

**Open Joint Stock
Company
“Kazanorgsintez”**

Consolidated Financial Statements
For the Year Ended 31 December 2007

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

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OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

STATEMENT OF MANAGEMENT’S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

The following statement, which should be read in conjunction with the independent auditors’ responsibilities stated in the independent auditors’ report set out on pages 2-3, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements of Open Joint Stock Company “Kazanorgsintez” and its subsidiaries (the “Group”).

Management is responsible for the preparation of consolidated financial statements that present fairly the financial position of the Group at 31 December 2007, and the consolidated results of its operations, changes in shareholders’ equity and cash flows for the year then ended, in accordance with International Financial Reporting Standards (“IFRS”).

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

- Selecting suitable accounting principles and applying them consistently;
- Making judgements and estimates that are reasonable and prudent;
- Stating whether IFRS have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- Preparing the consolidated financial statements on a going concern basis, unless it is inappropriate to presume that the Group will continue in business for the foreseeable future.

Management, within its competencies, is also responsible for:

- Designing, implementing and maintaining an effective system of internal controls throughout the Group;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking steps to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2007 were approved on 28 May 2008 in Kazan, Republic of Tatarstan, Russian Federation, by:



L. S. Alekhin
General Director



N. F. Gaynullina
Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of Open Joint Stock Company "Kazanorgsintez":

We have audited the accompanying consolidated financial statements of Open Joint Stock Company "Kazanorgsintez" and its subsidiaries (the "Group"), which comprise of the consolidated income statement for the year ended 31 December 2007, the consolidated balance sheet as at 31 December 2007, and the consolidated statements of changes in shareholders' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2007, and of its consolidated financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.



Moscow, Russia
28 May 2008

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

CONSOLIDATED INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

	Note	2007	2006
Sales	5	21,194,194	15,383,982
Cost of sales	6	(15,174,159)	(9,859,380)
Gross profit		6,020,035	5,524,602
Selling, general and administrative expenses	7	(2,529,681)	(2,026,232)
Loss from other sales, net		(168,806)	(194,003)
Finance costs, net	8	(339,024)	(152,174)
Income from investments, net	9	58,380	43,152
Foreign exchange gain, net		542,681	147,211
Other expenses, net	10	(195,927)	(154,894)
Profit before income tax		3,387,658	3,187,662
Income tax expense	11	(833,749)	(676,383)
Profit for the period		2,553,909	2,511,279
Attributable to:			
Shareholders of the parent company		2,552,980	2,523,545
Minority interest		929	(12,266)
		2,553,909	2,511,279
EARNINGS PER SHARE (RUR)			
Basic and diluted	28	1.42	1.40

OPEN JOINT STOCK COMPANY "KAZANORGSINTEZ"

CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 2007 (in thousands of Russian roubles)

	Notes	31 December 2007	31 December 2006
ASSETS			
NON-CURRENT ASSETS:			
Property, plant and equipment	12	34,840,461	24,873,904
Intangible assets	13	23,866	32,599
Other financial assets	14	52,100	52,100
Investments in associates	15	24,789	29,278
Advances paid for licenses	16	1,039,946	1,039,946
		<u>35,981,162</u>	<u>26,027,827</u>
CURRENT ASSETS:			
Inventories	17	3,073,991	2,257,163
Trade and other receivables	18	1,343,919	1,748,689
Income tax prepaid		56,533	-
Other prepaid and recoverable taxes	19	1,009,304	472,935
Cash and cash equivalents	20	455,205	784,163
		<u>5,938,952</u>	<u>5,262,950</u>
TOTAL ASSETS		<u>41,920,114</u>	<u>31,290,777</u>
EQUITY AND LIABILITIES			
EQUITY AND RESERVES:			
Share capital	21	1,904,710	1,904,710
Treasury shares	21	(7,712)	(46,251)
Additional paid-in capital	21	1,515,015	1,515,015
Retained earnings		11,691,746	9,801,397
Equity attributable to shareholders of the parent company		<u>15,103,759</u>	<u>13,174,871</u>
Minority interest		32,253	31,324
		<u>15,136,012</u>	<u>13,206,195</u>
NON-CURRENT LIABILITIES:			
Long-term borrowings	22	11,747,017	11,301,384
Deferred tax liabilities	11	1,498,196	1,214,125
Obligations under finance leases	23	91,359	79,082
		<u>13,336,572</u>	<u>12,594,591</u>
CURRENT LIABILITIES:			
Short-term borrowings	24	9,341,818	925,145
Trade payables	25	2,020,485	2,325,933
Other payables and accrued liabilities	26	1,078,559	686,942
Advances received from customers		855,078	1,380,324
Income tax payable		-	13,560
Other taxes payable	27	151,590	158,087
		<u>13,447,530</u>	<u>5,489,991</u>
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		<u>41,920,114</u>	<u>31,290,777</u>

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

	Notes	Equity attributable to shareholders of the parent company				Minority interest	Total equity	
		Share capital	Treasury shares	Additional paid-in capital	Retained earnings			Total
Balance at 31 December 2005		1,904,710	-	1,515,015	7,577,999	10,997,724	43,590	11,041,314
Profit for the period		-	-	-	2,523,545	2,523,545	(12,266)	2,511,279
Dividends	29	-	-	-	(300,147)	(300,147)	-	(300,147)
Re-acquisition of issued shares		-	(81,300)	-	-	(81,300)	-	(81,300)
Re-issuance of ordinary shares from treasury shares		-	35,049	-	-	35,049	-	35,049
Balance at 31 December 2006		1,904,710	(46,251)	1,515,015	9,801,397	13,174,871	31,324	13,206,195
Profit for the period		-	-	-	2,552,980	2,552,980	929	2,553,909
Dividends	29	-	-	-	(662,631)	(662,631)	-	(662,631)
Re-acquisition of issued shares		-	(9,359)	-	-	(9,359)	-	(9,359)
Re-issuance of ordinary shares from treasury shares		-	47,898	-	-	47,898	-	47,898
Balance at 31 December 2007		1,904,710	(7,712)	1,515,015	11,691,746	15,103,759	32,253	15,136,012

OPEN JOINT STOCK COMPANY "KAZANORGSINTEZ"

CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

	Notes	2007	2006
OPERATING ACTIVITIES:			
Cash flows from operations	30	2,578,855	5,810,126
Income tax paid		(458,725)	(152,454)
Interest paid		(1,338,430)	(773,783)
Net cash generated from operating activities		781,700	4,883,889
INVESTING ACTIVITIES:			
Purchase of property, plant and equipment		(10,066,527)	(10,587,399)
Proceeds on disposal of property, plant and equipment		55,448	159,412
Advances paid for licences		-	(356,281)
Proceeds on disposal of equity investments		19,392	-
Interest received		8,217	40,230
Dividends received		15	5,445
Net cash used in investing activities		(9,983,455)	(10,738,593)
FINANCING ACTIVITIES:			
Proceeds from short-term borrowings		7,125,123	1,428,083
Repayments of short-term borrowings		(4,310,297)	(1,726,424)
Proceeds from long-term borrowings		8,519,279	13,666,544
Repayments of long-term borrowings		(1,983,814)	(6,796,824)
Dividends paid		(359,828)	(74,757)
Re-acquisition of issued shares		(9,359)	(81,300)
Proceeds on re-issuance of ordinary shares from treasury shares		47,898	35,049
Repayment of obligations under finance leases		(180,851)	(265,600)
Net cash generated from financing activities		8,848,151	6,184,771
Net (decrease)/increase in cash and cash equivalents		(353,604)	330,067
Cash and cash equivalents at beginning of the period		784,163	426,320
Effect of exchange rate changes on cash held in foreign currencies		24,646	27,776
Cash and cash equivalents at end of the period		455,205	784,163
Non-cash transactions			
Property, plant and equipment acquired under finance lease agreements		289,193	166,273

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 *(in thousands of Russian roubles)*

1. GENERAL

Organisation

Open Joint Stock Company “Kazanorgsintez” (the “Company”) was incorporated in Kazan, Republic of Tatarstan, Russian Federation on 1 September 1993. The principal activity of the Company and its subsidiaries (the “Group”) is production of chemical products and derivatives thereof (mainly polyethylene) which are marketed and sold primarily in the Russian Federation.

