



JSC Lancaster Petroleum

Financial Statements

*Year ended December 31, 2007
with Independent Auditor's Report*

Ernst & Young

 **ERNST & YOUNG**

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Joint Stock Company Lancaster Petroleum

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

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the 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 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 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 financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The supplementary information about oil and gas producing activities is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in our audit of the financial statements and, accordingly, we express no opinion on it.

Ernst & Young LLP

June 29, 2008

BALANCE SHEET
As at December 31, 2007

<i>In thousands of Tenge</i>	Notes	2007	2006 (restated Note 4)
ASSETS			
Non-current assets			
Intangible assets	5	43,345	86,736
Property, plant and equipment	6	8,840,796	4,616,303
Other non-current assets	7	376,138	1,308,725
Deferred tax assets	25	161,130	—
Total non-current assets		9,421,409	6,011,764
Current assets			
Loan to related party	8	—	183,522
Inventories	9	218,895	134,940
Trade receivables	10	721,110	92,131
Due from related parties	27	2,344,339	286,829
Advances paid	11	228,532	414,196
Current tax assets		—	247,322
Other current assets	12	402,818	445,693
Bank deposits	13	58,696	6,897
Available-for-sale securities	14	—	293,050
Cash and cash equivalents	15	50,014	508,598
Total current assets		4,024,404	2,613,178
TOTAL ASSETS		13,445,813	8,624,942

BALANCE SHEET (continued)

As at December 31, 2007

<i>In thousands of Tenge</i>	Notes	2007	2006 (restated Note 4)
Equity			
Charter capital	16	1,500,000	1,500,000
Treasury shares	16	(150,000)	(150,000)
Revaluation reserve of available for sale securities		–	63,826
Retained earnings		4,690,907	3,699,297
Total equity		6,040,907	5,113,123
Liabilities			
Non-current liabilities			
Long-term interest-bearing loans	17	–	320,851
Abandonment and site restoration liabilities	18	241,048	157,199
Deferred tax liability	25	–	112,134
Total non-current liabilities		241,048	590,184
Trade payables	19	568,200	803,015
Due to related parties	27	26,416	49,474
Short-term interest-bearing loans	17	5,558,410	1,993,730
Corporate income tax payable		163,024	–
Excess profits tax payable		686,586	–
Other taxes payables		8,031	7,122
Other current liabilities		153,191	68,294
Total current liabilities		7,163,858	2,921,635
Total Liabilities		7,404,906	3,511,819
TOTAL SHAREHOLDER'S EQUITY AND LIABILITIES		13,445,813	8,624,942

The accounting policies and explanatory notes on pages 6 through 28 form an integral part of these financial statements.

Signed and authorized for release on behalf of the Board of the Company:

President

Chief Accountant



S. Sarbopayeva

STATEMENT OF INCOME
For the year ended December 31, 2007

<i>In thousands of Tenge</i>	Notes	2007	2006 (restated Note 4)
Revenue		7,673,788	6,037,319
Cost of sales	20	(1,965,748)	(1,291,566)
Gross profit		5,708,040	4,745,753
Dry hole expense		(293,552)	(2,076,055)
Geological and geophysical expenses	21	(804,113)	(217,641)
General and administrative expenses	22	(1,249,660)	(807,111)
Selling expenses	23	(872,334)	(670,684)
Loss on disposal of property, plant and equipment		(14,385)	(10,634)
Other operating income		9,654	590
Profit from operating activities		2,483,650	964,218
Finance expenses	24	(364,020)	(232,700)
Finance income	24	277	1,170
Gain on disposal of available for sale securities		12,934	-
Foreign exchange gain, net		255,134	(63,062)
Profit before income tax		2,387,975	669,626
Income tax expense	25	(776,127)	(291,379)
Excess profit tax expense	25	(620,238)	-
Net profit for the year		991,610	378,247
Basic earnings per share		735	280

The accounting policies and explanatory notes on pages 6 through 28 form an integral part of these financial statements.

Signed and authorized for release on behalf of the Board of the Company:

President

Chief Accountant



F. Hayes

S. Sarbopeyeva

STATEMENT OF CASH FLOWS

For the year ended December 31, 2007

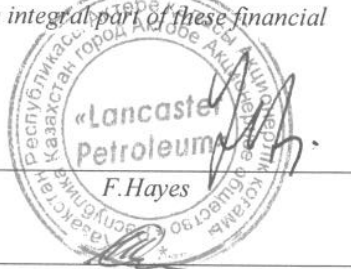
<i>In thousands of tenge</i>	Notes	2007	2006 (restated Note 4)
Cash flows from operating activities:			
Profit before income tax		2,387,975	669,626
Adjustments for:			
Depreciation and amortization		597,736	517,670
Dry hole expense		293,552	2,076,055
Provision charge		9,672	(187,462)
Unwinding discount		25,268	4,813
Usage of the liquidation fund		(9,216)	(1,317)
Provision for obsolete inventories		42,446	15,940
Finance costs		338,475	226,717
Loss from disposal of property, plant and equipment		798,367	10,634
Gain on sale of available for sale securities		(12,934)	-
Unrealized foreign exchange gain		(266,757)	-
Operating profit before working capital changes		4,204,584	3,332,676
(Increase) / decrease in operating assets:			
Inventories		(126,401)	(73,957)
Trade receivables		(651,169)	406,948
Advances paid and non-interest bearing loan		172,258	201,304
Due from related parties		(1,338,757)	(245,134)
Other current assets		(69,125)	(317,346)
Other non-current assets		145,243	(365,602)
Increase / (decrease) in operating liabilities:			
Due to related parties		(23,058)	28,350
Trade and other payables		(285,052)	485,485
Other current liabilities		96,434	(32,607)
Cash generated from operations		2,124,957	3,420,117
Interest paid		(693,591)	(259,183)
Income tax paid		(583,325)	(410,724)
Net cash flows provided by operating activities		848,041	2,750,210
Cash flows from investing activities:			
Purchase of property, plant and equipment		(5,246,039)	(2,837,192)
Proceeds from sale of property, plant and equipment		91,234	8,811
Purchase of intangible assets		-	(50,173)
Purchase of available-for-sale securities		-	(109,224)
Proceeds from sale of available-for-sale securities		350,715	224,000
Placement of bank deposits		(51,799)	14,516
Interest received		-	1,257
Net cash used in investing activities		(4,855,889)	(2,748,005)
Cash flows from financing activities:			
Proceeds from loans received		6,584,265	5,214,217
Repayment of loans		(3,035,001)	(4,762,128)
Net cash (used in) provided by financing activities		3,549,264	452,089
Net increase in cash and cash equivalents		(458,584)	454,294
Cash and cash equivalents at the beginning of the year	15	508,598	54,304
Cash and cash equivalents at the end of the year	15	50,014	508,598

The accounting policies and explanatory notes on pages 6 through 28 form an integral part of these financial statements.

