

OAO TMK

Consolidated Financial Statements

for the year ended December 31, 2011

Independent auditors' report

To the shareholders and Board of Directors
ОАО ТМК

We have audited the accompanying consolidated financial statements of ОАО ТМК and its subsidiaries ('the Group'), which comprise the consolidated statement of financial position as at December 31, 2011, the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

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

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the 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' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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



Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at December 31, 2011, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC

March 15, 2012

OAO TMK

Consolidated Financial Statements

for the year ended December 31, 2011

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OAo TMK
Consolidated Income Statement
for the year ended December 31, 2011
(All amounts in thousands of US dollars)

	NOTES	Year ended December 31,	
		2011	2010
Revenue:	1	6,753,517	5,578,599
<i>Sales of goods</i>		6,645,963	5,421,084
<i>Rendering of services</i>		107,554	157,515
Cost of sales	2	(5,307,243)	(4,285,349)
Gross profit		1,446,274	1,293,250
Selling and distribution expenses	3	(411,252)	(403,143)
Advertising and promotion expenses	4	(9,204)	(11,099)
General and administrative expenses	5	(282,785)	(231,975)
Research and development expenses	6	(18,690)	(13,309)
Other operating expenses	7	(53,325)	(44,978)
Other operating income	8	13,090	11,042
Impairment of goodwill	19	(3,368)	–
Impairment of investment in associate	10	(1,833)	–
Reversal of impairment of property, plant and equipment	18	73,417	–
Foreign exchange (loss)/gain, net		(1,254)	9,512
Finance costs		(302,786)	(430,586)
Finance income	9	32,063	18,895
Gain/(loss) on changes in fair value of derivative financial instrument	24	44,792	(12,361)
Share of loss of associate	10	(185)	–
Gain on disposal of assets classified as held for sale	11	19,184	–
Profit before tax		544,138	185,248
Income tax expense	12	(159,441)	(81,174)
Profit/(loss) for the year		384,697	104,074
Attributable to:			
Equity holders of the parent entity		380,130	104,334
Non-controlling interests		4,567	(260)
		384,697	104,074
Earnings per share attributable to equity holders of the parent entity (in US dollars)			
Basic	13	0.44	0.12
Diluted	13	0.40	0.12

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

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Consolidated Statement of Comprehensive Income
for the year ended December 31, 2011
(All amounts in thousands of US dollars)

	NOTES	2011	2010
Profit for the year		384,697	104,074
Exchange differences on translation to presentation currency ^(a)		(57,619)	(12,547)
Foreign currency loss on hedged net investment in foreign operation ^(b)	29 (x)	(67,772)	(8,847)
Income tax ^(b)	29 (x)	13,554	1,769
		(54,218)	(7,078)
Other comprehensive income/(loss) for the year, net of tax		(111,837)	(19,625)
Total comprehensive income/(loss) for the year, net of tax		272,860	84,449
Attributable to:			
Equity holders of the parent entity		273,303	85,929
Non-controlling interests		(443)	(1,480)
		272,860	84,449

- (a) The amount of exchange differences on translation to presentation currency represents other comprehensive loss of 52,609 (2010: 11,327) attributable to equity holders of the parent entity and other comprehensive loss of 5,010 (2010: 1,220) attributable to non-controlling interests.
- (b) The amount of foreign currency loss on hedged net investment in foreign operation, net of income tax, was attributable to equity holders of the parent entity.

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

OAo TMK
Consolidated Statement of Financial Position
as at December 31, 2011
(All amounts in thousands of US dollars)

	NOTES	2011		2010	
ASSETS					
Current assets					
Cash and cash equivalents	14, 27	230,593		157,524	
Trade and other receivables	15	766,155		716,897	
Accounts receivable from related parties	27	5,526		3,395	
Inventories	16	1,418,455		1,207,540	
Prepayments and input VAT	17	170,708		154,302	
Prepaid income taxes		29,580		18,099	
Other financial assets		4,047	2,625,064	3,966	2,261,723
Assets classified as held for sale		–	2,625,064	8,003	2,269,726
Non-current assets					
Investments in associates	10	1,717		–	
Intangible assets	19	413,263		474,791	
Property, plant and equipment	18	3,347,648		3,386,660	
Goodwill	19	547,211		554,353	
Deferred tax asset	12	97,880		135,307	
Other non-current assets	20	99,458	4,507,177	40,697	4,591,808
TOTAL ASSETS			7,132,241		6,861,534
LIABILITIES AND EQUITY					
Current liabilities					
Trade and other payables	21	862,940		732,733	
Advances from customers		188,861		136,885	
Accounts payable to related parties	27	733		8,434	
Provisions and accruals	22	46,075		42,153	
Interest-bearing loans and borrowings	23, 24	599,377		701,864	
Derivative financial instrument	24	3,024		47,816	
Dividends payable		323		430	
Income tax payable		4,078	1,705,411	3,846	1,674,161
Liabilities directly associated with the assets classified as held for sale		–	1,705,411	143	1,674,304
Non-current liabilities					
Interest-bearing loans and borrowings	23, 24	3,187,564		3,169,714	
Deferred tax liability	12	304,785		300,484	
Provisions and accruals	22	25,336		24,096	
Post-employment benefits	25	51,836		53,612	
Other liabilities		32,525	3,602,046	32,020	3,579,926
Total liabilities			5,307,457		5,254,230
Equity					
29					
Parent shareholders' equity					
Issued capital		326,417		326,417	
Treasury shares		(327,339)		(318,351)	
Additional paid-in capital		384,581		376,485	
Reserve capital		16,390		15,387	
Retained earnings		1,421,437		1,094,561	
Foreign currency translation reserve		(88,551)	1,732,935	18,276	1,512,775
Non-controlling interests			91,849		94,529
Total equity			1,824,784		1,607,304
TOTAL EQUITY AND LIABILITIES			7,132,241		6,861,534

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

OAo TMK
Consolidated Statement of Changes in Equity
for the year ended December 31, 2011
(All amounts in thousands of US dollars)

	Attributable to equity holders of the parent						Non-controlling interests	TOTAL	
	Issued capital	Treasury shares	Additional paid-in capital	Reserve capital	Retained earnings	Foreign currency translation reserve			Total
At January 1, 2011 (as reported)	326,417	(318,351)	362,898	15,387	1,122,771	18,276	1,527,398	109,509	1,636,907
Voluntary change in accounting policy	–	–	–	–	(28,210)	–	(28,210)	(1,393)	(29,603)
Recognition of the change in non-controlling interests in the subsidiary as an equity transaction (Note 29 vi)	–	–	13,587	–	–	–	13,587	(13,587)	–
At January 1, 2011 (as restated)	326,417	(318,351)	376,485	15,387	1,094,561	18,276	1,512,775	94,529	1,607,304
Profit for the year	–	–	–	–	380,130	–	380,130	4,567	384,697
Other comprehensive income/(loss) for the year, net of tax	–	–	–	–	–	(106,827)	(106,827)	(5,010)	(111,837)
Total comprehensive income/(loss) for the year, net of tax	–	–	–	–	380,130	(106,827)	273,303	(443)	272,860
Purchase of treasury shares (Note 29 xi)	–	(8,988)	–	–	–	–	(8,988)	–	(8,988)
Increase in reserve capital (Note 29 ii)	–	–	–	1,003	(1,003)	–	–	–	–
Dividends declared by the parent entity to its shareholders (Note 29 iii)	–	–	–	–	(51,993)	–	(51,993)	–	(51,993)
Dividends declared by subsidiaries of the Group to the non-controlling interest owners (Note 29 ix)	–	–	–	–	–	–	–	(338)	(338)
Sale of non-controlling interests (Note 29 v)	–	–	–	–	(42)	–	(42)	9,307	9,265
Increase in liability to non-controlling interests (Note 29 v)	–	–	(1,952)	–	–	–	(1,952)	–	(1,952)
Recognition of the change in non-controlling interests in the subsidiary as an equity transaction (Note 29 vi)	–	–	9,609	–	–	–	9,609	(9,609)	–
Acquisition of non-controlling interests in subsidiaries (Note 29 iv)	–	–	439	–	(14)	–	425	(1,799)	(1,374)
Increase in non-controlling interests from contributions of assets by the Group (Note 29 viii)	–	–	–	–	(202)	–	(202)	202	–
At December 31, 2011	326,417	(327,339)	384,581	16,390	1,421,437	(88,551)	1,732,935	91,849	1,824,784

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

OAO TMK
Consolidated Statement of Changes in Equity
for the year ended December 31, 2011 (continued)

(All amounts in thousands of US dollars)

	Attributable to equity holders of the parent						Total	Non-controlling interests	TOTAL
	Issued capital	Treasury shares	Additional paid-in capital	Reserve capital	Retained earnings	Foreign currency translation reserve			
At January 1, 2010 (as reported)	305,407	(37,378)	104,003	15,387	1,019,322	36,681	1,443,422	75,874	1,519,296
Voluntary change in accounting policy	–	–	–	–	(28,210)	–	(28,210)	(1,393)	(29,603)
At January 1, 2010 (as restated)	305,407	(37,378)	104,003	15,387	991,112	36,681	1,415,212	74,481	1,489,693
Profit/(loss) for the year	–	–	–	–	104,334	–	104,334	(260)	104,074
Other comprehensive income/(loss) for the year, net of tax	–	–	–	–	–	(18,405)	(18,405)	(1,220)	(19,625)
Total comprehensive income/(loss) for the year, net of tax	–	–	–	–	104,334	(18,405)	85,929	(1,480)	84,449
Issue of share capital (Note 29 i)	21,010	–	258,417	–	–	–	279,427	–	279,427
Purchase of treasury shares (Note 29 xi)	–	(280,973)	–	–	–	–	(280,973)	–	(280,973)
Dividends declared by subsidiaries of the Group to the non-controlling interest owners (Note 29 ix)	–	–	–	–	–	–	–	(8)	(8)
Sale of non-controlling interests (Note 29 v)	–	–	–	–	(741)	–	(741)	13,587	12,846
Recognition of the change in non-controlling interests in the subsidiary as an equity transaction (Note 29 vi)	–	–	13,587	–	–	–	13,587	(13,587)	–
Contributions from non-controlling interest owners (Note 29 vii)	–	–	–	–	–	–	–	23,124	23,124
Acquisition of non-controlling interests in subsidiaries (Note 29 iv)	–	–	478	–	(144)	–	334	(1,588)	(1,254)
At December 31, 2010	326,417	(318,351)	376,485	15,387	1,094,561	18,276	1,512,775	94,529	1,607,304

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

OAo TMK
Consolidated Statement of Cash Flows
for the year ended December 31, 2011
(All amounts in thousands of US dollars)

	NOTES	Year ended December 31,	
		2011	2010
Operating activities			
Profit before tax		544,138	185,248
Adjustments to reconcile profit before tax to operating cash flows:			
Depreciation of property, plant and equipment		266,537	215,416
Amortisation of intangible assets	19	69,234	85,199
Loss on disposal of property, plant and equipment	7	2,319	10,195
Impairment of goodwill	19	3,368	–
Reversal of impairment of property, plant and equipment	18	(73,417)	–
Impairment of investment in associate	10	1,833	–
Foreign exchange loss/(gain), net		1,254	(9,512)
Finance costs		302,786	430,586
Finance income	9	(32,063)	(18,895)
(Gain)/loss on changes in fair value of derivative financial instrument	24	(44,792)	12,361
Gain on disposal of assets classified as held for sale	11	(19,184)	–
Share of loss of associate	10	185	–
Allowance for net realisable value of inventory	16	(662)	(4,818)
Allowance for doubtful debts	30	19,551	5,420
Movement in other provisions		9,039	31,115
Operating cash flows before working capital changes		1,050,126	942,315
Working capital changes:			
Increase in inventories		(280,232)	(277,508)
Increase in trade and other receivables		(110,210)	(148,208)
(Increase)/decrease in prepayments		(26,862)	21,095
Increase in trade and other payables		172,369	90,862
Increase/(decrease) in advances from customers		88,875	(213,250)
Cash generated from operations		894,066	415,306
Income taxes paid		(106,926)	(28,987)
Net cash flows from operating activities		787,140	386,319
Investing activities			
Purchase of property, plant and equipment and intangible assets		(402,459)	(314,096)
Proceeds from sale of property, plant and equipment		1,431	386
Proceeds from disposal of subsidiaries	11	–	26,027
Purchase of ownership interest in associate	10	(4,004)	–
Issuance of loans		(1,333)	(968)
Proceeds from repayment of loans issued		962	1,277
Interest received		2,638	2,120
Dividends received		25,425	14,092
Net cash flows used in investing activities		(377,340)	(271,162)
Financing activities			
Purchase of treasury shares	29 (xi)	(8,988)	(280,973)
Proceeds from issue of share capital	29 (i)	–	279,427
Proceeds from borrowings		2,768,477	3,097,306
Repayment of borrowings		(2,764,149)	(2,994,735)
Interest paid		(287,533)	(342,743)
Reimbursement of interest paid		1,272	3,905
Payment of finance lease liabilities		(3,014)	(2,822)
Acquisition of non-controlling interest		(1,374)	(1,085)
Proceeds from sale of non-controlling interests	29 (v)	9,265	32,939
Contributions from non-controlling interest owners	29 (vii)	–	23,124
Dividends paid to equity holders of the parent		(47,313)	–
Dividends paid to non-controlling interest shareholders		(1,531)	(599)
Net cash flows used in financing activities		(334,888)	(186,256)
Net increase/(decrease) in cash and cash equivalents		74,912	(71,099)
Net foreign exchange difference		(1,843)	(15,133)
Cash and cash equivalents at January 1		157,524	243,756
Cash and cash equivalents at December 31		230,593	157,524

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

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Notes to the Consolidated Financial Statements for the year ended December 31, 2011

(All amounts are in thousands of US dollars, unless specified otherwise)

Corporate Information

These consolidated financial statements of OAO TMK and its subsidiaries (the “Group”) for the year ended December 31, 2011 were authorised for issue in accordance with a resolution of the General Director on March 15, 2012.

OAO TMK (the “Company”), the parent company of the Group, is an open joint stock company (“OAO”). Both registered and principal office of the Company is 40/2a Pokrovka Street, Moscow, the Russian Federation.

As at December 31, 2011, the Company’s controlling shareholder was TMK Steel Limited. TMK Steel Limited is ultimately controlled by D.A. Pumpyskiy.

The Group is one of the world’s leading producers of steel pipes for the oil and gas industry, a global company with extensive network of production facilities, sales companies and representative offices.

The principal activities of the Group are the production and distribution of seamless and welded pipes, including pipes with the entire range of premium connections backed by extensive technical support. Research centres established in Russia and in the United States are involved in new product design and development, experimental and validation testing and advanced metallurgical research.

Basis of Preparation of the Financial Statements

Statement of Compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) issued by the International Accounting Standards Board (“IASB”).

Basis of Accounting

Group companies maintain their accounting records in their local currency and prepare their statutory financial statements in accordance with the regulations on accounting and reporting of the country in which the particular subsidiary is resident. The consolidated financial statements are based on the statutory accounting records, with adjustments and reclassifications for the purpose of fair presentation in compliance with IFRS. The principal adjustments relate to (1) expense and revenue recognition, (2) valuation of unrecoverable assets, (3) depreciation and valuation of property, plant and equipment, (4) accounting for income taxes, (5) use of fair values, (6) business combinations and (7) translation to the presentation currency.

The consolidated financial statements have been prepared on an accrual basis and under the historical cost convention, except as disclosed in the accounting policies below. For example, property, plant and equipment are accounted for at deemed cost at the date of transition to IFRS.

All Group companies and associates have a December 31 accounting year-end.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Basis of Preparation of the Financial Statements (continued)

Functional and Presentation Currency

The presentation currency for the purpose of these consolidated financial statements of the Group is the US dollar because the presentation in US dollars is convenient for the major current and potential users of the Group's financial statements.

The functional currency of the Company and its subsidiaries located in the Russian Federation, Kazakhstan, Switzerland and Cyprus is the Russian rouble. The functional currencies of other foreign operations of the Group are the Euro, the United States dollar, the Romanian lei and Canadian dollar, which are the currencies of countries in which the Group's entities are incorporated.

