# Amtel-Vredestein N.V.

## Consolidated Financial Statements
## For the Year Ended 31 December 2007

1030376

## AMTEL-VREDESTEIN N.V.

### CONTENTS

## AMTEL-VREDESTEIN N.V.

**STATEMENT OF THE EXECUTIVE BOARD'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007**

The consolidated financial statements comprise the financial statements of Amtel-Vredestein N.V. and its subsidiaries (hereinafter referred to as "Amtel Group" or the "Group").

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the independent auditors' report set out on pages 2 to 3, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements of Amtel Group.

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

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

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

The Executive Board is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the consolidated financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with IFRS;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Detecting and preventing fraud and other irregularities.

Petr Zolotarev
Director A

Vadim Pesochinskiy
Director B

# Auditors' report

### Report on the financial statements

We have audited the accompanying financial statements 2007of Amtel-Vredestein N.V., Enschede. The financial statements consist of the consolidated financial statements and the company financial statements. The consolidated financial statements comprise the consolidated balance sheet as at December 31, 2007 profit and loss account, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The company financial statements comprise the company balance sheet as at December 31, 2007 the company profit and loss account for the year then ended and the notes.

### Management's responsibility

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Netherlands Civil Code for the preparation and fair presentation of the company financial statements in accordance with Part 9 of Book 2 of the Netherlands Civil Code, and for the preparation of the executiveboard report in accordance with Part 9 of Book 2 of the Netherlands Civil Code. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the 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.

### Auditor's responsibility

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with Dutch law. This law requires 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 auditor's 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 adverse audit opinion.

**Basis for adverse opinion**

The financial statements have been prepared using accounting principles based on the going concern assumption. In our view this constitutes a departure from International financial Reporting Standards as adopted by the European Union and from Part 9 of the Netherlands Civil code in the current circumstances. On the basis of the current information on the company's financial position and circumstances the going concern assumption is inappropriate.

The company communicated the following information to the users of the Company's financial information through press releases:

- ".. production at the Kirov and Voronezh manufacturing facilities has remained suspended as a result of the working capital shortage faced by the Group. The production suspension does not affect Vredestein Banden BV where production is at its normal level. The Company continues to explore a number of options to reduce the high levels of debt under which the Russian part of the Group continues to operate. The options being explored include the sale of certain of the Company's assets and/or divisions or the Group as a whole. The Company has now received payment acceleration requests from SRT and several of the banks lending to its Russian operations under its existing facilities and SRT's claim has been filed with the courts. The Company will be unable to fulfil these requests unless an alternative settlement solution can be agreed. The Company is currently in discussions with SRT and the lenders and hopes to negotiate a standstill agreement which will enable it to pursue value realisation options. "(press release of October 24, 2008)

- "The Company has been progressing proposals to address its challenging financial position and ensure its viability as a going concern, including a debt restructuring exercise and the business combination with OJSC SIBUR-Russian Tyres ("SRT"). The success of the proposed debt restructuring was contingent on the connected proposals for a business combination with SRT, which, as announced by the Company, terminated on 30 September. The Company has now received payment acceleration requests from several of its lending banks and is in continuing discussions with the lending banks and is exploring value realisation options, as announced in its press release on 24 October 2008" and

  "Based on the above, serious doubts have arisen about the likely success of the ongoing restructuring exercises conducted by the Company. As long as these doubts are not resolved, it is unclear whether the annual accounts 2007 can be drawn up on a "going concern" basis" and

  "The Company now announces that as a result hereof it will not be in a position to make available to its shareholders annual accounts 2007 on a going concern basis by 31 October 2008." (press release of October 31, 2008).

- "Amtel Vredestein N.V. ("AVNV") announces that its subsidiary company OJSC AMTEL-VREDESTEIN ("OJSC AV"), the holding company of the group's Russian business, is no longer able to satisfy its creditors' demands. The Executive Board of AVNV has determined that, due to the financial difficulties faced by AVNV, it will not be able to provide any additional finance to OJSC AV. This development may have consequences for the going concern status of AVNV given a number of guarantees provided by AVNV in favour of the creditors of OJSC AV". And

  "AVNV will not be in a position to publish audited accounts for the year ended 31 December 2007 in the near future due to its ongoing financial difficulties and the resulting uncertainty with regard to its going concern status." (press release of December 15, 2008)

- "The FY 2007 unaudited annual accounts and annual report of Amtel-Vredestein N.V. have been prepared on a going concern basis. The executive directors of Amtel-Vredestein N.V. are aware of the fact that there is currently uncertainty about the ability of Amtel-Vredestein N.V., to continue as a going concern. However, the executive directors are of the view that the annual accounts should be prepared on a going concern basis in view of the fact that a twelve month period has lapsed since 31 December 2007 and there being no certainty that the business will not be continued. However, this approach may not give a fair view going forward. Should the business or parts thereof not be continued in the future, this could have a material adverse effect on the operations, financial condition, assets and/or results of the Company, which, at this stage, cannot be quantified." And

  "The executive directors feel that preparing the FY2007 unaudited annual accounts on a going concern basis together with the inclusion of a warning about the possible inability to continue as a going concern as set out above gives the fairest view possible in the circumstances." And "However, in the view of the executive directors, it should not be relied upon that the FY2007 unaudited annual accounts and annual report 2007 have been prepared on a correct basis, and therefore that they give a true and fair view, given the uncertainties as to the business being able to continue as a going concern." (press release of January 2, 2009).

In addition the following elements have a significant impact on whether the going concern assumption is applicable:

- alledged default on certain of the loan obligations
- significant difficulty for the company to raise additional capital and cash required to fund ordinary business, redeem loan obligations and fund capital investment plans.

We have not received any other than the above mentioned information on the company's financial position and circumstances that could support applying the going concern assumption for the 2007 financial statement. Consequently the appropriate accounting principle for the financial statements should be current value.

The principal effects on the financial statements of the matter giving rise to our modification are not reasonably quantifiable by us. Moreover it is impracticable to set-out a full description of the omitted disclosures that are required under these circumstances by the applicable financial reporting frameworks.

**Adverse opinion with respect to the consolidated financial statements**

In our opinion, because of the significance of the matter described in the Basis for adverse opinion paragraph, the consolidated financial statements do not give a true and fair view of the financial position of Amtel-Vredestein N.V. as at December 31, 2007, and of its result and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Netherlands Civil Code.

**Adverse opinion with respect to the company financial statements**

In our opinion, because of the significance of the matter described in the Basis for adverse opinion paragraph, the company financial statements do not give a true and fair view of the financial position of Amtel-Vredestein N.V. as at December 31, 2007and of its result for the year then ended in accordance with Part 9 of Book 2 of the Netherlands Civil Code.

**Report on other legal and regulatory requirements**

Pursuant to the legal requirement under 2:393 sub 5 part e of the Netherlands Civil Code, we report, to the extent of our competence, that the executive board report is consistent with the financial statements as required by 2:391 sub 4 of the Netherlands Civil Code.

Deloitte Accountants B.V.

A.J.E. Jansman RA.

**AMTEL-VREDESTEIN N.V.**
**CONSOLIDATED STATEMENT OF OPERATIONS**
**FOR THE YEAR ENDED 31 DECEMBER 2007**
***In million USD, except earnings per share***

| | Notes | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|---|
| **Continuing operations** | | | |
| Revenue | 10 | 994 | 768 |
| Cost of sales, excluding depreciation and amortisztion | | (705) | (536) |
| Gross profit before depreciation and amortization | | 289 | 232 |
| Depreciation and amortization charges related to cost of sales | | (55) | (45) |
| **Gross profit** | | **234** | **187** |
| Distribution expenses | 11 | (118) | (84) |
| Administrative expenses | 12 | (98) | (65) |
| Research and development expenses | | (7) | (7) |
| Excess of fair value on acquisition | 9(ii) | - | 22 |
| Other operating income | | 4 | - |
| Other operating expense | 15 | (28) | (12) |
| Impairment of long lived assets | 14 | (136) | - |
| Restructuring costs | 16 | - | (3) |
| (Loss)/profit from operating activities | | (149) | 38 |
| Finance income | | 5 | 8 |
| Finance expenses | 17 | (75) | (53) |
| Foreign exchange (losses)/gains | | (3) | 15 |
| (Loss)/profit before tax | | (222) | 8 |
| Income tax expense | 18 | (20) | (7) |
| (Loss)/profit from continuing operations | | (242) | 1 |
| **Discontinued operations** | | | |
| Loss from discontinued operation | 7 | - | (6) |
| **Net loss** | | **(242)** | **(5)** |
| *Attributable to:* | | | |
| Minority interest | | 1 | - |
| Equity holders of the Parent | | (243) | (5) |
| Basic and diluted loss per share, USD | 31 | (3.57) | (0.07) |

The consolidated statement of operations is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 13 to 79.

