russia, as shown by achievement of \$11 net income per boe in 2010.

Growth of net income helped us to increase income to shareholders. We reacted to the decision by ConocoPhillips to exit its shareholding in LUKOIL by carrying out one of the largest-ever buyback transactions on the Russian market, with value in excess of \$3.4 billion. Net profit per share increased by 32.2% in comparison with 2009 and approached \$11.

We continue to expand our dividend payouts to shareholders. On April 26, 2011 the Board of Directors recommended the General Meeting of Shareholders to approve dividends of 59 roubles per share for 2010 (\$1.94 at the exchange rate on December 31, 2010). So the share of net profits paid as dividends will be more than 18%. Dividend yield in 2010 will be 3.5%.

In the **Exploration & Production segment** the Company increased its hydrocarbon output thanks to strong growth of gas production, rapid development of international projects and stabilization of production levels in Western Siberia. Daily hydrocarbon production by the Group rose by 1.2% to 2.24 million barrels of oil equivalent in 2010. Output of marketable gas rose by 24.5% thanks to increase of purchases by OJSC Gazprom.



VALERY GRAYFER

Chairman of the Board of Directors of LUKOIL



VAGIT ALEKPEROV

President of LUKOIL

Launch of production in the Caspian region was a particularly important event for the Company in 2010: commissioning of the Yu. Korchagin field was the first of a series of start-ups scheduled by LUKOIL at promising areas in the Caspian, which will ensure quality growth of production in the long term.

The Company is also pursuing expansion of its international E&P business. A consortium between LUKOIL and the American company Vanco won a tender for blocks 29 and 30 in the Black Sea, held as part of a 10-year licensing round by Romania's National Agency for Mineral Resources.

A major achievement in the Company's exploration business last year was the discovery of a deepwater oil field on the continental slope of the Gulf of Guinea (Ghana). The discovery was made at the Dzata structure as part of the Cape Three Points Deep Water (CTPDW) project, and is at a depth of 2,000 meters. Well depth is about 4,500 meters below sea level.

In the **Refining & Marketing segment** the Company focused its attention on capacity modernization in order to achieve further increase of the rate of conversion. We have invested and continued to invest considerable sums in our oil refineries to ensure leading positions in Russia for production of high-quality and environmentally friendly fuels. In December 2010 we commissioned a catalytic cracking facility at our Nizhny Novgorod

refinery, which is the largest catalytic cracking facility built in Russia for the last 25 years, enabling production of gasoline that fully meets Euro-4 standards.

Crude oil refining at Company facilities in 2010, including LUKOIL's share of refining at the ISAB and TRN complexes, rose by 5.6% to 66.2 million tonnes.

We completed creation of the Group's new **Power Generation sector** in 2010. LUKOIL Group now has power generating capacity of 4.4 GW and we plan to launch a further 600 MW capacity in 2011 using advanced gas turbines, which will make power and heat production significantly more efficient. Electricity output in 2010 was close to the level in 2009 and totaled 14.6 billion kWh. Heat production in 2010 was 15.3 million Gcals.

Innovation policy is becoming a key aspect of Company development, as application of new technologies increases efficiency of the business. We are now the first Russian Company with experience of work on Africa's deep-water continental shelf. We are continuing to perfect our technologies for production of heavy and high-viscosity oils in Russia and we accounted for 20% of total Russian output of oil in these categories in 2010. Testing is being carried out of extraction techniques for low-permeability reservoirs in Bazhenov strata. These strata are a close geological analogue of the well-known Bakken formations in the U.S. Their enormous potential for oil production has been held back by the lack of a

suitable technology. We are now working to address this task. We are also in dialogue with partners in Saudi Arabia on development of a project for extraction of non-traditional gas from reservoirs with low permeability.

In 2010 the Group created a unified corporate R&D center, LLC LUKOIL-Engineering. The task of the new LLC will be to organize and carry out R&D work in the geology, development and production spheres at all LUKOIL operating sites. A business structure has also been set up at OJSC RITEK for work with complex and unproductive

fields, and will spearhead use of innovative approaches in oil production.

LUKOIL is entering a new era of self-sufficient development in its jubilee year, 2011. Our main task in 2011 will be to configure a new development strategy based on strong cash flow, increase of oil recovery ratios, careful choice of investment projects, innovative development, maintenance of strong competitive positions, and growth of Company profitability and capitalization.

Chairman of the Board of Directors of LUKOIL



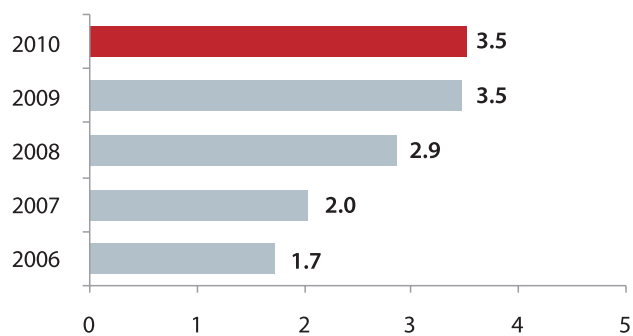
VALERY GRAYFER

President of LUKOIL

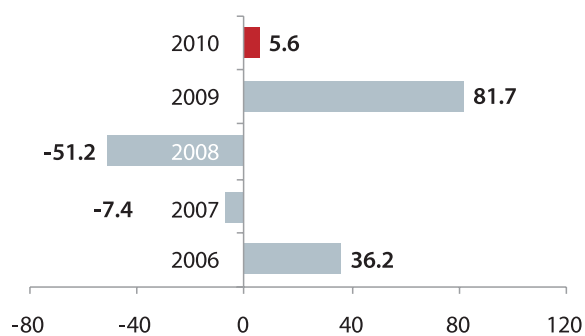


VAGIT ALEKPEROV

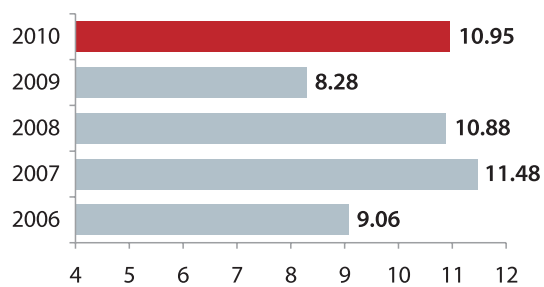
■ DIVIDEND YIELD, %



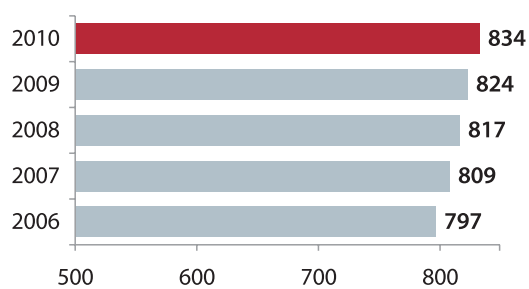
■ TOTAL SHAREHOLDER RETURN, %



■ BASIC EARNINGS PER SHARE, \$



■ HYDROCARBON PRODUCTION, million boe



LUKOIL IN THE WORLD

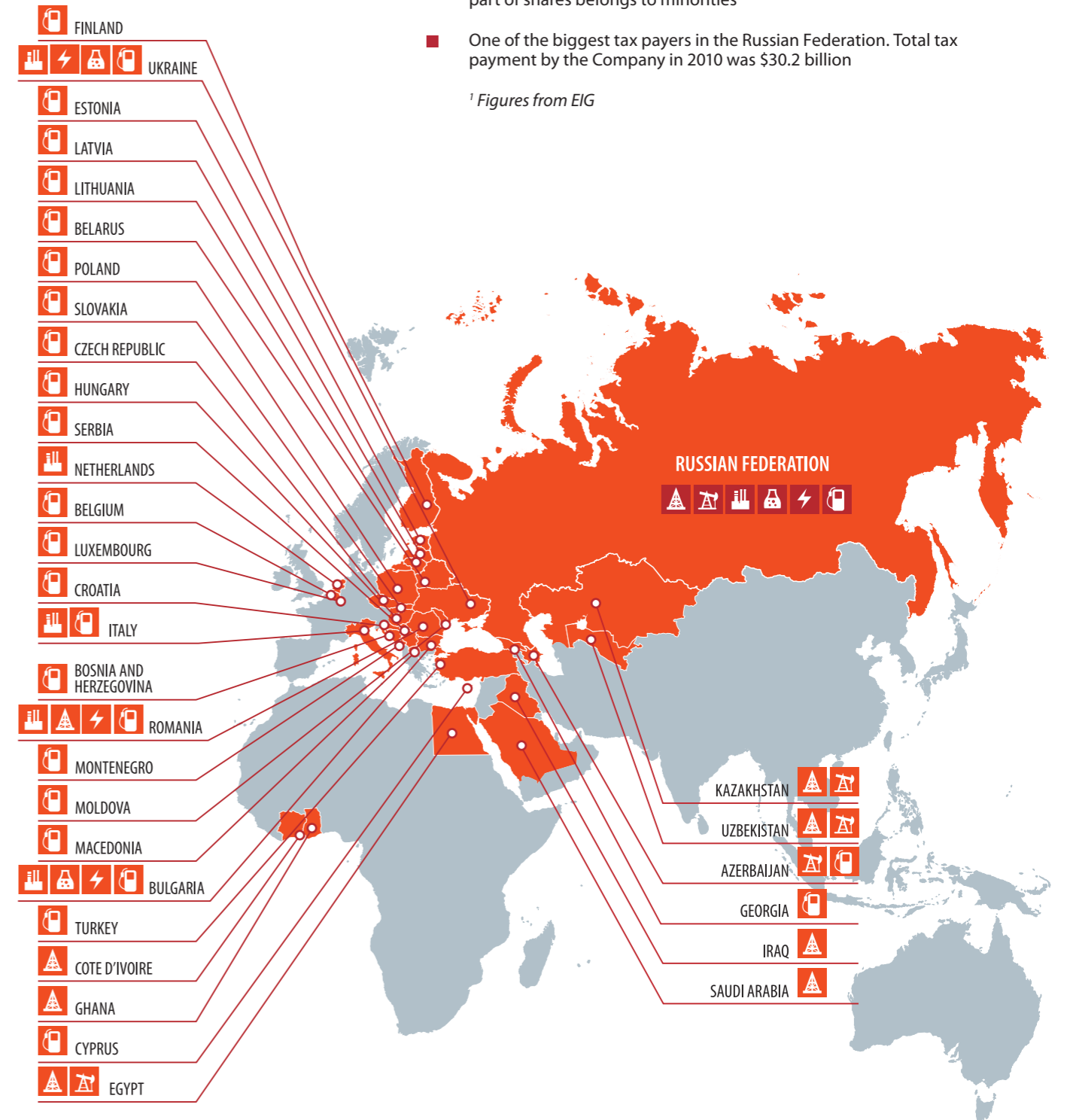
■ LUKOIL IS A MAJOR INTERNATIONAL VERTICALLY-INTEGRATED OIL & GAS COMPANY, ACCOUNTING FOR 2.2% OF GLOBAL OUTPUT OF CRUDE OIL

The strong position, which the Company enjoys today, is the fruit of 20 years work to expand the reserve base, increasing business scale by seeking out and executing strategic transactions.



- 2.2% of global production of crude oil¹
- 17.8% of Russian crude oil production and 18.2% of Russian crude oil refining
- One of the biggest Russian oil business groups with \$100 billion revenue and net income in excess of \$9 billion
- A leader among Russian companies by information openness and transparency. The first Russian company to obtain full listing for its shares on the London Stock Exchange
- The only privately owned Russian oil company, in which the largest part of shares belongs to minorities
- One of the biggest tax payers in the Russian Federation. Total tax payment by the Company in 2010 was \$30.2 billion

¹ Figures from EIG



MAIN OPERATING AND FINANCIAL INDICATORS

	2010	2009	Change, %
Sales, \$ million	104,956	81,083	29.4
EBITDA, \$ million	16,049	13,475	19.1
Net income, \$ million	9,006	7,011	28.5
Basic EPS, \$	10.95	8.28	32.2
ROACE, %	14.0	11.8	–
Capital expenditures, \$ million	6,844	6,534	4.7
Investments (acquisition of subsidiaries and minority stakes) ¹ , \$ million	1,124	2,945	-61.8
Share price (end of year, MICEX), roubles	1,732.02	1,695.47	2.16
Dividend per share, roubles	59	52	13.46
Main operating indicators			
Oil reserves, million barrels	13,319	13,696	-2.75
Gas reserves, billion cubic feet	23,615	22,850	3.3
Hydrocarbon reserves, million boe	17,255	17,504	-1.4
Crude oil production, million barrels	708.1	719.6	-1.6
Production of marketable natural gas, million cubic meters	12,770	10,218	25.0
Production of marketable associated gas, million cubic meters	5,784	4,680	23.6
Production of marketable hydrocarbons, thousand boe per day	2,239	2,212	1.2
Throughputs at own refineries and at ISAB and TRN, million tonnes	66.2	62.7	5.6
Gas processing, million cubic meters	3,178	2,962	7.3
Production of petrochemicals, million tonnes	1,036	0,902	14.9
Crude oil exports, million tonnes	40.59	42.02	-3.4
Petroleum product exports, million tonnes	25.82	27.76	-6.9
Crude oil sales, million tonnes	51.38	49.97	2.8
Wholesale sales of petroleum products, million tonnes	91.02	86.68	5.0
Retail sales of petroleum products, million tonnes	14.34	14.08	1.8
Number of filling stations (owned, leased and franchises)	6,508	6,620	-1.7
Average number of employees, thousand	130.0	143.4	-9.4

¹ Including prepayments related to acquisition of subsidiaries and non-controlling interests and non-cash transactions.

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

EVENTS IN 2010

JANUARY

LUKOIL signs a contract for development and production at the West Qurna-2 field in Iraq. Parties to the contract are Iraq's state-owned South Oil Company and a consortium of contractors consisting the Iraqi state North Oil Company (25%), LUKOIL (56.25%) and Norwegian Statoil (18.75%). The contract is for 20 years with an option to extend for 5 years. Drilling at the field is scheduled to start in 2011, and production should begin in early 2013.

LUKOIL approves an Energy-Saving Program for Group companies in 2010 and for the period 2010–2012. The Program will focus on better use of energy, and installation of new energy-efficient technology and equipment. The Company should obtain energy savings in excess of 2.4 billion kWh and more than 970,000 Gcals in 2010–2012 as a result of the Program. Target savings in money terms are 9.2 billion roubles (about \$300 million).

FEBRUARY

A consortium consisting of LUKOIL, the US company Vanco and the Ghana National Oil Company (GNPC) discovers substantial oil reserves at the Dzata structure, which is part of the CTPDW block, on the Ghana shelf in the Gulf of Guinea. The exploration well, Dzata-1, which made the discovery, has subsea depth of 4,500 meters. Further exploration is planned for purposes of reserve assessment and commercialization.

MARCH

LUKOIL approves a one-year R&D program for the Group in 2010 and a medium-term program of R&D work for the period 2011–2012. The one-year program includes

more than 800 research, design and technology tasks relating to field development as well as provision of various technology services. Financing is over 4 billion roubles (about \$140 million). Financing for the medium-term program is 12 billion roubles (over \$400 million). Most of spending in both programs is focused on the exploration & production segment.

APRIL

LUKOIL produces first oil at the Yu. Korchagin field in the Russian sector of the Caspian Sea. The field has 3P reserve in excess of 250 million boe. Peak annual production will be 2.4 million tonnes of crude oil and 1 billion cubic meters of gas. Investments for development of the field in 2004–2009 were about \$1.2 billion.



LUKOIL is acclaimed best Russian company for investor relations based on a survey by Institutional Investor magazine. More than 1,000 analysts and 650 fund managers from 531 companies took part in the survey.

JUNE

LUKOIL holds its Annual General Meeting of Shareholders, which approves the Annual Report for 2009 and annual accounts. Shareholders also approved payment of dividends for 2009 in the amount of 52 roubles per ordinary share (\$1.72 at the exchange rate of 31.12.2009).



JULY

A consortium of LUKOIL and the US company Vanco wins a tender for exploration and development of the Est Rapsodia and Trident blocks in the Romanian sector of the Black Sea. The blocks have total area of 2,000 km², and sea depth in the region is 90–1,000 meters. 3D seismic work is planned in order to clarify geological structure at the blocks. The LUKOIL share in the project is 80%, and the remaining 20% is held by Vanco.

The Board of Directors of LUKOIL approves a Code of Business Ethics. The Code regulates relations between employees and LUKOIL shareholders and investors, business partners, state authorities and public organizations. It also specifies corporate ethics and social responsibility.

A LUKOIL organization signs a agreement to acquire 7.6% of shares of LUKOIL from ConocoPhillips at \$53.25 per share to overall value of \$3.4 billion. The transaction was completed in August 2010. The agreement also includes a sixty-day option 2010 for acquisition of up to 11.61% of LUKOIL shares in ADR form.

AUGUST

LUKOIL Group takes an unsecured \$1.5 billion credit. The facility is for one year and is to be used for share buy-back from ConocoPhillips.

SEPTEMBER

LUKOIL and a group of investors, with Unicredit Bank acting as organizer, acquires 42.5 million common shares of LUKOIL in ADR form. This transaction represented partial use by the Company of the options provided under the agreement with ConocoPhillips, which was signed in July 2010. The transaction sum was about \$2.4 billion. The option was exercised in the framework of a program, approved by the Board of Directors, for increase of income to shareholders by market purchase of shares.

OCTOBER

LUKOIL begins retail sales of Euro-5 diesel fuel in Russia. The fuel is produced at Company refineries in Nizhny Novgorod, Perm and Ukhta. Euro-5 diesel has a high cetane number, which optimizes combustion of the fuel mixture, reduces noise and vibration, prevents corrosion processes, eases engine ignition and saves fuel.

NOVEMBER

LUKOIL takes 5th place among oil & gas companies in Europe, Middle East and Africa and 10th place globally in the Platts Top 250 Global Energy Company Rankings for 2010. Companies were assessed by four main criteria — asset size, turnover, income, profitability and return on average capital employed. The Company took 8th and 12th places in the same Platts rankings in 2009.

LUKOIL places two Eurobond tranches with overall value of \$1 billion at 6.125 coupon rate. The first tranche of \$800 million gives 6.25% yield to maturity and matures in 2020, and the second tranche of \$200 million gives 5.80% yield to maturity and has maturity in 2020. Funds raised from the placement were used for general corporate purposes, including repayment of existing debt.

DECEMBER

LUKOIL takes second place among the country's 75 biggest companies in a ranking by levels of social responsibility, prepared for 2010 by Trud newspaper and the Agency for Political and Economic Communications. For purposes of the ranking 'social responsibility' is understood to mean creation and preservation of jobs, tax discipline, delivering on commitments to employees, and playing an active part in projects to develop social infrastructure. The ranking is based on results of a survey among representatives of trade unions, research institutes, business associations and recruitment agencies, as well as members of the Social Chamber and deputies of the Russian State Duma.

LUKOIL signs a memorandum of understanding with the Skolkovo Foundation. The document states the LUKOIL will apply its R&D capacity in such spheres as energy efficiency in oil production and refining, clean and alternative energies, IT development, etc. Signing of an agreement on participation by LUKOIL in work by the Foundation is planned for spring 2011.

LUKOIL wins the nomination for 'Company with Best Corporate Governance' in the annual competition, 'Russian Corporate Governance Leaders', organized by the Association for Protection of Investor Rights,

which brings together some of the largest Russian and foreign institutional investors. Winners are determined by a three-stage secret ballot. Representatives of the investment community acclaimed LUKOIL for operating a system of corporate governance which has set standards in Russia over a number of years.

LUKOIL places \$1.5 billion of convertible bonds at 2.625% coupon rate, redeemable in June 2015. The bonds are convertible into ADRs trading on the London Stock Exchange, each of which represents one ordinary share of LUKOIL. The conversion price was set at \$73.7087 per ADR. The transaction represents the first large-scale issue of convertible debt instruments by a Russian issuer since the start of the crisis period. The LUKOIL bonds found strong among from the investment community thanks to the Company's high investment rating and positive attitude of investors towards the oil & gas sector.

LUKOIL starts production of Euro-4 automotive gasoline. Launch of Euro-4 gasoline production was made possible by commissioning in December 2010 of a catalytic cracking complex at the Nizhny Novgorod Refinery. Investments in the project were about \$1 billion. Euro-4 automotive gasoline gives 'clean' exhaust gas, minimizing content of sulphur oxides and products of incomplete combustion of aromatic hydrocarbons, including the particularly dangerous carcinogen and mutagen, benzopyrene.



1

OIL & GAS EXPLORATION AND 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.
- Greater use of advanced technology in operations.
- Application of financial criteria to assess projects and business results, and to optimize the asset portfolio.

E&P SEGMENT INDICATORS

Indicator	2010	2009	Change, %
Revenue, \$ million	36,976	24,353	51.8
EBITDA, \$ million	11,390	10,175	11.9
Net income, \$ million	6,226	5,456	14.1
Capital expenditure, \$ million	4,933	4,687	5.2

We focused our efforts in 2010 on efficient development of the Exploration & Production segment, which generates more than 69% of Company net income, and our efforts gave substantial results.

WE WERE ABLE TO RAISE AVERAGE DAILY OUTPUT OF HYDROCARBONS BY 1.2% THROUGH INCREASE OF GAS PRODUCTION AND REDUCING DECLINE RATES OF OIL OUTPUT IN WESTERN SIBERIA. DAILY PRODUCTION OF HYDROCARBONS WAS 2.239 MILLION BOE, CONSISTING OF 1.940 MILLION BARRELS FOR CRUDE OIL AND 0.299 MILLION BOE FOR GAS.

Start of oil production at the Yu. Korchagin field in the Caspian Sea and obtaining of tax preferences for the project are important achievements in 2010. Starting from December 2010 oil exported from the Yu. Korchagin

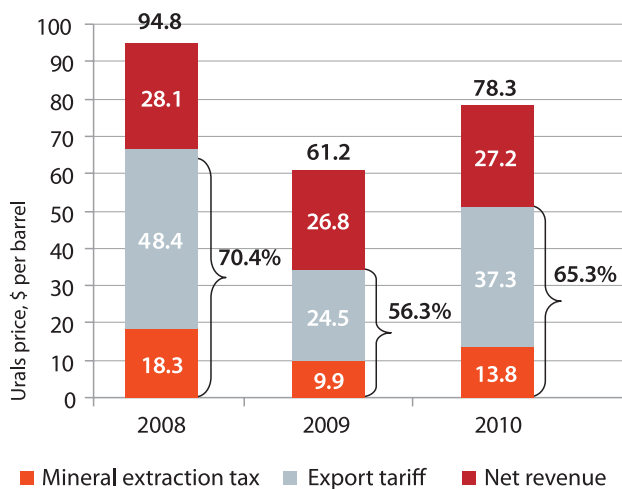
field is subject to export duties at a special low rate, comparable to that used for oil from fields in Eastern Siberia.

PRICE AND TAX ENVIRONMENT

Crude Oil Market

International prices for crude oil were higher in 2010 thanks to recovery of the world economy and soft monetary policies by central banks. Average price of Brent crude rose significantly by 28.9% in 2010 compared with 2009 to a level of \$79.5 per barrel. Most of the growth in oil prices occurred at the end of 2010.

REVENUE STRUCTURE OF A RUSSIAN CRUDE OIL EXPORTER, \$ per barrel



Crude oil prices in the first half of the year were in a corridor between \$67 and \$86 per barrel. Favorable macroeconomic statistics from the US and developing markets indicating the recovery in the consumer demand served as a growth driver for oil, but there was negative impact from decline of consumption in the Eurozone as a result of the debt crisis. Sentiment on commodity markets improved in the second half of the year. This was due, firstly, to the launch of 'quantitative easing' programs in a number of developed countries, which helped liquidity on goods and commodity markets and also on stock exchanges, supporting prices for oil and shares (further monetary emissions in the US weakened the dollar, which contributed to oil price growth). Secondly, steady growth of crude oil imports by China in an environment of refining volume growth and stable production roused expectations of further growth of demand in China. And, thirdly, onset of a cold winter with heavy snowfalls in Europe drove up demand for fuel oil.

The Company's main operating regions, accounting for 93% of crude oil production, are the oil & gas provinces of the Russian Federation (Western Siberia, Southern and Central Russia, and Timan-Pechora). So the price for Russian Urals export blend has direct impact on the Company's financial results. The average Urals price rose by 27.9% in 2010 compared with 2009 and was \$78.3 per barrel. The average price differential between Urals and Brent in 2010 was \$1.2 compared with \$0.5 in 2009. Weaker positions of Urals blend on the world market were due to increased output of competing types of crude by OPEC members as the world economy recovered.

For objective assessment of the market environment, in which the Company operated in 2010, it is important to take account of the tax burden on Russian oil exporters

and how it changed in comparison with 2009. The main types of tax payable by oil companies in Russia, including LUKOIL, are mineral extraction tax, excises and export duties. Rates of these taxes are tied to international prices for oil and vary as a function of international price levels.

As a result of growth of oil prices in 2010 the average mineral extraction tax rate for oil rose by 39.5% in dollar terms to \$13.8 per barrel.

The Company pays export duties on crude oil exports from Russia calculated using a progressive scale based on Urals prices. Increase of export duty on Urals oil in 2010 was 52%, and the average duty rate for the year was \$37.3 per barrel.

THE PRICE OF URALS OIL FOR A RUSSIAN EXPORTER NET OF TAXES (THE INTERNATIONAL MARKET PRICE WITHOUT EXPORT TARIFFS AND MINERAL EXTRACTION TAX) WAS \$27.2 PER BARREL IN 2010. THE SHARE OF MINERAL EXTRACTION TAX AND EXPORT TARIFFS IN THE AVERAGE ANNUAL OIL PRICE WAS 65.3%, 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 now governed by current legislation (at the date when a contract for mineral use comes into force), making LUKOIL liable for payment of income tax, tax on super profits, mineral extraction tax and a progressive rent tax. The Government of Kazakhstan presented plans in 2009 to lower corporate income tax rates in 2010-2011. However, no decision on this issue was taken in 2010.

Taxation of projects regulated by PSAs remains as stated in the agreements.

Gas market

There was a sharp increase of European spot prices for natural gas at the end of 2010 due to growth of oil prices, industrial recovery after the global recession, and cold weather in Europe at the start of the winter. Spot prices for gas on European exchanges exceeded prices in Gazprom's long-term export contracts for the first

time in a year and a half. At the same time gas prices on the American market were almost twice lower than in Europe, and this encouraged rapid developing of shale gas production in America. However, reserves of shale gas in the US continued to grow faster than production.

The price environment on the Russian domestic gas market remained unchanged in 2010. The average price of marketable gas rose slightly by 4.5% to \$34.9 per thousand cubic meters due to rouble appreciation.

The geography of LUKOIL's gas operations (most of the Company's gas is produced in Russia) entails that most of it is sold to OJSC Gazprom and to other Russian consumers. Most of LUKOIL's Russian gas output is sold at the well and then transported through the Unified Gas Supply System, which is owned by Gazprom. LUKOIL has no opportunity to export gas, because of Gazprom's ownership of the Supply System and its monopoly on exports. Gazprom increased its purchases from independent gas producers in Russia during 2010 thanks to increase of global demand. This resulted in significant growth of Company output of marketable gas (by 27.9%). Most of the growth was at the Nakhodkinskoye field, where production in 2010 rose by 37.2% to 8,146 million cubic meters. All of this gas was sold to Gazprom.

The Company pays natural gas extraction tax, rates of which have remained unchanged since 2008 at 147 roubles per thousand cubic meters.

Production of marketable gas by LUKOIL in international projects rose by 16.2% in 2010. 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 2010 exceeded \$140 per 1,000 cubic meters. Royalty is paid on production at a rate of 30% as part of the PSA agreement. LUKOIL has a seven-year holiday from income tax, beginning from the start of production, at the end of which income tax will also be payable at the rate fixed in the PSA. The Uzbek Government share in profit production varies depending on the project's internal rate of return for LUKOIL Group.

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.

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 RATES

LUKOIL Group produces most of its hydrocarbons inside Russia, so the largest part of Company costs are in roubles, while a significant share of revenues is expressed in US dollars or is tied to dollar oil prices to a significant extent. So rouble inflation and fluctuation



of the exchange rate can have substantial impact on Company results. Purchasing power of the US dollar in Russia, calculated from the \$/rouble exchange rate and the Russian inflation rate, declined by 11.6% in 2010 compared with 2009.

This development was one of the main causes of growth in lifting costs per unit of production in Russia last year: lifting costs rose from \$3.53 to \$4.11 per boe, or by 16.4%. Average unit lifting costs for the Group increased by 15.7% from \$3.56 to \$4.12 per boe in 2010. Capital expenditures in the E&P segment rose by 5.2% to \$4.9 billion.

LUKOIL pursued its strategy in 2010 for strengthening of the Company's financial position by focus on high-margin projects and increase of cash flows. As a result, most of capex growth in 2010 related to international projects, while growth of the indicator in Russia was only 0.5% (to \$3.9 billion).

ACQUISITIONS

The Company demonstrated its commitment to growth of shareholder value and increase of shareholder income in 2010. Following the decision by ConocoPhillips to exit its shareholding in LUKOIL, our Company carried out one of the largest buy-back transactions in the history of the Russian stock market, with value of \$3.4 billion. The operation was completed in August 2010. By carrying out the buy-back, LUKOIL protected its shareholders from a

sharp fall in the share price, which would have occurred, if the ConocoPhillips stake had been sold on the open market. ConocoPhillips had fully exited share capital of LUKOIL as of February 7, 2011.

BEST EFFORTS OF THE COMPANY TO MAXIMIZE SHAREHOLDER INCOME LED TO INCREASE OF EARNINGS PER SHARE FROM \$8.28 IN 2009 TO \$10.95 IN 2010.

The Company continued increase of its production capacities in 2010 through acquisition of highly efficient assets. A consortium of LUKOIL and the US company Vanco won a tender for exploration and development rights at the Est Rapsodia and Trident blocks in the Romanian sector of the Black Sea. The blocks cover an areas of 2,000 km², with water depth of 90–1,000 meters. LUKOIL has an 80% stake in the project, and the remaining 20% is held by Vanco.

OPTIMIZATION OF CORPORATE STRUCTURE AND CONSOLIDATION

The total number of LUKOIL subsidiaries and affiliates decreased by 19 in 2010 and totalled 362 (subsidiaries and affiliates determined in accordance with US GAAP), including disposal of 13 non-core assets. Several marketing operators were augmented by their merger with subsidiaries. Consolidation of 100% of shares in CJSC LUKOIL-Neftekhim was completed and target ownership structure for petrochemical assets was approved.



■ LICENSING

The Group continued its work in 2010 to obtain new licenses for mineral use and optimize its existing license portfolio in order to raise overall quality of the mineral base. LUKOIL obtained amendments and additions to conditions of its mineral use rights, extending the period of validity of its rights in some cases, as well as clarifying commitments of Group companies to achieve specific output levels in accordance with project documentation.

LUKOIL GROUP COMPANIES HAD 421 LICENSES ON THEIR BALANCE SHEETS AT THE END OF 2010, OF WHICH 340 WERE FOR EXPLORATION & PRODUCTION OF HYDROCARBONS, 18 WERE FOR GEOLOGICAL STUDY, INCLUDING PROSPECTING AND EVALUATION OF MINERAL FIELDS, AND 63 WERE FOR GEOLOGICAL STUDY, EXPLORATION AND PRODUCTION OF HYDROCARBONS.

The Company obtained 11 new licenses for use of mineral resources in 2010, of which 2 were based on proof of a field discovery, 8 were obtained as a result of auctions and competitions, and one was obtained through application for geological study. Spending on license acquisitions was \$15 million.

LUKOIL obtained reissue of 71 licenses for use of mineral resources in 2010 in connection with further restructuring of oil & gas production companies within the Group.

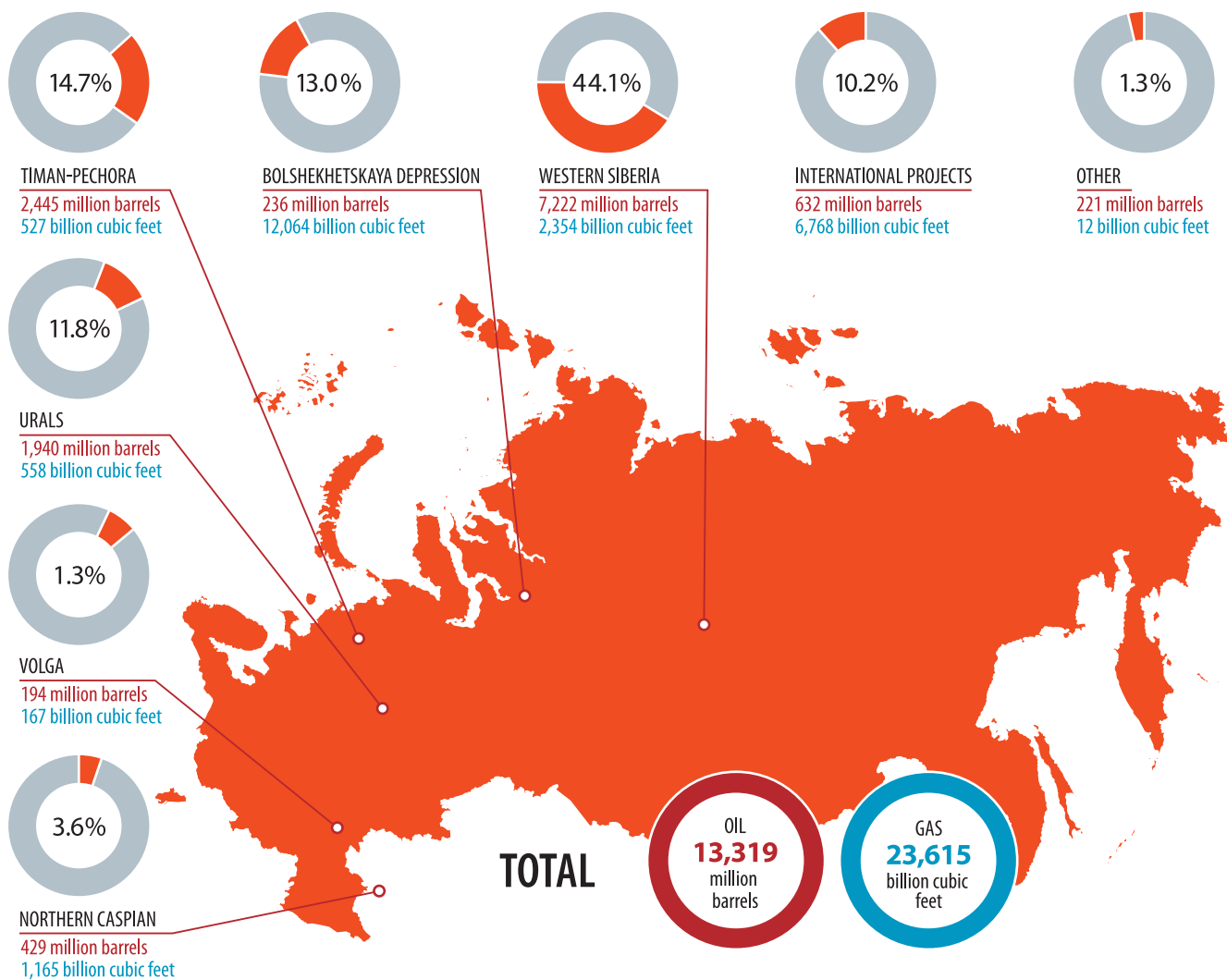
The Group registered 16 additions to licenses in 2010 in order to extend their period of validity. Work also continued on amendments and additions to current license agreements. A total of 35 additions were obtained to reflect changes in geological exploration schedules, clarification of borders of license 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

PROVED OIL & GAS RESERVES OF LUKOIL GROUP BY REGIONS IN 2010





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.

ACCORDING TO DATA AUDITED BY MILLER AND LENTS (USA), THE COMPANY'S PROVED RESERVES OF HYDROCARBONS AS OF JANUARY 1, 2011 WERE 17.255 BILLION BOE, CONSISTING OF 13.319 BILLION BARRELS OF OIL AND 23.615 TRILLION CUBIC FEET OF GAS.

The audit was carried out to the standards of the US Securities and Exchange Commission (SEC). The Company decided in 2009 to adopt SEC standards for measurement of reserves in order to ensure greater transparency and comparability of Group reserve figures with those of competitors.

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 before the start of development. The audit of LUKOIL reserves took account of changes in development plans contained in the Group's Strategic Development Program.

LUKOIL also completed an evaluation of contingent resources under PRMS classification in 2010. Unaudited figures as of January 1, 2011 showed 3C contingent

resources of 10.7 billion barrels of oil equivalent. These oil and gas volumes will be moved from resources to reserves in the future as the time for their development approaches, as the Company's associated gas utilization program moves forward, and as new technologies make production of hard-to-recover reserves commercially viable.

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 (Western Siberia), Uzbekistan and the Caspian region. 60% of Company proved reserves are in development (66% of oil reserves and 38% 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 control development costs in an efficient manner and to bring new fields into production rapidly.

Growth of proved hydrocarbon reserves in 2010 as a result of geological exploration work, production drilling and acquisitions was 687 million boe, representing 82% of production during the year. Growth due to geological exploration work and production drilling was 625 million boe, and 62 million boe were added as a result of acquisitions. So organic growth of hydrocarbon reserves compensated 75% of production (81% for

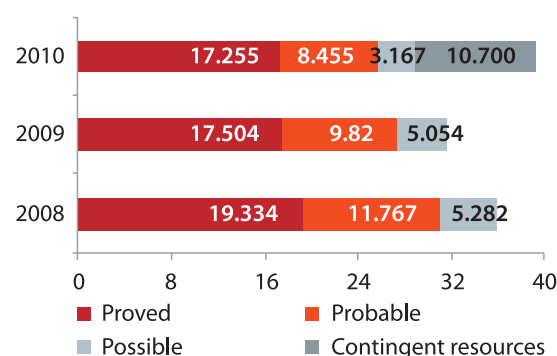
oil and 44% for gas). Most of the organic growth of proved oil reserves was obtained in Western Siberia (68% of the total) and the Komi Republic (12% of the total). Organic growth of proved gas reserves was also obtained in Western Siberia (61% of the total, including 35% at Bolshekhetskaya Depression) and in international projects: Kandym-Khauzak-Shady and Karachaganak (30% of the total for gas).

Proved reserves were lowered by 102 million boe in 2010 due to revision of earlier evaluations. One cause of the revision was worsening of economic parameters following increase of mineral extraction tax on oil and free gas.

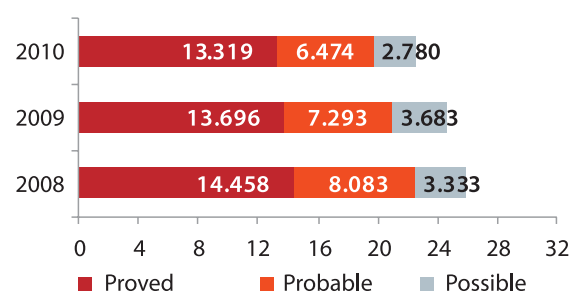
Inclusion of the Company's stake in proved reserves at the West Qurna-2 field, amounting to 62 million barrels of oil, did not have significant impact on total reserve levels for the Company, since the preliminary development plan only takes account of volumes brought into the first stage of development ('early oil'). However, significant increase of reserves is expected in the future as drilling-over of the field continues in the second development stage.

OVERALL, THE FIGURES FOR 2010 SHOW THAT LUKOIL REMAINS AMONG RUSSIAN AND INTERNATIONAL LEADERS BY VOLUME OF PROVED HYDROCARBON RESERVES. THE GROUP'S RATIO OF PROVED HYDROCARBON RESERVES TO PRODUCTION IS 21 YEARS (19 YEARS FOR OIL AND 31 YEARS FOR GAS).

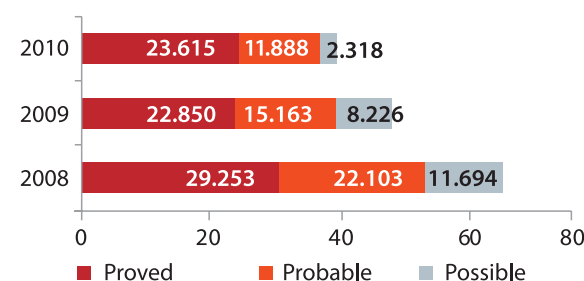
■ 3P HYDROCARBON RESERVES AND CONTINGENT RESOURCES, billion boe



■ 3P CRUDE OIL RESERVES, billion boe



■ 3P GAS RESERVES, trillion cubic feet



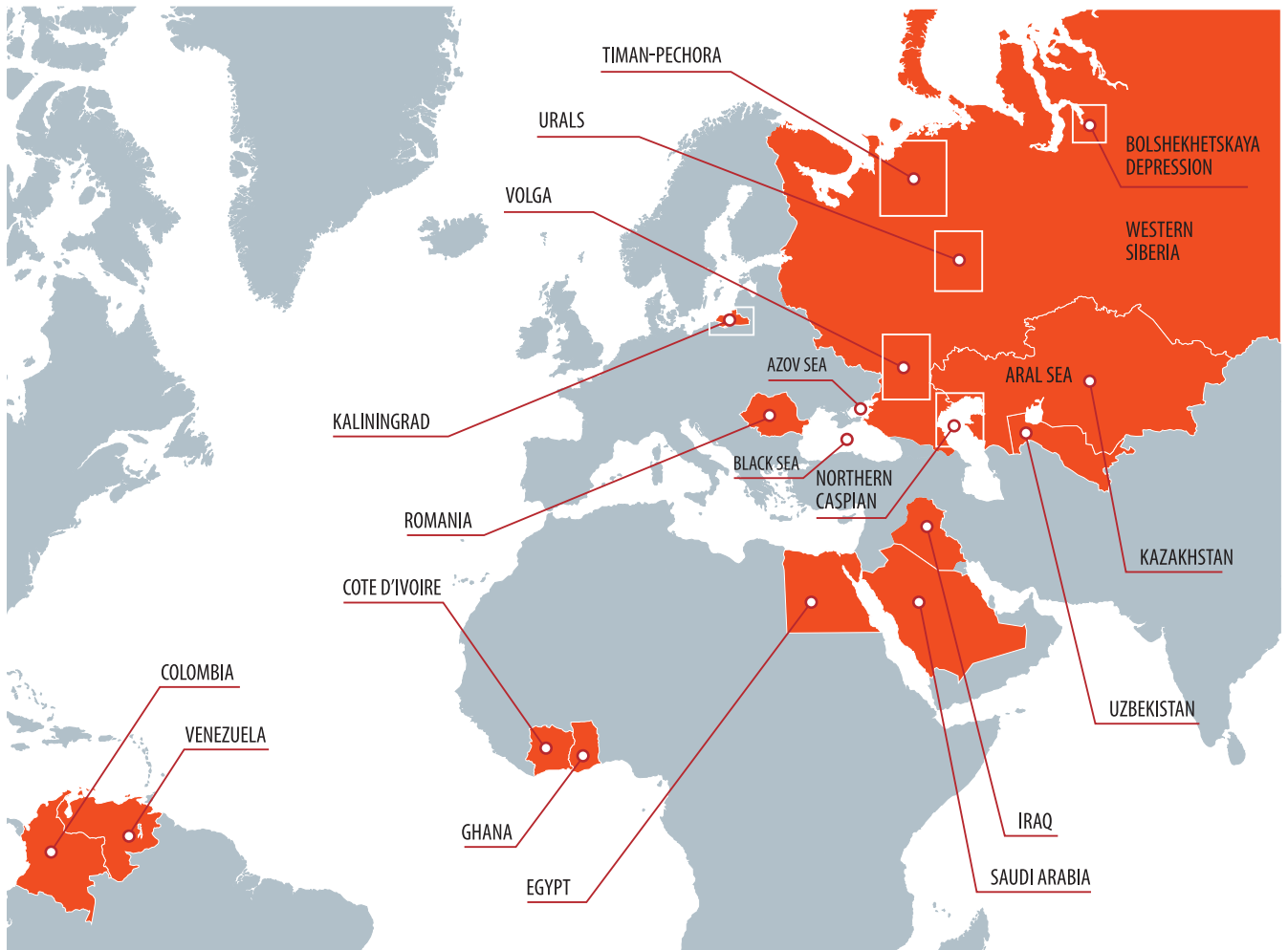
■ OIL & GAS RESERVES OF LUKOIL GROUP

January 1, 2011	Oil		Gas	Oil + gas ¹
	million barrels	billion cubic feet	billion cubic feet	million boe
Proved reserves	13,319	23,615	23,615	17,255
of which:				
Developed	8,790	8,882	8,882	10,270
Undeveloped	4,529	14,733	14,733	6,985
Probable reserves	6,474	11,888	11,888	8,455
Possible reserves	2,780	2,318	2,318	3,167

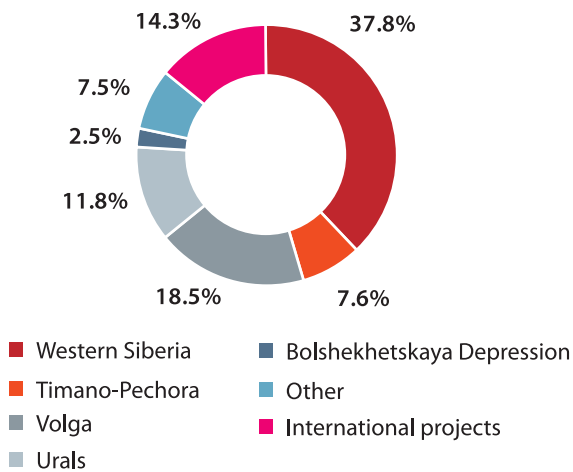
¹ The ratio used for recalculation of cubic feet as barrels of oil equivalent (boe) is: 1 boe = 6,000 cubic feet

■ GEOLOGICAL EXPLORATION

■ MAIN GEOLOGICAL EXPLORATION REGIONS OF LUKOIL GROUP



■ EXPLORATION DRILLING BY REGIONS (2010), %



Geological exploration work by companies of LUKOIL Group in 11 countries around the world is focused on replacement of production with new commercial reserves of hydrocarbons, and preparation of reserves for rapid launch and expansion of production in promising regions, both in Russia and abroad (Timan-Pechora, the Northern Caspian, the Bolshekhetskaya Depression, Ghana). The Company uses the latest technologies in order maximize efficiency of its geological exploration.

THE MOST NOTABLE ACHIEVEMENT OF LUKOIL'S GEOLOGICAL EXPLORATION WORK IN 2010 WAS THE FIRST-EVER DISCOVERY BY A RUSSIAN OIL COMPANY OF A DEEPWATER OIL & GAS FIELD. THE DISCOVERY WAS MADE ON THE CONTINENTAL SLOPE IN THE GULF OF GUINEA, OFF THE COAST OF GHANA, AS PART OF THE CTPDW PROJECT. THE FIELD IS A PART OF THE DZATA STRUCTURE, AND IS AT A SEA DEPTH OF 2,000 METERS. THE WELL, WHICH DISCOVERED THE FIELD, WAS DRILLED TO A DEPTH OF 4,500 METERS BELOW SEA LEVEL.

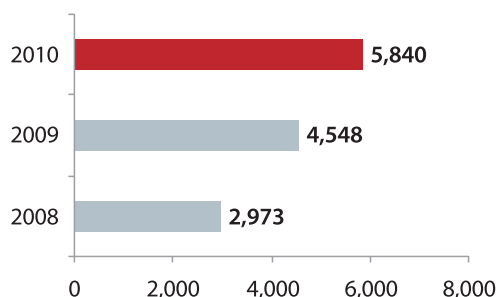
Most of the Company's geological oil & gas exploration work in 2010 was concentrated in Western Siberia, the Timan-Pechora oil province and international projects. The Company's largest prospecting projects in 2010 were further study of the Tsentralno-Astrakhanskoye gas and condensate field and work in the offshore Caspian to assess oil & gas prospects in Neocomian sediments at the Rakushechnoye field and Lower-Chalk and Jurassic sediments at the Ukatnaya structure. Prospecting work also continued in 2010 to study geological structure and oil & gas potential at the Denisovskaya Depression in the Komi Republic. Outside Russia we carried out studies of prospects on the West African shelf, in the Aral region and also as part of the Riyadh project in Saudi Arabia. Geological exploration work in other regions was focused on preparation and reconnaissance of prospective new geological targets and additional exploration at fields, which were discovered earlier.

The Company substantially increased 2D seismic work in 2010 to locate and detail geological structures and to prepare for drilling of prospecting and exploration wells, shooting a total of 6,178 km of 2D in comparison with 2,446 km in 2009. International projects accounted for 17% of the total, reflecting expansion of the Company's operations outside Russia. 3D seismic volumes also increased, reaching 5,840 km², of which 30% was as part of international projects. Quality of our seismic work and speed of processing and interpretation have improved in recent years, due particularly to application of new computer technologies.

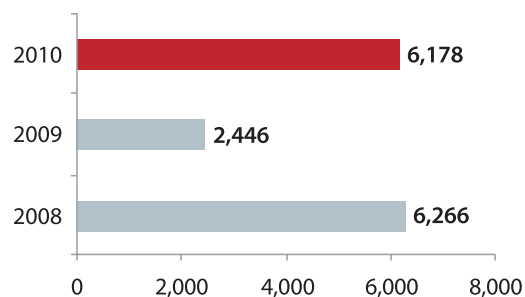
HIGH STANDARDS OF THE GROUP'S SEISMIC WORK ARE DEMONSTRATED BY CONSISTENT SUCCESS RATES ABOVE 70% IN PROSPECTING AND EXPLORATION DRILLING

LUKOIL companies are in the process of switching to denser and wider-amplitude observation systems in order to obtain more informative data and achieve more accurate forecasting of filtration-volume characteristics

■ 3D SEISMIC, km²



■ 2D SEISMIC, km





of reservoirs, and of their fracturing qualities. Surveys at the Tsentralno-Astrakhanskoye, Rossokhinskoye, Severo-Vozeiskoye and Sredne-Nazymskoye fields are using high-amplitude 3D techniques.

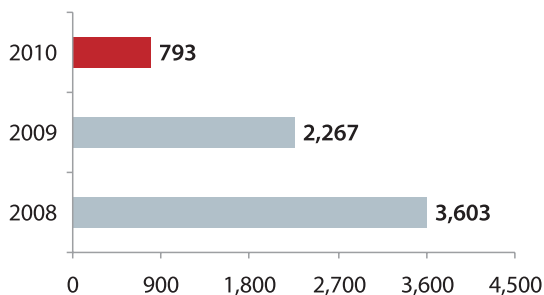
LUKOIL completed 793 km of electrical exploration in 2010. Vertical seismic profiling, which enables detailing of geological structure around an existing well, was carried out at eight wells. Total exploration drilling in 2010 amounted to 118,800 meters, and efficiency was 1,143 tonnes of conditional fuel per meter. A total of 32 prospecting and exploration wells were completed in 2010 of which 22 were productive.

Group companies discovered six fields in 2010 (Olginskoye in Tatarstan, Dulepovskoye in Perm Territory,

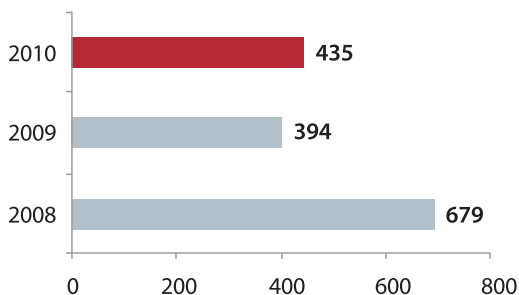
South-East Kyzylbairak and West Aral in Uzbekistan, Arcadia in Egypt and Dzata in Ghana), as well as 25 new oil deposits at fields in Western Siberia and Perm Territory.