On consolidation, assets and liabilities of Group companies reported in their functional currencies are translated into US dollars, the Group's presentation currency, at year-end exchange rates. Income and expense items are translated into US dollars at the annual weighted average rates of exchange or at the rate on the date of the transaction for significant items.

Transactions in foreign currencies are initially recorded in the functional currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the end of reporting period. All resulting differences are taken to the income statement with the exception of differences on foreign currency borrowings accounted for as hedges of net investment in foreign operations. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The Group hedges its net investment in operations located in the United States against foreign currency risks using US dollar denominated liabilities. Gains or losses on the hedging instruments relating to the effective portion of the hedge are recognised as other comprehensive income while any gains or losses relating to the ineffective portion are recognised in the income statement. On the disposal of the foreign operation, the cumulative value of any such gains or losses recognised as a component of other comprehensive income is transferred to the income statement.

Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Estimates and Assumptions

The key assumptions concerning the future and other key sources of estimation of uncertainty at the end of reporting period that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of Property, Plant and Equipment

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Group estimates the asset's recoverable amount. This requires an estimation of the value in use of the cash-generating units to which the item is allocated. The determination of impairments of property, plant and equipment involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment is based on a large number of factors, such as changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists. The determination of the recoverable amount of a cash-generating unit involves the use of estimates by management.

Methods used to determine the value in use include discounted cash flow-based methods, which require the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. These estimates, including the methodologies used, may have a material impact on the recoverable value and ultimately the amount of any property, plant and equipment impairment.

Assets that suffered an impairment are tested for possible reversal of the impairment at each reporting date if indications exist that impairment losses recognised in prior periods no longer exist or have decreased.

In 2011 and 2010, no impairment losses were recognised in respect of property, plant and equipment. In 2011, the Group reversed impairment losses of 73,417 recognised in 2008-2009 in respect of property, plant and equipment of European division cash-generating unit (Note 18).

Useful Lives of Items of Property, Plant and Equipment

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes accounted for as a change in an accounting estimate in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. There were no any changes in accounting estimates of remaining useful lives of items of property, plant and equipment in 2011.

Fair Value of Assets and Liabilities Acquired in Business Combinations

The Group is required to recognise separately, at the acquisition date, the identifiable assets, liabilities and contingent liabilities acquired or assumed in the business combination at their fair values, which involves estimates. Such estimates are based on valuation techniques, which require considerable judgment in forecasting future cash flows and developing other assumptions.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Estimates and Assumptions (continued)

Impairment of Goodwill and Intangible Assets with Indefinite Useful Lives

The Group determines whether goodwill and intangible assets with indefinite useful lives are impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill and intangible assets with indefinite useful lives are allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill as at December 31, 2011 was 547,211 (2010: 554,353). In 2011, the Group recognised impairment losses in the amount of 3,368 in respect of goodwill (Note 19) (2010: nil).

Post-Employment Benefits

The Group uses the actuarial valuation method for measurement of the present value of post-employment benefit obligations and related current service cost. This involves the use of demographic assumptions about the future characteristics of current and former employees who are eligible for benefits (mortality, both during and after employment, rates of employee turnover, disability and early retirement, etc.) as well as financial assumptions (discount rate, future salary). In the event that further changes in the key assumptions are required, the future amounts of the post-employment benefit costs may be affected materially (Note 25).

Allowances

The Group makes allowances for doubtful debts. Significant judgment is used to estimate doubtful accounts. In estimating doubtful accounts, such factors are considered as current overall economic conditions, industry-specific economic conditions, historical and anticipated customer performance. Changes in the economy, industry, or specific customer conditions may require adjustments to the allowance for doubtful debts recorded in the consolidated financial statements. As at December 31, 2011 and 2010, allowances for doubtful debts have been made in the amount of 31,782 and 17,947, respectively (Notes 15, 20, 30).

The Group makes allowances for obsolete and slow-moving raw materials and spare parts. In addition, certain finished goods, work in process and raw materials of the Group are carried at net realisable value. Estimates of net realisable value of finished goods are based on the most reliable evidence available at the time the estimates are made. These estimates take into consideration fluctuations of price or cost directly relating to events occurring subsequent to the end of reporting period to the extent that such events confirm conditions existing at the end of the period. As at December 31, 2011 and 2010, allowances for net realisable value of inventory were 15,826 and 17,112, respectively (Note 16).

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Estimates and Assumptions (continued)

Litigations

The Group exercises considerable judgment in measuring and recognising provisions and the exposure to contingent liabilities related to pending litigations or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the final settlement. Because of the inherent uncertainties in this evaluation process, actual losses may differ from the originally estimated provision. These estimates are subject to change as new information becomes available, primarily with the support of internal specialists, if available, or with the support of external consultants, such as actuaries or legal counsel. Revisions to the estimates may significantly affect future operating results of the Group.

Current Taxes

The Group is subject to taxes in different countries all over the world. Taxes and fiscal risks recognised in these consolidated financial statements reflect management's best estimate of the outcome based on the facts known at each reporting date in each individual country. These facts may include but are not limited to change in tax laws and interpretation thereof in the various jurisdictions where the Group operates.

Tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Furthermore, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management.

As a result, tax authorities may challenge transactions and Group's entities may be assessed additional taxes, penalties and interest, which can be significant. The final taxes paid are dependent upon many factors, including negotiations with taxing authorities in various jurisdictions, outcomes of tax litigation and resolution of disputes arising from tax audits. As at December 31, 2011, management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained (Note 28).

Deferred Tax Assets

Management judgment is required for the calculation of deferred income taxes. Deferred tax assets are recognised to the extent that their utilisation is probable. The utilisation of deferred tax assets will depend on whether it is possible to generate sufficient taxable income in the respective tax type and jurisdiction. Various factors are used to assess the probability of the future utilisation of deferred tax assets, including past operating results, the operational plan, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from these estimates or if these estimates are adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected. In the event that the assessment of future utilisation indicates that the carrying amount of deferred tax assets must be reduced, this reduction is recognised in profit or loss.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Judgments

In the process of applying the Group's accounting policies, management has made the following judgments, apart from those judgments involving estimates, which have a significant effect on the amounts recognised in the consolidated financial statements:

Consolidation of Special Purpose Entities

The Group determined that the substance of the relationship between the Group and TMK Capital S.A., a special purpose entity, indicates that the Group controls TMK Capital S.A. In July 2008 and in January 2011, TMK Capital S.A. issued notes due July 2011 and January 2018, respectively, to provide financing to the Group's companies (Note 23).

The Group determined that the substance of the relationship between the Group and TMK Bonds S.A., a special purpose entity, indicates that the Group controls TMK Bonds S.A. In February 2010, TMK Bonds S.A. completed the offering of convertible bonds due 2015 convertible into Global Depository Receipts each representing four ordinary shares of OAo TMK to provide financing to the Group's companies (Note 24).

Changes in Accounting Policies

Application of New and Amended IFRS and IFRIC

The Group has adopted the following new and amended IFRS and IFRIC in the consolidated financial statements for the annual period beginning on January 1, 2011:

- IAS 24 *Related Party Disclosures* (revised);
- IAS 32 *Financial Instruments: Presentation* (amended);
- IFRIC 14 *Prepayments of a Minimum Funding Requirement* (amended);
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*;
- Improvements to IFRSs (May 2010)

The principle effect of these changes in policies is discussed below.

IAS 24 *Related Party Disclosures* (revised)

The revision clarifies the definition of a related party. The new definitions emphasise a symmetrical view of related party relationships and clarify in which circumstances persons and key management personnel affect related party relationships of an entity. The revision introduces an exemption from the general related party disclosure requirements for transactions with a government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity. The revision did not have any impact on the financial position or performance of the Group.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Changes in Accounting Policies (continued)

Application of New and Amended IFRS and IFRIC (continued)

IAS 32 *Financial Instruments: Presentation* (amended) – Classification of Rights Issues

The amendment alters the definition of a financial liability in order to classify rights issues and certain options or warrants as equity instruments. The amendment is applicable if the rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. The amendment did not have effect on the financial position or performance of the Group.

IFRIC 14 *Prepayments of a Minimum Funding Requirement* (amended)

The amendment removes an unintended consequence when an entity is subject to minimum funding requirements and makes an early payment of contributions to cover such requirements. The amendment permits an entity to recognise a prepayment of future service cost as pension assets. The amendment had no impact on the financial position or performance of the Group.

IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*

The new interpretation addresses the accounting by an entity when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor of the entity to extinguish all or part of the financial liability. The interpretation had no effect on the financial position or performance of the Group.

Improvements to IFRSs

In May 2010, the International Accounting Standards Board issued "Improvements to IFRSs", primarily with a view to removing inconsistencies and clarifying wording. These are separate transitional provisions for each standard. The document sets out amendments to International Financial Reporting Standards, which are mainly related to changes for presentation, recognition or management purposes terminology or editorial changes. These amendments did not have any impact on the financial position or performance of the Group.

Voluntary Change in Accounting Policies

In the year ended December 31, 2011, the Group changed its accounting treatment in respect of certain payments made to retired employees. Previously such benefits were treated as those that do not represent a constructive obligation. Starting 2011, the Group considers such payments as a constructive obligation as the Group intends to continue paying such benefits. Consequently, the Group recognised liability on such benefits retrospectively as a part of defined benefit obligation. The impact of this voluntary change in accounting policy on the consolidated financial statements resulted in reduced retained earnings attributable to equity holders of the parent, reduced balance of non-controlling interests and increased post-employment benefits liability.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Changes in Accounting Policies (continued)

Reclassifications

Certain corresponding information presented in the consolidated financial statements for the year ended December 31, 2010 has been reclassified in order to achieve comparability with the presentation used in these consolidated financial statements.

New Accounting Pronouncements

The following new or amended (revised) IFRS and IFRIC have been issued but are not yet effective and not applied by the Group. This listing of standards and interpretations issued are those that the Group reasonably expects to have an impact on disclosures, financial position and performance when applied at a future date. The Group intends to adopt these standards when they become effective.

IFRS 7 *Financial Instruments: Disclosures* (amended)

In October 2010, the International Accounting Standards Board issued amendments to IFRS 7 – *Disclosures – Transfers of Financial Assets*. These amendments require additional disclosure about financial assets that have been transferred but not derecognised to enable users of the Group's financial statements to understand the relationship with those assets that have not been derecognised and their associated liabilities. In addition, the amendments require disclosures about continuing involvement in derecognised assets to enable users to evaluate the nature of, and risks associated with, the Group's continuing involvement in those derecognised assets. These amendments become effective for financial years beginning on or after July 1, 2011. In December 2011, the International Accounting Standards Board further amended IFRS 7 by clarifying requirements for offsetting financial assets and financial liabilities. These amendments become effective for financial years beginning on or after January 1, 2013. The amendments affect disclosure only and will have no impact on the Group's financial position or performance.

IFRS 9 *Financial Instruments* (effective for financial years beginning on or after January 1, 2015)

The standard as issued reflects the first phase of the International Accounting Standards Boards work on the replacement of IAS 39 *Financial Instruments: Recognition and Measurement* and applies to classification and measurement of financial assets and financial liabilities. In subsequent phases, the International Accounting Standards Board will address impairment methodology and hedge accounting. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets and financial liabilities. The Group will quantify the effect in conjunction with the other phases, when issued, to present a comprehensive picture.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Changes in Accounting Policies (continued)

New Accounting Pronouncements (continued)

IFRS 10 Consolidated Financial Statements (effective for financial years beginning on or after January 1, 2013)

IFRS 10 replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements. It also includes the issues raised in SIC-12 *Consolidation — Special Purpose Entities*. IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require management to exercise significant judgement to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27. The Group expects that the adoption of the new standard will not have a significant impact on its financial position or performance in the period of initial application.

IFRS 11 Joint Arrangements (effective for financial years beginning on or after January 1, 2013)

IFRS 11 replaces IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly-controlled Entities — Non-monetary Contributions by Venturers*. IFRS 11 removes the option to account for jointly controlled entities using proportionate consolidation. Jointly controlled entities must be accounted for using the equity method. The Group expects that the adoption of the new standard will not have a significant impact on its financial position or performance in the period of initial application.

IFRS 12 Disclosure of Involvement with Other Entities (effective for financial years beginning on or after January 1, 2013)

IFRS 12 includes all of the disclosures that were previously in IAS 27 *Consolidated and Separate Financial Statements* related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 *Interests in Joint Ventures* and IAS 28 *Investments in Associates*. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required. The amendment affects disclosures only and will have no impact on the Group's financial position or performance.

IFRS 13 Fair Value Measurement (effective for financial years beginning on or after January 1, 2013)

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Group is currently assessing the impact that this standard will have on the financial position and performance.

IAS 1 Financial Statement Presentation (amended) – Presentation of Items of Other Comprehensive Income (effective for financial years beginning on or after July 1, 2012)

The amendments change the grouping of items presented in other comprehensive income. Items that could be reclassified to profit or loss at a future point in time would be presented separately from items that will never be reclassified. The amendments affect presentation only and will have no impact on the Group's financial position or performance.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Changes in Accounting Policies (continued)

New Accounting Pronouncements (continued)

IAS 12 *Income Taxes* (amended) – Deferred Tax: Recovery of Underlying Assets (effective for financial years beginning on or after January 1, 2012)

The amendment clarifies the determination of deferred tax on investment property measured at fair value. The amendment introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. Furthermore, it introduces the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in IAS 16 always be measured on a sale basis of the asset. The Group expects that the adoption of the amended standard will not have a significant impact on its financial position or performance in the period of initial application.

IAS 19 *Employee Benefits* (revised) (effective for financial years beginning on or after January 1, 2013)

The revision includes a number of changes that range from fundamental changes such as removing the “corridor” mechanism (the revised standard requires actuarial gains and losses to be recognised in other comprehensive income when they occur) and the concept of expected returns on plan assets to new and revised disclosure requirements and simple clarifications and re-wording. The Group expects that the adoption of the amended standard will affect disclosures and presentation of financial statements only and will have no impact on the Group’s financial position or performance as the Group’s current accounting policy is to recognise actuarial gains and losses in the income statement in the period in which they occurred without using the “corridor” mechanism.

IAS 27 *Separate Financial Statements* (revised) (effective for financial years beginning on or after January 1, 2013)

As a consequence of the new IFRS 10 *Consolidated Financial Statements* and IFRS 12 *Disclosure of Involvement with Other Entities*, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. The revision will have no impact on the consolidated financial statements of the Group.

IAS 28 *Investments in Associates and Joint Ventures* (revised) (effective for financial years beginning on or after January 1, 2013)

As a consequence of the new IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Involvement with Other Entities*, IAS 28 has been renamed to IAS 28 *Investments in Associates and Joint Ventures*, and describes the application of the equity method to investments in joint ventures in addition to associates. The Group expects that the adoption of the amended standard will not have a significant impact on its financial position or performance in the period of initial application.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

A) Basis of Consolidation

A subsidiary is an entity in which the Group has an interest of more than one-half of the voting rights or otherwise has power to exercise control over its operations. Subsidiaries are consolidated from the date when control over their activities is transferred to the Company and are no longer consolidated from the date when control ceases.

All intragroup balances, transactions and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transactions provide evidence of an impairment of the asset transferred. Where necessary, accounting policies in subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to a parent. Non-controlling interests at the end of the reporting period represent the non-controlling interest shareholders' portion of the fair values of the identifiable assets and liabilities of the subsidiary at the acquisition date and the non-controlling interests' portion of movements in equity since the date of the combination. Non-controlling interest is presented within equity, separately from the parent's shareholders' equity.

Losses within subsidiary are attributed to the non-controlling interest even if that results in deficit balance.

When the Group increases its ownership interests in subsidiaries, the differences between the carrying values of net assets attributable to interests in subsidiaries acquired and the consideration given for such increases is either added to additional paid-in capital, if positive, or charged to accumulated profits, if negative.

When the Group grants put options to non-controlling interest shareholders at the date of acquiring control of a subsidiary the Group considers the terms of transaction to conclude on accounting treatment.

Where the terms of the put option provide the Group with a present ownership interest in the shares subject to the put, the shares are accounted for as acquired. Financial liabilities in respect of put options are recorded at fair value at the time of entering into the options, and are subsequently re-measured to fair value with the change in fair value recognised in the income statement.