The major production facilities of the Group are located in Kazan, Republic of Tatarstan, Russian Federation. The registered office of the Company is situated at 101, Belomorskaya Street, 420051, Kazan, Republic of Tatarstan, Russian Federation.

Details of the Company’s subsidiaries are in note 34.

Going concern assumption

At 31 December 2007, the Group’s current liabilities exceeded its current assets by RUR 7,508,578 thousand. Therefore, the Group is in violation of certain financial covenants related to outstanding bonds and accordingly, this obligation has been classified as a current liability.

Management is in discussion with lenders, and believes that the possibility that the banks and other major creditors of the Group will demand early repayment of outstanding amounts solely because of the working capital deficiency is low. Management has credit facilities for its day to day activities, and management has prepared a detailed cash flow forecasts and believes that future cash flows from operating and financing activities will be sufficient for the Group to meet its obligations as they become due (refer to note 35).

2. ADOPTION OF NEW AND REVISED STANDARDS

Standards and Interpretations effective in the current period

In the current year, the Group has adopted all new International Financial Reporting Standards (“IFRS”) and interpretations issued by International Financial Interpretation Reporting Interpretation Committee (“IFRIC”) that are mandatory for adoption in the annual periods beginning on or after 1 January 2007. Adoption of these standards and interpretations did not have any effect on the consolidated financial performance or position of the Group; however it did give rise to additional disclosures.

The principal effects of these changes are as follows:

IAS 1 Presentation of Financial Statements (amendment)

This amendment requires the Group to provide new disclosures to enable users of the financial statements to evaluate the Group’s principal objectives; policies and procedures for managing capital (refer to note 33).

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

IFRS 7 Financial Instruments: Disclosures

This standard introduces new disclosures that enable users of the financial statements to evaluate the significance of the Group’s financial instruments and the nature and extend of risks arising from those financial instruments. The new or expanded disclosures are included throughout the consolidated financial statements.

There are four interpretations issued by IFRIC effective for the current period. These are: IFRIC 7 *Applying the Restatement Approach Under IAS 29 Financial Reporting in Hyperinflationary Economies*, IFRIC 8 *Scope of IFRS 2*; IFRIC 9 *Reassessment of Embedded Derivatives*; and IFRIC 10 *Interim Financial Reporting and Impairment*. The adoption of these interpretations has not led to any changes in the Group’s accounting policies or disclosures provided in the consolidated financial statements.

Standards and Interpretations in issue not yet adopted

At the date of authorisation of these consolidated financial statements, the following Standards and Interpretations were in issue but not yet effective:

Standards and Interpretations	Effective for annual periods beginning on or after
IAS 1 <i>Presentation of Financial Statements (amendment)</i>	1 January 2009
IAS 23 <i>Borrowing Costs (amendment)</i>	1 January 2009
IAS 27 <i>Consolidated and Separate Financial Statements (amendment due to revision of IFRS 3)</i>	1 July 2009
IAS 28 <i>Investments in Associates (amendments due to revision of IFRS 3)</i>	1 July 2009
IAS 31 <i>Investments in Joint Ventures (amendments due to revision of IFRS 3)</i>	1 July 2009
IAS 32 <i>Financial Instruments: Presentation (amendment)</i>	1 January 2009
IFRS 2 <i>Share-based Payment (amendment)</i>	1 January 2009
IFRS 3 <i>Business Combinations (revised on applying the acquisition method)</i>	1 July 2009
IFRS 8 <i>Operating Segments</i>	1 January 2009
IFRIC 11 <i>IFRS 2 – Group and Treasury Share Transactions</i>	1 March 2007
IFRIC 12 <i>Service Concession Arrangements</i>	1 January 2008
IFRIC 13 <i>Customer Loyalty Programmes</i>	1 July 2008
IFRIC 14 <i>IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction</i>	1 January 2008

Management anticipates that the adoption of these Standards and Interpretations in the preparation of the consolidated financial statements in future periods will have no material impact on the consolidated financial statements of the Group.

Certain comparative information, presented in the consolidated financial statements for the prior reporting periods, has been reclassified in order to achieve comparability with the presentation used in the consolidated financial statements for the year ended 31 December 2007. Certain costs were reclassified between cost of sales, selling, administrative and general expenses and cost of other sales. Those reclasses did not affect net profit for the year ended 31 December 2006.

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

3. SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards.

Basis of preparation

The financial statements have been prepared on the historical cost basis except for the valuation of certain financial instruments. The principal accounting policies are set out below.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities (including special purpose entities) controlled by the Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Minority interests in the net assets (excluding goodwill) of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination (see below) and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Business combinations

Acquisitions of subsidiaries and businesses are accounted for using the purchase method. The cost of the business combination is measured as the aggregate of the fair values of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 *Business Combinations* are recognised at their fair values at the acquisition date, except for non-current assets that are classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 *(in thousands of Russian roubles)*

Investments in associates

An associate is an entity over which the Group has significant influence and that is not a subsidiary. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate) are not recognised, unless the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of the investment. Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

Special purpose entities

Special purpose entities (“SPEs”) are those undertakings that are created to satisfy specific business needs of the Group and the Group has the right to the majority of the benefits of the SPE, or exposed to risks associated with activities of the SPE.

SPEs are consolidated in the same manner as subsidiaries when the substance of the relationship indicates that the SPE is controlled by the Group.

Goodwill

Goodwill arising on the acquisition of a subsidiary represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary recognised at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

The Group's policy for goodwill arising on the acquisition of an associate is described under “Investments in associates” above.

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable.

Sale of goods

Revenue from the sale of goods is recognised when all the following conditions are satisfied:

- The Group has transferred to the buyer the significant risks and rewards of ownership of the goods, which is typically at the date of loading to third party for transportation;
- The Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the entity; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

Revenue from rendering of services is recognised at the time the services are provided.

Dividend, interest and other revenue

Dividend revenue from investments is recognised when the Group's right to receive payment has been established.

Interest revenue is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

The income from other sales includes revenues from sale of auxiliary items, net of cost of sales. Other sales primarily consist of sales of electricity, water and heat.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs (see below). Contingent rentals are recognised as expenses in the periods in which they are incurred.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 *(in thousands of Russian roubles)*

Foreign currencies

The functional currency of the Company and all its subsidiaries, which reflects the economic substance of their operations, and presentation currency of the consolidated financial statements of the Group, is the Russian rouble (“RUR”).

In preparing the financial statements of the individual entities, transactions in currencies other than the entity’s functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in profit or loss in the period in which they arise.

Borrowing costs

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

All other borrowing costs are recognised in the consolidated income statement in the period in which they are incurred.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

Current tax

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

Deferred tax

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

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 *(in thousands of Russian roubles)*

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

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

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

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

Current and deferred tax for the period

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

Property, plant and equipment

Property, plant and equipment held for use in the production or supply of goods or services, or for administrative purposes, are stated in the balance sheet at their cost less any accumulated depreciation and accumulated impairment losses.

Capitalised cost includes acquisition cost and major expenditures for improvements and replacements that extend the useful lives of the assets or increase their revenue generating capacity. Repair and maintenance expenditures that do not meet the foregoing criteria for capitalisation are charged to the income statement as incurred.

Depreciation is computed under the straight-line method utilizing the estimated useful lives of the assets, which are:

Buildings	20-80 years
Machinery and equipment	5-30 years
Other	3-10 years

Land occupied by the Group’s facilities is owned by the Group. Land is not depreciated and is included in property, plant and equipment.