Increase of proved reserves under SEC standards during 2010 through geological exploration and additional information obtained in the course of production drilling amounted to 625 million boe. Most of the organic growth of proved oil reserves was obtained in Western Siberia (68% of the total) and the Komi Republic (12% of the total). Organic growth of proved gas reserves was also obtained in Western Siberia (61% of the total, including 35% at Bolshekhetskaya Depression) and in international projects: Kandym-Khauzak-Shady and Karachaganak (30% of the total for gas). Spending by LUKOIL Group on geological exploration work in 2010 was \$435 million.

■ ELECTRIC EXPLORATION, km



■ SPENDING ON GEOLOGICAL EXPLORATION, \$ million



RUSSIA

Exploration drilling in Russia in 2010 totalled 102,000 meters, 2D seismic exploration was 5,076 km and 3D seismic was 4,116 km². Spending on geological exploration in Russia was \$236 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 particularly efficient and productive.

Exploration drilling in the District totalled 44,900 meters in 2010 and nine wells were completed, of which seven were productive. The success rate of exploration drilling was 78%. 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 shot 499 km of 2D seismic and 2,415 km² of 3D seismic in the course of the year. 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 prior to production drilling. Some 275 km² of 3D surveying was carried out at the Vostochno-Kayumovskiy areas, which were acquired in 2009.

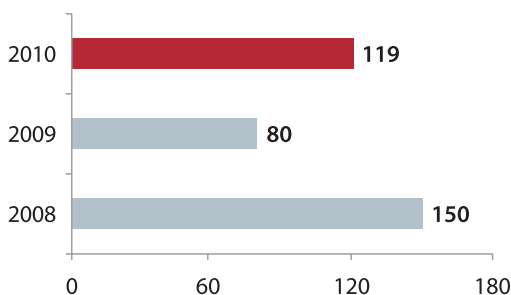
LUKOIL identified 14 new deposits at previously discovered fields in the region during 2010. Largest growth of oil reserves was at the Mishaevskoye, Pokachevskoye and

Vateganskoye fields, thanks to 3D work and exploration drilling. Proved hydrocarbon reserves of the Company in Khanti-Mansiysk Autonomous District to SEC standards were 7.6 billion boe by the end of the year. Significant oil flows were obtained at a number of fields.

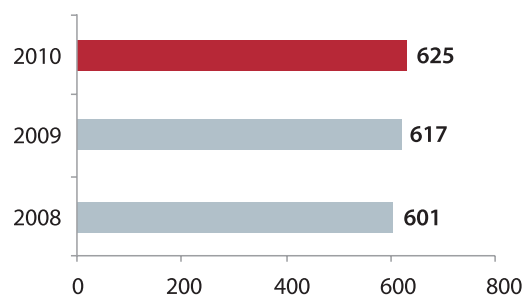
Testing of Achimian sediments gave a daily oil flow of 180 barrels and a daily flow of 160 barrels was obtained at the Yuzhno-Pokachevskoye field. Geological work led to a water-free daily flow of 1,010 barrels at the Kozhevskoye field. Drilling and well-testing was also carried out at the Vostochno-Perevalny, Zapadno-Kotukhtinsky, Aprelsky, and Bolshoi license areas. Oil flows were obtained at all wells and daily flow rate at the Vostochno-Perevalny field was up to 320 barrels.



■ HYDROCARBON RESERVE EXTENSIONS AND DISCOVERIES, million boe



■ EXPLORATION DRILLING, thousand meters



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, and Yuzhno-Tarasovskoye oil, gas and condensate fields, as well as the Urabor-Yakhinsky and Vansko-Namyssky areas.

2D seismic work amounting to 700 km was carried out at the Nakhodkinsky license area in order to identify non-anticlinal traps in chalk sediments.

Proved hydrocarbon reserves at Company fields in the Bolshekhetskaya Depression grew by 5.5% in 2010 compared with 2009 to 2.2 billion boe (more than 13% of LUKOIL's total proved hydrocarbon 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 2010. Volumes of 2D and 3D seismic work during 2010, for clarification of geological models, were 1,066 km and 813 km², respectively, and exploration drilling was 9,400 meters.

Total 9,400 km of prospecting and exploration drilling was carried out during 2010 in the **Komi Republic** and two wells were completed at the Bayandyskoye field, both of which were productive. The drilling success rate was thus 100%. Well-testing gave daily flows of 200 and 1000 barrels of oil, respectively. Both wells have been brought into production.

Testing of an exploration well was completed at the Oshskoye field in **Nenets Autonomous District**, and daily oil flow of 2,700 barrels was obtained. 2D seismic surveying was carried out on 710 km at the Yuzhno-Tedinsky and Predtimansky areas, and 776 km² of 3D seismic was shot at the Yuzhno-Khoreiverskoye, Vostochno-Tedinsky and Vangureyakhinskaya areas. A 3D survey of 128 km² was in progress during 2010 at the Denisovskaya Depression.

Geological work and additional information obtained in the course of production drilling added 78 million barrels of proved reserves to international standards in Timan-Pechora during 2010.

Naryanmarneftegaz, the joint venture between LUKOIL Group and ConocoPhillips began secondary testing of an exploration well to investigate production potential of a high-viscosity oil deposit in Carbonaceous sediments. Initial daily oil flow was 200 barrels.

Urals

The Urals is a traditional production region for the Company, and reserves in the region have been extensively explored. LUKOIL carried out 61 km of 2D seismic and 768 km² of 3D work in the region for geological purposes during 2010. Exploration drilling totaled 13,900 meters. Exploration drilling to discover new fields and increase reserves was carried out mainly in the vicinity of sites with established commercial oil presence.

In **Perm Territory** construction of three wells was completed, two wells were drilled, and testing work began at the Enapaevskaya and Zabrodovskaya areas. All of the wells gave flows from productive strata at daily rates of 100-200 barrels, so the prospecting success rate was 100%. One new field was discovered in 2010 — the Dulepovskoye field, at which testing gave an oil flow of 200 barrels per day.

Volga (onshore)

The Volga is another traditional hydrocarbon production region for LUKOIL and its geology has been extensively studied. Exploration drilling in 2010 was 19,500 meters and 1,385 km of 2D seismic was carried out in **Volgograd Region** (the administrative territory). LUKOIL companies also completed 593 km of electric exploration work and 100 km of geochemical studies. Drilling of an exploration well was begun at the Beshkulskoye field.

An exploration well was completed at the Nemirovskoye field and gave a commercial flow of 400 barrels per day when tested. The well has been brought into production. Drilling of an exploration well began at the Tsentralno-Astrakhanskoye field to clarify field structure, so that reserves can be transferred to the industrial category and 3D seismic work began in the northern part of the field (45 km² were shot during 2010).

Drilling and well testing were carried out at the Agryzsky, Menzelinsky and Ozerny areas in the **Republic of Tatarstan**. One prospecting well was completed at the Yuzhno-Izhevskaya structure and a new field —

the Olginskoye field — was discovered. Testing of a Zavolzhsky horizon in the Upper Devonian gave a daily oil flow of 610 barrels using a choke. C1 recoverable oil reserves are 1.4 million tonnes.

2D seismic work (301.3 km) was carried out at the Menzelinsky license area.



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.

In the **offshore Caspian** Well-7 was completed at the Rakushechnoye field, and results suggest C1 reserve increase of 621 billion cubic feet and additional 2.7 million boe of gas condensate. 2D seismic work was completed at the Tsentralno-Kaspiisky license area (500 km), and 200 km of electrical exploration was also 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 to Gazprom), drilled a prospecting well at the Ukatnaya structure and discovered oil & gas strata in Mid-Jurassic sediments. The deposit is in thin-layered, medium-to-fine grained sandstone. Strata testing gave flows of oil, gas and water, and discovery of a commercial hydrocarbon deposit was confirmed.

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 414 km of 2D seismic during 2010. The material has been processed and interpretation has begun.

Priazovneft discovered the Novoye field in the offshore Azov Sea in 2007 and has taken a joint decision with Rosneft to carry out further geological work at the central part of the license area.

Kaliningrad Region

LUKOIL companies carried out geological work in 2009 in Kaliningrad Region both onshore and in the offshore Baltic Sea. Offshore work was in preparation for drilling of a first prospecting well.

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 with LUKOIL participation was 17,300 meters in 2010. The Group's share of 2D seismic work in international projects in 2010 totaled 1,102 km and its share of 3D work was 1,724 km². Spending on geological exploration outside Russia was \$199 million.

LUKOIL was involved in geological exploration projects in nine countries outside Russia by the end of 2010: Colombia, Kazakhstan, Saudi Arabia, Uzbekistan, Cote d'Ivoire, Ghana, Egypt, Venezuela and Iraq (preparation for production). Seven exploration wells were drilled as part of these projects in the course of the year, of which four were productive (a success rate of 57%).

Drilling of Well Dzata-1 with depth of 4,500 meters was completed in 2010 at the **CTPDW block** in the **Republic of Ghana** (Company share in the project is 56.66%). The well discovered an oil and gas condensate field and confirmed presence of an oil & gas bearing system at the block. The main sandstone reservoir contains gas and light crude oil. The well was drilled using a semi-submersible rig with a dynamic positioning system. A plan of field evaluation was approved in 2010 in order to clarify filtration-volume features of reservoirs, the nature of saturation and geometry of deposits. The calculations, which

have been carried out, suggest that the field is commercially viable. Main risks are associated with confirmation of reserves and obtaining commercial flows. The Company is preparing for reconnaissance of other geological targets on the block territory, evaluation of which could increase the resource base and improve financial criteria of the project.

The Cape Three Points discovery makes LUKOIL the first Russian company to locate an oil & gas field on a deep-water continental slope, and proves that use of new technologies is helping the Company to remain in the oil & gas industry vanguard.

The Dzata structure confirms good prospects of Ghana's deepwater shelf and provides an excellent opportunity to deploy the latest production technology to best effect.

Drilling of Well Orca-1 to depth of 4,000 meters was completed at **Block CI-401 in Cote d'Ivoire**, and drilling gave evidence of oil & gas saturation in Campanian and Turonian stages, including a sample of water-free oil. The drilling results point to presence of lithologic and stratigraphic deposits in the Turonian complex at block CI-401.

A technical description was prepared for the Kakao site at **Block 205 in Cote d'Ivoire**. Hydrocarbon resources amounting to 147.3 million tonnes of oil and 31.3 billion

cubic feet of gas have been confirmed. Drilling of a well is planned in 2011.

At the **Riyadh (Block A) project in Saudi Arabia** drilling of Well Tukhman-4 was completed to sediments at the Sharavra formation, and a modest flow of gas and condensate was obtained from testing of the Unaiza formation. The well has been suspended until a technology can be applied to increase the flow rate. Additional testing of the middle and upper interval of the Sara formation was carried out at Well Faidakh-2. Current daily gas flow rate is 53,000 cubic meters. The well has been suspended pending choice of a technology, which can enhance the rate of flow.

3D survey work totaling 674 km² was carried out at **Condor project in Colombia** during 2010 in the region of the East-Guavio and Cumoral structures.

The first stage of preparatory work began at the end of 2009 for drilling of Well Amarilo-1, and a co-investor for well drilling is being sought. Preparation of an environmental impact assessment and the procedure of obtaining an environment license are also underway.

The investment consortium working on the **Aral project in the Uzbek sector of the Aral Sea** (LUKOIL has a 20% stake in the project) completed drilling of the first well, WAEx-1. Bottom-hole is at a depth of 3.3 km. The well has



found a multi-bed field with gas-condensate deposits in Mid-Jurassic sediments. Maximum daily gas flow is 319,500 cubic meters.

Preparatory work was carried out at the **Kungrad block in Uzbekistan** for drilling of Well Shege-1.

In the **South-West Gissar project in Uzbekistan** a well was drilled to 2,521 meters at the western dome of the South-East Kyzylbairak structure and penetrated prospective Upper Jurassic sediments obtaining a daily gas flow of 442,000 cubic meters. Prospecting and exploration Well Shamoltegmash-4 is to be drilled in 2011 in order to transfer reserves from C2 to C1 at the Kyzylbairak field. Planned well depth is 350 meters.

Preparations were made for drilling of a well in the **Kazakh sector of the Caspian Sea** as part of the **Tyub-Karagan** project. Geological resources at the structure are 317.6 million tonnes of conditional fuel under Russian classification.

In February 2009 the Group became the operator at the **WEEM Extension**, adjacent to the **WEEM block in**

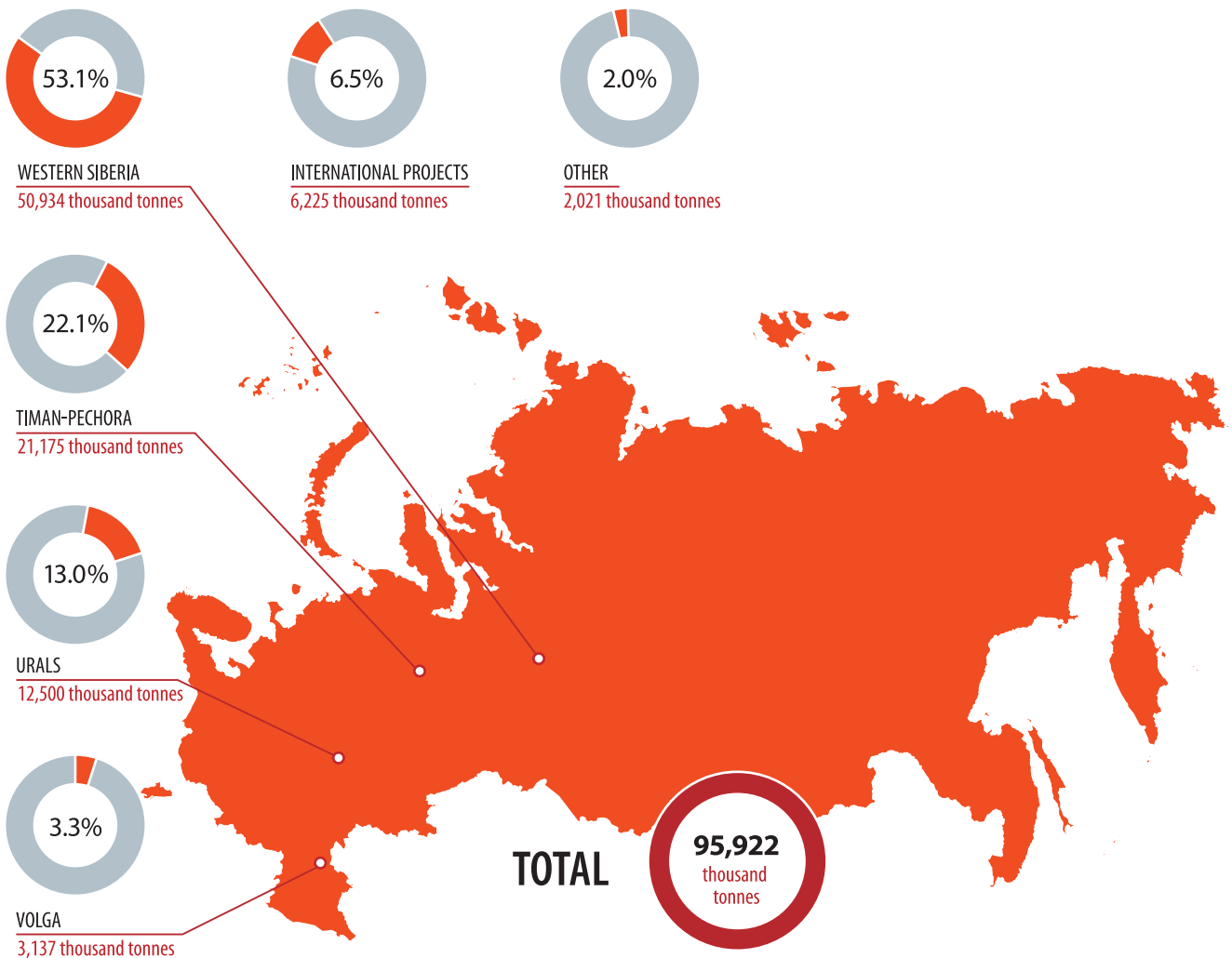
Egypt. More than 60% of the WEEM Extension was already studied by LUKOIL in 2006 using high-definition 3D seismic. A slanted well, WEEM E-A-1, drilled to a depth of 1,829 meters found more than 30 meters of oil-saturated reservoirs and obtained daily oil flow of 1,100 barrels from the Nubia structure. The well has reached the contour zone of the deposit. Drilling of Well WAE-2 has been completed: planned depth was 2,324 meters, but bottom-hole is at 2,658 meters. The well penetrated the Matulla and Nubia horizons in a lowered section of the block, but was unproductive. The well has been suspended pending a decision based on results of 3D seismic work.

LUKOIL won a tender in 2010 for exploration and development rights at the Est Rapsodia and Trident offshore blocks in the Black Sea off the coast of **Romania**. 3D seismic exploration work is planned to clarify geological structure of the blocks. A concession agreement is being prepared for signing with Romania's National Agency for Mineral Resources. An office of LUKOIL Overseas Holding Ltd will be opened for project management purposes.

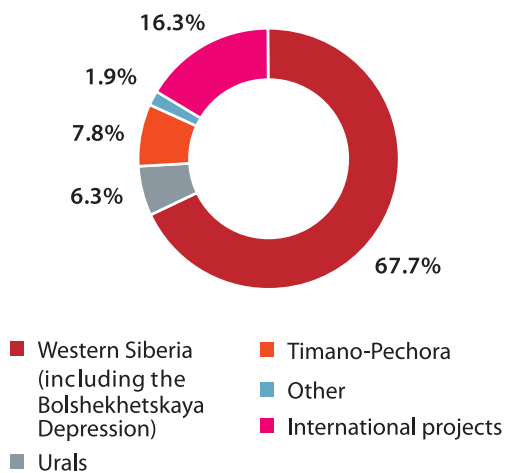


OIL FIELD DEVELOPMENT AND PRODUCTION

OIL PRODUCTION BY REGIONS



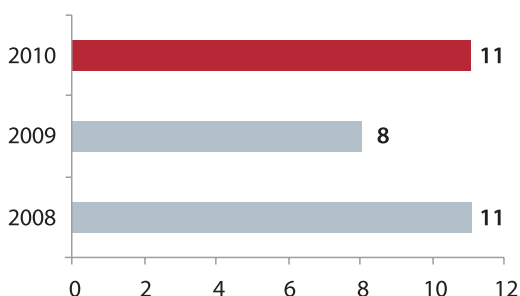
PRODUCTION DRILLING BY REGIONS (2010)



CRUDE OIL PRODUCTION BY LUKOIL GROUP IN 2010 (INCLUDING SHARE OF PRODUCTION BY EQUITY AFFILIATES) WAS 95.922 MILLION TONNES (1.940 MILLION BARRELS PER DAY).

Average daily output fell by 1.6% in comparison with 2009. Lower oil output in 2010 reflects a production decline at fields in Western Siberia, where the Company produces 53% of its crude, and was due primarily to objective changes in the structure of recoverable reserves. However, use of the latest enhanced recovery technologies and horizontal drilling enabled LUKOIL to reduce the rate of crude output decline in Western Siberia from 5.7% in 2009 to 3.8% in 2010. LUKOIL has also successfully addressed the problem of electricity supply shortages for production operations, which arose in recent years in Western Siberia. The Company is building and commissioning its own power generating capacities at fields, and the shortages have now been almost completely overcome.

NEW FIELDS COMMISSIONED, fields



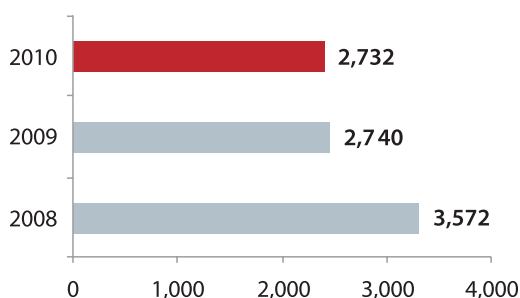
The main achievement in the Company's production business during 2010 was launch of production at the Yu. Korchagin field where annual oil extraction will reach 2.4 million tonnes and gas output will be 1 billion cubic meters at peak production. Yu. Korchagin is the first of a group of LUKOIL fields in Russian territorial waters of the Caspian Sea to have been brought into operation. Development of the field will use a system of long horizontal wells (over 5 km in length) representing a unique solution for the Russian industry. Logging will be carried out as part of the horizontal-well drilling process. Radial distribution of wells will enable simultaneous penetration of all productive layers.

The Company continued its work on improvement of field development efficiency and reduction of operating costs in the reporting year. 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 2010. As a result field development spending rose by 4.0% in 2010 compared with 2009 to a level of \$4.599 billion, despite increase of inflation to 8.7% and real strengthening of the rouble by 11.6%.

LUKOIL subsidiaries and equity affiliates produced hydrocarbons at 355 fields in Russia and 11 projects abroad in 2010. A total of 11 new fields were brought into development during the year, as follows: Severo-Pokamasovskoye, Mishaevskoye, Svobodnoye, Timerovskoye, Olginskoye and Lenzitskoye (Western Siberia); Yu. Korchagin (Volga); Sharonovskoye, Preobrazhenskoye (Urals); Olginskoye and Yu. Rossikhina (Timan-Pechora). The largest production increases (more than 200,000 tonnes) were achieved at four fields: Bayadynskoye and Usinskoye in Timan-Pechora; and Kechimovskoye and Urevskoye in Western Siberia.

The Company had 30,340 oil production wells as of January 1, 2011, of which 25,990 were actually in use, and the number of water injection wells was 10,320, of which 8,120 were under pressure. The number of oil production

OIL PRODUCTION DRILLING, thousand meters



wells was 2.0% higher than in 2009. The share of idle wells was almost unchanged from the end of 2009 at 14.3% of the total number. Average daily oil flow from wells in projects with Group participation was 14.5 tonnes.

Volumes of production drilling were nearly unchanged, totaling 2,732,000 meters, which is 0.3% less than in 2009. The number of new production wells brought into operation was 1,077, of which 101 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 35.8 tonnes, including 156.6 tonnes from horizontal wells. Flow rates at new wells were 3% higher than in 2009 thanks to improvement in geological and hydrodynamic models and greater application of such models in planning of drilling work, and also as a result of further work to improve well completion technologies and initial and secondary penetration of productive formations.

USE OF NEW DRILLING AND WELL COMPLETION TECHNOLOGIES, SELECTION OF OPTIMAL BOREHOLE TRAJECTORY WITH CLARIFICATION OF THE GEOLOGICAL MODEL DURING DRILLING, USE OF BOTTOM-HOLE CONTROL SYSTEMS AND REAL-TIME DRILLING MANAGEMENT TO MAXIMIZE BOREHOLE CONTACT WITH THE RESERVOIR GAVE AN INCREASE OF AVERAGE OUTPUT FROM HORIZONTAL WELLS BY 2.3 TIMES COMPARED WITH 2009.

The Company increased efficiency of sidetracks by 17.3% in 2010, despite a 15.2% reduction of this work in Russian operations compared with 2009. The improvement was mainly due to more accurate forecasting of geological structure and the structure of reserves at areas where sidetracks were used. Sidetrack drilling is carried out mainly at wells, which have been taken out of operation, in order to extract residual oil reserves. Sidetracks were drilled at 224 wells in 2010 and gave average daily flow of 19.7 tonnes.

Efficiency of hydrofracturing operations at Company wells in 2010 was comparable with the result in 2009. Positive effect from hydrofracturing was maintained thanks to effective planning work, selection of wells using full-time hydrodynamic models, and tighter control over the quality of materials and reagents used by service companies.

A total of 4,869 operations were carried out on productive formations using physical, chemical, hydrodynamic and heat techniques (see 'Exploration and Production Technologies' on page 78). Additional oil output in Russia thanks to application of enhanced oil recovery techniques was 22.1 million tonnes, or 25% of total oil production by the Group in Russia.

RUSSIA

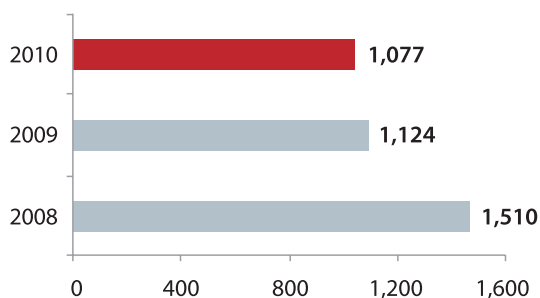
Oil production by LUKOIL in Russia during 2010 was 89.767 million tonnes, of which 89.431 million tonnes were produced by Group subsidiaries.

Subsidiaries and equity affiliates of LUKOIL produced hydrocarbons at 355 fields in Russia in 2010. Production drilling in Russia declined slightly to 2,286,000 meters. The Group owned 28,610 production wells at the end of 2010, of which 24,420 were actually in use.

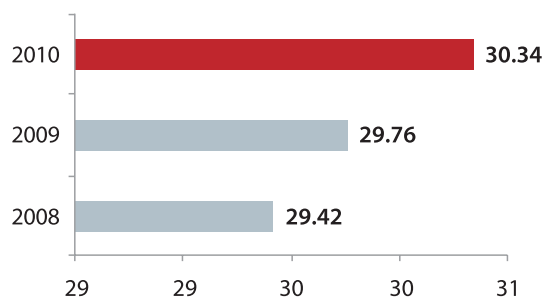
Western Siberia

Fields in **Western Siberia** accounted for 56.7% of LUKOIL's Russian oil production in 2010. Production in the region was somewhat lower than in 2009 at 50.93 million tonnes. Use of enhanced oil recovery methods and drilling of horizontal boreholes enabled LUKOIL to reduce the rate of production decline in Western Siberia from 5.7% in 2009 to 3.8% in 2010. The Company will continue to focus

OIL PRODUCTION WELL LAUNCHES, wells



OIL PRODUCTION WELLS, thousand wells





on stabilization of production levels in main operating regions, stepping up investments into development of new technologies and improvement of field efficiency.

Stabilization of output levels in Western Siberia is complicated by gradual natural exhaustion of the resource base, due to the long period of production at most Company fields in the region, which has depleted their reserves. LUKOIL is combating output decline by use of the latest technologies, which enable substantial increase of the recovery ratio 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 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 58).

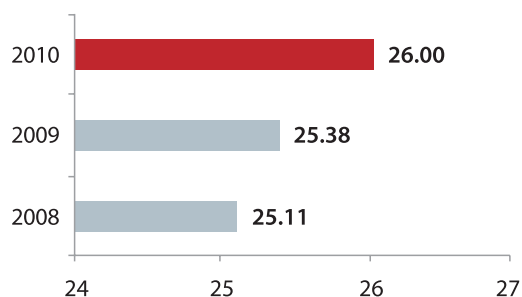
Despite long periods of exploitation, some of the Company's fields in Western Siberia have significant potential for production growth. In particular, the Kechimovskoye and Urevskoye fields showed strong oil production growth once again in 2010.

Oil production at the **Kechimovskoye field**, which was launched in 1995, grew by 30.2% in 2010 compared with 2009 to 2.01 million tonnes thanks to new production drilling: a total of 102 new wells were brought into production with average daily flow rates of 32.8 tonnes, including 27 horizontal wells with average daily flow rate of 61.9 tonnes. Oil production from new wells was 530,800. New wells brought into operation during 2009 (92 wells with average daily flow rate of 27.9 tonnes, totaling 644,300 tonnes in the year) made an important contribution to output in 2010, which was their first full calendar year in production. Work continued on a system to maintain reservoir pressure: 49 new injection wells were put under pressure during the reporting year.

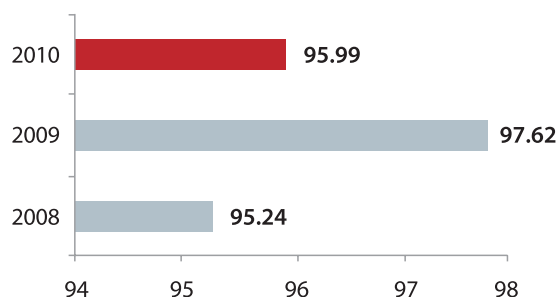
The Kechimovskoye field is one of the Company's largest investment projects in Western Siberia: in accordance with the project schedule, 361 wells remained to be drilled as of January 1, 2011, of which 270 oil wells and 91 injection wells.

Oil production at the **Urevskoye field**, which was brought into production in 1978, rose by 9.3% to 2.86 million tonnes in 2010. The increase was achieved thanks to production drilling: 83 new wells were launched with average daily output of 25.7 tonnes, including two horizontal wells with daily flow of 59.1 tonnes. Oil production at new wells in the reporting period was 352,300. A total of 12 sidetracks were drilled at the field in 2010 in order to maintain output levels at wells, and they gave average daily flow increases of 12.5 tonnes, producing 20,700

■ OIL PRODUCTION WELLS, thousand wells



■ OIL PRODUCTION, million tonnes



tonnes of additional oil in total. Work continued on a system for maintaining strata pressure, and 29 new injection wells were put under pressure in the reporting year. There were 843 wells still to be drilled at the Urevskoye field as of January 1, 2011, in accordance with the field development schedule. LUKOIL's development program for the Exploration & Production segment includes maintenance of high production drilling rates at Urevskoye with further increase of oil output.

Timan-Pechora

The Timan-Pechora oil province accounted for 23.6% of Company production in Russia in 2010. Output by LUKOIL in the province declined slightly in comparison with 2009 to a level of 21.18 million tonnes but Timan-Pechora still has great potential. LUKOIL will develop fields using new technologies in order to speed up extraction of heavy crude oil in Timan-Pechora. Such oil represents 4.3% of the Company's total proved hydrocarbon reserves, mostly located at the Yaregskoye and Usinskoye fields in Timan-Pechora.

The **Yaregskoye field** has proved reserves of 315 million barrels of high viscosity oil under SEC classification. Production at the field mainly uses a shaft technique. Industrial testing has been underway at Yaregskoye since 2005 of new techniques for production from the surface using horizontal wells and heat applications. The work will help the Company to assess technical aspects of use of horizontal wells for injection and production purposes. The technology is similar to Steam Assisted Gravity Drainage (SAGD), which is being applied for oil sands at Atabasca in Canada. Three pairs of horizontal boreholes with horizontal sections of 250–300 meters have been drilled using this technology at Test Area № 3. Further application of SAGD techniques involve constant steam input to an upper injection hole and extraction of oil from a lower production hole. Steam condenses on the walls of a steam chamber, which forms in the strata, then flows into the production hole together with oil under the effect of gravity.

Thermo-gravitational drainage technology was used at the Lyaelskaya area of the Yaregskoye field in 2010 for drilling of three horizontal wells with 1,000 meter horizontal sections. Industrial application of thermo-gravitational drainage will enable non-draining reserves to be brought into production, increasing the overall level of oil production at the Yaregskoye field.

The highest rate of oil production growth (more than 200,000 tonnes) in Timan-Pechora was achieved at the Usinskoye and Bayadynskoye fields.

Output increase of 210,700 tonnes (+10.0%) was achieved in 2010 at the **Usinskoye field**, thanks to higher extraction volumes from a Permian-Carbonaceous deposit (+219,200 tonnes). Higher extraction from the deposit was achieved using various efficient geological interventions (steam cycles, etc.), and diversion of wells to the deposit from other geological targets at the Usinskoye field.

Two wells were transferred from drilling to production status and gave average daily flow rates of 93.1 tonnes, totalling 8,900 tonnes for the year. A further 522 wells remain to be drilled as of January 1, 2011, in accordance with the field schedule. Application of enhanced recovery techniques in future drilling will enable the Company to maintain strong results in work at the Usinskoye field.

Extensive industrial testing of steam-heat treatment is being carried out in order to improve recovery ratios from high-viscosity Permian-Carbonaceous deposits. Heat treatment of strata using a system of horizontal boreholes was applied in practice at a deposit for the first time in 2010, and testing of a perpendicular thermo-gravitational drainage technique is planned. Drilling of a new horizontal well with length up to 900 meters is scheduled, and the well will be capable of supporting steam-cycle treatment techniques.

The **Permian-Carbonaceous deposit at the Usinskoye field** was brought into operation in 1977 and its proved reserves under SEC standards as of January 1, 2011 were 434 million barrels. Structure of the Carbonaceous reservoir is discontinuous, it contains high-viscosity oil and is a natural target for heat treatment. In order to raise the recovery ratio, steam is being injected in a steam-heat process across an area of the deposit, with application of a steam cycle at several production wells, combined in some places with use of chemical reagents. Additional output from the deposit thanks to application of heat methods has totaled 6.1 million tonnes since the





operation was started. Other new technologies are also being tested at the deposit, including drilling of radial drain-holes with subsequent steam-cycle treatment, and drilling of sidetracks. Application of binary mixtures at production wells is also planned.

The highest rates of production growth in Timan-Pechora were at the **Bayandyskoye field**. Growth of output at the field in 2010 compared with 2009 was 265,500 tonnes (+123.6%). This was achieved thanks to transfer of seven wells (six production and one exploration) from drilling to production status. These wells gave average daily oil flow of 258.5 tonnes and total output of 322,000 tonnes in the reporting period. The current state of development suggests that it will be possible to produce confirmed recoverable reserves without installing a system for maintenance of strata pressure. Construction of a horizontal well with horizontal section of about 3,000 meters is planned in order to optimize the well combination at this highly productive field.

Crude oil output at the **Yuzhnaya Khylichuya field**, which was commissioned jointly with ConocoPhillips in mid-2008, was 6.9 million tonnes in 2010, which is 1.1% less than in 2009. Rapid production drilling and simultaneous launch of new production wells in 2008–2009 gave high oil-take from initial recoverable reserves, so that

stabilization was inevitable in 2010, when five wells were transferred to production status (four production wells and one exploration well), with average daily output of 806 tonnes, and five injection wells were brought into operation. Measures to regulate field operations are now being carried out. They include reinforcement of the system for strata pressure maintenance at the north-eastern part of the deposit, and increase of injection pressure at the modular cluster pump station to planned levels.

LUKOIL is working hard to ensure rapid development of Timan-Pechora's substantial reserves, which will help to compensate natural decline of output in traditional production regions.

Urals

PRODUCTION OF OIL BY LUKOIL IN THE URALS REGION INCREASED TO 12.5 MILLION TONNES IN 2010, OR BY 3.8%, THANKS TO USE OF NEW TECHNOLOGIES, SUCH AS SIDETRACKS, RADIAL DRILLING AND ACID HYDROFRACTURING. THE URALS ACCOUNTED FOR 13.9% OF TOTAL PRODUCTION BY THE COMPANY IN RUSSIA DURING 2010, COMPARED WITH A FIGURE OF 13.4% IN 2009.

Output at the Unvinskoye field grew by 6.2% in 2010 to 1.5 million tonnes. The increase was due to extensive use of new enhanced recovery methods and large-scale production drilling. Eight sidetracks were drilled and gave average daily flow of 26 tonnes, four hydrofracturing operations were carried out, giving 20.4 tonnes additional daily flow, and radial drilling technology was used at two wells (resulting average daily production growth was 7.7 tonnes). Overall production growth as a result of these measures and various traditional technologies was more than 80,000 tonnes. Two new wells were transferred to production status with average daily flow of 34.4 tonnes, including one well with a horizontal borehole.

The Unvinskoye field is one of the Company's biggest investment projects in Perm Region by size of initial oil reserves. The field has been almost completely drilled over and only fringe zones of deposits remain to be drilled.

Oil production at the **Sibirskoye field** rose by 4.5% in 2010 to 0.7 million tonnes thanks to geological work at wells and use of various techniques for enhanced recovery and production intensification. The techniques were applied at nine wells in 2010 and enabled additional extraction of 12,700 tonnes of oil. However, most of production growth in 2010 was obtained from continuation of geological interventions from 2009: a total of 18 well operations, which gave average daily output growth of 19.9 tonnes and total additional output of 58,100 tonnes. Principal techniques used at the field are acid and proppant fracturing of strata, repeat fracturing of strata at a depression and drilling of sidetracks and radial holes at wells.

The field is of average size by reserves compared with others in the region around Perm. Main geological targets at the field are Riphean sediments of the Turnei-Famenskiye stages, Terrigenous sediments in the Tulsko-Bobrikovsky horizon and Carbonaceous sediments in the Bashkirean stage. Nearly all planned wells have now been drilled.

Volga

Crude oil production by LUKOIL in the Volga region increased by 2.1% in 2010 compared with 2009 to 3.14 million tonnes. Work by the Company to improve field development efficiency in the region has led to increase of the oil recovery rate and made it possible to maintain output levels, despite considerable depletion of reserves.

LUKOIL's most important achievement in the E&P segment during 2010 was launch of production at the **Yu. Korchagin field**, where peak production levels will be about 2.5 million tonnes of oil and 1 billion cubic meters of gas.

The Yu. Korchagin field is the first to come on line of a series of fields that are being developed by the Company in the offshore Caspian. Development of these fields will be the main source of oil production growth for LUKOIL in the medium term. The Yu. Korchagin and Viktor Filanovsky fields will account for most production growth, and they are the first in order for launch. The Yu. Korchagin field development will use a system of extra-long horizontal wells (over 5,000 meters), representing a unique solution for Russia. Well logging will be carried out in the process of horizontal drilling, and radial distribution of wells will enable simultaneous penetration of all productive strata. Rates of field development slowed down in 2010 due to lower commercial drilling speed and 14% loss of calendar work time due to accidents and downtime.

Work is being carried out on production stabilization at the **Pamyatno-Sasovskoye field**, which is one of the largest in the Volga region, accounting for 77% of LUKOIL's regional output. Total additional oil production achieved by drilling of sidetracks was 67,300 tonnes, average daily flow rates were increased by 122 tonnes. Two efficient repair and insulation operations were carried out, giving average 53.5 tonnes additional daily output, and adding 30,600 tonnes of oil for the year.

INTERNATIONAL PROJECTS

LUKOIL'S SHARE OF PRODUCTION IN INTERNATIONAL PROJECTS WAS 6.255 MILLION TONNES, WHICH IS 8.3% MORE THAN IN 2009. THE GROWTH WAS MAINLY DUE TO THE TENGIZ AND NORTH BUZACHI PROJECTS IN KAZAKHSTAN, SOUTH-WEST GISSAR IN UZBEKISTAN AND SHAKH-DENIZ IN AZERBAIJAN.

Production drilling in the Company's international projects increased by 25.6% in 2010 compared with 2009 to 446,000 meters. The number of oil production wells rose by 14.2% to 1,738, of which 1,583 were actually in use. A total of 279 new production wells were commissioned as part of international projects, in which the Company is a participant.

The largest oil production increase as part of international projects came from the **Tengiz** project in **Kazakhstan**.

Crude oil production from the project (Company share) grew by 101.8% to 1,296,000 tonnes, and average daily output per well was 955 tonnes. PreFEED work was completed in 2010 for planned expansion of the Tengiz field, which will involve construction of a new oil preparation plant with 12 million tonnes annual capacity and enlargement of the gas reinjection system. The Company plans to resume drilling at Tengiz in order to load existing plant capacities and as part of the future expansion project. The rate of use of associated gas at Tengiz has been raised to 99% thanks to a series of measures, ending routine flaring of gas at the field.

The Group's share of crude oil and gas condensate production in the **Karachaganak project in Kazakhstan** was 1.5 million tonnes in 2010, almost unchanged from the previous year. Five new horizontal wells with average daily flow of 761 tonnes were brought into production during the year as part of the field investment programme.

Rapid development work continued at the **Kumkol field in Kazakhstan** during the reporting year. LUKOIL's share in crude production in this project during 2010 was 1.47 million tonnes. 71 new production wells were drilled in the reporting year and gave average daily flow of 36 tonnes.

Share of the Group in the **KarakudukMunai project in Kazakhstan** was 718,900 tonnes in 2010. In the course of the year 19 new wells were brought into operation, and gave average daily production of 18.3 tonnes. Expansion of the system for maintenance of strata pressure was completed by commissioning of two pumping units with daily capacity of 10,000 cubic meters. The central oil processing unit was modernized by assembly and activation of a compressor with capacity of 1,100 cubic meters per hour. A separator for natural gas liquids was built and brought into use.

Intensive development work continued at the **North Buzachi field in Kazakhstan**, where LUKOIL's share of production grew by 3.8% to 497,500 tonnes, and 151 new production wells were commissioned giving average daily flows of 9.7 tonnes. Five pumping stations were built in the reporting year, and work was completed on three horizontal wells and eight sidetracks.

Oil production grew by 4.3% at the **Alibekmola and Kozhasai fields** (the **Kazakhoil Aktobe project in Kazakhstan**) to a level of 244,000 tonnes. Nine new wells were brought into operation with average daily output of 57.1 tonnes, and an agreement was reached for carrying out of two pilot actions for deep treatment of strata. Construction of a system of strata pressure



maintenance was completed at the Kozhasai field, and planning and equipment sourcing was carried out for a complex gas preparation facility at the Alibekmola field and a gas preparation facility at the Kozhasai field, both as part of the project for use of associated gas.

Gas condensate production as part of the **Shakh-Deniz** project in **Azerbaijan** rose by 7.3%, to 149,300 tonnes in response to growth of demand in Azerbaijan and from Turkish consumers. Four wells were in operation during 2010. Gas was supplied through the South-Caucasus pipeline to Azerbaijan, Georgia and Turkey. Condensate was shipped via the Baku-Tbilisi-Ceyhan pipeline.

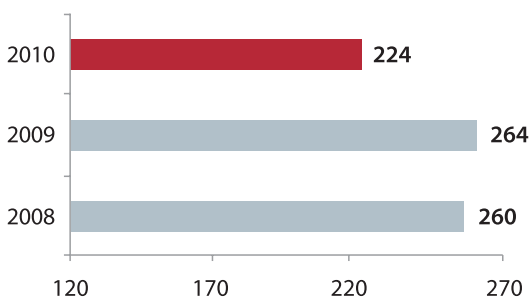
The Company's share of gas condensate production at the **Khauzak-Shady** area in **Uzbekistan** (developed as part of the Kandym-Khauzak-Shady project), which was commissioned in 2007, was 10,400 tonnes in 2010. One new production well was commissioned in the course of the year and gave daily flow of 2.8 tonnes of condensate. A tendering competition was announced for design and construction of a booster compressor station.

LUKOIL's share of production at the **South-West Gissar project** in **Uzbekistan**, which was acquired in 2008,

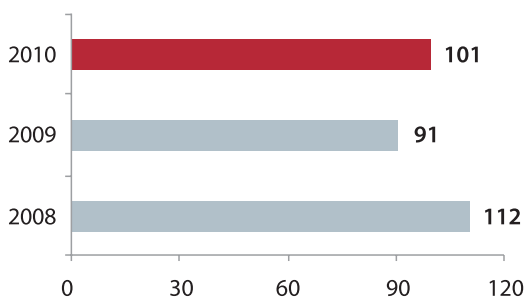
grew by a substantial 131% in 2010 compared with 2009 to 87,900 tonnes. Four new production wells were brought into operation during the reporting year and gave average daily output of 47.7 tonnes. A contract and agreement was made concerning supply of technical documentation and equipment for the Adamtash, Gumbulak, and Djarkuduk-Yangi-Kizilcha gas condensate fields in the Republic of Uzbekistan.

The Group's share in the **Meleiha project** in **Egypt** was 12.6% less in 2010 than in 2009 and amounted to 69,000 tonnes, despite overall growth of project output. This was due to reduction of LUKOIL's production share from 9.57% to 7.35% resulting from increase of Brent prices and 18% reduction of capital expenditures in 2010 to \$19.3 million. Lower investments were due to change in the construction schedule of the project operator, Agiba Petroleum, which delayed construction of vent lines to the new wells (part of the loss-reduction project) and construction of burial facilities for radioactive waste until 2011. A further 16 wells with average daily output of 34.9 tonnes were brought into operation in 2010.

■ DRILLING OF SIDETRACKS, sidetracks

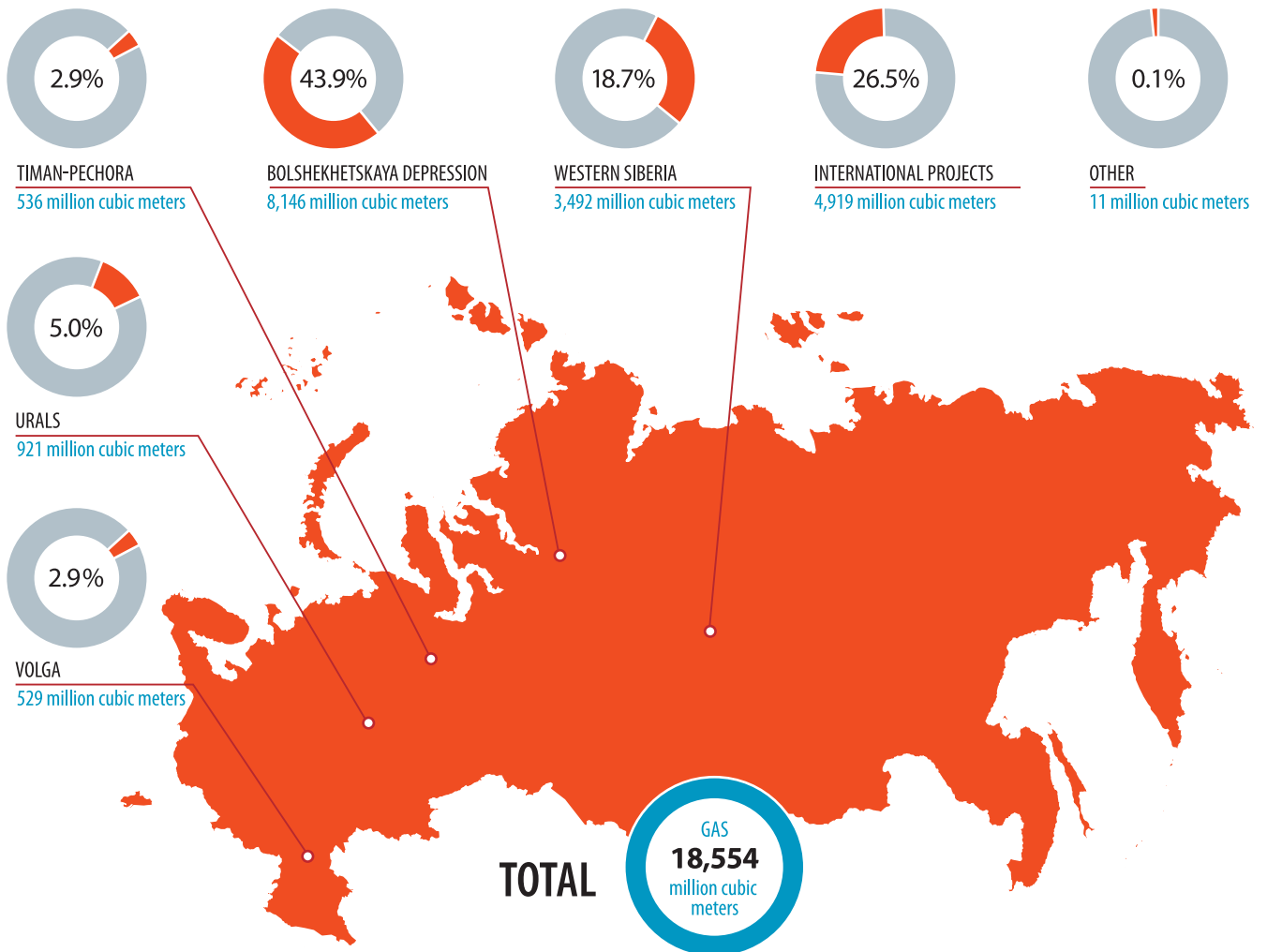


■ DRILLING OF HORIZONTAL WELLS, wells



GAS FIELD DEVELOPMENT AND GAS PRODUCTION

LUKOIL GROUP MARKETABLE GAS PRODUCTION BY REGIONS



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.

Total gas production by LUKOIL Group in 2010 (including the share of production by equity affiliates) rose by 20.4% to 21.328 billion cubic meters (344,000 boe per day). Output of marketable gas (net of own use, reinjection into reservoir formations and transport losses) rose by 24.5% to 18.554 billion cubic meters (299,000 boe per day), and the increase in Russia alone was 27.9%. Significant growth of marketable gas output was possible thanks to growth of purchases by Gazprom, due to increase of demand in Europe and the effect of a low base in 2009. European spot prices for gas rose sharply at the end of 2010 in the context of high oil prices, industrial recovery after the recession and severe weather conditions on the continent. As a result Company revenue from sales of natural gas increased by 46.2% in 2010 compared with 2009 to a level of \$835 million.

Most of the output growth was provided by the Nakhodkinskoye field, where production of marketable gas rose by 37.2% in 2010 to 8.146 billion cubic meters. All of this gas was sold to Gazprom. We also increased rates of associated gas use in Western Siberia. **Net income of LUKOIL Group in 2010 from gas projects in Russia was \$116 million, which is 107.1% more than in 2009.**

The Company was operating 397 gas wells at the end of 2010, of which 286 were in production.

Natural gas output rose by 21.8% to 13.936 billion cubic meters in 2010, of which 12.770 billion cubic meters was marketable gas. Increase in output of marketable gas was 25.0%.

Production of associated gas rose by 17.8% to 7.392 billion cubic meters, of which 5.784 billion cubic meters was marketable associated gas. Increase in marketable associated gas production was 23.6%. Growth in production of marketable associated gas was due to 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.

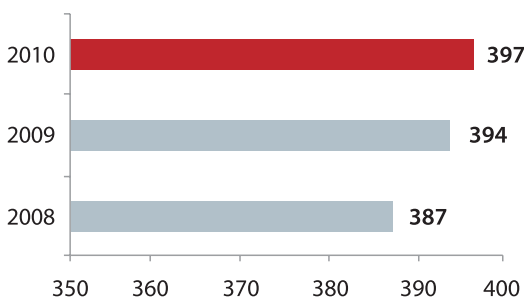
The Company has been increasing the share of associated gas, which it puts to use, year by year and the share reached 76.8% in 2010 compared with 71.1% in 2009 and 70.4% in 2008. The increase has been made possible by development of systems for utilization of associated gas at Company fields, including construction of compressor stations and gas pipelines. The level of utilization of associated gas at main Company fields in Western Siberia is now more than 95%.

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.

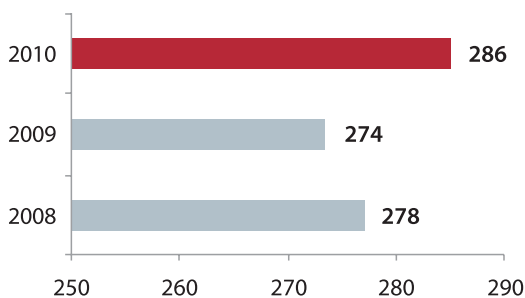
RUSSIA

Production of marketable gas in Russia in 2010 was 13.635 billion cubic meters, which is 27.9% more than in 2009.

■ GAS PRODUCTION WELLS, wells



■ GAS PRODUCTION WELLS IN USE, wells



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



The Company had 306 gas production wells in Russia at the end of 2010, of which 213 were actually in use.