When the terms of the put option do not provide a present ownership interest in the shares subject to the put, the Group determined that its accounting policy is to partially recognise non-controlling interests and to account such put options as the following:

- the Group determines the amount recognised for the non-controlling interest, including its share of profits and losses (and other changes in equity) of the subsidiary for the period;
- the Group derecognises the non-controlling interest as if it was acquired at that date;
- the Group records the fair value of financial liability in respect of put options; and
- the Groups accounts for the difference between the non-controlling interest derecognised and the fair value of financial liability as a change in the non-controlling interest as an equity transaction (in accordance with the Group's policy for the increase of its ownership interests in subsidiaries).

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

A) Basis of Consolidation (continued)

When the Group loses control over a subsidiary, it:

- Derecognises the assets (including goodwill) and liabilities of the subsidiary
- Derecognises the carrying amount of any non-controlling interest
- Derecognises the cumulative translation differences, recorded in equity
- Recognises the fair value of the consideration received
- Recognises the fair value of any investment retained
- Recognises any surplus or deficit in profit or loss
- Reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss or retained earnings, as appropriate.

B) Business Combination and Goodwill

Acquisition of Subsidiaries

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs are included in administrative expenses in the periods in which the costs are incurred.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability, are recognised either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it is not remeasured until it is finally settled within equity.

Goodwill

Goodwill is initially measured at cost being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interest over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in profit or loss. Goodwill is recorded in the functional currencies of the acquired subsidiaries.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

B) Business Combination and Goodwill (continued)

Goodwill (continued)

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that its carrying amount may be impaired. As at the acquisition date, goodwill is allocated to each of the cash-generating units (groups of cash-generating units), expected to benefit from the synergies of the combination. Impairment is determined by assessing the recoverable amount of the cash-generating unit (groups of cash-generating units), to which the goodwill relates. Where recoverable amount of cash-generating unit (groups of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Acquisition of Subsidiaries from Entities under Common Control

Purchases of subsidiaries from entities under common control are accounted for using the pooling of interests method.

The assets and liabilities of the subsidiary transferred under common control are recorded in the financial statements at the historical cost of the controlling entity (the "Predecessor"). Any difference between the total book value of net assets, including the Predecessor's goodwill, and the consideration paid is accounted for in the consolidated financial statements as an adjustment to equity. The financial statements, including corresponding figures, are presented as if the Company had acquired the subsidiary on the date it was initially acquired by the Predecessor.

C) Cash and Cash Equivalents

Cash is comprised of cash in hand and cash at banks.

Cash equivalents are comprised of short-term, liquid investments (with original maturity date less than 90 days) that are readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value. Cash equivalents are carried at fair value.

Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

D) Financial Assets

Initial Recognition and Measurement

The Group classifies its financial assets into the following categories: loans and receivables, financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial assets on initial recognition and, where allowed and appropriate, reevaluates this designation at each reporting date.

Financial assets are initially recognised at fair value plus directly attributable transaction costs. However when a financial asset at fair value through profit or loss is recognised, the transaction costs are expensed immediately.

Subsequent Measurement

The subsequent measurement of financial assets depends on their classification as described below:

Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments not quoted in an active market. Subsequent to initial measurement, such assets are carried at amortised cost using the effective interest method less any allowance for impairment. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Trade receivables, which generally are short term, are carried at original invoice amount less an allowance for doubtful debts. An allowance for doubtful debts is established in case of objective evidence that the Group will not be able to collect amounts due according to the original terms of contract. The Group periodically analyses trade receivables and makes adjustments to the amount of the allowance. The amount of the allowance is the difference between the carrying amount and recoverable amount. The amount of the doubtful debts expense is recognised in the income statement.

Financial Assets at Fair Value through Profit or Loss

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Financial assets are classified as held-for-trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments as defined by IAS 39. Gains or losses on held-for-trading assets are recognised in the income statement.

Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

D) Financial Assets (continued)

Held-to-Maturity Investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity, when the Group has the positive intention and ability to hold to maturity. Subsequent to initial recognition, held-to-maturity investments are recognised at amortised cost using the effective interest method less any allowance for impairment. During the period, the Group did not hold any investments in this category.

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 unrealised gains or losses being recognised as other comprehensive income until the financial assets are derecognised or determined to be impaired, at which time the cumulative gain or loss is included in the income statement.

Derivatives Designated as Hedging Instruments

Derivatives are financial instruments that change their values in response to changes in the underlying variable, require no or little net initial investment and are settled at a future date. Derivatives are primarily used to manage exposures to foreign exchange risk, interest rate risk and other market risks.

For the purpose of hedge accounting, derivatives are designated as instruments hedging the Group's exposure to changes in the fair value of a recognised asset or liability (fair value hedges), as instruments hedging the Group's exposure to variability in cash flows attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (cash flow hedges) and as hedges of a net investment in a foreign operation.

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group applies hedge accounting and the risk management objective and strategy for undertaking the hedge.

The Group's derivatives mainly consist of currency forwards and their use is governed by the Group's policies which are consistent with Group's overall risk management strategy. These derivatives are designated as hedging instruments in cash flow hedge. The objective of the hedge is to protect the value of highly probable future export sales in foreign currency against unfavourable variations of exchange rates.

The Group assesses effectiveness of such hedges at inception and verifies at regular intervals and at least on a quarterly basis, using prospective and retrospective testing. The effective part of the changes in fair value of hedging instruments is recognised in other comprehensive income while any ineffective part is recognised immediately in the income statement. When forecasted transaction occurs, the gains or losses previously recognised in other comprehensive income are transferred to the income statement. If the forecast transaction is no longer expected to occur, the cumulative gain or loss previously recognised in other comprehensive income is transferred to the income statement.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

D) Financial Assets (continued)

Impairment of Financial Assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred “loss event”) and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indicators that a debtor or a group of debtors is experiencing significant financial difficulties, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

The amount of the impairment loss is measured as a difference between the asset’s carrying amount and the present value of estimated future cash flows. The carrying amount of financial assets other than loans and receivables is reduced directly without the use of an allowance account and the amount of loss is recognised in the income statement.

E) Borrowings

Borrowings are initially recognised at fair value less directly attributable transaction costs. In subsequent periods, borrowings are measured at amortised cost using the effective interest method. Any difference between the initial fair value less transaction costs and the redemption amount is recognised within finance costs over the period of the borrowings.

Finance cost of the loans, including the issue costs and any discount on issue, is dealt with as a profit and loss charge over the term of the debt using the effective interest method. Carrying amount of the loan is decreased by unamortised balance of debt issue costs.

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of cost of respective assets. All other borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

F) Inventories

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and costs necessary to make the sale. The cost of inventories is determined on the weighted average basis.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

F) Inventories (continued)

The costs of inventories are comprised of all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present condition and location. The value of work in progress and finished goods includes costs of raw materials, direct labor, direct production costs and indirect production overheads including depreciation. Financing costs are not included in stock valuation.

The Group periodically analyses inventories to determine whether they are damaged, obsolete or slow-moving or if their net realisable value has declined, and makes allowance for such inventories.

In preparing the consolidated financial statements, unrealised profits resulting from intragroup transactions are eliminated in full.

G) Property, Plant and Equipment

Property, plant and equipment, except for the items acquired prior to January 1, 2003, are stated at historical cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any impairment in value. Such cost includes the cost of replacing part of plant and equipment when the cost is incurred if the recognition criteria are met.

The items of property, plant and equipment acquired prior to January 1, 2003, the date of transition to IFRS, were accounted for at deemed cost being their fair value as at January 1, 2003.

Depreciation is calculated on a straight-line basis. Average depreciation periods, which represent estimated useful economic lives of respective assets, are as follows:

Land	Not depreciated
Buildings	8-100 years
Machinery and equipment	5-30 years
Transport and motor vehicles	4-15 years
Furniture and fixtures	2-10 years

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised, and assets replaced are retired. Gains and losses arising from retirement of property, plant and equipment are included in the income statement as incurred.

When material repairs are performed, the Group recognises cost of repair as a separate component within the relevant item of property, plant and equipment if the recognition criteria are met.

The Group has the title to certain non-production and social assets, primarily buildings and social infrastructure facilities. The items of social infrastructure do not meet the definition of an asset according to IFRS. Construction and maintenance costs of social infrastructure facilities are expensed as incurred.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

H) Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to finance costs in the income statement.

The depreciation policy for depreciable leased assets is consistent with that for depreciable assets which are owned. If there is no reasonable certainty that the Group will obtain ownership by the end of the lease term, the asset is fully depreciated over the shorter of the lease term or its useful life.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

I) Intangible Assets (Other than Goodwill)

Intangible assets (other than goodwill) are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that intangible asset may be impaired. Amortisation period and amortisation method for an intangible asset with a finite life are reviewed at least at each year end. Changes in expected useful life or expected pattern of consumption of future economic benefits embodied in the asset are treated as changes in accounting estimates. Amortisation expense of intangible assets is recognised in the income statement in the expense category consistent with the function of an intangible asset.

Intangible assets with indefinite useful lives are not amortised, they are tested for impairment annually either individually or at the cash-generating unit level.

OAo TMK

Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

I) Intangible Assets (Other than Goodwill) (continued)

Research and Development

Costs incurred on development (relating to design and testing of new or improved products) are recognised as intangible assets only when the Group can demonstrate technical feasibility of completing intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, availability of resources to complete and ability to measure reliably the expenditure during the development. Other development expenditures are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs that have been capitalised are amortised from commencement of commercial production of the product on a straight-line basis over the period of its expected benefit. The carrying value of development costs is reviewed for impairment annually when the asset is not yet in use or more frequently when an indication of impairment arises during the reporting year.

J) Impairment of Non-Financial Assets (Other than Goodwill)

An assessment is made at each reporting date to determine whether there is an objective evidence that an asset or a group of assets may be impaired. When there is an indication that an asset may be impaired, the recoverable amount is assessed and, when impaired, the asset is written down immediately to its recoverable amount, which is the higher of the fair value less costs to sell and the value in use.

Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, after deducting any direct incremental disposal costs. Value in use is the present value of estimated future cash flows expected to arise from continuing use of an asset and from its disposal at the end of its useful life.

In assessing value in use, estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, recoverable amount is determined for the cash-generating unit to which the asset belongs.

Impairment loss is recognised for the difference between estimated recoverable amount and carrying value. Carrying amount of an asset is reduced to its estimated recoverable amount and the amount of loss is included in the income statement for the period.

Impairment loss is reversed if there is an indication that an impairment loss recognised in prior periods for an asset other than goodwill may no longer exist or may be decreased and if subsequent increase in recoverable amount can be related objectively to event occurring after the impairment loss was recognised. Impairment loss is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

Intangible assets not yet available for use are tested for impairment annually.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

K) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that outflow of resources will be required to settle obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

If the effect of time value of money is material, provisions are determined by discounting expected future cash flows at a pre-tax rate that reflects current market assessments of time value of money and where appropriate, risks specific to the liability. Where discounting is used, increase in provision due to the passage of time is recognised as a finance cost.

L) Post-Employment Benefits

The Group companies provide additional pensions and other post-employment benefits to their employees in accordance with collective bargaining agreements. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age, the completion of a minimum service period and the amount of the benefits stipulated in the collective bargaining agreements.

Liability recognised in the statement of financial position in respect of post-employment benefits is the present value of defined benefit obligation at the end of the reporting period less fair value of the plan assets. Defined benefit obligation is calculated by external consultants quarterly using the projected unit credit method. Present value of the benefits is determined by discounting estimated future cash outflows using interest rates of high-quality government bonds that are denominated in currency in which benefits would be paid, and that have terms to maturity approximating to the terms of the related obligations.

Actuarial gains and losses are recognised in the income statement in the period in which they occurred. Past service cost is recognised as an expense on a straight-line basis over the average period until the benefits become vested.

M) Value Added Tax

The Russian tax legislation partially permits settlement of value added tax ("VAT") on a net basis.

VAT is payable upon invoicing and delivery of goods, performing work or rendering services, as well as upon collection of prepayments from customers. VAT on purchases, even if they have not been settled at the end of the reporting period, is deducted from the amount of VAT payable.

Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

N) Deferred Income Tax

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income tax is recognised in the income statement, except to the extent that it relates to items directly taken to equity or other comprehensive income, in which case it is recognised against equity or other comprehensive income.

Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where deferred income tax arises from initial recognition of goodwill or of an asset or liability in transaction that is not a business combination and, at the time of the transaction, affects neither accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the end of the reporting period.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where timing of reversal of temporary differences can be controlled and it is probable that temporary differences will not be reversed in the near future.

O) Equity

Share Capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from proceeds in equity.

Treasury Shares

Own equity instruments which are acquired by the Group (treasury shares) are deducted from equity. No gain or loss is recognised in the income statement on the purchase, sale, issue or cancellation of treasury shares.

Dividends

Dividends are recognised as a liability and deducted from equity at the end of the reporting period only if they are declared before or on the end of the reporting period. Dividends are disclosed in the financial statements when they are proposed before the end of the reporting period or proposed or declared after the end of the reporting period but before the financial statements are authorised for issue.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

Significant Accounting Policies (continued)

P) Revenue Recognition

Revenue is recognised to the extent that it is probable that economic benefits will flow to the Group and the amount of revenue can be measured reliably. Revenues from sales of inventory are recognised when significant risks and rewards of ownership of goods have passed to the buyer. Revenues arising from rendering of services are recognised in the same period when the services are provided.

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, revenue is measured at the fair value of goods or services provided.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

1) Segment Information

Operating segments reflect the Group's management structure and the way financial information is regularly reviewed. For management purposes, the Group is organised into business divisions based on geographical location, and has three reportable segments:

- Russia segment represents the results of operations and financial position of plants located in Russian Federation, a finishing facility in Kazakhstan, Oilfield service companies and traders located in Russia, Kazakhstan, the United Arab Emirates, Switzerland, South Africa that are selling their production (seamless and welded pipes).
- Americas segment represents the results of operations and financial position of plants located in the United States of America and traders located in the United States of America and Canada (seamless and welded pipes).
- Europe segment represents the results of operations and financial position of plants and traders located in Europe (excluding Switzerland) selling their production (seamless pipes and steel billets).

Management monitors the operating results of its operating segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on adjusted EBITDA. Adjusted EBITDA is determined as profit/(loss) for the period excluding finance costs and finance income, income tax (benefit)/expense, depreciation and amortisation, foreign exchange (gain)/loss, impairment/(reversal of impairment) of non-current assets, movements in allowances and provisions, (gain)/loss on disposal of property, plant and equipment, (gain)/loss on changes in fair value of financial instruments, share of (profit)/loss of associate and other non-cash items. Group financing (including finance costs and finance income) is managed on a group basis and is not allocated to operating segments.

The following tables present revenue and profit information regarding the Group's reportable segments for the years ended December 31, 2011 and 2010, respectively.