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Assets held under finance leases are depreciated over their expected useful lives on the same basis as similar owned assets or, where shorter, the term of the relevant lease.

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

Construction in progress

Construction in progress comprises costs directly related to construction of property, plant and equipment including an appropriate allocation of directly attributable variable overheads that are incurred in construction. Depreciation of constructed assets commences when the assets are put into operation.

Intangible assets

Intangible assets acquired separately are reported at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged on a straight-line basis over their estimated useful lives.

The estimated useful life and amortisation method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Software costs incurred for the development, implementation and enhancement of the operating systems, are capitalised and amortised over the expected useful life of the system. Software costs relating to the maintenance of the operating system are recognised as an expense in the period in which they occur.

Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss.

If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

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

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Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour, transportation, handling costs and those overhead costs that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method. Net realisable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Work in progress and semi-finished products are valued at the net unit cost of production allocated to the estimated stage of completion.

Provisions

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

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

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

Cash and cash equivalents

Cash and cash equivalents include cash on hand, cash with banks, deposits and marketable securities with original maturity of three months or less.

Financial assets

Financial assets, except for cash and cash equivalents and financial assets out of scope of IAS 39 (Revised), Financial Instruments: Recognition and Measurement, are classified into the following specified categories: financial assets as “at fair value through profit or loss” (“FVTPL”), “held-to-maturity” (“HTM”) investments, “available-for-sale” (“AFS”) financial assets and “loans and receivables”. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

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

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

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Financial assets at FVTPL

The Group classifies financial assets as at FVTPL if:

- They have been acquired principally for the purpose of selling in the near future; or
- They are a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking.

HTM investments

Debt securities with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity are classified as HTM investments. HTM investments are recorded at amortised cost using the effective interest method less impairment, with income recognised on an effective yield basis.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for-sale financial assets are measured at fair value with gains and losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in equity is included in the income statement.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the closing of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques.

Dividends on AFS equity instruments are recognised in the consolidated income statement when the Group's right to receive payments is established.

Loans and receivables

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

Impairment of financial assets

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

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

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With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognised impairment loss is reversed through the consolidated income statement to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognised. Any increase in fair value of AFS equity securities subsequent to an impairment loss is recognised directly in equity.

Financial liabilities and equity instruments issued by the Group

Classification as debt or equity

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

Financial liabilities

Financial liabilities, including borrowings, trade and other payables are initially measured at fair value, net of transaction costs, and subsequently measured at amortised cost using the effective interest method.

Equity instruments

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

Employee benefit obligations

Remuneration to employees in respect of services rendered during a reporting period are recognised as an expense in that period.

The Group’s Russian subsidiaries are legally obliged to make defined contributions to the Russian Federation State Pension Fund. These contributions are recognised in the income statement as incurred.

In the Russian Federation all obligatory social contributions, including contributions to the Russian Federation State Pension Fund, are collected through a unified social tax (“UST”) calculated by the application of a regressive rate from 26% to 2% of the annual gross remuneration of each employee. UST is allocated to three state social funds, including the Russian Federation State Pension Fund at the rates varying from 20% to 2% of the annual gross remuneration of each employee. UST is recognised as an expense when employees have rendered service entitling them to the contributions.

Labour expenses include the amount of contribution to the Pension fund of the Russian Federation of RUR 363,887 thousand (year ended 31 December 2006 – RUR 287,861 thousand).

Segment reporting

The majority of the Group’s business operations are located in the Russian Federation and relate primarily to the production and marketing of chemical products and derivatives thereof (mainly ethylene and polyethylene). Therefore, business activities are subject to the same risks and returns and are addressed in the consolidated financial statements of the Group as one reportable segment.

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Dividends declared

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

Accumulated profit legally distributable by the Company are based on the amounts available for distribution in accordance with the applicable legislation and as reflected in the statutory financial statements of the individual entities of the Group. These amounts may differ significantly from the amounts calculated on the basis of IFRS.

Treasury shares

When Group companies purchase the Company’s equity share capital, the consideration paid including any attributable transaction costs is deducted from total equity as treasury shares until they are re-sold. When such shares are subsequently sold, any consideration received is included, net of associated income tax in equity. Treasury shares are recorded at cost. The gains (losses) arising from treasury share transactions are recognized as a movement in the consolidated statement of changes in shareholders’ equity.

Value-added tax

Value-added tax (“VAT”) related to sales is payable to the tax authorities on an accrual basis based upon invoices issued to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales.

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTIES

In the application of the Group’s accounting policies management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Critical judgements in applying accounting policies

The following are the critical judgements, apart from those involving estimations, that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognised in financial statements.

Taxation

Judgements are required in determining current income tax liabilities. The Group recognises liabilities for taxes based on estimates of whether additional taxes will be due. Where the final outcome of various tax matters is different from the amounts that were initially recorded, such differences will impact income tax and deferred tax provisions in the period in which such determination is made.

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The Group has not recognised a deferred tax liability in respect of temporary differences associated with investments in subsidiaries. The Group controls the timing of the reversal of those temporary differences and does not expect their reversal in the foreseeable future.

Environmental obligations

The Group’s activities are subject to various laws and regulations governing the protection of the environment. The Group pays fees to the regulatory authorities for the right to discharge within legal norms. Management believes this fee covers all environmental obligations, and this fee is recorded as an expense in the period incurred. No provisions for environmental obligations are recorded.

Key sources of estimation uncertainty

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

Useful economic lives of property, plant and equipment

Management assesses the useful economic lives of property, plant and equipment considering the current technical condition of assets and potential changes in technology and demand. Any changes of these conditions could affect prospective depreciation of property, plant and equipment and their carrying value.

Impairment of assets

The Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets are impaired. In making the assessment for impairment, assets that do not generate independent cash flows are allocated to an appropriate cash generating unit. Management necessarily applies its judgement in allocating assets that do not generate independent cash flows to appropriate cash generating units, and also in estimating the timing and value of underlying cash flows within the value in use calculation. Subsequent changes to the cash generating unit allocation or to the timing of cash flows could impact the carrying value of the respective assets.

Allowances for doubtful debts

The Group creates allowances for doubtful debts to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful debts, management bases its estimates on the current overall economic conditions, the aging of accounts receivable balances, historical write-off experience, customer creditworthiness and changes in payment terms.

Changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful debts recorded in the consolidated financial statements.

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5. SALES

	<u>2007</u>	<u>2006</u>
By geographic region:		
Domestic sales	15,356,486	12,568,787
Export sales	5,837,708	2,815,195
Total	<u>21,194,194</u>	<u>15,383,982</u>
By products:		
High density polyethylene	8,076,085	4,806,886
Low density polyethylene	5,467,782	4,878,948
Products produced by Ethylene plant	2,861,947	1,614,033
Organic products	1,967,281	1,890,857
Plastic goods	1,724,995	1,391,286
Bis-Phenol A	83,936	-
Tolling services	1,012,168	801,972
Total	<u>21,194,194</u>	<u>15,383,982</u>

6. COST OF SALES

	<u>2007</u>	<u>2006</u>
Raw materials	9,980,577	5,825,967
Energy and water	1,928,621	1,522,058
Labour costs	1,536,374	1,211,305
Depreciation	1,036,569	610,905
Auxiliary materials	557,615	549,242
Services	357,395	143,315
Other	50,921	83,029
Obsolescence provision (release)/ charge (refer to note 17)	(13,401)	3,193
	<u>15,434,671</u>	<u>9,949,014</u>
Increase in work in progress and finished goods	(260,512)	(89,634)
Total	<u>15,174,159</u>	<u>9,859,380</u>

7. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	<u>2007</u>	<u>2006</u>
General and administrative expenses	1,567,734	1,242,066
Selling expenses	492,849	302,110
Taxes, other than income tax	304,438	327,549
Depreciation and amortization	117,813	105,357
Bank charges	46,847	49,150
Total	<u>2,529,681</u>	<u>2,026,232</u>