Most of the Company's natural gas production in 2010 in Russia (more than 90%) came from the **Nakhodkinskoye field in the Bolshekhetskaya Depression**. Gas production there in 2010 was 8.2 billion cubic meters, which is 37.1% more than in 2009, reflecting increase of gas purchase volumes by Gazprom.

Scheduled work is being carried out at the field for modernization of low-temperature gas separation technologies in order to raise strata pressure in the complex gas preparation unit. Four turbodetander aggregates were brought into operation in a first stage of this work in 2010, and the second stage will involve installation of a booster compressor station, design of which began at the end of 2010. Completion of these tasks will ensure stability in production, preparation and transport of gas from the Nakhodkinskoye field.

Design work was completed in 2010 for the main compressor station in a gas transport system to serve fields in the Bolshekhetskaya Depression in the region of Nakhodkinskoye. Tendering competitions have been carried out and agreements have been made for construction of the station, and for design, manufacture, delivery, assembly and testing & commissioning of gas

pumping aggregates as well as ancillary equipment. Commissioning of the first part of the main compressor station is scheduled for the end of 2012.

LUKOIL began drilling work at gas condensate deposits at the **Pyakyakhinskoye field** in 2009. Two drilling rigs have been deployed at the field, the first section of a gas turbine power station was brought into operation in July, 10-kilowatt aerial transmission cables were installed to carry power to two drilling pads, and a well was drilled to provide gas for energy generation. There were eight wells at the field at the start of 2011: seven wells are suspended, and one well provides gas for an energy generation unit.

The plan for development of the Pyakyakhinskoye field was adjusted in 2010 based on results of geological work and production drilling, and on decisions that were taken for optimization of well performance.

LUKOIL has reached an agreement with OJSC Rosneft, by which the Company will accept 5.6 billion cubic meters of gas each year starting in 2013 from the Vankor field to be fed into the gas transport system serving the Bolshekhetskaya Depression in the region of the Khalmerpayutinskoye field and transport it to the Yamburgskaya gas compression station on Gazprom's Unified Gas Supply System. Construction of pipelines

from Khalmerpayutinskoye to Pyakyakhinskoye and from Pyakyakhinskoye to Nakhodkinskoye are scheduled for completion in 2013. Tenders have been carried out for purchases of pipes and pressure regulating equipment, and contactors for construction of the gas transport system have been selected.

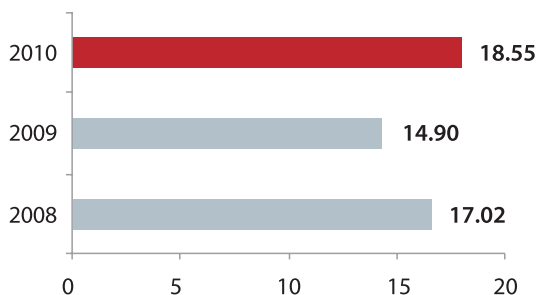
In return, Rosneft guarantees to accept up to 3 million tonnes per year of stabilized oil and condensate to be fed into the Vankor-Purpe pipeline for transport to the Transneft trunk pipeline system. However, LUKOIL has decided to use the Zapolyarye-Purpe pipeline (owned by Transneft) in preference to the Vankor route for liquid hydrocarbons, so construction of the Pyakyakhinskoye field and start of production have been synchronized with planned launch of the Zapolyarye-Purpe pipeline, which will pass across the Pyakyakhinskoye field.

When all fields in the Bolshekhetskaya Depression reach planned production levels, the Company's total output of natural gas in the region will be 20 billion cubic meters.

INTERNATIONAL PROJECTS

Production of marketable gas in 2010 as part of international projects rose by 16.2% to 4.919 billion cubic meters. The share of natural gas was 86%, representing a decline of 6 percentage points. The Company had 91 gas production wells in international projects at the end of 2010, of which 73 were actually in use.

MARKETABLE GAS PRODUCTION, billion cubic meters



Most of marketable gas production outside Russia (54%) 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 rose by 19.2% to 2.66 billion cubic meters in 2010. Production drilling at the area continued in 2010, and one new well was commissioned giving average additional daily gas flow of 356.2 cubic meters. Intensive work is also underway in **Uzbekistan** on drilling of gas wells at the Adamtash field as part of the Gissar project, where four new production wells were launched with average daily flow of 59,000 cubic meters. Full-scale production of natural gas is due to start at Adamtash in 2012.

The Company's share of gas output in the **Tengiz project** increased by a record 112% in 2010 to 568.4 million cubic meters. Completion of a project for utilization of associated gas raised the usage rate to 99%, and routine gas flaring is no longer carried out.

Marketable gas production in 2010 at the **Shakh-Deniz project in Azerbaijan**, which was brought into production in December 2006, was 545 million cubic meters (Company share), which is 5.2% more than in 2009, reflecting growth of consumer demand. Agreement was reached in 2010 between Azerbaijan and Turkey on price increase for first-stage gas from Shakh-Deniz. Agreement was also reached between Azerbaijan and its partners on extension of the project PSA for a further five years.



2

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

■ MAIN INDICATORS FOR LUKOIL'S REFINING & MARKETING BUSINESS

Indicator	2010	2009	Growth, %
Revenue, \$ million	99,976	77,434	29.1
EBITDA, \$ million	5,934	5,225	13.6
Net income, \$ million	2,934	2,263	29.7
Capital expenditures, \$ million	1,320	1,316	0.3

COMPANY RESULTS IN THE REFINING & MARKETING SEGMENT WERE IMPRESSIVE IN 2010: SEGMENT NET INCOME ROSE BY 29.7% TO \$2.934 BILLION.

The strong improvement of net income reflected recovery of demand and profitability of refining business as the world economy emerged from the financial crisis. LUKOIL pursued work in 2010 to develop its oil refining business through modernization and expansion of refining capacities.

rose by 28% (FOB Rotterdam), and prices for high-octane gasoline were 27% higher. The domestic market for petroleum products also saw price growth: boiler fuel oil was 51.3% more expensive and prices for AI-95 gasoline rose by 16.8%.

Refining of oil and petroleum products by the Company, including volumes at third-party refineries, totaled 66.29 million tonnes in 2010, of which volumes at Group refineries (including LUKOIL's share of ISAB and TRN) were 66.18 million tonnes (5.6% more than in 2009).

PRICE AND TAX ENVIRONMENT

Growth of the world economy led to gradual recovery in demand for petroleum products during 2010, and there was substantial price growth both domestically and on export markets. The external price environment was of greatest importance for LUKOIL since the Company sold 83% of its petroleum products outside Russia in the reporting year. Average prices for fuel oil in Europe

LUKOIL Group has five refineries outside Russia, which reduces risks associated with a single geographical region, and gives opportunities to take advantage of more favourable tax regimes in other countries. Many European countries provide attractive tax regimes for companies with operations on their territories.

This applies particularly to the TRN Refinery in the Netherlands, where the Government has consistently lowered corporate income tax rates over the last five

years despite problems in the global economy: rates have come down from 29.6% in 2006 to 25% in 2011. Also the mechanism for calculation of TRN's tax base is enshrined in a special agreement with the Dutch tax authorities. This makes TRN's tax position stable and predictable. The effective tax rate for TRN in 2010 was 21.7%.

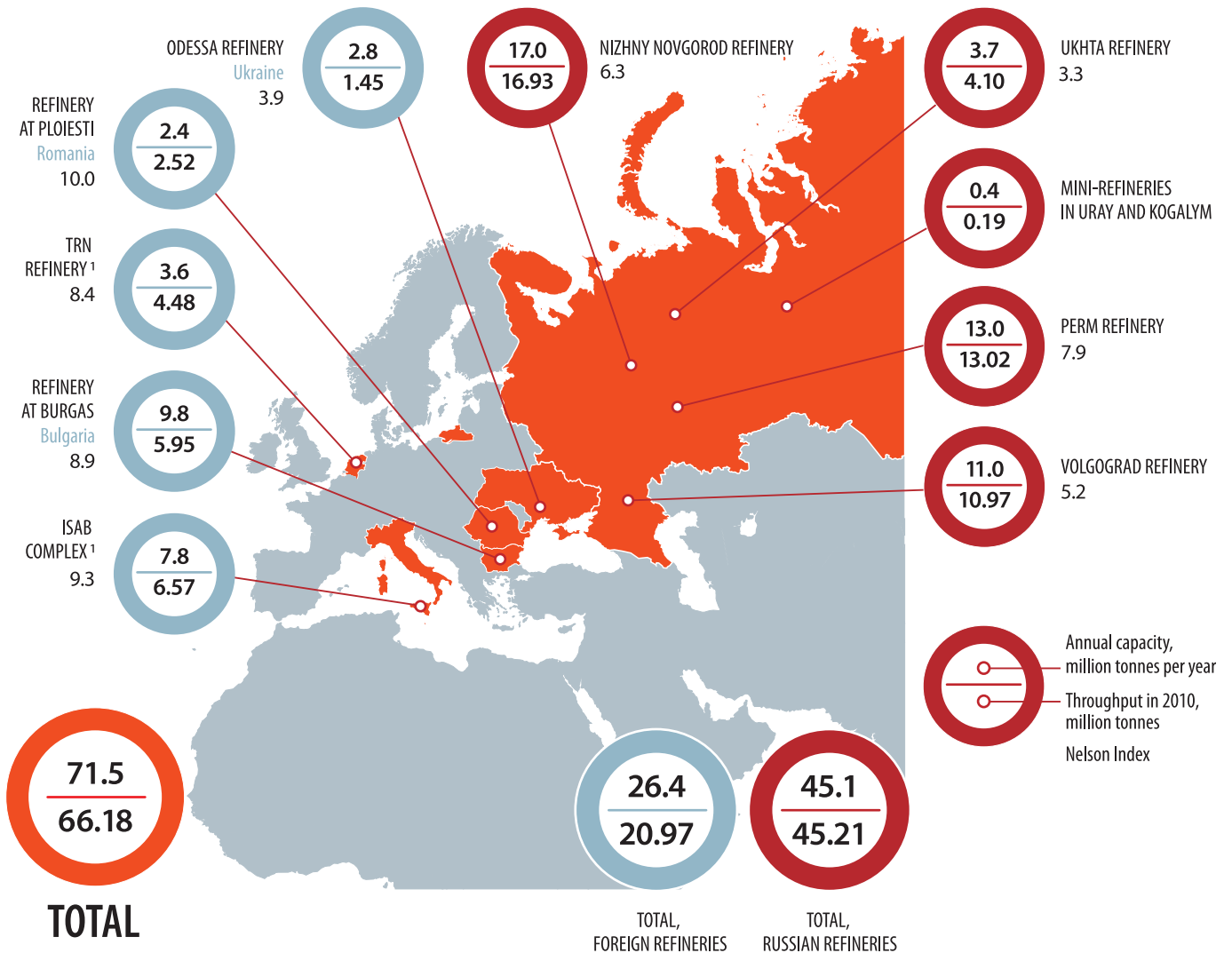
The ISAB Refinery is one of the biggest tax payers in its region. The Italian Government has brought in a number of tax measures since 2009, which are designed to

encourage fixed asset investment and reduce unemployment, and which have reduced the tax burden for the ISAB Refinery. Nevertheless the effective rate of tax paid by ISAB was 44% in 2010, which exceeds the level at other LUKOIL refineries. This was due to additional income tax, charged at 6.5%, and a special 16% tax on revaluation of inventories. Revenues from the latter tax are earmarked for income support to poor families, and it is levied on all companies in the Italian oil & gas sector.



OIL REFINING

LUKOIL GROUP REFINERIES



¹ Capacities of the ISAB and TRN refineries are shown as the Company share (49% and 45%, respectively).

NEW CATALYTIC CRACKING COMPLEX AT THE NIZHNY NOVGOROD REFINERY

REFINERY DESCRIPTION:

- The Refinery produces fuels and lubricants
- Located in the town of Kstovo in Nizhny Novgorod region
- Refines a blend of West Siberian oils and Tatarstan oils
- Crude oil is supplied to the Refinery via the Almeteyevsk — Nizhny Novgorod and Surgut — Polotsk pipelines
- Petroleum products are shipped by rail, road and river transport and by pipeline
- Capacity — 17.0 mln tons per year
- Nelson index — 6.3
- Main conversion process is visbreaking (42,200 barrels per day)

A new catalytic cracking complex was brought into operation at the Nizhny Novgorod refinery in 2010, and it is already producing Euro-4 gasoline. It is the largest catalytic cracking complex built in Russian for the last 25 years. Due to conversion of vacuum gas oil into light products the complex substantially increases the production of gasoline in the Central region. Project investments were about \$1 billion.

The new complex will increase total annual gasoline output at the Refinery from 1.8 to 3.2 million tonnes, and output of diesel fuel will be raised from 4.2 to 4.6 million tonnes. The complex can also produce 150,000 tonnes of propylene each year.

The new complex consists of five main units, as follows (figures are annual capacity):

- a vacuum gasoil hydrotreatment unit (2.5 million tonnes)
- a catalytic cracking unit (2 million tonnes) with a propylene concentration unit (150,000 tonnes of propylene)
- alkylation with blocks for isomerization of normal butanes and selective hydration of diene hydrocarbons. Alkylate capacity is 360,000 tonnes
- hydrogen production (40,000 tonnes)
- elemental sulphur production (130,000 tonnes)

The complex also comprises five infrastructure facilities: a sulphur granulation and shipment shop, a boiler water preparation unit, a water circulation block, flaring equipment, and inter-unit communications.

The production chain begins from the hydro-treatment unit, which is fed with vacuum gasoil from the primary refining facilities. Nitrogen and sulphur compounds are removed from the straight-run vacuum gasoil by application of hydrogen.

The output from this process — gasoil low in sulphur compounds — is sent to the catalytic cracking unit, where it is passed through a reactor, which converts heavy hydrocarbons into lighter ones at a high temperature in the presence of a catalyst.

The main outputs from catalytic cracking are gasoline fractions (53% of total outputs, with octane number of 92 or above), and propylene and butane-butylene fractions, which are sent to the alkylation unit to produce another gasoline alkylate component, with octane number of 95, free of sulphur compounds and aromatics. Sulphur is processed in the elemental sulphur unit.

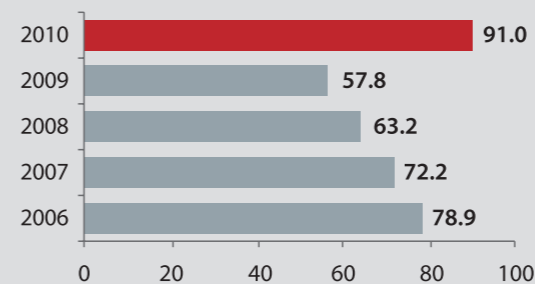
Marketable gasoline is produced in a constant flow at a blending facility, after which it is quality-tested and given a product passport, ready for delivery to customers.

An alkylation unit will be brought into operation at the Nizhny Novgorod Refinery in 2011, which will enable production of automotive gasoline to Euro-5 standards. Aromatic content in gasoline produced on the new equipment is no higher than 35%, maximum content of sulphur in class-4 fuel is 50 mg per kg, and 10 mg per kg in class-5 fuel. This gasoline ensures 'clean exhaust', minimizing sulphur oxide and products of incomplete aromatics combustion, including the highly carcinogenic and mutagenic benzopyrene.

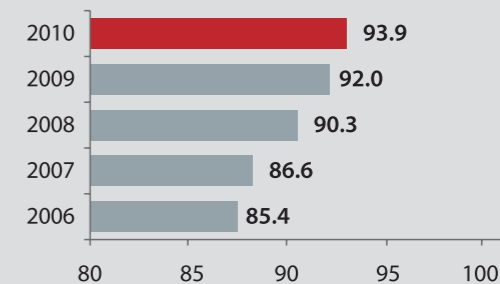
European Standards on Nizhny Novgorod Refinery

	2005	2006	2007	2008	2009	2010	2011
Gasoline		Euro-3	Euro-3	Euro-3	Euro-4	Euro-4	Euro-5
Diesel fuel	Euro-4	Euro-5	Euro-5	Euro-5	Euro-5	Euro-5	Euro-5

SHARE OF CLEAN DIESEL IN TOTAL OUTPUT OF DIESEL FUEL, %



SHARE OF HIGH-OCTANE GASOLINE IN TOTAL OUTPUT OF MOTOR GASOLINE, %



LUKOIL GROUP CONTINUED RAPID DEVELOPMENT OF ITS OIL REFINING BUSINESS IN 2010 THROUGH MODERNIZATION AND EXPANSION OF REFINING CAPACITIES.

THE VOLUME OF REFINERY THROUGHPUTS, INCLUDING PROCESSING AT THIRD-PARTY REFINERIES, WAS 66.29 MILLION TONNES IN 2010, OF WHICH 66.18 MILLION TONNES WERE REFINED AT GROUP REFINERIES (INCLUDING COMPANY SHARES OF REFINING AT THE ISAB AND TRN COMPLEXES), REPRESENTING AN INCREASE OF 5.6% OVER 2009.

Capital expenditures by LUKOIL on its refinery business in Russia and abroad were \$702 million in 2010 (the figure in 2009 was \$828 million).

The Group raised operating efficiency of its refineries in 2010 through measures 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 these measures was about \$208 million. The largest positive effect was at the Perm, Nizhny Novgorod, and Ukhta refineries (\$85 million).

Russian refineries

Crude oil throughput at Russian refineries in ownership of LUKOIL Group was 45.21 million tonnes in 2010, which is 1.7% more than in 2009. The share of high-octane gasoline in total output of gasoline at Group refineries in Russia (not including mini-refineries) rose to 91.5% in 2010 (from 89.7% in 2009). Light-product yield was 48.5%, down slightly from the previous year due to reduction in the amount of light fractions in refined oil and unscheduled downtime of hydrocracking facilities at the Perm Refinery.

Measures were implemented during the reporting year to reduce operating costs and raise production efficiency at Russian refineries. This enabled reduction of irretrievable losses at refineries from 0.51% to 0.47%. Average personnel numbers at Russian refineries were reduced by 2.0%. Capital expenditures at Company refineries in Russia were \$542 million in the reporting year (against \$520 million in 2010).

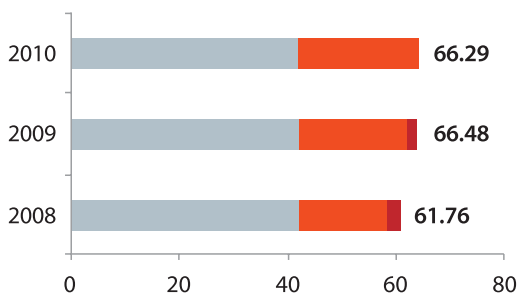
At the **Ukhta Refinery** test operation of the AT-1 distillation unit confirmed increase of light-oil refining by 10%. The rectification tube on the vacuum column of the atmospheric-vacuum distillation unit was replaced, and test operation confirmed 6% increase in production of diesel fraction from heavy crude oil supplied from the Yaregskoye field.

The new catalytic cracking complex at the **Nizhny Novgorod Refinery** was commissioned in 2010. The complex will increase annual output of high-octane automotive gasoline at the Refinery by 1.4 million tonnes and of diesel fuel by 400,000 tonnes, raising light product output by 12%. All of the gasoline produced will meet the standards of Euro-4 and Euro-5. The new complex raises the Nelson Complexity Index score at Nizhny Novgorod by 2.3 points. Reconstruction of the diesel hydrotreatment unit (completed in December 2009) has substantially increased output of diesel fuel that meets Euro-5 standards.

A new absorption and gas fractionation unit has been commissioned at the Refinery, which enables production of propane-butane fractions, providing inputs for the alkylation unit and for production of hydrogen in the catalytic cracking complex.

The **Volgograd Refinery** completed construction of a short-cycle absorption unit in 2010 to produce concentrated hydrogen for the needs of fuel hydrotreatment

REFINERY THROUGHPUTS BY LUKOIL, million tonnes



■ At third-party refineries	5.48	3.78	0.11
■ At the Company's foreign refineries	12.10	18.24	20.97
■ At the Company's refineries in Russia	44.18	44.46	45.21
Total	61.76	66.48	66.29

units. The heat exchanger on the diesel hydrotreatment units was modernized, increasing unit capacity by 8%. A production system was created for low-sulphur bunker fuel, providing supplies for development of LUKOIL's bunkering business.

Construction of a second section of the diesel hydrotreatment unit and modernization of coke production are currently in progress at the Refinery.

The **Perm Refinery** continued upgrading work on existing coke production facilities in 2010. The upgrade will reduce energy needs in coke production and enable launch of a new product: a coking additive for the metallurgy industry.

Foreign refineries

Refinery throughputs in 2010 at LUKOIL Group's international refineries, including the Group share of refining at the ISAB and TRN complexes, were 20.97 million tonnes, which is 14.9% more than in 2009, and met the Company's business targets based on levels of market demand. Production at Group own and third-party refineries increased by 16.9 compared to 2009 as a result of acquisition of the TRN refinery in September 2009. The production at our Bulgarian and Ukrainian refineries was lower due to performed overhauls.

Light product yield (not including ISAB and TRN) was 66.0% (up from 65.3% in 2009). Irretrievable losses at refineries outside Russia fell from 0.85% in 2009 to 0.64% in 2010.

Capital expenditures in modernization of the Group's foreign refineries were \$160 million in 2010 (\$308 million in 2009).

During the reporting year the **Burgas Refinery** started to operate a hydrotreatment unit for diesel and gasoline produced by catalytic cracking, enabling 100% output of diesel fuel and gasoline that meets Euro-5 standards.

The vacuum generating system for primary refining facilities at Burgas was also upgraded in 2010, which substantially improved quality of dark-product separation and improved the output balance between vacuum gasoil and boil fuel oil in favour of the former. A waste-heat boiler was installed on the primary refining unit, which will significantly reduce energy use in primary refining and create energy for refinery processes.

Design work on a heavy-residue processing complex was begun in 2010. Construction of the complex should be completed in 2015.

The **Ploiesti Refinery (Romania)** installed two coke chambers on the delayed coking facility in 2010 as part



of a program to improve reliability, and also completed work on a system to heat buildings at the Refinery using heat generated from refining processes, which will raise energy efficiency and lower operating costs.

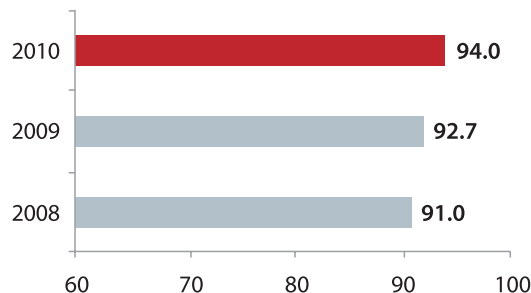
The **Odessa Refinery** completed construction of a gasoline blending facility, which will raise efficiency in production of marketable gasoline. The Refinery was stopped in the fourth quarter of 2010 due to unfavourable economic conditions in Ukraine.

The LUKOIL share in refinery throughput at the **ISAB Refining Complex** (Sicily, Italy), in which the Group bought a 49% stake in 2008, was 6.57 million tonnes in 2010.

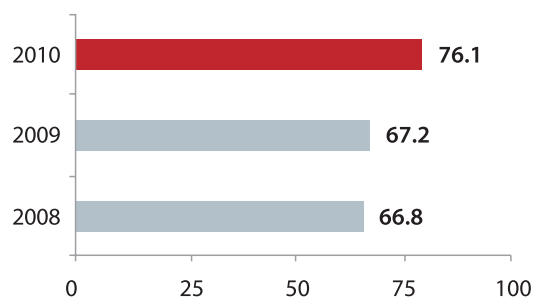
In September 2009 the Group began refining of oil at the **TRN Refinery** in the Netherlands after completing a transaction for acquisition of a 45% stake. The Group share in refining of oil and petroleum products at TRN was 4.48 million tonnes in 2010.



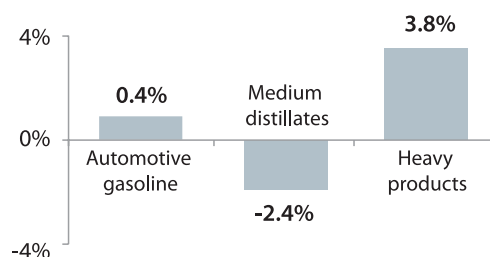
■ SHARE OF HIGH-OCTANE GASOLINE IN TOTAL GASOLINE PRODUCTION, %¹



■ SHARE OF DIESEL FUEL WITH SULPHUR CONTENT BELOW 50 PPM IN TOTAL DIESEL PRODUCTION, %¹



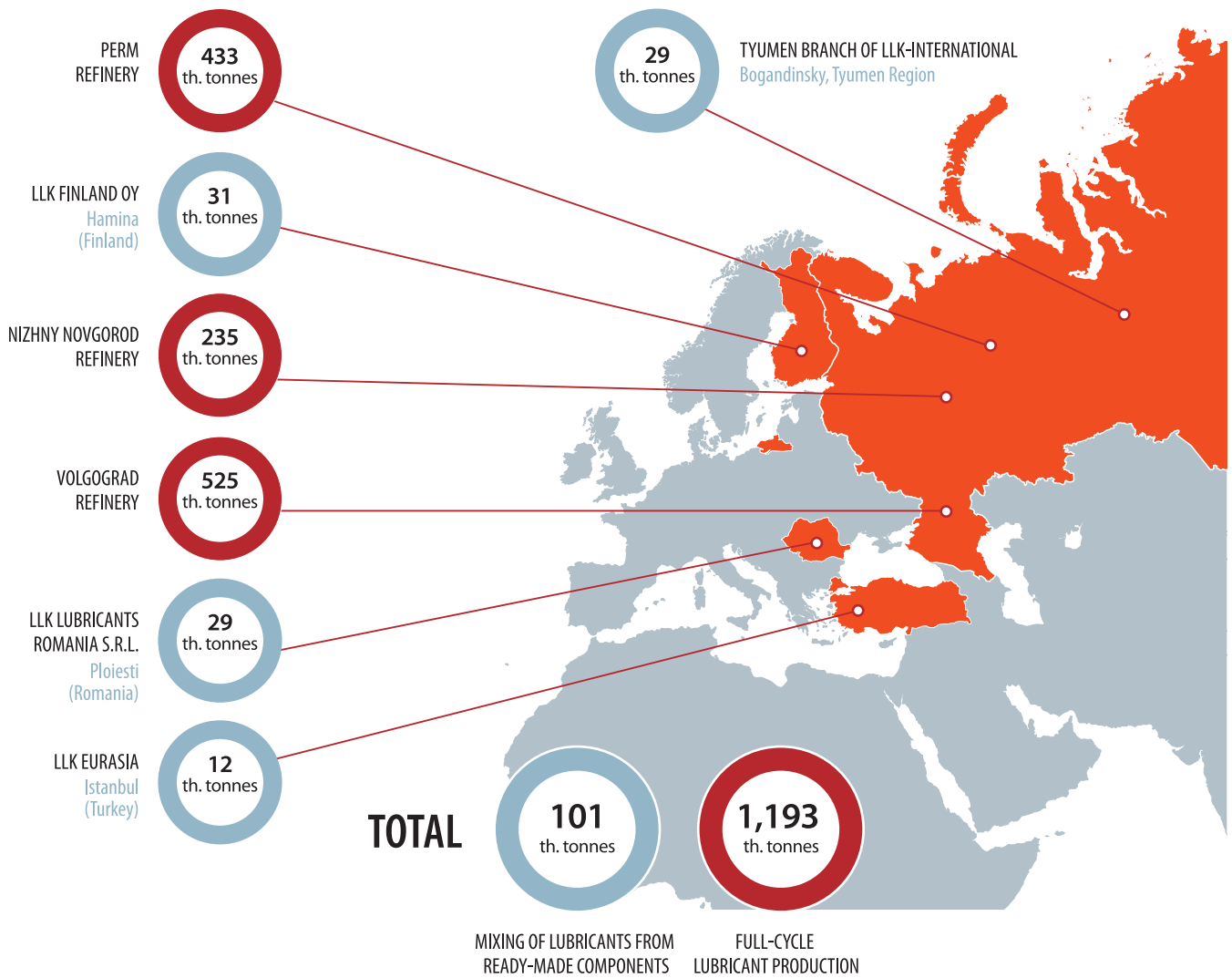
■ CHANGE IN OUTPUT LEVELS OF PETROLEUM PRODUCTS AT COMPANY REFINERIES IN 2010 COMPARED WITH 2009, %¹



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

PRODUCTION OF LUBRICANTS

LUBRICANT PRODUCTION AT LUKOIL GROUP REFINERIES





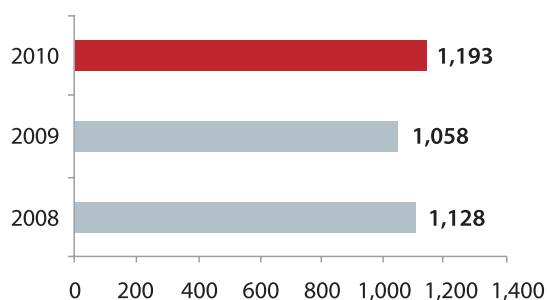
Production and sale of lubricants is an important part of LUKOIL's business. The Group is constantly improving the quality of products and expanding their range, as well as raising efficiency of the sales system and diversifying business geography.

LUKOIL is the leader on the Russian lubricants market, accounting for about 44% of domestic production. Lubricants are produced at Group refineries in Perm,

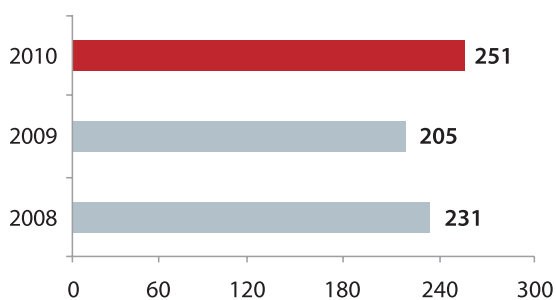
Volgograd and Nizhny Novgorod. The Company also mixes lubricants from ready-made components (both produced by the Company and bought from third parties) at facilities in Russia, Finland, Romania and Turkey.

Group refineries produced 1.19 million tonnes of lubricants in 2010, and lubricant mixing volumes were 101,000 tonnes. Output of packaged oils was 251,000 tonnes (205,000 tonnes in 2009).

■ LUBRICANT PRODUCTION AT COMPANY REFINERIES, thousand tonnes



■ PRODUCTION OF PACKAGED LUBRICANTS, thousand tonnes



LUKOIL PRODUCED 230 DIFFERENT OILS AND LUBRICANTS AND OTHER NON-FUEL AUTOMOTIVE CHEMICALS AT ITS RUSSIAN PLANTS IN 2010. 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.

The Group continued its efforts in 2010 to improve efficiency in sales of lubricants, including further development of an import substitution program. A full-time arrangement was put in place as part of the program for deliveries of lubricants to the coal mining company, OJSC Kuzbassrazrezugol, enabling LLK-International to make an agreement for 2011 and remain the sole supplier to this customer. Deliveries began to OJSC Metalloinvest and OJSC Mechel, and agreements were reached on starting cooperation with GMK Norilsk Nickel.

Sales by the Group of automotive chemicals were systematized in 2010: LLK Engineering took 2–3% market share and a place in the Top-10 automotive chemical brands in Russia.

LLK-NAFTAN, the joint venture between LUKOIL and the Naftan refinery (Belarus), met 46% of LUKOIL's requirements for additives used in lubricant production in 2010. The JV has increased output by almost seven times, from 3,000 to 20,000 tonnes, since its creation in 2006.

The Company carries out sales of lubricants in more than 40 countries worldwide and sales geography is constantly expanding. In 2010 LUKOIL began lubricant

sales in India, Bangladesh, Iraq, and several countries in North Africa and the Middle East.

The Company further expanded its lubricant sales in Turkey in 2010, making a contract for supplies to the service network of the automotive manufacturing group, Chelik Motors (assembly and sales of Honda, Isuzu, Kia, Lada, and Geely vehicles).

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 229,000 tonnes in 2010, which is 45% more than in 2009.

An important breakthrough in 2010 was design and application of a system for changeover of ship engines to LUKOIL NAVIGO lubricants without the need to wait for a scheduled oil change, which involves financial loss for the ship owner. The Company also cooperated with a British company, Seatec, to design and deploy a global service for technical support and analysis of LUKOIL NAVIGO lubricants. Approvals have been obtained from more than 80% of the world's ship engine manufacturers (including MAN, B&W, Sulzer, Wartsila and MAK). The Company's ship lubricants were available in 499 ports in more than 55 countries worldwide by the end of 2010.

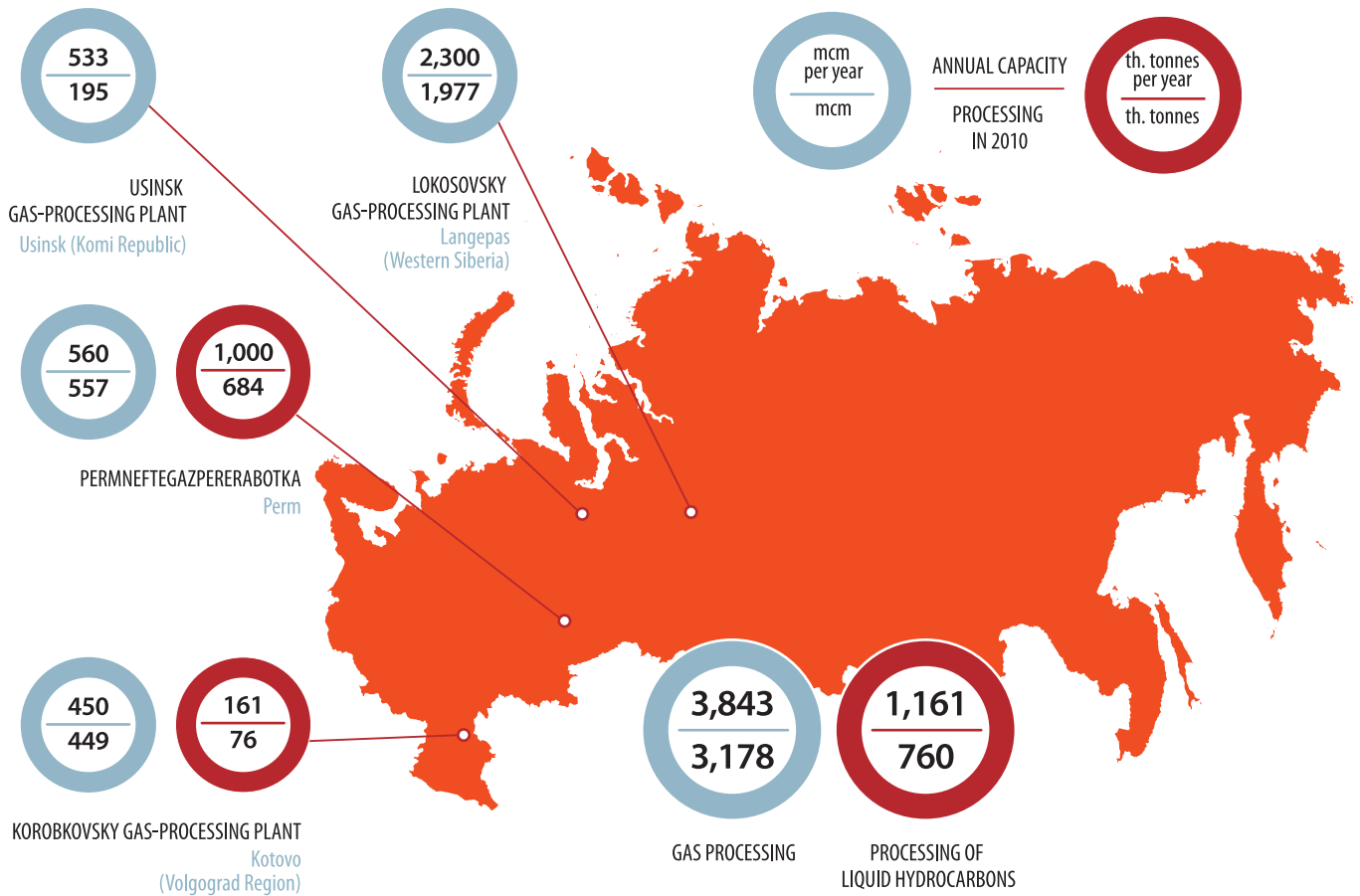
The Company has done much work to develop customer relations in its lubricant business. LUKOIL was among the first companies in the industry to offer comprehensive service with full product support, from placement of client orders to delivery of the product and final disposal of used lubricants.

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. A total of 40 new lubricant products were brought into production in 2010 and 144 manufacturer approvals were obtained.

GAS PROCESSING

GAS-PROCESSING PLANTS OF LUKOIL GROUP



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.

IN 2010 THE COMPANY'S GAS-PROCESSING PLANTS PROCESSED 3.178 BILLION CUBIC METERS OF GAS FEEDSTOCK AND 760,000 TONNES OF NATURAL GAS LIQUIDS (7% AND 6% MORE THAN IN 2009, RESPECTIVELY). THE INCREASE WAS DUE TO HIGHER DEMAND FOR PRODUCTS.

During 2010 company plants produced 2.471 billion cubic meters of stripped gas, 846,000 tonnes of liquefied gas and 889,000 tonnes of liquid hydrocarbons (stable gas naphtha, isopentane and hexane-heptane fractions, and natural gas liquids).

Work continued 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 meters.

Work was carried out at **Permneftegazpererabotka** to identify pipeline sections in need of replacement, which are located adjacent to residential areas, water crossings, railways and roads. Installation work was completed on a stenching unit for propane-butane mixtures.

Work in 2010 on safety systems at the **Lokosovsky Gas-processing Plant** included installation of a gas discharge pipe, modernization of flaring equipment, and modernization of fire and accident systems.

No major modernization work was carried out at the **Korobkovsky Gas-processing Plant**. However, a long-term program of measures was designed and approved to keep the Plant in working order and ensure operating safety.



PETROCHEMICALS

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

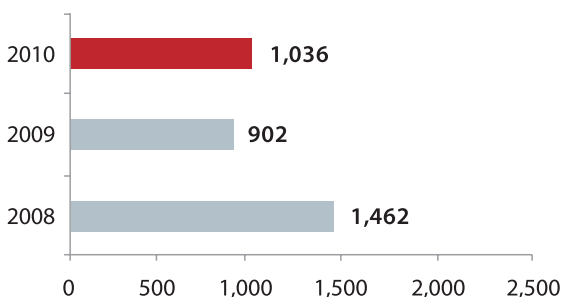


LUKOIL's petrochemical business is one of the biggest in Russia, CIS and Eastern Europe. Company plants in Russia, Ukraine and Bulgaria make pyrolysis and organic synthesis products, fuel fractions and polymer materials. LUKOIL meets a major share of Russian domestic demand for various chemicals and 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 1,036,000 tonnes of petrochemicals in 2010, which is 14.9% more than in 2009. The increase was due to the launch of production at Karpatneftekhim in September 2010 as well as increase of demand for petroleum products.

■ PETROCHEMICAL PRODUCTION, thousand tonnes



Demand for petrochemical products recovered in 2010, as did prices. The sale price for polyethylene in Russia rose by 15.6%, for polypropylene by 41.7%, and for benzol by 58.4%. Prices for all three products also rose in Europe, by 25.3% for polyethylene, 37.5% for polypropylene and 37.8% for benzol.

LUKOIL took further measures for modernization of existing production and installation of new facilities in 2010 as part of its strategy for development in the petrochemical sector. Capital expenditures in the sector were \$76 million in 2010, which is 33% less than in 2009.

Operations were resumed in September 2010 at Karpatneftekhim after completion of a new chlorine and caustic soda production unit with 200,000 tonnes annual capacity. Annual capacity of the new unit is 182,000 tonnes of gaseous chlorine and 200,000 tonnes of caustic soda. Completion of the project enables Karpatneftekhim to produce caustic soda, which meets international quality standards, and to fully cover the plant's own chlorine needs.

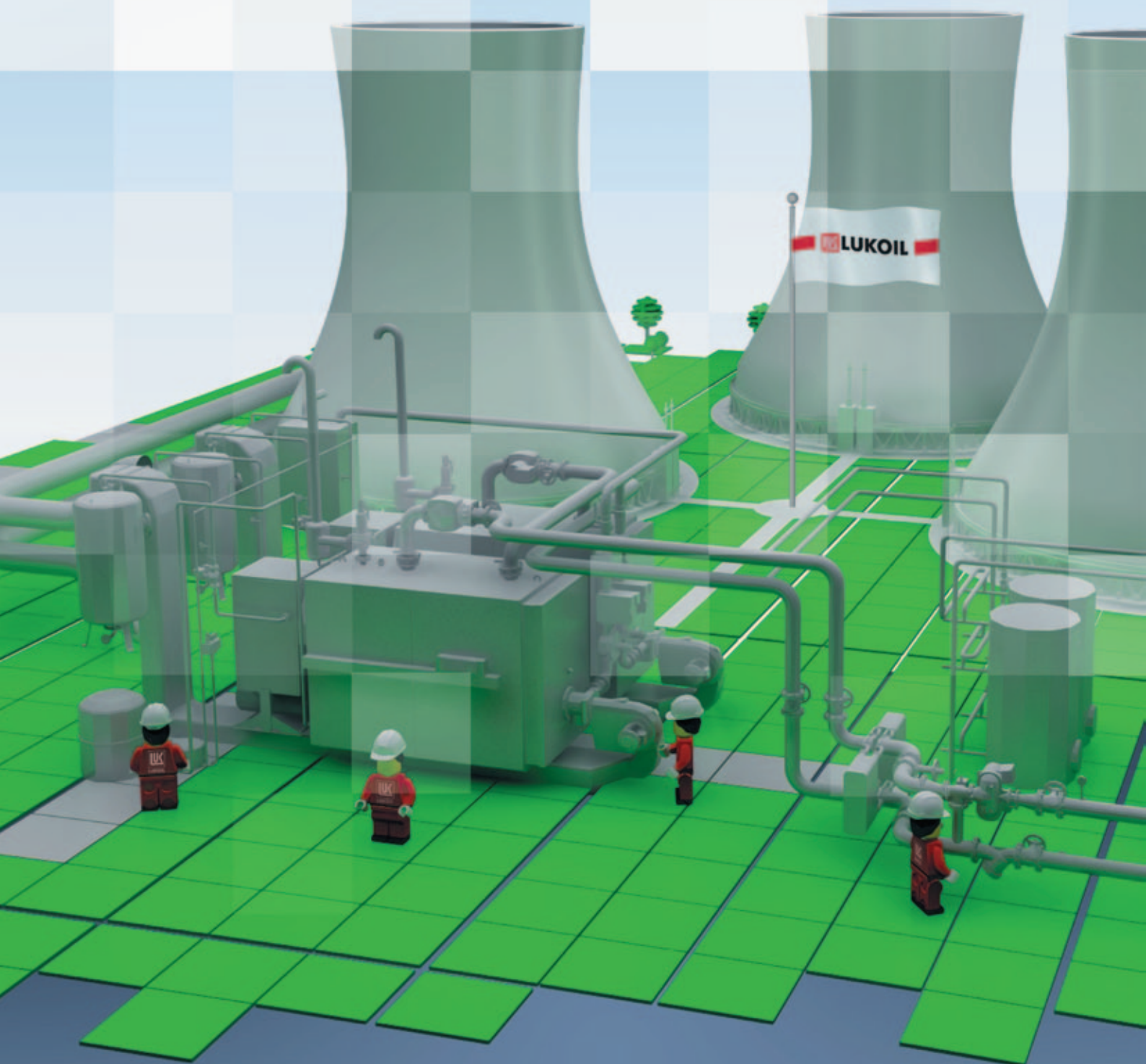
It was decided in 2010 to include a commercial project for expansion of sodium cyanide production to 18,000 tonnes per year in the investment program for Saratovorgsintez. The existing unit was inspected and changes were made to current technical documentation. Equipment delivery and assembly work is due to be carried out in 2011.

Work was completed at Stavrolen for installation and launch of a polyethylene compounding line. The Stavrolen plant will be the site for one of the main projects scheduled by LUKOIL in the next few years: construction of the Caspian Gas-chemical Complex. The Complex will use hydrocarbons produced by LUKOIL Group in the Caspian region. 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.

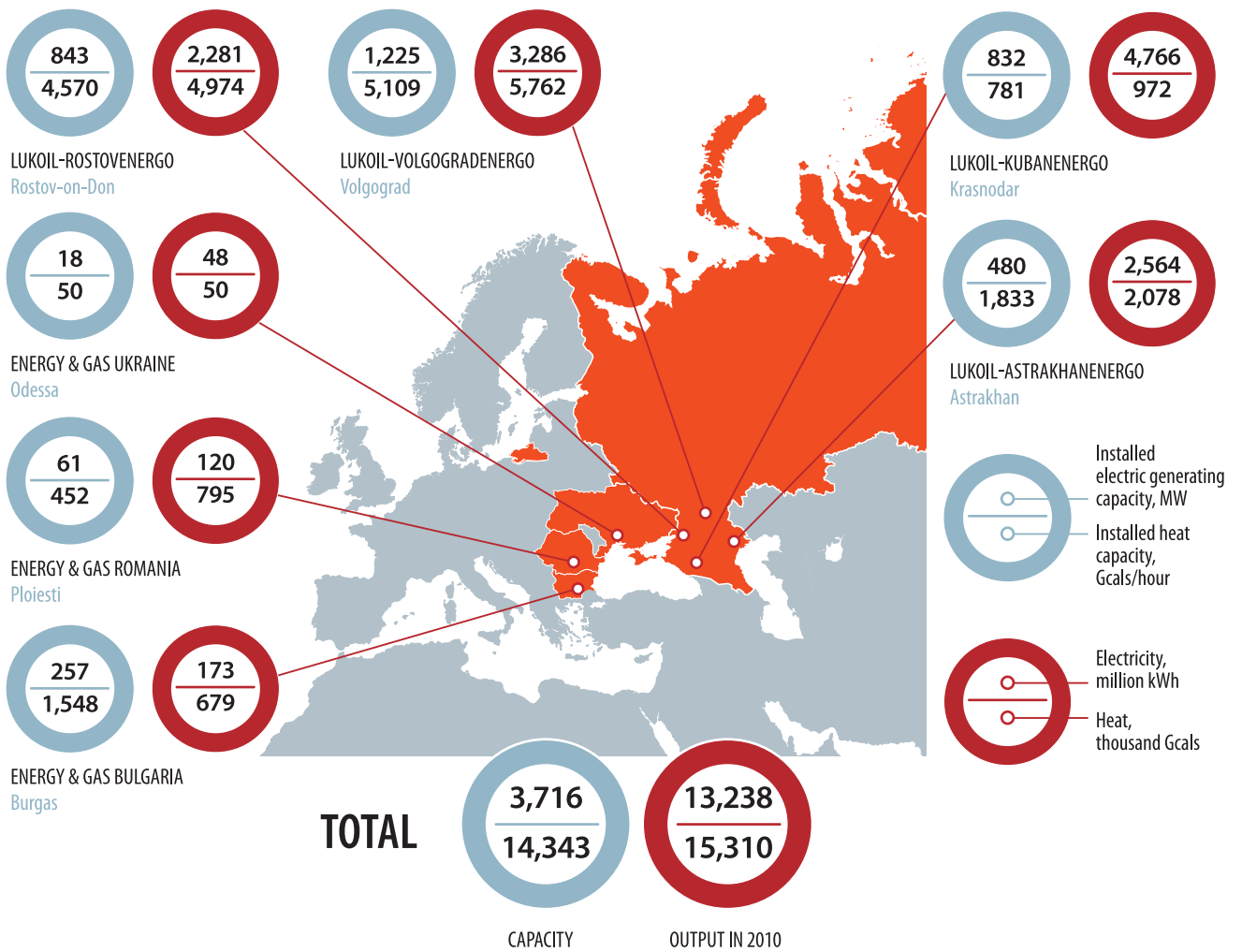
Pre-project work and configuration of the Complex was completed in 2010. The first gas-processing line with 2 billion cubic meter capacity is scheduled for launch in 2015, and modernization of existing ethylene and polyethylene facilities will be completed at the same time. That will be followed in 2017 by launch of new ethylene and polyethylene capacities together with a second gas-processing line with capacity of 4 billion cubic meters.

3

POWER GENERATION



■ LUKOIL POWER GENERATING COMPANIES



LUKOIL's new business sector, Power Generation, was created in 2008 as part of the Group's Strategic Development Program, and the sector has a special role to play in the Group's updated Strategy for 2010-2019. Power Generation sector will be an important factor for growth of cash flow and shareholder value in the long term.

The new business comprises all aspects of power generation, including delivery and marketing of electrical energy and of heat produced at power plants. The nucleus of the segment is the Russian power generating company, UGK TKG-8, which was acquired by LUKOIL in 2008, but it also includes companies producing electricity and heat in Bulgaria, Romania, and Ukraine.

THE SECTOR PROVIDES ENERGY BOTH FOR THE COMPANY'S OWN NEEDS (IN THE EXPLORATION & PRODUCTION AND REFINING & MARKETING SEGMENTS) AND FOR EXTERNAL POWER AND HEAT CUSTOMERS IN THE SOUTHERN FEDERAL DISTRICT OF RUSSIA.

BUSINESS RESTRUCTURING

Reorganization of UGK-TGK-8 was completed in the reporting year. The company was renamed 'LUKOIL-Ecoenergo' and was united with the Company's hydroelectric facilities. LUKOIL-Ecoenergo will now focus specifically on renewable energy projects (wind power, hydroelectric and solar power).

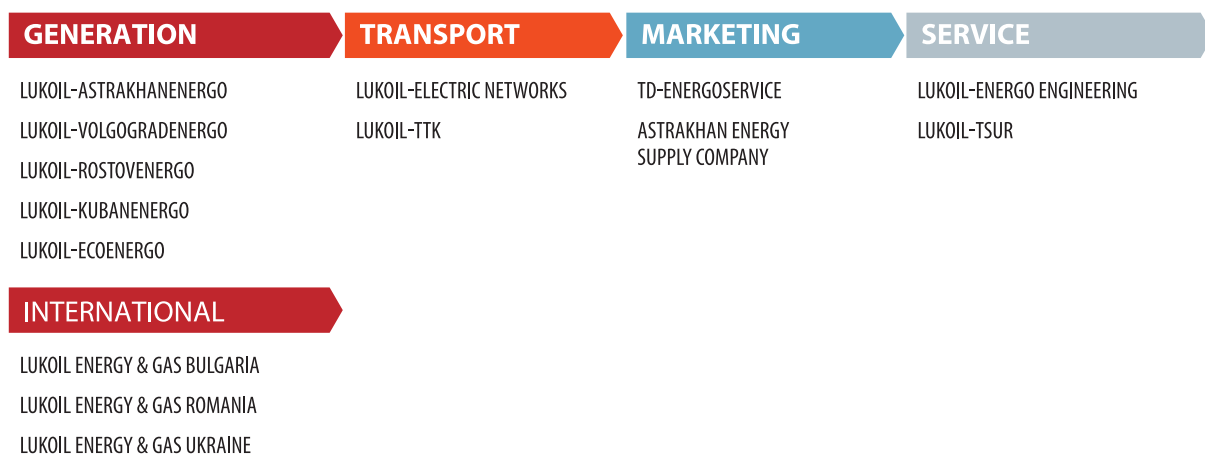
ELECTRICITY AND HEAT GENERATION

Companies in LUKOIL's Power Generation sector generated about 13.2 billion kWh of power in 2010. Total supplies of heat were 15.3 million Gcal, which is 9% less than in 2009. Lower heat production in the reporting year was due to a decline in demand from consumers in the Southern Federal District.