Year ended December 31, 2011	Russia	Americas	Europe	TOTAL
Revenue	4,788,039	1,590,399	375,079	6,753,517
Cost of sales	(3,752,176)	(1,279,603)	(275,464)	(5,307,243)
GROSS PROFIT	1,035,863	310,796	99,615	1,446,274
Selling, general and administrative expenses	(529,741)	(149,305)	(42,885)	(721,931)
Other operating income/(expenses), net	(38,780)	2,255	(3,710)	(40,235)
OPERATING PROFIT	467,342	163,746	53,020	684,108
ADD BACK:				
Depreciation and amortisation	228,405	98,476	8,890	335,771
Loss/(gain) on disposal of property, plant and equipment	2,083	(49)	285	2,319
Allowance for net realisable value of inventory	(426)	(107)	(129)	(662)
Allowance for doubtful debts	17,819	897	835	19,551
Movement in other provisions	5,408	2,427	1,204	9,039
	253,289	101,644	11,085	366,018
ADJUSTED EBITDA	720,631	265,390	64,105	1,050,126

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

1) Segment Information (continued)

Year ended December 31, 2011	Russia	Americas	Europe	TOTAL
RECONCILIATION TO PROFIT BEFORE TAX:				
ADJUSTED EBITDA	720,631	265,390	64,105	1,050,126
Reversal of adjustments from operating profit to EBITDA	(253,289)	(101,644)	(11,085)	(366,018)
OPERATING PROFIT	467,342	163,746	53,020	684,108
Impairment of goodwill	(3,368)	–	–	(3,368)
Impairment of investment in associate	(1,833)	–	–	(1,833)
Reversal of impairment of property, plant and equipment	–	–	73,417	73,417
Foreign exchange gain/(loss), net	(2,021)	(2,738)	3,505	(1,254)
OPERATING PROFIT AFTER IMPAIRMENT AND FOREIGN EXCHANGE GAIN/(LOSS)	460,120	161,008	129,942	751,070
Finance costs				(302,786)
Finance income				32,063
Gain on changes in fair value of derivative financial instrument				44,792
Share of loss of associate				(185)
Gain on disposal of assets classified as held for sale				19,184
PROFIT BEFORE TAX				544,138

Year ended December 31, 2010	Russia	Americas	Europe	TOTAL
Revenue	3,997,737	1,324,380	256,482	5,578,599
Cost of sales	(3,065,574)	(1,022,663)	(197,112)	(4,285,349)
GROSS PROFIT	932,163	301,717	59,370	1,293,250
Selling, general and administrative expenses	(470,495)	(152,734)	(36,297)	(659,526)
Other operating income/(expenses), net	(32,867)	700	(1,769)	(33,936)
OPERATING PROFIT	428,801	149,683	21,304	599,788
ADD BACK:				
Depreciation and amortisation	172,647	119,928	8,040	300,615
Loss/(gain) on disposal of property, plant and equipment	9,650	(26)	571	10,195
Allowance for net realisable value of inventory	(3,247)	(529)	(1,042)	(4,818)
Allowance for doubtful debts	6,520	(1,103)	3	5,420
Movement in other provisions	18,346	12,603	166	31,115
	203,916	130,873	7,738	342,527
ADJUSTED EBITDA	632,717	280,556	29,042	942,315

Year ended December 31, 2010	Russia	Americas	Europe	TOTAL
RECONCILIATION TO PROFIT BEFORE TAX:				
ADJUSTED EBITDA	632,717	280,556	29,042	942,315
Reversal of adjustments from operating profit to EBITDA	(203,916)	(130,873)	(7,738)	(342,527)
OPERATING PROFIT	428,801	149,683	21,304	599,788
Foreign exchange gain/(loss), net	19,391	–	(9,879)	9,512
OPERATING PROFIT AFTER FOREIGN EXCHANGE GAIN/(LOSS)	448,192	149,683	11,425	609,300
Finance costs				(430,586)
Finance income				18,895
Loss on changes in fair value of derivative financial instrument				(12,361)
PROFIT BEFORE TAX				185,248

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

1) Segment Information (continued)

The following tables present additional information of the Group's reportable segments as at December 31, 2011 and 2010:

Year ended December 31, 2011	Russia	Americas	Europe	TOTAL
Segment assets	4,771,557	1,957,104	403,580	7,132,241
Property, plant and equipment expenditure	247,629	64,322	14,047	325,998

Year ended December 31, 2010	Russia	Americas	Europe	TOTAL
Segment assets	4,585,342	1,941,572	334,620	6,861,534
Property, plant and equipment expenditure	228,657	36,188	5,456	270,301

The following table presents the revenues from external customers for each group of similar products and services for the years ended December 31, 2011 and 2010, respectively:

Sales to external customers	Welded pipes	Seamless pipes	Other operations	TOTAL
Year ended December 31, 2011	2,535,658	3,910,622	307,237	6,753,517
Year ended December 31, 2010	2,351,729	2,951,592	275,278	5,578,599

The following tables present the geographic information. The revenue information is disclosed based on the location of the customer. Non-current assets are disclosed based on the location of the Group's assets and include property, plant and equipment, intangible assets and goodwill.

Year ended December 31, 2011	Russia	Americas	Cent.Asia & Caspian Region	Middle East & Gulf Region	Africa	Europe	Asia & Far East	TOTAL
Revenue	4,070,519	1,801,174	197,276	67,671	4,237	589,397	23,243	6,753,517
Non-current assets	2,746,620	1,296,053	21,633	42	17	243,757	-	4,308,122

Year ended December 31, 2010	Russia	Americas	Cent.Asia & Caspian Region	Middle East & Gulf Region	Africa	Europe	Asia & Far East	TOTAL
Revenue	3,485,287	1,434,653	161,115	56,132	13,030	398,586	29,796	5,578,599
Non-current assets	2,882,293	1,330,740	25,270	46	23	177,432	-	4,415,804

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

2) Cost of Sales

Cost of sales for the year ended December 31 was as follows:

	2011	2010
Raw materials and consumables	3,720,904	2,971,841
Staff costs including social security	661,764	540,214
Energy and utilities	400,169	336,072
Depreciation and amortisation	257,589	218,251
Repairs and maintenance	162,434	110,087
Freight	63,741	52,259
Contracted manufacture	55,625	70,597
Taxes	51,777	43,543
Professional fees and services	25,841	19,986
Rent	10,450	8,900
Travel	2,596	1,568
Communications	1,173	858
Insurance	803	774
Other	3,798	4,045
Total production cost	5,418,664	4,378,995
Change in own finished goods and work in progress	(147,035)	(170,645)
Cost of sales of externally purchased goods	33,235	80,949
Obsolete stock, write-offs/(reversal of write-offs)	2,379	(3,950)
Cost of sales	5,307,243	4,285,349

3) Selling and Distribution Expenses

Selling and distribution expenses for the year ended December 31 were as follows:

	2011	2010
Freight	212,425	207,384
Depreciation and amortisation	65,536	81,304
Staff costs including social security	58,807	53,980
Consumables	20,020	18,465
Bad debt expense	19,618	5,740
Professional fees and services	14,701	18,196
Rent	7,953	6,690
Travel	4,501	4,185
Utilities and maintenance	2,169	1,587
Insurance	1,731	1,303
Communications	1,294	1,282
Taxes	849	1,281
Other	1,648	1,746
	411,252	403,143

4) Advertising and Promotion Expenses

Advertising and promotion expenses for the year ended December 31 were as follows:

	2011	2010
Exhibits and catalogues	5,451	4,014
Outdoor advertising	2,256	5,800
Media	877	636
Other	620	649
	9,204	11,099

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

5) General and Administrative Expenses

General and administrative expenses for the year ended December 31 were as follows:

	2011	2010
Staff costs including social security	158,573	126,525
Professional fees and services	55,056	47,737
Depreciation and amortisation	13,224	12,658
Travel	12,928	9,132
Utilities and maintenance	9,126	7,626
Transportation	6,130	4,571
Insurance	5,366	3,957
Communications	5,307	4,102
Rent	5,294	5,427
Taxes	5,174	5,241
Consumables	4,123	2,795
Other	2,484	2,204
	282,785	231,975

6) Research and Development Expenses

Research and development expenses for the year ended December 31 were as follows:

	2011	2010
Staff costs including social security	11,669	9,510
Professional fees and services	2,999	1,578
Depreciation and amortisation	1,003	643
Consumables	860	379
Travel	731	378
Utilities and maintenance	727	426
Transportation	285	153
Other	416	242
	18,690	13,309

7) Other Operating Expenses

Other operating expenses for the year ended December 31 were as follows:

	2011	2010
Sponsorship and charitable donations	17,579	10,207
Social and social infrastructure maintenance expenses	16,859	12,104
Penalties, fines and expenses related to tax issues	12,567	8,675
Loss on disposal of property, plant and equipment	2,319	10,195
Other	4,001	3,797
	53,325	44,978

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

8) Other Operating Income

Other operating income for the year ended December 31 was as follows:

	2011	2010
Gain from penalties and fines	4,235	2,340
Reimbursement from insurance company	1,272	–
Assets received for free	494	553
Gain on sales of current assets	43	296
Income from emission rights sale	–	2,149
Other	7,046	5,704
	13,090	11,042

9) Finance Income

Finance income for the year ended December 31 was as follows:

	2011	2010
Dividends	27,481	14,992
Interest income - bank accounts and deposits	3,333	3,024
Gain on disposal of other investments	1,249	879
	32,063	18,895

10) Investments in Associates

Volgograd River Port

On August 4, 2011, the Group acquired 25.5% ownership interest in Volgograd River Port for 112,825 thousand Russian roubles (4,004 at the exchange rates as at the payment dates).

As at December 31, 2011, there was objective evidence of impairment of investment in Volgograd River Port, therefore, the Group performed an impairment test at that date in respect of this investment. As a result of that test, the Group determined that the carrying value of investment in Volgograd River Port exceeds its recoverable amount. Consequently, the Group recognised impairment of investment in Volgograd River Port in the amount of 1,833.

Movement in investment in Volgograd River Port was as follows:

Acquisition of share in associate	4,004
Share of loss of associate	(185)
Impairment of investment in associate	(1,833)
Currency translation adjustment	(324)
Investment in associate as at December 31, 2011	1,662

Lhoist-TMK B.V.

On November 4, 2011, the Group established a new entity Lhoist-TMK B.V. with the ownership interest of 30%.

As at December 31, 2011, the carrying value of investment in Lhoist-TMK B.V. was 55.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

11) Gain on Disposal of Assets Classified as Held for Sale

On May 27, 2011, the Group sold 100% ownership interest in TMK HYDROENERGY POWER S.R.L.

As at the date of disposal the carrying amounts of assets and liabilities were as follows:

	May 27, 2011
Cash and cash equivalents	12
Trade receivables	685
Inventories	59
Prepayments	12
Current assets	768
Property, plant and equipment	8,702
Intangible assets	105
Deferred tax asset	138
Non-current assets	8,945
Total assets	9,713
Trade and other payables	(170)
Total liabilities	(170)
Net assets	9,543

Gain from disposal of TMK HYDROENERGY POWER S.R.L. in the amount of 19,184 was included in the income statement for the year ended December 31, 2011.

In December 2010, the Group received 26,027 as a consideration from the purchaser. The cash consideration received was included in advances from customers.

12) Income Tax

Income tax expense for the year ended December 31 was as follows:

	2011	2010
Current income tax expense	98,034	53,985
Current income tax benefit	–	(2,430)
Adjustments in respect of income tax of previous periods	(634)	(1,697)
Deferred tax expenses arising from write-down of deferred tax asset	2,193	46
Deferred income tax expense related to origination and reversal of temporary differences	59,848	31,270
Total income tax expense	159,441	81,174

Profit before tax for financial reporting purposes is reconciled to tax expense as follows:

	2011	2010
Profit before tax	544,138	185,248
Theoretical tax charge at statutory rate in Russia of 20%	108,828	37,050
Adjustment in respect of income tax of previous years	(634)	(1,697)
Effect of items which are not deductible or assessable for taxation purposes	17,333	30,455
Effect of different tax rates in countries other than Russia	25,228	14,689
Tax on dividends distributed by the Group's subsidiaries to parent company	11,537	2,085
Effect of differences in tax rates on dividend income	(3,023)	(1,649)
Effect of change of US (state) effective tax rate	(1,909)	1,317
Deferred tax expenses arising from write-down of deferred tax asset	2,193	46
Effect of unrecognised tax credits, tax losses and temporary difference of a prior period	152	(971)
Other	(264)	(151)
Total income tax expense	159,441	81,174

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

12) Income Tax (continued)

Deferred income tax assets and liabilities, their movements for the years ended December 31, 2011 and 2010 were as follows:

	2011	Change recognised in income statement	Change recognised in other comprehensive income	Foreign currency translation reserve	2010	Change recognised in income statement	Change recognised in other comprehensive income	Foreign currency translation reserve	2009
Deferred income tax liability:									
Valuation and depreciation of property, plant and equipment	(282,741)	(22,522)	–	11,557	(271,776)	(18,945)	–	1,481	(254,312)
Valuation and amortisation of intangible assets	(46,686)	12,615	–	(16)	(59,285)	13,330	–	(1)	(72,614)
Valuation of accounts receivable	(5,985)	(34)	–	339	(6,290)	429	–	50	(6,769)
Valuation of inventory	(2,960)	(12,401)	–	131	9,310	(8,854)	–	(30)	18,194
Prepayments and other current assets	(529)	1,976	–	(11)	(2,494)	(2,996)	–	(3)	505
	(338,901)	(20,366)	–	12,000	(330,535)	(17,036)	–	1,497	(314,996)
Deferred income tax asset:									
Tax losses available for offset	98,049	(42,957)	13,554	(4,244)	131,696	(21,395)	1,769	(975)	152,297
Provisions and accruals	14,441	1,350	–	(457)	13,548	8,951	–	(45)	4,642
Trade and other payable	5,393	565	–	39	4,789	(2,025)	–	(9)	6,823
Finance lease obligations	6,709	71	–	(381)	7,019	(1)	–	(55)	7,075
Impairment of accounts receivable	5,477	3,354	–	(423)	2,546	(397)	–	(14)	2,957
Other	1,927	(4,058)	–	225	5,760	587	–	(17)	5,190
	131,996	(41,675)	13,554	(5,241)	165,358	(14,280)	1,769	(1,115)	178,984
Net deferred income tax liability	(304,785)	(14,313)	–	10,012	(300,484)	(30,076)	–	1,256	(271,664)
Net deferred income tax asset	97,880	(47,728)	13,554	(3,253)	135,307	(1,240)	1,769	(874)	135,652

In the context of the Group's current structure, tax losses and current tax assets of the different companies are not offset against taxable profits and current tax liability of other companies and, accordingly, taxes may accrue even where there is a net consolidated tax loss. Therefore, a deferred tax asset of one subsidiary of the Group is not offset against the deferred tax liability of another subsidiary.

As at December 31, 2011, the deferred tax asset for 3,439 (2010: 3,633) relating to tax deductible losses incurred in transactions with securities has not been recognised, as it is not probable that sufficient taxable profit on transactions with securities will be available to offset the deductible temporary differences to which the asset relates. Such tax losses are offset only against future taxable profits generated in transactions with securities over a period of 3 years.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

12) Income Tax (continued)

The Group recognised the deferred tax assets for the companies with net loss. The Group believes that this tax loss will be recovered as future taxable profits will exceed recognised tax asset on tax loss.

As at December 31, 2011, the Group has not recognised deferred tax liability in respect of 1,301,486 (2010: 1,321,361) temporary differences associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

13) Earnings per Share

Basic earnings per share are calculated by dividing the profit for the period attributable to ordinary shareholders of the parent entity by the weighted average number of ordinary shares in issue during the period.

Diluted earnings per share are calculated by dividing the profit for the period attributable to ordinary shareholders of the parent entity adjusted for interest expense and other gains and losses for the period, net of tax, relating to convertible bonds by the weighted average number of ordinary shares outstanding during the period plus the weighted average number of shares that would be issued on the conversion of all the potential dilutive ordinary shares into ordinary shares.

In calculation of diluted earnings per share, the denominator represents the weighted average number of ordinary shares which could be outstanding assuming that all of the convertible bonds were converted into ordinary shares (Note 24).

	Year ended December 31,	
	2011	2010
Profit for the year attributable to the equity holders of the parent entity	380,130	104,334
Effect of convertible bonds, net of tax (if dilutive)	(1,710)	–
Profit for the year attributable to the equity holders of the parent entity adjusted for the effect of dilution	378,420	104,334
Weighted average number of ordinary shares outstanding	864,976,286	860,480,570
Weighted average number of ordinary shares outstanding adjusted for the effect of dilution	936,751,609	860,480,570
Earnings per share attributable to equity holders of the parent entity, basic and diluted in US dollars		
Basic	0.44	0.12
Diluted	0.40	0.12
Earnings per share attributable to equity holders of the parent entity, basic and diluted in Russian roubles		
Basic	12.91	3.68
Diluted	11.87	3.68

In the year ended December 31, 2010, the convertible bonds were antidilutive as the interest expense and other gains and losses for the period, net of tax, relating to convertible bonds divided by the number of ordinary shares obtainable on the conversion of the convertible bonds exceeded basic earnings per share.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

14) Cash and Cash Equivalents

Cash and cash equivalents were denominated in the following currencies:

	2011	2010
Russian rouble	164,695	108,516
US dollar	60,980	39,819
Euro	3,235	4,823
Romanian lei	1,205	4,035
Other currencies	478	331
	230,593	157,524

The above cash and cash equivalents consisted primarily of cash at banks.

As at December 31, 2011, the amount of cash and cash equivalents included 42,291 which is available to finance investing activities only (December 31, 2010: 55,780).