## AMTEL-VREDESTEIN N.V.

### CONSOLIDATED BALANCE SHEET
### AS AT 31 DECEMBER 2007
***In million USD***

| | Notes | 31 December 2007 | 31 December 2006 |
|---|---|---|---|
| **ASSETS** | | | |
| *Non-current assets* | | | |
| Property, plant and equipment | 19 | 606 | 547 |
| Intangible assets | 20 | 238 | 344 |
| Financial assets | 21 | - | 13 |
| Advances | 22 | - | 27 |
| Deferred tax assets | 18 | 8 | 9 |
| | | 852 | 940 |
| *Current assets* | | | |
| Financial assets | 21 | 6 | 11 |
| Inventories | 23 | 202 | 193 |
| Trade and other receivables | 24 | 250 | 242 |
| Cash and cash equivalents | 25 | 22 | 28 |
| | | 480 | 474 |
| Assets classified as held for sale | 8 | 73 | - |
| | | 553 | 474 |
| **TOTAL ASSETS** | | **1 405** | **1 414** |
| **EQUITY AND LIABILITIES** | | | |
| *Total Equity attributable to the equity holders of the parent* | 26 | | |
| Issued capital | | 1 | 1 |
| Additional paid in capital | | 474 | 460 |
| Foreign currency translation reserve | | 58 | 22 |
| Accumulated losses | | (324) | (81) |
| | | 209 | 402 |
| *Minority interest* | 26(iii) | 9 | 8 |
| Total Equity | | 218 | 410 |
| *Non-current liabilities* | | | |
| Retirement benefit obligation | 27 | 34 | 34 |
| Finance lease liabilities – long term | 29 | 15 | 21 |
| Deferred tax liabilities | 18 | 58 | 60 |
| Loans and borrowings | 28 | 253 | 239 |
| | | 360 | 354 |
| *Current liabilities* | | | |
| Bank overdraft | 28 | 35 | 26 |
| Finance lease liabilities – short term | 29 | 7 | 6 |
| Trade and other payables | 30 | 268 | 203 |
| Loans and borrowings | 28 | 490 | 415 |
| | | 800 | 650 |
| Liabilities directly associated with assets classified as held for sale | 8 | 27 | - |
| Total liabilities | | 1 187 | 1 004 |
| **TOTAL EQUITY AND LIABILITIES** | | **1 405** | **1 414** |

The consolidated balance sheet is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 13 to 79.

## AMTEL-VREDESTEIN N.V.

**CONSOLIDATED STATEMENT OF CASH FLOWS**
**FOR THE YEAR ENDED 31 DECEMBER 2007**
***In million USD***

| | Notes | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Net result for the year | | (242) | (5) |
| *Non-cash adjustments:* | | | |
| Depreciation and amortization expense | | 65 | 57 |
| Excess of the acquirer's share in net indentifiable assets over the cost of acquisition | | - | (22) |
| Interest expense | | 72 | 51 |
| Interest income | | (5) | (7) |
| Impairment of long lived assets | | 136 | - |
| Impairment loss recognized on financial assets | | 2 | 4 |
| Loss on disposal of property, plant and equipment | | 7 | 3 |
| Gain on sale of discontinued operations | | - | (2) |
| Changes in fair value of financial instruments | | (1) | (1) |
| Income tax expense | | 20 | 7 |
| Equity settled employee benefits | | 14 | 3 |
| Foreign exchange losses/(gains) | | 3 | (15) |
| Operating cash flows before changes in working capital and provisions, income taxes and interest paid | | 71 | 73 |
| Decrease/(increase) in inventories | | 7 | (11) |
| Decrease in provisions | | (3) | (3) |
| Increase in trade and other receivables | | (1) | (26) |
| Increase/(decrease) in trade and other payables | | 63 | (12) |
| Cash flows from operations before income taxes and interest paid | | 137 | 21 |
| Income tax paid | | (17) | (8) |
| Cash flows generated from operating activities | | 120 | 13 |
| **INVESTING ACTIVITIES** | | | |
| Acquisition of property, plant and equipment | | (108) | (67) |
| Acquisition of intangible assets | | (3) | (3) |
| Proceeds from disposal of investments/ return of loans provided | | 8 | 29 |
| Acquisition of investments/loans provided | | (13) | (2) |
| Acquisition of subsidiaries, net of cash acquired | | (11) | (128) |
| Proceeds from sales of discontinued operations, net of cash disposed | | - | (1) |
| Proceeds from disposal of property, plant and equipment | | 7 | 2 |
| Interest received | | 4 | 5 |
| Cash flows used in investing activities | | (116) | (165) |

The consolidated statement of cash flows is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 13 to 79.

## AMTEL-VREDESTEIN N.V.

**CONSOLIDATED STATEMENT OF CASH FLOWS (CONTINUED)**
**FOR THE YEAR ENDED 31 DECEMBER 2007**
***In million USD***

| | Note | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|---|
| **FINANCING ACTIVITIES** | | | |
| Interest paid | | (69) | (46) |
| Proceeds from borrowings | | 844 | 498 |
| Repayment of borrowings | | (794) | (346) |
| Contribution by shareholder | | - | 3 |
| Cash flows (used in)/from financing activities | | (19) | 109 |
| Net decrease in cash and cash equivalents | | (15) | (43) |
| Cash and cash equivalents at beginning of year | 25 | 2 | 42 |
| Effects of foreign currency translation on cash and cash equivalents | | - | 3 |
| Cash and cash equivalents at end of year | 25 | (13) | 2 |

The consolidated statement of cash flows is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 13 to 79.

## AMTEL-VREDESTEIN N.V.

### CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
### FOR THE YEAR ENDED 31 DECEMBER 2007
***In million USD***

| | Notes | Issued capital | Additional paid-in capital | Foreign currency translation reserve | (Accumulated losses)/ Retained earnings | Total equity attributable to the equity holders to the parent | Minority interest | Total equity |
|---|---|---|---|---|---|---|---|---|
| Balance at 1 January 2006 | | 1 | 457 | (11) | (76) | 371 | 7 | **378** |
| Foreign currency translation | | - | - | 33 | - | 33 | 1 | **34** |
| Loss for the period | | - | - | - | (5) | (5) | - | **(5)** |
| Equity settled employee benefits | 36 | - | 3 | - | - | 3 | - | **3** |
| *Total recognised income and expenses for the period* | | *-* | *-* | *33* | *(5)* | *28* | *-* | ***28*** |
| **Balance at 31 December 2006** | | **1** | **460** | **22** | **(81)** | **402** | **8** | **410** |
| Balance at 1 January 2007 | | 1 | 460 | 22 | (81) | 402 | 8 | **410** |
| Foreign currency translation | | - | - | 36 | - | 36 | - | **36** |
| (Loss)/profit for the period | | - | - | - | (243) | (243) | 1 | **(242)** |
| Equity settled employee benefits | 36 | - | 14 | - | - | 14 | - | **14** |
| *Total recognised income and expenses for the period* | | *-* | *-* | *36* | *(243)* | *(207)* | *1* | ***(206)*** |
| **Balance at 31 December 2007** | | **1** | **474** | **58** | **(324)** | **209** | **9** | **218** |

The consolidated statement of changes in equity is to be read in conjunction with the notes to and forming part of the consolidated financial statements set out on pages 13 to 79.

## 1. BACKGROUND

### *(i).* General information

Amtel-Vredestein N.V., further referred to as "the Parent Company", or "the Company" was incorporated by Amtel Luxemburg S.A. as a private company with limited liability (Besloten Vennootschap) on 30 July 2002 in accordance with the Civil Law of the Netherlands. In August 2005 the Company was reorganised into a public limited liability company (Naamloze Vennootschap). The Company operates under the laws of the Netherlands, with its registered office at Ir.E.L.C.Schiffstraat 370, 7545 RD Enschede, the Netherlands.

These consolidated financial statements comprise the Parent Company and its subsidiaries (further referred to as "the Group" or "Amtel Group").

### *(ii).* Operations

The Group operates in the tyre manufacturing and distribution business. The Group includes a number of tyre production facilities located in Russia and in the Netherlands. The plants produce a wide range of tyres for a variety of vehicles, including passenger cars, trucks, agricultural and military vehicles and bicycles. The distribution business includes a number of retail outlets and a wholesale division. The products of the Group are distributed in Russia, the Netherlands and other countries.

### *(iii).* Russian business environment

The Russian Federation has been experiencing political and economic change that has affected, and may continue to affect, the activities of the enterprises operating in this environment. Consequently, operations in the Russian Federation involve risks that typically do not exist in other, more mature markets. The accompanying consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from the management's assessment.

## 2. BASIS OF PREPARATION

### *(i).* Going concern

Amtel Group has started its modernization program in 2002 and since then has always implemented a growth and expansion strategy. The expansion program included acquisitions of Vredestein Banden, Moscow Tyre Factory and a retail and wholesale distribution network.

During the course of these years, the Group has spent over USD 800 million to implement the aforementioned strategy and as a result the Group has turned cash positive from operating activities in 2007. However, since the majority of the expansion was financed through loans and borrowing and since some of the investments did not meet the forecasted targets, the Group has continued to be cashflow negative. As at 31 December 2007 current liabilities exceeded current assets by USD 274 million and in July 2008 the Group has defaulted on some of its loan obligations. Furthermore, due to the shortage of cash, the Group has been unable to meet its trade creditor terms and to finalise the Voronezh expansion project. These conditions raise substantial doubt about the Group's ability to continue as a going concern.

At the date of approval of these financial statements the management is leading negotiations with potential strategic investors. However, taking into account the events, described in detail in Note 38, the Executive Board is unable to say whether the Group will be able to generate sufficient cash flows, therefore the continuity of the Group is currently uncertain, in which case the underlying assumption of going concern may no longer be appropriate. In this event, the value of fixed assets, intangible and other assets might become impaired and additional liabilities may be incurred. Please refer to the Statement of the Executive Board's responsibilities for the preparation and approval of the consolidated financial statements for the year ended 31 December 2007.

### *(ii).* Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the EU further to the IAS Regulation (EC 1606/2002). Management has reviewed the standards not endorsed by the EU as at the date of the issue of the financial statements and has concluded that those are not applicable to the Group.

### *(iii).* Basis of measurement

The consolidated financial statements are prepared on the historical cost basis, except for the revaluation of certain non current assets and financial instruments. The principle accounting policies are set out below.

## 3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and have been applied consistently by the Group entities.

Certain comparative amounts have been reclassified to conform to the current year's presentation. In addition, the comparative statement of operations has been re-presented as if an operation discontinued during the current period had been discontinued from the start of the comparative period (Refer to Note 7).

### *(i).* Basis of consolidation

The consolidated financial statements include the accounts of Amtel-Vredestein N.V. and all subsidiaries. A list of significant subsidiaries has been included in Note 37.