Work continued in 2010 under the Capacity Provision Agreement, to which LUKOIL committed during reorganization of RAO UES (the former Russian power sector monopoly). Steam turbine facilities are being built in Astrakhan Region (110 MW capacity) and Krasnodar Territory (410 MW), which should enter service in 2011. However, these two facilities, with combined capacity in excess of 500 MW are only the first stage of LUKOIL's ongoing work for modernization of Russian energy facilities and capacity expansion in energy-deficient regions. Other projects in the Southern District in fulfilment of the Capacity Provision Agreement are now at the design stage, and LUKOIL is committed to building 900 MW of generating capacity in total.

LUKOIL is also working consistently to optimize production costs of its generating assets and to maintain close control of anti-crisis program implementation in terms of reduction of non-production expenses.

■ STRUCTURE OF LUKOIL'S POWER GENERATION BUSINESS



SMALL-SCALE GENERATING

LUKOIL IS RAPIDLY DEVELOPING ITS OWN POWER GENERATING FACILITIES AT OIL & GAS FIELDS, ENABLING THE GROUP TO SUBSTANTIALLY REDUCE ELECTRICITY PURCHASES AND INCREASE THE RATE OF ASSOCIATED GAS USE BY TURNING IT INTO ELECTRICITY.

Installed capacity of small-scale generating facilities is 0.7 GW. The Group generated 1,409 million kWh of electricity at its own facilities in 2010, representing 9.9% of total consumption in production operations.

Electricity supply arrangements have been made more secure by use of the latest technologies in investment projects for construction and reconstruction of the Company's own generating facilities. Use of new technologies also enables the Company to limit spending on its electricity needs, through improvement of energy efficiency and use of the Company's own refined products as generating fuel.

ENERGY-SAVING TECHNOLOGIES

LUKOIL works constantly to improve reliability of its electricity supply arrangements and to reduce spending on energy. These efforts have been coordinated through corporate programs for energy saving and improvement of reliability of power supplies.

Spending on measures as part of the program for improving reliability of electricity supplies was over \$149 million in 2010. Implementation of the program reduced power cuts and resulting underproduction of crude oil by nearly 30%. Also during the reporting year Petrotel LUKOIL S.A. brought a power and heat generating facility into test production using circulating fluidized-bed technology, in order to improve reliability and enable flexibility in power supplies.

An energy audit schedule for Group oil & gas production subsidiaries was approved during 2010. The purpose of the audit is to identify potential for energy saving and greater efficiency in use of electricity, and also to devise energy-saving measures. Energy audits were carried out

in 2010 at LUKOIL-Western Siberia, LUKOIL-Perm, LUKOIL-Komi, LUKOIL-Volgogradneftepererabotka and LUKOIL-Nizhegorodnefteorgsintez.

A generating unit that meets the latest efficiency and ecology criteria was launched and put into commercial use in 2010 by LUKOIL Energy & Gas Ukraine. Visbreaking residues from refining operations in Ukraine can now be put to commercial use as main fuel inputs to the new generating unit.

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.

RENEWABLE ENERGY

UGK-TGK-8, renamed 'LUKOIL-Ecoenergo' at the end of 2010, now brings together all of the hydroelectric generating facilities of LUKOIL. The main purpose of LUKOIL-Ecoenergo is to carry out renewable energy projects.

LUKOIL specialists are fully aware of the huge potential for resource and energy savings, which is offered by alternative sources of energy. Renewable energy projects are being considered, which would use hydro, wind, solar and geothermal energy. These activities are being pursued in partnership with international companies, which are also interested in development of renewables. In 2010 LUKOIL signed an agreement of mutual understanding with the Italian company, ERG Renew, on cooperation in the field of renewable energy. In accordance with the agreement, the partners will consider potential for combining their renewable energy businesses in Bulgaria, Romania, Serbia and Russia. The primary focus will be on wind power projects. ERG has extensive experience in construction and operation of renewable energy facilities.

4

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 SUPPLIES BY THE COMPANY IN 2010, INCLUDING DELIVERIES FOR REFINING AT THE COMPANY'S OWN REFINERIES AND AT THIRD-PARTY REFINERIES, WERE 114 MILLION TONNES. DELIVERIES OF OIL TO THE DOMESTIC MARKET WERE MORE EFFICIENT THAN MOST NON-CIS DELIVERY EXPORT ROUTES, SO THAT SUBSTANTIAL VOLUMES OF OIL WERE REALLOCATED FROM LESS EFFICIENT EXPORT ROUTES TO COMPANY REFINERIES OR TO THE DOMESTIC MARKET.

Refining at facilities inside Russia remains the most efficient use of crude oil produced by LUKOIL. **Crude oil deliveries to Group refineries in Russia** were 45.21 million tonnes in 2010, which is nearly 2% more than in 2009. In order to optimize transport costs the Company resumed the practice of crude oil substitution with other companies in deliveries to refineries. Starting in May 2010 LUKOIL-Western Siberia delivered 50,000 tonnes of oil per month to refineries at Ufa, which are owned by Bashneft, and Bashneft supplied an equivalent amount of oil to LUKOIL's Nizhny Novgorod Refinery. Total oil supplies using this arrangement were in excess of 500,000 tonnes.

Crude oil deliveries to the **Group's foreign refineries and to the ISAB and TRN complexes**¹ were 20.97 million tonnes in 2010, which is 15% more than in 2009. The increase was due to acquisition of a stake in TRN in September 2009. LUKOIL also delivered its oil to third-party refineries outside Russia in 2010, but the volume

of such deliveries was much reduced in comparison with 2009 (by 97% to 110,000 tonnes). This reduction was due to halting of deliveries to refineries in Belarus at the end of 2009, after refining in Belarus became less profitable. In the third quarter of 2010 the Company began refining of crude oil at a third party refinery in Kazakhstan.

Some 3.6 million tonnes of crude oil were sold on the **domestic market** in 2010, which is 22% more than in 2009. The increase was a result of reallocation of crude oil volumes which were previously refined at third party refineries in Russia and Belarus.

Crude oil exports from Russia by LUKOIL subsidiaries (including oil acquired from other producers) were 40.59 million tonnes in 2010 (815 th. barrels per day), which is 3.4% less than in 2009. Lower exports were the result of lower output and also termination of deliveries to Belarus refineries.

Most exports of crude oil in 2010 were via the Transneft pipeline system (deliveries via the system were 78% of exports during the year), but Transneft deliveries declined by 4.3% in the reporting year to 31.59 million tonnes. The volume of export deliveries by-passing the Transneft system in 2010 was 9 million tonnes, unchanged from 2009. These deliveries 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

¹ Including deliveries of petroleum products to the ISAB and TRN complexes.

is sold at the price for Urals blend crude, making Urals blend the Company's main export commodity).

THE COMPANY EXPORTED 8.73 MILLION TONNES OF CRUDE OIL VIA ITS OWN TRANSPORT TERMINALS IN 2010. EXPORTS THROUGH THE VARANDEY TERMINAL IN 2010 WERE 7.5 MILLION TONNES, AND EXPORTS THROUGH THE PORT OF SVETLY WERE 1.2 MILLION TONNES.

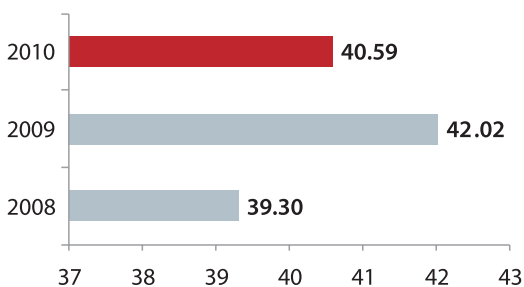
The Company managed export deliveries in 2010 in order to make them as efficient as possible. Black Sea export deliveries, which had been scheduled for shipment via the port of Yuzhny, were redirected to a more efficient route — via the port of Primorsk.

The situation on the freight market and low tariffs for demurrage made deliveries of oil by RITEK via the northern export route financially advantageous. A logistics system was designed and implemented on the route using LUKOIL's own infrastructure (direct transportation to Europe without trans-shipment onto Aframax-type tankers).

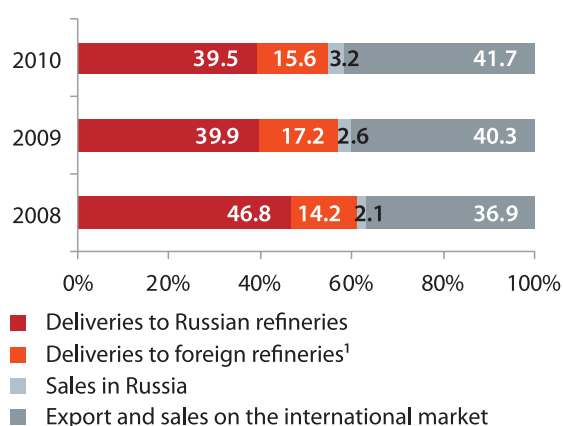
Sales of crude oil on the **international market** (exports and oil produced outside Russia) were 47.74 million tonnes in 2010, of which 3.18 million tonnes were sold in near-abroad countries and 44.56 million tonnes on other markets. Total sales of oil on Russian and international markets in 2010 were 51.38 million tonnes, which is 2.8% more than in 2009.



■ CRUDE OIL EXPORTS FROM RUSSIA, million tonnes



■ STRUCTURE OF CRUDE OIL DELIVERIES, %



¹ Including deliveries of petroleum products to the ISAB and TRN complexes

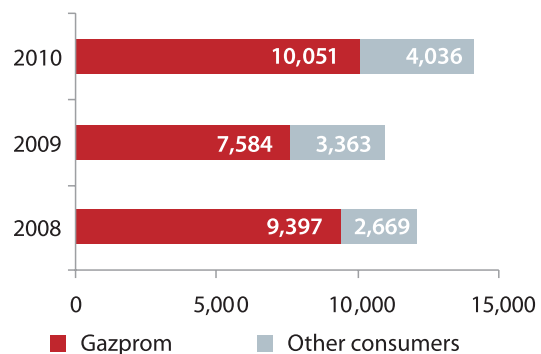
GAS DELIVERIES

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.

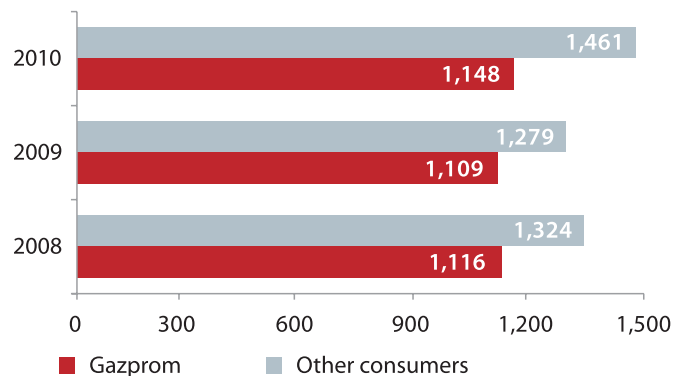
Sales of natural, associated, stripped and dry gas by the Group's Russian organizations totalled 14.087 billion cubic meters in 2010, which is 29% more than in 2009. Of this total, 10.051 billion cubic meters of gas were sold to Gazprom (including more than 8 billion cubic meters of natural gas from the Company's Nakhodkinskoye field) and 4.036 billion cubic meters of gas were sold to other consumers. Increase of sales volumes was due to higher global demand for gas and corresponding lifting of purchase volume restrictions by Gazprom. There was also an increase by three times in associated gas deliveries by LUKOIL-Western Siberia to Purgaz, after the Severo-Gubkinskoye field reached full operating capacity (the field was launched in June 2009).

Average-weighted price of gas sales in the reporting year rose by 7.4% in comparison with 2009 to 1,238 roubles per thousand cubic meters (1,148 roubles in sales to Gazprom and 1,461 roubles in sales to end-users). The increase was due to growth of more efficient sales to end-users.

STRUCTURE OF GAS SALES BY LUKOIL, billion cubic meters



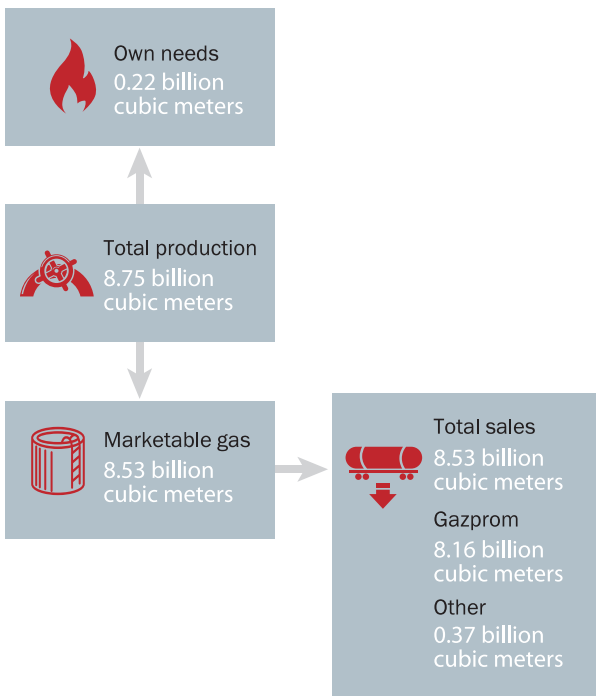
LUKOIL SELLING PRICE FOR GAS, roubles per thousand cubic meter



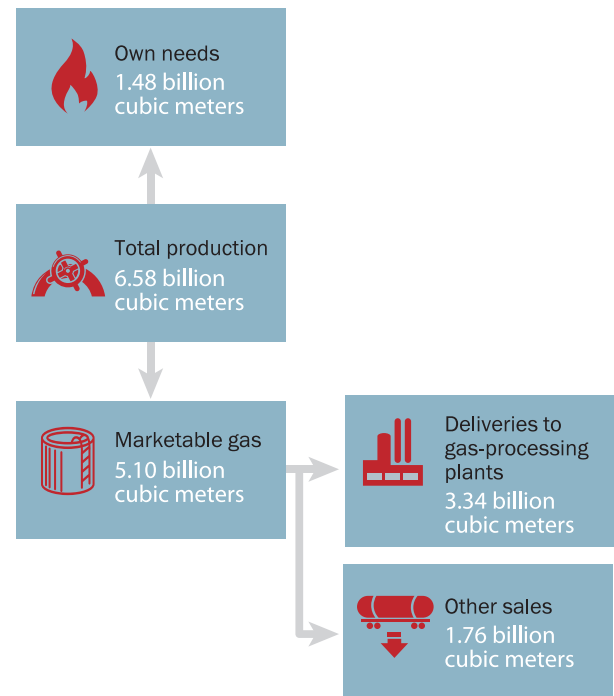
GAS PRODUCTION AND SUPPLY STRUCTURE

RUSSIA

NATURAL GAS

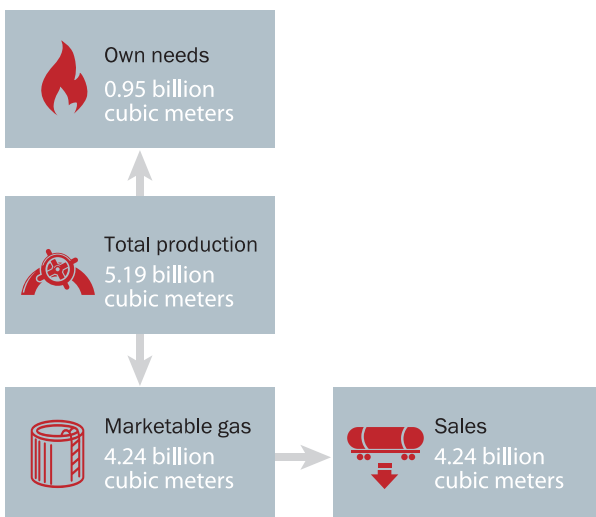


ASSOCIATED GAS

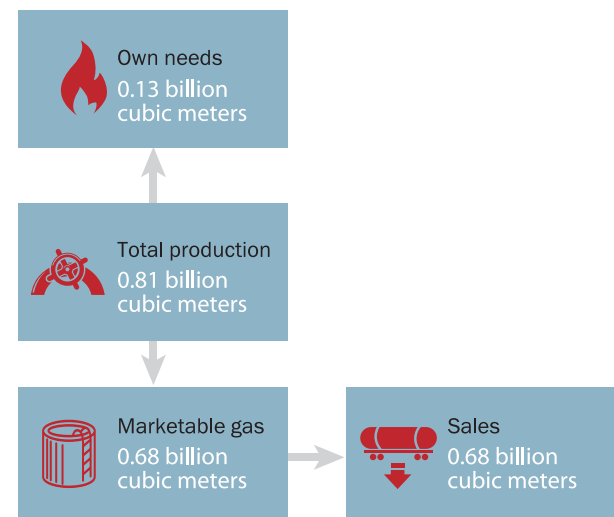


INTERNATIONAL

NATURAL GAS

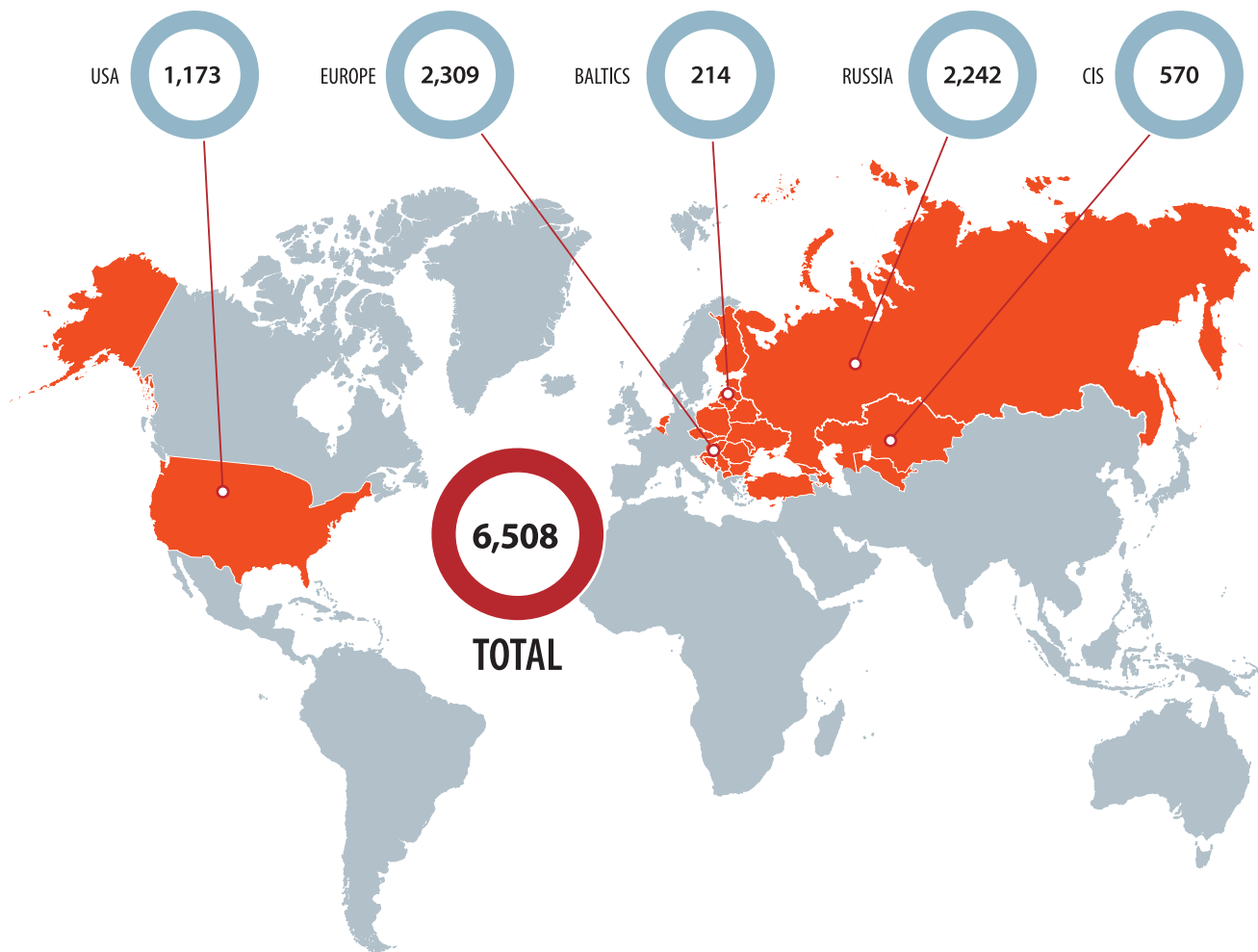


ASSOCIATED GAS



PETROLEUM PRODUCT MARKETING

LUKOIL RETAIL NETWORK (NUMBER OF FILLING STATIONS)



PETROLEUM PRODUCT WHOLESAL

Volume of LUKOIL's petroleum product wholesale business in Russia in the accounting year was 10.98 million tonnes, which is 12% more than in 2009.

Petroleum product exports decreased by 6.9% in 2010 to 25.8 million tonnes due to increase in deliveries of medium distillates to the Russian domestic market. Structure of exports remained unchanged in the reporting year, and was dominated by heating oil, diesel fuel and vacuum gas oil, which accounted for 92% of total export volumes. The Company's petroleum product export structure mainly corresponds to the structure of product exports from Russia as a whole.

Railway remained the chief means of transport for Group exports of petroleum products (over 80% of the total in 2010). The Company used the rail infrastructure for shipment of petroleum products to the Vysotsk terminal. A total 12.3 million tonnes of petroleum products were shipped through Vysotsk in the reporting year, including 3.4 million tonnes of vacuum gasoil, 3.6 million tonnes of diesel fuel and 5 million tonnes of fuel oil.

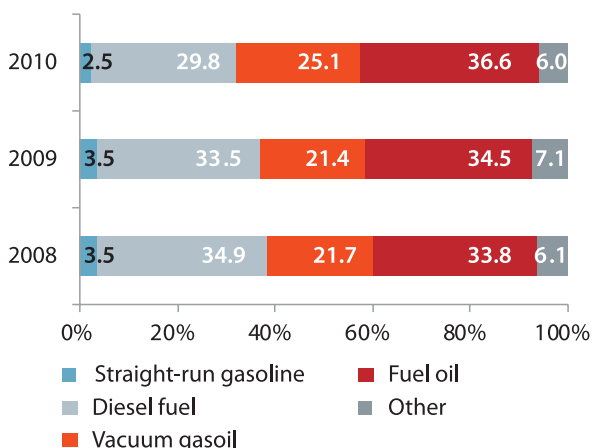
Export of petroleum products was also carried out by sea and river transport, and by pipeline (respectively 11% and 9% of export volumes) in the reporting year.

The Company continued its efforts to optimize petroleum product deliveries in 2010. Export deliveries of diesel fuel with sulphur content of 10 ppm via the port of Primorsk were increased and deliveries of vacuum gasoil were redirected from the port of Vysotsk to Baltic ports without loss of efficiency, freeing capacity at Vysotsk for shipment of fuel oil via the most efficient route. Products were also exported using new routes in 2010 including jet fuel Jet A-1 and diesel fuel delivered to Afghanistan, and bitumen to countries in West and East Africa and to Indonesia.

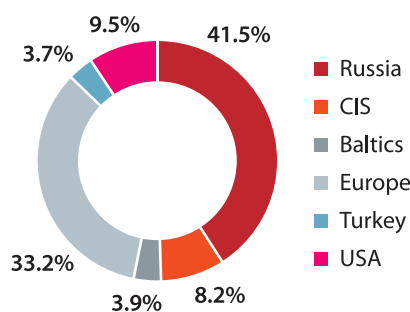
LUKOIL is rapidly developing its international petroleum product trading business, increasing both scale and international diversification. The Group's objective is this business is to achieve maximum efficiency in resource placement, including direct sales to end-users without use of intermediaries, as well as deliveries of third-party petroleum products and supplying own sales networks. Petroleum product wholesaling on international markets (including export) rose by 4.1% in 2010 to 80.04 million tonnes.

LUKOIL has trading offices in nine countries worldwide and makes deliveries of crude oil and petroleum 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 90 countries worldwide during the reporting year.

STRUCTURE OF PETROLEUM PRODUCT EXPORTS, %



STRUCTURE OF PETROLEUM PRODUCT SALES IN 2010 (own production, wholesale and retail)



PETROLEUM PRODUCT RETAIL

By the start of 2011 the Company's retail network extended to 27 countries, including Russia, CIS and European countries (Azerbaijan, Belarus, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Finland, Georgia, Hungary, Italy, Latvia, Lithuania, Luxembourg, Macedonia, Moldova, Montenegro, Poland, Romania, Serbia, Slovakia, Turkey and Ukraine) as well as the USA. The network includes 189 storage facilities with total capacity of 2.88 million cubic meters and 6,508 filling stations (including franchises).

RETAIL SALES OF COMPANY PETROLEUM PRODUCTS THROUGH OWNED AND LEASED FILLING STATIONS INCREASED BY 1.8% IN THE REPORTING YEAR COMPARED WITH 2009 TO A LEVEL OF 14.34 MILLION TONNES. AVERAGE DAILY SALES PER FILLING STATION (OWNED OR LEASED) ROSE FROM 7.8 TO 8.1 TONNES THANKS TO OPTIMIZATION OF THE RETAIL NETWORK AND REDUCTION IN NUMBERS OF STATIONS WITH LOW EFFICIENCY.

Increase of retail sales mainly reflected a trend on the Russian market, where sales volumes were 13% higher than in 2009. Retail sales outside Russia declined in 2010, mainly due to restructuring of the Company's retail network in the US.

The Company continued optimization of its retail network in 2010 in order to reduce costs and increase efficiency. In Europe and the CIS the changes affected 100 filling stations (one was leased, 13 were closed down, one was sold and 85 were franchised) and three storage facilities, which were temporarily closed. In Russia the changes affected 25 filling stations (eight were leased, one was closed down, and 16 were sold) and nine storage facilities (seven were sold and two were temporarily closed). However, construction and acquisition of highly-efficient stations continued, and upgrading was carried out at existing stations. In Europe and the CIS 23 filling stations were built, 59 were acquired and 50 were upgraded. In Russia 38 filling stations were built, 26 were acquired and 45 were upgraded.

Investments in the retail sector in 2010 were \$414 million.

The Company continued to implement its program for development of a marketing and sales network for liquefied and compressed gas in 2010. Total Group sales of these products were 836,300 tonnes (of which 474,500 tonnes via the retail network), which is 12.3% more than in 2009.

The Company continued to develop its system for non-cash payment by customers at its filling stations in 2010, using the LICARD fuel card system. A total of 2,864 filling



stations in Russia were capable of accepting the cards for payment at the start of 2011, of which 1,952 were LUKOIL stations. There were 673 stations using the card outside Russia, of which 530 were Company stations.

The total number of stations accepting LUKOIL fuel cards was 3,537 at the start of 2011, having increased by 56 since the start of 2010. More than 4.4 million LICARDs were in circulation as of January 1, 2011 (including more than 4.2 million inside Russia), representing an increase of 35% compared with 2009.

Total volume of fuel sales using all LICARD types was 3.65 million tonnes in 2010, of which about 3.44 million tonnes inside Russia and about 212,000 tonnes abroad.

Russia

As of January 1, 2011 LUKOIL's retail network in Russia consisted of 2,242 filling stations (including franchises) and 110 storage facilities with reservoir capacity of 1.11 million cubic meters. The filling stations and storage facilities 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 2010 was 7.02 million tonnes, which is

13% more than in 2009. Average daily sales per filling station in Russia rose to 10.2 tonnes.

Investments in development of the Group's Russian retail business were \$204 million in 2010.

The Company sold 16 filling stations and seven storage facilities in 2010 as part of its program for optimization of the sales network, and leased out eight filling stations, while one filling station was closed down and two storage facilities suspended operations. The Group acquired and built 64 new filling stations, and rebuilt 45. Three of total 38 filling stations newly built by the Company are in 'Olympic' format, of which two were built face-to-face on opposite sides of the M-7 highway in Nizhny Novgorod Region and the third is at Utkina Zavod in Leningrad Region.

The Company continued to develop production and sales of its new-generation EKTO fuel brands in 2010. Total EKTO sales (gasoline and diesel) through the Company's Russian retail network in 2010 were 2.67 million tonnes, which is 23% more than in 2009. The share of EKTO brands in total sales of retail fuel by LUKOIL in Russia rose to 38% from 35% in 2009.

Total sales of EKTO gasoline in 2010 through the Company's retail network were 1.6 million tonnes, which is 23% more than in 2009, and the share of EKTO gaso-



LUKOIL BEGAN RETAIL SALES OF EURO-5 DIESEL FUEL IN 2010

During 2010 LUKOIL began retail sales in Russia of diesel fuel that meets Euro-5 criteria. The fuel is produced at Company refining facilities in Nizhny Novgorod, Perm and Ukhta and is sold under the EKTO Diesel brand through LUKOIL filling stations. Euro-5 diesel produced by the Company had been exported in previous periods.

LUKOIL made substantial investments in new production facilities to enable changeover to Euro-5 diesel, including a hydrocracking complex at the Perm Refinery, modernization of the diesel hydrotreatment facility at the Nizhny Novgorod Refinery, and installation of a number of other units, which use the most up-to-date catalytic systems.

Euro-5 diesel has a high cetane number, which ensures best-possible combustion of the fuel mixture, reduces noise and vibration, prevents corrosion, facilitates engine ignition, and reduces fuel consumption. Euro-5 diesel also slows down engine wear and prolongs life of the exhaust system, piston units, and the fuel system.

line in total gasoline retail sales rose to 31% from 28% in 2009. Sales of EKTO diesel fuel at filling stations were 1.08 million tonnes, which is 24% more than in 2009. The share of EKTO diesel in total Russian retail sales of diesel fuel was almost unchanged from 2009 at 56%.

Work continued in 2010 on development of retail sales of non-fuel products and services by LUKOIL Group's Russian petroleum product organizations (part of the Group's Refining & Marketing Strategy for the period 2010-2019). Revenue from sales of non-fuel products and services through the Group's retail network was over \$210 million in 2010 (45% of this revenue was from sales of food goods, 26% represented packaged products, and 22% was from accessories). The revenue increase reflects improvement in service quality at filling stations and expansion of the range of goods and services on offer. Development of non-fuel business is an important factor for positioning of LUKOIL Group as a customer-oriented company with international standards of service.

International

LUKOIL's retail network in the CIS (outside Russia), Europe, and the USA consists of 4,266 filling stations (including franchises) and 79 storage facilities with reservoir capacity of 1.77 million cubic meters.

Retail sales of petroleum products on international markets in the reporting year were 7.31 million tonnes, which is 7% less than in 2009. The decline was due to lower consumer demand resulting from shrinkage of household incomes and associated reduction of tourist and vehicle traffic, as well as falls in industrial output in a number of countries. Average daily sales per filling station in Europe and CIS countries (except Russia) were 6.5 tonnes compared with 7 tonnes in 2009. Sales per station in the USA were 7 tonnes in 2010 (withdrawal of inefficient stations gave an increase in sales volume per filling station in the USA, despite reduction of demand).

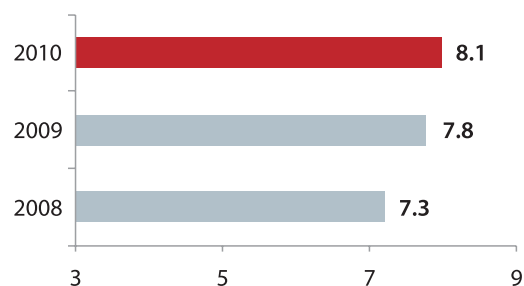
Investments for retail network development in Europe and the CIS (outside Russia) were \$210 million in 2010.

The Group brought 82 new filling stations into operation in Europe and the CIS (outside Russia) during 2010, of which 23 were newly built and 59 were acquired, and upgraded 50 filling stations.

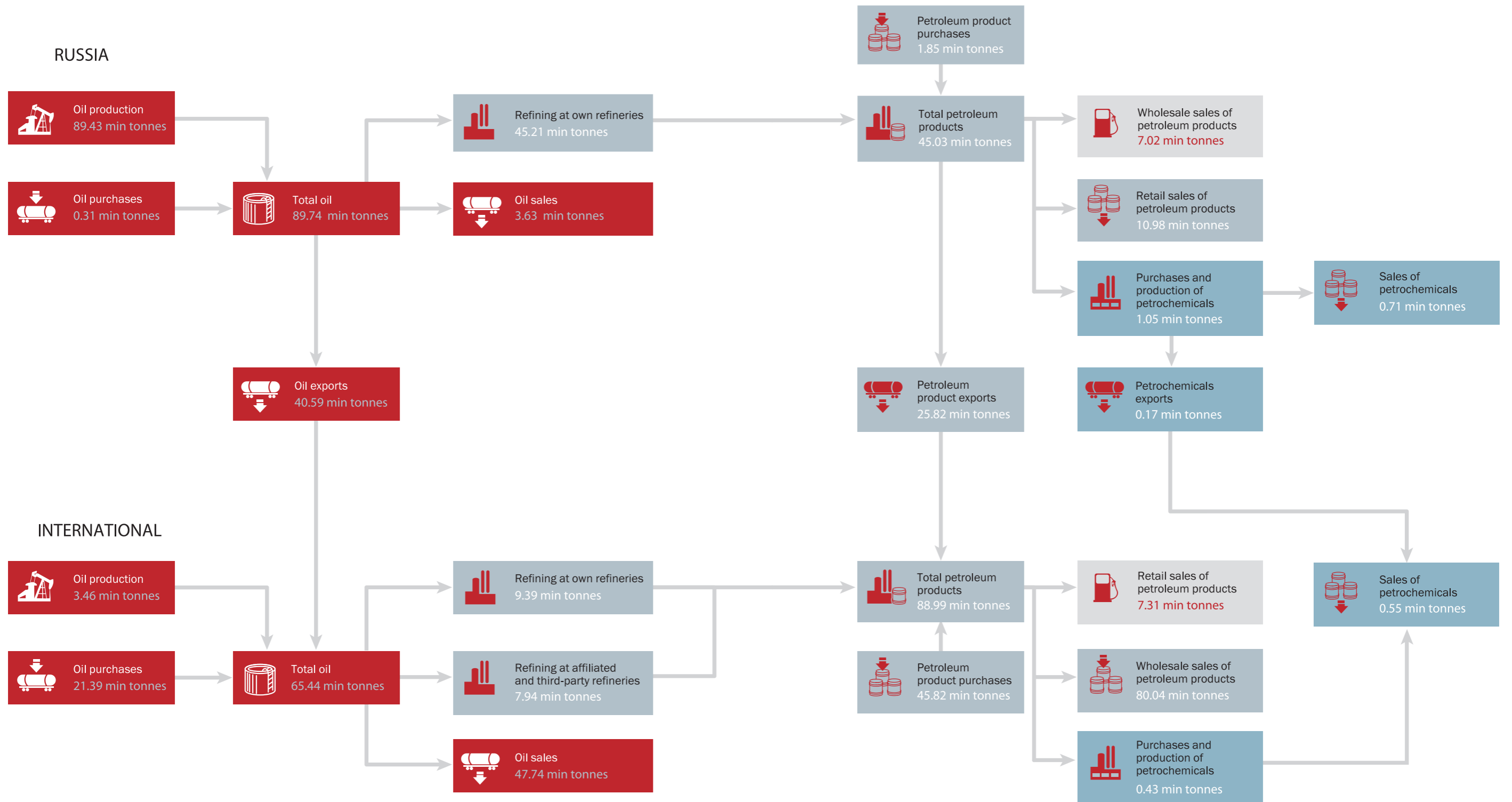
Work continued to promote the Group's EKTO fuel brand on foreign markets in 2010 (in Lithuania, Latvia, Estonia, Ukraine, Romania, Turkey, and Moldova). Total sales of EKTO fuel (diesel and gasoline) in 2010 were 768,300 tonnes, which is 3.6 times more than in 2009.

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 in Europe and the CIS were more than \$500 million in 2010. The Company plans to further increase non-fuel revenues from filling stations abroad through marketing, optimization of the product range, improvement of catering services, new service additions, work with big suppliers, other trading practices, and better standards of customer service.

■ **AVERAGE DAILY SALES OF PETROLEUM PRODUCTS PER FILLING STATION, tonnes**



TRADE BALANCE OF LUKOIL SUBSIDIARIES (2010)



5

TECHNOLOGY
AND INNOVATION



LUKOIL COUNTS NEW TECHNOLOGY AND INNOVATION AMONG ITS COMPETITIVE STRENGTHS. THE COMPANY'S SPECIALISTS BOTH DESIGN NEW TECHNOLOGIES AND WORK TO MODERNIZE EXISTING TECHNOLOGIES.

The Group continued to work closely in 2010 with the Russian Corporation of Nanotechnologies (RUSNANO) on commercialization of nanotechnologies and their application in the oil & gas industry. The companies are working jointly on design and development 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 at Group enterprises of other nanotechnologies, developed with RUSNANO's participation. These include multi-functional nano-coatings, sulphur purification units that use nano-catalyzers, and a number of other nanotechnologies.

LUKOIL Group spent more than \$120 million on research & development in 2010, substantially more than \$80 million in 2009. Institutes in the Company's R&D complex carried out project and research tasks and other work with total value of \$200 million during the year.

EXPLORATION & PRODUCTION TECHNOLOGIES

LUKOIL fully recognizes the vital role of technology in supporting competitiveness of the Exploration & Production segment. Most R&D work in the segment in 2010 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 in development of offshore fields.

Production of oil began in 2010 at the Yu. Korchagin field, where a system of extra-long horizontal wells (more than 5 km) is being applied. This is a unique project solution in Russia. All works at the field are being carried out on a 'zero-discharge' basis, which excludes negative environmental impacts.

In 2009 a consortium of LUKOIL and the Norwegian company Statoil won development rights at West Qurna-2, which is one of the largest oil fields in the Republic of Iraq with recoverable reserves estimated at 14 billion barrels of oil. A preliminary development plan was prepared and agreed between the partners in 2010, specifying measures to clarify filtration-volume features

of productive layers at the field and a schedule for drilling of wells in the 'early oil' stage.

Work at West-Qurna in 2011 will involve 3D seismic, drilling of two appraisal wells and the start of production drilling for early oil (four wells). Oil production at the field should begin in 2013. Target annual oil production level of 1.800 mln barrels per day should be attained in 2017.

LUKOIL continued to make extensive use of horizontal well drilling, which offers well productivity growth of 1.5–2 times. The usage of horizontal and multi-branch horizontal wells increases the filtration area, preventing water penetration into the well. A total of 101 new horizontal wells were commissioned in 2010 with average daily flow rate of 156.6 tonnes.

ENHANCED OIL RECOVERY TECHNIQUES

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 low permeability reservoirs, 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.**

The Group carried out 4,869 EOR operations in 2009, which is 229 less than in 2009. Additional production obtained as a result of EOR techniques was 22 million tonnes, or 25% of total oil production by the Company in Russia. Most of the additional production volume (14 million tonnes) was obtained using physical methods, primarily hydrofracturing.

The Group carried out 690 hydrofracturing operations at fields in 2010, achieving average additional oil flows of 10.8 tonnes per day. The extent and the effectiveness of hydrofracturing operations in 2010 was greater than in 2009. Hydrofracturing was applied as a method of intensifying production mainly at fields that have been in development for a long period of time and have highly depleted reserves. LUKOIL achieved higher levels of additional oil flow from hydrofracturing operations in 2010 than in 2009 through improvement of hydrofracturing design, selection of wells using hydrodynamic models, and tighter quality control over the materials and reagents, which were used by service companies.

Use of other EOR methods (hydrodynamic, heat, chemical methods and oil production intensification) gave 8 million tonnes of production. The Company continued to make extensive use of chemical technologies in 2010. The number of chemical EOR interventions was almost

unchanged (1,351 in 2010 compared with 1,357 in 2009) and gave 1.8 million tonnes additional output.

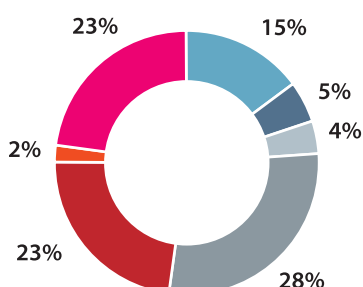
Drilling of sidetracks at existing wells has also proved a highly-efficient form of EOR. The Company continued drilling of sidetracks in 2010, when 224 such operations were carried out (264 in 2009), giving average daily flow increase of 19.7 tonnes. The Company reduced drilling of sidetracks at Russian fields by 15.2% in 2010, but efficiency of the technique increased by 17.3%. The efficiency improvement was achieved thanks to greater accuracy in forecasting of the geological structure of reserves at locations where sidetracks were drilled. Sidetracks are mainly used to extract residual oil reserves at wells, which have been taken out of operation.

PRODUCTION OF HIGH-VISCOSITY OIL

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. Thermal methods are used at both fields to increase oil recovery and annual production is about 2.3 million tonnes, representing two thirds of total heavy oil production in Russia.

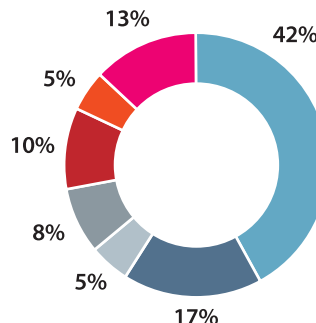
The **Permocarbon deposit at the Usinskoye field** is being developed using areal steam-heating and cyclic-steam stimulation. There has been successful work in recent years to improve efficiency of thermal applications

■ STRUCTURE OF EOR TECHNIQUES USED BY LUKOIL GROUP IN 2010



- Hydrofracturing
- Other physical techniques
- Hydrodynamic techniques
- Intensification of oil production
- Drilling of sidetracks
- Chemical techniques
- Heat techniques

■ SHARES OF ADDITIONAL PRODUCTION OBTAINED BY USE OF VARIOUS EOR TECHNIQUES IN 2010



- Hydrofracturing
- Other physical techniques
- Hydrodynamic techniques
- Intensification of oil production
- Drilling of sidetracks
- Chemical techniques
- Heat techniques

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.

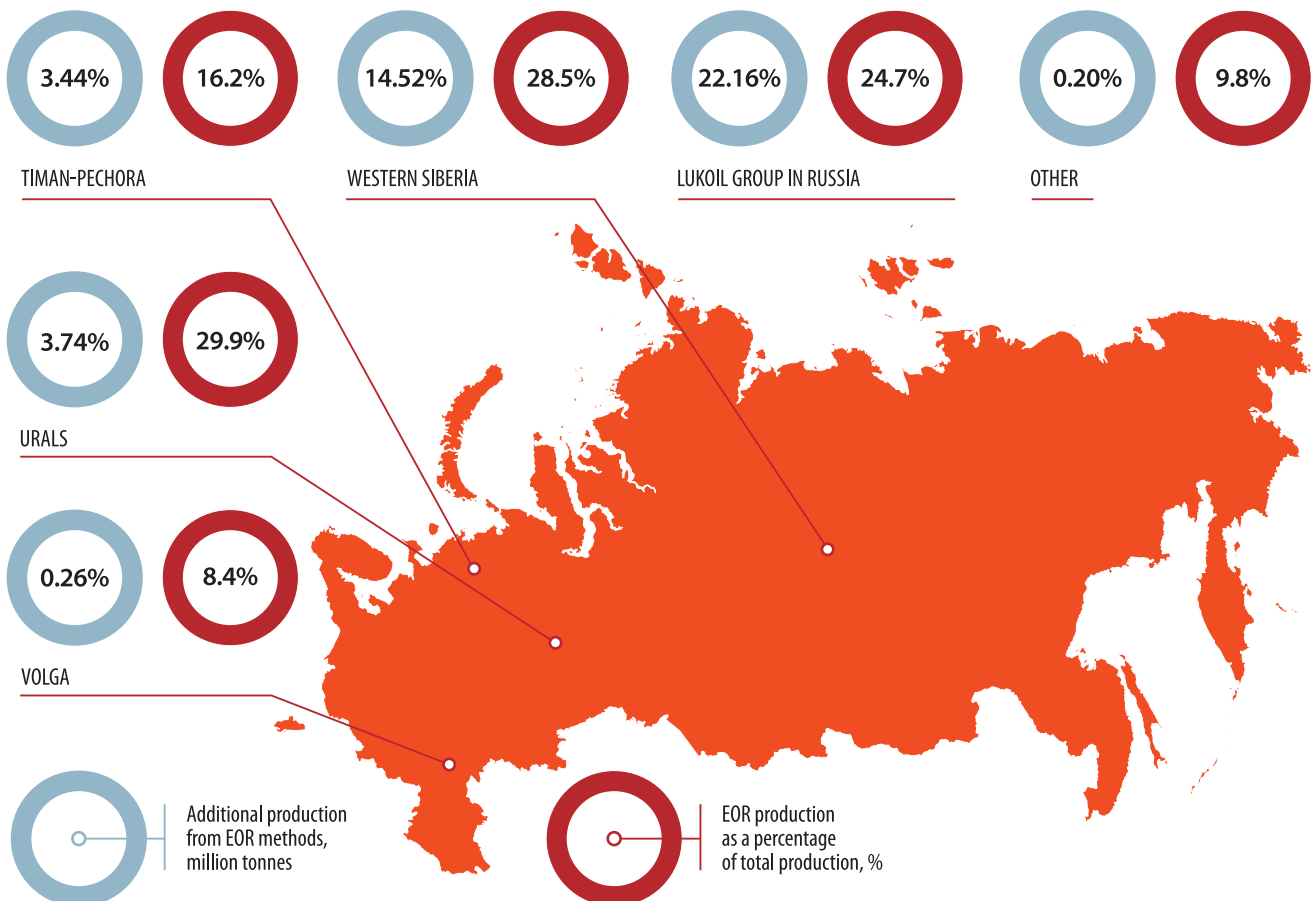
The **Yaregskoye field** is being developed using a thermo-shaft technology. Surface production is still at the industrial testing stage, with the objective of establishing optimal techniques for use of horizontal wells in injection and production applications. Three horizontal wells with horizontal sections of 1,000 meters were drilled in 2010 at the Lyaelskaya area of the Yaregskoye field for application of thermo-gravitational strata draining technology. Another two production wells and then five

injection wells will be drilled in 2011, creating a total of five well-pairs. The area will then be tested by primary steam injection into the injection and production wells. Oil production should begin in 2012.

Industrial application of thermo-gravitational strata draining will enable development of non-draining reserves (up to 16.5 million tonnes), increasing overall output at the Yaregskoye field.

Further use was made in 2010 of assembled drive mechanisms using permanent-magnet motors for pump installations, developed and produced by LUKOIL Group. New types of cavity pumps are being used in Timan-Pechora for production of high-viscosity oil using permanent-magnet-motor drives. Work in 2011 will include testing of metal carcasses for oil production equipment with various new protective coatings, including coatings obtained using gas thermal deposition and nanotechnologies.

■ EFFECT FROM EOR IN RUSSIA (2010)

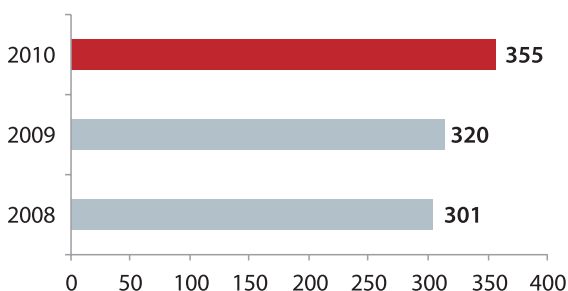


GEOLOGICAL AND HYDRODYNAMIC MODELS

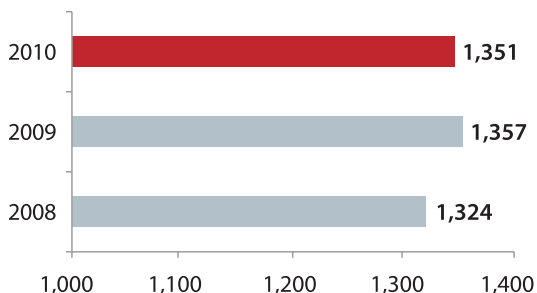
Oil & gas production subsidiaries of LUKOIL were producing hydrocarbons at 355 fields in the Russian Federation during 2010. Project documents for development work at these fields identify 986 geological targets for development. Geological and hydrodynamic modelling is used for monitoring of development processes, choice of technologies, and for measuring efficiency during production of reserves. By the end of the reporting year geological and hydrodynamic models had been prepared for a total of 964 geological targets. Use of geological and hydrodynamic models allows optimal technological solutions to be put into effect during field

development, tailored 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, and are designed to 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, use of modelling has enabled the Company to keep output levels steady and in some cases to increase output. This result reflects improved quality of the models and ever greater 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.

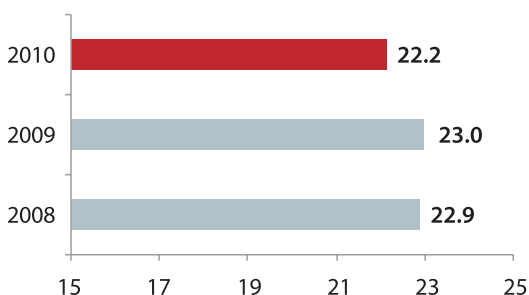
■ NUMBER OF GEOLOGICAL-HYDRODYNAMIC FIELD MODELS



■ USE OF CHEMICAL METHODS, wells



■ ADDITIONAL PRODUCTION FROM EOR IN RUSSIA, million tonnes



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 2010 TO MODERNIZE EXISTING UNITS AND LAUNCH NEW UNITS AT COMPANY REFINERIES IN ORDER TO INCREASE YIELD OF HIGH-QUALITY PRODUCTS. THE HIGHLIGHT OF SUCH WORK IN 2010 WAS LAUNCH AT THE NIZHNY NOVGOROD REFINERY OF A CATALYTIC CRACKING COMPLEX AND A NEW ABSORPTION-GAS FRACTIONATION UNIT.

Other improvements to refining technology in the reporting year included completion of a short-cycle absorption block for hydrogen at the **Volgograd Refinery**. Modernization of the heat exchanger on the diesel hydrotreatment unit was also carried out at Volgograd.

A diesel hydrotreatment unit and a unit for hydrotreatment of catalytic-cracking gasoline were brought into operation at the **Burgas Refinery** in Bulgaria during 2010.

LUKOIL is also devoting much attention to development of up-to-date production technologies for lubricants and additives, which is the responsibility of a science and technology unit within the Company. 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.

Work was carried out in the same sphere for development of new-generation turbine lubricant technologies. Company specialists have 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 lubricants. Steps were taken to improve yield of priority products, reduce energy consumption and raise the quality of base oils. The Company began production of 40 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 at an ever increasing number of Group organizations. Progressive creation and development of the Integrated Management System with SAP archi-

ture had enabled installation of 23 modules at nearly 110 Group organizations by the end of 2010.

Work continued in 2010 to prepare for implementation of the IMS Global Solution. It will allow Company employees to work in a unified IT space, supporting proper balance and efficiency of the LUKOIL management system. In 2010 the LUKOIL Management Committee approved main documents for the management system, setting out the final form which it will take, and prepared for a pilot project.

Elements of the IMS are to be developed and applied in all spheres of Group business.