Signed and authorized for release on behalf of the Board of the Company:

President

Chief Accountant



F. Hayes

S. Sarbopeyeva

STATEMENT OF CHANGES IN EQUITY

For the year ended December 31, 2007

<i>In thousands of tenge</i>	Charter capital	Treasury shares	Additional paid in capital	Retained earnings	Revaluation reserve of available-for-sale securities	Total Equity
As at December 31, 2005	1,500,000	(150,000)	30,337	3,290,713	–	4,671,050
Restatement of error (Note 4)	–	–	(30,337)	30,337	–	–
As at December 31, 2005 as restated	1,500,000	(150,000)	–	3,321,050	–	4,671,050
Fair value change of available for sale securities, net of tax	–	–	–	–	63,826	63,826
Total income and expense for the year (restated Note 4)	–	–	–	378,247	–	378,247
As at December 31, 2006 (restated Note 4)	1,500,000	(150,000)	–	3,699,297	63,826	5,113,123
Treasury shares-additional paid-in capital	–	–	–	–	–	–
Sale of available for sale securities	–	–	–	–	(63,826)	(63,826)
Profit for the year	–	–	–	991,610	–	991,610
As at December 31, 2007	1,500,000	(150,000)	–	4,690,907	–	6,040,907

The accounting policies and explanatory notes on pages 6 through 28 form an integral part of these financial statements.

Signed and authorized for release on behalf of the Board of the Company:

President

Chief Accountant



S.Sarbopeyeva

NOTES TO THE FINANCIAL STATEMENTS*In thousands of tenge***1. GENERAL INFORMATION**

JSC Lancaster Petroleum (the "Company") was renamed on September 2, 2007 as an assignee of JSC KKM Operating Company, which was established on April 4, 2004 as a joint stock company through the merging of Kumsai Munay LLP, Mortuk Munay LLP and Kokzhide Munay LLP, which were fully owned by JSC KKM Holding at the date of the merger. The Company is engaged in exploration and production of oil from properties within the Republic of Kazakhstan.

The Company signed a subsoil use contract with the Government of Kazakhstan on December 25, 1995 and holds licenses for hydrocarbon exploration and production (the "Licenses") on Kokzhide, Kumsai and Mortuk fields; along with these Licenses the Company concluded agreements with the Government of Kazakhstan on exploration and development of these oil fields (the "Agreements"). These Agreements were amended in December 2004, April 2005 and July 2007, and as the result, the rights to explore and produce oil for the Mortuk field were extended till mid 2026, and for Kokzhide and Kumsai fields till mid 2027. On December 29, 2006 the Company signed a subsoil use contract with the Government of Kazakhstan on North Karpovsky field.

The Company's registered legal address is: 4 A Levitan Street, Aktobe, Republic of Kazakhstan.

The financial statements of the Company for the year ended December 31, 2007 were authorized for issue by the Board of Directors of the Company on June 29, 2008.

Political and economic environment

The Kazakh economy continues to display certain traits consistent with that of a market economy in transition. These characteristics have in the past included higher than normal historic inflation, lack of liquidity in the capital markets, and the existence of currency controls, which cause the national currency to be illiquid outside of Kazakhstan. The continued success and stability of the Kazakh economy will be significantly impacted by the government's continued actions with regard to supervisory, legal, and economic reforms.

As at December 31, 2007, management of the Company does not believe that any material matters exist relating to the developing markets and evolving fiscal and regulatory environment in Kazakhstan, including current pending or future governmental claims and demands, which would require adjustment to the accompanying financial statements in order for those statements not to be misleading.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The financial statements have been prepared under the historical cost convention for financial instruments which are carried at fair value.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 3.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****Changes in accounting policy and disclosures**

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Company has adopted the following new and amended IFRS and IFRIC interpretations during the year. Adoption of these revised standards and interpretations did not have any effect on the financial performance or position of the Company. They did however give rise to additional disclosures, including in some cases, revisions to accounting policies.

- IFRS 7 Financial Instruments: Disclosures
- IAS 1 Presentation of Financial statement (Amended)
- IAS 23 Borrowing Costs (Amended) (early adoption)
- IFRIC 8 Scope of IFRS 2
- IFRIC 9 Reassessment of Embedded Derivatives
- IFRIC 10 Interim Financial Reporting and Impairment

IFRS 7, Financial Instruments: Disclosures

This standard requires disclosures that enable users of the financial statements to evaluate the significance of the Company's financial instruments and the nature and extend of risks arising from those financial instruments. The new disclosures are included throughout the financial statements. While there has been no effect on the financial position or results of operations, comparative information has been revised where needed.

IAS 1, Presentation of Financial statement (amendment)

This amendment requires the Company to make new disclosures to enable users of the financial statements to evaluate the Company's objective, policies and processes for managing capital. These new disclosures are shown in Note 28.

IAS 23 Borrowing Costs (amendment) (early adoption)

The amendment to IFRS 23 requires borrowing costs to be capitalized when such costs relate to qualifying assets. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. The adoption of the standard has resulted in the Company capitalising interest on all new qualifying assets.

IFRIC 8, Scope of IFRS 2

This interpretation requires IFRS 2 to be applied to any arrangements in which the entity cannot identify specifically some or all of the goods received, in particular where equity instruments are issued for consideration which appears to be less than fair value. As the Company has no equity instruments, the interpretation had no impact on the financial position or performance of the Company.

IFRIC 9, Reassessment of Embedded Derivatives

IFRIC 9 states that the date to assess the existence of an embedded derivative is the date that an entity first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows. The Company has derivatives embedded in the host sales contract and as the accounting policies applied by the Company prior to the issuance of IFRIC 9 *Reassessment of Embedded Derivatives* were in line with this interpretation it had no effect on the financial position or performance of the Company.

IFRIC 10, Interim Financial Reporting and Impairment

The Company adopted IFRIC Interpretation 10 as of January 1, 2007, which establishes that an entity must not reverse an impairment loss recognized in a previous interim period in respect of goodwill or an investment in either an entity instruments or a financial assets carried at cost. As the Company had no impairment losses previously reversed, the interpretation had no impact on the financial position or performance of the Company.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****New accounting developments**

The following IFRS and IFRIC interpretations have been released however are not yet in effect as of December 31, 2007 and have not been adopted by the Company:

- IFRS 3 Business Combinations (Amended)
- IFRS 8 Operating Segments
- IAS 1R Presentation of financial statements (Amendment)
- IAS 27 Consolidated and Separate Financial Statements (Amended)
- IAS 32 Financial Instruments: Presentation (Amendment);
- IFRIC 11 Group and Treasury Share Transactions
- IFRIC 12 Service Concession Arrangements
- IFRIC 13 Customer Loyalty Programs
- IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

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

Functional currency and foreign currency translation

The Kazakhstan Tenge (“Tenge” or “KZT”) is the functional currency of the Company as it is the currency that reflects the economic substance of the underlying events and circumstances relevant to the Company.

Transactions in other currencies are treated as transactions in foreign currencies.