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8. FINANCE COSTS, NET

	<u>2007</u>	<u>2006</u>
Interest expense on loans and borrowings	1,357,835	942,937
Interest expense on obligations under finance leases	29,154	24,053
Other expenses	1,287	1,664
Less: amount included in the cost of qualifying assets	<u>(1,049,252)</u>	<u>(816,480)</u>
Total	<u>339,024</u>	<u>152,174</u>

9. INCOME FROM INVESTMENTS, NET

	<u>2007</u>	<u>2006</u>
Income from disposal of subsidiaries	35,244	-
Income from disposal of associate (refer to note 15)	14,785	-
Interest income	8,217	40,230
Income/(loss) from associates (refer to note 15)	119	(2,523)
Dividends received	<u>15</u>	<u>5,445</u>
Total	<u>58,380</u>	<u>43,152</u>

10. OTHER EXPENSES, NET

	<u>2007</u>	<u>2006</u>
Rent of land	203,877	140,078
Maintenance of social infrastructure	24,474	14,744
Other, net	<u>(32,424)</u>	<u>72</u>
Total	<u>195,927</u>	<u>154,894</u>

Maintenance of social infrastructure comprises primarily operating costs of facilities such as hotel, dormitory and other sports facilities.

Expenses for rent of land relate to rent of an idle plot of land in the remote region of Tatarstan Republic, the agreement was concluded at the request of the local tax authorities.

11. INCOME TAX

The Group's provision for income tax is as follows:

	<u>2007</u>	<u>2006</u>
Current income tax	549,678	406,799
Correction of income tax of prior periods	-	(143,960)
Deferred tax	<u>284,071</u>	<u>413,544</u>
Total	<u>833,749</u>	<u>676,383</u>

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The following presents a reconciliation of theoretical income tax calculated at the rate effective in the Russian Federation (24%) to the amount of actual income tax expense recorded in the consolidated income statement:

	<u>2007</u>	<u>2006</u>
Profit before income tax	3,387,658	3,187,662
Theoretical income tax expense at 24%	813,038	765,039
Effect of non-deductible expenses and other permanent differences, net	<u>20,711</u>	<u>(88,656)</u>
Income tax expense	<u>833,749</u>	<u>676,383</u>

Temporary differences between the Russian statutory tax accounts and these financial statements give rise to the following deferred tax liabilities:

	<u>31 December 2007</u>	<u>31 December 2006</u>
Property, plant and equipment	1,526,117	1,227,489
Provision for doubtful debts	(5,082)	(8,208)
Accrued expenses	<u>(22,839)</u>	<u>(5,156)</u>
Deferred tax liabilities, net	<u>1,498,196</u>	<u>1,214,125</u>

The movements in the Group’s deferred tax position were as follows:

	<u>2007</u>	<u>2006</u>
Balance at beginning of the period	1,214,125	800,581
Charge to income statement	<u>284,071</u>	<u>413,544</u>
Balance at end of the period	<u>1,498,196</u>	<u>1,214,125</u>

12. PROPERTY, PLANT AND EQUIPMENT

	<u>Land and buildings</u>	<u>Machinery and equipment</u>	<u>Other assets</u>	<u>Construction in progress</u>	<u>Total</u>
<i>Cost</i>					
At 1 January 2006	7,845,317	10,552,606	1,098,180	6,293,483	25,789,586
Additions	-	48,425	-	11,519,978	11,568,403
Disposals	(16,454)	(206,700)	(6,600)	(159,477)	(389,231)
Transfers	916,908	2,767,831	76,788	(3,761,527)	-
At 31 December 2006	8,745,771	13,162,162	1,168,368	13,892,457	36,968,758
Additions	48,582	252,459	22,322	10,962,695	11,286,058
Disposals	(44,057)	(140,248)	(15,627)	(13,884)	(213,816)
Transfers	1,890,998	3,788,312	461,083	(6,140,393)	-
At 31 December 2007	<u>10,641,294</u>	<u>17,062,685</u>	<u>1,636,146</u>	<u>18,700,875</u>	<u>48,041,000</u>

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	Land and buildings	Machinery and equipment	Other assets	Construction in progress	Total
<i>Accumulated depreciation</i>					
At 1 January 2006	(4,266,243)	(6,902,675)	(397,820)	-	(11,566,738)
Charge for the year	(163,700)	(514,017)	(54,539)	-	(732,256)
Eliminated on disposals	12,194	185,410	6,536	-	204,140
At 31 December 2006	(4,417,749)	(7,231,282)	(445,823)	-	(12,094,854)
Charge for the year	(196,973)	(895,435)	(144,045)	-	(1,236,453)
Eliminated on disposals	8,689	111,932	10,147	-	130,768
At 31 December 2007	(4,606,033)	(8,014,785)	(579,721)	-	(13,200,539)
<i>Net book value</i>					
At 31 December 2006	4,328,022	5,930,880	722,545	13,892,457	24,873,904
At 31 December 2007	6,035,261	9,047,900	1,056,425	18,700,875	34,840,461

The Group's plant sites occupy approximately 473.5 hectares of land for which the Group holds the title. Currently, there is no charge to the Group for land use, except for certain annual taxes, which are expensed as incurred.

At 31 December 2007 property, plant and equipment with a carrying value of RUR 2,379,222 thousand (31 December 2006 – RUR 457,509 thousand) were pledged to secure certain long-term loans granted to the Group (refer to note 22).

During the year ended 31 December 2007 interest of RUR 1,049,252 thousand has been capitalized in property, plant and equipment (year ended 31 December 2006 – RUR 816,480 thousand) (refer to note 8).

At 31 December 2007, property, plant and equipment include assets held under a number of finance lease agreements (refer to note 23) with the carrying value of RUR 703,805 thousand (31 December 2006 – RUR 467,818 thousand). At the end of the lease term the Group takes automatic ownership of the assets. The Group's obligations under finance leases are secured by lessors' title on the leased assets.

13. INTANGIBLE ASSETS

Intangible assets primarily comprise costs incurred in connection with acquisition and implementation of management information system SAP R/3 and are amortised over a period of thirteen years.

	31 December 2007	31 December 2006
Book value	108,964	109,351
Accumulated amortisation	(85,098)	(76,752)
Net book value	23,866	32,599

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14. OTHER FINANCIAL ASSETS

	31 December 2007		31 December 2006	
	% ownership	Amount	% ownership	Amount
OJSC “Tatneftekhiminvestholding”	7%	38,537	7%	38,537
National non-state pension fund	5%	10,557	5%	10,557
OJSC “Kazanskaya yarmarka”	2%	2,950	2%	2,950
Other	-	56	-	56
Total		52,100		52,100

Management was unable to determine the fair value of unquoted shares using valuation techniques that are supported by publicly available market information. As a result, available-for-sale investments are presented at cost, net of impairment provision.

15. INVESTMENTS IN ASSOCIATES

Name of associate	Principal activity	31 December 2007		31 December 2006	
		% ownership	Carrying value	% ownership	Carrying value
LLC “Taif-Invest”	Investing activity	40	24,789	40	24,670
CJSC “Ankorit”	Trading company	-	-	39	4,608
LLC “Novomoskovsky trubny zavod”	Manufacturing	26	-	26	-
Total			24,789		29,278

	2007	2006
Total assets	148,903	1,046,965
Total liabilities	(144,740)	(992,863)
Net assets	4,163	54,102

One of the associates is loss making. The Group has not recognised the losses beyond the value of the investment.

	2007	2006
Group’s share of net assets of associates	24,789	29,278
Total revenue	1,031,389	1,254,774
Total loss for the period	19,680	11,036
Unrecognised share of losses in an associate	6,316	4,998
Group’s share of profit/ (loss) of associates	119	(2,523)

In January 2007, the Group disposed of its share in CJSC “Ankorit” for cash consideration of RUR 19,392 thousand, recording a gain of RUR 14,785 thousand.