15) Trade and Other Receivables

Trade and other receivables consisted of the following:

	2011	2010
Trade receivables	758,343	710,714
Officers and employees	1,964	2,235
Other accounts receivable	37,630	21,884
Gross accounts receivable	797,937	734,833
Allowance for doubtful debts	(31,782)	(17,936)
Net accounts receivable	766,155	716,897

Accounts receivables in the amount of 103,851 were pledged as security for borrowings as at December 31, 2011 (December 31, 2010: 91,661) (Note 23).

16) Inventories

Inventories consisted of the following:

	2011	2010
Raw materials	389,140	335,362
Work in process	373,423	356,392
Finished goods and finished goods in transit	429,573	333,205
Goods for resale	17,254	4,084
Supplies	224,891	195,609
Gross inventories	1,434,281	1,224,652
Allowance for net realisable value of inventory	(15,826)	(17,112)
Net inventories	1,418,455	1,207,540

Inventories carried at net realisable value in the amount of 330,008 (December 31, 2010: 262,328) were included in inventories as at December 31, 2011.

As at December 31, 2011, certain items of inventory with a carrying amount of 121,365 (December 31, 2010: 122,794) were pledged as security for borrowings (Note 23).

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

16) Inventories (continued)

The following summarises the changes in the allowance for net realisable value of inventory:

	2011	2010
Balance at the beginning of the year	17,112	22,133
Decrease in allowance	(662)	(4,818)
Currency translation adjustments	(624)	(203)
Balance at the end of the year	15,826	17,112

17) Prepayments and Input VAT

Prepayments and input VAT consisted of the following:

	2011	2010
Prepayment for VAT, input VAT	111,459	92,304
Prepayment for services, inventories	51,435	45,778
Prepayment for insurance	3,708	9,887
Deferred charges	2,221	4,372
Prepayment for other taxes	931	1,551
Prepayment for property tax	698	179
Prepayment for rent	256	231
	170,708	154,302

Input VAT, representing amounts payable or paid to suppliers, is recoverable from the tax authorities via offset against VAT payable to the tax authorities on the Group's revenue or via direct cash receipts from the tax authorities. Management periodically reviews the recoverability of the balance of input VAT and believes it is recoverable within one year.

18) Property, Plant and Equipment

Movement in property, plant and equipment for the year ended December 31, 2011 was as follows:

	Land and buildings	Machinery and equipment	Transport and motor vehicles	Furniture and fixtures	Leasehold improve- ments	Construction in progress	TOTAL
<u>COST</u>							
Balance at January 1, 2011	1,248,487	2,536,920	60,317	47,585	9,911	554,106	4,457,326
Additions	–	–	–	–	–	325,998	325,998
Assets put into operation	71,153	272,618	3,784	10,820	3,051	(361,426)	–
Disposals	(3,977)	(15,739)	(1,723)	(662)	–	(376)	(22,477)
Currency translation adjustments	(64,078)	(129,406)	(2,925)	(2,865)	(102)	(22,899)	(222,275)
BALANCE							
AT DECEMBER 31, 2011	1,251,585	2,664,393	59,453	54,878	12,860	495,403	4,538,572
<u>ACCUMULATED DEPRECIATION AND IMPAIRMENT</u>							
Balance at January 1, 2011	(181,734)	(834,077)	(25,587)	(26,576)	(2,692)	–	(1,070,666)
Depreciation charge	(37,687)	(217,261)	(4,267)	(8,252)	(711)	–	(268,178)
Reversal of impairment	–	73,417	–	–	–	–	73,417
Disposals	2,048	10,755	1,645	619	–	–	15,067
Currency translation adjustments	11,210	45,007	1,417	1,779	23	–	59,436
BALANCE							
AT DECEMBER 31, 2011	(206,163)	(922,159)	(26,792)	(32,430)	(3,380)	–	(1,190,924)
NET BOOK VALUE							
AT DECEMBER 31, 2011	1,045,422	1,742,234	32,661	22,448	9,480	495,403	3,347,648
NET BOOK VALUE							
AT JANUARY 1, 2011	1,066,753	1,702,843	34,730	21,009	7,219	554,106	3,386,660

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

18) Property, Plant and Equipment (continued)

Movement in property, plant and equipment for the year ended December 31, 2010 was as follows:

	Land and buildings	Machinery and equipment	Transport and motor vehicles	Furniture and fixtures	Leasehold improve- ments	Construction in progress	TOTAL
<u>COST</u>							
Balance at January 1, 2010	1,243,839	2,370,728	59,571	40,466	9,439	567,204	4,291,247
Additions	–	–	–	–	–	270,301	270,301
Assets put into operation	32,374	232,626	4,263	8,172	485	(277,920)	–
Transfer to assets held for sale	(8,844)	(730)	(301)	(13)	–	(158)	(10,046)
Disposals	(1,779)	(33,227)	(1,289)	(576)	–	(707)	(37,578)
Currency translation adjustments	(17,103)	(32,477)	(1,927)	(464)	(13)	(4,614)	(56,598)
BALANCE							
AT DECEMBER 31, 2010	1,248,487	2,536,920	60,317	47,585	9,911	554,106	4,457,326
<u>ACCUMULATED DEPRECIATION AND IMPAIRMENT</u>							
Balance at January 1, 2010	(150,761)	(692,309)	(23,150)	(20,758)	(1,589)	–	(888,567)
Depreciation charge	(35,720)	(177,543)	(4,165)	(6,506)	(1,024)	–	(224,958)
Transfer to assets held for sale	1,486	527	59	3	–	–	2,075
Disposals	563	21,129	1,027	424	–	–	23,143
Currency translation adjustments	2,698	14,119	642	261	(79)	–	17,641
BALANCE							
AT DECEMBER 31, 2010	(181,734)	(834,077)	(25,587)	(26,576)	(2,692)	–	(1,070,666)
NET BOOK VALUE							
AT DECEMBER 31, 2010	1,066,753	1,702,843	34,730	21,009	7,219	554,106	3,386,660
NET BOOK VALUE							
AT JANUARY 1, 2010	1,093,078	1,678,419	36,421	19,708	7,850	567,204	3,402,680

As at December 31, 2011, bank borrowings were secured by properties and equipment with a carrying value of 391,897 (December 31, 2010: 746,307) (Note 23).

In 2011 and 2010, no impairment losses were recognised in respect of property, plant and equipment.

As at December 31, 2011, the Group determined that the value in use of European division cash-generating unit significantly exceeded its carrying value. The Group used pre-tax discount rate of 13.36% for the calculation of the value in use of this cash-generating unit. The increase of its recoverable amount was mostly due to the increase of the share of the most profitable products in total production and sales volume of European division cash-generating unit. As a result, the Group reversed the impairment loss recognised in 2008-2009 in respect of property, plant and equipment of European division cash-generating unit in the amount of 73,417.

Capitalised Borrowing Costs

The Group started to capitalise borrowing costs for all eligible assets where construction was commenced on or after January 1, 2009. The amount of borrowing costs capitalised during the year ended December 31, 2011 was 4,682 (2010: 4,488). The rate of the specific borrowing used to determine the amount of borrowing costs eligible for capitalisation was 5.19% in 2011 (2010: 5.19%).

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

19) Goodwill and Other Intangible Assets

Movement in intangible assets for the year ended December 31, 2011 was as follows:

	Patents and trademarks	Goodwill	Software	Customer relationships	Proprietary technology	Backlog	Other	TOTAL
COST								
Balance at January 1, 2011	209,578	567,681	16,972	472,300	14,100	8,500	7,265	1,296,396
Additions	11	–	6,850	–	–	–	1,861	8,722
Disposals	(4)	–	(861)	–	–	–	(2,537)	(3,402)
Currency translation adjustments	(44)	(4,858)	(1,419)	–	–	–	(315)	(6,636)
BALANCE AT DECEMBER 31, 2011	209,541	562,823	21,542	472,300	14,100	8,500	6,274	1,295,080
ACCUMULATED AMORTISATION AND IMPAIRMENT								
Balance at January 1, 2011	(231)	(13,328)	(11,963)	(226,389)	(4,499)	(8,500)	(2,342)	(267,252)
Amortisation charge	(81)	–	(2,309)	(63,685)	(1,762)	–	(1,397)	(69,234)
Impairment	–	(3,368)	–	–	–	–	–	(3,368)
Disposals	1	–	849	–	–	–	2,117	2,967
Currency translation adjustments	17	1,084	1,120	–	–	–	60	2,281
BALANCE AT DECEMBER 31, 2011	(294)	(15,612)	(12,303)	(290,074)	(6,261)	(8,500)	(1,562)	(334,606)
NET BOOK VALUE AT DECEMBER 31, 2011	209,247	547,211	9,239	182,226	7,839	–	4,712	960,474
NET BOOK VALUE AT JANUARY 1, 2011	209,347	554,353	5,009	245,911	9,601	–	4,923	1,029,144

Movement in intangible assets for the year ended December 31, 2010 was as follows:

	Patents and trademarks	Goodwill	Software	Customer relationships	Proprietary technology	Backlog	Other	TOTAL
COST								
Balance at January 1, 2010	209,740	568,891	17,049	472,300	14,100	8,500	5,708	1,296,288
Additions	28	–	75	–	–	–	1,907	2,010
Disposals	(181)	–	–	–	–	–	(304)	(485)
Currency translation adjustments	(9)	(1,210)	(152)	–	–	–	(46)	(1,417)
BALANCE AT DECEMBER 31, 2010	209,578	567,681	16,972	472,300	14,100	8,500	7,265	1,296,396
ACCUMULATED AMORTISATION AND IMPAIRMENT								
Balance at January 1, 2010	(217)	(13,429)	(8,930)	(147,092)	(2,737)	(8,500)	(1,562)	(182,467)
Amortisation charge	(82)	–	(3,118)	(79,297)	(1,762)	–	(940)	(85,199)
Disposals	61	–	–	–	–	–	143	204
Currency translation adjustments	7	101	85	–	–	–	17	210
BALANCE AT DECEMBER 31, 2010	(231)	(13,328)	(11,963)	(226,389)	(4,499)	(8,500)	(2,342)	(267,252)
NET BOOK VALUE AT DECEMBER 31, 2010	209,347	554,353	5,009	245,911	9,601	–	4,923	1,029,144
NET BOOK VALUE AT JANUARY 1, 2010	209,523	555,462	8,119	325,208	11,363	–	4,146	1,113,821

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

19) Goodwill and Other Intangible Assets (continued)

Customer relationships represent non-contracted interactions with clients. Remaining amortisation period for customer relationships is 5-7 years. Customer relationships are amortised using the diminishing balance method which reflects the pattern of consumption of the economic benefits that customer relationships provide.

Goodwill relates to the assembled workforce and synergy from integration of the acquired subsidiaries into the Group.

Patents and trademarks include intangible assets with indefinite useful lives with the carrying value of 208,700 (2010: 208,700).

The carrying amount of goodwill and intangible assets with indefinite useful lives were allocated among cash-generating units as follows as at December 31:

	2011		2010	
	Goodwill	Intangible assets with indefinite useful lives	Goodwill	Intangible assets with indefinite useful lives
American division	472,968	208,700	472,968	208,700
European division	6,185	–	6,324	–
Kaztrubprom Plant	4,863	–	8,301	–
Oilfield division	29,957	–	31,648	–
Other cash-generating units	33,238	–	35,112	–
	547,211	208,700	554,353	208,700

The Group determines whether goodwill and intangible assets with indefinite useful lives are impaired on an annual basis and when circumstances indicate the carrying value may be impaired.

As at June 30, 2011, there were indicators of impairment of Kaztrubprom Plant cash-generating unit, therefore, the Group performed an impairment test at that date in respect of this unit. As a result of that test, the Group determined that the carrying value of Kaztrubprom Plant cash-generating unit exceeds its recoverable amount. Consequently, the Group recognised impairment of Kaztrubprom Plant cash-generating unit's goodwill in the amount of 3,368.

Goodwill and intangible assets with indefinite useful lives were tested for impairment at December 31, 2011. As a result of the test, the Group determined that the carrying values of all cash-generating units do not exceed their recoverable amounts. Consequently, no additional impairment losses were recognised in the year ended December 31, 2011. In 2010, no impairment losses were recognised in respect of goodwill and intangible assets with indefinite useful lives.

For the purpose of impairment testing of goodwill the Group has determined value in use of each of its cash-generating units. The value in use has been calculated using cash flow projections based on the actual operating results and business plans approved by management and appropriate discount rates reflecting time value of money and risks associated with respective cash-generating unit or group of cash-generating units. The key assumptions used by management in calculation of the value in use are presented in the table below. For the periods not covered by management plans, cash flow projections have been estimated by extrapolating the respective business plans taking into account business cycles using zero growth rate.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

19) Goodwill and Other Intangible Assets (continued)

Cash-generating units	Period of forecast, years	Pre-tax discount rate, %
American division	5	12.01
European division	5	13.36
Kaztrubprom Plant	5	11.59
Oilfield division	5	12.48
Other cash-generating units	5	11.92

With regard to the assessment of value in use of European division no reasonably possible change in the key assumptions would cause the carrying value of this unit to exceed its recoverable amount.

The recoverable amounts of American division, Kaztrubprom Plant, Oilfield division and Taganrog Metallurgical Works (which is included in other cash-generating units) are based on the business plans approved by management. The reasonably possible deviation of assumptions from these plans could lead to an impairment. The calculation of value in use of these cash-generating units was the most sensitive to the following assumptions:

Discount Rates

Discount rates reflect the current market assessment of the risks specific to cash generating unit. The discount rates have been determined using the CAPM concept and analysis of industry peers. Reasonably possible change in discount rate could lead to impairment of goodwill.

A 10% increase in the discount rate of Oilfield division would result in an impairment of goodwill in the amount of 987.

Costs

If costs of American division were 5% higher than those assumed in the impairment test during the period of forecast, this would lead to the full impairment of goodwill in the amount of 472,968.

If costs of Kaztrubprom Plant were 5% higher than those assumed in the impairment test during the period of forecast, this would lead to an impairment of goodwill in the amount of 4,469.

If costs of Oilfield division were 5% higher than those assumed in the impairment test during the period of forecast, this would lead to the full impairment of goodwill in the amount of 29,957.

If costs of Taganrog Metallurgical Works were 5% higher than those assumed in the impairment test during the period of forecast, this would lead to the full impairment of goodwill in the amount of 31,103.

Commodity Prices

If prices of American division forecasted for 2012 were 5% lower than those assumed in the impairment test, this would lead to the full impairment of goodwill in the amount of 472,968.

If prices of Kaztrubprom Plant forecasted for 2012 were 5% lower than those assumed in the impairment test, this would lead to the full impairment of goodwill in the amount of 4,863.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

19) Goodwill and Other Intangible Assets (continued)

If prices of Oilfield division forecasted for 2012 were 5% lower than those assumed in the impairment test, this would lead to the full impairment of goodwill in the amount of 29,957.

If prices of Taganrog Metallurgical Works forecasted for 2012 were 5% lower than those assumed in the impairment test, this would lead to the full impairment of goodwill in the amount of 31,103.

20) Other Non-Current Assets

Other non-current assets consisted of the following:

	2011	2010
Prepayments for acquisition of property, plant and equipment	80,389	29,774
Restricted cash deposits for fulfillment of guaranties	7,850	1,659
Loans to employees	5,840	5,357
Other	5,379	3,918
	99,458	40,708
Allowance for doubtful debts	–	(11)
	99,458	40,697

21) Trade and Other Payables

Trade and other payables consisted of the following:

	2011	2010
Trade payables	653,100	531,888
Liabilities for VAT	55,103	28,120
Accounts payable for property, plant and equipment	42,282	65,410
Payroll liabilities	30,348	29,942
Accrued and withheld taxes on payroll	16,204	14,368
Liabilities under put options of non-controlling interest shareholders in subsidiaries	14,051	14,934
Liabilities for property tax	13,399	10,281
Notes issued to third parties	8,408	7,226
Sales rebate payable	7,926	7,134
Liabilities for other taxes	3,442	4,500
Other payables	18,677	18,930
	862,940	732,733

22) Provisions and Accruals

Provisions and accruals consisted of the following:

	2011	2010
Current:		
Provision for bonuses	21,488	20,710
Accrual for unused annual leaves, current portion	10,549	9,546
Accrual for long-service benefit	10,209	8,468
Current portion of post-employment benefits	2,693	1,850
Provision for tax and other fines	204	241
Environmental provision, current portion	932	1,338
	46,075	42,153
Non-current:		
Accrual for unused annual leaves	20,930	19,379
Environmental provision	4,406	4,717
	25,336	24,096

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

23) Interest-Bearing Loans and Borrowings

Interest-bearing loans and borrowings consisted of the following:

	2011	2010
<i>Current:</i>		
Bank loans	242,830	201,585
Interest payable	27,981	26,473
Current portion of non-current borrowings	329,009	125,104
Current portion of bearer coupon debt securities	–	350,759
Unamortised debt issue costs	(2,269)	(3,648)
	597,551	700,273
Finance lease liability - current	1,826	1,591
Total short-term loans and borrowings	599,377	701,864
<i>Non-current:</i>		
Bank loans	2,459,613	2,733,457
Bearer coupon debt securities	1,043,806	897,034
Unamortised debt issue costs	(21,136)	(20,048)
Less: current portion of non-current borrowings	(329,009)	(125,104)
Less: current portion of bearer coupon debt securities	–	(350,759)
	3,153,274	3,134,580
Finance lease liability - non-current	34,290	35,134
Total long-term loans and borrowings	3,187,564	3,169,714

As at December 31, 2010, the Group pledged its rights under sales contracts in Romania totaling to 9,444 as collateral under loan agreements in addition to collaterals disclosed in Notes 15, 16, 18. There were no such pledges as at December 31, 2011.