Monetary assets and liabilities denominated in foreign currencies are translated at exchange rates prevailing at the balance sheet dates. Transactions denominated in foreign currencies are recorded at the exchange rate prevailing at the date of the transaction. Any exchange gains and losses arising from assets and liabilities denominated in foreign currencies subsequent to the date of the underlying transaction are credited or charged to the statement of income.

The weighted average currency exchange rates established by the Kazakhstan Stock Exchange (“KASE”) are used as the official currency exchange rates in Kazakhstan.

Currency exchange rate of KASE as of December 31, 2007 was equivalent to 120,30 Tenge to 1 US dollar and was used to translate monetary assets and liabilities denominated in US dollars as at December 31, 2007 (2006: 127,00 Tenge to 1 US dollar). The currency exchange rate of KASE as at April 29, 2008 was 120.52 Tenge to 1 US dollar.

Intangible assets

Intangible assets include licenses for subsurface use and computer software reflected at initial cost less accumulated amortization. Licenses are amortized on a unit of production basis. Amortization of other intangible assets is calculated on a straight-line basis over the estimated useful lives of the assets, within a range of 1 to 10 years.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to definite is made on a prospective basis.

Licenses

License expenses associated with exploration, development and production of oil and gas reserves are capitalized as intangible assets and amortized over the life of the license from the date the relevant field commences commercial production stage.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****Property, plant and equipment***Oil and Gas assets**Exploration expenditure*

Geological and geophysical exploration costs are capitalized as work-in-progress till completion and then written-off against income as incurred. Costs directly associated with an exploration well are capitalized within property, plant and equipment as construction work-in-progress, until the drilling of the well is complete and the results have been evaluated. These costs include materials and fuel used, rig costs and payments made to contractors. If hydrocarbons are not found, the exploration expenditure is expensed. If hydrocarbons are found and, subject to further appraisal activity, which may include the drilling of further wells (exploration or exploratory-type stratigraphic test wells), are likely to be capable of commercial development, the costs continue to be carried as an asset. All such carried costs are subject to technical, commercial and management review at least once a year to confirm the continued intent to develop or otherwise extract value from the discovery. When this is no longer the case, the costs are written off.

When proved reserves of oil and natural gas are determined and development is sanctioned, the relevant expenditure is transferred to property, plant and equipment (oil and gas properties).

Development expenditure

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of development wells is capitalized within oil and gas assets.

Oil and Gas Assets

Oil and gas assets are initially stated at cost less accumulated depreciation, depletion and impairment. The cost of self-constructed assets includes the cost of materials, direct labor and an appropriate proportion of overheads directly related to construction.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation and the initial estimate of any decommissioning obligation, if any. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Oil and natural gas properties are depreciated using a unit-of-production method over proved developed reserves.

Other Property, Plant and Equipment

Property, plant and equipment are initially stated at cost less accumulated depreciation, depletion and impairment. The cost of self-constructed assets includes the cost of materials, direct labor and an appropriate proportion of overheads directly related to construction.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation and the initial estimate of any decommissioning obligation, if any. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Property, plant and equipment, other than oil and gas properties, are carried at cost less accumulated depreciation and depreciated on a straight-line basis over the estimated useful lives set out in the following table:

Buildings and constructions	10 – 50 years
Machinery and equipment	15 – 30 years
Vehicles	7 – 11 years
Other	3 – 10 years

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge*

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**Property, plant and equipment (continued)**

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

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

When each major repair is performed, its cost is recognised as a component in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied.

All assets under construction are classified as "Capital Work in Progress" and are not depreciated. Once projects are completed and put into use they are transferred to in service assets and become subject for depreciation

Inventories

Inventories are stated at the lower of cost and net realizable value on a weighted average basis. Cost includes all costs incurred in the normal course of business in bringing each item to its present location and condition. The cost of crude oil is the cost of production, including the appropriate proportion of depreciation, depletion and amortization and overheads based on normal capacity. Net realizable value of crude oil is based on estimated selling price in the ordinary course of business less any costs expected to be incurred to complete the sale. Materials and supplies inventories are carried at amounts that do not exceed the expected amounts recoverable in the normal course of business

Impairment of non-financial assets

The Company assesses assets or groups of assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Individual assets are grouped for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. If any such indication of impairment exists or when annual impairment testing for an asset group is required, the Company makes an estimate of its recoverable amount. An asset group's recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of an asset group exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are adjusted for the risks specific to the asset group and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in profit or loss.

After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****Financial assets**

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, held to maturity investments, or available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

The Company determines the classification of its financial assets on initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

All regular way purchases and sales of financial assets are recognized on the trade date, which is the date that the Company commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held-to-maturity when the Company has the positive intention and ability to hold to maturity. After initial measurement held-to-maturity investments are measured at amortized cost using the effective interest method.

Trade and other receivables

Trade and other receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Trade accounts receivable are generally have a short-term and are recognized and carried at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

Available-for-sale financial investments

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 other categories. After initial measurement, available-for-sale financial assets are measured at fair value with unrealized gains or losses recognized directly in equity until the investment is derecognized or determined to be impaired at which time the cumulative gain or loss previously recorded in equity is recognized in profit or loss. The Company has investment securities classified as available for sale financial investments as at December 31, 2006. The investment securities were sold during 2007.

Impairment of financial assets

The Company assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss shall be recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date. Any subsequent reversal of an impairment loss is recognized in profit or loss.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Company will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****Impairment of financial assets (continued)***Available-for-sale financial investments*

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from equity to profit or loss. Reversals in respect of equity instruments classified as available-for-sale are not recognised in profit or loss. Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

Derecognition of financial assets and liabilities*Financial asset*

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired;
- the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement; or
- the Company has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

Cash and cash equivalents

Cash and cash equivalents are defined as cash on hand, demand deposits and short-term and highly liquid investments with original maturity of not more than three months readily convertible to known amounts of cash, are subject to insignificant risk of change in value and are carried at cost.

Interest-bearing loans and borrowings

All loans and borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest method.

Gains and losses are recognized in net profit or loss when the liabilities are derecognized as well as through the amortization process.

Interest relating to qualifying assets is capitalised to that asset. All other interest is expensed as finance costs in the statement of income.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****Treasury shares**

Own equity instruments which are reacquired (treasury shares) are deducted from equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company's own equity instruments.

Deferred income tax

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences:

- except where the deferred income tax liability arises from goodwill amortization or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carry-forward of unused tax assets and unused tax losses can be utilized:

- except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognized to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantially enacted at the balance sheet date.

Other taxes

Kazakhstan also has various taxes that are assessed on a Company's activities. These taxes are included as a component of cost of sales and general and administrative expenses in the income statement.

Trade and other payables

Liabilities for trade and other amounts payable are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Company.

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)****Provisions (continued)***Abandonment and Site Restoration (decommissioning)*

Provision for decommissioning is recognized in full, on a discounted basis, at the commencement of oil and natural gas production. The amount recognized is the present value of the estimated future expenditure determined in accordance with local conditions and requirements. A corresponding tangible fixed asset of an amount equivalent to the provision is also created. This asset is subsequently depreciated as part of the capital costs of the production and transportation facilities on a unit-of-production basis.