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16. ADVANCES PAID FOR LICENSES

Advances paid for licenses are comprised of prepaid amounts for licenses for bis-phenol and polycarbonate plastic and high density polyethylene production technologies.

17. INVENTORIES

	<u>31 December 2007</u>	<u>31 December 2006</u>
Stores and materials	2,158,403	1,615,488
Work in progress and semi-finished products	367,935	241,771
Finished goods	549,908	415,560
Less: provision for obsolescence	<u>(2,255)</u>	<u>(15,656)</u>
Total	<u>3,073,991</u>	<u>2,257,163</u>

One of the Group’s subsidiaries is engaged in the agricultural activities of breeding livestock intended for the production of meat and planting and harvesting of potato and other agricultural products. The aggregated biological assets of this subsidiary are not material to the accompanying Group’s consolidated financial statements and are included in stores and materials.

18. TRADE AND OTHER RECEIVABLES

	<u>31 December 2007</u>	<u>31 December 2006</u>
Trade receivables	604,926	1,102,457
Advances paid	606,841	441,960
Other receivables and prepaid expenses	175,715	294,634
Less: provision for doubtful debts	<u>(43,563)</u>	<u>(90,362)</u>
Total	<u>1,343,919</u>	<u>1,748,689</u>

The prevailing majority of sales of goods are contracted at prepayment basis. Post payment sales are used to promote new types of product to the markets. The maximum credit period on post payment sales of goods is 30 days. In case of delay, interest is charged at 3% (2% for export contracts) per month on the outstanding balance. The Group has analyzed all receivables over 90 days for recoverability, because historical experience indicates that accounts receivable aged between 90 and 180 days are recovered by 50 percent and receivables over 180 days are generally not recoverable. Based on the results of this analysis, and in the cases where the Group has no collateral and no counter liabilities, the Group identified specific accounts and provided fully for the receivables that are past due beyond 180 days and provided 50 percent for the receivables between 90 days and 180 days.

Before accepting any new customer, the Group uses an internal procedure to assess the potential customer’s credit quality and defines credit limits by customer. Only customers, which have long-term relationship with the Company and good credit history, can have contracts with post sales payments. All new customers have to pass an approval procedure, which includes: security check, check of incorporation documents, tax registration, feasibility analysis and credit history.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

Included in the Group’s trade receivable balance are debtors with a carrying amount of RUR 37,523 thousand (2006 - RUR 37,398 thousand) which are past due at the reporting date for which the Group has not provided as the amounts are still considered recoverable. The Group does not hold any collateral over these balances.

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

	31 December 2007	31 December 2006
90-180 days	7,951	2,952
180-365 days	25,375	15,364
1 year – 3 years	4,197	19,082
Total	37,523	37,398

Movement in the provision for doubtful debts:

	31 December 2007	31 December 2006
Balance at beginning of the year	90,362	66,814
Impairment losses recognised on receivables	9,267	27,459
Amounts written off as uncollectible	(49,548)	-
Amounts recovered during the year	(6,518)	(3,911)
Balance at end of the year	43,563	90,362

In determining the recoverability of a trade receivable, the Group considers any change in the credit quality of the trade receivable from the date credit was initially granted up to the reporting date. The concentration of credit risk is limited due to the customer base being large and unrelated. Accordingly, management believes that there is no further credit provision required in excess of the allowance for doubtful debts.

Ageing of impaired trade and other receivables:

	31 December 2007	31 December 2006
90-180 days	253	2,222
180-365 days	5,085	-
1 year – 3 years	21,231	67,700
Over 3 years	16,994	20,440
Total	43,563	90,362

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

19. OTHER PREPAID AND RECOVERABLE TAXES

	<u>31 December 2007</u>	<u>31 December 2006</u>
Value added tax	1,009,304	472,764
Other taxes	-	171
Total	<u>1,009,304</u>	<u>472,935</u>

20. CASH AND CASH EQUIVALENTS

	<u>31 December 2007</u>	<u>31 December 2006</u>
Current accounts, including:		
RUR-denominated	82,086	400,921
USD-denominated	89,270	11,327
EUR-denominated	34,344	44,255
Letters of credit	241,854	310,602
Other cash and cash equivalents	7,651	17,058
Total	<u>455,205</u>	<u>784,163</u>

21. SHARE CAPITAL AND ADDITIONAL PAID-IN CAPITAL

	<u>31 December 2007 ‘000 shares</u>	<u>31 December 2006 ‘000 shares</u>
<i>Authorised number of shares</i>		
Ordinary shares at par value of RUR 1 each	2,505,114	2,505,114
Preferred shares at par value of RUR 1 each	119,596	119,596
Total authorised shares	<u>2,624,710</u>	<u>2,624,710</u>
<i>Issued and fully paid number of shares</i>		
Ordinary shares at par value of RUR 1 each	1,785,114	1,785,114
Preferred shares at par value of RUR 1 each	119,596	119,596
Total issued and fully paid shares	<u>1,904,710</u>	<u>1,904,710</u>
<i>Treasury shares</i>		
At the beginning of the year	3,300	-
Re-acquired by the Group	748	5,694
Re-issued from treasury shares	(3,400)	(2,394)
At the end of the year	<u>648</u>	<u>3,300</u>

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Treasury shares are recorded as a deduction from shareholders' equity at 31 December 2007, in the amount of RUR 7,712 thousand (31 December 2006 – RUR 46,251 thousands).

The share capital balance was adjusted for the effects of inflation in accordance with IAS 29 “Financial Reporting in Hyperinflationary Economies”. The effect of such adjustments was recorded as Additional paid-in capital. The adjustment was determined using the inflation rate index from 1 September 1993, the date the Company was established as a joint stock company, through 31 December 2002.

Group's ownership structure is as follows:

	% of ownership	
	31 December 2007	31 December 2006
OJSC “Svyazinvestneftekhim”	26.6%	26.6%
LLC “Telecom-Management”	50.2%	50.0%
Other legal entities and individuals	23.2%	23.4%
Total	100.0%	100.0%

Common shareholders are allowed one vote per share. Preferred shares are non-voting. All common shares and preferred shares are eligible for distribution of earnings available in accordance with Russian statutory accounting regulations. Preferred shares holders are entitled to an annual payment of dividends in the amount equal to 25% of their par value. Shareholders of preferred shares have a preferred right to recover the par value of preferred shares in liquidation.

One share of the Company, held by the Government of Tatarstan, carries the right to veto certain decisions taken at shareholders' and Board of Directors' meetings. Decisions subject to veto include: increases and decreases in share capital, amendments to the Company's charter, liquidation or reorganization of the Group or any of its subsidiaries or branches and investments in other legal entities. This veto right is referred to as “Golden Share”, and the term was extended indefinitely in 1998 by a decree of the President of Tatarstan and may be utilized by the Government of Tatarstan notwithstanding its voting rights are less than 25% of the Group.

Ultimate beneficial owners of the Group are:

- OJSC “TAIF” (“TAIF”), which controls LLC “Telecom-Management”; and
- The Government of Tatarstan, through its control of OJSC “Svyazinvestneftekhim”.

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22. LONG-TERM BORROWINGS

	<u>31 December 2007</u>	<u>31 December 2006</u>
Banks:		
USD denominated fixed rate	2,175,481	2,356,334
RUR denominated fixed rate	3,943,462	385,947
USD denominated floating rate	2,710,936	1,140,888
RUR denominated floating rate	597,334	-
EUR denominated floating rate	3,486,116	2,623,174
Non-convertible bonds (fixed rate loan participation notes)	-	5,350,114
Total long-term borrowings	12,913,329	11,856,457
Less: Current portion repayable within one year and shown under short-term borrowings (refer to note 24)	(1,166,312)	(555,073)
Net long-term borrowings	11,747,017	11,301,384

Loan participation notes in the amount of USD 200,000 thousand, bearing interest at 9.25%, due on 30 October 2011 were issued in 2006 by Kazanorgsintez S.A., a special purpose entity, on a limited recourse basis for the sole purpose of funding a loan to the Company. The notes are fully and unconditionally guaranteed by the Company. Interest payments on the notes are due semi-annually in April and October of each year, commencing on 30 April 2007.