The carrying amounts of the Group's borrowings are denominated in the following currencies:

	Interest rates for the year	2011	Interest rates for the year	2010
Russian rouble	Fixed 6.7% - 9.5%	1,712,829	Fixed 4.3% - 10%	1,640,713
	Fixed 5.25%	385,981	Fixed 10%	193,129
	Fixed 7.75%	512,935	Fixed 5.25%	377,910
US Dollar	Fixed 3.15% - 7%	447,541	Fixed 2.6% - 8.5%	1,244,629
	Cost of funds + 1.75% - 2.5% (*)	5,424		
	Variable:	440,304	Variable:	112,546
	Libor (1m) + 2.25% - 4.15%		Libor (1m) + 1.75% - 5.65%	
	Libor (3m - 13m) + 1% - 2.75%		Libor (1w) + 2.39%	
	Fixed 5.19%	74,510	Fixed 5.19%	84,420
	Variable:	170,953	Variable:	179,248
Euro	Euribor (1m) + 1.6% - 4.05%		Euribor (1m) + 1.6%	
	Euribor (3m) + 2.7% - 3.5%		Euribor (3m) + 2.7% - 4%	
	Euribor (6m) + 0.26% - 0.3%		Euribor (5m) + 1.1%	
	Euribor (10m - 15m) + 1.1%		Euribor (6m) + 0.26% - 1.1%	
			Euribor (8m) + 1.1%	
			Euribor (12m) + 1.2%	
Romanian Lei	Robor (6m) + 3%	348	Fixed 10.5% - 11%	2,253
Swiss Frank		–	Variable:	5
			Libor (1w) + 2.39%	
		3,750,825		3,834,853

(*) Cost of funds represents internal rate of a bank.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

23) Interest-Bearing Loans and Borrowings (continued)

Loan Participation Notes

On January 27, 2011, TMK Capital S.A., a Luxemburg special purpose entity, completed the offering of loan participation notes due 2018 in the total amount of 500,000 with a coupon of 7.75% per annum, payable on semi-annual basis. The notes are admitted for trading on the London Stock Exchange. As at December 31, 2011, an aggregate of 500,000 of notes remained outstanding.

On July 29, 2011, the Group fully repaid 10% loan participation notes in the amount of 186,700 issued in 2008 by TMK Capital S.A.

Bank Loans

In January 2011, the Group partially repaid 1,107,542 Gazprombank loan facilities using the proceeds from issuance of 7.75% loan participation notes in the amount of 500,000. In October 2011, the Group refinanced a further part of Gazprombank loan facilities in the amount of 207,542 using proceeds from Nordea Bank loan and cash generated from operations. As at December 31, 2011, the principle outstanding balance of the loan facilities in Gazprombank was 400,000.

In February-April 2011, the Group entered into several loan agreements with Gazprombank with a maturity in 2014. The proceeds from these loans were used to repay loans from Sberbank in the aggregated amount of 4,000,000 thousand Russian roubles (135,206 at the exchange rates as at the payment dates), a loan from VTB in the amount of 94,000 and for settlement of liability under 5,000,000 thousand Russian roubles bonds issued on February 21, 2006 (170,892 at the exchange rate as at the payment date). As at December 31, 2011, the aggregated principle outstanding balance of these loans in Gazprombank was 11,400,490 thousand Russian roubles (354,096 at the exchange rate as at December 31, 2011).

In April 2011, the Group refinanced Sberbank loans in the aggregated amount of 7,118,490 thousand Russian roubles (250,273 at the exchange rates as at the payment dates) with new Sberbank loans in the aggregated amount of 6,900,000 thousand Russian roubles (244,477 at the exchange rates as at the cash proceeds dates). As at December 31, 2011, the aggregated principle outstanding balance of these loans in Sberbank was 6,900,000 thousand Russian roubles (214,312 at the exchange rate as at December 31, 2011).

In July 2011, the Group entered into loan agreement with Gazprombank in the amount of 150,000 with a maturity in 2012. The proceeds from this loan were used for partial repayment of 10% loan participation notes in the amount of 186,700 issued by TMK Capital S.A. As at December 31, 2011, the principle outstanding balance of this loan in Gazprombank was 36,660.

In August 2011, the Group entered into syndicated credit facility with Wells Fargo Capital Finance, LLC, Bank of America, N.A., GE Capital Finance Inc., JPMorgan Chase Bank, N.A. and ING Capital LLC with a maturity in 2016. The proceeds from this credit facility were partially used to refinance 96,706 of the Wells Fargo senior secured credit facility. As at December 31, 2011, the aggregated principle outstanding balance under the facility was 146,168.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

23) Interest-Bearing Loans and Borrowings (continued)

Bank Loans (continued)

In October 2011, the Group entered into loan with Nordea Bank in the amount of 200,000 with a maturity in 2017. The proceeds from this loan were used for partial repayment of Gazprombank loan facilities. As at December 31, 2011, the principle outstanding balance of Nordea Bank loan was 200,000.

Russian Bond Obligations

On February 15, 2011, the Group fully repaid its liability under 5,000,000 thousand Russian roubles bonds issued on February 21, 2006 (170,892 at the exchange rate as at the payment date) using the proceeds from the loan provided by Gazprombank.

Unamortised Debt Issue Costs

Unamortised debt issue costs represent agent commission and arrangement costs paid by the Group in relation to the arrangement of loans and issue of notes.

As at December 31, 2011, the Group had unutilised borrowing facilities in the amount of 736,163 (December 31, 2010: 588,281).

Finance Lease Liabilities

Starting from 2001, the Group entered into lease agreements under certain of which it has a bargain option to acquire the leased assets at the end of lease term ranging from 3 to 20 years. The estimated average remaining useful life of leased assets varies from 8 to 17 years.

The leases are accounted for as finance leases in the consolidated financial statements. The carrying value of the leased assets was as follows as at December 31:

	2011	2010
Machinery and equipment	26,030	28,372
Transport and motor vehicles	609	183
	26,639	28,555

The leased assets are included in property, plant and equipment in the consolidated statement of financial position.

Future minimum lease payments under finance leases with the present value of the net minimum lease payments were as follows as at December 31, 2011:

	Minimum payments	Present value of payments
2012	3,011	1,826
2013-2016	11,563	7,500
after 2016	32,456	26,790
Total minimum lease payments	47,030	36,116
Less amounts representing finance charges	(10,914)	
Present value of minimum lease payments	36,116	36,116

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

23) Interest-Bearing Loans and Borrowings (continued)

Finance Lease Liabilities (continued)

Future minimum lease payments under finance leases with the present value of the net minimum lease payments were as follows as at December 31, 2010:

	Minimum payments	Present value of payments
2011	2,779	1,591
2012-2015	10,779	6,571
after 2015	35,142	28,563
Total minimum lease payments	48,700	36,725
Less amounts representing finance charges	(11,975)	
Present value of minimum lease payments	36,725	36,725

In the years ended December 31, 2011 and December 31, 2010, the average interest rate under the finance lease liabilities was 3%.

24) Convertible Bonds

On February 11, 2010, TMK Bonds S.A., the Group's special purpose entity, completed the offering of 4,125 convertible bonds due 2015 convertible into Global Depository Receipts ("GDR") each representing four ordinary shares of OAO TMK. The bonds are listed on the London Stock Exchange. The bonds have nominal value of 100,000 US dollars each and were issued at 100% of their principal amount. The convertible bonds carry a coupon of 5.25% per annum, payable on a quarterly basis. The conversion can be exercised at the option of bondholders on any date during the period commencing 41 days following the February 11, 2010 and ending on the date falling seven London business days prior to the maturity date or, if earlier, ending on the seventh day prior to any earlier date fixed for redemption of the Convertible bonds. As at December 31, 2011, the bonds are convertible into GDRs at conversion price of 22.927 US dollars per GDR (December 31, 2010: 23.075 US dollars per GDR). The conversion price was adjusted in 2011 as a result of dividends in respect of 2010 distributed by the parent entity.

The Group can early redeem all outstanding bonds, in whole but not in part, at any time on or after March 4, 2013 at their principal amount plus accrued interest, if the volume weighted average price of the GDRs traded on the London Stock Exchange during 30 consecutive dealing days exceeds 130 per cent of the conversion price (the "Issuer Call"). In addition, the Group has the option to redeem the bonds at the principal amount plus accrued interest if 15% or less of the bonds remain outstanding. Bondholders have the right to request redemption of the bonds on the third anniversary following the issue date at the principal amount plus accrued interest.

The Group determined that the convertible bonds represent a combined financial instrument containing two components: the bond liability (host component) and an embedded derivative representing conversion option in foreign currency combined with the Issuer Call (the "Embedded Conversion Option").

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

24) Convertible Bonds (continued)

The Embedded Conversion Option in foreign currency was classified as financial instrument at fair value through profit or loss. The Embedded Conversion Option was initially recognised at the fair value of 35,455. The Group used binomial options pricing model for initial and subsequent measurement of fair value of this embedded derivative. For the purposes of this model, the Group assessed that the credit spread comprised 1,094 bps and 650 bps as at December 31, 2011 and 2010, respectively. As at December 31, 2011, the fair value of the Embedded Conversion Option was 3,024 (December 31, 2010: 47,816). The change in the fair value of the embedded derivative during the year ended December 31, 2011 resulted in a gain of 44,792 (2010: loss of 12,361), which has been recorded as gain/(loss) on changes in fair value of derivative financial instrument in the income statement.

The fair value of the host component of 368,149 at the initial recognition date has been determined as a residual amount after deducting the fair value of the Embedded Conversion Option from the issue price of the convertible bonds of 412,500 adjusted for transaction costs of 8,896. The host component is subsequently carried at the amortised cost using the effective interest method. As at December 31, 2011, the carrying value of the host component was 385,981 (December 31, 2010: 377,910).

There were no conversions of the bonds during the year ended December 31, 2011.

25) Post-Employment Benefits

The Group companies provide additional pensions and other post-employment benefits to their employees in accordance with collective bargaining agreements. Defined benefits consist of lump-sum amounts payable at the retirement date and certain regular post-retirement payments. These benefits generally depend on years of service, level of compensation and amount of pension payment under the collective bargaining agreement. The Group pays the benefits when they fall due for payment.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

25) Post-Employment Benefits (continued)

The following table summarises the components of net benefit expense recognised in the consolidated income statement and amounts recognised in the consolidated statement of financial position by country:

	Russia		Romania		USA		Total	
	2011	2010	2011	2010	2011	2010	2011	2010
<i>Movement in the benefit liability:</i>								
At January 1	52,855	48,242	1,651	1,342	956	–	55,462	49,584
Benefit expense	3,371	6,136	(47)	595	707	458	4,031	7,189
Benefit paid	(1,768)	(1,363)	(83)	(157)	(142)	–	(1,993)	(1,520)
Other	–	–	–	–	–	498	–	498
Currency translation adjustment	(2,962)	(160)	(9)	(129)	–	–	(2,971)	(289)
At December 31	51,496	52,855	1,512	1,651	1,521	956	54,529	55,462
Short-term	2,596	1,772	97	78	–	–	2,693	1,850
Long-term	48,900	51,083	1,415	1,573	1,521	956	51,836	53,612
<i>Net benefit expense (recognised in cost of sales, general and administrative expenses and selling and distribution expenses):</i>								
Current service cost	1,065	796	88	65	380	290	1,533	1,151
Interest cost on benefit obligation	2,092	1,807	150	121	55	30	2,297	1,958
Net actuarial (gain)/loss recognised in the period	(484)	3,363	(263)	202	272	138	(475)	3,703
Past service cost	698	170	(22)	207	–	–	676	377
Net benefit expense/(income)	3,371	6,136	(47)	595	707	458	4,031	7,189

The Group expects to contribute 2,693 to its defined post-employment benefit programme in 2012.

	2011	2010
Present value of defined benefit obligation	56,455	57,655
Unrecognised past service cost	(1,926)	(2,193)
Benefit liability as at December 31	54,529	55,462

The Group had no plan assets and unrecognised actuarial gains or losses in the year ended December 31, 2011.

The following table is a summary of the present value of the benefit obligation and experience adjustments as at December 31:

	2011	2010
Defined benefit obligation as at December 31	56,455	57,655
Experience adjustments on plan liabilities	325	4,120

The principal actuarial assumptions used in determining pension obligations for the Group's plan are shown below:

	Russia		Romania		USA	
	2011	2010	2011	2010	2011	2010
Discount rate	8.31%	7.96%	current 9.21%, decreasing to 4.38% in the long-term	current 8.74%, decreasing to 4.29% in the long-term	4.85%	5.75%
Average long-term rate of compensation increase	6.7%	6.3%	current 3.14%, changing to 3.5% in the long-term	current 5.5%, decreasing to 3.5% in the long-term	3.5%	3.5%