***Subsidiaries***

Subsidiaries are those enterprises controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

***Associates and joint ventures***

Associates are those entities in which the Company has significant influence, but not control, over the financial and operating policies. Joint ventures are those entities over whose activities the Company has joint control, established by contractual agreement and requiring unanimous consent for strategic financial and operating decisions. Associates and joint ventures are accounted for using the equity method (equity accounted investees). The consolidated financial statements include the Company's share of the income and expenses of equity accounted investees, after adjustments to align the accounting policies with those of the Company, from the date that significant influence or joint control commences until the date that significant influence or joint control ceases. When the Company's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued except to the extent that the Company has an obligation or has made payments on behalf of the investee.

***Transactions eliminated on consolidation***

Intragroup balances and transactions, and any unrealised gains arising from intragroup transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with jointly controlled enterprises are eliminated to the extent of the Company's interest in the enterprise. Unrealised gains resulting from transactions with jointly controlled entities are eliminated against the investment in the jointly controlled entity. Unrealised losses are eliminated in the same way as unrealised gains except that they are only eliminated to the extent that there is no evidence of impairment.

### *(ii).* Business combinations

***Acquisitions***

In accounting for the acquisition of subsidiaries the purchase accounting method is used. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued, and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are initially measured at fair value at the acquisition date. The excess of the cost of acquisition over the fair value of the Company's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the statement of operations. The assets and liabilities from business combinations arising from transfers of interests in entities that are under the control of the Group are accounted for at the carrying amounts recognized previously.

***Disposals***

The gain or loss on the sale of a subsidiary, representing the difference between the consideration received and the net assets of the subsidiary including attributable goodwill, is recognised in the statement of operations.

***(iii).* Foreign currencies**

The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency), which reflects the economic substance of its operations. The functional currency of the Company is the Euro ("EUR") and its subsidiaries' are the currencies of the countries of their domicile.

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

Management of the Group has chosen to present consolidated financial statements in the USD, which is convenient for the current and potential users of these consolidated financial statements. All financial information presented in USD has been rounded to the nearest million.

The translation from functional currency into presentation currency is performed as follows. Assets and liabilities are expressed in USD using exchange rates prevailing at the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are classified as equity and transferred to the Group's foreign currency translation reserve. Such exchange differences are recognised in the income statement for the period in which the foreign operation is disposed of. Goodwill and fair value adjustments arising on business combinations are treated as assets and liabilities of the respective operation and translated at the closing rate

The exchange rates used by the Group in the preparation of the consolidated financial statements are as follows:

| | 31 December 2007 | 31 December 2006 |
|---|---|---|
| **Year-end rates** | | |
| RUR / 1 US Dollar | 24.55 | 26.33 |
| Euro / 1 US Dollar | 1.46 | 1.32 |
| **Average rates** | | |
| RUR / 1 US Dollar | 25.58 | 27.19 |
| Euro / 1 US Dollar | 1.37 | 1.26 |

### *(iv).* Property, plant and equipment

***Owned assets***

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads.

Cost of property, plant and equipment acquired as part of the business combination is determined by reference to its fair value at the date of the business combination, which is determined by an independent appraiser.

Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant and equipment.

Interest related to loans provided for investments in qualifying property, plant and equipment which were not acquired through business combinations is capitalised as a part of investment in property, plant and equipment. Capitalisation of interest costs is suspended during extended periods in which active development is interrupted.

***Leased assets***

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Plant and equipment acquired by way of finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and impairment losses.

***Subsequent expenditure***

Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, is capitalised with the carrying amount of the component being written off. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is recognised in the statement of operations as an expense as incurred.

***Depreciation***

Depreciation is charged to the statement of operations on a straight-line basis over the estimated useful lives of the individual assets. Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use.

The estimated average useful lives are as follows:

| | |
|---|---|
| Buildings | 8 to 30 years; |
| Plant and equipment | 3 to 10 years; |
| Fixtures and fittings | 3 to 7 years. |

The residual value, depreciation method and useful lives are reassessed annually.

***(v).* Intangible assets**

***Goodwill***

All business combinations are accounted for by applying the purchase method. Goodwill arising on acquisitions represents the excess of the cost of the acquisition over the fair value of the net identifiable assets. Goodwill is stated at cost less accumulated impairment losses. For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergy of the combination. Cash-generating units to which goodwill is allocated are tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in subsequent periods.

Negative goodwill arising on acquisitions represents the excess of the fair value of the net identifiable assets acquired over the cost of acquisition. Negative goodwill is recognised directly in the statement of operations.

***Internally-generated intangible assets - research and development expenditure***

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from development (or from the development phase of an internal project) is recognised if, and only if, all of the following have been demonstrated:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- the intention to complete the intangible asset and use or sell it;
- the ability to use or sell the intangible asset;
- how the intangible asset will generate probable future economic benefits;
- the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- the ability to measure reliably the expenditure attributable to the intangible asset during its development.

The amount initially recognised for internally-generated intangible assets is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria listed above. Where no internally-generated intangible asset can be recognised, development expenditure is charged to profit or loss in the period in which it is incurred.

Subsequent to initial recognition, internally-generated intangible assets are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets acquired separately

*Other intangible assets*

Other intangible assets, which have finite useful lives, are stated at cost less accumulated amortisation and impairment losses.

Amortisation is charged to the statement of operations on a straight-line basis over the estimated useful lives of the intangible assets unless such lives are indefinite. Intangible assets are amortised from the date the asset is available for use.

The estimated useful lives are as follows:

| | |
|---|---|
| Land lease rights | 42 years; |
| Research and development | 6 years; |
| Trade marks | 10 years; |
| Other | 3 to 6 years. |

The residual value, amortization method and useful lives are reassessed annually.

**(vi). Non-current assets held for sale**

Non-current assets and disposal groups held for sale are stated at the lower of carrying amount and fair value less costs to sell. No depreciation is recorded for non-current assets held for sale.

**(vii). Financial assets**

Investments are recognised and derecognised on trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

The Group's financial assets have been classified as loans and receivables. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

***Effective interest method***

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period. Income is recognised on an effective interest basis for all debt instruments.

***Loans and receivables***

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

***Impairment of financial assets***

Financial assets are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

Objective evidence of impairment could include:

- Significant financial difficulty of the issuer or counterparty; or
- Default or delinquency in interest or principal payments; or
- It becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period, as well as observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in 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 through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

***Derecognition of financial assets***

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

### *(viii).* Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The cost of inventories is based on the weighted average principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

### *(ix).* Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

### *(x).* Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of impairment loss (if any). Where it is not possible to estimate the recoverable amount of the individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in the profit and loss.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

### *(xi).* Financial liabilities

Financial liabilities are classified into the following specified categories:

- financial guarantee contract liabilities; and
- other financial liabilities.

***Financial guarantee contract liabilities***

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies set out above.

***Other financial liabilities***

Other financial liabilities, including loans and borrowings, are initially measured at fair value, net of transaction costs. Financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

***Provisions and accruals***

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

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

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

Loans and borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, loans and borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the statement of operations over the period of the borrowings on an effective interest basis.

*(xii).* **Financial instruments**

The Group enters into a variety of derivative financial instruments to manage its exposure to interest rate, including interest rate swaps and caps.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship. The Group does not apply hedge accounting for any of its derivatives.

A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be.

### *(xiii).* Leasing

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

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

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

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

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

### *(xiv).* Income tax

Income tax for the year comprises current and deferred tax. Income tax is recognised in the statement of operations except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill; initial recognition of assets or liabilities that affect neither accounting nor taxable profit; and investments in subsidiaries where the Parent Company is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

### *(xv).* Revenue

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

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

### *(xvi).* Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time when the assets are substantially ready for their intended use or sale. Investment income earned on temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

### *(xvii).* Employee benefits

***Defined contribution plans***

The Group's Russian subsidiaries are legally obliged to make defined contributions to the Russian Federation ("RF") State Pension Fund. The Group's contributions to the RF State Pension Fund relating to defined contribution plans are charged to the statement of operations in the period to which they relate.

In the RF all state social contributions, including contributions to the RF State Pension Fund, are collected through a unified social tax ("UST") calculated by the application of a regressive rate from 26% to 2% of the annual gross remuneration of each employee. UST is allocated to three state social funds, including the RF State Pension Fund, where the rate of contributions to that fund vary from 20% to 2%, depending on the annual gross remuneration of each employee.

Contributions to defined contribution retirement benefit plans are recognised as an expense when employees have rendered service.

***Defined benefit plans***

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets is deducted.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the statement of operations on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in the statement of operations. The discount rate is the yield at the balance sheet date on AAA credit rated bonds that have maturity dates approximating to the terms of the Group's obligations. The calculation is performed by a qualified actuary using the project unit credit method.

Actuarial gains and losses in calculating the Group's obligation in respect of a plan, to the extent that any cumulative unrecognised actuarial gain or loss exceeds 10 per cent of the greater of the present value of the defined benefit obligation and the fair value of plan assets, that portion is recognised in the statement of operations over the expected average remaining working lives of the employees participating in the plan. Otherwise, the actuarial gain or loss is not recognised.

***Share-based payment transactions***

Equity-settled share-based payments to employees and others providing similar services are measured at the fair value of the equity instruments at the grant date.

The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest. At each balance sheet date, the Group revises its estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognised in profit or loss over the remaining vesting period, with a corresponding adjustment to the equity-settled employee benefits reserve.

***(xviii).*** **Adoption of new and revised standards**

***Standards and Interpretations effective in the current period***

For the year ended 31 December 2007 the Group has adopted IFRS 7 "Financial Instruments: Disclosures" which is effective for annual reporting periods beginning on or after 1 January 2007, and the consequential amendment to IAS 1 "Presentation of Financial Statements". The impact of the adoption of IFRS 7 and the changes to IAS 1 has been to expand the disclosures provided in these financial statements regarding the Group's financial instruments and management of capital (refer to Note 32).