The interest rates per annum on long-term borrowings vary as follows:

	<u>2007</u>	<u>2006</u>
Banks:		
USD denominated fixed rate	6.83% to 7.9%	2% to 7.9%
RUR denominated fixed rate	9.0% to 14%	9.5% to 14%
USD denominated floating rate	LIBOR plus 0.75% to LIBOR plus 2.85%	LIBOR plus 0.75% to LIBOR plus 2.85%
RUR denominated floating rate	MOSPRIME plus 2.0%	-
EUR denominated floating rate	EURIBOR plus 0.4% to EURIBOR plus 2.75%	EURIBOR plus 0.4% to EURIBOR plus 2.75%
Non-convertible bonds	-	9.25%

As at 31 December 2007, long-term borrowings totalling RUR 6,616,851 thousand (31 December 2006 - RUR 1,337,872 thousand) are secured by the pledge of equipment with the carrying value of RUR 2,379,222 thousand (31 December 2006 – RUR 457,509 thousand).

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

At 31 December 2007, the contractual undiscounted maturity profile calculated using interest rates in effect at 31 December 2007 are as follows:

	<u>Less than 1 year</u>	<u>1 to 5 years</u>	<u>Later than 5 years</u>	<u>Total</u>
Banks:				
USD denominated fixed rate	507,073	1,541,455	1,023,313	3,071,841
RUR denominated fixed rate	376,052	3,883,975	1,348,524	5,608,551
USD denominated floating rate	397,906	2,547,614	19,944	2,965,465
RUR denominated floating rate	56,009	716,422	-	772,431
EUR denominated floating rate	741,618	2,143,381	1,453,291	4,338,290
	<u>2,078,658</u>	<u>10,832,847</u>	<u>3,845,073</u>	<u>16,756,577</u>

At 31 December 2006, the contractual undiscounted maturity profile calculated using interest rates in effect at 31 December 2006 are as follows:

	<u>Less than 1 year</u>	<u>1 to 5 years</u>	<u>Later than 5 years</u>	<u>Total</u>
Banks:				
USD denominated fixed rate	248,994	1,596,057	1,523,434	3,368,485
RUR denominated fixed rate	44,385	294,260	281,163	619,808
USD denominated floating rate	168,047	1,140,019	66,700	1,374,767
EUR denominated floating rate	418,581	1,796,992	1,033,905	3,249,478
Bonds fixed rate	571,020	7,131,977	-	7,702,997
	<u>1,451,027</u>	<u>11,959,305</u>	<u>2,905,202</u>	<u>16,315,534</u>

Breach of loan agreements

As of 31 December 2007, the Group had breached the financial ratio covenants determined by Loan Participation Notes agreement (in the amount of USD 200,000 thousand due in 2011, issued by Kazanorgsintez S.A.). The Group has applied to the Noteholders to amend the Limitation on Indebtedness covenant in the Loan Agreement (refer to note 35).

Accordingly, the full amount due under this debt has been recorded as a current liability.

23. OBLIGATIONS UNDER FINANCE LEASES

	<u>31 December 2007</u>	<u>31 December 2006</u>
Minimum lease payments		
Due within one year	180,275	91,539
Due later than one year and not later than five years	96,416	83,443
Total future lease payments	276,691	174,982
Less: future finance charges	(21,888)	(15,545)
Present value of minimum lease payments	254,803	159,437
Less: current portion of finance lease obligations (refer to note 26)	(163,444)	(80,355)
Non-current finance lease obligations	91,359	79,082

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The Group leases production equipment and other assets under a number of financial lease agreements. The average lease term is 1.5 years. For the year ended 31 December 2007 the weighted average effective interest was 14% (2006 – 12%). All leases are on a fixed repayment basis and denominated in USD and EUR. The Group’s obligations under finance leases are secured by lessors’ title on the leased assets.

24. SHORT-TERM BORROWINGS

	31 December 2007	31 December 2006
Banks:		
RUR denominated fixed rate	2,088,426	54,208
USD denominated floating rate	974,647	-
EUR denominated floating rate	124,986	315,864
Non-convertible bonds (fixed rate loan participation notes) (refer to note 22)	4,987,447	-
Current portion of long-term borrowings repayable within one year (refer to note 22)	<u>1,166,312</u>	<u>555,073</u>
Total	<u>9,341,818</u>	<u>925,145</u>

The interest rates per annum on these borrowings vary as follows:

	2007	2006
RUR denominated fixed rate	2% to 14%	6% to 13%
USD denominated floating rate	LIBOR plus 1.5 % to LIBOR plus 2.25%	-
EUR denominated floating rate	EURIBOR plus 2.75%	EURIBOR plus 2.75%
Non-convertible bonds	9.25%	-

At 31 December 2007, the contractual undiscounted maturity profile calculated using interest rates in effect at 31 December 2007 are as follows:

	Less than 1 month	1 to 3 months	3 months to 1 year	Total
Banks:				
RUR denominated fixed rate	431,176	761,394	907,538	2,100,109
USD denominated floating rate	574	289,632	708,968	999,174
EUR denominated floating rate	443	83,550	44,896	128,889
Non-convertible bonds	-	-	-	6,731,966
Current portion of long-term borrowings	<u>144,253</u>	<u>107,423</u>	<u>914,636</u>	<u>1,166,312</u>
Total	<u>576,446</u>	<u>1,241,999</u>	<u>2,576,039</u>	<u>11,126,450</u>

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At 31 December 2006, the contractual undiscounted maturity profile calculated using interest rates in effect at 31 December 2006 are as follows:

	<u>Less than 1 month</u>	<u>1 to 3 months</u>	<u>3 months to 1 year</u>	<u>Total</u>
Banks:				
RUR denominated fixed rate	-	4,049	51,877	55,926
EUR denominated floating rate	10,259	310,426	-	320,685
Current portion of long-term borrowings	<u>209,077</u>	<u>68,953</u>	<u>277,043</u>	<u>555,073</u>
Total	<u>219,336</u>	<u>383,428</u>	<u>328,920</u>	<u>931,684</u>

25. TRADE PAYABLES

The average credit period on purchases of goods is 60 days. No interest is charged on the outstanding balance during credit period. Thereafter, interest is charged at an average rate of 1.96% per annum on the unsettled balance. The Group has financial risk management policies in place to ensure that all payables are paid within the credit period.

At 31 December 2007, trade accounts payable primarily denominated in RUR includes payables on purchases of raw materials, energy, maintenance services, spare parts and consumables. The fair value of trade accounts payable approximates their carrying amounts.

The table below summarises the maturity profile of the Group’s trade and other payables based on contractual undiscounted payments:

	<u>31 December 2007</u>	<u>31 December 2006</u>
Within 60 days	1,973,870	2,295,912
60-365 days	<u>46,615</u>	<u>30,021</u>
Total	<u>2,020,485</u>	<u>2,325,933</u>

26. OTHER PAYABLES AND ACCRUED LIABILITIES

	<u>31 December 2007</u>	<u>31 December 2006</u>
Dividends payable	603,014	300,211
Accrued employee benefits	248,006	105,401
Customs duties	-	94,380
Current portion of finance lease obligations (refer to note 23)	163,444	80,355
Deferred income	5,758	4,554
Other payables and accrued liabilities	<u>58,337</u>	<u>102,041</u>
Total	<u>1,078,559</u>	<u>686,942</u>

Dividends payable are due for payment before 15 June 2008.

Accrued employee benefits include unpaid salaries and wages, provisions for unused vacations and bonuses.