6

SOCIAL
RESPONSIBILITY



LUKOIL IS GUIDED IN ITS WORK BY THE HIGHEST STANDARDS OF CARE FOR THE ENVIRONMENT AND INDUSTRIAL SAFETY. THE COMPANY ACKNOWLEDGES

ITS RESPONSIBILITY TO SOCIETY FOR RATIONAL USE OF RESOURCES AND TAKES ACCOUNT OF THE ENVIRONMENTAL IMPLICATIONS OF ITS OPERATIONS.

PROTECTING THE ENVIRONMENT

Scheduled work continued in 2010 at LUKOIL Group to ensure industrial and environmental safety and for prevention and resolution of emergency situations. A re-certification audit of the Group's health, safety and environment management system was carried out by auditors of Bureau Veritas, who visited eight LUKOIL organizations and the Group's central headquarters. For the first time in the history of Company HSE audits, no substantial compliance failure was found. The system was once again recommended for re-certification as compliant with criteria of the ISO 14001 and OHSAS 18001 standards.

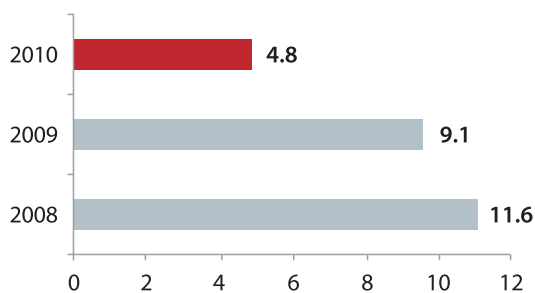
Environmental measures as part of the Group's HSE policy are carried out in the framework of LUKOIL's medium-term Environmental Safety Program for 2009-2013 and of environmental action plans of subsidiaries, which are prepared annually. In 2010 LUKOIL achieved steady reduction of industrial impacts on the environment and improvement of environmental indicators in its operating regions thanks to measures, which included:

modernization of purification facilities; improvement of systems dealing with dangerous waste; landscaping of production zones and adjacent areas; and monitoring of the state of the environment.

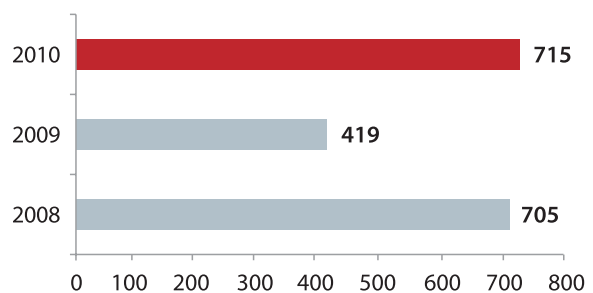
Implementation of environment policy by the Company is significantly hampered by inadequacy of environmental legislation, which is subject to frequent changes and various interpretations. The Company's environmental services and subsidiaries spend much time studying changes in the law, adapting their activity to new legal requirements, and preparing proposals for improvements to current legislation.

Monitoring of environment law, rapid notification of relevant departments of subsidiaries concerning changes, and legal assistance by the Group enabled LUKOIL companies to avoid serious criticisms and claims from government environmental control and supervisory organizations during 2010.

WASTE WATER DISCHARGE, million cubic meters



ENVIRONMENTAL SPENDING, \$ million



A number of changes in Russian environmental law, which were approved at the end of 2009 and in 2010, have substantial impact on environmental security work by companies in LUKOIL Group. The changes include:

- approval by the President of Russia in December 2009 of the Climate Doctrine of the Russian Federation, which coordinates actions to ensure Russia's safe and sustainable development in the context of climate change
- approval by the Russian Government of the Federal Target Program, 'Clean Water', for implementation in 2011–2017, and also of various rules regulating proper and sustainable use of water resources
- approval by the Russian Ministry of Natural Resources of legal rules governing formation of waste and limits on its storage, rules for calculation of damage caused to environmental components, and other documents
- approval of various hygiene standards and norms (for levels of pollutants in the atmosphere and soil, hygiene quality in preparation of drinking water, etc.)

Preparation by the Russian Ministry of Natural Resources of a draft Decree, 'On approval of methodological instructions for calculating indicators of associated gas burning', which details requirements of the Government Resolution №7, dated 08.01.2009, setting a 95% target for associated gas utilization by 2012.



LUKOIL ACHIEVED A NEARLY TWOFOLD REDUCTION OF FOUL WATER DISCHARGE IN 2010 THANKS TO MORE EFFICIENT OPERATION OF PURIFICATION EQUIPMENT.

Volumes of dangerous waste held by LUKOIL companies were reduced by 56,000 tonnes in 2010. LUKOIL is implementing a program for utilization of associated gas to ensure compliance with Government requirements, by which at least 95% of associated gas must be utilized by 2012 (companies, which fail to meet this target, will be subject to extra environmental impact payments). Measures as part of the program enabled LUKOIL to raise the share of associated gas, which is utilized, from 71% in 2009 to 77% in 2010. The Company also carried out work in 2010 for installation of facilities for utilization of associated gas in Kazakhstan, specifically for generation of electricity to power the Company's production operations.

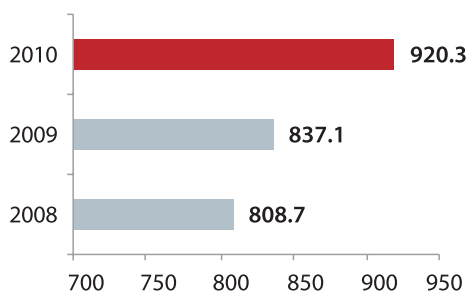
ORGANIZATIONS IN LUKOIL GROUP SPENT ABOUT \$715 MILLION IN 2010 ON MEASURES TO ENSURE ENVIRONMENTAL SAFETY (SPENDING IN 2009 WAS \$420 MILLION).

Environmental security measures at LUKOIL companies in 2010 included: actions for rational use of water resources and prevention of water pollution; reduction of atmospheric emissions; recycling of accrued waste that contains crude oil; and non-polluting, sustainable use of land. Specific steps carried out in the reporting year were as follows:

- diagnostics and major repairs of pipelines;
- modernization and construction of facilities, which increase the rate of utilization of associated gas;
- acquisition of equipment for resolving crude oil and petroleum product leakages;
- recultivation of disturbed land and land polluted by crude oil;
- various works for monitoring of environmental components;
- construction of new and reconstruction of existing networks for water supply and water discharge;
- installation of chlorination units for decontamination of industrial and river water;
- replacement of equipment and optimization of technologies for reducing pollutant emissions;
- construction of a complex for processing of waste that contains crude oil.

Thanks to these actions, the Company succeeded in reducing the share of additional (non-standard) environmental impact payments from 22% of its total environmental impact payments in 2009 to 17.6% in 2010.

■ RECYCLING AND BURIAL OF TOXIC WASTE, thousand tonnes



HEALTH AND SAFETY

LUKOIL continued to ensure health and safety of its employees in the reporting period in accordance with the Company's Health, Safety & Environment Policy for the 21st Century and with due respect for Russian law and the laws of countries where LUKOIL has operations.

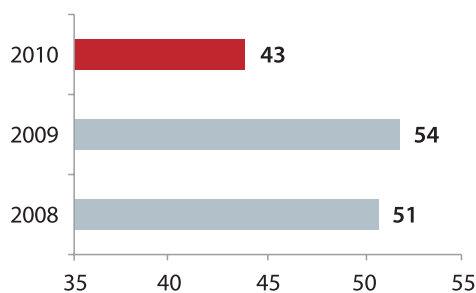
LUKOIL also pursued work in 2010 to implement its Program for health and safety, improvement of working conditions, and prevention and resolution of emergency situations at organizations in LUKOIL Group for 2006–2010. Spending on measures as part of the Program was about \$212 million.

Accident and injury rates improved in 2010 compared with 2009. There were 43 accidents at LUKOIL organiza-

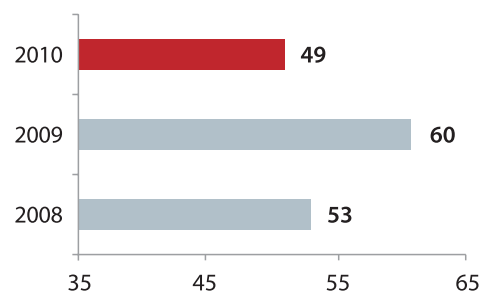
tions during the year compared with 51 in the previous year. The number of personnel who suffered injuries declined from 60 to 49, and fatalities were down from 5 to 2.

Scheduled preventative measures ensured that there were no incidents during 2010, which could be classed as emergencies. Safety drills and training sessions are held regularly at sea and river terminals, and at production, refining and storage sites, to ensure that the Company's special teams and equipments remain in a high state of readiness to deal with any oil or petroleum product leakages. A total of 80 drills and training sessions were held in 2010 for dealing with emergency oil and product leakages.

NUMBER OF ACCIDENTS



NUMBER OF ACCIDENTS



PERSONNEL AND SOCIAL PROGRAMS

WE UNDERSTAND THAT SOCIAL GUARANTEES AND PROVISIONS ARE AN IMPORTANT FACTOR DETERMINING PRODUCTIVE AND HIGH-QUALITY PERFORMANCE IN THE WORK PLACE. WE ALSO UNDERSTAND THAT THE EXCELLENT RESULTS, WHICH LUKOIL ACHIEVES IN ITS BUSINESS YEAR-ON-YEAR, DEPEND ON THE DAILY CONTRIBUTIONS OF THE MANY THOUSANDS OF PEOPLE WHO WORK AT THE COMPANY. WE THEREFORE 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.

Work continued in 2010 for implementation of the LUKOIL Group HR Policy, the Company's Social Code, and Functional HR Strategy. As instructed by the Company President, work was carried out in the reporting year to create a Code of Business Ethics and Rules of Corporate Culture. A Business Ethics Commission was set up inside the Company.

Further steps were taken in 2010 for restructuring of LUKOIL Group in order to improve operating and financial efficiency. A number of structural sub-divisions were reorganized, non-core sub-divisions were transferred from the Group to external providers, and changes were made to organizational structure and overall numbers of subsidiaries in several business sectors: electric power, refining, petrochemicals and gas processing. As a result the overall number of employees at LUKOIL organizations decreased by 9.4% in comparison with

2009, with the largest reduction in the exploration & production segment, where employee numbers fell by 11.8%. Increase in revenue contributed to much higher productivity levels in the Company in 2010: revenue rose by 42.8% and net income by 24.7% per employee.

In fulfilment of the Group's HR Policy, further improvements were made in 2010 to the system of remuneration at LUKOIL companies. Performance criteria were proposed for determining the size of annual bonuses to deputy heads of LUKOIL companies as part of efforts to optimize incentives throughout the Group. 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, taking part in surveys of wage and compensation levels that are carried out by leading consulting companies.

In addition to material incentives, LUKOIL uses moral encouragement as a way of developing personnel potential: 16 Company employees received national awards for professional excellence and for conscientious and successful work, while 550 were awarded sectoral marks of distinction for their work, and 702 employees and 33 groups of workers were presented with Company awards in 2010. 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.

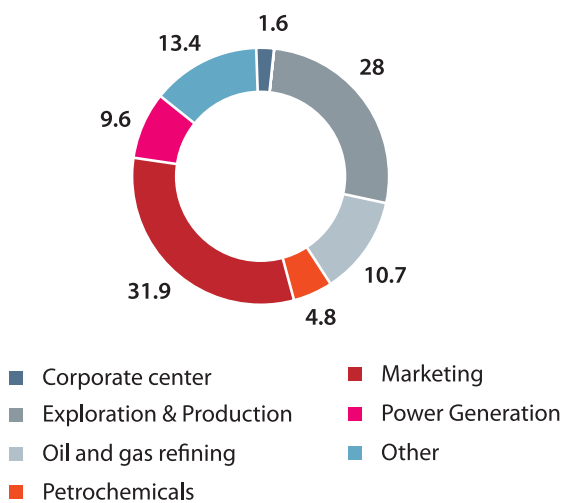


The Company continued implementation of social programs and measures, which are designed to attract highly qualified personnel to LUKOIL and ensure that they remain our employees. Spending in 2010 by LUKOIL organizations on social programs for employees, their families and pensioners were \$296 million. Social programs being implemented by the Company include:

- leisure and recreation provisions for employees and their families, organization of sport and fitness events
- health care and medical treatment for Company employees, including voluntary health insurance
- 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

By the end of 2010 a total of 39,300 Russian employees of LUKOIL had entered the shared funding system, and the sum of their annual contributions was about \$11 million. **The Company's total contributions under non-state pension provision programs in Russia and abroad for the reporting period were over \$30 million.**

EMPLOYEES BY BUSINESS SEGMENTS AS OF JANUARY 1, 2011, %





The Company makes full use of social partnerships in the labour sphere in order to maintain current levels of social provision for employees, their families and pensioners. We are constantly expanding cooperation with trade unions, government bodies and local communities as part of these efforts.

Since 2008 LUKOIL has been the official representative of the Russian Union of Industrialists and Entrepreneurs in the Tripartite Commission for Regulation of Social and Labour Relations, which is the most senior social partnership organization acting under the Labour Code of the Russian Federation. The Company has taken an active part in the Commission's work, making proposals for drafting of new laws and other legal acts in the labour sphere at the stage of their design by the Government.

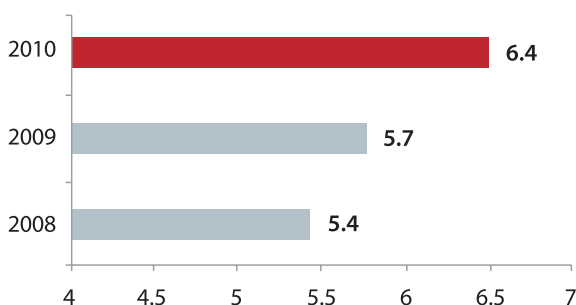
In 2010 the Company took part in 10 sessions of the Commission, at which 74 issues were considered, and also in 34 meetings of the Commission's permanent working groups, at which 54 topical labour issues were discussed.

Training and professional study is a highly important part of HR management at LUKOIL, particularly for employees in positions of responsibility and reserve executives. LUKOIL has a program for training of reserve executives for positions of responsibility at the parent Company and subsidiaries, and various training measures were carried out under this program in 2009-2010. Programs for development of leadership potential and management skills have been designed and are being provided at oil & gas sector institutes and other Russian and foreign higher-education establishments. 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. In 2010 a total of 18 employees from the corporate centre and 94 employees of LUKOIL subsidiaries benefited from additional study periods as part of MBA programs at the leading Russian oil & gas institutes — the Gubkin Russian State Oil & Gas University and the Oil & Gas Business Institute.

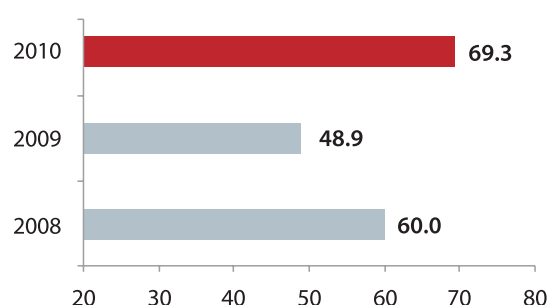
LUKOIL designed and approved a General Program for Cooperation with Higher Education Institutes in 2010 to optimize personnel training work, which was carried out jointly with such institutes. Seminars were organized for personnel of LUKOIL Overseas Holding in May 2010 as part of the Program to help familiarize Company specialists with foreign countries, where LUKOIL now has business: Iraq, Colombia, Venezuela, Cote d'Ivoire and Saudi Arabia. A total of 137 employees attended the seminars.

The Company continues to pay stipends and grants on a selective basis to students and young teachers at

■ HYDROCARBON PRODUCTION PER EMPLOYEE, thousand boe



■ NET INCOME PER EMPLOYEE, \$ thousand



higher education institutes, with which the Group has cooperation agreements, as well as organizing visits and work experience at LUKOIL companies (at product facilities and for pre-diploma purposes) for students at such institutes.

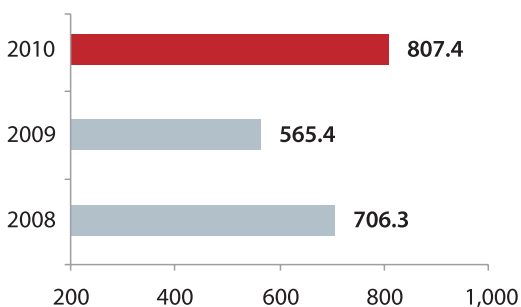
Work continued in 2010 to set up a Corporate Study Center in Astrakhan for training of LUKOIL personnel. As required by legislation, the Centre has been registered as a non-state institution for further professional education, and has obtained a license for provision of education services.

Further steps were taken in the reporting year to develop the Company's distance learning system. At present 41 Group organizations are connected to the system, which had 61,000 registered users at the end of 2010. A total of 9,800 applications have been made to carry out studies using the system and 5,900 courses of study have been completed by LUKOIL employees. New study courses were designed in the reporting year on topical themes, and a total of 120 courses had been designed and placed in open access on the portal by the end of 2010. In July 2010 Company specialists took part in the 7th International Exhibition and Conference on e-Learning in Russia, at which the Group was awarded a special prize for support to e-learning.

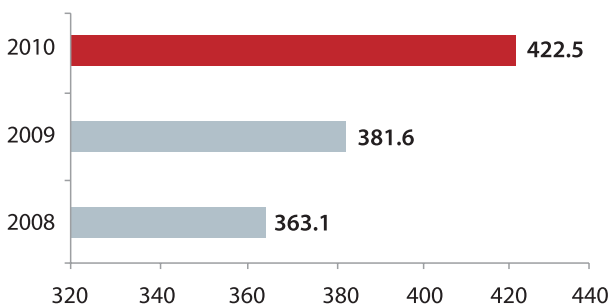
The personnel exchange program between LUKOIL and ConocoPhillips has been an important part of the process for improving professional training of Company specialists. A fifth group of 13 specialists from LUKOIL completed a period of work experience at ConocoPhillips as part of the program in 2010.

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 fifth competition in 2010 to find the Best Young Specialist of the Year: 152 competitors took part in 17 categories, and 71 employees won awards. Results were also announced in 2010 of LUKOIL's Fuel & Energy 2009 competition, which sought the best fuel and energy R&D designs by young specialists. More than 140 entries were submitted and there were about 40 prize winners.

SALES PER EMPLOYEE, \$ thousand



REFINERY THROUGHPUT AT OWN REFINERIES PER EMPLOYEE, tonnes



SPONSORSHIP AND CHARITY

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. At the same time, the Company has come to understand the danger of creating social dependence through charity actions. LUKOIL therefore makes increasing use, alongside its traditional charity actions, of strategic support programs and social investments, which combine solutions to social problems with strategic interests of the Company. This approach is based on joint work between business and the non-profit and government sectors to address urgent social and economic problems in local communities.

TOTAL SPENDING BY THE COMPANY ON CHARITY AND SOCIAL PROGRAMS WAS ABOUT \$112 MILLION IN 2010.

The Company's social policy and charity activities have two principal components:

- social investments
- sponsorship and traditional charity programs

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 and 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.

The Company, its subsidiaries and the LUKOIL Charity Fund provide help to children in 60 Russian children's homes and boarding schools, ensuring that they remain in good health and obtain an education, which will enable them to acquire a profession and find their place in life: 52 out of 55 children who left LUKOIL-sponsored children's homes in 2010 entered higher or technical education, and three went straight into employment.



Every year the LUKOIL Charity Fund organizes summer vacations by the Black Sea for children from sponsored children's homes in Ishim, Kirov, Rostov-on-Don, Nizhny Novgorod, Kstovo, Sasykol and Perm Region as well as organizing educational trips around Russia.

The Charity Fund has also been providing special LUKOIL grants since 2006 to students who continue their studies in higher education or technical institutes after leaving children's homes. Such grants were paid to 80 young people in 2010.

Since 2008 LUKOIL and its subsidiaries in Astrakhan Region have been working on a project, by which children from care homes and disadvantaged families are trained for work in managerial and technical capacities at LUKOIL. The project is motivated by a severe deficit of technical specialists, needed for new large-scale projects, which LUKOIL is implementing in the region. Gifted children from disadvantaged backgrounds will be prepared for work at the Company in technical and higher-education colleges: 20 such students have already been placed at Astrakhan Polytechnic-College and the Volga-Caspian Fishery and Industry Complex. The LUKOIL Charity Fund is covering costs of their tuition and living expenses, and they will be given employment at Group organizations in the region after completion of their studies.

In Nizhny Novgorod Region the Company provides assistance to the Kstovo Oil Industry Polytechnic, where students also include children who were formerly at LUKOIL care homes. The students regularly visit LUKOIL's

Nizhny Novgorod Refinery to learn about its operations and to acquire practical knowledge and skills. This helps to achieve social adaptation of young people, who have had a relatively difficult start in life.

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 a larger program, 'Illustrated Books for Blind Children'. Publications were supplied to specialized children's institutions in Rostov Region in 2010 as part of this project.

EDUCATION PROGRAMS

CONCERN FOR THE YOUNG GENERATION AND TRAINING OF QUALIFIED, YOUNG SPECIALISTS FOR THE RUSSIAN OIL INDUSTRY ARE IMPORTANT ASPECTS OF LUKOIL'S BUSINESS. THE GROUP CARRIES OUT MUCH WORK ON BRINGING EDUCATION AND SCIENCE CLOSER TO PRODUCTION. EDUCATIONAL PROGRAMMES HAVE A THREE-STAGE A 'SCHOOL — UNIVERSITY — ENTERPRISE' SYSTEM. THESE PROGRAMMES ARE BEING ACTIVELY IMPLEMENTED IN REGIONS WHERE LUKOIL HAS OPERATIONS.

The Company's program of assistance to higher education institutions enables them to improve their teaching resources, ensuring that the educational process is up-to-date and of a high standard. Help with acquisition of laboratory equipment is one important contribution made by LUKOIL. The Company allocated substantial amounts for development of teaching resources and reconstruction of buildings at Russian higher-education institutions in 2008-2010, when recipients included the Gubkin State Oil & Gas University, Tyumen State Oil & Gas University, Ufa State Oil and Technical University, Ukhta State Technical University, Perm State Technical University, the Diplomatic Academy of the Russian Ministry of Foreign Affairs and the Financial University (attached to the Russian Federal Government).

Since 2000 the Company has paid grants to particularly talented students at oil industry and technical institutes in Russia. In 2010 monthly corporate grants of 2,500-3,000 roubles were paid 208 students in various Russian cities.

About 90 talented young teachers at leading Russian oil & gas institutes received grants in 2010 as part of LUKOIL's program for support to young teachers. Grant payments as part of this program totaled \$300,000 in 2010.

SUPPORT FOR MEDICAL INSTITUTIONS

LUKOIL Group provides assistance to a number of major specialized medical research centers, including the the Center for Haematology Research, and the Russian Cardiovascular Scientific and Production Complex.

The Company also supports development of the system of medical services in regions where it has operations. About 10 Russian hospitals obtained expensive equipment from the Company in 2008-2010 including Astrakhan Children's Clinical Hospital №1, Penza Region Clinical Hospital, City Children's Hospital №1 in St. Petersburg, Liman Central District Hospital and Novoburassk Central District Hospital.

SOCIAL PROJECT COMPETITIONS

Social project competitions, which are held annually by LUKOIL subsidiaries in association with the LUKOIL Charity Fund, represent a particularly efficient way of implementing programs of social importance. Holding

of the competitions in regions, where the Company has operations, has become an integral part of LUKOIL's system of corporate responsibility. The competition mechanism for allocating funds has been found to operate very well in encouraging projects and initiatives among local communities to address their specific problems and aspirations. This in turn increases the efficiency of LUKOIL's social and charity allocations.

Social project competitions have been held in regions of LUKOIL presence since 2002, when the first competition was organized in Perm Territory. Geography of the events has greatly increased in recent years: they are now held in 10 of Russia's administrative regions. In 2010 a social projects competition was held in Tatarstan for the first time. A total of 8,600 projects have been proposed over nine years and 1,700 projects have received funding. The total amount spent to date by LUKOIL on social project funding is \$10 million.

Nearly 400 projects were selected for financing in 2010 out of 1,923 applications, which were submitted for consideration in various regions. The competition budget in 2010 was about \$2 million.

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 2010 to mark the 65th Anniversary of Victory in the Great Patriotic War (World War II).



In the years since they began, LUKOIL's social project competitions have proved their worth as a unique vehicle for nurturing social initiative. Independent experts agree that the competition mechanism enables funds to be allocated more efficiently. Most importantly, the system has a strong motivational element, encouraging 'grassroots' initiative by the people and organizations, who receive funding.

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.

CULTURAL AND HISTORICAL HERITAGE

Support to culture is a traditional sphere of sponsorship and charity for Russian companies. Partnership with cultural organizations has a dual nature, combining sponsorship (financing of productions, concerts, exhibitions, etc.) with a charity element. The Company supports various types of classical art and, together with its subsidiaries, lends a hand in the revival of religious and spiritual traditions.

IN 2010 LUKOIL CONTINUED ITS PROGRAMME OF SUPPORT TO A NUMBER OF LEADING RUSSIAN MUSEUMS. THE COMPANY PROVIDED FINANCIAL SUPPORT TO THE TRETYAKOV GALLERY, THE MUSEUMS OF THE MOSCOW KREMLIN, THE PUSHKIN MUSEUM OF FINE ART, THE RUSSIAN MUSEUM, THE CENTRAL STATE MUSEUM OF CONTEMPORARY RUSSIAN HISTORY, THE VYATKA V.M. AND A.M. VASNETSOV ART MUSEUM, AND THE NIZHNY NOVGOROD STATE MUSEUM OF FINE ART.

LUKOIL has a long-running association with the Tchaikovsky Symphony Orchestra, conducted by Vladimir Fedoseyev and the Perm State Theatre of Opera and Ballet. The Company has also provided financing over many years to the Kaliningrad Regional Philharmonia to finance its program, 'Bring the family to the concert hall', as well as to the Urals Academic Philharmonic Orchestra. LUKOIL supports the Spasskaya Bashnya festival of military bands, which is held annually on Red Square in Moscow.

LUKOIL provides support to religious institutions that have an important place in society. The Company is

helping to finance restoration and rebuilding of churches and monasteries, supports the Optina Pystyn Monastery, as well as funds purchases of auditorium equipment for Cyril and Methodius post-graduate and doctoral courses. Funding was also provided in 2010 to the Central Office of Muslims of Russia and to the Church of St.Vladimir in Sochi. Company subsidiaries take an active part in revival and development of centers of religious and spiritual life in Russia and abroad.

LUKOIL-Perm has carried out a number of programs in recent years to support traditional crafts of ethnic groups in the Russian North. The 11th inter-regional festival of historic towns along the Kama river was held in 2010 in the town of Kudymkar with support from LUKOIL-Perm, and the Company also helps to organize the Selenitovaya Shkatulka children's arts & crafts festival in the village of Ashap (Orda District). The community of stone-engravers in Orda District is one of very few, which has kept this tradition alive in modern Russia, and has won recognition both in Russia and internationally.

ASSISTANCE TO PEOPLES OF THE FAR NORTH

Operations by LUKOIL 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. Areas that are being developed for extraction of oil & gas are also areas where these peoples carry out economic activities (reindeer herding, fishing and hunting), that are essential to their way of life. Resulting changes can give rise to social and economic problems. LUKOIL's objective is to resolve these issues by moving gradually away from charity provision to the indigenous inhabitants of these regions and towards an economic partnership with them.

In the Khanty-Mansiysk Autonomous District (Yugra), the Nenets Autonomous District, and the Komi Republic LUKOIL has made and is implementing agreements on socio-economic development and improvements to infrastructure and dwellings on the land traditionally inhabited and exploited by indigenous groups in order to preserve and support the traditional life-styles of the Khanti, Mansi and Nenets peoples. LUKOIL also has a cooperation agreement with the organization 'Save Yugra' and the association 'Yamal for our Children'.

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 the armed forces, who have perished in more recent 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.

LUKOIL realized a number of events in the year of 65th anniversary of the Great Victory. Excursions to the museums and places of military glory, recreational tours, health resort treatment and medical inspections were organized for veterans of the World War II. Company provided support for holding the exhibitions, organizing books and medals to mark the memorable date.

SPORT

Russian sport has been a beneficiary of LUKOIL's social policy over many years. Company priorities in the sphere 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.

The Company has proved its commitment to encouraging health and fitness among its own workers and their families by organizing regular competitions in various summer and winter sports. LUKOIL's international amateur sports competitions ('Spartakiada') are among the biggest events in Russia for popularization of fitness and mass sport among corporate employees. The first such competition was held in 2001 in Astrakhan, the second in Perm in 2003, the third in Kaliningrad in 2005, and the fourth in 2007 in Kogalym. The fifth LUKOIL Spartakiada will be held in summer 2011 in Perm. Another corporate sports competition, held in 2010, was the LUKOIL President's Cup, which was dedicated to the 65th anniversary of Victory in the Great Patriotic War,



and which attracted participation by 300 sportsmen in 10 teams from LUKOIL operating regions.

LUKOIL backs professional sport in Russia by its support to leading sports teams, including Moscow Spartak football team, the Zarya Kaspiya handball team (Astrakhan), Spartak water polo team (Volgograd), the Dinamo-Yantar volleyball team (Kaliningrad), Dinamo ice-hockey team (Moscow), and Torpedo ice-hockey team (Nizhny Novgorod).

For many years the Company has been general sponsor of the national ski-racing team and partner of the Russian Ski-Racing Federation. LUKOIL assists both in training of the national team and development of amateur ski sport in Russia. As part of its support to the Russian Olympic Movement the Company is cooperating with the Russian Olympic Support Foundation, which provides targeted support to sportsmen and women in Russian national teams practising Olympic sports.

LUKOIL also plays a major role in development of sport among children and young people. The Company has provided support since 2001 for one of Russia's biggest sports organizations, the Children's Football League. About 3,000 teams and 5,000 young footballers from all over Russia take part in League competitions each year. Since 2002 the Children's Football League has held an annual tournament under the title, 'LUKOIL International Children's League of Champions'. A special children's football competition was organized in 2010 jointly with sports clubs and organizations that are supported by the Company to celebrate the 65th anniversary of Victory in 1945.



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 successes and victories of LUKOIL Racing Team, which is the strongest car racing team in Russia, continue to prove the efficiency of the Company's fuels and lubricants.

BLOOD DONATION

IN 2010 LUKOIL INVITED ITS EMPLOYEES TO VOLUNTEER AS BLOOD DONORS AND ORGANIZED SESSIONS FOR THAT PURPOSE AT COMPANY PREMISES.

The first such action was carried out in April 2010, and 152 Company employees took part. A second action was carried out in December 2010 at the Company's central office, and was attended by 280 employees. The total amount collected was 170 liters, which was used to help patients of the Haematology Center of the Russian Academy of Medical Science. The action helps to address a pressing social problem, strengthens corporate culture and facilitates cohesion among the Company workers. LUKOIL plans to hold more such actions in the future.

THE LUKOIL MUSEUM

LUKOIL's museum network consists of LUKOIL Corporate Museum created in 2005 and more than 20 museums in Group organizations in various regions of Russia, and also in Ukraine, Bulgaria and Romania.

More than 15 travelling exhibitions were held in 2010 including 'LUKOIL in Africa', '80 years of the Gubkin Oil & Gas University', 'LUKOIL Charity Actions', '65 Years since Victory', 'We were young too', and 'Five years of LLK-International'. The exhibitions were displayed at the Company's central office and elsewhere. A stand presenting LUKOIL's history and current business was also presented at the European Business Summit in Brussels.

A LUKOIL section was included in the exhibition, 'From Soviet Electrification to 21st Century Innovation', which was held at the Central State Museum of Contemporary Russian History.

The LUKOIL Museum holds regular sessions with students of the Gubkin Oil & Gas University to study the history of the Russian oil industry.

7

CORPORATE GOVERNANCE
AND SECURITIES

CORPORATE GOVERNANCE



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'S CORPORATE GOVERNANCE SYSTEM ATTACHES SPECIAL IMPORTANCE TO PROTECTING THE RIGHTS OF MINORITY SHAREHOLDERS.

High quality of the Company's corporate governance system has been recognized by the investment community for over many years. In 2010 LUKOIL won the nomination for 'Company with Best Corporate Governance' in the annual competition, 'Russian Corporate Governance Leaders', organized by the Association for Protection of Investor Rights, which brings together some of the largest Russian and foreign institutional investors.

BOARD OF DIRECTORS AND MANAGEMENT COMMITTEE

BOARD OF DIRECTORS OF LUKOIL

The Board of Directors plays a crucial role in LUKOIL's system of corporate governance, exercising overall control of Company activities in the interests of investors and shareholders. In accordance with Russian legislation and the LUKOIL Charter, the Board of Directors defines priorities for Company development and ensures efficient functioning of the Company's executive bodies.

The Board of Directors of LUKOIL has 11 members who are elected by a cumulative vote of the General Meeting of Shareholders. Shareholders who own no less than 2% of voting shares in the Company have the right to propose candidates to the Board. Such proposals must be submitted to the Company not later than 30 days after the end of the financial year. The Board of Directors takes a decision on the final list of candidates during the last five days before the end of that period, usually by a vote in absentia. Members of the Board of Directors are elected until the next General Meeting of Shareholders and there is no limit on the number of times they can be re-elected.

In accordance with the Code of Corporate Conduct, which was recommended for adoption by companies by the Decree of the Federal Commission for the Securities Market on April 4, 2002, the Board of Directors of LUKOIL includes independent directors, whose presence enables the Board to formulate an objective opinion on matters discussed and therefore to strengthen confidence in the Company on the part of investors and shareholders. At the present time 7 of the 11 members of the Board of Directors are independent.

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, and specifically concerning: inclusion in the AGM agenda of issues related to any increase of LUKOIL's charter capital above 10% or issue of securities, which can be converted into more than 10% of the Company's outstanding shares, during any 12 month period; and approval of any transaction or any number of interrelated transactions amounting to more than 7.5% of consolidated non-core asset value.

The Board of Directors held 8 meetings in person during 2010 and carried out 17 votes in absentia. The Board of Directors dealt with the following matters in its competence during 2010:

- definition of Company business priorities, strategic, medium-term and annual planning, and review of business results
- in-depth study and design of specific measures for development of specific Group business segments
- improvement of corporate governance (approval of the LUKOIL Program for improvement of shareholder rights mechanisms in the period 2010–2014, and approval of performance criteria for the the Board of Directors and its committees)
- appointment of the Management Committee, selection of the external auditor
- preparations for holding the General Meeting of Shareholders
- approval of transactions with interest.



MEMBERS OF THE BOARD OF DIRECTORS OF LUKOIL



VALERY GRAYFER

Chairman of the LUKOIL Board of Directors
CEO of RITEK (1992 – January 2010), Chairman of the RITEK Board of Directors (from January 12, 2010)

Born 1929

Graduated in 1952 from the 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 President of the Russian Federation in 2009. Deputy to the USSR Oil Industry Minister, Head of the Tyumen Main Office for the Oil & Gas Industry (from 1985). CEO of RITEK (1992-2009); Chairman of the Board of Directors of RITEK (from 2010). Chairman of the Board of Directors of LUKOIL (from 2000). Professor of the 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, eight medals, and official thanks of the President of the Russian Federation. Winner of two Russian Government Prizes. Worked in the oil industry in Azerbaijan and Western Siberia (from 1968). CEO of Kogalymneftegaz (oil production company), a division of Glavtyumenneftegaz within the Ministry of the Oil & Gas Industry of the USSR (1987-1990). Deputy, then First Deputy to the USSR Oil & Gas Industry Minister (1990-1991). President of Langepasuraykogalymneft (oil production group) (1992-1993). Chairman of the Board of Directors of LUKOIL (1993-2000). President of LUKOIL (from 1993).

Elected to the LUKOIL Board of Directors since 1993.



IGOR BELIKOV

Independent Member of the Board of Directors of LUKOIL ¹
 Director of the Russian Institute of Directors (since 2002)
 Member of the HR and Remuneration Committee of the LUKOIL Board of Directors

Born 1956

Graduated in 1980 from Voronezh State University, post-graduate studies at the Africa Institute of the Academy of Sciences of the USSR, Candidate of Historical Science, completed a period of study at London University, Diploma in Banking and Insurance awarded by the Further Qualification Institute of the Financial Academy (attached to the Government of the Russian Federation), Audit Certificate and Corporate Governance Certificate from Schulich School of Business (York University, Toronto, Canada, 2002), Corporate Governance Consulting Certificate (Global Corporate Governance Forum, Washington, USA, 2008).

Director in the Russian Institute of directors since 2002. Co-author of the Russian Code of Corporate Conduct (2002) and of the first National Report on Corporate Governance (2004). Member of the Expert Council of the Federal Commission for the Securities Market (FCSM) (2002-2004). Executive Secretary of the National Council for Corporate Governance (2003-2004). Member of the Expert Council for Corporate Governance at the Federal Service for Financial Markets, Deputy Chairman of the College of the Association of Corporate Directors, member of the International Corporate Governance Network (ICGN) (from 2004). Expert on the Intergovernmental Group of Experts on International Accounting Standards of the UN Conference on Trade and Development (UNCTAD, Geneva) (2003-2006).

Elected to the Board of Directors of LUKOIL since 2008 (except the period from June 2009 to June 2010).



VIKTOR BLAZHEEV

Independent Member of the LUKOIL Board of Directors ¹
 Rector of the Kutafin Moscow State Academy of Law
 Member of the LUKOIL BoD Audit Committee

Born 1961

Graduated from the All-Union Correspondence-Study Law Institute (ACLI) in 1987; completed a post-graduate program at ACLI/Moscow Law Institute in the Civil Litigation Faculty 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 Department of the Moscow State Academy of Law (1999-2001). Vice-Rector of Moscow State Academy of Law in charge of academic agenda (2001-2002). First Vice-Rector of Moscow State Academy of Law in charge of academic agenda (2002-2007). Rector of Kutafin Moscow State Academy of Law (from 2007).

Elected to the LUKOIL Board of Directors since 2009.

¹ 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.



DONALD WALLETT JR

Independent Member of the LUKOIL Board of Directors ¹
 President of the Asia-Pacific Regional Division 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 (2002-2005). Vice-President for the Shtokman Project in the Russia/Caspian Region Division of ConocoPhillips (2005-2006). Russia/Caspian Region President of ConocoPhillips (December 2006 to August 2010). President of the Asia-Pacific Regional Division of ConocoPhillips (from September 2010).

Elected to the LUKOIL Board of Directors since 2007.



GERMAN GREF

Independent Member of the LUKOIL Board of Directors ¹
 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 (1998-2000). Minister of Economic Development and Trade of the Russian Federation (2000-2007). President, Chairman of the Executive Board of SBERBANK (Savings Bank of the Russian Federation) (from 2007).

Elected to the LUKOIL Board of Directors since 2009.

¹ 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.



IGOR IVANOV

Independent Member of the LUKOIL Board of Directors ¹
 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 (1993-1998). Minister of Foreign Affairs of the Russian Federation (1998-2004). Secretary of the Security Council of the Russian Federation (2004-2007).

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 & 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) (1988-1993). Vice-President of LUKOIL (1993-1994). First Vice-President of LUKOIL (1994-2006). First Executive Vice-President of LUKOIL (from 2006).

¹ 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.



SERGEY MIKHAILOV

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 Remuneration 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. Service in armed forces (1974-1992). Head of Section, Deputy Chairman of the Russian Federal Property Fund (1992-1996). Head of Restructuring and Investment Department of Ministry of Industry (1996-1997). CEO of Management-Center (management company) (1997-2003). CEO of the company Management-Consulting (from 2001 till February 28, 2011). CEO of Consulting group (since 2002). Chairman of the Board of Directors of Capital Unit Investment Funds (Management Company), Member of the Board of Russian Mediagroup, Spartak-Moscow Football Club, and Petrocommerce Commercial Bank (from 2004). Member of the Board of Directors of IFD Capital and of Izvestiya Newspaper Editorial (from 2005). Chairman of the Board of Directors of Capital Investment Group (2008-2009). Member of the Board of Directors of Capital Management Company (from 2008). Chairman of the Board of Directors of Capital Group Asset Management (from 2010).

Elected to the LUKOIL Board of Directors since 2003.



MARK MOEBIUS

Independent Member of the Board of Directors of LUKOIL ¹
 Executive President of Templeton Emerging Markets Group
 Member of the Strategy and Investment Committee of the Board of Directors

Born in 1936

Graduated from the Massachusetts Institute of Technology (USA) in 1964; Bachelors and Masters degrees. The University of Boston (USA). Doctor of Economic and Political Science. Executive President of Templeton Asset Management Ltd till August, 2010. Since August, 2010 Executive President of Templeton Emerging Markets Group, part of Franklin Templeton Investments (since 1987).

Elected to the Board of Directors of LUKOIL in 2002-2004 and since June 2010.

¹ 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 ¹
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 Remuneration Committee

Born in 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 the 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 (2002-2006). Member of the Public Chamber of the Russian Federation (2005-2009). President of the Russian Union of Industrialists and Entrepreneurs (from 2005). Member of the Competitiveness and Enterprise Council of the Prime Minister of Russia, member of Government Commissions for Administrative Reform, for Legislature, for Investment Projects of National Importance, and for High-Technology and Innovation.

Elected to the LUKOIL Board of Directors since 2005.

¹ 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.

COMMITTEES OF THE BOARD OF DIRECTORS

COMMITTEES OF THE BOARD OF DIRECTORS HAVE BEEN CREATED TO ENSURE EFFICIENT FUNCTIONING OF THE BOARD OF DIRECTORS, AS FOLLOWS: FOR STRATEGY AND INVESTMENTS; FOR AUDIT; AND FOR HR AND REMUNERATION. THE COMMITTEES CARRY OUT PRELIMINARY EXAMINATION OF MATTERS OF IMPORTANCE AND PREPARE RECOMMENDATIONS TO THE BOARD OF DIRECTORS.

STRATEGY AND INVESTMENT COMMITTEE

The Committee for Strategy and Investments prepares recommendations to the Board of Directors concerning strategy objectives for long-term Company development. The principal function of the Committee is to prepare recommendations on the following issues:

- 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

Members of the Strategy and Investments Committee are elected from among BoD members and are three in number. At least one member of the Committee must be independent, assuming presence of at least one independent member on the Board. Committee members are elected at a meeting of the newly elected Board of Directors for the period until election of the next Board of Directors by the General Meeting of Shareholders.

The Committee consists of Igor Ivanov (Chairman), Ravil Maganov, Mark Moebius and Donald Walette Jr.

AUDIT COMMITTEE

The Audit Committee analyzes the results of audit of the financial accounts of LUKOIL, carried out by external auditors, and prepares recommendations to the BoD for decisions on the following issues:

- selection of the candidate for external auditor of the Company
- assessment of the auditor's opinion
- assessment of the level of objectivity and independence of the Company auditor

Members of the Audit Committee are elected from among non-executive members of the Board of Directors of the Company and are at least three in number. At least one members of the Committee must be independent, assuming presence of at least one independent member on the Board. Committee members are elected at a meeting of the newly elected Board of Directors for the period until election of the next Board of Directors by the General Meeting of Shareholders.

The Committee consists of German Gref (Chairman), Sergei Mikhailov and Viktor Blazheev.

HR AND REMUNERATION COMMITTEE

The HR and Remuneration Committee has responsibility for the following issues:

- defining criteria for choice of candidates to the Board of Directors, Management Committee and the post of Company President
- preliminary assessment of candidates to the Management Committee and post of Company President
- preparing recommendations to the Board of Directors for decisions on HR issues and issues of remuneration to members of Company management bodies and of the Audit Commission

Members of the HR and Remuneration Committee are elected from among non-executive members of the Board of Directors of the Company and are at least three in number. At least one member of the Committee must be independent, assuming presence of at least one independent member on the Board. Committee members are elected at a meeting of the newly elected Board of Directors for the period until election of the next Board of Directors by the General Meeting of Shareholders.

The Committee consists of Alexander Shokhin (Chairman), Igor Belikov and Sergei Mikhailov.

PARTICIPATION BY MEMBERS OF THE BOARD OF DIRECTORS AT IN-PERSON MEETINGS OF THE BOARD OF DIRECTORS IN 2010¹

	Board of Directors
Valery Grayfer	8/8
Vagit Alekperov	8/8
Igor Belikov	5/5
Viktor Blazheev	8/8
Donald Wallette Jr	7/8
German Gref	7/8
Igor Ivanov	8/8
Ravil Maganov	8/8
Richard Matzke. (until June 24, 2010)	3/3
Sergei Mikhailov	8/8
Mark Moebius	5/5
Nikolai Tsvetkov (until June 24, 2010)	3/3
Alexander Shokhin	7/8

¹ In accordance with the resolution of the Board of Directors, for purposes of defining a quorum in conduct of a BoD meeting and voting results, the written opinion of an absent Board member concerning the agenda items, which is received by the Board Secretary before the start of the meeting, is taken into account. So a Board member who submits his written opinion before the start of the meeting is considered to have taken part in the meeting.

CODE OF CORPORATE CONDUCT

In August 2010 the Board of Directors of LUKOIL approved the new Code of Corporate Conduct of LUKOIL, which regulates the most important rules of conduct for Company business and its employees, ethical norms for intra-corporate relations and social responsibility.

Specifically, the document regulates the relationships of LUKOIL employees with investors and shareholders of the Company. The Code give special attention to disclosure of information, which could have significant impact on the Company share price (insider information). A special procedure is set out, which give an unambiguous definition of an 'insider', a list of insiders is to be constantly updated, and a special procedure for conduct of operations with shares of LUKOIL is prescribed for insiders. The Code also regulates conflicts of interest when an employee of LUKOIL could fail in his loyalty and objectivity with respect to the Company as a result of family and other connections. The conflict of personal interests with interests of the Company could have impact on Company performance in such instances, and the Company has the right to prevent such conflicts from arising.

A separate part of the Code is devoted to relationships between employees within the Company. The Code forbids discrimination against any employees on grounds of sex, race age, nationality, religion or political convictions.

The Code sets out rules to govern relationships with business partners, by which LUKOIL should establish and maintain a mutually beneficial relationship with any partners if those partners and the Company follow principles of mutual respect and mutual advantage, honesty and good faith, and strict observance of obligations. At the same time, the Company stands for fair competition and observance of all current laws on competition in all its countries of presence.

The Code also sets out rules for relationships with government bodies and social organizations, with special attention to health, safety and environment issues.

In accordance with the Code, a Commission for Business Ethics has been set up in the Company.

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. CEO of Kogalymneftegaz (oil production company), a division of Glavtyumenneftegaz within the Ministry of the Oil & Gas Industry of the USSR (1987-1990). Deputy, then First Deputy to the USSR Oil & Gas Industry Minister (1990-1991). President of Langepasuraykogalymneft (oil production group) (1992-1993). Chairman of the Board of Directors of LUKOIL (1993-2000). President of LUKOIL from 1993. Elected to the LUKOIL Board of Directors since 1993.

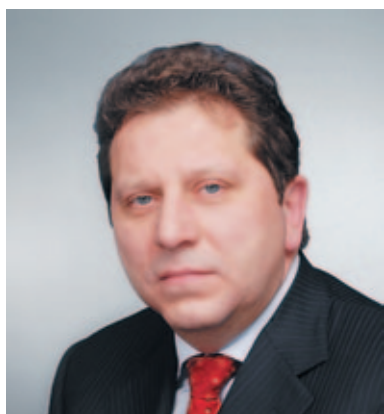


ANATOLY BARKOV

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 (1987-1992). Executive Director, then Director of the Department of Foreign Projects at Langepasuraykogalymneft (1992-1993). Vice-President, Head of the Main Division of General Affairs, Corporate Security and Communications of LUKOIL (from 1993).



VADIM VOROBEV

Member of the Management Committee of LUKOIL
Vice-President, Head of the Main Department for Petroleum Product Marketing of LUKOIL

Born 1961

Graduated in 1983 from Gorky State University (Nizhny Novgorod State University in 1998). Candidate of Economic Science. Awarded a medal, 'For services to Russia' (2nd grade). Komsomol and Communist Party work (1981-1992). Management positions in insurance and bank structures in Nizhny Novgorod (1992-1998). Vice-President, President of NORSI-OIL (1998-2002). CEO of LUKOIL-Volganefteprodukt (2002-2005). Vice-President of the Main Department for Coordination of Petroleum Product Sales in Russia (2005-2009). Vice-President, Head of the Main Department for Coordination of Petroleum Product Sales in Russia (from 2009).



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 (1992-1993). First Vice-President of LUKOIL (from 1993).



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. Chief Engineer, Deputy CEO, CEO of Langepasneftgaz (oil production company) (1988-1993). Vice-President of LUKOIL (1993-1994). First Vice-President of LUKOIL (1994-2006). First Executive Vice-President of LUKOIL (from 2006).



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 (1992-1993). Head of the LUKOIL Legal Department (1994-1999). Head of the Main Division of Legal Support at LUKOIL since 2000.



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, 'For services to Russia' (2nd grade). Director and CEO of international auditing firm KPMG (1994-1997). Vice-President, Head of the Main Division of Treasury and Corporate Finance of LUKOIL from 1997.



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 (1976-2001). Head of Human Resources Department of LUKOIL (2001-2003). Head of the Main Division of Human Resources at LUKOIL from 2003.



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. Doctor of Engineering, Doctoral Candidate in Geological and Mineral Sciences. Awarded a medal, 'For services to Russia' (2nd grade). Winner of a Russian Government Prize. Chief Engineer, Head of Lasyeganneft oil & gas production unit of LUKoil-Langepasneftegaz (1990-1996). First Deputy CEO for Production, CEO of 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) (1992-1999). Vice-President of LUKOIL and CEO of LUKOIL-Western Siberia (1999-2005). 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. Worked at LUKOIL-Prague, LUKOIL-Bulgaria, and the Moscow Representative Office of the company LITASCO., First Deputy Head of the Office of the Board of Directors of LUKOIL (2003-2005). First Deputy Head of the Main Division of Supplies and Sales of LUKOIL (2005-2007). Vice-President, Head of the Main Division of Supplies and Sales of LUKOIL (from 2007).



GENNADY FEDOTOV

Member of the LUKOIL Management Committee
Vice-President, Head of the Main Division for Economics and Planning of LUKOIL

Born 1970

Graduated from the Moscow Physics and Technology Institute in 1993. Worked at the companies Halliburton and Shell (1994-2002). Head of section, Deputy Head, Head of the Main Division for Corporate Budget and Economic Planning of LUKOIL (2002-2007). Vice-President, Head of the Main Division for Economics and Planning of LUKOIL (from 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 of Philosophy. Awarded an order and 7 medals. CEO of LUKoil Consulting (1993-1994). Vice-President and Head of Main Division of Strategic Development and Investment Analysis of LUKOIL (from 1994).

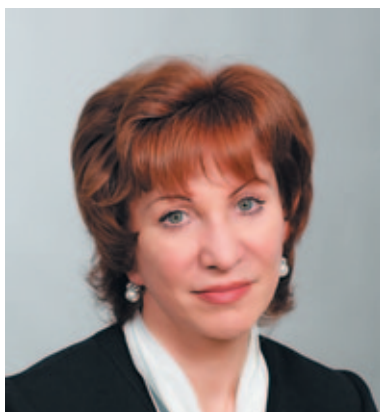


EVGUENY KHAVKIN

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 two medals. Worked in oil companies in Western Siberia (from 1988). Deputy Head, then First Deputy Head of the BoD Office of LUKOIL (1997-2003). BoD Secretary, Head of the BoD Office of LUKOIL (from 2003).