Changes in the measurement of an existing decommissioning liability that results from changes in the estimated timing or amount of the outflow of resources embodying economic benefits required settling the obligation, or change in the discount rate is reflected as an adjustment to the provision and the fixed asset.

The long-term inflation and discount rates used to determine the balance sheet obligation at December 31, 2007 were 5% and 16% respectively (2006: 7% and 10%). Movements in the provision for asset retirement obligations are disclosed in Note 18.

Revenue recognition

Revenue is recognized when it is probable that the economic benefits associated with the transaction will flow to the Company and the amount of revenue can be reliably measured. Revenue from sale of crude oil is recognized when delivery has taken place and risks and rewards of ownership of the goods have passed to the customer. Crude oil shipped but not yet delivered to the customer is recorded as inventory in the balance sheet.

Expense recognition

Expenses are accounted for at the time the actual flow of the related goods or services occur, regardless of when cash or its equivalent is paid, and are reported in the financial statements in the period to which they relate.

Related parties

For the purposes of these 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 when making financial or operational decisions. In considering each possible related party relationship, attention is paid to the substance of the relationship, not merely the legal form.

Related parties include Company shareholders, key management personnel, associates and enterprises in which a substantial interest in the voting power is owned, directly or indirectly, by the Company's shareholder or key management personnel.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES

The preparation of the financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities during the reporting period. The most significant estimates are discussed below:

Oil and gas reserves

The cost of oil and gas properties is amortized at the field level using the unit-of-production method using proved developed reserves. Unit of production rates are based on oil and gas reserves estimated to be recoverable from existing facilities based on expected terms of the respective production agreements. The Company's reserve estimates include only crude oil and natural gas which management believes can be reasonably produced within the expected terms of the respective production agreements. The Company uses reserve estimates provided by internationally recognized petroleum engineers to assess the oil and gas reserves of its oilfields. In interim periods between external evaluations, the Company uses its in house petroleum engineers to estimate to assess the oil and gas reserves of its oil fields.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES (continued)***Oil and gas reserves (continued)*

Proved oil and gas reserves cannot be measured exactly. Reserves estimates are based on many factors related to reservoir performance that requires evaluation by the engineers interpreting the available data, as well as price and other economic factors. The reliability of these estimates at any point in time depends on both the quality and quantity of the technical and economic data, and the production performance of the reservoirs as well as engineering judgment. Consequently, reserve estimates are subject to revision as additional data become available during the producing life of reservoir.

When commercial reservoir is discovered, proved reserves are initially determined based on limited data from the first well or wells. Subsequent data may better define the extent of the reservoir and additional production performance, well tests and engineering studies will likely improve the reliability of the reserve estimate. The evolution of technology may also result in the application of improved recovery techniques such as supplemental or enhanced recovery projects, or both, which have the potential to increase the reserves beyond those envisioned during the early years of reservoir's producing life.

Proved oil and gas are the estimated quantities of crude oil, natural gas and natural gas liquids, which geological and engineering data demonstrate with reasonable certainty to be recoverable in the future years from known reservoirs under existing economic and operating conditions, i.e., prices and costs as of the date the estimate is made. Prices include consideration of changes in existing prices provided only by contractual arrangements, but not on escalations based upon future conditions. Proved developed reserves are those reserves, which can be expected to be recovered through existing wells with existing equipment and operating methods. Proved undeveloped reserves are those reserves, which are expected to be recovered from new wells on undrilled acreages or from existing wells where relatively major expenditure is required.

When determining oil and gas reserves, assumptions that were valid at the time of estimation may change when new information becomes available. Any changes could affect prospective depreciation and depletion rates and assets carrying values.

The calculation of the units of production rate of depreciation and depletion could be impacted to the extent that actual production in the future is different from current forecast production based on proved developed mineral reserves, which would generally arise as a result of significant changes in any of factors or assumptions used in estimating oil reserves.

These factors could include:

- Changes to proved developed oil reserves;
- The grade of oil reserves varying significantly from time to time;
- Differences between actual commodity prices and commodity price assumptions used in the estimation of oil reserves;
- Unforeseen operational issues at oil fields; and
- Changes in capital, operating oil producing, processing and reclamation costs, discounts rates and foreign exchange rates possibly adversely affecting the economic viability of oil reserves.

The majority of other property, plant and equipment are depreciated on straight line basis over their useful economic lives. Management reviews the appropriateness of assets useful economic lives at least annually; any changes could affect prospective depreciation and depletion rates and asset carrying values.

Abandonment and Site Restoration (decommissioning)

The Company estimates future dismantlement and site restoration cost for oil and gas properties with reference to the estimates provided from either internal or external engineers after taking into consideration the anticipated method of dismantlement and the extent of site restoration required in accordance with current legislation and industry practice. The amount of the obligation is the present value of the estimated expenditures expected to be required to settle the obligation adjusted for expected inflation and discounted using average long-term risk-free interest rates for emerging market sovereign debt adjusted for risks specific to the Kazakhstan market. The Company reviews site restoration provisions at each balance sheet date and adjusts it to reflect the current best estimate in accordance with IFRIC 1 "Changes in Existing Decommissioning, Restoration and Similar Liabilities".

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES (continued)***Abandonment and Site Restoration (decommissioning) (continued)*

Estimating the future closure costs involves significant estimates and judgments by management. Significant judgments in making such estimates include estimate of discount rate and timing of cash flow. The management made its estimate based on the assumption that cash flow will take place at the expected end of the licenses. Management of the Company believes that the interest rates on its debt financing shall provide best estimates of applicable discount rate. The discount rate shall be applied to the nominal amounts the managements expect to spend on site restoration in the future. The Company estimates future well abandonment cost using current year prices and the average long-term inflation rate.

4. RESTATEMENT OF COMPARATIVE INFORMATION

	Adjustment	As previously reported	Effect of corrections	As restated
Balance sheet as at December 31, 2005:				
Retained Earnings	1	3,290,713	30,337	3,321,050
Additional paid in capital	1	30,337	(30,337)	-
Balance sheet as at December 31, 2006:				
Property, plant and equipment	2	4,604,496	11,807	4,616,303
Inventory	2	146,747	(11,807)	134,940
Advances paid	3	528,268	(114,072)	414,196
Deferred tax asset	4	62,227	(62,227)	-
Trade payables	3	(917,087)	114,072	(803,015)
Deferred tax liability	4	-	(112,134)	(112,134)
Retained earnings	1&4	(3,843,321)	144,024	(3,699,297)
Statement of income for year ended December 31, 2006				
Income tax expense	4	117,018	174,361	291,379
Net profit for the year	4	552,608	(174,361)	378,247
Basic earnings per share		409		280

Adjustment 1

In December 2005 the Company acquired 150,000 of its own shares. The acquisition was offset against the receivable from the previous owner. The receivable had originally been discounted through the statement of income. The difference of 43,340 thousand Tenge between the par value of the shares and the discounted value of the receivable was treated as an equity transaction and recorded net of tax of 13,003 thousand Tenge in additional paid in capital at the amount of 30,337 thousand Tenge. The financial statements have been restated to reverse the discount through retained earnings.