Four Interpretations issued by the International Financial Reporting Interpretations Committee are effective for the current period. These are: IFRIC 7, "Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies"; IFRIC 8, "Scope of IFRS 2; IFRIC 9, Reassessment of Embedded Derivatives"; and IFRIC 10, "Interim Financial Reporting and Impairment". The adoption of these Interpretations has not led to any changes in the Group's accounting policies.

***Early adoption of Standards and Interpretations***

In addition, the Group has elected to adopt the following Standards and Interpretations in advance of their effective dates:

- IAS 23 (Revised) "Borrowing Costs" (effective for accounting periods beginning on or after 1 January 2009);
- IFRS 8 "Operating Segments" (effective for accounting periods beginning on or after 1 January 2009).

The revisions to IAS 23 have had no impact on the Group's accounting policies. The principal change to the Standard, which was to eliminate the previously available option to expense all borrowing costs when incurred, has no impact on these financial statements because it has always been the Group's accounting policy to capitalise borrowing costs incurred on qualifying assets.

IFRS 8 is a disclosure Standard which has resulted in a re-designation of the Group's reportable segments (refer to Note 5), but has no impact on the reportable results or financial position of the Group.

***Standards and Interpretations in issue but not yet adopted***

At the date of authorisation of these consolidated financial statements, other than the Standards adopted by the Group in advance of their effective dates (as described above) the following Standards and Interpretations were in issue but not yet effective:

- IAS 1 "Presentation of Financial Statements (amended)" – effective 1 January 2009;
- IAS 27 "Consolidation and Separate Financial Statements (amended due to revision of IFRS 3)" – effective 1 July 2009;
- IAS 28 "Investments in Associates (amended due to revision of IFRS 3)" – effective 1 July 2009;
- IAS 31 "Investments in Joint Ventures (amended due to revisions of IFRS 3)" – effective 1 July 2009;
- IAS 32 "Financial Instruments: Presentation (amendment)" – effective 1 January 2009;
- IAS 36 "Impairment of Assets (amendment)" – effective 1 January 2009;
- IAS 38 "Intangible Assets (amendment)" – effective 1 January 2009;
- IAS 39 "Financial Instruments: Recognition and Measurement (amendment)" – effective 1 January 2009;
- IAS 40 "Investment Property (amendment)" – effective 1 January 2009;
- IAS 41 "Agriculture (amendment)" – 1 January 2009;
- IFRS 2 "Share-based payments (amendment)" – effective 1 January 2009;
- IFRS 3 "Business Combinations (revised on applying the acquisition method)" – effective 1 July 2009;
- IFRIC 11: "IFRS 2 - Group and Treasury Share Transactions" (effective 1 March 2007);
- IFRIC 12: "Service Concession Arrangements" (effective 1 January 2008); and
- IFRIC 13: "Customer Loyalty Programmes" (effective 1 July 2008);
- IFRIC 14: "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" (effective 1 January 2008);
- IFRIC 15: "Agreements for the Construction of Real Estate" (effective 3 July 2008);
- IFRIC 16: "Hedges of a Net Investment in a Foreign Operation" (effective 3 July 2008).

The impact of the adoption of these standards and interpretations in the preparation of the consolidated financial statements in future periods is currently being assessed by management.

## 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES

In the application of the Group's accounting policies, which are described in Note 3, the directors are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

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

**(i). Critical judgments in applying accounting policies**

The following are the critical judgements, apart from those involving estimations (below), that the directors have made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the consolidated financial statements.

***Going concern***

The consolidated financial statements have been prepared on the basis that Group will continue as a going concern. As described in Note 2(i), in the event that Group will not be successful in generating sufficient cash flows, the continuity of the Group could be uncertain, in which case the underlying assumption of going concern may not be appropriate.

***Impairment of goodwill, tangible and intangible assets***

In order to assess whether any impairment losses should be recognised in relation to goodwill, tangible and intangible assets, the Group performed a review, with the assistance of an independent expert, as described in Notes 3(v) and 3(x).

The following key assumptions were used in determining the recoverable amount of the cash generating unit:

- A constant growth model was used to estimate the terminal value for the discounted cash flow analysis. A terminal growth of 4% was considered in estimating the terminal value;
- The terminal value was derived at the end of the five year interim period. It was anticipated that the acquired company would have achieved a stable long-term rate of growth;
- A pre-tax weighted average cost of capital of 14.2% to 16.15% was used as a discount rate for determination of the recoverable amount (Refer to Note 20(i)).

As a result of the impairment test a loss of USD 136 million was recognised in the consolidated financial statements (Refer to Note 14).

**(ii). Key sources of estimation uncertainty**

***Allowance for slow-moving inventories***

Allowance for slow moving inventories are made to reduce excess inventories to their estimated net realisable values, as necessary. The Group records inventory allowances based on historical experiences with customers and current and forecasted demand for the inventory.

***Allowance for trade and other receivables***

The allowance for trade and other receivables is based on management's evaluation of the volume of the receivables outstanding, past experience and general economic conditions.

*Defined Benefit Plan*

In 2007 employees of Vredestein Banden B.V. and its subsidiaries were eligible to participate in a defined benefit plan (Refer to Note 27). The obligations in relation to the defined benefit plan were acquired as part of the business combination and have been continued since.

The principal assumptions used for the purposes of actuarial valuations were as follows:

| | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| *Active employee members* | | |
| Number | 1,244 | 1,139 |
| Average age | 43 | 43 |
| Average past services | 15 | 17 |
| Individual salary increase (dependant on age) | 2.5%-5.0% | 0.0%-2.5% |
| Employee turnover (dependant on age) | 0.0%-7.0% | 0.0%-7.0% |
| Discount rate | 5.70% | 4.75% |
| Expected return on assets | 5.45% | 5.00% |

The mortality level was assessed in accordance with the Dutch Mortality table of 2007.

*Income tax*

As described in Note 35, Russian taxation is at a relatively early stage of development and is subject to varying interpretations and inconsistencies. The Group has made a provision for taxes based on its interpretation of current and previous legislation.

Deferred tax assets are reviewed at each balance sheet date and reduced to the extent that it is no longer probably that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. The estimation of that probability includes judgements based on expected performance. Various factors are considered in assessing the probability of the future recovery of deferred tax assets, including past operating results, operational plan, expiration of tax losses and tax planning strategies. Actual results may differ from those estimates.

*Share based payments*

The fair value of the options granted is measured using a binomial option model, taking into account the terms and conditions upon which the options were granted. The Group recognizes the expense over the vesting period based on an estimate of the number of equity instruments expected to vest. The amount recognized as an expense is adjusted to reflect the actual number of share options that vest.

*Useful lives of assets*

The useful economic lives of the Group's assets are determined by management at the time the asset is acquired and regularly reviewed for appropriateness.

## 5. SEGMENT REPORTING

The Group has adopted IFRS 8 "Operating Segments" in advance of its effective date, with effect from 1 January 2007. IFRS 8 requires that operating segments be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segments and assess its performance. In contrast, the predecessor Standard IAS 14 "Segment Reporting" required the entity to identify two sets of segments (business and geographical), using a risk and rewards approach, with the entity's system of internal financial reporting to key management personnel' serving only as a starting point for the identification of such segments. As a result, following adoption of IFRS 8, the identification of the Group's reportable segments have been identified and presented.

In prior years, segment information reported externally was analysed primarily on the basis of two geographic segments; Russia and Europe. In addition, the Group reported as a secondary segment, two business segments; tyres and raw materials (which was discontinued in 2006). However, information reported to the Group's chief operating decision maker for the purpose of resource allocation and assessment of segment performance is more specifically focused and also includes the new segment "retail and distribution" which was relatively minor in 2006 but has significantly grown in 2007 as a result of expansion and additional business acquisitions.

The following is an analysis of the Group's revenue and results by reportable segment. Amounts reported for the prior year have been restated to conform with the requirements of IFRS 8.

**2007**

| *In million USD* | European manu-facturing | Russian manu-facturing | Retail and distribution | Corporate | Elimination | Consoli-dated |
|---|---|---|---|---|---|---|
| Revenue from external customers | 397 | 345 | 252 | - | - | 994 |
| Inter-segment revenue | 5 | 94 | 2 | - | (101) | - |
| Segment revenues | 402 | 439 | 254 | - | (101) | 994 |
| Segment result | 14 | (55) | (161) | (46) | 6 | (242) |
| Segment assets | 586 | 1 170 | 146 | 123 | (620) | 1 405 |
| Goodwill, included in segment assets | 134 | 64 | - | - | - | 198 |
| Segment liabilities | 368 | 906 | 319 | 214 | (620) | 1 187 |
| Capital expenditure | (31) | (103) | (4) | - | - | (138) |
| Interest revenue | 1 | 4 | - | - | - | 5 |
| Interest expense | (11) | (46) | (2) | (13) | - | (72) |
| Income tax expense | (6) | (5) | 3 | (12) | - | (20) |
| Depreciation / amortisation | (27) | (34) | (4) | - | - | (65) |
| Impairment of long lived assets | - | (15) | (121) | - | - | (136) |
| Inventory impairment | - | - | (7) | - | - | (7) |
| Impairment losses recognized on receivables | (1) | (6) | (7) | - | - | (14) |

**2006**

| *In million USD* | European manu-facturing | Russian manu-facturing | Retail and distribution | Corporate | Elimination | Consolidated |
|---|---|---|---|---|---|---|
| Revenue from external customers | 336 | 327 | 105 | - | | 768 |
| Inter-segment revenue | 5 | 10 | - | - | (15) | - |
| Segment revenues | 341 | 337 | 105 | - | (15) | 768 |
| Discontinued operations | | | | | | 49 |
| Consolidated revenue | | | | | | 817 |
| Profit from continuing operations | 14 | (2) | (9) | (1) | (1) | 1 |
| Discontinued operations | | | | | | (6) |
| Net loss | | | | | | (5) |
| Segment assets | 508 | 626 | 277 | 176 | (173) | 1,414 |
| Goodwill, included in segment assets | 119 | 61 | 101 | - | - | 281 |
| Segment liabilities | 326 | 345 | 287 | 214 | (168) | 1,004 |
| Capital expenditure | (23) | (33) | (5) | - | - | (61) |
| Interest revenue | 2 | 5 | - | - | - | 7 |
| Interest expense | (9) | (17) | (2) | (23) | - | (51) |
| Income tax expense | (2) | (6) | 1 | - | - | (7) |
| Depreciation / amortisation | (24) | (30) | (3) | - | - | (57) |
| Inventory impairment | - | - | - | - | - | - |
| Impairment losses recognized on receivables | (3) | (1) | (1) | - | - | (5) |
| Restructuring charges | - | (3) | - | - | - | (3) |

Segment result represents the result of each segment without allocation of corporate costs including interest on Group loans and borrowings, equity settled employee benefits and directors' fees. This is the measure reported to the chief operating decision maker for the purpose of resource allocation and assessment of segment performance.