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

26) Principal Subsidiaries

Company	Location	Main activity	Actual ownership interest	Effective ownership interest	Actual ownership interest	Effective ownership interest
			December 31, 2011	December 31, 2011	December 31, 2010	December 31, 2010
OAO "Seversky Tube Works"	Russia	Manufacturing of seamless and welded steel pipes, steel billets	94.63%	94.63%	94.37%	94.37%
OAO "Sinarsky Pipe Plant"	Russia	Manufacturing of seamless steel pipes	94.40%	94.40%	94.27%	94.27%
OAO "Taganrog Metallurgical Works"	Russia	Manufacturing of seamless and welded steel pipes, steel billets	96.13%	96.13%	96.10%	96.10%
OAO "Volzhsky Pipe Plant"	Russia	Manufacturing of seamless and welded steel pipes, steel billets	100.00%	100.00%	100.00%	100.00%
OAO "Orsky Machine Building Plant"	Russia	Manufacturing of joints for drill pipes and other products	75.00%	75.00%	75.00%	75.00%
OOO "TMK-INOX" *	Russia	Manufacturing and sales of steel pipes	51.00%	48.15%	53.00%	49.97%
ZAO "TMK-CPW" *	Russia	Manufacturing of welded steel pipes	51.00%	48.26%	51.00%	48.13%
TOO "TMK-Kaztrubprom"	Kazakhstan	Manufacturing of seamless steel pipes	100.00%	100.00%	100.00%	100.00%
IPSCO Tubulars Inc.	USA	Manufacturing of welded steel pipes	100.00%	100.00%	100.00%	100.00%
IPSCO Koppel Tubulars, L.L.C.	USA	Manufacturing of seamless steel pipes	100.00%	100.00%	100.00%	100.00%
IPSCO Tubulars (KY) Inc.	USA	Manufacturing of welded steel pipes	100.00%	100.00%	100.00%	100.00%
IPSCO Tubulars (OK) Inc.	USA	Manufacturing of seamless and welded steel pipes	100.00%	100.00%	100.00%	100.00%
Ultra Premium Oilfield Services, Ltd	USA	Manufacturing of premium pipes connections, services for oil and gas industries	100.00%	100.00%	100.00%	100.00%
S.C. TMK-ARTROM S.A.	Romania	Manufacturing of seamless steel pipes	92.66%	92.66%	92.66%	92.66%
S.C. TMK-RESITA S.A.	Romania	Manufacturing of steel billets	100.00%	100.00%	100.00%	100.00%
OOO "TMK-Premium Services"	Russia	Promotion and development of premium connections	100.00%	100.00%	100.00%	100.00%
ZAO "Trade House TMK"	Russia	Sales & distribution of pipes, raw materials procurement	100.00%	100.00%	100.00%	100.00%
OOO "Skladskoy Kompleks TMK"	Russia	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TOO "TMK-Kazakhstan"	Kazakhstan	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TMK Global S.A.	Switzerland	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TMK Europe GmbH	Germany	Sales & distribution of pipes, raw materials and equipment procurement	100.00%	100.00%	100.00%	100.00%
TMK Italia s.r.l.	Italy	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TMK Middle East FZCO	UAE	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TMK North America Inc.	USA	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TMK IPSCO INTERNATIONAL, L.L.C.	USA	Sales & distribution of pipes	100.00%	100.00%	0.00%	0.00%
TMK IPSCO Canada, Ltd.	Canada	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
TMK Africa Tubulars (PTY) Ltd.	South Africa	Sales & distribution of pipes	100.00%	100.00%	100.00%	100.00%
OOO "Predpriyatiye "Truboplast"	Russia	Coating of pipes	100.00%	100.00%	100.00%	100.00%
ZAO "Pipe Repair Department"	Russia	Services for oil and gas industries	100.00%	100.00%	100.00%	100.00%
OOO "Central Pipe Yard"	Russia	Services for oil and gas industries	100.00%	100.00%	100.00%	100.00%
OAO "Russian Research Institute of the Tube and Pipe Industries"	Russia	In-house R&D facility	97.36%	97.36%	97.36%	97.36%
OAO "Sinarskaya heat and power plant"	Russia	Heat and electrical energy production	68.79%	64.93%	68.79%	64.85%
TMK HYDROENERGY POWER S.R.L.	Romania	Electrical energy production	0.00%	0.00%	100.00%	100.00%
OOO "TMK Metallurgical Service"	Russia	Maintenance and repair of equipment	0.00%	0.00%	100.00%	94.37%
TMK NSG, L.L.C. (former NS Group, Inc.)	USA	Holding company of US assets	100.00%	100.00%	100.00%	100.00%
UPOS GP, L.L.C.	USA	Holding company of US assets	100.00%	100.00%	100.00%	100.00%
UPOS, L.L.C.	USA	Holding company of US assets	100.00%	100.00%	100.00%	100.00%
Blytheville Finance Corporation	USA	Financial investments	100.00%	100.00%	100.00%	100.00%
Rockarrow Investments Ltd.	Cyprus	Stock servicing	100.00%	100.00%	100.00%	100.00%
TMK Capital S.A.	Luxembourg	Financing (SPV)	0.00%	0.00%	0.00%	0.00%
TMK Bonds S.A.	Luxembourg	Financing (SPV)	0.00%	0.00%	0.00%	0.00%
OOO "Pokrovka 40"	Russia	Assets holding	100.00%	100.00%	100.00%	100.00%
OOO "TMK Oilfield Services"	Russia	Management services	100.00%	100.00%	100.00%	100.00%
OOO "Accounting services center"	Russia	Accounting shared-services	100.00%	100.00%	100.00%	100.00%
OOO "Blagoustroystvo"	Russia	Services	100.00%	100.00%	100.00%	100.00%
OOO "SinaraTransAvto"	Russia	Services	100.00%	94.40%	100.00%	94.27%
OOO "TMK-Trans"	Russia	Logistics	100.00%	100.00%	100.00%	100.00%

* The Group recorded a liability under put option in the consolidated financial statements

Actual ownership interest in subsidiaries differs from the effective ownership interests due to the existence of non-controlling interests in subsidiaries that hold ownership interest in other subsidiaries.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

27) Related Parties Disclosures

For the purposes of the financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions or had significant balances outstanding as at December 31, 2011 and 2010 are detailed below.

Transactions with the Parent Company and Entities with Significant Influence

As at December 31, 2010, the Group had a liability of 5,300 in respect of the guarantee provided by Bravecorp Limited (an entity under common control with the parent company, TMK Steel Limited). During the year ended December 31, 2011, the Group settled a liability in full amount.

In June 2011, the Group approved the distribution of final dividends in respect of 2010 year, from which 555,274 thousand Russian roubles (19,588 at the exchange rate at the date of approval) related to TMK Steel Limited, Bravecorp Limited and Tirelli Holdings Limited (entities under common control with TMK Steel Limited).

In November 2011, the Group approved the distribution of interim dividends in respect of six months 2011, from which 607,536 thousand Russian roubles (19,697 at the exchange rate at the date of approval) related to TMK Steel Limited, Bravecorp Limited and Tirelli Holdings Limited.

The Group paid final dividends in respect of 2010 year and interim dividends in respect of six months 2011 to TMK Steel Limited, Bravecorp Limited and Tirelli Holdings Limited in full amount as at December 31, 2011.

Transactions with Associates

During the year ended December 31, 2011, the Group rendered services to its associates and received services from its associates in the amounts of 415 and 532, respectively (2010: nil).

Compensation to Key Management Personnel of the Group

Key management personnel comprise members of the Board of Directors, the Management Board and certain executives of the Group, totaling 29 persons as at December 31, 2011 (28 persons as at December 31, 2010).

The Group provides compensation to key management personnel only in the form of short-term employee benefits, which include:

- Wages, salaries, social security contributions and other benefits in the amount of 15,211 for the year ended December 31, 2011 (2010: 9,136);
- Provision for performance bonuses which are dependent on operating results for 2011 year in the amount of 4,335 for the year ended December 31, 2011 (2010: 3,086).

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

27) Related Parties Disclosures (continued)

Compensation to Key Management Personnel of the Group (continued)

The amounts disclosed above are recognised as general and administrative expenses in the income statement during the reporting period.

In the years ended December 31, 2011 and 2010, the Group did not provide compensation to key management personnel in the form of post-employment benefits, other long-term benefits, share-based payment or termination benefits.

The balance of loans issued to key management personnel amounted to 1,103 as at December 31, 2011 (December 31, 2010: 396).

The Group guaranteed debts of key management personnel outstanding as at December 31, 2011 in the amount of 2,574 with maturity in 2014 – 2017 (December 31, 2010: 3,368).

In 2010, the Group paid 2,494 to the member of key management personnel for the guarantee issued.

Transactions with Other Related Parties

The following table provides balances with other related parties as at December 31:

	2011	2010
Cash and cash equivalents	125,687	47,151
Accounts receivable	5,417	3,305
Prepayments	109	90
Accounts payable	(733)	(2,157)
Interest payable	–	(977)

The following table provides the total amount of transactions with other related parties for the year ended December 31:

	2011	2010
Sales revenue	12,440	4,718
Purchases of goods and services	8,700	7,576
Interest income from loans and borrowings	614	521
Interest expenses from loans and borrowings	235	460

In the year ended December 31, 2011, sales transactions with related parties constituted approximately 0.18% of the total Group's sales (2010: 0.08%).

Notes to the Consolidated Financial Statements (continued)

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28) Contingencies and Commitments

Operating Environment of the Group

Significant part of the Group's principal assets are located in the Russian Federation and USA, therefore its significant operating risks are related to the activities of the Group in these countries.

In the wake of the global financial crisis, all countries continue to face an uneven economic recovery. Despite the stabilisation measures introduced by the Russian Government in 2011 there continues to be uncertainty regarding further economic growth which could negatively affect the Group's future financial position, results of operations and business prospects.

The US economy is recovering slower than expected, and the economic growth slowed-down starting the second quarter of 2011. An uncertainty over the US economic growth could have a negative impact on the Group's future financial position, results of operations and business prospects.

While management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Group's results and financial position in a manner not currently determinable.

Taxation

Tax, currency and customs legislation is subject to varying interpretations and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Management believes that it has paid or accrued all taxes that are applicable. Where uncertainty exists, the Group has accrued tax liabilities based on management's best estimate of the probable outflow of resources embodying economic benefits, which will be required to settle these liabilities.

Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. It is not practical to determine the amount of unasserted claims that may manifest, if any, or the likelihood of any unfavourable outcome. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Up to the date of authorisation of these consolidated financial statements for issuance, the court proceedings had not been finalised for the claims in the amount of 36,807 thousand Russian roubles (1,143 at the exchange rate as at December 31, 2011). Management believes that the Group's position is justified and it is not probable that the ultimate outcome of these matters will result in additional losses for the Group. Consequently, the amounts of tax claims being contested by the Group were not accrued in the consolidated financial statements for the year ended December 31, 2011.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

28) Contingencies and Commitments (continued)

Contractual Commitments and Guarantees

As at December 31, 2011, the Group had contractual commitments for the acquisition of property, plant and equipment from third parties for 3,884,084 thousand Russian roubles (120,638 at the exchange rate as at December 31, 2011), 35,551 thousand Euros (46,014 at the exchange rate as at December 31, 2011), 489 thousand Romanian lei (147 at the exchange rate as at December 31, 2011) and 26,155 thousand US dollars for the total amount of 192,954 (all amounts of contractual commitments are expressed net of VAT). The Group had paid advances of 80,389 with respect to such commitments (2010: 29,774).

Under contractual commitments disclosed above, the Group opened unsecured letters of credit in the amount of 8,739 (2010: 8,330).

Insurance Policies

The Group currently maintains insurance against losses that may arise in case of property damage, accidents, transportation of goods. The Group also maintains corporate product liability and directors and officers liability insurance policies. Nevertheless, any recoveries under maintained insurance coverage that may be obtained in the future may not offset the lost revenues or increased costs resulting from a disruption of operations.

Legal Claims

During the period, the Group was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. Management believes there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Company.

Guarantees of Debts of Others

The Group guaranteed debts of others outstanding as at December 31, 2011 in the amount of 3,378 (December 31, 2010: 4,664).

29) Equity

i) Share Capital

	2011	2010
Number of shares		
<i>Authorised, issued and fully paid</i>		
<i>Ordinary shares of 10 Russian roubles each</i>		
As at January 1	937,586,094	873,001,000
Share capital increase	–	64,585,094
As at December 31	937,586,094	937,586,094

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

29) Equity (continued)

i) Share Capital (continued)

On February 5, 2010, the Board of Directors authorised an increase of share capital.

In June 2010, the Group received 8,589,818 thousand Russian roubles (279,427 at the historical exchange rate) as consideration from shareholders for the issuance of 64,585,094 shares with par value of 10 Russian roubles each at price of 133 Russian roubles per share.

On November 30, 2010, the Group finalised the increase of share capital by 64,585,094 shares with par value of 10 Russian roubles each by means of an open subscription at price of 133 Russian roubles per share. Number of shares subscribed represented approximately 7.4% of the Company's issued and fully paid share capital before additional issue. After completion of the share capital increase, the total number of the issued and fully paid shares was 937,586,094.

ii) Reserve Capital

According to Russian Law, the Company must create a reserve capital in the amount of 5% of the share capital per the Russian statutory accounts by annual appropriations that should be at least 5% of the annual net profit per the statutory financial statements. The reserve capital can be used only for covering losses and for the redemption of the Company's bonds and purchase of its own shares if there are no other sources of financing.

In 2011 the Company reported net profit in Russian statutory accounts (net loss in 2010) and subsequently increased reserve capital by 32,292 Russian roubles (1,003 at the exchange rate as at December 31, 2011) to the amount of 5% of the share capital per the Russian statutory accounts.

iii) Dividends Declared by the Parent Entity to its Shareholders

On June 28, 2011, the annual shareholder meeting approved final dividends in respect of 2010 year in the amount of 796,948 thousand Russian roubles (28,113 at the exchange rate at the date of approval) or 0.85 Russian roubles per share (0.03 US dollars per share), from which 60,839 thousand Russian roubles (2,146 at the exchange rate at the date of approval) related to the treasury shares in possession of the Group.

On November 7, 2011, the extraordinary shareholders' meeting approved interim dividends in respect of six months 2011 in the amount of 871,955 thousand Russian roubles (28,270 at the exchange rate at the date of approval) or 0.93 Russian roubles per share (0.03 US dollars per share), from which 69,211 thousand Russian roubles (2,244 at the exchange rate at the date of approval) related to the treasury shares in possession of the Group.

In accordance with Russian legislation, dividends may only be declared to the shareholders from accumulated undistributed and unreserved earnings as shown in the Company's Russian statutory financial statements. The Company had 246,033 of undistributed and unreserved earnings recognised in Russian statutory financial statements as at December 31, 2011. In addition, the Group's share in the undistributed and unreserved earnings of its subsidiaries was 1,322,904 as at December 31, 2011.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

29) Equity (continued)

iv) Acquisition of Non-controlling Interests in Subsidiaries

In the year ended December 31, 2011, the Company purchased additional 0.26% of OAO "Seversky Tube Works" shares, 0.13% of OAO "Sinarsky Pipe Plant" shares, 0.03% of OAO "Taganrog Metallurgical Works" shares. The total cash consideration for the shares amounted to 1,374.

The excess in the amount of 14 of the consideration given for the shares over the carrying values of net assets attributable to interest in OAO "Taganrog Metallurgical Works" was charged to accumulated profit. The excess in the amount of 439 of the carrying values of net assets attributable to interest in OAO "Seversky Tube Works" and OAO "Sinarsky Pipe Plant" over the consideration paid for such non-controlling interest is recorded in additional paid-in capital.

In the year ended December 31, 2010, the Company purchased additional 0.15% of OAO "Seversky Tube Works" shares, 0.11% of OAO "Sinarsky Pipe Plant" shares, 0.04% of OAO "Taganrog Metallurgical Works" shares and 49% ownership interest in OOO "TMK Metallurgical Service". The total cash consideration for the shares amounted to 1,254.

The excess in the amount of 144 of the consideration given for the shares over the carrying values of net assets attributable to interest in OAO "Seversky Tube Works", OAO "Sinarsky Pipe Plant" and OAO "Taganrog Metallurgical Works" was charged to accumulated profit. The excess in the amount of 478 of the carrying values of net assets attributable to interest in OAO "Seversky Tube Works" over the consideration paid for such non-controlling interest is recorded in additional paid-in capital.

v) Sale of Non-controlling Interests

In December 2010, the Group increased share capital of OOO "TMK-INOX". The share capital increase was partially financed by the non-controlling interest shareholder. Cash consideration received from the non-controlling interest shareholder amounted to 1,000 million Russian roubles (32,939 at historical exchange rate). As a result of the transaction, the ownership interest of the Group in OOO "TMK-INOX" decreased and amounted to 53.00%. The difference between the consideration received and the carrying values of net assets attributable to non-controlling interest in the amount of 741 was charged to accumulated profit. As non-controlling interest shareholder has a right to sell its ownership interest to the Group under certain circumstances beyond the Group's control starting 2018, the Group recognised the amount of 20,015 at the exchange rate as at December 31, 2010 as a liability to non-controlling interest shareholder under put option and included it in other non-current liabilities. As at December 31, 2011, the fair value of liability under put option was reassessed by the Group and amounted to 20,898.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

29) Equity (continued)

v) Sale of Non-controlling Interests (continued)

In the year ended December 31, 2011, the Group increased share capital of OOO "TMK-INOX". The share capital increase was partially financed by the non-controlling interest shareholder. Cash consideration received from the non-controlling interest shareholder amounted to 298,500 thousand Russian roubles (9,265 at historical exchange rate). As a result of the transaction, the ownership interest of the Group in OOO "TMK-INOX" decreased to 51.00%. The difference between the consideration received and the carrying values of net assets attributable to non-controlling interests in the amount of 42 was charged to accumulated profit.

vi) Recognition of the Change in Non-controlling Interests in the Subsidiary as an Equity Transaction

In the year ended December 31, 2011, the increase of non-controlling interests in OOO "TMK-INOX" amounted to 9,609, including 302 of the non-controlling interest's share of profit, net of dividends attributable to the non-controlling interest shareholder (2010 year: 13,587 and nil, respectively). This amount was recognised in additional paid-in capital.

vii) Contributions from Non-controlling Interest Owners

In 2010, the Group established a new subsidiary, OAO "Sinarskaya heat and power plant". The 31.21% ownership interest in OAO "Sinarskaya heat and power plant" was acquired by a third party for 700 million Russian roubles (23,124 at historical exchange rate). As a result of the transaction, the Group's ownership interest in OAO "Sinarskaya heat and power plant" amounted to 68.79%. As at the date of the transaction, the Group recognised non-controlling interest in the amount of 23,124.

viii) Increase in Non-controlling Interests from Contribution of Assets by the Group

During the year ended December 31, 2011, the Group made additional contribution of assets to the capital of OAO "Sinarskaya heat and power plant". As a result of the transaction, net assets attributable to non-controlling interests increased by 202. The effect of the increase of non-controlling interests in the amount of 202 was charged to accumulated profit.

ix) Dividends Declared by Subsidiaries of the Group to the Non-controlling Interest Owners

During the years ended December 31, 2011 and 2010, the Group's subsidiaries declared dividends to the non-controlling interest owners in the amounts of 338 and 8, respectively.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

29) Equity (continued)

x) Hedges of Net Investment in Foreign Operations

At the date of the acquisition of controlling interests in NS Group, Inc. and IPSCO Tubulars, Inc. the Group hedged its net investment in these operations against foreign currency risk using borrowings in US dollars made by Russian companies of the Group. As at December 31, 2011, the Group designated US dollar denominated loans in the amount of 1,158,610 (December 31, 2010: 1,158,610) as the hedging instrument. The aim of the hedging was to eliminate foreign currency risk associated with the repayment of these liabilities resulting from changes in US dollar/Russian rouble spot rates.