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27. OTHER TAXES PAYABLE

	<u>31 December 2007</u>	<u>31 December 2006</u>
Property tax	39,953	35,262
Land tax	39,200	31,643
Unified social tax	29,768	33,846
Personal income tax	27,209	17,890
Other taxes	15,460	39,446
Total	<u>151,590</u>	<u>158,087</u>

28. EARNINGS PER SHARE

Basic earnings per share

	<u>2007</u>	<u>2006</u>
Weighted average number of ordinary shares outstanding (thousands)	1,785,114	1,785,114
Adjusted for weighted average number of treasury shares (thousands)	(873)	(1,700)
Weighted average number of ordinary shares in issue (thousands)	1,784,241	1,783,414
Profit for the year attributable to the Group’s equity holders	2,552,980	2,523,545
Less: after-tax amount of preferred dividends	(27,208)	(27,208)
Basic earnings per share (RUR)	1.42	1.40

29. DIVIDENDS

	<u>31 December 2007</u>	<u>31 December 2006</u>
Dividends declared in respect of the year ended 31 December 2005:		
- ordinary shares (RUR 0.1514 per share)	-	270,248
- preferred shares (RUR 0.25 per share)	-	29,899
Dividends declared in respect of the year ended 31 December 2006:		
- ordinary shares (RUR 0.3545 per share)	632,732	-
- preferred shares (RUR 0.25 per share)	29,899	-
Total	<u>662,631</u>	<u>300,147</u>

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30. RECONCILIATION OF PROFIT BEFORE INCOME TAX TO CASH FLOWS FROM OPERATIONS

	<u>2007</u>	<u>2006</u>
OPERATING ACTIVITIES:		
Profit before income tax	3,387,658	3,187,662
Adjustments for:		
Depreciation and amortisation	1,244,799	740,000
Income from investments, net	(58,380)	(43,152)
Change in provision for doubtful debts	2,749	23,548
Change in obsolescence provision	(13,401)	3,193
Loss on disposal of property, plant and equipment	27,600	25,679
Finance costs, net	339,024	152,174
Foreign exchange gain, net	(542,681)	(147,211)
Other	-	186
	<hr/>	<hr/>
Operating cash flow before movements in working capital	4,387,368	3,942,079
Decrease/ (increase) in trade and other receivables	402,408	(875,895)
(Increase)/ decrease in taxes recoverable and prepaid, other than income tax	(592,902)	478,183
Increase in inventories	(803,427)	(441,095)
(Decrease)/ increase in trade payables	(193,375)	1,288,696
(Decrease)/ increase in advances received from customers	(525,246)	1,229,665
Increase in other payables and accrued liabilities	15,038	80,857
(Decrease)/ increase in other taxes payable	(111,009)	107,636
	<hr/>	<hr/>
Cash flows from operations	<u>2,578,855</u>	<u>5,810,126</u>

31. RELATED PARTIES

Related parties are considered to include shareholders, affiliates, entities under common ownership and control and members of key management personnel.

Transactions with shareholders, associates and other related parties are in the ordinary course of business with terms and conditions similar to transactions with third parties.

Included in financial statements are the following transactions and balances with shareholders:

	<u>2007</u>	<u>2006</u>
Sales of goods and services	63,813	105,007
Purchase of goods and services	-	100,886
Re-issuing of treasury shares	48,012	37,578
	<hr/>	<hr/>
	31 December 2007	31 December 2006
	<hr/>	<hr/>
Trade accounts receivable and advances given	554	750
Trade accounts payable and advances received	2,026	1,048,762
Dividends payable	518,780	217,466

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Included in financial statements are the following transactions and balances with other related parties:

	<u>2007</u>	<u>2006</u>
Sales of goods and services	690,372	221,529
Purchase of goods and services	3,447,670	3,051,834
Interest received	221	1,398
Dividends payable	2	2
	<u>31 December</u>	<u>31 December</u>
	<u>2007</u>	<u>2006</u>
Cash and cash equivalents	83,955	22,077
Trade accounts receivable and advances given	246,824	187,468
Trade accounts payable and advances received	326,246	161,651
Loans and borrowings	39,634	-

Key management compensation for the year ended 31 December 2007, amounted to RUR 55,494 thousand (for the year ended 31 December 2006 – RUR 41,199 thousand) and included salaries and bonuses to employees of the Group and remuneration to members of Board of Directors.

32. COMMITMENTS AND CONTINGENCIES

Capital commitments

The Board of Directors of the Company approved a strategic plan for the development of its production facilities through 2010 (the “Plan”). According to that Plan the following new production facilities will be installed:

- Bisphenol producing plant;
- Polycarbonate plastics plant;
- New ethylene plant;
- New recycling and other auxiliary workshops.

The total capital commitments for 2008 are estimated at RUR 7.7 billion, including RUR 1.1 billion of contracted commitments. Management expects to finance capital expenditures through current profit and long-term borrowings.

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Operating Lease

The Group leases certain utilities and equipment. The respective lease agreements have the following terms: an average life of 1 to 5 years with no renewal option at the end of the term. There are no restrictions placed upon the Group by entering into these agreements.

Future minimum rental expenses under non-cancellable operating leases at 31 December 2007 are as follows:

	<u>Less than 1 year</u>	<u>1 to 5 years</u>	<u>Total</u>
Lease contracts:			
Equipment	20,492	11,953	32,445
Utilities	2,102	-	2,102
Total	<u>22,594</u>	<u>11,953</u>	<u>34,547</u>

Litigation

Unresolved tax litigation at 31 December 2007, amounted to approximately RUR 74,131 thousand. Management believes that the risk of an unfavourable outcome to the litigation is possible. The Group has won the above mentioned case in the court of first instance at the date of issuing these statements.

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

Russian taxation contingencies

The taxation system in the Russian Federation is at a relatively early stage of development, and is characterised by numerous taxes, frequent changes and inconsistent enforcement at federal, regional and local levels.

The Government of the Russian Federation has commenced a revision of the Russian tax system and passed certain laws implementing tax reform. The new laws reduce the number of taxes and overall tax burden on businesses and simplify tax laws. However, these new tax laws continue to rely heavily on the interpretation of local tax officials and fail to address many existing problems. Many issues associated with the practical application of new legislation are unclear and complicate the Group's tax planning and related business decisions.

In terms of Russian tax legislation, authorities have a period of up to three years to re-open tax declarations for further inspection. Changes in the tax system that may be applied retrospectively by authorities could affect the Group's previously submitted and assessed tax declarations.

While management believes that it has adequately provided for tax liabilities based on its interpretation of current and previous legislation, the risk remains that tax authorities in the Russian Federation could take differing positions with regard to issues of interpretation. This uncertainty may expose the Group to additional taxation, fines and penalties that could be significant.

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With regard to matters where practice concerning payment of taxes is unclear, management estimated possible tax exposures at 31 December 2007 to be approximately RUR 73,389 thousand (31 December 2006 – RUR 36,090 thousand).

Russian Federation risk

As an emerging market, the Russian Federation does not possess a fully developed business and regulatory infrastructure including stable banking and judicial systems, which would generally exist in a more mature market economy. The economy of the Russian Federation is characterized by a currency that is not freely convertible outside of the country, currency controls, low liquidity levels for debt and equity markets, and continuing inflation. As a result, operations in the Russian Federation involve risks that are not typically associated with those in more developed markets.

Stability and success of Russian economy and the Group’s business mainly depends on the effectiveness of economic measures undertaken by the government as well as the development of legal and political systems.

Environmental matters

The Group’s management believes that it is in compliance with all current existing environmental laws and regulations of the Russian Federation. However, environmental laws and regulations continue to evolve. The Group is unable to predict the timing or extent to which those environmental laws and regulations may change. Such change, if it occurs, may require that the Group modernize technology to meet more stringent standards.

Russian insurance environment

The Russian insurance industry is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available in Russia.