Adjustment 2

Material and spare parts used for capital projects amounting to 11,807 thousand Tenge have been restated as construction in progress within property plant and equipment.

Adjustment 3

An amount of 114,072 thousand Tenge originally included within trade payables has been restated as payments relating to the payable balance had previously been included in advance payments.

Adjustment 4

Deferred tax liabilities in respect of property, plant and equipment were not recorded in 2006. The financial statements have been restated to reflect the deferred tax liability.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***5. INTANGIBLE ASSETS**

As at December 31, 2007 and 2006 intangible assets represented licenses for subsurface use and computer software.

6. PROPERTY, PLANT AND EQUIPMENT

The movement on property, plant, and equipment for the years ended December 31, 2007 and 2006 was as follows:

	Oil and gas properties	Buildings and constructions	Machinery and equipment	Vehicles	Other assets	Construction in progress (restated)	Total (restated)
Cost							
31-Dec-05	2,599,751	540,682	121,406	145,373	47,477	2,468,949	5,923,638
Additions	187,518	66,048	53,293	90,413	19,296	1,684,101	2,100,669
Transfers	841,129	25,693	5,053	313	–	(872,188)	–
Disposals	(19,218)	(11,497)	(2,555)	–	(596)	(2,076,055)	(2,109,921)
31-Dec-06	3,609,180	620,926	177,197	236,099	66,177	1,204,807	5,914,386
Additions	548,165	22,839	14,466	76,726	21,417	5,208,927	5,892,540
Transfers	(446,255)	(374,371)	(133,312)	171,109	3,771	779,058	–
Disposals	(38,444)	–	(1,686)	(5,797)	(2,449)	(1,040,845)	(1,089,221)
31-Dec-07	3,672,646	269,394	56,665	478,137	88,916	6,151,947	10,717,705
Accumulated depreciation:							
31-Dec-05	(723,921)	(26,789)	(14,531)	(36,899)	(7,174)	–	(809,314)
Charge	(447,230)	(15,842)	(11,863)	(29,525)	(7,541)	–	(512,001)
Disposals	19,218	1,412	2,400	–	202	–	23,232
31-Dec-06	(1,151,933)	(41,219)	(23,994)	(66,424)	(14,513)	–	(1,298,083)
Charge	(515,286)	(8,614)	(8,676)	(48,071)	(9,866)	–	(590,513)
Transfers	71,798	23,276	13,111	(106,981)	(1,204)	–	–
Disposals	7,029	–	1,232	2,409	1,017	–	11,687
31-Dec-07	(1,588,392)	(26,557)	(18,327)	(219,067)	(24,566)	–	(1,876,909)
Net book value:							
31-Dec-05	1,875,830	513,893	106,875	108,474	40,303	2,468,949	5,114,324
31-Dec-06	2,457,247	579,707	153,203	169,675	51,664	1,204,807	4,616,303
31-Dec-07	2,084,254	242,837	38,338	259,070	64,350	6,151,947	8,840,796

As at December 31, 2007, the Company pledged the property, plant and equipment to secure borrowings.

Within construction in progress the Company has KZT 3,531,774 thousand (2006: 32,082) relating to the exploration of the North Karpovskiy Field.

During the year the company wrote off KZT 783,982 of construction in progress expenditure related to the geological and geophysical expenditure in the statement of income (Note 21).

During 2006, Management wrote off part of Well G-70 the Company's largest exploration well as they believed that no commercial oil reserves would be found in the drilled direction. Management did not write off the top portion of the well as they believed it would be used to explore reserves in a different direction. In 2008 Management wrote off the remaining portion of this well (Note 30).

7. OTHER NON-CURRENT ASSETS

As at December 31, other non-current assets consisted of the following:

Description	2007	2006
Technological crude oil	124,636	172,733
Advances to vendors for property, plant and equipment	62,979	850,323
Production spare parts	188,523	285,669
	376,138	1,308,725

Technological crude oil represents oil in CPC and KTO pipelines.

Advances to vendors represented advances given for capital construction works.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***8. LOAN TO RELATED PARTY**

During 2006 the Company provided a KZT denominated non-interest bearing loan to Lancaster Group of KZT 420,000 thousand with a maturity in 2007. As at December 31, 2007 the loan was restructured and the balance transferred to related party receivables (Note 27).

9. INVENTORIES

As at December 31, inventories comprised:

Description	2007	2006
Spare parts	130,876	109,844
Crude oil	72,340	323
Fuel	11,123	6,821
Construction materials	7,520	1,298
Other materials	70,483	47,655
Total inventory	292,342	165,941
Less provision for obsolescence and impairment	(73,447)	(31,001)
Total inventory net of provisions	218,895	134,940

No inventory was pledged as at December 31, 2007 against bank loans.

The movements in obsolescence and impairment provision for the years ended December 31, were as follows:

Description	2007	2006
Reserve as at January 1	31,001	15,061
Additional provision for the year	42,446	15,940
Obsolescence reserve as at December 31	73,447	31,001

10. TRADE RECEIVABLES

Trade receivables are interest free and normally receivable within 30 days. All trade receivables are current as at December 31, 2007 and 2006.

11. ADVANCES PAID

As at December 31, prepayments comprised:

Description	2007	2006
Advances for raw materials	92,749	178,721
Advances for services	135,783	235,475
	228,532	414,196

12. OTHER CURRENT ASSETS

As at December 31, other current assets comprised:

Description	2007	2006
VAT recoverable	339,886	277,286
Receivables from sale of investments	–	112,000
Property tax prepaid	15,129	6,444
Due from employees	3,313	–
Other	44,490	49,963
	402,818	445,693

As at December 31, 2007, VAT recoverable consists of Tenge denominated VAT paid on local services provided and goods supplied by Kazakhstani suppliers.

Other includes the receivables prepaid expenses for insurance.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***13. BANK DEPOSITS**

Bank deposits represent short term deposits with original maturities greater than 3 months. The deposits on hand as at year are due to mature in April 2008 (2006: January, 2007) and have an interest rate of 6.5% (2006: 3%). All deposits are denominated in Tenge.

14. AVAILABLE FOR SALE SECURITIES

As December 31, 2006 available for sale securities consisted of shares of JSC "Pana Insurance" of KZT 120,000 thousand as well as shares and GDRs of JSC "E&P KazMunaiGas" of KZT 173,050 thousand. Both investments were denominated in KZT. As at December 31, 2007 all available for sale securities had been sold.

15. CASH AND CASH EQUIVALENTS

As at December 31, cash and cash equivalents comprised the following:

Description	2007	2006
KZT bank account	7,472	338,199
US Dollar bank account	33,432	168,906
Cash on hand	2,841	1,493
Cash in transit	6,269	-
	50,014	508,598

As at December 31, 2007 and 2006 current accounts with banks were interest free.