The Group's revenues from its major products and services were as follows:

| | Revenue from external customers | |
|---|---|---|
| | 2007 | 2006 |
| Tyres | 876 | 724 |
| *- PCT* | *612* | *508* |
| *- light-truck tyres* | *108* | *85* |
| *- truck tyres* | *63* | *52* |
| *- agricultural tyres* | *78* | *61* |
| *- bicycle tyres* | *10* | *12* |
| *-other tyre products* | *5* | *6* |
| Parts and accessories | 103 | 7 |
| Other operations | 15 | 37 |
| Revenue from continuing operations | 994 | 768 |
| Discontinued operations | - | 49 |
| **Consolidated revenue** | **994** | **817** |

The Group operates in two principle geographic areas – Russia (Russian manufacturing and retail and distribution) and Europe (European manufacturing). The European manufacturing takes place in the Netherlands and is distributed into a number of countries in Europe.

The Group's revenue from external customers and information about its segment assets (non-current) by geographical location are detailed below:

| | **Russia** | | **Europe** | | **Elimination** | | **Consolidated** | |
|---|---|---|---|---|---|---|---|---|
| *In million USD* | **2007** | **2006** | **2007** | **2006** | **2007** | **2006** | **2007** | **2006** |
| Sales to external customers | 597 | 530 | 397 | 287 | - | - | 994 | 817 |
| Inter-segment revenue | 21 | 11 | 5 | 4 | (26) | (15) | - | - |
| Segment revenues | 618 | 541 | 402 | 291 | (26) | (15) | 994 | 817 |
| **Non-current assets** | **491** | **611** | **361** | **329** | **-** | **-** | **852** | **940** |

In 2007, included in revenues arising from sale of tyres, are revenues of approximately USD 251 million which arose from sales to the Group's largest customer.

## 6. RESTRUCTURING OF MANUFACTURING

In July 2005 the Group commenced a restructuring of its tyre production. As part of this process, it was decided to stop the production of truck and bicycle tyres in Voronezh and the number of employees within Voronezh and Kirov factories were substantially reduced. In December 2005 the Group sold its Krasnoyarsk Tyre Complex as well as Volgograd Carbon Black Plant.
In December 2006 the Group sold its 100% owned subsidiary OOO Khimvololokno Amtel-Kuzbass (Kemerovo Chemical Fibre Plant).

In November 2007, the Group decided to cease production of tyres in the Moscow Tyre Plant-M due to the significantly higher cost of production in the capital. The property and the associated assets and liabilities have been classified as held for sale – refer to Note 8. The Group has retained title to the brands and production assets, and is in the process of transferring these assets to the Voronezh facility.

As a result of the various restructuring activities the Group has either disposed of or discontinued the production of unprofitable truck tyres, bicycle tyres as well as non-core products such as carbon black and chemical fibers. The Group has substantially improved its product mix and cost structure.

## 7. DISCONTINUED OPERATIONS

Discontinued operations in 2006 comprise of the disposal of the Group's chemical fiber production activity in the Kemerovo Chemical Fiber Plant ("Kemerovo"). The results of the discontinued operations and net cash flows of Kemerovo are set out below.

| *In million USD* | **Year ended 31 December 2006** |
|---|---|
| **Loss for the year from discontinued operations** | |
| Revenues | 49 |
| Expenses | (57) |
| Loss before tax | (8) |
| Gain on sale of discontinued operations | 2 |
| Loss for the year from discontinued operations | (6) |
| | |
| **Cash flows from discontinued operations** | |
| Net cash used in operating activities | (2) |
| Cash flows from financing activities | 3 |
| | |
| **Net cash flows** | 1 |

Details of the assets and liabilities disposed of are set out below:

| *in million USD* | **Year ended 31 December 2006** |
|---|---|
| Property, plant and equipment | - |
| Current assets | 6 |
| Liabilities | (8) |
| Group's share of the net liabilities disposed of | (2) |
| Gain / (Loss) on disposal | 2 |
| | |
| **Consideration received** | - |

In 2007 the Group disposed of three insignificant regional outlets OOO "AV-TO Kirov", OOO "Russhina Master" and OOO "Nord Tyre".

## 8. ASSETS CLASSIFIED AS HELD FOR SALE

On 22 November 2007 the Supervisory Board approved a plan to cease tyre production in the Moscow Tyre Plant – M facility and dispose of the land lease rights, building and associated assets and liabilities. The disposal is consistent with the Group's long-term business restructuring policy to improve the efficiency of the business and reduce its level of debt (Refer to Note 6). The disposal was completed in March 2008 for a consideration of USD 77 million and no impairment was recognized on reclassification of the assets as held for sale at 31 December 2007.

The assets and liabilities which have been classified as held for sale are included in the Russian manufacturing segment – refer to Note 5. The major classes of assets and liabilities classified as held for sale at the balance sheet date are as follows:

| *USD million* | **31 December 2007** |
|---|---|
| **Non-current assets** | |
| Property, plant and equipment | 40 |
| Intangible assets | 9 |
| Investments in equity securities (long-term) | 8 |
| Loans originated (long-term) | 3 |
| | **60** |
| **Current assets** | |
| Trade and other receivable | 11 |
| Financial assets | 2 |
| | **13** |
| **Assets classified as held for sale** | **73** |

| *USD million* | 31 December 2007 |
|---|---|
| **Non-current liabilities** | |
| Long-term loans and borrowings | (23) |
| | **(23)** |
| **Current liabilities** | |
| Trade and other payables | (4) |
| | **(4)** |
| **Liabilities directly associated with assets classified as held for sale** | **(27)** |
| **Net Assets** | **46** |

## 9. ACQUISITIONS

### *(i).* Acquisitions in 2007

In July 2007 the Group acquired a 100% participating interest in OOO "Dakar plus", a retail store, specializing in the sale of tyres and other car related accessories.

The Group determined the fair values of property, plant and equipment and intangible assets, as well as the allocation of the purchase price to the assets, liabilities and assumed contingent liabilities with the assistance of an independent appraiser. The fair value adjustment on acquisition was not material. The effect of the acquisition on the Group's assets and liabilities was as follows:

| | in million USD |
|---|---|
| Property, plant and equipment | 1 |
| Current assets | 1 |
| Net assets at the date of acquisition | 2 |
| Goodwill on acquisition | 1 |
| **Consideration paid in cash** | **3** |

From the date of acquisition to 31 December 2007, OOO "Dakar plus" was not material in terms of revenues and results to the Group. If the combination had occurred from the beginning of the year, the loss and revenues of the Group would not have been changed materially.

### *(ii).* Acqusitions in 2006

*Acquisition of Moscow Tyre Plant - M*

In August 2006, the Group acquired 100% of the shares of CJSC Moscow Tyre Plant-M, as well as 100% of the shares of LLC ShinTech, the OJSC Moscow Tyre Plant affiliate which holds title to most of the modern equipment acquired in the transaction (together referred to as "Moscow Tyre Plant" or "MTP").

The Group determined the fair values of the identifiable assets, liabilities and contingent liabilities of the acquired companies at the date of acquisition. The determination of the fair values of property, plant and equipment and intangible assets, as well as the allocation of the purchase price to the assets, liabilities and assumed contingent liabilities was performed with the assistance of an independent appraiser.

The effect of the acquisition on the Group's assets and liabilities was as follows:

| | USD million |
|---|---|
| Property, plant and equipment | 99 |
| Intangible assets – land lease rights and brand name | 14 |
| Current assets | 10 |
| Current liabilities | (11) |
| Non-current liabilities | (13) |
| Deferred tax liabilities recognized | (12) |
| Net assets at the date of acquisition | 87 |
| Excess of fair value on acquisition | (22) |
| Consideration | 65 |
| | |
| Payable consideration | 51 |
| Additional agency fees | 14 |
| | |
| **Consideration** | **65** |

The purchase consideration was settled in Roubles and USD and was equivellent to USD 50 million at the date of settlement. As at 31 December 2007, an equivellent to USD 13 million remains outstanding and has been recorded as payable to related parties – refer to Note 30. At the date of acquisition the cash balance was USD 2 million.

The additional agency fees amounting to USD 14 million consisted of payments to companies associated with the sellers in the form of agency agreements. These fees have been recognized as costs directly attributable to acquisition.

Excess of fair value on acqusition in the amount of USD 22 million has been recognised in the consolidated statement of operations. The excess of fair value on acquisition was due to significant restructuring and investment required to the production facility. Furthermore, the Group would benefit from its significant scale of operations, not available to MTP on a stand alone basis.

The acquired company previously reported under Russian GAAP. Thus it was impracticable to determine the pre-acquisition carrying amount under IFRS and this information is not presented in these consolidated financial statements.

MTP contributed USD nil million of revenue and a loss before tax of USD 2 million from the date of acquisition to 31 December 2006. If the combination had occurred on 1 January 2006, the revenue of the Group from continuing operations would have been USD 6 million and the loss for the year from continuing operations would have been USD 5 million.

