

DESCRIPTION OF THE MAIN RISKS

Operating

- Risks associated with geological exploration operations
- Licensing risks
- Project risks
- Risks associated with human resources
- Risks associated with occupational and industrial safety
- Environmental risks
- Risks associated with information security

Market

- Risks associated with a possible change in prices for purchased raw materials and services
- Risks associated with a possible change in the price of oil, petroleum products, gas, and gas products
- Risks associated with industry-wide competition
- Risks associated with a possible change in the economic environment

Government regulation

- Risks associated with more sanctions from the EU and the U.S.
- Political risks
- Risks associated with foreign assets
- Corruption risks
- Risks associated with changes to judicial practice on matters related to the Company’s operations
- Risks associated with changes to the tax legislation of the Russian Federation
- Risks associated with changes to the rules for customs control and duties

Financial

- Credit risk of counterparties
- Risk associated with borrowing
- Foreign exchange risk
- Interest risk

Strategic

- Risk of failing to achieve strategic goals

Partner

- Risks associated with attracting partners

Description

Risk management measures

1. OPERATING RISKS

1.1. Risks associated with geological exploration operations

One of the Company’s key strategic objectives is growth in the raw hydrocarbon resource base in quantitative and qualitative terms in order to ensure the required level of production, which in turn largely depends on the success of geological exploration. The main risks associated with geological exploration operations are the failure to confirm the planned level of hydrocarbon reserves and objective deterioration in the quality of the resource base. Another important factor is geological exploration work in different geographic regions, including regions with adverse climatic conditions and environmental restrictions, which often lead to the risk of increased costs. Estimates depend on a number of variable factors and assumptions, including the following:

- the correlation of the historical level of productivity in the region of production with the productivity of other regions that are comparable in terms of characteristics;
- the interpretation of geological exploration data;
- the effect of the requirements of government structures and legislative acts.

Gazprom Neft manages licensing risks associated with geological exploration work by making timely changes to the design documents for geological exploration

Gazprom Neft has considerable experience conducting geological exploration work and employing the latest geophysical methods to search for and explore hydrocarbons as well as advanced technologies in the drilling and development of fields, including in harsh natural and climatic conditions, which results in the decreased probability of such risks. The Company has hired the auditor DeGolyer & MacNaughton to perform an independent audit of reserves based on the estimates of the Gazprom Neft’s subsidiaries. Gazprom Neft actively cooperates with government structures at the federal and regional levels on matters concerning the sustainable use of subsoil resources