16. CHARTER CAPITAL

At December 31, 2007 the Company's authorized, issued and paid-in charter capital comprised 1,350,000 (2006: 1,350,000) common shares.

In December 2005 the Company purchased back 150,000 of its own shares from KKM Holding JSC.

Following is a list of shareholders:

	2007		2006	
	Share	Number of Shares	Share	Number of Shares
Lancaster Group Pte. Ltd.	89.5%	1,342,500	79%	1,342,500
Oman CPC Company	0.5%	7,500	1%	7,500
Treasury shares	10%	150,000	10%	150,000
	100%	1,500,000	100%	1,500,000

Common shares give the holders the right to participate in the management of the Company and shareholders are permitted one vote per share.

The Company did not pay or declare any dividends during the year ended December 31, 2007 and 2006. In 2008 the Company declared dividends in the amount USD 10,000 thousand (Note 30).

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***17. INTEREST-BEARING LOANS**

At December 31, interest-bearing loans comprised:

<i>In thousands of tenge</i>	Original Currency	Date of Issue	Maturity Date	Interest rate	Frequency of payments	2007	2006
Long-term borrowings							
				till 23 September 10.73%; from 24 September	interest - monthly; principal - at maturity	-	320,657
KazkommertsBank	USD	Jul 2006	Dec 2008	14%			
		Dec 2004-	Nov 2006-	14.0%-14.5%	interest - monthly; principal - at maturity	-	194
Bank Turan Alem	KZT	Jul 2005	Feb 2010				
Long-term borrowings							
						-	320,851
Short-term borrowings							
				till 23 September 10.73%; from 24 September	interest - monthly; principal - at maturity	5,558,410	1,993,730
KazkommertsBank	USD	Jul 2006	Dec 2008	14%			

Kazkommertsbank

On July 17, 2006 the Company opened a credit line with Kazkommertsbank of USD 80,000 thousand for two years. Under this credit line Kazkommertsbank provided a number of short-term and long-term loans to the Company for capital investments and to replenish its working capital. Original interest on the loans was 10.7 % per annum. The interest rate can be varied at the discretion of the bank in the event the bank's cost of capital changes. Starting from September 2007, the Bank charges 14% per annum. As of December 31, 2007 the Company has withdrawn KZT 5,553,410 thousand or 58% of the total credit line. Company pledged the movable and immovable property and right for subsurface usage on North Karpovski and Kokzhide. In 2008 the Bank prolonged the credit line by the end of the year and increased the interest rate to 16% per annum. The Company is a guarantee to the third parties for: Aktas LLP in the amount of USD 10,000 thousand.

18. ABANDONMENT AND SITE RESTORATION LIABILITY

The abandonment and site restoration liability has been recorded in the financial statements to reflect the cost of restoring well sites to their original condition. The cost has been estimated based on management's best estimates and available historical data.

The movements in the abandonment and site restoration liability for the years ended December 31, were as follows:

Description	2007	2006
Abandonment and site restoration liability as at January 1	157,199	68,758
Unwinding of discount	25,268	4,813
Revision of estimates	63,793	-
Used during the year	(9,216)	(1,317)
Additional provision for the year	4,004	84,945
Abandonment and site restoration liability as at December 31	241,048	157,199

As Kazakh laws and regulations concerning environmental assessments and cleanups evolve, the Company may incur future costs the amount of which is currently indeterminable. Such costs, when known, will be provided for as new information, legislation and estimates evolve.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***19. TRADE ACCOUNTS PAYABLE**

At December 31, 2007 and 2006, the ten largest suppliers accounted for 80% and 85% of the total trade accounts payable, respectively. Trade accounts payable are represented by payables to suppliers and denominated in KZT.

20. COST OF SALES

The composition of cost of sales for the years ended December 31, was as follows:

Description	2007	2006
Salaries and related costs	588,844	326,310
Depreciation and amortization	570,128	497,140
Royalty	213,301	187,625
Services	108,442	86,203
Security	94,601	39,067
Repair and maintenance	83,440	43,401
Fuel and electricity	70,156	65,022
Materials	61,745	16,928
Taxes and fees	58,439	31,910
Provision for inventory impairment	37,063	–
Transportation expenses	18,063	37,751
Other	85,266	29,762
Total	1,989,488	1,361,119
Change in work in progress and finished goods:		
Work in progress and finished goods in progress at 1 January	173,056	103,503
Work in progress and finished goods at 31 December	(196,796)	(173,056)
Net changes in work in progress and finished goods	(23,740)	(69,553)
Total cost of sales	1,965,748	1,291,566

21. GEOLOGICAL AND GEOPHYSICAL EXPENSES

Geological and geophysical expenses for the year ended December 31, were divided between fields as follows:

	2007	2006
Kumsai field	611,625	160,094
Kokgide field	51,279	57,547
North Karpovskoye field	141,209	–
	804,113	217,641

Geological and geophysical expenses for the years ended December 31, 2007 and 2006 represent costs related to seismic works, geophysical research, and exploration of reserves.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***22. GENERAL AND ADMINISTRATIVE EXPENSES**

The composition of general and administrative expenses for the year ended December 31, was as follows:

Description	2007	2006
Professional services	516,289	160,645
Salaries and related costs	279,842	239,043
Insurance	78,537	357,155
Charity	75,042	27,700
Business trips	72,408	28,649
Operational expenses	36,082	–
Bank commissions	30,316	46,357
Depreciation and amortization	27,608	21,606
Fines and penalties	24,128	2,881
Rent and office maintenance	20,282	21,593
Training	18,091	7,595
Communication	13,694	21,121
(Recovery) / provision charge	9,672	(187,462)
Operating taxes	9,250	6,931
Provision for inventory obsolescence	5,383	15,940
Other expenses	33,036	37,357
Total	1,249,660	807,111

23. SELLING EXPENSES

The composition of selling expenses for the year ended December 31, was as follows:

Description	2007	2006
Transportation	845,431	640,179
Customs fees	18,536	16,809
Salaries and related expenses	3,908	4,115
Oil loading	208	191
Other expenses	4,251	9,390
Total	872,334	670,684

Transportation expenses in 2007 and 2006 represent costs related to transportation of oil through the pipeline, which is owned by CPC that provides oil pipeline transportation services throughout Kazakhstan.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***24. FINANCE COSTS**

The composition of finance costs for the year ended December 31, was as follows:

Description	2007	2006
Interest income	277	1,170
Interest expense		
Interest expenses – bank loans	312,196	161,306
Interest on advance payments from customers	26,556	22,536
Unwinding of discount for liquidation fund	25,268	4,813
Penalty on early settlement of the loan	–	30,198
Imputed interest	–	13,813
Interest expenses – Neston's loan	–	34
Total finance cost	364,020	232,700
Net finance cost	363,743	231,530

In 2007 and 2006 interest on advance payments from customers mostly represents interest charged on the advance from KazMunayGaz Trade House, a subsidiary of national company “KazMunayGaz”. The Company sells oil on a prepayment basis to its major customers KazMunayGaz Trade House. According to the contract the Company is obliged to pay interest for prepayment from the date of payment till the bill of lading date in amount of LIBOR+2.5%, for the years ended December 31, 2007 and 2006.