The effectiveness of the hedging relationship was tested using the dollar offset method by comparing the cumulative gains or losses due to changes in US dollar/Russian rouble spot rates on the hedging instrument and on the hedged item. In the year ended December 31, 2011, the effective portion of net losses from spot rate changes in the amount of 1,991,882 thousand Russian roubles (67,772 at historical exchange rates), net of income tax benefit of 398,376 thousand Russian roubles (13,554 at historical exchange rates), was recognised in other comprehensive income (foreign currency translation reserve).

xi) Treasury Shares

	2011		2010	
	Number of shares	Cost	Number of shares	Cost
Outstanding as at January 1	71,575,796	318,351	7,097,364	37,378
Purchased during the period	2,844,700	8,988	64,478,432	280,973
Outstanding as at December 31	74,420,496	327,339	71,575,796	318,351

In the year ended December 31, 2011, the Group purchased 2,844,700 shares of the Company for 8,988. As at December 31, 2011, the Group owned 74,420,496 treasury shares.

In the year ended December 31, 2010, the Group purchased 64,478,432 shares of the Company from TMK Steel for 280,973 (including transaction fees of 2,000).

In order to facilitate the issuance of the convertible bonds, investment banks offered to certain institutional investors an opportunity to borrow GDRs of OAO TMK during the term of the bonds.

30) Financial Risk Management Objectives and Policies

The Group's principal financial liabilities comprise bank loans, bonds issued, trade payables, liabilities under put options of non-controlling interest shareholders in subsidiaries and finance leases. The main purpose of these financial liabilities is to raise finance for the Group's operations. The Group has various financial assets such as trade receivables and cash and deposits, which arise directly from its operations.

In the course of its business, the Group is exposed to a number of financial risks: market risk (including interest rate risk, foreign currency risk and other price risk), liquidity risk and credit risk. The presented information shows susceptibility of the Group concerning each of these risks. The Board of Directors reviews and establishes policies for managing each of these risks which are summarised below.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Market Risk

The Group is exposed to risk from movements in interest rates, foreign currency exchange rates and market prices that affect its assets, liabilities and anticipated future transactions. The objective of market risk management is to manage and control market risk exposures, while optimising the return on the risk.

Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Group's interest rate risk management policy is to minimise risk with the aim to achieve financial structure objectives defined and approved in the management's plans. Borrowing requirements of the Group's companies are pooled by the Group's central finance department in order to manage net positions and the funding of portfolio developments consistently with management's plans while maintaining a level of risk exposure within prescribed limits.

The Group borrows on both a fixed and variable rate basis. EURIBOR and LIBOR served as the basis for the calculation of interest rates on loans with variable rate. These loans accounted for 16% of the total loan portfolio at the end of 2011 (8% at the end of 2010). The Group considers such risks as not significant and is not using instruments to hedge such interest-rate risks at present. Nevertheless, the Group monitors interest rates and will use instruments to hedge such risk as necessary.

The Group does not have any financial assets with variable interest rate.

The following table demonstrates the sensitivity to reasonably possible changes in interest rates, with all other variables held constant, of the Group's profit before tax (through the impact on floating rate borrowings).

	Basis points	Effect on profit before tax
As at December 31, 2011		
Increase in LIBOR	15	(660)
Decrease in LIBOR	(15)	660
Increase in EURIBOR	15	(262)
Decrease in EURIBOR	(15)	262
As at December 31, 2010		
Increase in LIBOR	100	(1,126)
Decrease in LIBOR	(25)	281
Increase in EURIBOR	100	(1,792)
Decrease in EURIBOR	(25)	448

Foreign Currency Risk

The Group's exposure to currency risk relates to sales, purchases and borrowings that are denominated in a currency other than the respective functional currencies of the Group's subsidiaries, and the Group's net investments in foreign operations. The currencies in which these transactions and balances primarily denominated are US dollars and Euro.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Foreign Currency Risk (continued)

The Group's exposure to currency risk determined as the net monetary position in respective currencies was as follows as at December 31:

	2011	2010
USD/RUR (*)	(1,336,893)	(1,457,948)
EUR/RUR	(198,643)	(323,931)
EUR/USD	(17,634)	21,467
USD/RON	(11,445)	(90,967)
EUR/RON	(70,128)	(5,541)
KZT/RUR	5,621	4,544
USD/CAD	600	-

* As disclosed in Note 29 the Group hedged its net investments in foreign operations against foreign currency risk using borrowings in US dollars made by Russian companies of the Group. The net monetary position in USD/RUR included the hedging instruments in the amount of 1,158,610 (2010: 1,158,610) which exposure to currency risk is reflected directly in other comprehensive income.

The Group hedges its exposure to currency risk related to Euro denominated sales of Romanian subsidiaries using EUR/RON forward contracts. The fair value of these forward contracts in the amount of 3 was included in other financial assets as at December 31, 2011.

The Group doesn't have other formal arrangements to manage currency risks of the Group's operations and balances. However, the Group seeks to bring its financial liabilities in foreign currency in line with export net sales, thus mitigating currency risk.

The following table demonstrates the sensitivity to reasonably possible changes in the respective currencies, with all other variables held constant, of the Group's profit before tax and other comprehensive income. In estimating reasonably possible changes for 2011 and 2010 the Group assessed the volatility of foreign exchange rates during the three years preceding the end of the reporting period.

	As at December 31, 2011					
	Volatility range		Effect on Income Statement		Effect on Statement of Comprehensive Income	
	Low	High	Low	High	Low	High
USD/RUR	12.57%	-12.57%	(22,410)	22,410	(145,637)	145,637
EUR/RUR	9.96%	-9.96%	(19,785)	19,785	-	-
EUR/USD	11.44%	-11.44%	(2,017)	2,017	-	-
USD/RON	14.24%	-14.24%	(1,630)	1,630	-	-
EUR/RON	5.04%	-5.04%	(3,537)	3,537	-	-
KZT/RUR	16.88%	-16.88%	949	(949)	-	-
USD/CAD	11.61%	-11.61%	70	(70)	-	-

	As at December 31, 2010					
	Volatility range		Effect on Income Statement		Effect on Statement of Comprehensive Income	
	Low	High	Low	High	Low	High
USD/RUR	11.91%	-11.91%	(35,651)	35,651	(137,990)	137,990
EUR/RUR	10.07%	-10.07%	(32,620)	32,620	-	-
EUR/USD	11.75%	-11.75%	2,522	(2,522)	-	-
USD/RON	16.49%	-16.49%	(15,000)	15,000	-	-
EUR/RON	7.85%	-7.85%	(435)	435	-	-
KZT/RUR	12.57%	-12.57%	571	(571)	-	-

Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Other Price Risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The Group's exposure to other price risk relates to changes of the fair value of its derivative financial instrument as a result of fluctuations of GDR's quotations. The Group manages its exposure to other price risk by holding treasury shares in the quantity corresponding to the number of shares in which convertible bonds are convertible.

The reasonably possible changes in the price of underlying GDRs, with all other variables held constant, would have an effect on the Group's profit before tax. In estimating reasonably possible fluctuations of GDR's quotations, the Group assessed the volatility of GDRs during the year ended December 31, 2011. A 43.69% increase to the value of GDR as at December 31, 2011 would reduce profit before tax by 12,065. A 43.69% decrease from the value of GDR as at December 31, 2011 would result in the increase of profit before tax by 2,898.

Liquidity Risk

Liquidity risk arises when the Group encounters difficulties to meet commitments associated with liabilities and other payment obligations. The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group manages liquidity risk by targeting an optimal ratio between equity and total debt consistent with management plans and business objectives. This enables the Group to maintain an appropriate level of liquidity and financial capacity as to minimise borrowing expenses and to achieve an optimal profile of composition and duration of indebtedness. The Group has access to a wide range of funding at competitive rates through the capital markets and banks and coordinates relationships with banks centrally. At present, the Group believes it has access to sufficient funding and has also both committed and uncommitted borrowing facilities to meet currently foreseeable borrowing requirements.

Effective management of the liquidity risk has the objective of ensuring both availability of adequate funding to meet short-term requirements and due obligations, and a sufficient level of flexibility in order to fund the development plans of the Group's business, maintaining an adequate finance structure in terms of debt composition and maturity. This implies the adoption of a strategy for pursuing an adequate structure of borrowing facilities (particularly availability of committed borrowings facilities) and the maintenance of cash reserves.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Liquidity Risk (continued)

The table below summarises the maturity profile of the Group's financial liabilities based on contractual undiscounted payments, including interest payments:

As at December 31, 2011	Less than 3 months	3 to 12 months	1 to 2 years	2 to 3 years	3 to 4 years	> 4 years	Total
Trade and other payables	716,807	5,521	–	–	–	–	722,328
Accounts payable to related parties	733	–	–	–	–	–	733
Interest-bearing loans and borrowings:							
Principal	143,427	430,238	794,855	697,143	326,800	1,413,894	3,806,357
Interest	73,454	178,888	204,430	140,586	109,790	147,356	854,504
Dividends payable	323	–	–	–	–	–	323
Liabilities under put options of non-controlling interest shareholders in subsidiaries	14,051	–	–	–	–	–	14,051
Other non-current liabilities	–	–	403	595	1,129	30,398	32,525
	948,795	614,647	999,688	838,324	437,719	1,591,648	5,430,821

As at December 31, 2010	Less than 3 months	3 to 12 months	1 to 2 years	2 to 3 years	3 to 4 years	> 4 years	Total
Trade and other payables	617,862	5,171	–	–	–	–	623,033
Accounts payable to related parties	7,457	977	–	–	–	–	8,434
Interest-bearing loans and borrowings:							
Principal	346,061	332,978	429,252	822,783	560,812	1,407,200	3,899,086
Interest	91,411	207,935	238,268	189,386	139,254	171,767	1,038,021
Dividends payable	261	169	–	–	–	–	430
Liabilities under put options of non-controlling interest shareholders in subsidiaries	14,934	–	–	–	–	–	14,934
Other non-current liabilities	–	–	599	1,040	466	29,915	32,020
	1,077,986	547,230	668,119	1,013,209	700,532	1,608,882	5,615,958

Credit Risk

Credit risk is the potential exposure of the Group to losses that would be recognised if counterparties failed to perform or failed to pay amounts due. Financial instruments that potentially expose the Group to concentrations of credit risk consist primarily of cash and trade accounts receivable.

The credit risk arising from the Group's normal commercial operations is controlled by each operating unit within Group-approved procedures for evaluating the reliability and solvency of each counterparty, including receivable collection. The monitoring activity of credit risk exposure is performed at the Group level according to set guidelines and measurement techniques to qualify and monitor counterparty risk.

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Credit Risk (continued)

The Group sells goods to some of the biggest Russian and international companies on credit terms. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures.

As at December 31, 2011, accounts receivable from the three biggest debtors of the Group amounted to 256,961 (December 31, 2010: 234,055). Management determines concentration by reference to receivables from particular customers as percentage of total accounts receivable.

The maximum exposure to credit risk is equal to the carrying amount of financial assets, which are disclosed below:

	2011	2010
Cash and cash equivalents	230,593	157,524
Trade and other receivables	766,226	716,940
Accounts receivable from related parties	5,417	3,305
Other financial assets	4,047	3,966
Other	13,690	7,016
	1,019,973	888,751

The ageing analysis of trade and other receivables, accounts receivable from related parties and other financial assets is presented in the table below:

	2011		2010	
	Gross amount	Impairment	Gross amount	Impairment
Current Trade and other receivables - not past due	636,820	(2,345)	578,481	(292)
Current Trade and other receivables - past due				
less than 30 days	77,758	(990)	65,141	(43)
between 30 and 90 days	24,139	(3,489)	33,412	(229)
over 90 days	59,220	(24,958)	57,799	(17,372)
Accounts receivable from related parties - not past due	5,417	-	3,305	-
Non-current Trade and other receivables - not past due	71	-	54	(11)
Other - not past due	13,690	-	7,016	-
	817,115	(31,782)	745,208	(17,947)

Movement in allowance for doubtful debts was as follows:

	2011	2010
Balance at the beginning of the year	17,947	15,172
Utilised during the year	(3,431)	(2,347)
Additional increase in allowance	19,551	5,420
Currency translation adjustment	(2,285)	(298)
Balance at the end of the year	31,782	17,947

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Capital Management

The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximise the return to shareholders. The Board of directors reviews the Group's performance and establishes key performance indicators. In addition, the Group is subject to externally imposed capital requirements (debt covenants) which are used for capital monitoring. Through 2011, the Group was in compliance with such externally imposed capital requirements. The Group met its objectives for managing capital.

Capital includes equity attributable to the equity holders of the parent entity.

The Group manages its capital structure and adjusts it by issue of new shares, dividend payments to shareholders, purchase of treasury shares. The Group monitors the compliance of the amount of legal reserve with the statutory requirements and makes appropriations of profits to legal reserve. In addition, the Group monitors distributable profits on a regular basis and determines the amounts and timing of dividend payments.

Fair Value of Financial Instruments

The carrying amounts of financial instruments, such as cash and cash equivalents, short-term and long-term investments, short-term accounts receivable and short-term loans approximate their fair value.

The following table shows financial instruments which carrying amounts differ from fair values:

	As at December 31, 2011		As at December 31, 2010	
	Net carrying amount	Fair Value	Net carrying amount	Fair Value
Financial Liabilities				
Fixed rate long term bank loans	1,778,324	1,776,743	2,471,628	2,469,174
Variable rate long term bank loans	467,749	439,413	244,378	242,660
Bonds due 2013	155,298	155,143	164,059	165,371
Bonds due 2011	–	–	164,059	165,010
5.25 per cent convertible bonds liability	388,508	384,054	382,216	404,123
7.75 per cent loan participation notes due 2018	500,000	429,690	–	–
10 per cent loan participation notes due 2011	–	–	186,700	193,261

The fair value of the bonds and notes was determined based on market quotations. The fair value of fixed-rate bank loans was calculated based on the present value of future principal and interest cash flows, discounted at prevailing interest rates of 9%, 7% and 5% per annum for loans denominated in Russian rouble, US dollar and Euro, respectively, as at December 31, 2011 (9%, 8% and 5% per annum for loans denominated in Russian rouble, US dollar and Euro, respectively, as at December 31, 2010).

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

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Notes to the Consolidated Financial Statements (continued)

(All amounts are in thousands of US dollars, unless specified otherwise)

30) Financial Risk Management Objectives and Policies (continued)

Fair Value of Financial Instruments (continued)

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly;

Level 3: techniques which use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

As at December 31, 2011 and 2010, the Group held the following financial instruments measured at fair value:

	2011	Level 2	2010	Level 2
Liabilities measured at fair value				
Derivative financial instrument	3,024	3,024	47,816	47,816

During the reporting period, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

31) Subsequent Events

Bank Loans

In January 2012, the Group fully repaid a short-term loan from Gazprombank in the principal amount of 36,660 in accordance with the terms of the loan agreement.