The Group maintains insurance cover for major production assets including insurance cover for damage related to explosion or environmental damage arising from accidents on the Group’s property or related to the Group’s operations. The Group does not have coverage for business interruption. Management believes that the existing level of insurance coverage addresses all major risks which could have a material effect on the Group’s operations and financial position.

33. FINANCIAL RISK MANAGEMENT

Capital risk management

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance. The Group’s overall strategy remains unchanged from 2006.

The capital structure of the Group consists of debt, which includes the borrowings disclosed in notes 22 and 24, cash and cash equivalents disclosed in note 20 and equity attributable to equity holders of the parent, comprising issued capital as disclosed in note 21, reserves and retained earnings.

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Major classes of financial instruments

The following table sets out the carrying amount of the Group’s financial instruments per categories at the following dates:

	<u>31 December 2007</u>	<u>31 December 2006</u>
Financial Assets		
Cash and cash equivalents	455,205	784,163
Trade and other accounts receivable	754,526	1,314,621
Other financial assets	52,100	52,100
Investments in associates	24,789	29,278
Total	<u>1,286,620</u>	<u>2,180,162</u>
Financial Liabilities		
Finance lease liabilities	254,803	159,437
Long-term borrowings	11,747,017	11,301,384
Short-term borrowings	9,341,818	925,145
Trade accounts payable	2,020,485	2,325,933
Other payables and accrued liabilities	661,351	496,632
Total	<u>24,025,474</u>	<u>15,208,531</u>

The Group’s operations are dependent on a stable gas supply. Presently, the gas market in Russia is controlled by OJSC “Gazprom” and its subsidiaries, the Group’s major supplier of gas. The management of the Group is continuously engaged in ensuring a stable supply of gas.

Liquidity risk management

Liquidity risk is the risk that the Group will not be able to settle all liabilities as they are due. The Group manages its liquidity risk through a combination of short-term and long-term financing and self generated funds.

At 31 December 2007, the Group had credit facilities for the management of its day to day liquidity requirements available in the amount RUR 2,894,958 thousands (31 December 2006 – RUR 4,828,174 thousands).

The summaries of maturity profile of the Group’s financial liabilities at 31 December 2007 and 2006 on contractual payments are presented in notes 22, 23, 24 and 25.

Foreign currency risk management

Currency risk is the risk that the financial results of the Group will be adversely impacted by changes in exchange rates to which the Group is exposed. The Group undertakes certain transactions denominated in foreign currencies. Hence, exposures to exchange rate fluctuations arise.

The Group is exposed to currency risk in that a significant portion of long and short term borrowings are denominated in foreign currencies. The Group management controls over this risk by aligning the foreign currency borrowings with expected currency sales proceeds.

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

The carrying amounts of the Group’s foreign currency denominated monetary assets and monetary liabilities at the reporting date are as follows:

	Liabilities		Assets	
	31 December 2007	31 December 2006	31 December 2007	31 December 2006
USD denominated	(11,210,974)	(8,974,775)	365,957	373,497
EUR denominated	(3,730,661)	(3,131,859)	41,630	60,157

Foreign currency sensitivity analysis

The Group is mainly exposed to USD and EUR.

The following table details the Group’s sensitivity to a 10% increase and decrease in RUR against the relevant foreign currencies. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management’s assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 10% change in foreign currency rates. A positive number below indicates an increase in profit where RUR strengthens 10% against the relevant currency. For a 10% weakening of RUR against the relevant currency, there would be an equal and opposite impact on the profit and other equity, and the balances below would be negative.

	USD Impact		EUR Impact	
	2007	2006	2007	2006
Increase in profit before income tax	1,084,502	860,128	368,903	307,170

This is mainly attributable to the exposure outstanding on USD and EUR borrowings at year end in the Group.

The Group’s sensitivity to foreign currency has increased during the current period mainly due to additional USD denominated borrowings during the year which is due to decline of USD against RUR exchange rate anticipation.

Interest rate risk management

The Group is exposed to interest rate risk as entities in the Group borrow funds at both fixed and floating interest rates. The risk is managed by the Group by maintaining an appropriate mix between fixed and floating rate borrowings. The Group also has the possibility to early redemption of the contracts without significant costs.

Interest rate sensitivity analysis

The sensitivity analyses below have been determined based on the exposure to interest rates for non-derivative instruments at the balance sheet date. For floating rate liabilities, the analysis is prepared assuming the amount of liability outstanding at the balance sheet date was outstanding for the whole year. A 100 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management’s assessment of the reasonably possible change in interest rates.

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If interest rates had been 100 basis points higher/ lower and all other variables were held constant, the Group’s profit before income tax for the year ended 31 December 2007 would decrease/ increase by RUR 77,591 thousand (2006 - decrease/ increase by RUR 40,158 thousand). This is mainly attributable to the Group’s exposure to interest rates on its variable rate borrowings.

The Group’s sensitivity to interest rates has increased during the current period mainly due to the increase in variable rate loans and borrowings.

Credit risk management

Credit risk refers to the risk that counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss from defaults. New customers are dealt only on 100% advance terms. The Group uses available financial information and its own trading records to rate its major customers. The Group’s exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties.

The Group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The Group defines counterparties as having similar characteristics if they are related entities. Concentration of credit risk did not exceed 5% of gross monetary assets at any time during the year.

Fair value of financial instruments

The fair values of financial assets and financial liabilities are determined as follows:

- The fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets is determined with reference to quoted market prices;
- The fair value of other financial assets and financial liabilities is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments.

Management believes that the carrying values of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate their fair values.

OPEN JOINT STOCK COMPANY “KAZANORGSINTEZ”

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousands of Russian roubles)

34. INVESTMENTS IN SUBSIDIARIES

The Company’s ownership interest in the significant consolidated entities is as follows:

	Nature of business	% of ownership	
		31 December 2007	31 December 2006
Subsidiaries			
<i>Incorporated in Russian Federation</i>			
LLC “Agrosintez”	Agriculture	-	100
OJSC “Luch Sintez”	Agriculture	-	98
OJSC “Spetsneftekhimmontazh”	Repair & Maintenance	100	100
OJSC “Shelangovsky plodovoyagodny sovkhoz”	Agriculture	-	90
LLC “Tatkhimremont”	Repair & Maintenance	100	100
LLC “Trade House Orgsintez”	Trading	70	70
LLC “Kolos-Sintez”	Agriculture	51	51
LLC “DK Khimikov”	Entertainment	100	100
<i>Incorporated in Hungary</i>			
LLC “Elmer”	Trading	50	50
Special purpose entity			
<i>Incorporated in Luxembourg</i>			
Kazanorgsintez S.A.	Financing	-	-

On 8 June 2007, LLC “Agrosintez” was declared bankrupt. The Group also has disposed of OJSC “Luch Sintez” and OJSC “Shelangovsky plodovoyagodny sovkhoz”, subsidiaries of LLC “Agrosintez”.

35. EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

In 2008, the Group obtained three short-term loans for the total amount of RUR 2,600,000 thousand and USD 40,000 thousand.

In the period from 31 December 2007 up to the date of issuing these consolidated financial statements the Group has re-acquired 48,000 treasury shares amounting RUR 560 thousand.

On 16 April 2008, the shareholders of the Company approved dividends for the fiscal year ended 31 December 2007 in amount of RUR 750,996 thousand for ordinary shares and RUR 29,899 thousand for preferred shares. Dividends are payable by 16 April 2009.

On 16 April 2008, the shareholders of the Company approved an increase in the authorised number of ordinary shares up to 25 billion shares with par value of RUR 1 each.

On 3 May 2008, The Group has applied to Noteholders to amend the Limitation on Indebtedness covenant in the Loan Agreement up to the end of second quarter of 2009 and to waive the breach of covenant. Approval for these proposals was sought by way of Extraordinary Resolution considered and approved at a meeting of Noteholders held on 21 May 2008.