25. INCOME TAXES

The Company is subject to income tax of 30% on taxable profit as determined under the laws of the Republic of Kazakhstan. Income tax expense consisted of the following for the year ended December 31:

	2007	2006
Corporate income tax	983,043	615,805
Excess profit tax	686,586	–
Current income tax	1,669,629	615,805
Corporate income tax	(206,916)	(324,426)
Excess profit tax	(66,348)	–
Deferred income tax	(273,264)	(324,426)
Income tax expense	1,396,365	291,379

A reconciliation of the income tax expense applicable to profit before income tax at the statutory income tax rate against current income tax expense was as follows for the year ended December 31:

	2007	2006
Accounting profit before income tax	2,387,976	669,626
Corporate income tax expense at 30%	716,392	200,888
Excess profit tax at 21%	501,474	–
Provision charge / (reverse)	2,901	(56,239)
Other non-temporary differences	175,598	146,730
Income tax expense reported in the accompanying financial statements	1,396,365	291,379

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***25. INCOME TAXES (continued)**

Deferred tax balances calculated by applying the statutory tax rates in effect at the respective balance sheet dates plus the estimated excess profit tax rates the Company is expected to incur against temporary differences between the tax basis of assets and liabilities and the amounts reported in the financial statements, consisted of the following at December 31:

	2007	2006
Deferred tax assets:		
Losses carried forward	291,252	-
Property, plant and equipment	31,890	-
Accrued expenses	128,595	3,479
Inventory	37,458	5,047
	489,195	8,526
Deferred tax liabilities:		
Property, plant and equipment	(319,614)	(112,434)
Intangible assets	(8,451)	(8,226)
	(328,065)	(120,660)
Net deferred tax asset / (liability)	161,130	(112,134)

The Republic of Kazakhstan's tax code covers various taxes such as value added tax, corporate income tax, and payroll taxes, together with others. The tax code has not been in force for significant periods, in contrast to more developed market economies; therefore, implementing regulations are often unclear or non-existent. Accordingly, few precedents with regard to issues have been established. Often, different opinions regarding legal interpretation exist both among and within government ministries and various inspectorates; thus creating uncertainties and areas of conflict. Tax declarations, together with other legal compliance areas (as examples, customs and currency control matters) are subject to review and investigation by a number of authorities that are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Kazakhstan substantially more significant than typically found in countries with more developed tax systems. Generally, tax declarations remain open and subject to inspection for a period of five years. Management believes that it has adequately provided for tax liabilities in the accompanying financial statements; however, the risk remains that relevant authorities could take different positions with regard to interpretative issues and the effect could be significant.

26. EARNINGS PER SHARE

Earnings per share is calculated by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the period, excluding the average number of ordinary shares purchased by the Company and held as treasury shares (Note 16).

The following reflects the income and share data used in the basic earnings per share computation:

	2007	2006
Weighted average number of ordinary shares outstanding	1,350,000	1,350,000
Profit for the year attributable to equity holders	991,610	378,247
Basic earnings per share, KZT	735	280

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***27. RELATED PARTY TRANSACTIONS**

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the related party relationships for those related parties with whom the Company entered into significant transactions for the year ended December 31, 2007 and 2006 or had significant balances outstanding at December 31, 2007 and 2006 are detailed below.

Balances and transactions with related parties of the Company as at and for the year ended December 31, 2007 and 2006 consisted of the following:

Revenues

Revenues	Nature of Transactions	2007	2006
Lancaster Group Kazakhstan	Sales of shares	–	112,033
KazInvestBank	Interest expenses	–	1,152
ERC Holding	Interest expenses	–	119
		–	113,304

Expenses

Expenses	Nature of Transactions	2007	2006
Lancaster Group Kazakhstan	Professional services	301,899	29,872
Lancaster Group Kazakhstan	Sales of shares	–	112,033
Pana Insurance	Insurance	–	356,142
Oman CPC Company	Transportation	143,451	67,782
Neston Production Ltd.	Interest expenses	–	34
LFK Arlan	Interest free loan	12,200	–
		457,550	565,863

Account Receivables and Advances paid

	Nature of Transactions	2007	2006
Lancaster Group Kazakhstan	Interest free loan and consulting fee	2,283,506	138,000
LFK Arlan	Interest free loan	20,930	36,330
KKM Holding JSC	Interest free loan	10,000	370
Lancaster Realty	Interest free loan	29,903	112,000
ERC Holding	Interest free loan	–	129
		2,344,339	286,829

Accounts payable

	Nature of Transactions	2007	2006
Pana Insurance	Insurance	–	38,060
Oman CPC Company	Transportation	26,416	11,414
		26,416	49,474

Accounts receivable are unsecured, interest free with no fixed terms of repayment.

Accounts payable are interest free and normally payable within 30 days.

Shares of Pana Insurance were sold in August 2007

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***27. RELATED PARTY TRANSACTIONS (continued)****Compensation to key management personnel**

Key management personnel totaled 6 persons as at December 31, 2007 and 2006. Total compensation to key management personnel included in personnel costs in the accompanying statement of income amounted to KZT 199,861 thousand and KZT 161,315 thousand for the years ended December 31, 2007 and December 31, 2006, respectively. Compensation to key management personnel consists of contractual salary.

28. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Company, in connection with its activities, is exposed to various financial risks associated with its financial instruments. Financial instruments are comprised primarily of cash and cash equivalents, trade receivables, other receivables, accounts payable and loans.

Interest rate risk

The Company's only interest rate risk relates to interest payable associated with its loans. The Company does not enter into any hedging instruments to mitigate any potential risk, as management does not believe the interest rate risk associated with the loan obligation is significant. The interest rates on the loans are fixed subject to variation at the discretion of the bank in the event the bank's cost of capital changes. All existing loans mature by July 2008. As at the date of this report there has been no change in interest rates reported in these financial statements. Management does not expect any changes to the date of maturity.

Liquidity risks

Liquidity risk arises from the possibility that customers may not be able to settle obligations to the Company within the normal terms of trade. To manage this risk the Company enters into prepayment contracts with the majority of its customers.

Cash flow requirements are monitored on a regular basis and management ensures that sufficient funds are available to meet any commitments as they arise. The management of the Company believes that any possible fluctuations of future cash flows associated with a monetary financial instrument will not have a material impact on the Company's operations.