Description	Risk management measures
<p>1.2. License risks</p>	
<p>The Company performs its subsoil resource operations on the basis of special permit documents and licenses for the right to use subsoil sites, which specify the intended use (type of subsoil use), spatial boundaries, dates, and mandatory conditions for the use of the subsoil resources. Existing law envisages administrative sanctions for the unlicensed use of a subsoil site, and there is a risk of criminal liability in a number of cases</p> <p>The failure to meet the conditions for the use of subsoil resources may entail administrative liability with the imposition of fines, while the violation of significant conditions for the use of subsoil resources may entail the risk of the early termination of a license in accordance with Article 23 of Federal Law No. 2395-1 dated 21 February 1992 "On Subsoil Resources". If the right to use subsoil resources is terminated prematurely, the Company bears both reputational risks as well as material damages related to the expenses incurred on acquiring the right to use the subsoil resources, investments to develop the subsoil site and decreased capitalization associated with the loss of the resource base</p>	<p>The Company views the prohibition on the unlicensed use of subsoil resources as a categorical imperative. The Company provides end-to-end surveying support for all stages of prospecting, exploration, and production drilling as an exhaustive measure to prevent the unlicensed use of subsoil resources.</p> <p>The Company's Subsoil Use Monitoring System (SUMS) automated complex with its well-developed matrix for the risks involved with fulfilling the main (significant) conditions for the use of subsoil resources is the main risk management tool that is used to assess the current state of risks using matrix indicators and plan for an acceptable level of risk in the future.</p> <p>Permanent regional commissions for the licensing of subsidiaries review the status of current and potential license risks and the implementation of targeted measures to mitigate such risks on a quarterly basis.</p> <p>The CEOs of the Company's subsidiaries are responsible for withholding a license for the right to use subsoil resources</p>
<p>1.3. Project risks</p>	
<p>The Company continuously develops and implements investment projects that aim to achieve strategic goals, in particular growth in the extraction of raw commodities and improvements in the quality of the products manufactured. When implementing projects, the Company encounters a variety of risks that could lead to a violation of the deadlines and/or the increased cost of the project. The main factors behind such risks are poor planning, violations of the project terms and safety requirements by contractors as well as new circumstances (increased cost of materials, errors in the assessment of infrastructure conditions, and switching equipment suppliers)</p>	<p>The Company manages these risks, while paying special attention to the development and coordination stages of investment projects. In 2014, a risk management system was introduced to the process of preparing and implementing major projects. This system is based on the generally accepted approach in the global industry to establishing a project's value using the Stage-Gate process with a risk assessment of the project at each of its stages. Requirements for contractors are based on a risk assessment and also take into account the requirements of the laws of the country in which the project is being implemented. In addition, the Company has established a project monitoring system</p>
<p>1.4. Risks associated with human resources</p>	
<p>The Company's business depends on highly skilled key employees, and a lack of skilled labour, in particular in engineering and technical areas, may lead to risks associated with a shortage of personnel. The Company's success largely depends on the efforts and abilities of key employees, including skilled technical personnel, as well as the Company's ability to recruit and retain such personnel. Competition for personnel in Russia and abroad may intensify due to the limited number of skilled specialists on the labour market. The inability to recruit new skilled personnel and/or retain existing skilled personnel could have a negative effect on the Company's appeal as an employer. Demand for skilled employees and the related expenses are expected to grow, thereby reflecting the considerable interest in such resources from other industries and social projects</p>	<p>The Company offers a safe workplace and competitive salaries and provides training for employees in specially designed programmes. In addition, the Company is improving personnel recruiting procedures and implementing measures that aim to reduce personnel turnover and encourage the self-development of personnel</p>

Description	Risk management measures
1.5. Risks associated with occupational safety and industrial safety	
<p>The Company is exposed to risks involving the safety of employees, equipment, buildings, and structures. Numerous factors may have a negative effect on the Company's core activities, including the breakdown or failure of equipment, labour disputes, injury to personnel and third parties, natural disasters, political disputes, or acts of terrorism. Any of the risk factors may have a significantly adverse impact on the business, financial condition, and results of the Company's activities</p>	<p>In order to mitigate these risks, the Company is implementing a large-scale integrated programme that aims to ensure safe working conditions for employees and safe manufacturing processes. This programme complies with the best international practices and is based on enhancing the role of production managers at all levels in ensuring work safety. The Company has successfully applied the experience gained from international oil companies by adapting it to the conditions of its production sites. In particular, the Company has introduced behavioural safety audits and internal incident investigations in order to identify and eliminate their causes, is implementing a transport safety programme, has introduced risk assessment for hazardous work, and holds numerous drills, training exercises, and seminars for all levels of the organization. The Company has certified the work safety management system for compliance with the OHSAS 18001 international standard, adheres to the principle of continuous improvement, and has selected priority areas of this system for the coming years. The Company declared 2016 the Year of Occupational Safety</p>
1.6. Environmental risks	
<p>The production activities of Gazprom Neft are fraught with the potential risk of an environmental impact that exceeds the permitted standards, which may result in civil liability and the need for work to eliminate such damage. The Company is fully aware of its social responsibility to create safe working conditions and maintain a favourable environment, continuously monitors its activities to ensure compliance with the relevant environmental standards, and is implementing an environmental protection programme. In the future, costs associated with observing environmental requirements or obligations may increase</p>	<p>The industrial safety policy of Gazprom Neft aims to ensure compliance with the requirements of current environmental legislation by investing substantial funds in environmental measures, including the use of technologies that ensure minimal negative impact on the environment. These activities have resulted in a significant decline in the probability of risks associated with environmental pollution. The Company also follows the changes in environmental legislation in the different countries in which it operates</p>
1.7. Risks associated with information security	
<p>As a major high-tech company, Gazprom Neft pays special attention to the assessment and analysis of risks associated with information technologies, automation, and telecommunications (ITAT). ITAT risks are associated with the management of ITAT activities, the functioning of IT systems as well as the possible risks of sanctions on foreign software</p>	<p>The Company's goal in ITAT risk management is to enhance the ability to effectively achieve business objectives through projecting ITAT risk factors and to maximize the effectiveness of ITAT risk management activities.</p> <p>The Company constantly monitors and closely analyses both threats that are already known as well as potential threats to ITAT.</p> <p>The Company's Department of Information Technologies, Automation, and Telecommunications is responsible for developing regulatory documents governing the risk management activities of ITAT and also implements a number of activities that aim to reduce the impact of such risks by:</p> <ul style="list-style-type: none"> ■ Ensuring the identification of events that may have a negative impact on the achievement of the Company's objectives; ■ Ensuring the analysis, assessment, and prioritization of ITAT risks; ■ Ensuring an optimal response strategy and the implementation of ITAT risk management activities; <p>Ensuring continuous monitoring and control over the implementation of ITAT risk management activities</p>