***Aquisition of retail regional chains***

In 2006 the Group acquired 100% share of a number of retail businesses specializing in sales of tyres and other car related accessories and services in numerous regions throughout Russia. As of December 31, 2006, the Company's trade network consisted of 115 outlets.

The Group determined the fair values of the identifiable assets, liabilities and contingent liabilities of the acquired companies at the date of acquisition. The determination of the fair values of property, plant and equipment and intangible assets, as well as the allocation of the purchase price to the assets, liabilities and assumed contingent liabilities was performed with the assistance of an independent appraiser.

The effect of the acquisition on the Group's assets and liabilities was as follows:

| | USD million |
|---|---|
| Property, plant and equipment | 12 |
| Current assets | 15 |
| Non-current liabilities | (2) |
| Net assets at the date of acquisition | 25 |
| Goodwill arising on acquisition | 41 |
| Consideration | 66 |
| | |
| Payable consideration | 25 |
| Additional agency fee | 41 |
| | |
| **Consideration** | **66** |

The purchase consideration was settled in a number of installements in Roubles and USD and totalled an equivellent of USD 4 million in 2005, USD 52 million in 2006 and USD 8 million in 2007.

The additional agency fees amounting to USD 41 million consisted of payments to companies associated with the sellers in the form of agency agreements. These fees have been recognized as costs directly attributable to acquisition.

At the date of acquisition, the cash balance was USD nil.

Goodwill arose on acquisition of retail regional chains because the cost of the combination included a control premium paid to acquire the retail business. The consideration paid for the combination effectively included amounts in relation to the benefit of expected synergies, revenue growth and future market development. At the time of acquisition these benefits were not recognised separately from goodwill as the future economic benefits arising from them could not have been reliably measured.

The acquired company previously reported under Russian GAAP. Thus it was impracticable to determine the pre-acquisition carrying amount under IFRS and this information is not presented in these consolidated financial statements.

The retail regional chains contributed USD 37 million of revenue and a loss before tax of USD 1 million from the date of acquisition to 31 December 2006. If the combination had occurred on 1 January 2006, the revenue of the Group from continuing operations would have been USD 74 million and the loss for the year from continuing operations would have been USD 2 million.

***Acquisition of wholesale auto parts and tyre distributor***

In October 2006, the Group acquired 100% of shareholders equity of regional wholesale auto parts, tyre and accessories distributor LLC Trade House Pigma, based in Nizhny Novgorod.

The Group determined the fair values of the identifiable assets, liabilities and contingent liabilities of the acquired company at the date of acquisition. The determination of the fair values of property, plant and equipment and intangible assets, as well as the allocation of the purchase price to the assets, liabilities and assumed contingent liabilities were performed with the assistance of an independent appraiser.

The effect of the acquisition on the Group's assets and liabilities was as follows:

| | USD million |
|---|---|
| Property, plant and equipment | 2 |
| Identifiable intangible assets – customer network | 12 |
| Current assets | 96 |
| Current liabilities | (97) |
| Deferred tax liabilities | (3) |
| Net assets at the date of acquisition | 10 |
| Goodwill arising on acquisition | 21 |
| Consideration paid in cash | 31 |
| | |
| Payable consideration | 3 |
| Additional agency fee | 28 |
| | |
| **Consideration** | **31** |

The purchase consideration was settled in Roubles and USD and amounted to USD 30 million at the date of settlement. At the date of acquisition, the cash balance was USD 2 million.

The additional agency fees amounting to USD 28 million consisted of payments to companies associated with the sellers in the form of agency agreements. These fees have been recognized as costs directly attributable to acquisition.

Goodwill arose on acquisition of regional wholesale auto parts, tyre and accessories distributor because the cost of the combination included a control premium paid to acquire the wholesale business. The consideration paid for the combination effectively included amounts in relation to the benefit of expected synergies, revenue growth and future market development. At the time of acquisition these benefits were not recognised separately from goodwill as the future economic benefits arising from them could not have been reliably measured.

The acquired company previously reported under Russian GAAP. Thus it was impracticable to determine the pre-acquisition carrying amount under IFRS and this information is not presented in these consolidated financial statements.

LLC Trade House Pigma contributed USD 51 million of revenue and a loss before tax of USD 1 million from the date of acquisition to 31 December 2006. If the combination had occurred on 1 January 2006, the revenue of the Group from continuing operations would have been USD 204 million and the loss for the year from continuing operations would have been USD 3 million.

## 10. REVENUE

An analysis of the Group's revenues for the year (excluding finance income), for both continuing and discontinued operations, is as follows:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Revenues from sales of tyres | 876 | 724 |
| Revenue from sale of parts and accessories | 103 | 7 |
| Revenue from sales of raw materials | 1 | - |
| Other | 14 | 37 |
| | 994 | 768 |
| **Discontinued operations** | | |
| Revenue from sale of raw materials and other | - | 49 |
| | **994** | **817** |

## 11. DISTRIBUTION EXPENSES

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Salaries and related expenses | (45) | (32) |
| Advertising and marketing expenses | (20) | (20) |
| Transportation and insurance | (15) | (9) |
| Operating leases | (14) | (4) |
| Warehouse expenses | (8) | (6) |
| Business trip | (5) | (5) |
| Depreciation | (4) | (5) |
| Agent and commission fee | (1) | - |
| Security services | (1) | (1) |
| Maintenance and repairs | (1) | (1) |
| Other | (4) | (1) |
| | **(118)** | **(84)** |

## 12. ADMINISTRATIVE EXPENSES

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Salaries and related expenses | (37) | (24) |
| Equity settled employee benefits | (14) | (3) |
| Taxes other than on profit | (10) | (5) |
| Consulting services | (9) | (1) |
| Insurance | (3) | (4) |
| Recruiting and training services | (3) | (2) |
| Depreciation | (2) | (1) |
| Communication | (2) | (2) |
| Security services | (2) | (2) |
| Software, office equipment | (2) | (2) |
| Operating leases | (2) | (1) |
| Stationary and household | (1) | (2) |
| Transportation | (1) | (1) |
| Repairs and maintenance | (1) | (1) |
| Business trip | (1) | (1) |
| Auditor remuneration: audit fees | (1) | (2) |
| Auditor remuneration: other services | - | (1) |
| Public and investor relations | (1) | (1) |
| Other | (6) | (9) |
| | **(98)** | **(65)** |

## 13. PERSONNEL EXPENSES

The average number of employees in the Group during 2007 was 9,543 (2006: 9,393). The average number of employees in Russia and the Netherlands were 8,300 and 1,243 respectively (2006: 8,176 and 1,217 respectively). Numbers of participants in pension program in Dutch tyre plant is 1,205 (2006: 1,139) – refer to Note 4.

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Wages and salaries | (156) | (122) |
| Termination payments | (3) | - |
| Contributions to the pension fund | (19) | (15) |
| Other social charges | (16) | (12) |
| Equity settled employee benefits | (14) | (3) |
| | **(208)** | **(152)** |

Included in cost of goods sold and administrative expenses is USD 3 million in relation to the Dutch defined benefit pension plan (2006: USD 3 million) – refer to note 27.

Staff costs are included in cost of sales, administrative and distribution expenses as follows:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Cost of sales | (112) | (92) |
| Distribution expenses | (45) | (32) |
| Administrative expenses | (37) | (24) |
| Equity settled employee benefits | (14) | (3) |
| Restructuring costs, salaries and wages | - | (2) |
| | (208) | (153) |

## 14. IMPAIRMENT OF LONG LIVED ASSETS

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Impairment of goodwill (refer to Note 20(i)) | (109) | - |
| Impairment of property, plant and equipment (refer to Note 19(iv)) | (10) | - |
| Impairment of other intangible assets (refer to Note 20(i)) | (17) | - |
| | (136) | - |

## 15. OTHER OPERATING EXPENSES

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Loss on disposal of property, plant and equipment | (7) | (3) |
| Impairment losses recognised on receivables | (14) | (5) |
| Provision for inventory obsolescence | (7) | - |
| Other operating expenses | - | (4) |
| | (28) | (12) |

## 16. RESTRUCTURING COSTS

Restructuring costs comprise the following – also refer to Note 6:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Wages and salaries | - | (2) |
| Other expenses | - | (1) |
| | - | (3) |

## 17. FINANCE EXPENSES

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Continuing operations** | | |
| Interest on bank overdrafts and loans | (73) | (49) |
| Interest on obligations under finance leases | (3) | (4) |
| Total interest expense | (76) | (53) |
| Less: amounts included in the cost of qualifying asset | 4 | 2 |
| Bank fees and charges | (3) | (2) |
| | (75) | (53) |

The weighted average capitalisation rate on funds borrowed generally is 7% per annum (2006: 10% per annum).

## 18. INCOME TAXES

### *(i).* Income tax recognised in profit or loss:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Tax expense comprises: | | |
| Current tax expense | (26) | (14) |
| Deferred tax benefit | 6 | 7 |
| | (20) | (7) |
| Attributable to: | | |
| Continuing operations | (20) | (7) |

The total charge for the year can be reconciled to the accounting profit as follows:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| (Loss)/profit from continuing operations | (222) | 8 |
| Loss from discontinued operations | - | (6) |
| Loss from operations | (222) | 2 |
| Income tax benefit calculated at 25.5% (2006: 29.6%) | 57 | 1 |
| Effect of expenses that are not deductible | (13) | (12) |
| Write off of unrecoverable income tax receivable | (12) | - |
| Change in unrecognised deferred tax assets | (13) | 2 |
| Impairment on goodwill that is not deductible | (28) | - |
| Equity settled employee benefits | (4) | (1) |
| Effect on deferred tax balances due to change in income tax in the Netherlands | - | 4 |
| Effect of different tax rates of subsidiaries operating in other jurisdictions | (4) | (1) |
| Other | (3) | (2) |
| **Income tax expense recognised in profit or loss** | (20) | (7) |

The tax rate used for the 2007 and 2006 reconciliations above is the corporate tax rate payable in the Netherlands of 25.5% and 29.6% respectively under the tax law in that jurisdiction. Tax rate in Russia, where a significant portion of activities is conducted, for 2007 and 2006 is 24%.