The table below summarizes the maturity profile of the Company's financial liabilities at December 31, 2007 based on contractual undiscounted payments:

December 31, 2007	On demand	Less than 3 months	3-12 months	1-5 years	more than 5 years	Total
Borrowings	-	5 000	5 553 410	-	-	5 558 410
Trade and other payables	747 807	857 641	-	-	-	1 605 448
	747 807	862 641	5 553 410	-	-	7 163 858

Year ended

December 31, 2006	On demand	Less than 3 months	3-12 months	1-5 years	more than 5 years	Total
Borrowings	-	-	1 993 730	320 851	-	2 314 581
Trade and other payables	920 783	7 122	-	-	-	927 905
	920 783	7 122	1 993 730	320 851	-	3 242 486

Commodity price risk

The Company is exposed to commodity price risk, since oil prices are determined by world market. The Company does not hedge this risk.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***28. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)****Credit risks**

Credit risks or the risk of counterparties defaulting, is controlled by the application of credit approvals, limits and monitoring procedures. The extent of the Company's credit exposure is represented by the balance of accounts receivable. While the Company may be subject to losses up to the contract value of the instruments in the event of non-performance by its counterparts, it does not expect such losses to occur.

Currency risk

Currency risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates. The Company's operations are carried out in the Republic of Kazakhstan and, as such, a significant portion of the Company's business is transacted in Kazakh Tenge. Company's management believes that any possible fluctuations of foreign exchange rates will not have a material impact on the financial position of the Company and the results of its operations.

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant, of the Company's profit before tax (due to changes in the fair value of monetary assets and liabilities).

	<i>Increase / decrease in US dollar rate</i>	<i>Effect on profit before tax</i>
2007	5%	241 044
	-5%	(241 044)
2006	5%	106 153
	-5%	(106 153)

Fair value of financial instruments

Set out below is a comparison by category of carrying amounts and fair values of all of the Company's financial instruments that are carried in the balance sheet:

	Carrying amount		Fair value	
	2007	2006	2007	2006
Financial assets:				
Trade and other receivables	1,352,460	954,092	1,352,460	954,092
Cash and cash equivalents and Bank deposits	108,710	515,495	108,710	515,495
Available for sale securities	-	293,050	-	293,050
Financial aid	-	183,522	-	183,522
Financial liabilities:				
Short term interest bearing loans	5,558,410	2,314,581	5,558,410	2,314,581
Trade and other payables	721,391	871,309	721,391	871,309

The fair value of borrowings is based on cash flows discounted using the market interest rates. Fair values of available-for-sale investments, bank deposits, trade and other receivables, cash and cash equivalents and trade and other payables approximate their carrying amounts due to their short maturity.

29. COMMITMENTS AND CONTINGENCIES**Commitment**

As at December 31, 2007 Company had commitments for a minimal work program in an amount of KZT 13,063,200 thousand (2006: KZT 13,806,170 thousand).

Social and education commitments

As required by the Contract with the Government, the Company is obliged to spend: (i) KZT 22,550 thousand per annum to finance social infrastructure and (ii) 1.5 percent from the capital expenditures incurred during the year for education purposes of the citizens of Kazakhstan on an annual basis until the end of the Contract.

NOTES TO THE FINANCIAL STATEMENTS (continued)*In thousands of tenge***29. COMMITMENTS AND CONTINGENCIES (continued)****Legal actions and claims**

The Company is subject to various legal proceedings related to business operations, such as property damage claims. The Company does not believe that pending or threatened claims of these types, individually or in aggregate, are likely to have any material adverse effect on the Company's financial position or results of operations.

The Company assesses the likelihood of material liabilities arising from individual circumstances and makes provision in its financial statements only where it is probable that events giving rise to the liability will occur and the amount of the liability can be reasonably estimated. No provision has been made in these financial statements for any of the contingent liabilities mentioned above.

Tax contingencies

Kazakhstan legislative acts and regulations are not always clearly written and their interpretation is subject to the opinions of the local tax inspectors and the Ministry of Finance of the Republic of Kazakhstan. Instances of inconsistent opinions between local, regional and national tax authorities are not unusual. The current regime of penalties and interest related to reported and discovered violations of Kazakhstan laws, decrees and related regulations are severe. Penalties include confiscation of the amounts at issue (for currency law violations), as well as fines of generally 50% of the taxes unpaid. Interest is assessed at 20%. As a result, penalties and interest can result in amounts that are multiples of any incorrectly reported taxes resulting in an understatement.

The Company believes that it has paid or accrued all taxes that are applicable. Where practice concerning the provision of taxes is unclear, the Company has accrued tax liabilities based on management's best estimate. The Company's policy is to recognize provisions in the accounting period in which a loss is deemed probable and the amount is reasonably determinable.

Because of the uncertainties associated with the Kazakhstan tax system, the ultimate amount of taxes, penalties and interest, if any, may be in excess of the amount expensed to date and accrued at December 31, 2007. It is not practicable to determine the amount of unasserted claims that may

Environmental matters

The Company may also be subject to loss contingencies relating to regional environmental claims that may arise from the past operations of the related fields in which it operates. As Kazakhstani laws and regulations evolve concerning environmental assessments and site restoration, the Company may incur future costs, the amount of which is currently indeterminable due to such factors as, the ultimate determination of responsible parties associated with these costs and the Government's assessment of respective parties' ability to pay for the costs related to environmental reclamation. The calculation of abandonment and site restoration is considered in Note 16. It is the opinion of management that such costs will not have a material effect on the financial condition of the Company and accordingly no provisions for future environmental claims or penalties are included in the accompanying financial statements.

However, depending on any unfavorable claims or penalties assessed by the Kazakhstani regulatory agencies, it is possible that the Company's future results of operations or cash flow could be materially affected in a particular period.

30. SUBSEQUENT EVENTS**Dividends**

Dividends of KZT 1,199,971 thousand were declared and paid April 30, 2008. Shareholders agreed to offset the dividends payable against related party debt as consideration for the dividends.

Exploration Well G-70

At the beginning of 2008 the Company wrote off the remaining portion of exploration well G-70 with a net book value of KZT 716,327 thousand.

**SUPPLEMENTAL INFORMATION – INFORMATION ABOUT OIL AND GAS
PRODUCING ACTIVITIES - UNAUDITED**

In thousands of tenge

PROVED OIL AND GAS RESERVE QUANTITIES (unaudited)

As at years ended December 31, 2006 Kokzhide and Kumsai field received an independent appraisal of their proved reserves.

As determined by independent reservoir engineers, McDaniels that performed the appraisal of oil reserves as at June 30, 2006 the following information presents the balances of proved oil and gas reserve quantities as at December 31, 2006.

The McDaniels follows the SPE/WPC (Society of Petroleum Engineers/World Petroleum Congress) definition of recoverable hydrocarbon reserves and follows SPE reserves estimation.

In determining proved reserve quantities, proved reserves are the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

Proved developed reserves are those reserves, which are expected to be recovered through existing wells with existing equipment and operating methods. Proved undeveloped reserves are those reserves, which are expected to be recovered as a result of future investments to drill new wells, to re-complete existing wells and/or install facilities to collect and deliver the production from existing and future wells.

<i>In thousands of tones</i>	2007 (unaudited)	2006 (unaudited)
Proved developed reserves as at January 1,	427,824	534,550
Production for the year	(112,799)	(106,726)
Proved developed reserves as at December 31,	315,025	427,824
Total proved (developed and undeveloped) reserves as at December 31, 2007	782,275	895,074