LYUBOV KHOBA

Member of the LUKOIL Management Committee
Chief Accountant of LUKOIL (until 25.08.2009, inclusively)

Born 1957

Graduated in 1992 from Sverdlovsk Institute of National Economy. Doctoral Candidate of Economics. Honored Economist of the Russian Federation. Awarded two medals and an order. Chief Accountant at Kogalymneftegaz (1991-1993). Chief Accountant at LUKOIL (1993-2000). Vice-President of LUKOIL, Head of Financial Accounting (2000-2003). Chief Accountant and Vice-President of LUKOIL (2003-2004). Chief Accountant of LUKOIL (2004 to August 25, 2009, inclusively).

■ **SHARES OF BOD AND MANAGEMENT COMMITTEE MEMBERS IN CHARTER CAPITAL,
AS OF DECEMBER 31, 2010 ¹**

BoD and Management Committee members	Stake, %
Vagit Alekperov	20.60 ²
Igor Belikov	-
Viktor Blazheev	-
Donald Wallyette, Jr	-
Valery Grayfer	0.007
German Gref	-
Igor Ivanov	-
Ravil Maganov	0.37
Sergei Mikhailov	0.04
Mark Moebius	-
Alexander Shokhin	-
Anatoly Barkov	0.07
Vadim Vorobev	0.006
Sergey Kukura	0.39
Ivan Masliaev	0.02
Alexander Matytsyn	0.30
Anatoly Moskalenko	0.01
Vladimir Mulyak	0.01
Vladimir Nekrasov	0.04
Valery Subbotin	0.005
Gennady Fedotov	0.001
Leonid Fedun	9.27 ²
Evgueny Khavkin	0.01
Lyubov Khoba	0.34

¹ Unless otherwise indicated, 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 TO MEMBERS OF THE BOARD OF DIRECTORS AND MANAGEMENT COMMITTEE

Each member of the Board of Directors was paid a remuneration of 4.47 million roubles in 2010 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, as defined by the AGM on 24 June 2004, in the amount of factually incurred and documentarily confirmed expenditures.

In the reporting 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 during the year, additional compensations of a social nature, and annual long-term premium payments in the framework of the long-term incentive program for employees of LUKOIL and its subsidiaries. Size of 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.

■ REMUNERATION PAID TO MANAGEMENT COMMITTEE AND BOD MEMBERS OF LUKOIL

	Paid in 2010, thousand roubles				
	Salary	Bonuses	Remuneration	Other payments	Total
Board of Directors ¹	–	–	58,738.0	5,644.0	64,382.0
Management Committee	452,294.0	430,488.8	32,862.0	21,544.8	937,189.6

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.

■ CHANGES IN GROUP STRUCTURE

The Program for restructuring of LUKOIL has been in progress since 2002. Its main purpose is to increase shareholder value by raising the level of transparency and efficiency of management processes, consolidating core subsidiaries and withdrawing non-core and inefficient assets from the Group.

Total value of shares and stakes in charter capital of subsidiaries and affiliates, which were withdrawn from the Group in 2010 was about \$113 million.

The most significant event in 2010 was complete exit by ConocoPhillips from the Company's share capital. In July 2010 a LUKOIL Group organization signed an agreement with a subsidiary of ConocoPhillips for acquisition from

the subsidiary of 64.6 million ordinary shares (7.6% of total shares) in LUKOIL at a price of \$53.25 apiece. Total value of the purchase was therefore \$3.4 billion. The transaction was completed in 2010. The agreement also included an option for acquisition until September 26, 2010 of remaining 98.7 million shares of LUKOIL (11.61%) in the form of depositary receipts. In September the Company partly exercised the option and purchased 42.5 million of its own shares in ADR form from ConocoPhillips jointly with a group of investors and UniCredit Bank. Value of the transaction was \$2.38 billion. ConocoPhillips sold its remaining shares in LUKOIL during the first quarter of 2011, so it has now completely exited share capital of the Company.

■ FINANCIAL MANAGEMENT

THE COMPANY USES A GLOBAL APPROACH TO FINANCIAL MANAGEMENT, REFLECTING THE SCALE AND GEOGRAPHICAL DIVERSITY OF ITS BUSINESS. THE SYSTEM FOR CENTRALIZED MANAGEMENT OF TREASURY OPERATIONS, WHICH WAS CREATED INSIDE THE COMPANY IN 2006, ENSURES EFFICIENT DISTRIBUTION OF CAPITAL AMONG GROUP ORGANIZATIONS.

Work continued in 2010 for improvement of the cash management system inside LUKOIL Group. Specifically, possibilities were reviewed for optimizing systems of cash management inside Russia, and a model was designed for calculation of the liquidity ratio in compliance with the method used by Standard & Poor's.

The first stage of a project for construction of a risk management system was completed in 2010, as a result of

which information on positions of LUKOIL organizations was collected and processed, and an assessment was made of vulnerability of LUKOIL Group to various types of risk.

The Company was able to provide sufficient level of liquidity and keep its cost of debt at best market levels in the reporting year, despite instability on international financial markets and adoption of tougher positions by creditors. This ensured smooth financing of LUKOIL Group business in full measure and to the schedules, which were laid down by Company management.

Specifically, more than \$4 billion of long-term loans were raised in 2010, which is an unprecedented sum in the history of the Group. At the same time, external debt of LUKOIL Group declined in comparison with 2009.

In August 2010 LUKOIL Group drew a club credit of \$1.5 billion for one year. The credit was arranged quickly and at the best market rate of LIBOR + 1.4% annualized. The money was used to finance repurchase of a share stake from ConocoPhillips.

In August 2010 the Company registered a program for issue of rouble bonds to the value of 100 billion roubles with 10-year maturity. This will enable LUKOIL to access capital markets in order to raise financing for long periods on optimal market terms.

In November 2010 the Company placed an issue of Eurobonds with value of \$1 billion for 10 years. Despite volatility on international capital markets the placement was carried out at a record-low coupon rate for a Russian company (6.125%). The money raised was used for refinancing of the Company's short-term debt.

IN DECEMBER 2010 LUKOIL ISSUED CONVERTIBLE BONDS TO THE VALUE OF \$1.5 BILLION FOR 4.5 YEARS, WITH COUPON RATE OF 2.625% ANNUALIZED. THE ACTION WAS THE LARGEST-EVER CONVERTIBLE BOND PLACEMENT BY A RUSSIAN ISSUER. APPLICATIONS FROM INVESTORS EXCEEDED THE PLACEMENT VOLUME BY FOUR TIMES, WHICH PROVES SUCCESS OF THE TRANSACTION AND THE HIGH DEGREE OF INVESTOR INTEREST IN THE COMPANY.

A pre-export credit of \$1.2 billion was repaid in 2010 ahead of time, saving \$100 million in interest expenses and reducing the share of secured debt in total Group debt from 16% to 4%.

INTERNAL CONTROL AND INTERNAL AUDIT

The system of internal 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.

There were 19 control and internal audit checks at LUKOIL Group organizations during 2010, spread over all business segments. 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 business of Group organizations and designing recommendations on ways to minimize 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
- ensuring safe-keeping of LUKOIL Group assets and their efficient use

Results of audit and control checks were submitted to the Company President, brought to the notice of heads of

subsidiaries, and of the Audit Committee of the Board of Directors of LUKOIL, in accordance with the established procedure.

Audit recommendations and management decisions were designed based on outcome of the checks in order to raise efficiency of Company business and minimize any risks, which had been identified. Based on these recommendations, subsidiaries and Group sub-divisions, which supervise the activity of subsidiaries, have designed measures to eliminate failures and violations that were identified by the internal audit process.

In order to ensure efficiency of its internal audit process, LUKOIL constantly monitors execution of decisions taken by the Company's governing bodies as a result of audits and execution of approved measures that have been designed on the basis of internal audit recommendations. Monitoring showed that 90.6% of such instructions were executed to schedule in 2010 (the level in 2009 was 93.3%).

The Company works constantly to organize and coordinate audit activity at LUKOIL Group organizations. Checks of financial and business activity during 2009 were

held at 73 Group organizations in the reporting year in order to ensure coordination of the activity of members of audit commissions, and preliminary candidates were nominated for election to the audit commissions of 70 Company subsidiaries and Naryanmarneftegas for 2010-2011 to be further approved by the Company's executive bodies.

The Company continued its work in 2010 to improve its risk management system. As part of this work tasks were defined in 2010 for creation of a risk management system that meets the latest criteria, and a LUKOIL draft policy for risk management was designed for subsequent consideration and approval by the Board of Directors.

A number of corporate transactions and investment projects of LUKOIL Group organizations were reviewed and approved during 2010 in order to ensure observance of the proper procedure for decision-making in matters that concern the interests of the Company and its shareholders. Opinions were prepared with respect to 11 substantial transactions, and materials were considered and opinions were issued with respect to 40 investment projects.

INFORMATION DISCLOSURE

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 THE SCALE AND EFFICIENCY OF INFORMATION DISCLOSURE 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
- conference calls and webcasts for the investment community to accompany publication of financial results and announcement of other important corporate events
- annual publication of international audit of Company hydrocarbon reserves
- 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
- regular meetings with investors and shareholders
- trips for representatives of the investment community to Company operating regions

THE COMPANY GAVE SPECIAL ATTENTION IN THE REPORTING YEAR TO MEETINGS WITH SHAREHOLDERS FOR PURPOSES OF IMPARTING INFORMATION. SUCH MEETINGS WERE HELD IN 2010 IN VOLGOGRAD, KALININGRAD, AND PERM. MATTERS DISCUSSED AT THE MEETINGS INCLUDED: RIGHTS AND DUTIES OF SHAREHOLDERS; DIVIDEND POLICY OF LUKOIL AND PROCEDURE FOR DIVIDEND PAYMENT; OWNERSHIP RIGHTS TO SHARES THAT ARE INHERITED; DETAILS OF HOW INHERITED DIVIDENDS CAN BE RECEIVED; CHANGES OF SHAREHOLDERS DETAILS IN THE REGISTER OF OWNERS OF SECURITIES; AND OBTAINING INFORMATION FROM THE SHAREHOLDER REGISTER.

Meetings with shareholders were carried out as part of the Program for improvement of shareholder rights mechanisms in the period 2010-2014, which was approved by the Board of Directors of LUKOIL on May 18, 2010. This Program calls for regular meetings with Company shareholders living in various regions of the Russian Federation and wider use of information technologies, and electronic means of communication with shareholders in order to ensure that they are better informed of their rights and the means of exercising those rights.

COMPANY SECURITIES

There was a process of consolidation on the market for Company shares in 2010. The sharp fall of the LUKOIL share prices in 2008 (-53.6%), caused by the international financial crisis, and the strong growth of capitalization in 2009 (+76.3%) was followed by a process of stabilization in 2010 as the world economy emerged from the acute stage of the crisis. LUKOIL remained among the most liquid securities on the Russian stock market during the year and its shares were included in calculation of all main stock indexes. Main venues for trading of Company shares remained the Moscow Inter-bank Currency Exchange (hereinafter 'MICEX') and the RTS Stock Exchange (hereinafter 'RTS'). The portions of LUKOIL shares, which were traded on these exchanges in 2010 were 6.5% and 5.87%, respectively.

One of the main factors determining price trends for Company shares in 2010 was the impact of information concerning changes in main shareholders (exit by ConocoPhillips from its position as a shareholder of LUKOIL). Shares were also influenced by Russian Government preparations for changes in the system of oil sector

taxation, as well as a sustained moderate upward trend throughout the year on the market for crude oil.

As well as impact from external factors, shares were also affected by intra-corporate developments. In particular measures were taken by LUKOIL in 2010 to improve corporate business efficiency and increase free cash flow, production began on the Caspian shelf, and projects were successfully implemented in West Africa, Iraq and Uzbekistan. Strength of company results has been acknowledged by sector experts, and the results are an excellent foundation for further growth of LUKOIL's capitalization in the future.

The LUKOIL share price rose by 2.16% in 2010 (based on MICEX trading) to a level of 1,732 roubles at the end of the reporting period (\$56.8). Growth of prices for Company shares in 2010 was somewhat below the rate of growth of all Russian oil & gas sector stocks (the MICEX oil & gas index rose by 17.6%) and that of the MICEX Index (23.2%).

LUKOIL SHARE PERFORMANCE ON THE MICEX IN 2010, roubles



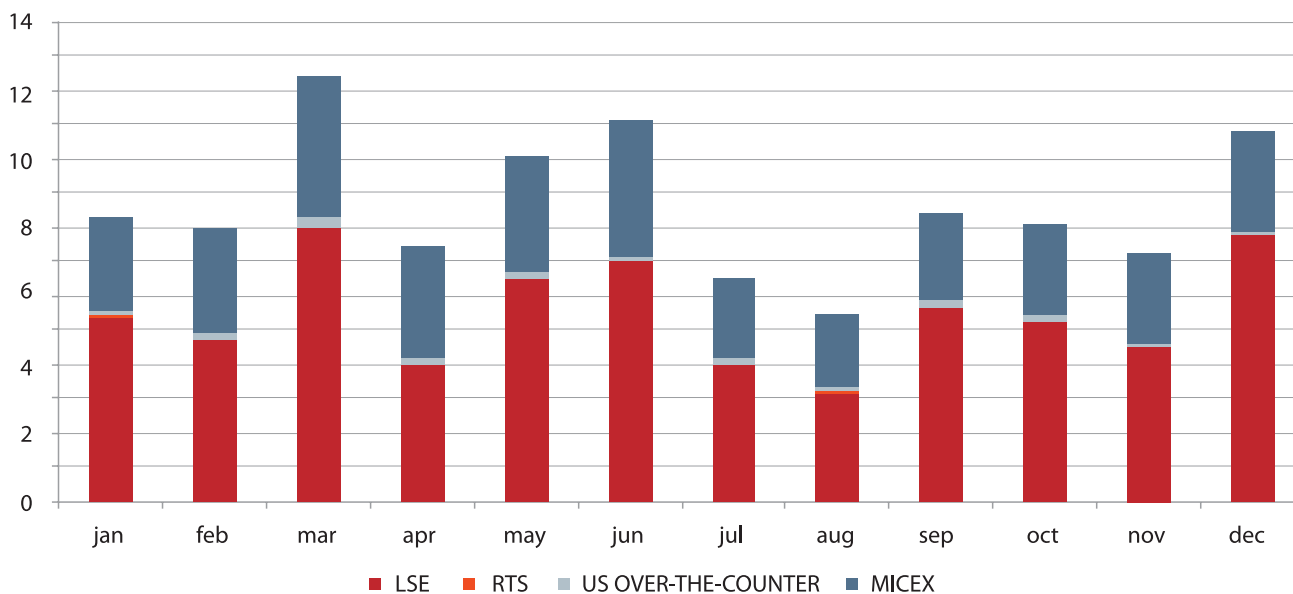
There was some decline in volumes of trading in LUKOIL shares on Russian exchanges in 2010 compared with 2009, but there was growth in volumes of trading on the London Stock Exchange in ADRs issued on Company shares. Depository certificates were also traded over-the-counter in the US and on other exchanges in London, Frankfurt, Munich and Stuttgart. By the end of the year the total number of ADRs issued on Company shares was equivalent to 563.99 million shares (66.31% of Company charter capital). LUKOIL ADR trading volumes on the main exchange outside Russia, where they are traded — the London Stock Exchange — increased by 13.2% to \$50.1 billion. LUKOIL ADRs were in second position by trading volumes among foreign companies listed on the IOB system of the LSE (16.2% of total monthly trading volumes in that system).

LUKOIL shares continued to be used as the base instrument for derivatives, which are traded on futures markets. Future and option contracts for delivery of LUKOIL shares are among the most popular trading instruments on the futures section of the RTS.

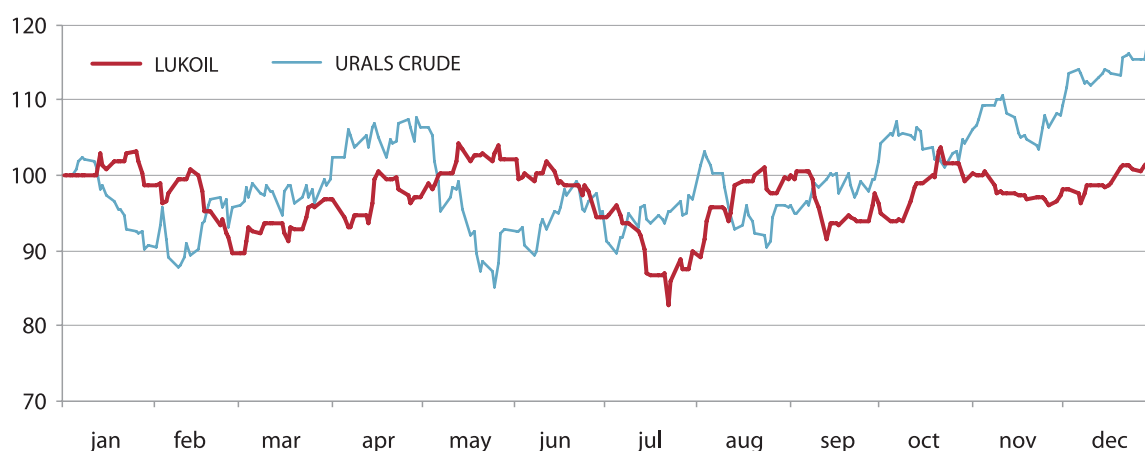
LUKOIL issued and placed two issues of Eurobonds at the end of 2010. The first issue of \$1 billion with repayment in 2020 was placed in November 2010. These bonds were issued in two simultaneous tranches (as a single issue). The first tranche with total value of \$800 million was placed at 99.08% of nominal value, with yield to maturity equal to 6.25% annualized. The second tranche of \$200 million was placed at 102.44% of nominal value with 5.80% yield to maturity. In December 2010 LUKOIL carried out placement of unsubordinated, unsecured convertible Eurobonds, repayable in June 2015. Bonds to the value of \$1.5 billion were placed with yield of 2.625% annualized.

LUKOIL made every effort in the reporting year to maintain and increase its shareholder value. Operating indicators were improved and a tight policy of cost management was implemented, as a result of which the Company achieved a record level of free cash flow. This enabled the Company to retain its attractiveness as an object for investment, despite instability in the world financial system.

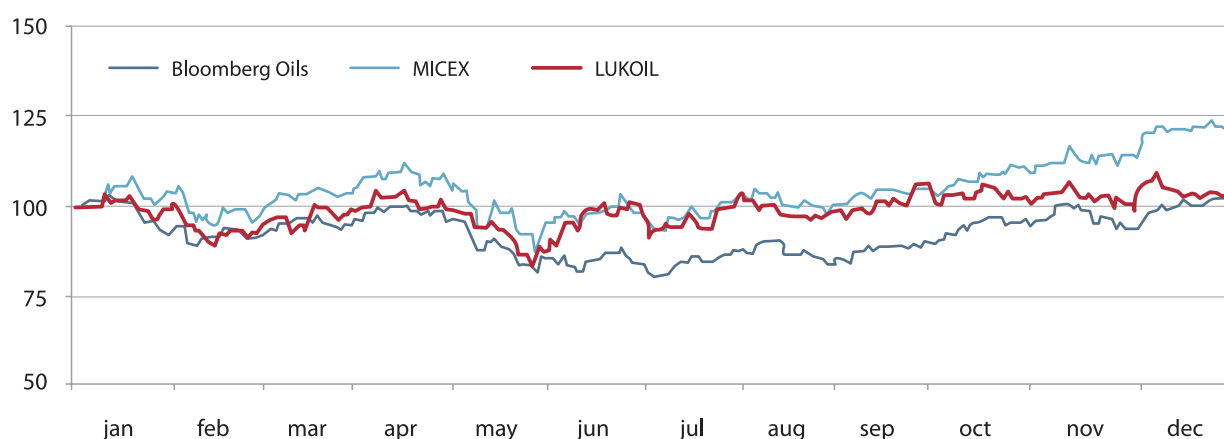
■ MONTHLY VOLUME OF TRADING IN SHARES (ADRS) OF LUKOIL IN 2010, \$ billion



■ LUKOIL SHARE PRICE ON MICEX COMPARED WITH URALS OIL PRICE IN 2010, %



■ LUKOIL SHARE PRICE COMPARED WITH BLOOMBERG OILS INDEX AND MICEX INDEX IN 2010, %



■ CHANGES IN OWNERSHIP STRUCTURE OF LUKOIL SHARE CAPITAL IN 2010

Main LUKOIL shareholders ¹ (> 1% of ordinary shares)

	Number of shares on January 1, 2010	% of total shares on January 1, 2010	Number of shares on January 1, 2011	% of total shares on January 1, 2011
ING Bank (Eurasia) ZAO	588,130,232	69.15%	645,159,254	75.85
Depository-Clearing Company	75,790,805	8.91%	69,483,048	8.17
National Depository Center	38,176,573	4.49%	52,526,643	6.18
SDK Garant	33,177,732	3.90%	33,411,404	3.93
DK URALSIB	13,574,885	1.60%	12,065,926	1.42

¹ Nominee.

■ 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 2010 ON RESULTS FOR 2009 WERE \$1,428 MILLION OR 20.4% OF CONSOLIDATED NET INCOME OF LUKOIL GROUP FOR 2009 UNDER US GAAP.

The Company decided in 2009 to steadily increase the share of dividends in net income from previously approved 15% to 30%. Dividend payments for 2010 will be increased in comparison with payments for 2009. On April 26, 2011 the Board of Directors recommended the Annual General Meeting of Shareholders to approve dividends for 2010 at a level of 59 roubles per share (\$1.94 at the exchange rate on December 31, 2010). So the share of dividends in consolidated net income of LUKOIL will be 18.3%. Dividend yield will be 3.5%. Basic earnings per share in 2010 were \$10.95 in comparison with \$8.28 in 2009.

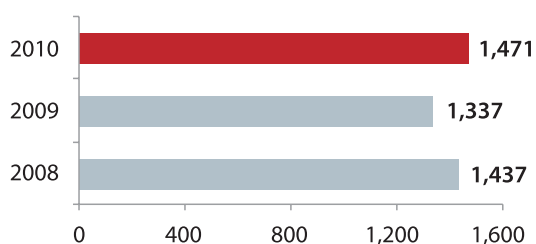
■ DIVIDENDS PER COMMON SHARE (ROUBLES) AND DIVIDEND YIELD (%)

	Dividend, roubles	Dividend yield, % ²
2006	38	1.77
2007	42	2.10
2008	50	2.38
2009	52	3.62
2010 ¹	59	3.52

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 ordinary shares (based on MICEX trading) and the exchange rate at the end of the year, for which the dividends are paid.

■ DIVIDENDS PAID ON ORDINARY SHARES OF THE COMPANY, \$ million



OAO "LUKOIL"

CONSOLIDATED FINANCIAL STATEMENTS

(prepared in accordance with US GAAP)

As of December 31, 2010 and 2009 and for each of the years in
the three-year period ended December 31, 2010



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10 Presnenskaya Naberezhnaya
Moscow, Russia 123317

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Fax +7 (495) 937 4400/99
Internet www.kpmg.ru

Independent Auditors' Report

The Board of Directors
OAO LUKOIL:

We have audited the accompanying consolidated balance sheets of OAO LUKOIL and subsidiaries as of December 31, 2010 and 2009, 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, 2010. These consolidated financial statements are the responsibility of the Company's management. 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 subsidiaries as of December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the years in the three year period ended December 31, 2010, in conformity with U.S. generally accepted accounting principles.

ZAO KPMG

ZAO KPMG
Moscow, Russian Federation
March 4, 2011

ZAO KPMG, a company incorporated under the Laws of the Russian Federation, a subsidiary of KPMG Europe LLP, and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

	Note	2010	2009
Assets			
Current assets			
Cash and cash equivalents	3	2,368	2,274
Short-term investments		168	75
Accounts receivable, net	5	8,219	5,935
Inventories	6	6,231	5,432
Prepaid taxes and other expenses		2,934	3,549
Other current assets		697	574
Total current assets		20,617	17,839
Investments	7	5,637	5,944
Property, plant and equipment	8, 9	54,629	52,228
Deferred income tax assets	13	676	549
Goodwill and other intangible assets	10	1,446	1,653
Other non-current assets		1,012	806
Total assets		84,017	79,019
Liabilities and Equity			
Current liabilities			
Accounts payable		5,607	4,906
Short-term borrowings and current portion of long-term debt	11	2,125	2,058
Taxes payable		2,099	1,828
Other current liabilities		944	902
Total current liabilities		10,775	9,694
Long-term debt	12, 16	9,069	9,265
Deferred income tax liabilities	13	2,417	2,080
Asset retirement obligations	8	1,788	1,189
Other long-term liabilities		360	412
Total liabilities		24,409	22,640
Equity	15		
OAO LUKOIL stockholders' equity			
Common stock		15	15
Treasury stock, at cost		(3,683)	(282)
Equity-linked notes		(980)	-
Additional paid-in capital		4,700	4,699
Retained earnings		59,212	51,634
Accumulated other comprehensive loss		(67)	(75)
Total OAO LUKOIL stockholders' equity		59,197	55,991
Non-controlling interests		411	388
Total equity		59,608	56,379
Total liabilities and equity		84,017	79,019

President of OAO LUKOIL

Alekperov V.Y.

Chief accountant of OAO LUKOIL

Kozyrev I.A.

	Note	2010	2009	2008
Revenues				
Sales (including excise and export tariffs)	22	104,956	81,083	107,680
Costs and other deductions				
Operating expenses		(7,969)	(7,124)	(8,126)
Cost of purchased crude oil, gas and products		(43,579)	(31,977)	(37,851)
Transportation expenses		(5,608)	(4,830)	(5,460)
Selling, general and administrative expenses		(3,558)	(3,306)	(3,860)
Depreciation, depletion and amortization		(4,154)	(3,937)	(2,958)
Taxes other than income taxes	13	(8,978)	(6,474)	(13,464)
Excise and export tariffs		(18,878)	(13,058)	(21,340)
Exploration expenses		(336)	(218)	(487)
Loss on disposals and impairments of assets		(363)	(381)	(425)
Income from operating activities		11,533	9,778	13,709
Interest expense		(712)	(667)	(391)
Interest and dividend income		174	134	163
Equity share in income of affiliates	7	472	351	375
Currency translation loss		(122)	(520)	(918)
Other non-operating income (expense)		125	(13)	(244)
Income before income taxes		11,470	9,063	12,694
Current income taxes		(2,104)	(1,922)	(4,167)
Deferred income taxes		(247)	(72)	700
Total income tax expense	13	(2,351)	(1,994)	(3,467)
Net income		9,119	7,069	9,227
Less: net income attributable to non-controlling interests		(113)	(58)	(83)
Net income attributable to OAO LUKOIL		9,006	7,011	9,144
Earnings per share of common stock attributable to OAO LUKOIL (US dollars):				
Basic	15	10.95	8.28	10.88
Diluted	15	10.94	8.28	10.88

	2010		2009		2008	
	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)		(282)		(1,591)	
Stock purchased	(3,664)		–		(219)	
Stock disposed	263		–		1,528	
Balance as of December 31	(3,683)		(282)		(282)	
Equity-linked notes						
Balance as of January 1	–		–		–	
Equity-linked notes purchased	(980)		–		–	
Balance as of December 31	(980)		–		–	
Additional paid-in capital						
Balance as of January 1	4,699		4,694		4,499	
Premium on non-outstanding shares issued	1		–		20	
Effect of stock compensation plan	98		20		103	
Convertible bonds issue	113		–		–	
Changes in non-controlling interests	(141)		(15)		–	
Treasury stock disposed	(70)		–		–	
Proceeds from sale of treasury stock in excess of carrying amount	–		–		72	
Balance as of December 31	4,700		4,699		4,694	
Retained earnings						
Balance as of January 1	51,634		45,983		38,349	
Net income	9,006	9,006	7,011	7,011	9,144	9,144
Dividends on common stock	(1,428)		(1,360)		(1,510)	
Balance as of December 31	59,212		51,634		45,983	
Accumulated other comprehensive loss, net of tax						
Balance as of January 1	(75)		(70)		(59)	
Pension benefits:						
Prior service cost	12	12	(4)	(4)	(5)	(5)
Actuarial (loss) gain	(4)	(4)	1	1	(6)	(6)
Unrecognized loss on available-for-sale securities	–	–	(2)	(2)	–	–
Balance as of December 31	(67)		(75)		(70)	
Total comprehensive income for the year		9,014		7,006		9,133
Total OAO LUKOIL stockholders' equity as of December 31	59,197		55,991		50,340	
Non-controlling interests						
Balance as of January 1	388		670		577	
Net income attributable to non-controlling interests	113		58		83	
Changes in non-controlling interests	(90)		(340)		10	
Balance as of December 31	411		388		670	
Total equity as of December 31	59,608		56,379		51,010	

The accompanying notes are an integral part of these consolidated financial statements

	Share activity		
	2010	2009	2008
	(thousands of shares)	(thousands of shares)	(thousands of shares)
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)	(3,836)	(23,321)
Purchase of treasury stock	(68,912)	-	(2,899)
Disposal of treasury stock	3,540	-	22,384
Balance as of December 31	(69,208)	(3,836)	(3,836)

	Note	2010	2009	2008
Cash flows from operating activities				
Net income attributable to OAO LUKOIL		9,006	7,011	9,144
Adjustments for non-cash items:				
Depreciation, depletion and amortization		4,154	3,937	2,958
Equity share in income of affiliates, net of dividends received		316	(213)	(238)
Dry hole write-offs		225	117	317
Loss on disposals and impairments of assets		363	381	425
Deferred income taxes		247	72	(700)
Non-cash currency translation gain		(44)	(57)	(668)
Non-cash investing activities		(67)	(20)	(29)
All other items — net		167	138	404
Changes in operating assets and liabilities:				
Trade accounts receivable		(2,285)	(1,171)	2,647
Inventories		(813)	(1,719)	963
Accounts payable		1,508	96	(989)
Taxes payable		274	292	(521)
Other current assets and liabilities		490	19	599
Net cash provided by operating activities		13,541	8,883	14,312
Cash flows from investing activities				
Acquisition of licenses		(15)	(40)	(12)
Capital expenditures		(6,596)	(6,483)	(10,525)
Proceeds from sale of property, plant and equipment		128	91	166
Purchases of investments		(137)	(216)	(398)
Proceeds from sale of investments		126	478	636
Sale of subsidiaries and equity method affiliates, net of cash disposed		130	92	3
Acquisitions of subsidiaries and equity method affiliates (including advances related to acquisitions), net of cash acquired		(932)	(2,473)	(3,429)
Net cash used in investing activities		(7,296)	(8,551)	(13,559)
Cash flows from financing activities				
Net movements of short-term borrowings		(213)	(1,281)	974
Cash received under sales-leaseback transaction		–	–	235
Proceeds from issuance of long-term debt		2,515	5,467	2,884
Principal repayments of long-term debt		(2,267)	(2,697)	(1,547)
Dividends paid on Company's stock		(1,471)	(1,337)	(1,437)
Dividends paid to non-controlling interest stockholders		(85)	(85)	(168)
Financing received from non-controlling interest stockholders		18	20	39
Purchase of Company's stock		(3,664)	–	(219)
Sale of Company's stock		193	–	–
Purchase of equity-linked notes		(980)	–	–
Purchases of non-controlling interests		(192)	(372)	–
Other – net		–	–	2
Net cash (used in) provided by financing activities		(6,146)	(285)	763
Effect of exchange rate changes on cash and cash equivalents		(5)	(12)	(118)
Net increase in cash and cash equivalents		94	35	1,398
Cash and cash equivalents at beginning of year		2,274	2,239	841
Cash and cash equivalents at end of year	3	2,368	2,274	2,239
Supplemental disclosures of cash flow information				
Interest paid		718	520	440
Income taxes paid		2,126	1,575	4,902

The accompanying notes are an integral part of these consolidated financial statements

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 the majority of operations in the Russian Federation and 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, 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, 2010, 2009 and 2008, exchange rates of 30.48, 30.24 and 29.38 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 receivable

Accounts 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

The cost of finished goods and purchased products is determined using the FIFO cost method. 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 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 con-

ditions 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 fair value 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 are expected to 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 (except those issued with interest rate lower than market value) 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 and the carrying amounts are adjusted as amortization accumulates.

For borrowings (including convertible notes) issued with interest rate lower than market interest rate, the Group determines book value using market interest rate. The resulting difference is allocated to additional paid-in capital and is amortized at a constant rate over the term of the borrowings. 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 the 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 December 2010, the FASB issued Accounting Standards Update ("ASU") No. 2010-29, *"Disclosure of Supplementary Pro Forma Information for Business Combinations."* This ASU requires that the pro forma information be presented as if the business combination occurred at the beginning of the prior annual reporting period for purposes of calculating both the current reporting period and the prior reporting period pro forma financial information. The ASU also requires that this disclosure be accompanied by a narrative description of the amount and nature of material nonrecurring pro forma adjustments. The ASU No. 2010-29 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010-29 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows presentation.

In December 2010, the FASB issued ASU No. 2010-28, *"When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts."* This ASU modifies Step 1 of the goodwill impairment test

for reporting units with zero or negative carrying amounts. As a result, ASU No. 2010-28 is eliminating an entity's ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative despite the existence of qualitative factors that indicate the goodwill is more likely than not impaired. Therefore, goodwill impairments may be reported sooner than under current practice. The ASU No. 2010-28 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010-28 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In July 2010, the FASB issued ASU No. 2010-20, *"Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses,"* which amends Accounting Standards Codification ("ASC") No. 310, *"Receivables."* This ASU provides financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables and requires entities provide disclosures that facilitate financial statement users' evaluation of the following: 1) the nature of credit risk inherent in the entity's portfolio of financing receivables; 2) how that risk is analyzed and assessed in arriving at the allowance for credit losses; 3) the changes and reasons for those changes in the allowance for credit losses. The ASU No. 2010-20 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010-20 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows and did not require additional disclosures.

In January 2010, the FASB issued ASU No. 2010-06, *"Improving Disclosures about Fair Value Measurements,"* which requires reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information about purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair-value measurements. This ASU also clarifies existing fair-value measurement disclosure guidance about the level of disaggregation, inputs, and valuation techniques. ASU No. 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for the detailed Level 3 roll forward disclosures (which are effective for the annual reporting periods starting after December 15, 2010 and for interim periods within those annual reporting periods). The Group adopted the requirements of ASU No. 2010-06 (except for the detailed Level 3 roll forward disclosures) starting from the first quarter of 2010. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows and did not require additional disclosures.

NOTE 3. CASH AND CASH EQUIVALENTS

	As of December 31, 2010	As of December 31, 2009
Cash held in Russian rubles	367	557
Cash held in other currencies	1,506	1,384
Cash of a banking subsidiary in other currencies	171	131
Cash held in related party banks in Russian rubles	320	174
Cash held in related party banks in other currencies	4	28
Total cash and cash equivalents	2,368	2,274

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:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Non-cash investing activity	67	20	29
Non-cash acquisitions	–	100	1,969
Total non-cash transactions	67	120	1,998

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

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Net cash used in investing activity	7,296	8,923	13,559
Non-cash acquisitions	–	100	1,969
Non-cash investing activity	67	20	29
Total investing activity	7,363	9,043	15,557

NOTE 5. ACCOUNTS RECEIVABLE, NET

	As of December 31, 2010	As of December 31, 2009
Trade accounts receivable (net of provisions of \$182 million and \$191 million as of December 31, 2010 and 2009, respectively)	6,748	4,389
Current VAT and excise recoverable	1,149	1,205
Other current accounts receivable (net of provisions of \$50 million and \$41 million as of December 31, 2010 and 2009, respectively)	322	341
Total accounts receivable, net	8,219	5,935

NOTE 6. INVENTORIES

	As of December 31, 2010	As of December 31, 2009
Crude oil and petroleum products	5,093	4,391
Materials for extraction and drilling	356	387
Materials and supplies for refining	37	37
Other goods, materials and supplies	745	617
Total inventories	6,231	5,432

NOTE 7. INVESTMENTS

	As of December 31, 2010	As of December 31, 2009
Investments in equity method affiliates and joint ventures	4,529	4,754
Long-term loans given by non-banking subsidiaries	1,092	1,176
Other long-term investments	16	14
Total long-term investments	5,637	5,944

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.

	Year ended December 31, 2010		Year ended December 31, 2009		Year ended December 31, 2008	
	Total	Group's share	Total	Group's share	Total	Group's share
Revenues	24,348	3,672	5,139	2,275	4,590	2,144
Income before income taxes	9,187	675	1,305	478	1,602	807
Less income taxes	(2,682)	(203)	(407)	(127)	(869)	(432)
Net income	6,505	472	898	351	733	375

	As of December 31, 2010		As of December 31, 2009	
	Total	Group's Share	Total	Group's Share
Current assets	7,462	1,359	6,796	1,524
Property, plant and equipment	18,053	5,099	18,877	5,284
Other non-current assets	989	350	607	240
Total assets	26,504	6,808	26,280	7,048
Short-term debt	701	57	442	274
Other current liabilities	2,844	551	3,982	817
Long-term debt	7,809	1,079	7,769	732
Other non-current liabilities	1,805	592	1,633	471
Net assets	13,345	4,529	12,454	4,754

In December 2009, a Group company acquired the remaining 46% 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 Kazakhstan 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 second installment in the amount of \$800 million was paid in December 2010; the remaining amount should be paid no later than December 2011. 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 S.A. to acquire a 45% interest in the TRN refinery in the Netherlands. The transaction was finalized in September 2009 in the amount of approximately \$688 million (after completion adjustment). 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 allowed 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.

NOTE 8. PROPERTY, PLANT AND EQUIPMENT AND ASSET RETIREMENT OBLIGATIONS

	At cost		Net	
	As of December 31, 2010	As of December 31, 2009	As of December 31, 2010	As of December 31, 2009
Exploration and Production:				
Western Siberia	26,137	23,465	15,260	13,878
European Russia	25,660	24,908	17,713	17,761
International	7,114	6,371	5,624	5,170
Total	58,911	54,744	38,597	36,809
Refining, Marketing, Distribution and Chemicals:				
Western Siberia	5	6	3	5
European Russia	11,057	10,009	7,205	6,717
International	6,883	6,849	4,511	4,783
Total	17,945	16,864	11,719	11,505
Other:				
Western Siberia	185	186	89	94
European Russia	4,404	4,170	3,881	3,697
International	440	189	343	123
Total	5,029	4,545	4,313	3,914
Total property, plant and equipment	81,885	76,153	54,629	52,228

The Company performs a regular annual impairment test of its assets. The test is based on geological models and development programs, which are revised on a regular basis at least annually. The fair value of tested assets is determined using the present value of the expected cash flows.

As a result of the test, during the year ended December 31, 2010, the Company recognized an impairment loss of \$164 million for its exploration and production assets in the Western Siberia, Timan-Pechora and Central European regions of Russia. During the year ended December 31, 2009, the Company recognized an impairment loss of \$238 million for its exploration and production assets in

the Timan-Pechora and Central European regions of Russia. During the year ended December 31, 2009, 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.

As of December 31, 2010 and 2009, the asset retirement obligations amounted to \$1,798 million and \$1,199 million, respectively, of which \$10 million was included in "Other current liabilities" in the consolidated balance sheets as of each balance sheet date. During 2010 and 2009, asset retirement obligations changed as follows:

	2010	2009
Asset retirement obligations as of January 1	1,199	728
Accretion expense	124	63
New obligations	190	146
Changes in estimates of existing obligations	314	311
Spending on existing obligations	(6)	(7)
Property dispositions	(4)	(13)
Foreign currency translation and other adjustments	(19)	(29)
Asset retirement obligations as of December 31	1,798	1,199

The asset retirement obligations incurred during 2010 and 2009 were Level 3 (unobservable inputs) fair value measurements.

NOTE 9. SUSPENDED WELLS

Net changes in capitalized exploratory suspended wells during 2010, 2009 and 2008 were as follows:

	2010	2009	2008
Balance as of January 1	406	337	216
Additions pending the determination of proved reserves	156	124	130
Charged to expenses	(94)	(36)	(9)
Reclassification to proved properties	(63)	(19)	-
Balance as of December 31	405	406	337

Aging of capitalized suspended exploratory well costs were as follows

	As of December 31, 2010	As of December 31, 2009	As of December 31, 2008
Exploratory well costs capitalized			
for a period of one year or less	213	124	125
for two years	7	122	88
for three years	89	86	61
for four years	82	58	49
for five years or more	14	16	14
for a period of greater than one year	192	282	212
Total exploratory well costs capitalized	405	406	337
Number of projects that have exploratory well costs capitalized for a period greater than one year	11	15	20

Aging of the exploratory wells that have been capitalized for more than one year since completion of drilling as of December 31, 2010:

Project name (field name)	Location	As of December 31, 2010	Years wells drilled
Block A	Saudi Arabia	154	2007-2008
Vinnikovskoe	European Russia	7	2008
Centralno-Astrakhanskoe	European Russia	6	2008-2009
Gabishevskoe	European Russia	5	2008-2009
Shiriaevskoe	European Russia	4	2004-2005
6 projects of less than \$4 million each	European Russia	16	2005-2009
Total of 11 projects		192	

The Company is currently evaluating the development plans for these projects.

NOTE 10. GOODWILL AND OTHER INTANGIBLE ASSETS

The carrying value of goodwill and other intangible assets as of December 31, 2010 and 2009 was as follows:

	As of December 31, 2010	As of December 31, 2009
Amortized intangible assets		
Software	391	419
Licenses and other assets	409	465
Goodwill	646	769
Total goodwill and other intangible assets	1,446	1,653

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

In December 2010, the Group recognized an impairment loss of \$114 million relating to goodwill on the acquisition of the Akpet group due to a change in market conditions partly caused by legislative changes. The fair value was determined based on a present value technique (Level 3 fair value measurements). The Akpet group operates petrol

filling stations on the basis of dealer agreements and owns eight refined product terminals, five LNG storage tanks, three jet fuel terminals and a lubricant production plant in Turkey. There were other minor changes in goodwill relating to the disposition of assets.

NOTE 11. SHORT-TERM BORROWINGS AND CURRENT PORTION OF LONG-TERM DEBT

	As of December 31, 2010	As of December 31, 2009
Short-term borrowings from third parties	728	442
Short-term borrowings from related parties	66	77
13.5% Russian ruble bonds	–	496
Current portion of long-term debt	1,331	1,043
Total short-term borrowings and current portion of long-term debt	2,125	2,058

Short-term borrowings from third parties are unsecured and include amounts repayable in US dollars of \$609 million and \$282 million, amounts repayable in Euros of \$29 million and \$76 million, amounts repayable in Russian rubles of nil and \$18 million and amounts repayable in other currencies of \$90 million and \$66 million as of December 31, 2010 and 2009, respectively. The weighted-average interest rate on short-term borrowings from third parties was 1.87% and 2.02% per annum as of December 31, 2010 and 2009, 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. The bonds were placed at their face value with a maturity of 364 days. The coupon yield was 13.5% per annum and was paid at the maturity date. In June 2010, the Company redeemed all issued bonds in accordance with the conditions of the bond issue.

NOTE 12. LONG-TERM DEBT

	As of December 31, 2010	As of December 31, 2009
Long-term loans and borrowings from third parties (including loans from banks in the amount of \$2,071 million and \$3,967 million as of December 31, 2010 and 2009, respectively)	3,764	4,043
Long-term loans and borrowings from related parties	–	1,939
6.375% non-convertible US dollar bonds, maturing 2014	896	895
2.625% convertible US dollar bonds, maturing 2015	1,388	–
6.356% non-convertible US dollar bonds, maturing 2017	500	500
7.250% non-convertible US dollar bonds, maturing 2019	595	595
6.125% non-convertible US dollar bonds, maturing 2020	998	–
6.656% non-convertible US dollar bonds, maturing 2022	500	500
7.10% Russian ruble bonds, maturing 2011	262	265
13.35% Russian ruble bonds, maturing 2012	820	827
9.20% Russian ruble bonds, maturing 2012	328	331
7.40% Russian ruble bonds, maturing 2013	197	198
Capital lease obligations	152	215
Total long-term debt	10,400	10,308
Current portion of long-term debt	(1,331)	(1,043)
Total non-current portion of long-term debt	9,069	9,265

Long-term loans and borrowings

Long-term loans and borrowings from third parties include amounts repayable in US dollars of \$1,707 million and \$3,493 million, amounts repayable in Euros of \$369 million and \$487 million, amounts repayable in Russian rubles of \$1,667 million (including loans from ConocoPhillips) and \$42 million, and amounts repayable in other currencies of \$21 million and \$21 million as of December 31, 2010 and 2009, respectively. This debt has maturity dates from 2011 through 2038. The weighted-average interest rate on long-term loans and borrowings from third parties was 4.50% and 2.77% per annum as of December 31, 2010 and 2009, respectively. The weighted-average interest rate on long-term loans and borrowings from third parties, excluding ConocoPhillips, which ceased to be a related party of the Group by the end of the third quarter of 2010, was 1.92% per annum as of December 31, 2010.

A number of long-term loan agreements contain certain financial covenants which are being met by the Group. Approximately 8% of total long-term loans and borrowings from third parties are secured by export sales and property, plant and equipment.

A Group company has an unsecured syndicated loan agreement with an outstanding amount of \$720 million as of December 31, 2010, 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 \$212 million as of December 31, 2010, maturing in 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 \$221 million as of December 31, 2010, 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 \$158 million as of December 31, 2010. 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 \$121 million as of December 31, 2010, maturing up to 2019. Borrowings under this agreement bear interest at euribor plus 0.125% per annum.

A Group company has an unsecured loan agreement with Citibank with an outstanding amount of \$100 million as of December 31, 2010, maturing in 2011. Borrowings under this agreement bear interest at one month LIBOR plus 0.90% per annum.

As of December 31, 2010, the Group has a number of other loan agreements with fixed rates with a number of banks and other organizations totaling \$133 million, maturing from 2011 to 2017. The weighted average interest rate under these loans was 3.98% per annum.

As of December 31, 2010, the Group has a number of other floating rate loan agreements with a number of banks and other organizations totaling \$442 million, maturing from 2011 to 2018. The weighted average interest rate under these loans was 1.18% per annum.

Group companies have a number of loan agreements nominated in Russian rubles with ConocoPhillips, the Group's former related party, with an outstanding amount of \$1,657 million as of December 31, 2010. This amount includes \$1,424 million loaned by ConocoPhillips to our joint venture OOO Narianmarneftegaz ("NMNG") (refer to Note 18. Consolidation of Variable Interest Entity). Borrowings under these agreements bear interest at fixed rates ranging from 6.8% to 8.0% per annum and have maturity dates up to 2038. Financing under these agreements is used to develop oil production and distribution infrastructure in the Timan-Pechora region of the Russian Federation.

US dollar convertible bonds

In December 2010, a Group company issued unsecured convertible bonds totaling \$1.5 billion with a coupon yield of 2.625% and maturity in June 2015. The bonds were placed at face value. The bonds are convertible into LUKOIL ADRs (each representing one ordinary share of the Company) and have a conversion price of \$73.7087 per ADR. Bondholders have the right to convert the bonds into LUKOIL ADRs during the period starting from 40 days after the issue date and ending 6 dealing days before the maturity date. The issuer has the right to redeem the bonds after December 31, 2013.

US dollar non-convertible bonds

In November 2010, a Group company issued two tranches of non-convertible bonds totaling \$1.0 billion with a coupon yield of 6.125% and maturity in 2020. The first tranche totaling \$800 million was placed at a price of 99.081% of

the bond's face value with a resulting yield to maturity of 6.250%. The second tranche totaling \$200 million was placed at a price of 102.44% of the bond's face value with a resulting yield to maturity of 5.80%. These tranches have a half year coupon period.

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 with a resulting yield to maturity of 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 with a resulting yield to maturity of 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. The 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. The 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 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.

Maturities of long-term debt

Annual maturities of total long-term debt during the next five years, including the portion classified as current, are \$1,331 million in 2011, \$1,556 million in 2012, \$645 million in 2013, \$1,069 million in 2014, \$1,548 million in 2015 and \$4,251 million thereafter.

NOTE 13. 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.

Starting on January 1, 2009, operations in the Russian Federation are subject to a Federal income tax rate of 2.0% and a regional income tax rate that varies from 13.5% to 18.0% at the discretion of the individual regional administration. Until January 1, 2009, the Federal income tax rate was 6.5% and regional income tax rate varied from 13.5% to 17.5%. 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, 2010 and 2009, and during 2010, 2009 and 2008, 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 tax years beginning in 2008.

There are not currently, and have not been during the three years ended December 31, 2010, 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:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Domestic	10,569	9,013	12,767
Foreign	901	50	(73)
Income before income taxes	11,470	9,063	12,694

Domestic and foreign components of income taxes were:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Current			
Domestic	1,693	1,677	3,614
Foreign	411	245	553
Current income tax expense	2,104	1,922	4,167
Deferred			
Domestic	299	98	(523)
Foreign	(52)	(26)	(177)
Deferred income tax expense (benefit)	247	72	(700)
Total income tax expense	2,351	1,994	3,467

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:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Income before income taxes	11,470	9,063	12,694
Notional income tax at the Russian statutory rate (20% for the years 2010 and 2009, and 24% for 2008)	2,294	1,813	3,047
Increase (reduction) in income tax due to:			
Non-deductible items, net	266	252	792
Foreign rate differences	(4)	68	159
Effect of enacted tax rate changes	-	-	(299)
Domestic regional rate differences	(226)	(251)	(261)
Change in valuation allowance	21	112	29
Total income tax expense	2,351	1,994	3,467

Taxes other than income taxes were:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Mineral extraction tax	7,864	5,452	12,267
Social taxes and contributions	429	399	512
Property tax	518	470	405
Other taxes and contributions	167	153	280
Taxes other than income taxes	8,978	6,474	13,464

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

	As of December 31, 2010	As of December 31, 2009
Other current assets	77	66
Deferred income tax assets — non-current	676	549
Other current liabilities	(85)	(50)
Deferred income tax liabilities — non-current	(2,417)	(2,080)
Net deferred income tax liability	(1,749)	(1,515)

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, 2010	As of December 31, 2009
Accounts receivable	42	42
Long-term liabilities	387	295
Inventories	1	5
Property, plant and equipment	263	209
Accounts payable	14	28
Operating loss carry forwards	527	555
Other	161	132
Total gross deferred income tax assets	1,395	1,266
Less valuation allowance	(418)	(397)
Deferred income tax assets	977	869
Property, plant and equipment	(2,513)	(2,189)
Accounts payable	(2)	(6)
Accounts receivable	(30)	(7)
Long-term liabilities	(61)	(58)
Inventories	(57)	(68)
Investments	(15)	(16)
Other	(48)	(40)
Deferred income tax liabilities	(2,726)	(2,384)
Net deferred income tax liability	(1,749)	(1,515)

As a result of acquisitions during 2009 the Group recognized a net deferred tax liability of \$35 million.

As of December 31, 2010, retained earnings of foreign subsidiaries included \$17,777 million for which deferred taxation has not been provided because remittance of the earnings has been indefinitely postponed through re-investment 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, "Foreign currency matters" and ASC No. 740, "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 ruble 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, 2010 and 2009.

As of December 31, 2010, the Group had operating loss carry forwards of \$2,073 million of which \$3 million expire during 2011, \$203 million expire during 2012, \$444 million expire during 2013, \$14 million expire during 2014, \$1 million expire during 2015, \$389 million expire during 2016, \$40 million expire during 2017, \$6 million expire during 2018, \$15 million expire during 2019, \$15 million expire during 2020, \$374 million expire during 2021, \$5 million expire during 2025, \$67 million expire during 2026, \$77 million expire during 2027, \$107 million expire during 2028, \$60 million expire during 2029, \$64 million expire during 2030, and \$187 million have an indefinite carry forward.