***(ii).* Deferred tax balances**

| *2006 in million USD* | Opening balance | Charged to income | Acquisitions/ Disposals | Translation differences | Closing balance |
|---|---|---|---|---|---|
| **Temporary differences** | | | | | |
| Property, plant & equipment | (48) | 2 | (7) | (7) | (60) |
| Other long-term assets | - | (1) | (7) | (9) | (17) |
| Current assets | 6 | 1 | (1) | 5 | 11 |
| Liabilities | 10 | 4 | - | 4 | 18 |
| Tax losses | 8 | (1) | - | 6 | 13 |
| Unrecognised deferred tax assets | (16) | 2 | - | (2) | (16) |
| | (40) | 7 | (15) | (3) | (51) |

| *2007 in million USD* | Opening balance | Charged to income | Acquisitions/ Disposals | Translation differences | Closing balance |
|---|---|---|---|---|---|
| Temporary differences | | | | | |
| Property, plant & equipment | (60) | 30 | - | (5) | (35) |
| Other long-term assets | (17) | 8 | - | (1) | (10) |
| Current assets | 11 | - | - | 1 | 12 |
| Liabilities | 18 | (15) | - | 2 | 5 |
| Tax losses | 13 | (4) | - | (1) | 8 |
| Unrecognised deferred tax assets | (16) | (13) | - | (1) | (30) |
| | (51) | 6 | - | (5) | (50) |

Deferred tax balances are presented on the balance sheet as follows:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Deferred tax assets | 8 | 9 |
| Deferred tax liabilities | (58) | (60) |
| **Total deferred taxes** | (50) | (51) |

***(iii).* Unrecognized deferred tax assets**

The following deferred tax assets have not been recognised at the balance sheet date:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Valuation allowance for tax losses carried forward | 2 | 5 |
| Valuation allowance for other deferred tax assets | 28 | 11 |
| **Unrecognised deferred tax assets** | **30** | **16** |

The unrecognised tax losses began to expire in 2005 and will be fully expired by 2015.
Taxable temporary differences in respect of subsidiaries, branches, as well as associates and interests in joint ventures for which deferred tax liabilities have not been recognised are attributable to the following:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Domestic subsidiaries | 2 | 2 |
| Foreign subsidiaries | 28 | 39 |
| | **30** | **41** |

## 19. PROPERTY, PLANT AND EQUIPMENT

| *In million USD* | Buildings | Plant and equipment | Fixtures and fittings | Construction in progress | Total |
|---|---|---|---|---|---|
| *Cost* | | | | | |
| At 1 January 2006 | 139 | 537 | 98 | 45 | 819 |
| Additions | 10 | 27 | 11 | 10 | 58 |
| Acquisition through business combinations | 45 | 55 | 1 | 12 | 113 |
| Disposals | - | (5) | (1) | - | (6) |
| Disposal of subsidiaries | (9) | (14) | (2) | (1) | (26) |
| Foreign currency translation difference | 14 | 57 | 9 | 7 | 87 |
| **At 31 December 2006** | **199** | **657** | **116** | **73** | **1,045** |
| Additions | 10 | 60 | 13 | 52 | 135 |
| Acquisition through business combinations | 1 | - | - | - | 1 |
| Disposals | (8) | (9) | (1) | (5) | (23) |
| Foreign currency translation difference | 15 | 63 | 13 | 7 | 98 |
| Reclassified as held for sale | (40) | - | - | - | (40) |
| **At 31 December 2007** | **177** | **771** | **141** | **127** | **1,216** |

| *In million USD* | Buildings | Plant and equipment | Fixtures and fittings | Construction in progress | Total |
|---|---|---|---|---|---|
| *Accumulated depreciation and impairment* | | | | | |
| At 1 January 2006 | (35) | (307) | (71) | 1 | (412) |
| Depreciation charge | (9) | (34) | (9) | - | (52) |
| Disposals | - | 2 | - | - | 2 |
| Disposal of subsidiaries | 2 | 7 | 1 | - | 10 |
| Foreign currency translation difference | (4) | (33) | (8) | (1) | (46) |
| At 31 December 2006 | (46) | (365) | (87) | - | (498) |
| Depreciation charge | (8) | (38) | (13) | - | (59) |
| Disposals | 1 | 7 | 1 | - | 9 |
| Impairment losses | - | (10) | - | - | (10) |
| Foreign currency translation difference | (4) | (39) | (10) | - | (53) |
| Reclassified as held for sale | 1 | - | - | - | 1 |
| At 31 December 2007 | (56) | (445) | (109) | - | (610) |
| **Net book value at 31December 2006** | **153** | **292** | **29** | **73** | **547** |
| **Net book value at 31 December 2007** | **121** | **326** | **32** | **127** | **606** |

### *(i).* Changes in estimates of useful lives

In 2006 an additional charge was recognized in the amount of USD 3 million as a result of changes in the estimated useful lives of certain fixed assets in the Voronezh facility from 10 to 7 years. The impact of the change in 2007 is USD 500 thousand and nil thereafter, since the fixed assets have been disposed.

### *(ii).* Assets pledged as security

Refer to Note 28(ii) for the details and value of property, plant and equipment which has been pledged to secure certain bank borrowings of the Group.

### *(iii).* Leased plant and machinery

The Group leases production equipment under a number of finance lease agreements. At the end of the lease period, the Group has the option to purchase the equipment at nominal value. At 31 December 2007 the net book value of leased plant and machinery was USD 34 million (2006: USD 36 million). The Group's obligations under the finance leases are secured by the lessors' title over the leased equipment – refer to note 29.

### *(iv).* Impairment of property, plant and equipment

During 2007 the Group carried out a review of the recoverable value of manufacturing equipment which is to be transferred from the Moscow facility to Voronezh (refer to Note 6). The recoverable amount of the relevant assets has been determined on the basis of their value in use. The discount rate used in measuring value in use was 15.5% per annum. In addition, the Group identified certain equipment in the Voronezh facility, which is impaired. These assets are used in the Group's Russian manufacturing segment. As a result, the Group recognised an impairment loss of USD 10 million (refer to Note 14).

## 20. INTANGIBLE ASSETS

| *In million USD* | Goodwill | Research and develop-ment | Brand names | Land lease rights | Software | Customer base | Total |
|---|---|---|---|---|---|---|---|
| *Cost* | | | | | | | |
| At 1 January 2006 | 199 | 14 | 20 | 1 | 4 | - | 238 |
| Additions | - | 2 | - | - | 1 | - | 3 |
| Acquisitions through business combinations | 62 | - | 5 | 9 | - | 12 | 88 |
| Disposals | - | - | (2) | - | - | - | (2) |
| Transfers | - | - | - | (2) | - | - | (2) |
| Foreign currency translation difference | 20 | 1 | 3 | 2 | - | - | 26 |
| **As at 31 December 2006** | **281** | **17** | **26** | **10** | **5** | **12** | **351** |
| Additions | - | 3 | - | - | - | - | 3 |
| Acquisitions through business combinations | 1 | - | - | - | - | - | 1 |
| Reclassified as held for sale | - | - | - | (10) | - | - | (10) |
| Foreign currency translation difference | 25 | 3 | 1 | 1 | - | 2 | 32 |
| **As at at 31 December 2007** | **307** | **23** | **27** | **1** | **5** | **14** | **377** |

| *In million USD* | Goodwill | Research and develop-ment | Brand names | Land lease right | Software | Customer base | Total |
|---|---|---|---|---|---|---|---|
| *Accumulated amortisation and impairment* | | | | | | | |
| Balance at 1 January 2006 | - | (2) | - | - | - | - | (2) |
| Amortisation charge | - | (2) | - | (2) | (1) | - | (5) |
| Balance at 31 December 2006 | - | (4) | - | (2) | (1) | - | (7) |
| Amortisation charge | - | (3) | (1) | - | (1) | (1) | (6) |
| Impairment losses charged to profit or loss | (109) | - | (4) | - | - | (13) | (126) |
| Reclassified as held for sale | - | - | - | 1 | - | - | 1 |
| Foreign currency translation difference | - | (1) | - | - | - | - | (1) |
| Balance at 31 December 2007 | (109) | (8) | (5) | (1) | (2) | (14) | (139) |
| **Carrying amount** | | | | | | | |
| **As at 31 December 2006** | **281** | **13** | **26** | **8** | **4** | **12** | **344** |
| **As at 31 December 2007** | **198** | **15** | **22** | **-** | **3** | **-** | **238** |

### *(i).* Impairment

For the purposes of impairment testing, goodwill was allocated to the Group's cash generating units, being: Voronezh tyre plant, Kirov tyre plant, manufacturing unit in Holland namely Vredestein Banden B.V., the retail distribution business and the wholesale distribution business. In 2006 the Group recognised the following cash generating units; manufacturing unit (Russia), manufacturing unit (Netherlands) and retail distribution business. The change in cash generating units occurred with an increased level of activities in the retail and wholesale distribution business and with the change in the way goodwill is monitored.

These units represent the level within the Group at which the goodwill is monitored for internal management purposes and to which goodwill, if any, is associated. The 2006 comparative information has been presented in a manner which is consistent with 2007.

Before recognition of impairment losses, the aggregate carrying amounts of goodwill were allocated to each cash generating unit as follows:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Voronezh Tyre Plant | 35 | 33 |
| Kirov Tyre Plant | 29 | 28 |
| Manufacturing unit (Holland) | 134 | 119 |
| Retail distribution business | 86 | 80 |
| Wholesale distribution business | 23 | 21 |
| | **307** | **281** |

The recoverable amounts of the cash generating units were determined based on a value in use calculation which uses cash flow projections based on financial budgets approved by the directors covering a 5 year period. The recoverable amounts were determined with the assistance of American Appraisal (AAR) Inc., independent appraiser.