Description	Risk management measures
2. MARKET RISKS	
Gazprom Neft's core businesses are oil and gas production, oil refining, and the sale of oil and petroleum products, thus the Company is exposed to risks that are traditionally inherent to the oil and gas industry, namely:	
<ul style="list-style-type: none"> ■ risks associated with a possible change in prices for purchased raw materials and services; ■ risks associated with a possible change in oil and petroleum product prices; ■ risks associated with industry-wide competition; ■ risks caused by economic instability in the industry 	
2.1. Risks associated with a possible change in prices for purchased raw materials and services	
<p>In the process of its business operations, Gazprom Neft uses the infrastructure of monopoly service providers for the transportation of oil and petroleum products and the supply of electricity and also uses raw materials and services that are purchased from a wide range of suppliers. The Company has no control over the infrastructure of these monopoly service providers, the amount of tariffs charged, or the pricing of raw materials and services by suppliers</p>	<p>The Company is implementing a number of measures that aim to mitigate the impact of such risks:</p> <ul style="list-style-type: none"> ■ long-term planning of commodity flows and the timely provisioning of the cumulative flow of oil and petroleum products as well as the necessary rolling stock; ■ the optimal redistribution of commodity flows by transportation type; ■ the use of alternative and internal sources of power generation; ■ long-term contracting with fixed volumes and prices for the entire duration of the contracts; ■ the use of transparent cost revision formulas as part of long-term service contracts that are strictly dependent on market fluctuations. <p>These measures make it possible to reduce risks associated with the use of services and the acquisition of goods from monopoly providers to an acceptable level and ensure the Company's uninterrupted operations</p>
2.2. Risks associated with possible changes in the price of oil, petroleum products, gas, and gas products	
<p>The Company's financial indicators are directly related to the price level of crude oil and petroleum products. The Group is unable to fully control the prices of its products, which depend on fluctuations related to the balance of supply and demand on the global and domestic markets for crude oil and petroleum products as well as the actions of the regulatory authorities</p>	<p>The Group has a business planning system which at its core has a scenario-based approach for determining the Company's key performance indicators depending on oil prices on the global market. This approach makes it possible to cut costs, including by reducing them or carrying them over to future periods of investment programmes as well as other mechanisms.</p> <p>These measures enable the Company to reduce risks to an acceptable level.</p>
2.3. Risks associated with industry-wide competition	
<p>There is intense competition in the Russian oil and gas industry between the leading Russian oil and gas companies in the main areas of production and economic activities, including:</p> <ul style="list-style-type: none"> ■ the acquisition of licenses for the right to use subsoil resources to produce hydrocarbons at auctions organized by the government authorities; ■ the acquisition of other companies that own licenses for the right to use subsoil resources to produce hydrocarbons or that own existing assets associated with production raw hydrocarbons; ■ the hiring of leading independent service companies; ■ the acquisition of high-tech equipment; ■ the hiring of experienced and the most qualified specialists; ■ access to critical transportation infrastructure; ■ the acquisition of existing assets and the construction of new assets that increase the product sales volume to end users. 	<p>The implementation of the portfolio of strategic projects that aim to develop key areas of Gazprom Neft's business ensures the gradual strengthening of the Company's positions in the oil and gas industry through a reduction in risks associated with industry-wide competition</p>
<p>In addition, there is competition from the suppliers of alternative energy sources, including coal and nuclear energy as well as renewable energy sources</p>	