NOTE 14. 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 a 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% of annual salary up to October 1, 2010 and up to 4% of annual salary in further periods). 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, 2010 and 2009. 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, 2010 and 2009.

The following table provides information about the benefit obligations and plan assets as of December 31, 2010 and 2009. The benefit obligations below represent the projected benefit obligation of the pension plan.

	2010	2009
Benefit obligations		
Benefit obligations as of January 1	291	288
Effect of exchange rate changes	(2)	(7)
Service cost	16	17
Interest cost	23	23
Plan amendments	6	6
Actuarial loss (gain)	2	(3)
Acquisitions	3	8
Benefits paid	(40)	(30)
Curtailement gain	(3)	(11)
Benefit obligations as of December 31	296	291
Plan assets		
Fair value of plan assets as of January 1	108	88
Effect of exchange rate changes	(1)	(1)
Return on plan assets	6	12
Employer contributions	39	45
Divestiture	-	(6)
Benefits paid	(40)	(30)
Fair value of plan assets as of December 31	112	108
Funded status	(184)	(183)
Amounts recognized in the consolidated balance sheet as of December 31, 2010 and 2009		
Accrued benefit liabilities included in "Other long-term liabilities"	(144)	(143)
Accrued benefit liabilities included in "Other current liabilities"	(40)	(40)

Weighted average assumptions used to determine benefit obligations as of December 31, 2010 and 2009:

	2010	2009
Discount rate	7.80%	8.70%
Rate of compensation increase	7.70%	8.10%

Weighted average assumptions used to determine net periodic benefit costs for the year ended December 31, 2010 and 2009:

	2010	2009
Discount rate	8.70%	9.00%
Rate of compensation increase	8.10%	8.61%
Expected rate of return on plan assets	10.07%	10.89%

Included in accumulated other comprehensive loss as of December 31, 2010 and 2009, are the following before-tax amounts that have not yet been recognized in net periodic benefit cost:

	2010	2009
Unamortized prior service cost	84	96
Unrecognized actuarial gain	(6)	(10)
Total costs	78	86

Amounts recognized in other comprehensive loss during the year ended December 31, 2010 and 2009:

	2010	2009
Additional loss (gain) arising during the period	4	(5)
Additional prior service cost from plan amendment	6	6
Re-classified prior service cost amortization	(18)	(2)
Net amount recognized for the period	(8)	(1)

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, 2010	As of December 31, 2009
Promissory notes of Russian issuers	–	3%
Russian corporate bonds	37%	25%
Russian municipal bonds	2%	4%
Bank deposits	41%	42%
Equity securities of Russian issuers	5%	8%
Shares of OAO LUKOIL	1%	2%
Shares in investment funds	13%	14%
Other assets	1%	2%
	100%	100%

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 with low and medium risk ratings. Maturities range from one to three years.

Components of net periodic benefit cost were as follows:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Service cost	16	17	22
Interest cost	23	23	19
Less expected return on plan assets	(11)	(10)	(11)
Amortization of prior service cost	18	2	11
Curtailement gain	(3)	(11)	–
Total net periodic benefit cost	43	21	41

Total employer contributions for 2011 are expected to be \$32 million. An amount of \$14 million before-tax is included in other comprehensive income and expected to be recognized in the net periodic benefit cost in 2011.

The following benefit payments, which reflect expected future services, as appropriate, are expected to be paid:

	2011	2012	2013	2014	2015	5-year period 2011-2015	5-year period 2016-2020
Pension benefits	55	15	10	10	9	99	28
Other long-term employee benefits	40	16	15	14	13	98	56
Total expected benefits to be paid	95	31	25	24	22	197	84

NOTE 15. STOCKHOLDERS' EQUITY

Common stock

	As of December 31, 2010 (thousands of shares)	As of December 31, 2009 (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)
Treasury stock	(69,208)	(3,836)
Outstanding common stock	781,355	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 139,853 million Russian rubles, 45,148 million Russian rubles and 66,926 million Russian rubles respectively for 2010, 2009 and 2008, pursuant to the statutory financial statements, which at the US dollar exchange rates as of December 31, 2010, 2009 and 2008, amounted to \$4,589 million, \$1,493 million and \$2,278 million, respectively.

At the annual stockholders' meeting on June 24, 2010, dividends were declared for 2009 in the amount of 52.00 Russian rubles per common share, which at the date of the meeting was equivalent to \$1.68. Dividends payable of \$13 million are included in "Other current liabilities" in the consolidated balance sheets as of December 31, 2010 and 2009.

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 decision was equivalent to \$1.78.

Earnings per share

The calculation of diluted earnings per share for these years was as follows:

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Net income	9,006	7,011	9,144
Add back interest on 2.625% convertible US dollar bonds, maturing 2015 (net of tax at effective rate)	3	–	–
Total diluted net income	9,009	7,011	9,144
Weighted average number of outstanding common shares (thousands of shares)	822,359	846,646	840,108
Add back treasury shares held in respect of convertible debt (thousands of shares)	892	–	–
Weighted average number of outstanding common shares, after dilution (thousands of shares)	823,251	846,646	840,108

Treasury shares

On July 28, 2010, a Group company signed a stock purchase agreement with a ConocoPhillips' subsidiary to purchase 64.6 million of the Company's ordinary shares at \$53.25 per share for the total amount of \$3,442 million. This transaction was finalized in August 2010. Additionally, under this agreement the Group had a 60-day option to purchase any or all of the remaining 98.7 million of the Company's ordinary shares held by the ConocoPhillips' subsidiary for the price of \$56 per share.

On September 26, 2010, the Group company exercised its option to acquire shares from the ConocoPhillips' subsidiary by sending a notice of exercise in respect of 42,500,000 LUKOIL ADRs (each representing one ordinary share of the Company). The Group company sold these ADRs to UniCredit Bank AG. These transactions were completed on September 29, 2010 when 42,500,000 LUKOIL ADRs were directly transferred to UniCredit Bank AG, and UniCredit Bank AG paid the purchase price of \$2.38 billion to the ConocoPhillips' subsidiary.

Simultaneously, UniCredit Bank AG issued a series of equity-linked notes to the Group company that are redeemable for 17,500,000 LUKOIL ADRs on or before September 29, 2011. These equity-linked notes have been classified within OAO LUKOIL stockholders' equity.

UniCredit Bank AG also issued an option to the Group company to purchase from UniCredit Bank AG an additional 25,000,000 LUKOIL ADRs on or before September 29, 2011. The option provides for the purchase of LUKOIL ADRs at market price with a floor of \$56 per ADR and is not valid if the market price per ADR is \$50 or below. This option currently has a fair value of zero.

A related party of the Group has equity-linked notes that are redeemable for 25,000,000 LUKOIL ADRs on or before September 29, 2011 should the Group company not exercise its option or the option becomes invalid. If the Group company exercises the option the related party will receive from UniCredit Bank AG the cash value of ADRs equivalent to that paid by the Group company.

NOTE 16. FINANCIAL AND DERIVATIVE INSTRUMENTS

Fair value

The fair values of cash and cash equivalents, current accounts 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, 2010 and 2009 was \$10,225 million and \$9,976 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, 2010, 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 hedge accounting, defined by ASC No. 815, "Derivative and hedging," 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, 2010				As of December 31, 2009			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Commodity derivatives	-	226	-	226	-	341	-	341
Total assets	-	226	-	226	-	341	-	341
Liabilities								
Commodity derivatives	-	(264)	-	(264)	-	(386)	-	(386)
Total liabilities	-	(264)	-	(264)	-	(386)	-	(386)
Net liabilities	-	(38)	-	(38)	-	(45)	-	(45)

The derivative values above are based on an analysis of each contract as the fundamental unit of account as required by ASC No. 820, "Fair Value Measurements and Disclosures;" 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, 2010 was:

	As of December 31, 2010
Assets	
Accounts receivable	224
Liabilities	
Accounts payable	264

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 \$26 million and accounts payable in the amount of \$66 million.

Financial results 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, 2010 and 2009 amounted to a net loss of \$232 million (of which realized losses were \$235 million and unrealized gain was \$3 million) and a net loss of \$781 million (of which realized losses were \$406 million and unrealized losses were \$375 million), respectively.

As of December 31, 2010, 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, 2010 was not significant.

The impact from foreign currency derivatives during the year ended December 31, 2010 on the consolidated income statement was not significant. The net position of outstanding foreign currency swap contracts as of December 31, 2010 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.

There were no derivative instruments with such credit-risk-related contingent features that were in a liability position on December 31, 2010. The Group posted \$3 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, 2010, 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 \$16 million in total.

NOTE 17. BUSINESS COMBINATIONS

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. 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.

This business combination did not have a material impact on the Group's consolidated operations for the year ended December 31, 2009. Therefore, no pro-forma income statement information has been provided.

NOTE 18. 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 originally 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 former related party. Based on the requirements of ASC No. 810, "Consolidation" the Group performs a regular qualitative analysis as to whether it is the primary beneficiary of this VIE. As a result the Group is still considered to be the primary beneficiary of NMNG and consolidated it.

NMNG's total assets were approximately \$5.5 billion and \$5.9 billion as of December 31, 2010 and 2009, respectively.

NOTE 19. COMMITMENTS AND CONTINGENCIES

Capital expenditure, exploration and investment programs

Under the terms of existing exploration and production license agreements in Russia the Group has to fulfill certain obligations: 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 \$720 million related to various production sharing agreements over the next 27 years.

The Company has signed a three-year agreement for the years 2010-2012 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 2011 to be approximately \$1,139 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 2011 to be approximately \$349 million.

The Group has a commitment to execute the capital construction program of its power generation segment and under the terms of this program power plants with a total capacity of 890 MW should be constructed. Currently the Group is approving certain amendments to the capital construction program, including its extension by the end of 2013. As of December 31, 2010, the Group estimates the amount of this commitment to be approximately \$660 million.

Operating lease obligations

Group companies have commitments of \$846 million primarily for the lease of vessels and petroleum distribution outlets. Operating lease expenses were \$155 million and \$185 million during the years ended December 31, 2010 and 2009, respectively. Commitments for minimum rentals under these leases as of December 31, 2010 are as follows:

	As of December 31, 2010
2011	220
2012	168
2013	130
2014	110
2015	100
beyond	118

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 differ-

ing 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 \$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 to the Bankruptcy Court and requesting the case be heard by the 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 were stayed pending further order of the Court. On July 7, 2010, the District Court denied ADC's Motion for Withdrawal of reference and returned the case to the Bankruptcy Court for the determination of the Company's Motion for Remand and Abstention seeking return of the case to the Colorado state court. On October 28, 2010, the Bankruptcy Court granted the Company's Motion for Remand and Abstention and remanded the case to the Denver District Court (Colorado state court) where it is now pending. ADC is expected to commence discovery regarding general jurisdiction shortly after the Court holds a status conference on March 18, 2011. Management intends to contest jurisdiction and denies all material allegations against the Company. Management does not believe that the ultimate resolution of this matter will have a material adverse effect on the Group's financial condition.

As of the date the financial statements were available to be issued 76 claims in relation to a violation of the anti-monopoly regulation were initiated against several Group companies in Russia and abroad. The Group companies were accused of violations primarily involving abuse of their dominant market position and execution of coordinated actions in oil products retail markets.

In 2008 and 2009, the Federal Anti-monopoly Service of the Russian Federation ("FAS of Russia") considered two cases which resulted in decisions being issued against a number of 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.

As for the first case, the Group refinery plants appealed the decisions of FAS of Russia in the Moscow Arbitration Court. These appeals were combined in one proceeding. In addition the Group's refinery plants appealed against the administrative fines accrued by FAS of Russia to the courts in their locations. Due to abandonment of the claim by the Group's refinery plants the combined proceeding was terminated on December 13, 2010. Due to the same reason appeals against the administrative fines of the Group's refinery plants have also been terminated. The Group's refinery plants filed an application to FAS of Russia asking for payment deferrals for the fines accrued. As of the date the financial statements were available to be issued, deferral has been approved for some of the Group's refineries. The remaining applications are under consideration.

As for the second case, the Group's refinery plants filed claims against the decisions of FAS of Russia and administrative fines accrued. Due to the signing of the agreement

between FAS of Russia and OOO LUKOIL-Volgogradneftepererabotka, OOO LUKOIL-Nizhegorodnefteorgsintez and OOO LUKOIL-Permnefteorgsintez fines were significantly reduced and lawsuits were terminated. A similar agreement is agreed to be signed with OOO LUKOIL-UNP. Currently, proceedings on this case are stayed. OOO LUKOIL-Nizhegorodnefteorgsintez has already paid the fines. FAS of Russia approved payment deferrals for OOO LUKOIL-Volgogradneftepererabotka and OOO LUKOIL-Permnefteorgsintez. OOO LUKOIL-UNP is going to file an application for payment deferrals to FAS of Russia.

The total amount of administrative penalties claimed from the Group which are estimated to be possible and probable is currently \$106 million, of which a provision of \$96 million was accrued in the Group's consolidated financial statements as of December 31, 2010 as probable to be paid. These expenses were included in "Other non-operating expense" of the consolidated statements of income.

On February 9, 2011, FAS of Russia filed a new lawsuit against the three largest Russian oil companies, including the Company, accusing them of abuse of their dominant position in the oil products market. However, the Company is not aware of the claim details until the case starts being considered. The order of legal proceedings has not been received by the Company as of the date the financial statements were available to be issued.

In March 2010, an ethanol purchase agreement signed by Getty Petroleum Marketing Inc., a Group Company, and Bionol Clearfield LLC came into force. The initial term of the agreement was five years. On June 1, 2010, Getty Petroleum Marketing Inc. filed an Arbitration claim to make amendments to the ethanol purchase agreement and to compensate for losses. On June 18, 2010, Bionol Clearfield LLC filed a counter-claim to the Arbitration tribunal of the American Arbitration Association with examination of the case in Boston to execute the agreement or to pay compensation. The amount of the claim of Bionol Clearfield LLC is \$250 million. The counterparties came to an agreement about the schedule of court hearings and documents submission. Hearings began on February 16, 2011. At this time it is not possible to predict whether any of the issues in the Arbitration are remote or probable, or the likely outcome of the Arbitration. Management does not believe that the ultimate resolution of this matter will have a material adverse effect on the Group's financial condition.

The Group is involved in cost recovery disputes with the Republic of Kazakhstan. The Group's share of the claim is approximately \$244 million. Management is of the view that substantially all of the amounts subject to dispute are in fact recoverable under the Final Production Sharing Agreement. Management believes that the ultimate reso-

lution of the claim 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. As a result of the purchase of the Company's shares by a Group company from ConocoPhillips in September 2010 (refer to Note 15. Stockholders' equity), ConocoPhillips ceased to be a related party of the Group by the end of the third quarter of 2010.

Below are related party transactions not disclosed elsewhere in the financial statements. Refer also to Notes 3, 4, 7, 11, 12, 14, 15, 18 and 21 for other transactions with related parties.

Sales of oil and oil products to related parties were \$2,383 million, \$1,152 million and \$436 million for the years ended December 31, 2010, 2009 and 2008, respectively.

Other sales to related parties were \$134 million, \$69 million and \$86 million for the years ended December 31, 2010, 2009 and 2008, respectively.

Purchases of oil and oil products from related parties were \$521 million, \$862 million and \$1,891 million for the years ended December 31, 2010, 2009 and 2008, respectively.

Purchases of processing services from related parties were \$719 million, \$539 million and nil for the years ended December 31, 2010, 2009 and 2008, respectively.

Purchases of insurance services from related parties were nil, nil and \$93 million during the years ended December 31, 2010, 2009 and 2008, respectively.

Other purchases from related parties were \$39 million, \$28 million and \$33 million for the years ended December 31, 2010, 2009 and 2008, respectively.

Amounts receivable from related parties, including loans and advances, were \$419 million and \$591 million as of December 31, 2010 and 2009, respectively. Amounts payable to related parties were \$114 million and \$97 million as of December 31, 2010 and 2009, respectively.

NOTE 21. COMPENSATION PLAN

Since December 2009, the Company has a compensation plan to certain members of management for the period from 2010 to 2012, which is based on assigned shares and provides compensation consisting of two parts. The first part represents annual bonuses that are based on the number of assigned shares and the 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 part is based upon the Company's common stock appreciation from 2010 to 2012, with rights vesting after the date of the compensation plan's termination. The number of assigned shares is approximately 17.3 million shares.

For the first part of the share plan the Group recognizes a liability based on expected dividends and the number of assigned shares.

The second part of the share plan is classified as equity settled. The grant date fair value of the plan was estimated at \$295 million using the Black-Scholes-Merton option-pricing model, assuming a risk-free interest rate of 8.0% per annum, an expected dividend yield of 3.09% per annum, an expected term of three years and a volatility factor of 34.86%. The expected volatility factor was estimated based on the historical volatility of the Company's shares for the previous five year period up to January 2010.

As of December 31, 2010, there was \$197 million of total unrecognized compensation cost related to unvested benefits. This cost is expected to be recognized periodically by the Group up to December 2012.

During the period from 2007 to 2009, the Company had a compensation plan available to certain members of

management. Its conditions were similar to the conditions of the new compensation plan introduced in December 2009. The number of assigned shares was approximately 15.5 million shares. Because of an unfavorable market situation the conditions for exercising the second part of this share plan were not met and therefore no payments or share transfers to employees took place by the end of the compensation plan.

Related to these plans the Group recorded \$129 million, \$105 million and \$134 million of compensation expenses during 2010, 2009 and 2008, respectively, of which \$98 million, \$20 million and \$103 million, respectively, are recognized as an increase in additional paid-in capital. As December 31, 2010 and 2009, \$33 million and \$26 million related to these plans are included in "Other current liabilities" of the consolidated balance sheets, respectively. The total recognized tax benefits related to these accruals were \$21 million during the years ended December 31, 2010, 2009 and 2008.

NOTE 22. SEGMENT INFORMATION

Presented below is information about the Group's operating and geographical segments for the years ended December 31, 2010, 2009 and 2008, in accordance with ASC No. 280, "Segment reporting."

The Group has the following operating segments — exploration and production; refining, marketing and distribution; chemicals; power generation 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. The power generation segment produces steam and electricity, distributes them and provides related services. The activities of the other business operating segment include 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

2010	Exploration and production	Refining, marketing and distribution	Chemicals	Power generation	Other	Elimination	Consolidated
Sales							
Third parties	3,091	99,064	1,331	1,416	54	–	104,956
Inter-segment	33,885	912	278	1,277	529	(36,881)	–
Total sales	36,976	99,976	1,609	2,693	583	(36,881)	104,956

Operating expenses	3,891	3,085	385	1,913	335	(1,640)	7,969
Depreciation, depletion and amortization	2,841	967	40	183	123	–	4,154
Interest expense	874	1,153	29	38	409	(1,791)	712
Income tax expense	1,449	880	37	(14)	–	(1)	2,351
Net income	6,226	2,934	102	(167)	(12)	(77)	9,006
Total assets	59,176	62,458	1,524	4,454	16,575	(60,170)	84,017
Capital expenditures	4,933	1,320	76	420	95	–	6,844

2009	Exploration and production	Refining, marketing and distribution	Chemicals	Power generation	Other	Elimination	Consolidated
Sales							
Third parties	2,257	76,650	1,022	1,087	67	–	81,083
Inter-segment	22,096	784	162	1,065	725	(24,832)	–
Total sales	24,353	77,434	1,184	2,152	792	(24,832)	81,083

Operating expenses	3,500	2,682	352	1,474	472	(1,356)	7,124
Depreciation, depletion and amortization	2,612	936	41	198	150	–	3,937
Interest expense	886	1,205	14	52	381	(1,871)	667
Income tax expense	1,221	821	12	(7)	6	(59)	1,994
Net income	5,456	2,263	(69)	(162)	(147)	(330)	7,011
Total assets	55,033	56,286	1,371	4,041	14,250	(51,962)	79,019
Capital expenditures	4,687	1,316	113	283	135	–	6,534

2008	Exploration and production	Refining, marketing and distribution	Chemicals	Power generation	Other	Elimination	Consolidated
Sales							
Third parties	1,753	103,132	2,067	654	74	–	107,680
Inter-segment	25,854	1,582	28	1,260	808	(29,532)	–
Total sales	27,607	104,714	2,095	1,914	882	(29,532)	107,680
Operating expenses	3,490	4,713	798	1,171	523	(2,569)	8,126
Depreciation, depletion and amortization	1,939	816	34	69	100	–	2,958
Interest expense	870	570	4	60	241	(1,354)	391
Income tax expense	955	2,510	14	(83)	17	54	3,467
Net income	4,234	5,130	(117)	(85)	(75)	57	9,144
Total assets	47,130	45,039	940	3,982	9,573	(35,203)	71,461
Capital expenditures	7,890	2,067	121	364	147	–	10,589

Geographical segments

	2010	2009	2008
Sales of crude oil within Russia	956	735	600
Export of crude oil and sales of crude oil by foreign subsidiaries	26,342	19,914	24,007
Sales of petroleum products within Russia	10,928	8,101	13,872
Export of petroleum products and sales of petroleum products by foreign subsidiaries	60,018	46,888	62,542
Sales of chemicals within Russia	728	514	880
Export of chemicals and sales of chemicals by foreign subsidiaries	642	574	1,232
Other sales within Russia	2,881	2,235	2,335
Other export sales and other sales by foreign subsidiaries	2,461	2,122	2,212
Total sales	104,956	81,083	107,680

2010	Western Siberia	European Russia	International	Elimination	Consolidated
Sales					
Third parties	385	17,231	87,340	–	104,956
Inter-segment	17,417	27,416	38	(44,871)	–
Total sales	17,802	44,647	87,378	(44,871)	104,956
Operating expenses	2,300	4,686	1,972	(989)	7,969
Depletion, depreciation and amortization	968	2,425	761	–	4,154
Interest expense	33	530	427	(278)	712
Income taxes	631	1,362	359	(1)	2,351
Net income	2,984	5,556	542	(76)	9,006
Total assets	21,785	56,897	30,225	(24,890)	84,017
Capital expenditures	2,004	3,329	1,511	–	6,844

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	1,972	4,387	1,173	(408)	7,124
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					
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	1,918	5,155	2,274	(1,221)	8,126
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

The Group's international sales to third parties include sales in Switzerland of \$53,245 million, \$37,724 million and \$47,066 million for the years ended December 31, 2010, 2009 and 2008, respectively. The Group's international sales to third parties include sales in the USA of \$8,595 million, \$8,144 million and \$12,171 million for the years ended December 31, 2010, 2009 and 2008, 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 4, 2010.

In January 2011, the Company received notice that the Board of Directors of ERG S.p.A. ("ERG") resolved to sell to the Company 11% in the joint venture to operate the ISAB refining complex located in Priolo (Italy). This is a partial exercise of ERG's option to sell its stake. Thus, the Group's ownership will be increased from 49% to 60%. The transaction is expected to be finalized at the end of the first quarter of 2011 and the amount payable will be €205 million (\$283 million), excluding inventory. The notice was received in accordance with the initial agreement on creation of the joint venture signed in 2008. Based on the agreement ERG 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%.

This section provides unaudited supplemental information on oil and gas exploration and production activities in accordance with ASC No. 932, "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, 2010	International	Russia	Total consolidated companies	Group's share in equity companies
Unproved oil and gas properties	536	302	838	293
Proved oil and gas properties	6,578	50,662	57,240	2,319
Accumulated depreciation, depletion, and amortization	(1,490)	(18,530)	(20,020)	(597)
Net capitalized costs	5,624	32,434	38,058	2,015

As of December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies
Unproved oil and gas properties	545	305	850	285
Proved oil and gas properties	5,826	47,237	53,063	1,998
Accumulated depreciation, depletion, and amortization	(1,201)	(16,460)	(17,661)	(454)
Net capitalized costs	5,170	31,082	36,252	1,829

As of December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies
Unproved oil and gas properties	519	507	1,026	158
Proved oil and gas properties	5,391	42,248	47,639	855
Accumulated depreciation, depletion, and amortization	(901)	(14,649)	(15,550)	(209)
Net capitalized costs	5,009	28,106	33,115	804

II. COSTS INCURRED IN OIL AND GAS PROPERTY ACQUISITION, EXPLORATION, AND DEVELOPMENT ACTIVITIES

Year ended December 31, 2010	International	Russia	Total consolidated companies	Group's share in equity companies
Acquisition of properties — proved	113	–	113	–
Acquisition of properties — unproved	–	15	15	122
Exploration costs	199	220	419	16
Development costs	798	3,686	4,484	115
Total costs incurred	1,110	3,921	5,031	253

Year ended December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies
Acquisition of properties — proved	–	17	17	1,154
Acquisition of properties — unproved	–	23	23	97
Exploration costs	221	162	383	11
Development costs	549	3,726	4,275	146
Total costs incurred	770	3,928	4,698	1,408

Year ended December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies
Acquisition of properties — proved	806	6	812	–
Acquisition of properties — unproved	49	5	54	6
Exploration costs	357	313	670	9
Development costs	719	6,430	7,149	139
Total costs incurred	1,931	6,754	8,685	154

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, 2010	International	Russia	Total consolidated companies	Group's share in equity companies
Revenue				
Sales	1,926	19,956	21,882	1,350
Transfers	–	12,278	12,278	13
Total revenues	1,926	32,234	34,160	1,363
Production costs (excluding production taxes)	(218)	(3,023)	(3,241)	(113)
Exploration expense	(240)	(96)	(336)	(2)
Depreciation, depletion, and amortization	(292)	(2,469)	(2,761)	(127)
Accretion expense	(14)	(35)	(49)	–
Taxes other than income taxes	(257)	(17,872)	(18,129)	(321)
Related income taxes	(314)	(1,813)	(2,127)	(275)
Total results of operations for producing activities	591	6,926	7,517	525

Year ended December 31, 2009	International	Russia	Total consolidated companies	Group's share in equity companies
Revenue				
Sales	1,472	13,870	15,342	824
Transfers	–	11,850	11,850	17
Total revenues	1,472	25,720	27,192	841
Production costs (excluding production taxes)	(195)	(2,592)	(2,787)	(98)
Exploration expense	(147)	(71)	(218)	(10)
Depreciation, depletion, and amortization	(323)	(2,235)	(2,558)	(105)
Accretion expense	–	(43)	(43)	–
Taxes other than income taxes	(206)	(12,830)	(13,036)	(186)
Related income taxes	(198)	(1,399)	(1,597)	(203)
Total results of operations for producing activities	403	6,550	6,953	239

Year ended December 31, 2008	International	Russia	Total consolidated companies	Group's share in equity companies
Revenue				
Sales	1,839	24,307	26,146	1,112
Transfers	–	17,941	17,941	11
Total revenues	1,839	42,248	44,087	1,123
Production costs (excluding production taxes)	(202)	(3,006)	(3,208)	(74)
Exploration expense	(356)	(131)	(487)	(7)
Depreciation, depletion, and amortization	(313)	(1,572)	(1,885)	(52)
Accretion expense	–	(25)	(25)	–
Taxes other than income taxes	(61)	(24,668)	(24,729)	(170)
Related income taxes	(294)	(3,272)	(3,566)	(481)
Total results of operations for producing activities	613	9,574	10,187	339

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 years 2010 and 2009) or year-end price (for the year 2008) 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, 2010, 2009 and 2008, are shown in the tables set out below.

Millions of barrels	Consolidated subsidiaries			Group's share in equity companies
	International	Russia	Total	
Crude oil				
January 1, 2008	301	15,191	15,492	223
Revisions of previous estimates	80	(1,205)	(1,125)	1
Purchase of hydrocarbons in place	17	19	36	5
Extensions and discoveries	30	493	523	6
Production	(24)	(660)	(684)	(19)
December 31, 2008	404	13,838	14,242	216
Revisions of previous estimates	(85)	(636)	(721)	15
Purchase of hydrocarbons in place	–	39	39	102
Extensions and discoveries	37	503	540	–
Production	(27)	(673)	(700)	(20)
Sales of reserves	–	(17)	(17)	–
December 31, 2009	329	13,054	13,383	313
Revisions of previous estimates	(4)	(292)	(296)	(5)
Purchase of hydrocarbons in place	62	–	62	–
Extensions and discoveries	10	550	560	10
Production	(26)	(658)	(684)	(24)
December 31, 2010	371	12,654	13,025	294
Proved developed reserves				
December 31, 2008	208	8,806	9,014	156
December 31, 2009	186	8,442	8,628	199
December 31, 2010	207	8,401	8,608	182

The minority interest share included in the above total proved reserves was 187 million barrels, 242 million barrels and 426 million barrels as of December 31, 2010, 2009 and 2008, respectively. The minority interest share included in the above proved developed reserves was

132 million barrels, 135 million barrels and 203 million barrels as of December 31, 2010, 2009 and 2008, 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
	International	Russia	Total	
Natural gas				
January 1, 2008	4,902	22,845	27,747	174
Revisions of previous estimates	566	(386)	180	4
Purchase of hydrocarbons in place	1,395	4	1,399	–
Extensions and discoveries	118	310	428	7
Production	(175)	(500)	(675)	(11)
December 31, 2008	6,806	22,273	29,079	174
Revisions of previous estimates	(294)	(6,081)	(6,375)	(3)
Purchase of hydrocarbons in place	–	13	13	130
Extensions and discoveries	294	164	458	–
Production	(175)	(436)	(611)	(15)
December 31, 2009	6,631	15,933	22,564	286
Revisions of previous estimates	(35)	1,214	1,179	11
Extensions and discoveries	98	226	324	4
Production	(187)	(540)	(727)	(26)
December 31, 2010	6,507	16,833	23,340	275
Proved developed reserves				
December 31, 2008	1,912	5,893	7,805	114
December 31, 2009	2,002	5,636	7,638	157
December 31, 2010	2,715	6,024	8,739	143

The minority interest share included in the above total proved reserves was 31 billion cubic feet, 36 billion cubic feet and 34 billion cubic feet as of December 31, 2010, 2009 and 2008, respectively. The minority interest share included in the above proved developed reserves was

21 billion cubic feet, 23 billion cubic feet and 24 billion cubic feet as of December 31, 2010, 2009 and 2008, respectively. Substantially all minority interests relate to the reserves in the Russian Federation.

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 years 2010 and 2009) or year-end price (for the year 2008) 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.

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.

	International	Russia	Total consolidated companies	Group's share in equity companies
As of December 31, 2010				
Future cash inflows	40,871	432,401	473,272	18,629
Future production and development costs	(23,193)	(313,375)	(336,568)	(9,503)
Future income tax expenses	(3,843)	(19,775)	(23,618)	(2,107)
Future net cash flows	13,835	99,251	113,086	7,019
Discount for estimated timing of cash flows (10% p.a.)	(8,641)	(60,808)	(69,449)	(3,656)
Discounted future net cash flows	5,194	38,443	43,637	3,363
Minority share in discounted future net cash flows	–	963	963	–

	International	Russia	Total consolidated companies	Group's share in equity companies
As of December 31, 2009				
Future cash inflows	31,025	385,266	416,291	14,816
Future production and development costs	(18,778)	(254,811)	(273,589)	(7,692)
Future income tax expenses	(2,337)	(22,285)	(24,622)	(1,489)
Future net cash flows	9,910	108,170	118,080	5,635
Discount for estimated timing of cash flows (10% p.a.)	(6,468)	(66,015)	(72,483)	(3,013)
Discounted future net cash flows	3,442	42,155	45,597	2,622
Minority share in discounted future net cash flows	–	1,370	1,370	–

	International	Russia	Total consolidated companies	Group's share in equity companies
As of December 31, 2008				
Future cash inflows	26,612	312,334	338,946	5,546
Future production and development costs	(18,647)	(185,733)	(204,380)	(3,074)
Future income tax expenses	(318)	(21,250)	(21,568)	(516)
Future net cash flows	7,647	105,351	112,998	1,956
Discount for estimated timing of cash flows (10% p.a.)	(6,132)	(64,296)	(70,428)	(950)
Discounted future net cash flows	1,515	41,055	42,570	1,006
Minority share in discounted future net cash flows	–	1,333	1,333	–

VI. PRINCIPAL SOURCES OF CHANGES IN THE STANDARDIZED MEASURE OF DISCOUNTED FUTURE NET CASH FLOWS

Consolidated companies	2010	2009	2008
Discounted present value as at January 1	45,597	42,570	71,871
Net changes due to purchases and sales of minerals in place	(193)	86	(279)
Sales and transfers of oil and gas produced, net of production costs	(12,454)	(11,151)	(15,663)
Net changes in prices and production costs estimates	22,241	36,633	(113,710)
Net changes in mineral extraction taxes	(23,976)	(27,376)	79,317
Extensions and discoveries, less related costs	1,886	1,878	1,423
Development costs incurred during the period	5,565	3,201	3,528
Revisions of previous quantity estimates	(433)	(4,495)	(3,520)
Net change in income taxes	407	(1,104)	11,054
Other changes	(141)	70	123
Accretion of discount	5,138	5,285	8,426
Discounted present value at December 31	43,637	45,597	42,570

Group's share in equity companies	2010	2009	2008
Discounted present value as at January 1	2,622	1,006	4,828
Net changes due to purchases and sales of minerals in place	–	1,182	17
Sales and transfers of oil and gas produced, net of production costs	(927)	(547)	(872)
Net changes in prices and production costs estimates	2,296	2,129	(6,343)
Net changes in mineral extraction taxes	(985)	(1,086)	901
Extensions and discoveries, less related costs	53	3	38
Development costs incurred during the period	120	31	51
Revisions of previous quantity estimates	(56)	137	13
Net change in income taxes	(294)	(442)	1,553
Other changes	234	95	239
Accretion of discount	300	114	581
Discounted present value at December 31	3,363	2,622	1,006

OAO "LUKOIL"

**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, 2010, and each of the years ended December 31, 2010, 2009 and 2008, 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 43 for a discussion of some of the factors that could cause actual results to differ materially.

■ KEY FINANCIAL AND OPERATIONAL RESULTS

	2010	Change to 2009, %	2009	Change to 2008, %	2008
Sales (millions of US dollars)	104,956	29.4	81,083	(24.7)	107,680
Net income attributable to OAO LUKOIL (millions of US dollars)	9,006	28.5	7,011	(23.3)	9,144
EBITDA (millions of US dollars)	16,049	19.1	13,475	(14.7)	15,797
Taxes other than income taxes, excise and export tariffs (millions of US dollars)	(27,856)	42.6	(19,532)	(43.9)	(34,804)
Basic earning per share of common stock attributable to OAO LUKOIL (US dollars)	10.95	32.2	8.28	(23.9)	10.88
Diluted earning per share of common stock attributable to OAO LUKOIL (US dollars)	10.94	32.1	8.28	(23.9)	10.88
Hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE)	817,335	1.2	807,301	0.5	803,109
Crude oil production by the Group including our share in equity affiliates (thousands of tonnes)	95,992	(1.7)	97,615	2.5	95,240
Gas available for sale produced by the Group including our share in equity affiliates (millions of cubic meters)	18,554	24.5	14,898	(12.5)	17,020
Refined products produced by the Group including our share in equity affiliates (thousands of tonnes)	63,596	6.2	59,879	12.9	53,033
Hydrocarbon proved reserves including our share in equity affiliates (millions of BOE)	17,255	(1.4)	17,504	(9.5)	19,334

In 2010, our net income was \$9,006 million, which is \$1,995 million, or 28.5%, more than in 2009.

Positive dynamic of our net income for 2010 was mainly due to a sharp increase in hydrocarbon prices, compared to 2009. Also, in the third quarter of 2010, we recognized a \$438 million gain resulting from a successful completion of the legal dispute regarding one of our joint ventures in Kazakhstan. At the same time, our results were affected by increased extraction taxes and export tariff rates, which growth rates were even higher than those of our revenue, appreciation of the Russian ruble, increase in operating and transportation expenses and impairment losses in total amount of \$306 million recognized in the fourth quarter of 2010.

■ BUSINESS OVERVIEW

The primary activities of OAO LUKOIL and its subsidiaries are crude 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, 2011 amounted to 17.3 billion BOE and comprised of 13.3 billion BOE of crude oil and 23.6 trillion cubic feet of gas.

Our operations are divided into four 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.
- **POWER GENERATION** — which includes generation, transportation and sales of electricity, heat and related services.

Other businesses include banking, finance and other activities. Each of our four 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 13, 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 crude oil refining 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 2010:

EXPLORATION AND PRODUCTION

- 11 new oil and gas fields were brought into production (2009: 8 oil and gas fields).
- On April 28, 2010, first oil was extracted at the Yu.Korchagin oilfield in the Russian offshore of the Caspian Sea.
- Consortium of LUKOIL and Vanco won a tender to explore and develop Est Rapsodia and Trident blocks in the Romanian offshore of the Black Sea.
- LUKOIL signed a contract for exploration and development of West Qurnah-2 field in Iraq.

REFINING

- In 2010, we launched a catalytic cracking complex at our refinery in Nizhny Novgorod. With this complex in operation, the refinery's production of high-octane gasoline and diesel fuel increases by 1.4 million tonnes per year and 0.4 million tonnes per year, respectively.

The whole volume of motor fuels produced will be fully compliant to Euro-4 and Euro-5. Light distillates output is increased by 12% and refinery's Nelson complexity index is increased by two points.

MARKETING

- 64 new petrol stations were brought into operation.
- Retail sales of Euro-5 diesel fuel commenced on domestic market.

Other achievements in 2010 are described in detail further in this report.

■ CHANGES IN THE GROUP STRUCTURE

In January 2011, the Company received notice that the Board of Directors of ERG S.p.A. ("ERG") resolved to sell to the Company 11% in the joint venture to operate the ISAB refining complex ("ISAB") located in Priolo (Italy). This is a partial exercise of ERG's option to sell its stake. Thus, the Group's ownership will be increased from 49% to 60%. The transaction is expected to be finalized at the end of the first quarter of 2011 and the amount payable will be €205 million (\$283 million), excluding inventory. The notice was received in accordance with the initial agreement on creation of the joint venture signed in 2008. Based on the agreement ERG 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%. In December 2008, the Group completed the acquisition of a 49.0% 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 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, includes three jetties and storage tanks totaling 3,700 thousand cubic meters and has an annual refining capacity of 16 million tonnes.

On July 28, 2010, a Group company signed a stock purchase agreement with a ConocoPhillips' subsidiary to purchase 64.6 million of the Company's ordinary shares at \$53.25 per share for the total amount of \$3,442 million. This transaction was finalized in August 2010. Additionally, under this agreement the Group had a 60-day option to purchase any or all of the remaining 98.7 million of the Company's ordinary shares held by the ConocoPhillips' subsidiary for the price of \$56 per share. On September 26, 2010, the Group company exercised its option to acquire shares from the ConocoPhillips' subsidiary by sending a notice of exercise in respect of 42,500,000 LUKOIL

ADRs (each representing one ordinary share of the Company). The Group company sold these ADRs to UniCredit Bank AG. These transactions were completed on September 29, 2010 when 42,500,000 LUKOIL ADRs were directly transferred to UniCredit Bank AG, and UniCredit Bank AG paid the purchase price of \$2.38 billion to the ConocoPhillips' subsidiary. Simultaneously, UniCredit Bank AG issued a series of equity-linked notes to the Group company that are redeemable for 17,500,000 LUKOIL ADRs on or before September 29, 2011. These equity-linked notes have been classified within OAO LUKOIL stockholders' equity. UniCredit Bank AG also issued an option to the Group company to purchase from UniCredit Bank AG an additional 25,000,000 LUKOIL ADRs on or before September 29, 2011. The option provides for the purchase of LUKOIL ADRs at market price with a floor of \$56 per ADR and is not valid if the market price per ADR is \$50 or below. As of February 7, 2011, ConocoPhillips realized the remainder of its holding in LUKOIL in the open market and thereby fully quit LUKOIL share capital.

In January 2010, the Company signed an agreement to develop the West Qurna-2 field located in the south of Iraq. The parties to the agreement are the Iraqi 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%. The West Qurna-2 field has recoverable crude oil reserves of about 12.9 billion barrels.

In December 2009, the Group acquired the remaining 46.0% interest in its equity affiliate LUKARCO B.V. ("LUKARCO") for \$1.6 billion, thereby increasing the ownership stake to 100%. LUKARCO is a holding company, which owns a 5.0% share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, and a 12.5% share in 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 5.0% and the ownership in CPC from 6.75% to 12.5%. The first installment in amount of \$300 million was paid in December 2009. \$800 million were paid in December 2010 and the remaining amount should be paid no later than December 2011.

In accordance with the Group's plans to develop its refining capacity in Europe, in June 2009, a Group company entered into an agreement with Total S.A. to acquire a 45.0% interest in TRN refinery in the Netherlands ("TRN"). The transaction was finalized in September 2009 in the amount of approximately \$688 million (after completion adjustment). 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 allowed us 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.

In order to expand the Group's presence on the most advantageous retail markets in the Russian Federation, in the fourth quarter of 2008, the Group acquired for \$493 million 100% interests in ZAO Association Grand and OOO Mega Oil M, owning 181 petrol stations in Moscow, the Moscow region and other regions of central European Russia. 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, which between them own 96 petrol stations and plots of land in Moscow, the Moscow region and other regions of central European Russia.

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 made at the date of finalization, the second payment in amount of

\$150 million was made 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 accordance with the Company's plans to develop its power generation business, in March 2008, a Group company entered into an agreement with a related party to acquire a 64.31% interest in OAO UGK TGK-8 ("TGK-8") for approximately \$2,117 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%. In September 2009, TGK-8 was reorganized into a limited liability company. 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.

■ RESOURCE BASE

The table below summarizes the net oil-equivalent proved reserves of consolidated subsidiaries and our share in equity affiliates under SEC standards (until the economic limit of commercial production is reached) that have been derived or extracted from the reports of Miller and Lents, Ltd., our independent reservoir engineers, dated as at January 1, 2011 and 2010.

(millions of BOE)	Changes in 2010				
	January 1, 2011	Production ¹	Extensions, discoveries and changes in structure	Revision of previous estimates	January 1, 2010
Western Siberia	9,861	(451)	423	138	9,751
Timan-Pechora	2,533	(160)	80	(122)	2,735
Ural region	2,033	(97)	64	(58)	2,124
Volga region	845	(27)	17	(40)	895
Other in Russia	223	(16)	14	(6)	231
Outside Russia	1,760	(83)	89	(14)	1,768
Proved oil and gas reserves	17,255	(834)	687	(102)	17,504
Probable oil and gas reserves	8,455				9,820
Possible oil and gas reserves	3,167				5,054

¹ Gas production shown before own consumption.

The Company's proved reserves as at January 1, 2011 amount to 17,255 million BOE and comprise of 13,319 million BOE of crude oil and 23,615 billion cubic feet of gas.

In 2010, proved reserves growth as a result of geological exploration, production drilling and acquisitions, totaled 687 million BOE of which geological exploration and production drilling accounted for 625 million BOE, while

acquisitions accounted for 62 million BOE. The increment of the gas reserves was mainly caused by continued development of the Bolshekhetskaya Depression and the commencement of drilling at Pyakyakhinskoye field.

The adoption of the law on the adjustment of rates of the mineral extraction tax for oil and gas, starting from 2011, resulted in the cutting of our proved reserves by 118 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 OOO LUKOIL-Western Siberia, OOO LUKOIL-Komi and OOO LUKOIL-Perm. Also we have a consolidated joint venture with ConocoPhillips, OOO Narianmarneftegaz ("NMNG"), 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, Iraq, Ghana and Cote d'Ivoire.

The table below summarizes the results of our exploration and production activities.

	2010	2009	2008
		(thousand BOE per day)	
Daily production of hydrocarbons, including the Company's share in equity affiliates, including:	2,239	2,212	2,194
- crude oil	1,940	1,972	1,921
- natural and petroleum gas ¹	299	240	273
		(US dollar per BOE)	
Hydrocarbon extraction expenses	4.12	3.56	4.12
- in Russia	4.11	3.53	4.11
- outside Russia	4.29	3.99	4.32
		(millions of US dollars)	
Hydrocarbon extraction expenses	3,241	2,787	3,208
- in Russia	3,023	2,592	3,006
- outside Russia	218	195	202
Exploration expenses	336	218	487
- in Russia	96	71	131
- outside Russia	240	147	356
Mineral extraction tax	7,864	5,452	12,267
- in Russia	7,795	5,399	12,267
- outside Russia	69	53	-

¹ Gas available for sale (excluding gas produced for our own consumption).

CRUDE OIL PRODUCTION. In 2010, our daily crude oil production decreased by 1.6%, compared to 2009. The Group produced (including our share in equity affiliates) 708.1 million barrels, or 96.0 million tonnes of crude oil.

The following table represents our crude oil production in 2010 and 2009 by major regions.

(thousands of tonnes)	Change to 2009			2009	
	2010	Total, %	Change in structure		Organic change
Western Siberia	50,934	(3.8)	–	(2,028)	52,962
Timan-Pechora	21,175	(2.2)	–	(487)	21,662
Ural region	12,385	3.6	–	427	11,958
Volga region	2,916	2.4	–	68	2,848
Other in Russia	2,021	(5.1)	–	(109)	2,130
Crude oil produced in Russia	89,431	(2.3)	–	(2,129)	91,560
Crude oil produced internationally	3,460	(1.6)	–	(55)	3,515
Total crude oil produced by consolidated subsidiaries	92,891	(2.3)	–	(2,184)	95,075
Our share in crude oil produced by equity affiliates:					
in Russia	336	9.1	–	28	308
outside Russia	2,765	23.9	575	(42)	2,232
Total crude oil produced	95,992	(1.7)	575	(2,198)	97,615

The main oil producing region of the Company is Western Siberia where we produced 54.8% of our crude oil in 2010 (55.7% in 2009 and 60.5% in 2008). A significant impact on our production in Western Siberia was caused by increased field depletion rate as well as a reduced drilling footage. The reduction in drilling footage was due to implementation of the Company's strategy aiming at strengthening its financial position through focusing on high return projects and boosting cash flows.

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 Khylychuyu oil field, located in the Timan-Pechora region. We produced 6.9 million tonnes from this field in 2010, compared to 7.0 million tonnes in 2009. This oil field is developed by NMNG, our joint venture with ConocoPhillips.

In December 2009, we started production drilling on the Yu. Korchagin field in the Caspian Sea. In April 2010, we began commercial production at the field. Maximum annual production from this field is expected

to be 2.5 million tonnes of crude oil and gas condensate, and 1.0 billion cubic meters of gas. Starting from December 2010, a reduced export tariff rate is applied to crude oil produced and exported from this field. According to the current legislation, extraction tax for this field is zero. In 2010, we produced 55 thousand tonnes from that field and thereby couldn't benefit a lot from above mentioned tax incentives.

The structural growth of our share in equity affiliates' production outside of Russia is explained by the increase in our effective share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, to 5.0% as a result of acquiring the remaining 46.0% interest in LUKARCO.

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

	2010		2009		2008	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Crude oil purchases in Russia	2,243	306	4,442	606	1,730	236
Crude oil purchases internationally	156,759	21,386	150,258	20,499	76,078	10,379
Total crude oil purchased	159,002	21,692	154,700	21,105	77,808	10,615

Substantial part of crude oil purchased on the international market was made for refining. In 2010, we purchased 12,516 thousand tonnes of crude oil to process at our and at third party refineries (including 4,574 thousand tonnes at ISAB and 2,292 thousand tonnes at TRN), compared to 11,313 thousand tonnes in 2009 (including 5,116 thousand tonnes at ISAB and 698 thousand tonnes at TRN refinery complex).

GAS PRODUCTION. In 2010, we produced 18,554 million cubic meters of gas available for sale (including our share in equity affiliates), an increase of 24.5%, compared to 2009.

Our major gas production field is the Nakhodkinskoe gas field, where we produced 8,146 million cubic meters of natural gas in 2010, compared to 5,936 million cubic meters in 2009. This 37.2% increase in gas production from the field resulted from the increase in purchases of our gas by OAO Gazprom ("Gazprom") starting from the second half of 2009. Also, during 2010, we increased utilization rates of petroleum gas in Western Siberia.

Our international gas production increased by 16.2%. Production from the Khauzak gas field in Uzbekistan was 2,655 million cubic meters of natural gas, compared to 2,227 million cubic meters in 2009. In 2010, our share in production from the Shakh-Deniz field in Azerbaijan was 545 million cubic meters, compared to 518 million cubic meters in 2009. As a result of acquisition of the remaining share in LUKARCO we increased our share in production of petroleum gas from Tengiz field by 300 million cubic meters.

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. Moreover, we currently have a 49% stake in the ISAB refinery complex in Italy and a 45% interest in TRN refinery in the Netherlands.

Compared to 2009, production at our consolidated and affiliated refineries increased by 6.2%. Russian refineries increased their production by 1.8%. Production of our international refineries including our share of production

at ISAB and TRN increased by 16.9%. The increase was a result of acquisition of TRN in September 2009. The production at our Bulgarian and Ukrainian refineries was lower due to performed overhauls. The Odessa refinery was stopped in the fourth quarter of 2010 due to unfavorable economic conditions in Ukraine. In 2010, our share of refined products produced at ISAB amounted to 6,540 thousand tonnes (6,153 thousand tonnes in 2009) and our share in production of TRN amounted to 4,468 thousand tonnes (1,528 thousand tonnes in 2009).

We invested, and continue to invest, significant resources in our refineries aiming at taking leading position in Russia in producing ecological fuel of high quality standards. Thus, in December 2010, we launched a catalytic cracking complex at our refinery in Nizhny Novgorod that enabled us to start production of gasoline fully compliant to Euro-4 quality standard. Related investments amounted to approximately \$1 billion.

In Russia, LUKOIL holds the leading position in production and sales of European standards motor fuel being ahead of the official terms of their obligatory implementation in the country. At our Russian refineries we produced 8,429, 7,266 and 7,224 thousand tonnes of Euro 4 and Euro 5 diesel fuel, and 5,373, 4,746 and 4,191 thousand tonnes of Euro 3 gasoline in 2010, 2009 and 2008, respectively. In the end of 2010, we commenced production of Euro-4 gasoline.

Along with our own production of refined products we can refine crude oil at third party refineries depending on market conditions and other factors. Before 2010, we processed crude oil at third party refineries in Russia primarily to supply our network in the Ural region and for export sales. In 2010, we sell our crude oil to these refineries and purchase refined products from them. In order to supply our retail networks in Eastern Europe, we refined crude oil in Belarus and Serbia. Refined products processed in Belarus were used for supplying our local retail network and for wholesale export. In the end of 2009, we ceased refining of crude oil in Belarus due to decreased profitability of such operations as a result of certain amendments in the customs legislation. However, in the third quarter of 2010, we began refining our crude oil at a third party refinery in Kazakhstan. The following table summarizes key figures for our refining activities.

	2010	2009	2008
	(millions of US dollars)		
Own refining expenses	1,088	923	1,115
- in Russia	806	671	780
- outside Russia	282	252	335
Refining expenses at ISAB and TRN	719	543	39
Refining expenses at third party refineries	5	170	400
- in Russia	1	126	341
- outside Russia	4	44	59
Capital expenditures	702	828	1,023
- in Russia	542	520	688
- outside Russia	160	308	335
	(thousand barrels per day)		
Refinery throughput at the Group refineries	1,103	1,099	1,112
- in Russia ¹	904	889	881
- outside Russia	199	210	231
Refinery throughput at ISAB and TRN ^{2,3}	222	155	13
Refinery throughput at third party refineries	2	77	110
- in Russia	–	41	64
- outside Russia	2	36	46
Total refinery throughput	1,327	1,331	1,235
	(thousand of tonnes)		
Refined products produced at the Group refineries	52,588	52,198	52,455
- in Russia ¹	43,172	42,408	42,067
- outside Russia	9,416	9,790	10,388
Production of ISAB and TRN ²	11,008	7,681	578
Refined products produced at third party refineries	107	3,485	5,004
- in Russia	–	1,873	2,881
- outside Russia	107	1,612	2,123
Total refined products produced	63,703	63,364	58,037

¹ Excluding mini refineries.

² Group's share.

³ Including refined products processed.

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 27 countries through 6 thousand petrol stations. Most of the stations operate under the LUKOIL brand. We continuously develop our retail business and the LUKOIL brand by expanding our retail network.

The table below summarizes figures for our trading activities.

	2010	2009	2008
	(thousand of tonnes)		
Retail sales	14,336	14,079	14,164
Wholesale sales	91,020	86,681	80,983
Total refined products sales	105,356	100,760	95,147
Refined products purchased in Russia	1,853	625	1,635
Refined products purchased internationally	45,816	41,445	38,743
Total refined products purchased	47,669	42,070	40,378

Refined products purchases in Russia increased in 2010 compared to 2009 due to termination of processing activities at third-party refineries. We began to sell our crude oil to these refineries and purchased refined products back from them. In 2010, these purchases amounted to approximately 870 thousand tonnes. Our international purchases increased due to expansion of trading activities and increased purchases for refining at ISAB and TRN refineries.

EXPORTS OF CRUDE OIL AND REFINED PRODUCTS FROM RUSSIA. In 2010, our export of crude oil from Russia was 3.4% less than in 2009, and we exported 45.4% of our total domestic crude oil production (45.9% in 2009 and 43.8% in 2008).

The volumes of crude oil exported from Russia by our subsidiaries are summarized as follows:

	2010		2009		2008	
	(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	231,525	31,586	241,890	33,000	264,393	36,070
Exports of crude oil bypassing Transneft	65,999	9,004	66,109	9,019	23,639	3,225
Total crude oil exports	297,524	40,590	307,999	42,019	288,032	39,295

The overall decrease of our export from Russia was a result of decreased crude oil production, cease of processing operations in Belarus and respective decrease of export to CIS. However, export to far-abroad increased by 2,984 thousand tonnes, or by 8.9%, compared to 2009.

In 2010, the crude oil exported through our own export infrastructure amounted to 8,732 thousand tonnes and was on the level of 2009.

In 2010, we exported from Russia 25.8 million tonnes of refined products, a decrease of 6.9%, compared to 2009. This was mainly due to decreased export to CIS. Released

volumes were sold on domestic market. Primarily, we export from Russia diesel fuel, fuel oil and gasoil. These products account for approximately 92% of our refined products export volumes.

In 2010, our revenue from export of crude oil and refined products from Russia both to the Group companies and third parties amounted to \$22,178 million and \$14,088 million, respectively (\$17,485 million for crude oil and \$11,414 million for refined products in 2009).

POWER GENERATION. In 2010, we continued to develop the new power generation sector of our business as part of our strategic development program. This new sector encompasses all aspects of the power generation business, from generation to transmission and sale of heat and electrical power. Our power generation business sector now includes OOO "LUKOIL-Kubanenergo", OOO "LUKOIL-Astrakhanenergo", OOO "LUKOIL-Volgograd-

energo", OOO "LUKOIL-Rostovenergo", OOO "LUKOIL-TTK" (all spun off from TGK-8), our own power generating facilities at our oil and gas fields and power generators in Bulgaria, Romania and Ukraine. Our total output of electrical energy was 13.2 billion kW-h in 2010 and 13.1 billion kW-h in 2009. Our total output of heat energy was approximately 15.3 million Gcal in 2010 (15.1 million Gcal in 2009).

■ 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 2010, the Brent crude oil price fluctuated between \$67 and \$94 per barrel and reached its peak of \$94.00 in late December of 2010.

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. Despite that, average international crude oil prices for 2008 were almost \$100 per barrel.

During the second half of 2009, the crude oil price stabilized around \$70 per barrel and since then fluctuated within sloping upward trend. At the same time, average international crude oil prices for 2009 were about \$60 per barrel, which was significantly lower compared to 2008.

Substantially all crude oil we export is Urals blend. The following table shows the average crude oil and refined product prices products in 2010, 2009 and 2008.

	2010	Change to 2009, %	2009	Change to 2008, %	2008
(in US dollars per barrel, except for figures in percent)					
Brent crude	79.50	28.9	61.67	(36.6)	97.26
Urals crude (CIF Mediterranean) ¹	78.29	27.9	61.22	(35.4)	94.76
Urals crude (CIF Rotterdam) ¹	78.26	28.0	61.15	(35.5)	94.83
(in US dollars per metric tonne, except for figures in percent)					
Fuel oil 3.5% (FOB Rotterdam)	442.35	28.0	345.72	(24.8)	459.74
Diesel fuel 10 ppm (FOB Rotterdam)	688.46	28.7	534.84	(43.6)	948.11
High-octane gasoline (FOB Rotterdam)	735.24	27.0	579.01	(30.8)	836.79

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 2010, 2009 and 2008.

	2010	Change from 2009, %	2009	Change from 2008, %	2008
(in US dollars per metric tonne, except for figures in percent)					
Fuel oil	245.27	51.3	162.12	(32.1)	238.87
Diesel fuel	557.36	20.5	462.65	(37.8)	744.07
High-octane gasoline (Regular)	714.26	22.1	584.87	(22.2)	751.95
High-octane gasoline (Premium)	743.17	16.8	636.24	(26.0)	860.07

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 devaluation of the ruble against the US dollar generally causes our costs to decrease in US dollar terms, and vice versa. The devaluation 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 11.6% in 2010, compared to 2009.

The following table gives data on inflation in Russia and the change in the ruble-dollar exchange rate.

	2010	2009	2008
Ruble inflation (CPI), %	8.7	8.9	13.3
Change of the ruble-dollar exchange rate, %	(0.8)	(2.9)	(19.7)
Average exchange rate for the period (ruble to US dollar)	30.37	31.72	24.86
Exchange rate at the end of the period (ruble to US dollar)	30.48	30.24	29.38

■ 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 2010, 2009 and 2008, the tax charge on the operations in Russia was approximately 85%, 81% 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, property tax, VAT and 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 2010, 2009 and 2008, respectively, were 77%, 75% and 81%. In 2010, tax expenses in Russia were about 49% 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.

		2010 ¹	Change to 2009, %	2009 ¹	Change to 2008, %	2008 ¹
Export tariffs on crude oil	\$/tonne	273.55	52.0	179.93	(49.3)	355.08
Export tariffs on refined products						
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	\$/tonne	196.60	47.2	133.54	(46.9)	251.53
Liquid fuels (fuel oil)	\$/tonne	105.91	47.2	71.93	(46.9)	135.51
Excise on refined products						
Straight-run gasoline	RUR/tonne	4,290.00	10.0	3,900.00	46.8	2,657.00
High-octane gasoline	RUR/tonne	3,992.00	10.0	3,629.00	–	3,629.00
Low-octane gasoline	RUR/tonne	2,923.00	10.0	2,657.00	–	2,657.00
Diesel fuel	RUR/tonne	1,188.00	10.0	1,080.00	–	1,080.00
Motor oils	RUR/tonne	3,246.10	10.0	2,951.00	–	2,951.00
Mineral extraction tax						
Crude oil	RUR/tonne	3,075.76	33.6	2,302.85	(30.8)	3,328.35
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:

		2010 ¹	Change to 2009, %	2009 ¹	Change to 2008, %	2008 ¹
Excise on refined products						
Straight-run gasoline	\$/tonne	141.26	14.9	122.94	15.0	106.90
High-octane gasoline	\$/tonne	131.45	14.9	114.40	(21.7)	146.01
Low-octane gasoline	\$/tonne	96.25	14.9	83.76	(21.7)	106.90
Diesel fuel	\$/tonne	39.12	14.9	34.04	(21.7)	43.45
Motor oils	\$/tonne	106.89	14.9	93.02	(21.7)	118.73
Mineral extraction tax						
Crude oil	\$/tonne	101.28	39.5	72.59	(45.8)	133.91
Natural gas	\$/1,000 m ³	4.84	4.5	4.63	(21.7)	5.91

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. The base rate is 419 rubles per metric tonne extracted and it is adjusted depending on the international market price of Urals blend and the ruble exchange rate. The tax rate is zero when the average Urals blend international market price for a tax period was less than or equal to \$15.00 per barrel. Each \$1.00 per barrel increase in the international Urals blend price over the threshold (\$15.00 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).

The base rate for 2012 and 2013 is currently set at 446 rubles and 470 rubles per metric tonne extracted, respectively. However, the rate may be amended by the authorities later on.

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, the Caspian

Sea and the Nenetsky Autonomous District, 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.

In 2010, the Group produced crude oil from certain oilfields in the Caspian Sea and the Nenetsky Autonomous District and benefited from the application of zero tax rate. However, in beginning of December 2010, we exceeded the accumulated production limit of 15 million tonnes at Yuzhnoye Khylichuyu oilfield eligible for the incentive. Thus, starting from December 2010, we pay mineral extraction tax at a regular rate at this field.

NATURAL GAS EXTRACTION TAX RATE. The mineral extraction tax on natural gas production is calculated using a flat rate. During the period since January 1, 2006 till December 31, 2010, the rate of 147 rubles per thousand cubic meters of natural gas extracted was in effect. However, the rate was raised up to 237 rubles per thousand cubic meters since January 1, 2011.

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.

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.

Starting from the end of 2009, zero export duty rate was set for crude oil produced at certain fields in Eastern Siberia. However, in July 2010, a zero rate for these fields was substituted for special reduced export duty rate. Effective from December 2010, the list of the oilfields where reduced rate applies also includes our Yu. Korchagin and V. Filanovsky oilfields located in the Caspian Sea.

EXPORT DUTY RATES ON REFINED PRODUCTS prior to 2011 were set by the Russian government. The rate of export duty depended on internal demand for refined products and international crude oil market conditions. Starting from 2011, export duty rates on crude oil refined products are calculated as follows: export duty rate on refined products equals current crude oil export duty rate multiplied by a coefficient according to the table below.

	2011	2012	2013
Multiplier for:			
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	0.670	0.640	0.600
Liquid fuels (fuel oil)	0.467	0.529	0.600
Motor and other oils	0.467	0.529	0.600
Other products	0.467	0.529	0.600

Equivalent average ratios calculated for 2010 would be 0.719 for light and middle distillates, diesel fuel and gasoils and 0.387 for liquid fuels and motor oils.

CRUDE OIL AND REFINED PRODUCTS EXPORTED TO CIS COUNTRIES, other than Ukraine and Belarus, are not subject to export duties.

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 was not subject to export duty. Volumes of crude oil above this limit were taxed at a regular export duty rate.

In 2009, crude oil exported from Russia to Belarus was subject to export duties calculated with the application

of a coefficient 0.356 (0.335 in 2008) to the regular export duty rate set by the Russian government.

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.

Starting from 2011, excise rates on refined products in Russia are increased and now depend on ecological class of fuel. Excise tax rates for 2011 are listed below:

Gasoline		
Below Euro 3	RUR/tonne	5,995.00
Euro 3	RUR/tonne	5,672.00
Euro 4 and 5	RUR/tonne	5,143.00
Diesel fuel		
Below Euro 3	RUR/tonne	2,753.00
Euro 3	RUR/tonne	2,485.00
Euro 4 and 5	RUR/tonne	2,247.00
Motor oils	RUR/tonne	4,681.00
Straight-run gasoline	RUR/tonne	6,089.00

INCOME TAX. Starting from January 1, 2009, the Federal income tax rate is 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, GAS 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 Au-

tonomous 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.

In Russia, most of gas is sold at the wellhead and then transported through the Unified Gas Supply System ("UGSS"). The UGSS is responsible for gathering, transporting, dispatching and delivering substantially all natural gas supplies in Russia and is owned and operated by Gazprom. The FST regulates natural gas transportation tariffs. We do not have any possibility to sell our gas other than through UGSS.

YEAR ENDED DECEMBER 31, 2010, COMPARED TO YEARS ENDED DECEMBER 31, 2009 AND DECEMBER 31, 2008

The table below presents our consolidated statements of income for the periods indicated.

	2010	2009	2008
	(millions of US dollars)		
Revenues			
Sales (including excise and export tariffs)	104,956	81,083	107,680
Costs and other deductions			
Operating expenses	(7,969)	(7,124)	(8,126)
Cost of purchased crude oil, gas and products	(43,579)	(31,977)	(37,851)
Transportation expenses	(5,608)	(4,830)	(5,460)
Selling, general and administrative expenses	(3,558)	(3,306)	(3,860)
Depreciation, depletion and amortization	(4,154)	(3,937)	(2,958)
Taxes other than income taxes	(8,978)	(6,474)	(13,464)
Excise and export tariffs	(18,878)	(13,058)	(21,340)
Exploration expense	(336)	(218)	(487)
Loss on disposals and impairments of assets	(363)	(381)	(425)
Income from operating activities	11,533	9,778	13,709
Interest expense	(712)	(667)	(391)
Interest and dividend income	174	134	163
Equity share in income of affiliates	472	351	375
Currency translation loss	(122)	(520)	(918)
Other non-operating income (expense)	125	(13)	(244)
Income before income taxes	11,470	9,063	12,694
Current income taxes	(2,104)	(1,922)	(4,167)
Deferred income taxes	(247)	(72)	700
Total income tax expense	(2,351)	(1,994)	(3,467)
Net income	9,119	7,069	9,227
Less: net income attributable to noncontrolling interests	(113)	(58)	(83)
Net income attributable to OAO LUKOIL	9,006	7,011	9,144
Basic earning per share of common stock attributable to OAO LUKOIL (in US dollars)	10.95	8.28	10.88
Diluted earning per share of common stock attributable to OAO LUKOIL (in US dollars)	10.94	8.28	10.88

The analysis of the main financial indicators of the financial statements is provided below.

■ SALES REVENUES

Sales breakdown	2010	2009	2008
	(millions of US dollars)		
Crude oil			
Export and sales on international markets other than CIS	25,251	18,276	22,382
Export and sales to CIS	1,091	1,638	1,625
Domestic sales	956	735	600
	27,298	20,649	24,607
Refined products			
Export and sales on international markets			
Wholesale	50,340	38,023	50,553
Retail	9,678	8,865	11,989
Domestic sales			
Wholesale	5,427	3,820	8,049
Retail	5,501	4,281	5,823
	70,946	54,989	76,414
Petrochemicals			
Export and sales on international markets	642	574	1,232
Domestic sales	728	514	880
	1,370	1,088	2,112
Gas and gas products			
Export and sales on international markets	1,565	1,091	926
Domestic sales	786	548	985
	2,351	1,639	1,911
Sales of energy and related services	1,416	1,087	654
Other			
Export and sales on international markets	890	1,030	1,286
Domestic sales	685	601	696
	1,575	1,631	1,982
Total sales	104,956	81,083	107,680

Sales volumes	2010	2009	2008
Crude oil	(thousands of barrels)		
Export and sales on international markets other than CIS	326,669	305,273	242,784
Export and sales to CIS	23,280	39,106	31,629
Domestic sales	26,637	21,909	15,408
	376,586	366,288	289,821
Crude oil	(thousands of tonnes)		
Export and sales on international markets other than CIS	44,566	41,647	33,122
Export and sales to CIS	3,176	5,335	4,315
Domestic sales	3,634	2,989	2,102
	51,376	49,971	39,539
Refined products	(thousands of tonnes)		
Export and sales on international markets			
Wholesale	80,043	76,885	67,669
Retail	7,314	7,863	8,200
Domestic sales			
Wholesale	10,977	9,796	13,314
Retail	7,022	6,216	5,964
	105,356	100,760	95,147
Total sales volume of crude oil and refined products	156,732	150,731	134,686

Realized average sales prices	2010		2009		2008	
	(\$/barrel)	(\$/tonne)	(\$/barrel)	(\$/tonne)	(\$/barrel)	(\$/tonne)
Average realized price international						
Oil (excluding CIS)	77.30	566.60	59.87	438.84	92.19	675.76
Oil (CIS)	46.84	343.35	41.89	307.05	51.38	376.58
Refined products						
Wholesale		628.91		494.55		747.06
Retail		1,323.31		1,127.44		1,462.14
Average realized price within Russia						
Oil	35.90	263.18	33.56	245.97	38.97	285.66
Refined products						
Wholesale		494.37		389.92		604.55
Retail		783.49		688.74		976.40

During 2010, our revenues increased by \$23,873 million, or by 29.4%, compared to 2009 (in 2009 decreased by \$26,597 million, or by 24.7%, compared to 2008). Our revenues from crude oil sales increased by \$6,649 million, or by 32.2% (in 2009 decreased by \$3,958 million, or by 16.1%, compared to 2008). Our revenues from sales of refined products increased by

\$15,957 million, or by 29.0% (in 2009 decreased by \$21,425 million, or by 28.0%, compared to 2008). In 2010, the increase in sales revenue was due to sharp increase in hydrocarbon prices, compared to 2009. Moreover, the appreciation of the ruble against the US dollar also seriously affected our average realized prices in Russia.

Sales of crude oil

2010 VS. 2009

Our total crude oil sales revenues increased by \$6,649 million, or by 32.2%, mainly due to growth of crude oil prices.

Cease in crude oil refining at third party refineries in Russia and Belarus released crude oil volumes for marketing. As a result, our crude oil sales raised by 2.8% in terms of volumes.

In 2010, revenue from export of crude oil from Russia both to the Group companies and third parties amounted to \$22,178 million.

2009 VS. 2008

Our total crude oil sales revenues decreased by 16.1%. We sold crude oil to third parties mostly outside Russia and the 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, revenue from export of crude oil from Russia both to the Group companies and third parties amounted to \$17,485 million.

Sales of refined products

2010 VS. 2009

In 2010, our revenue from the wholesale of refined products outside of Russia increased by \$12,317 million, or by 32.4%, due to increased average realized price by 27.2%. The decrease in output at our refineries in Bulgaria due to overhaul and in Ukraine due to refinery stand-by and termination of processing activities in Russia were almost fully compensated by commencement of crude oil refining at TRN in September 2009. At the same time, expansion of trading activities led to an increase in wholesales volumes by 4.1%.

In 2010, our revenue from international retail sales increased by \$813 million, or by 9.2%. Positive effect

from the increase of average retail prices by 17.4% was partially offset by 7.0% sales volumes decrease, that reflects restructuring of our retail network in the USA.

In 2010, our revenue from the wholesale of refined products on the domestic market increased by \$1,607 million, or by 42.1%, mainly due to an increase in the average realized price by 26.8%. Sales volumes increased by 1,181 thousand tonnes, or by 12.1%. This was primarily due to a decrease in refined products export to Belarus.

In 2010, our revenue from retail sales in Russia increased by \$1,220 million, or by 28.5%, due to an increase both in volumes, being a result of higher average daily sales per petrol station, and in prices. In 2010, our retail sales revenue was 50.3% of total refined products sales in Russia (in 2009 — 52.8%).

In 2010, our revenue from export of refined products from Russia both to Group companies and third parties amounted to \$14,088 million.

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%, 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%, 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%, 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.

Sales of petrochemical products

2010 VS. 2009

In 2010, our revenue from sales of petrochemical products increased by \$282 million, or by 25.9%. Outside of Russia, decrease in sales volumes due to decreased refining and trading was compensated by price growth. At the same time, in the fourth quarter of 2010, we commenced production at our petrochemical plant Karpatnaftochim Ltd. in Ukraine after modernization and construction of a chlorine and caustic production line. The growth of domestic sales revenue was largely a result of increase in realized prices and the effect of the real ruble appreciation against the US dollar.

2009 VS. 2008

In 2009, our revenue from sales of petrochemical products decreased by \$1,024 million, or by 48.5%. 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.

Sales of gas and gas products

2010 VS. 2009

In 2010, sales of gas and gas refined products increased by \$712 million, or by 43.4%. Gas products sales revenue increased by \$424 million, or by 40.8%, primarily as a result of an increase in sales prices. Retail gas product revenue increased up to \$506 million, or by 22.2%, due to price growth. Retail revenue represented 37.8% and 44.0% of our total gas product revenue in 2010 and 2009, respectively.

Natural gas sales revenue amounted to \$835 million — an increase of 46.2%, compared to 2009. Our domestic natural gas sales revenue significantly increased as a result of increased sales to Gazprom, the major purchaser of our natural gas produced in the Russian Federation.

In 2010, we sold 8,146 million cubic meters of natural gas to Gazprom (5,936 million cubic meters in 2009). The average realized price increased by 4.5% to \$34.9 per 1,000 cubic meters as a result of the ruble appreciation.

In 2010, natural gas sales revenue outside of Russia increased by \$174 million mostly as a result of a revision of sale prices related to the Shakh-Deniz field for 2008-2010 which led to additional revenue of \$101 million, recognized in the third quarter of 2010.

2009 VS. 2008

In 2009, sales of gas and gas refined products decreased by \$272 million, or by 14.2%. 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.

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.

Sales of energy and related services

We have been developing our power generation business since the acquisition of TGK-8 in May 2008. Substantially we sell energy and related services domestically. International sales are relatively insignificant.

2010 VS. 2009

In 2010, our revenue from sales of electricity, heat and related services increased by \$329 million, or by 30.3%, as we continued to develop the new power generation segment as part of our strategic development program. The ruble appreciation also contributed to the increase of this revenue.

2009 VS. 2008

In 2009, our revenue from sales of electricity, heat and related services increased by \$433 million, or by 66.2%. Our power generation and distribution business emerged in May 2008 and substantially expanded in 2009 that was reflected in sales growth.

Sales of other products

Other sales include transportation services, non-petroleum sales through our retail network, crude oil extraction services, rental revenue, and other revenue of our production and marketing companies from sales of goods and services not related to our primary activities.

2010 VS. 2009

In 2010, our other sales decreased by \$56 million, or by 3.4%. A decrease of transportation services provided abroad was partially compensated by higher non-petroleum retail revenue. During 2010, sales of goods and other products from our retail stations amounted to \$606 million, an increase of \$38 million compared to 2009.

2009 VS. 2008

In 2009, our other sales decreased by \$351 million, or by 17.7%. Other sales in Russia were affected by devaluation of the ruble. Outside of Russia we had a decrease of trans-

portation services provided and volumes of non-petroleum sales from our retail stations.

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.

■ OPERATING EXPENSES

Operating expenses include the following:

	2010	2009	2008
	(millions of US dollars)		
Hydrocarbon extraction expenses	3,241	2,787	3,208
Own refining expenses	1,088	923	1,115
Refining expenses at third parties and affiliated refineries	724	713	439
Expenses for crude oil transportation to refineries	1,048	955	1,072
Power generation and distribution expenses	654	450	260
Petrochemical expenses	221	127	235
Other operating expenses	1,322	1,385	1,547
	8,298	7,340	7,876
Change in operating expenses in crude oil and refined products inventory originated within the Group ¹	(329)	(216)	250
Total operating expenses	7,969	7,124	8,126

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 2009, operating expenses increased by \$845 million, or by 11.9%, which is mainly explained by general increase in operating expenses in Russia due to the real ruble appreciation against the US dollar by 11.6%, increase in hydrocarbon extraction expenses, refining expenses and power generation and distribution expenses.

Hydrocarbon extraction expenses

Our extraction expenses include expenditures related to repairs of extraction equipment, labor costs, expenses on enhancing reservoir recovery, fuel and electricity costs, property insurance of extraction equipment and other similar costs.

2010 VS. 2009

In 2010, our extraction expenses increased by \$454 million, or by 16.3%. This was due to increase in expenses for power supply, general increase in expenses and the effect of the real ruble appreciation against the US dollar. Our average hydrocarbon extraction cost increased from \$3.56 to \$4.12 per BOE, or by 15.7%, compared to 2009.

2009 VS. 2008

In 2009, our extraction expenses decreased by \$421 million, or by 13.1%, 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.

Own refining expenses

2010 VS. 2009

In 2010, our refining expenses increased by \$165 million, or by 17.9%.

Refining expenses at our domestic refineries increased by 20.1%, or by \$135 million, mainly as a result of the real ruble appreciation against the US dollar, increase in power supply costs and higher consumption of additives.

Refining expenses at our international refineries increased by 11.9%, or by \$30 million, mainly as a result of increased power supply costs.

2009 VS. 2008

In 2009, our refining expenses decreased by \$192 million, or by 17.2%.

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.

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.

2010 VS. 2009

As opposed to 2009, we did not process crude oil on third party refineries during 2010 in Russia and Belarus. Nevertheless, the commencement of crude oil refining at TRN in late September 2009 almost fully compensated for that. As a result, the overall decrease of throughput at third party and affiliated refineries was 2.8%, compared to 2009 (including refined products processed). At the same time, in 2010, refining expenses at third party and affiliated refineries increased by 1.5%, compared to 2009, because processing cost at our refineries in Western Europe is higher than at the refineries in Russia or Belarus. Starting from the third quarter of 2010, we also refined crude oil on a third party refinery in Kazakhstan.

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.

Petrochemical operating expenses

2010 VS. 2009

In 2010, operating expenses of our petrochemical plants increased by \$94 million, or by 74.0%. Expenses in Russia were impacted by increased production, increased cost of raw materials and ruble appreciation to the US dollar. Despite petrochemical capacity downtime in Bulgaria and Ukraine in 2010, the decrease of our international petrochemical operating expenses compared to

2009 was insignificant due to sizeable share of fixed costs. In the fourth quarter of 2010, we commenced production at our petrochemical plant Karpatnaftochim Ltd. in Ukraine after modernization and construction of a chlorine and caustic production line.

2009 VS. 2008

In 2009, operating expenses of our petrochemical companies decreased by \$108 million, or by 46.0%, 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.

Expenses for crude oil transportation to refineries

Expenses for crude oil transportation to refineries include pipeline, railway, freight and other costs related to delivery of Group's own crude oil to refineries for further processing.

2010 VS. 2009

Expenses for crude oil transportation to refineries increased in 2010 by \$93 million, or by 9.7%, due to an increase in transportation tariffs and as a result of a real ruble appreciation in Russia (see Transportation expenses below). Moreover, in 2010, we dramatically increased volumes of own crude oil supplies to TRN.

2009 VS. 2008

Expenses for crude oil transportation to refineries decreased in 2009 by \$117 million, or by 10.9%, 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.

Power generation and distribution expenses

2010 VS. 2009

Power generation and distribution expenses increased by \$204 million, or by 45.3%, following expansion of our power generating business and as a result of the real ruble appreciation in Russia.

2009 VS. 2008

Power generation and distribution expenses increased by \$190 million, or by 73.1%. Our power generation and distribution business emerged in May 2008 and substantially expanded in 2009 that was reflected in operating expenses growth.

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 transportation services, crude oil extraction services, operating expenses of our gas processing plants, costs of other services provided and goods sold by our production and marketing companies, and of non-core businesses of the Group.

2010 VS. 2009

In 2010, our other operating expenses decreased by \$63 million, or by 4.5%, mainly due to decrease of volume of transportation services provided abroad.

2009 VS. 2008

In 2009, our other operating expenses decreased by \$162 million, or by 10.5%. In 2008, other operating expenses included \$116 million of excise included in processing fee paid to third parties refineries, compared to \$54 million in 2009. Besides, other operating expenses in Russia were affected by the ruble devaluation. Outside of Russia, operating expenses were lower than in 2008 due to a decrease of transportation services provided.

■ COST OF PURCHASED CRUDE OIL, GAS AND PRODUCTS

Cost of purchased crude oil, gas and products includes cost of crude oil and refined products purchased for trading or refining, gas and fuel oil to supply our power generation entities and the result of hedging of international crude oil and refined products sales.

2010 VS. 2009

In 2010, cost of purchased crude oil, gas and products increased by \$11,602 million, or by 36.3%, due to an increase in crude oil and refined products prices and increase in volumes of refined products purchases.

In 2010, we recognized a \$232 million expense from hedging, compared to a \$781 million expense in 2009.

2009 VS. 2008

Cost of purchased crude oil, gas and products decreased by \$5,874 million in 2009, or by 15.5%, 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.

In 2009, we recognized a \$781 million expense from hedging, compared to a \$902 million gain in 2008.

■ TRANSPORTATION EXPENSES**2010 VS. 2009**

In 2010, our transportation expenses increased by \$778 million, or by 16.1%. This was primarily due to increase of ruble denominated pipeline and railway transportation tariffs in Russia, which was emphasized by the ruble appreciation.

Our actual transportation expenses related to crude oil and refined products deliveries to various export destinations, weighted by volumes transported, changed in 2010, compared to 2009, as follows: crude oil pipeline tariffs increased by 23.3%, railway tariffs for refined products transportation increased by 21.1%, crude oil freight rates decreased by 7.8%, and refined products freight rates increased by 23.8%.

2009 VS. 2008

In 2009, our transportation expenses decreased by \$630 million, or by 11.5%. 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.

■ 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.

2010 VS. 2009

In 2010, our selling, general and administrative expenses increased by \$252 million, or by 7.6%, substantially due to the effect of ruble appreciation on selling, general and administrative expenses in Russia and salaries indexation.

2009 VS. 2008

In 2009, our selling, general and administrative expenses decreased by \$554 million, or by 14.4%. The decrease was primarily due to the devaluation of the ruble. Nevertheless, this was partially offset by movements in provision for bad debts and the effect of changes in the Group's structure.

■ 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.

2010 VS. 2009

Our depreciation, depletion and amortization expenses increased by \$217 million, or by 5.5%.

2009 VS. 2008

Our depreciation, depletion and amortization expenses increased by \$979 million, or by 33.1%. 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 Khylychuyu oil field.

■ EXPLORATION EXPENSES**2010 VS. 2009**

During 2010, exploration expense increased by \$118 million, or 54.1%. Dry hole costs increased by \$108 million to \$225 million.

In 2010, we charged to expense cost of dry wells in Columbia and Cote d'Ivoire in amount of \$112 million and

\$68 million, respectively. Dry hole write-off in Russia amounted to \$42 million in 2010.

2009 VS. 2008

During 2009, exploration expense decreased by \$269 million, or by 55.2%. 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.

■ INTEREST EXPENSE

2010 VS. 2009

In 2010, interest expense increased by \$45 million, which is 6.7% more than in the previous year. This increase mainly relates to discounting of the VAT recoverable of our refinery in Ukraine as a result of the restructuring of this receivable.

2009 VS. 2008

In 2009, interest expense amounted to \$667 million, or 70.6% more than in 2008. 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).

■ 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.

2010 VS. 2009

At 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%. Largely as a result of this, our share in income of affiliates increased by \$121 million, or by 34.5%.

2009 VS. 2008

Compared to 2008, our share in income of affiliates decreased by \$24 million, or by 6.4%.

■ OTHER NON-OPERATING INCOME

In 2010, other non-operating income included a \$438 million gain related to successful settlement of a corporate dispute between a Group company and a CNPC group company regarding Turgai Petroleum, our joint venture in Kazakhstan, and a \$96 million expense related to provisions accrued in respect of claims to the Group companies by Federal Anti-monopoly Service of the Russian Federation (FAS of Russia).

As a result, other non-operating income in 2010 amounted to \$125 million, compared to a \$13 million loss in 2009 and a \$244 million loss in 2008.

■ TAXES OTHER THAN INCOME TAXES

	2010	2009	2008
	(millions of US dollars)		
In Russia			
Mineral extraction taxes	7,795	5,399	12,267
Social security taxes and contributions	327	330	435
Property tax	479	438	374
Other taxes	93	92	180
Total in Russia	8,694	6,259	13,256
International			
Mineral extraction taxes	69	53	–
Social security taxes and contributions	102	69	77
Property tax	39	32	31
Other taxes	74	61	100
Total internationally	284	215	208
Total	8,978	6,474	13,464

2010 VS. 2009

In 2010, taxes other than income taxes increased by \$2,504 million, or 38.7%, mainly due to an increase in mineral extraction taxes in Russia. This is explained by an increase in the tax rate following the increase of international crude oil prices.

Application of zero tax rate for crude oil produced in Timan-Pechora and decreased rate for depleted oilfields led to approximately \$1,313 million tax reduction (in 2009 — about \$961 million). The major oilfield where we benefited from zero extraction tax rate was the Yuzhnoye Khylychuyu field. In early December 2010, accumulated volume of production from the Yuzhnoye Khylychuyu field exceeded the incentive level of 15 million tonnes and since that moment we have been paying extraction tax in full.

2009 VS. 2008

In 2009, taxes other than income taxes decreased by 51.9%, or by \$6,990 million, 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 decreased rate for depleted oilfields led to approximately \$961 million tax reduction.

■ 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.

	2010	2009	2008
	(millions of US dollars)		
In Russia			
Excise tax and sales taxes on refined products	951	763	956
Crude oil export tariffs	10,513	6,251	11,911
Refined products export tariffs	3,574	2,306	4,119
Total in Russia	15,038	9,320	16,986
International			
Excise tax and sales taxes on refined products	3,700	3,524	3,984
Crude oil export tariffs	136	107	143
Refined products export tariffs	4	107	227
Total internationally	3,840	3,738	4,354
Total	18,878	13,058	21,340

2010 VS. 2009

In spite of a decrease in crude oil and refined products export volumes, export tariffs increased by \$5,456 million, or by 62.2%, due to an increase in tariff rates in Russia as a result of international crude oil prices growth. The increase in excises in Russia resulted from the ruble appreciation, increase of excise rate and increase in sales volumes.

Starting from the end of 2009, for crude oil produced at certain fields in Eastern Siberia a reduced export duty rate was set. Starting from December, 2010 the Group applies reduced export duty rate for the crude oil produced from the Yu. Korchagin field in the Caspian Sea, however due to relatively small amount of crude oil export from that field the effect of this incentive on our 2010 financial results was insignificant.

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%, 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 vol-

umes 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.

■ LOSS ON DISPOSALS AND IMPAIRMENTS OF ASSETS

2010 VS. 2009

In 2010, loss on disposals and impairments of assets amounted to \$363 million, compared to \$381 million in 2009.

As a result of an impairment test performed in December 2010, we recognized an impairment loss of \$163 million for certain upstream properties in the Timan-Pechora, Western Siberia and Central European regions of Russia; and an impairment loss of \$29 million related to certain our European downstream assets. We also wrote off goodwill related to our Turkish downstream subsidiary in amount of \$114 million due to a change in market conditions partly caused by legislative changes.

2009 VS. 2008

In 2009, loss on disposals and impairments of assets amounted to \$381 million, compared to \$425 million in 2008.

In 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.

■ INCOME TAXES

2010 VS. 2009

In 2010, our total income tax expense increased by \$357 million, or by 17.9%. Income before income tax increased by \$2,407 million, or by 26.6%.

In 2010, our effective income tax rate was 20.5%, compared to 22.0% in 2009, while the maximum statutory rate for the Russian Federation is 20%.

2009 VS. 2008

In 2009, our total income tax expense decreased by \$1,473 million, or by 42.5%, 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).

■ RECONCILIATION OF NET INCOME TO EBITDA (EARNINGS BEFORE INTEREST, INCOME TAXES, DEPRECIATION AND AMORTIZATION)

	2010	2009	2008
	(millions of US dollars)		
Net income	9,006	7,011	9,144
Add back:			
Income tax expense	2,351	1,994	3,467
Depreciation and amortization	4,154	3,937	2,958
Interest expense	712	667	391
Interest and dividend income	(174)	(134)	(163)
EBITDA	16,049	13,475	15,797

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

	2010	2009	2008
	(millions of US dollars)		
Net cash provided by operating activities	13,541	8,883	14,312
Net cash used in investing activities	(7,296)	(8,551)	(13,559)
Net cash (used in) provided by financing activities	(6,146)	(285)	763

OPERATING ACTIVITIES

Our primary source of cash flow is funds generated from our operations. During 2010, cash generated by operating activities amounted to \$13,541 million, which is 52.4% more than in 2009, mainly due to an increase in net revenue. On the other hand, our operating cash flows were affected by an increase in working capital by \$826 million, compared to January 1, 2010. But this increase was relatively small, compared to 2009, when our working capital increased by \$2,483 million.

The increase of working capital was mainly caused by:

- a \$813 million net increase in inventory
- a \$783 million net increase in trade accounts receivable and payable
- a \$134 million net increase in other assets and liabilities

At the same time, the negative effect from the above mentioned factors was partly offset by an \$830 million net decrease in VAT accounts receivable and a \$74 million net decrease in other taxes accounts receivable and payable.

INVESTING ACTIVITIES

The decrease in cash used in investing activities resulted from a decrease in payments for acquisitions by \$1,541 million. Our capital expenditures, including non-cash transactions, increased by \$310 million, or 4.7%, compared to the previous year.

In 2010, we paid \$800 million as a second installment within the acquisition of LUKARCO and invested

\$122 million in common stock of National oil consortium, a joint venture of five major Russian oil companies involved into exploration activities in Venezuela.

In 2009, we paid the remaining amount of \$1,066 million for the acquisition of a 49% stake in the ISAB refinery complex, approximately \$600 million within the acquisition of 45% interest in the TRN refinery, and settled a \$150 million liability within the acquisition of Akpet. Other acquisitions refer to advances for downstream assets in Russia.

FINANCING ACTIVITIES

In 2010, net movements of short-term and long-term debt generated an inflow of \$35 million, compared to an inflow of \$1,489 million in 2009.

In December 2010, we completed the issuance of \$1.5 billion 2.625% senior unsecured convertible bonds due June 2015. The bonds are convertible into LUKOIL ADRs listed on the London Stock Exchange each representing one ordinary share of LUKOIL. The bonds were issued by a Group company at 100% of their principal amount with the conversion price set at \$73.7087 per LUKOIL ADR. Bondholders will be able to convert their bonds into LUKOIL ADRs at any point from 40 days after the issue date to the sixth dealing day prior to the final maturity date. We will have the right to redeem the bonds at any time after December 31, 2013.

In November 2010, we completed the issuance of a dual-tranche offering of 6.125% notes due 2020 in aggregate principal amount of \$1.0 billion. The notes were issued in two tranches at the same time and form part of the same series. \$800 million of the notes were issued at a price of 99.081% of their face value, resulting in a yield to maturity

of 6.25%, and \$200 million of the notes were issued at a price of 102.44% of their face value, resulting in a yield to maturity of 5.80%.

As a part of Company's shares purchase option from a subsidiary of ConocoPhillips, in September 2010, a Group company purchased a series of equity-linked notes exchangeable for 17,500,000 LUKOIL ADRs issued by UniCredit Bank AG for approximately \$980 million.

In August 2010, we raised a \$1.5 billion loan facility from a group of banks due in one year. The facility was partially prepaid in November 2010 in amount of \$1.0 billion.

In August 2010, we purchased approximately 7.599% of our shares at \$53.25 per share for approximately \$3.44 billion from a subsidiary of ConocoPhillips.

In June 2009, we completed offering of three series of stock exchange bonds on MICEX, altogether worth 15 billion rubles. Coupon rate for each of the issues was set at 13.5%. The bonds had maturity period of 364 days and were repaid in June 2010.

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. All these loans were repaid in 2009.

■ CREDIT RATING

In November 2010, 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 October 2010, Moody's affirmed the Company's long-term corporate family rating and long-term issuer rating of Baa2 with stable outlook.

In February 2011, Fitch Ratings affirmed the Company's long-term issuer default rating of BBB- with stable outlook and short-term issuer default rating of F3.

Our credit ratings have not changed since then.

■ ANALYSIS OF CAPITAL EXPENDITURES

	2010	2009	2008
	(millions of US dollars)		
Capital expenditures¹			
Exploration and production			
Russia	3,936	3,916	6 813
International	997	771	1,076
Total exploration and production	4,933	4,687	7,889
Refining, marketing and distribution			
Russia	945	808	1,346
International	375	508	721
Total refining, marketing and distribution	1,320	1,316	2,067
Chemicals			
Russia	27	13	23
International	49	100	98
Total chemicals	76	113	121
Power generation and distribution	420	283	364
Other	95	135	148
Total capital expenditures	6,844	6,534	10,589
Acquisitions of subsidiaries²			
Exploration and production			
Russia	–	–	4
International	922	300	357
Total exploration and production	922	300	361
Refining, marketing and distribution			
Russia	7	212	636
International	3	2,069 ³	1,397
Total refining, marketing and distribution	10	2,281	2,033
Power generation and distribution	–	10	3,191 ⁴
Other	–	1	3
Less cash acquired	–	(19)	(190)
Total acquisitions	932	2,573	5,398

¹ Including non-cash transactions and prepayments.

² Including prepayments related to acquisitions of subsidiaries 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 2010, our capital expenditures, including non-cash transactions, increased by \$310 million, or 4.7%, compared to the previous year. Our capital expenditures in exploration and production increased by \$246 million, or by 5.2%. Our capital expenditures in Iraq in 2010 included payment of \$112 million non-recoverable signature bonus for entering West Qurnah-2 project. In April 2010, we started commercial production on the Yu. Korchagin

field in the Caspian Sea. 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.

Capital expenses of our power generation and distribution entities related to fulfillment of their investment program.

The table below shows our exploration and production capital expenditures in promising new production regions.

	2010	2009	2008
	(millions of US dollars)		
Northern Timan-Pechora	285	385	1,878
Yamal	162	131	161
Caspian region ¹	370	532	420
Ghana	87	73	34
Cote d'Ivoire	92	31	11
Iraq	172	–	–
Total	1,168	1,152	2,504

¹Russian and international projects.

■ CONTRACTUAL OBLIGATIONS, OTHER CONTINGENCIES AND OFF BALANCE SHEET ARRANGEMENTS

■ CAPITAL COMMITMENTS AND CONTRACTUAL OBLIGATIONS

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 \$720 million related to various production sharing agreements over the next 27 years.

The Company has signed a three-year agreement for the years 2010–2012 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 2011 to be approximately \$1,139 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 2011 to be approximately \$349 million.

The Group has a commitment to execute the capital construction program of its power generation segment 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, including its extension by the end of 2013. As of December 31, 2010, the Group estimates the amount of this commitment to be approximately \$660 million.

The following table displays our total contractual obligations and other commitments:

(millions of US dollars)	Total	2011	2012	2013	2014	2015	After
On balance sheet							
Short term debt	794	794	–	–	–	–	–
Long-term bank loans and borrowings	2,071	954	337	378	129	119	154
Long-term non-bank loans and borrowings	1,693	53	51	50	24	21	1,494
6.375% Non-convertible US dollar bonds, maturing 2014	896	–	–	–	896	–	–
2.625% Convertible US dollar bonds, maturing 2015	1,388	–	–	–	–	1,388	–
6.356% Non-convertible US dollar bonds, maturing 2017	500	–	–	–	–	–	500
7.250% Non-convertible US dollar bonds, maturing 2019	595	–	–	–	–	–	595
6.125% Non-convertible US dollar bonds, maturing 2020	998	–	–	–	–	–	998
6.656% Non-convertible US dollar bonds, maturing 2022	500	–	–	–	–	–	500
7.10% Russian ruble bonds, maturing 2011	262	262	–	–	–	–	–
13.35% Russian ruble bonds, maturing 2012	820	–	820	–	–	–	–
9.20% Russian ruble bonds, maturing 2012	328	–	328	–	–	–	–
7.40% Russian ruble bonds, maturing 2013	197	–	–	197	–	–	–
Capital lease obligations	152	62	20	20	20	20	10
TOTAL	11,194	2,125	1,556	645	1,069	1,548	4,251
Off balance sheet							
Operating lease obligations	846	220	168	130	110	100	118
Capital commitments in PSAs	720	662	20	2	2	2	32
Capital commitments of power generating segment	660	345	169	146	–	–	–
Obligation under contract with OOO Eurasia Drilling Company	1,139	1,139	–	–	–	–	–
Obligation under contract with ZAO Globalstroy-Engineering	349	349	–	–	–	–	–

■ 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 to the Bankruptcy Court and requesting the case be heard by the 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 were stayed pending further order of the Court. On July 7, 2010, the District Court denied ADC’s Motion for Withdrawal of reference and returned the case to the Bankruptcy Court for the determination of the Company’s Motion for Remand and Abstention seeking return of the case to the Colorado state court. On October 28, 2010, the Bankruptcy Court granted the Company’s Motion for Remand and Abstention and remanded the case to the Denver District Court (Colorado state court) where it is now pending. ADC is expected to commence discovery regarding general jurisdiction shortly after the Court holds a status conference on March 18, 2011. Management intends to contest jurisdiction and denies all material allegations against the Company. Management does not believe that the ultimate resolution of this matter will have a material adverse effect on the Group’s financial condition.

As of the date the financial statements were available to be issued 76 claims in relation to a violation of the anti-monopoly regulation were initiated against several Group companies in Russia and abroad. The Group companies were accused of violations primarily involving abuse of their dominant market position and execution of coordinated actions in oil products retail markets.

In 2008 and 2009, the Federal Anti-monopoly Service of the Russian Federation (“FAS of Russia”) considered two cases which resulted in decisions being issued against a number of 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.

As for the first case, the Group refinery plants appealed the decisions of FAS of Russia in the Moscow Arbitration Court. These appeals were combined in one proceeding. In addition the Group’s refinery plants appealed against the administrative fines accrued by FAS of Russia to the courts in their locations. Due to abandonment of the claim by the Group’s refinery plants the combined proceeding was terminated on December 13, 2010. Due to the same reason appeals against the administrative fines of the Group’s refinery plants have also been terminated. The Group’s refinery plants filed an application to FAS of

Russia asking for payment deferrals for the fines accrued. As of the date the financial statements were available to be issued, deferral has been approved for some of the Group's refineries. The remaining applications are under consideration.

As for the second case, the Group's refinery plants filed claims against the decisions of FAS of Russia and administrative fines accrued. Due to the signing of the agreement between FAS of Russia and OOO LUKOIL-Volgogradneftepererabotka, OOO LUKOIL-Nizhegorodnefteorgsintez and OOO LUKOIL-Permnefteorgsintez fines were significantly reduced and lawsuits were terminated. A similar agreement is agreed to be signed with OOO LUKOIL-UNP. Currently, proceedings on this case are stayed. OOO LUKOIL-Nizhegorodnefteorgsintez has already paid the fines. FAS of Russia approved payment deferrals for OOO LUKOIL-Volgogradneftepererabotka and OOO LUKOIL-Permnefteorgsintez. OOO LUKOIL-UNP is going to file an application for payment deferrals to FAS of Russia.

The total amount of administrative penalties claimed from the Group which are estimated to be possible and probable is currently \$106 million, of which a provision of \$96 million was accrued in the Group's consolidated financial statements as of December 31, 2010 as probable to be paid. These expenses were included in "Other non-operating expense" of the consolidated statements of income.

On February 9, 2011, FAS of Russia filed a new lawsuit against the three largest Russian oil companies, including the Company, accusing them of abuse of their dominant position in the oil products market. However, the Company is not aware of the claim details until the case starts being considered. The order of legal proceedings has not been received by the Company as of the date the financial statements were available to be issued.

In March 2010, an ethanol purchase agreement signed by Getty Petroleum Marketing Inc., a Group Company, and Bionol Clearfield LLC came into force. The initial term of the agreement was five years. On June 1, 2010, Getty Petroleum Marketing Inc. filed an Arbitration claim to make amendments to the ethanol purchase agreement and to compensate for losses. On June 18, 2010, Bionol Clearfield LLC filed a counter-claim to the Arbitration tribunal of the American Arbitration Association with examination of a case in Boston to execute the agreement or to pay compensation. The amount of the claim of Bionol Clearfield LLC is \$250 million. The counterparties came to an agreement about the schedule of court hearings and documents submission. Hearings began on February 16, 2011. At this time it is not possible to predict whether any of the issues in the Arbitration are remote or probable, or the likely outcome of the Arbitration. Management does not believe that the ultimate resolution of this matter will have a material adverse effect on the Group's financial condition.

The Group is involved in cost recovery disputes with the Republic of Kazakhstan. The Group's share of the claim is approximately \$244 million. Management is of the view that substantially all of the amounts subject to dispute are in fact recoverable under the Final Production Sharing Agreement. Management believes that the ultimate resolution of the claim 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.

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.

■ 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 December 2010, the FASB issued Accounting Standards Update ("ASU") No. 2010-29, "Disclosure of Supplementary Pro Forma Information for Business Combinations." This ASU requires that the pro forma information be presented at if the business combination occurred at the beginning of the prior annual reporting period for purposes of calculating both the current reporting period and the prior reporting period pro forma financial information. The ASU also requires that this disclosure be accompanied by a narrative description of the amount and nature of material nonrecurring pro forma adjustments. The ASU No. 2010-29 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010-29 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In December 2010, the FASB issued ASU No. 2010-28, "When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts." This ASU modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. As a result, ASU No. 2010-28 is eliminating an entity's ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative despite the existence of qualitative factors that indicate

the goodwill is more likely than not impaired. Therefore, goodwill impairments may be reported sooner than under current practice. The ASU No. 2010-28 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010-28 for the 2010 annual financial statements. This adoption did not have a material impact on the Group's results of operations, financial position or cash flows.

In July 2010, the FASB issued ASU No. 2010-20, "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," which amends Accounting Standards Codification ("ASC") No. 310, "Receivables." This ASU provides financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables and requires entities provide disclosures that facilitate financial statement users' evaluation of the following: 1) the nature of credit risk inherent in the entity's portfolio of financing receivables; 2) how that risk is analyzed and assessed in arriving at the allowance for credit losses; 3) the changes and reasons for those changes in the allowance for credit losses. The ASU No. 2010-20 is effective for the Group for the reporting periods ending after December 15, 2010. The Group adopted ASU No. 2010-20 for the 2010 annual financial statements. This

adoption did not have a material impact on the Group's results of operations, financial position or cash flows and did not require additional disclosures.

In January 2010, the FASB issued ASU No. 2010-06, "Improving Disclosures about Fair Value Measurements," which requires reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information about purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair-value measurements. This ASU also clarifies existing fair-value measurement disclosure guidance about the level of disaggregation, inputs, and valuation techniques. ASU No. 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for the detailed Level 3 roll forward disclosures (which are effective for the annual reporting periods starting after December 15, 2010 and for interim periods within those annual reporting periods). The Group adopted the requirements of ASU No. 2010-06 (except for the detailed Level 3 roll forward disclosures) starting from the first quarter of 2010. 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
- 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

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

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.

REFERENCE INFORMATION

The most complete and up-to-date information about LUKOIL can always be found on the Company's website: www.lukoil.ru (Russian) or www.lukoil.com (English).

The site also provides information about trends and results of LUKOIL's business, as well as accurate and up-to-date information about events concerning the Company and the whole spectrum of LUKOIL activities, including details of the Company's social and environmental policies.

The Investor Center section of the site presents the company's financial and industrial results, dividend history, share prices, an investor calculator, presentations for investors, and Company reports.

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■ Published reports

Electronic versions of the following reports are available on the Company web site:

1. Report on Company Business.
2. Consolidated Financial Accounts.
3. Quarterly Consolidated Financial Accounts.
4. Management Discussion and Analysis of Financial Situation and Results of Operations
5. Analyst DataBook.
6. Fact book

■ Concepts and abbreviations used in the 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 2010 (30.37 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.

■ 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



www.lukoil.com