The following discount rates and terminal growth rates were applied in determining the recoverable amount:

| | 2007 | | 2006 | |
|---|---|---|---|---|
| | Discount rate % | Terminal growth rate % | Discount rate % | Terminal growth rate % |
| Voronezh Tyre Plant | 15.5 | 4.0 | 17.7 | 4.0 |
| Kirov Tyre Plant | 15.5 | 4.0 | 17.7 | 4.0 |
| Manufacturing unit (Holland) | 14.2 | 2.5 | 14.2 | 2.5 |
| Retail distribution business | 16 | 4.0 | 15.9 | 4.0 |
| Wholesale distribution business | 16.15 | 4.0 | 15.9 | 4.0 |

Cashflow projections during the budget period are based on long term growth rate expectation and inflation forecasts. The values assigned to the key assumptions represent management's assessment of future trends in the tyre production industry and are based on both external and internal sources (historic data). Key assumptions include inflation, raw material prices and the growth in the market for tyres.

As a result of the impairment test of goodwill and other intangible assets, an impairment loss of USD 126 million was recognised (2006: nil). The main factor contributing to the impairment were continuing losses in the retail and wholesale distribution businesses, which were predominately acquired in 2005 and 2006.

The impairment relates to the following intangible assets:

| *in million USD* | Year ended 31 December 2007 |
|---|---|
| **Goodwill** | |
| Retail distribution business | (86) |
| Wholesale distribution business | (23) |
| | (109) |
| Customer base, wholesale distribution business | (13) |
| Brand names, manufacturing | (4) |
| | **(126)** |

## 21. FINANCIAL ASSETS

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| **Loans and receivables carried at amortised cost** | | |
| *Current* | | |
| Kemerovo Chemical Fibre Plant receivables – long-term portion | - | 10 |
| Loans originated -long term | 6 | 1 |
| | **6** | **11** |
| *Non-current* | | |
| Kemerovo Chemical Fibre Plant receivables – long-term portion | - | 7 |
| Loans originated -long term | - | 6 |
| | **-** | **13** |

The long-term loan has been provided to the third party at 3.5% per annum with maturity in March 2008. For the year ended 31 December 2007, the loan is included in current financial assets. In November 2007, the Group disposed of the remaining portion of the receivable from Kemerovo Chemical Fibre Plant. As a result of the disposal a loss of USD 2 million was recorded in other operating expense.

## 22. ADVANCES

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| **Advances for acquisition of equipment** | **-** | **27** |

## 23. INVENTORIES

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Raw materials | 39 | 36 |
| Work in progress | 10 | 9 |
| Finished goods | 160 | 151 |
| Impairment for inventory obsolescence | (7) | (3) |
| | **202** | **193** |

Refer note 28(ii) for the value of inventory securing bank borrowings of the Group.

The cost of inventories recognised as an expense during the period, in respect to continuing operations, was USD 536 million (2006: USD 427 million). In 2007 the write-down of inventories to net realisable value amounted to USD 1 million (2006: nil). There were no reversals of write-downs in 2007 (2006: USD 1 million). The write-downs and reversals are included in other operating esxpenses. Refer to Note 15.

## 24. TRADE AND OTHER RECEIVABLES

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Trade accounts receivable | 190 | 157 |
| Provision for doubtful debts | (18) | (14) |
| | 172 | 143 |
| VAT receivable | 36 | 37 |
| Taxes receivable other than VAT | 7 | 6 |
| Receivables from related parties | - | 23 |
| Advances issued | 9 | 10 |
| Other receivables | 26 | 23 |
| | **250** | **242** |

Other receivables comprise of tax escrow account, prepayments and other receivables. Refer to note 28(ii) for the value of receivables securing bank loans of the Group.

The average credit period on sale of goods is 90 days (2006: 90 days). No interest is charged on the initial 30 days from the date of the invoice. Thereafter, interest is generally chargeable at 10% to 11% per annum on the outstanding balance, in accordance with the terms of the contract. However, these penalties are rarely enforced.

The Group has provided fully for all receivables over 365 days because historical experience is such that receivables past due beyond 365 days are generally not recoverable. Trade receivables between 90 days and 365 days are provided for based on estimated irrecoverable amounts.

Before acceptance of any new customer, the Group uses an internal credit system to assess the potential customer's credit quality and defines credit limits separately for each individual customer. Credit limits attributable to a customer is regularly reviewed at least on an annual basis. Of the receivables balance at the end of the year, the Group's five largest customers represent 10% (2006: 8%) of the outstanding balance. Individually these customer balances do not exceed 3% of the total trade receivable balance.

The summary below shows the credit limits and outstanding balances of top five counterparties at the respective balance sheet date:

| | | 31 December 2007 | | 31 December 2006 | |
|---|---|---|---|---|---|
| *in million USD* | **Customer location** | **Credit limit** | **Outstanding balance** | **Credit limit** | **Outstanding balance** |
| Customer A | Nizhny Novgorod | n/a | 6 | n/a | 7 |
| Customer B | Voronezh | n/a | 6 | n/a | 2 |
| Customer C | Moscow Region | 20 | 3 | n/a | - |
| Customer D | Nizhny Novgorod | n/a | 2 | n/a | 2 |
| Customer E | Togliatti | n/a | 2 | n/a | 1 |
| **Total** | | | **19** | | **12** |

Included in the Group's trade receivables balance are debtors with a carrying amount of USD 125 million (2006: USD 94 million) which are past due at the respective reporting date and which the Group still considers recoverable. The Group does not hold any collateral over these outstanding balances. The weighted average age of these receivables is 24 days (2006: 26 days).

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

| *in million USD* | **31 December 2007** | **31 December 2006** |
|---|---|---|
| Past Due: | | |
| less than 30 days | 63 | 46 |
| 30 – 90 days | 19 | 13 |
| 90 – 180 days | 12 | 11 |
| 180 – 365 days | 22 | 17 |
| Thereafter | 9 | 7 |
| **Total** | **125** | **94** |

Movement in the allowance for doubtful debt in respect of trade and other receivables:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| **Balance at beginning of the year** | (14) | (12) |
| Impairment losses recognized on receivables | (18) | (5) |
| Amounts written-off as uncollected | 12 | 4 |
| Amount recovered during the year | 4 | - |
| Effect of translation to presentation currency | (2) | (1) |
| **Balance at end of the year** | **(18)** | **(14)** |

Included in allowance for doubtful debt are individually impaired trade receivables with a balance of USD 9 million. The Group does not hold any collateral over these balances.

Aging of impaired trade receivables:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| 180-365 days | 1 | - |
| Thereafter | 17 | 14 |
| **Total** | **18** | **14** |

## 25. CASH AND CASH EQUIVALENTS

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Cash in bank | 14 | 20 |
| Other cash balances | 8 | 8 |
| Cash and cash equivalents in the balance sheet | 22 | 28 |
| Bank overdrafts | (35) | (26) |
| **Cash and cash equivalents in the statement of cash flows** | **(13)** | **2** |

## 26. EQUITY

| *Number of shares at par value of EUR 0.01 per share* | Ordinary shares |
|---|---|
| On issue at 1 January 2006 | 68,140,803 |
| Issued to management – September 2006 | 36,000 |
| On issue at 31 December 2006 | 68,176,803 |
| On issue at 1 January 2007 | 68,176,803 |
| Issued to management – August, September 2007 | 105,000 |
| On issue at 31 December 2007 | 68,281,803 |

**Issue of shares**

In August and September 2007, the Parent Company issued 105,000 ordinary shares to the Managers of the Group for a cash consideration of Euro 0.01 per share. The fair value of the shares issued of USD 440 thousand was included in salaries and related expenses as part of administrative expenses.

***(i).* Share option plans**

In January 2007, share options (SOP I and SOP II) issued to executives in October 2005 were cancelled. As a result of the cancellation, the Group recognised a charge of USD 9.5 million.

Subsequent to the appointment of a new management team in July 2007, the CEO of the Group was granted a right to purchase up to 3% of the ordinary shares of the Company at a price of USD 4.5 per share. In accordance with the terms of the share-based agreement, share options vest immediately, having an option life of three years, subject to further reappointment.

The following share-based payment arrangements were in existence during the current and comparative reporting periods:

| | Number | Grant date | Expiry date | Exercise price USD | Fair value at grant date USD |
|---|---|---|---|---|---|
| **Option series** | | | | | |
| Series 1: SOP I – October 2005 | 260 000 | 25 October 2005 | May 2011 | 12.72 | 1.30 |
| Series 2: SOP II – October 2005 | 4 429 152 | 25 October 2005 | May 2010 | 11.00 | 2.80 |
| Series 3: SOP III – July 2007 | 2 045 304 | 2 July 2007 | July 2010 | 4.5 | 2.17 |

The weighted average fair value of the share options granted during the financial year 2007 was 2.17 USD (2006: 2.05 USD). Options were priced using a binominal option pricing model. Where relevant, the expected life used in the model has been adjusted to management's best estimate of the effect of non-transferability, exercise restrictions (including the probability of meeting market conditions attached to the option), and behavioral considerations. The expected volatility for SOP I and SOP II was based on historical share price volatility over the previous 2 years. In relation to SOP III, since the Group's GDR's have been illiquid and on a continued decline due to significant risks in relation to the expected major restructuring, assumptions on the expected volatility have been made on the basis of the average volatility for the past year of eight different peer companies.

| **Inputs into the model** | **Series 1** | **Series 2** | **Option Series Series 3** |
|---|---|---|---|
| Grant date share price | 11.00 | 11.00 | 5.75 |
| Exercise price | 12.72 | 11.00 | 4.5 |
| Expected volatility | 30% | 30% | 30% |
| Option life | 2 years | 5 years | 3 years |
| Dividend yield | 3.00% | 3.00% | - |
| Risk free interest rate | 4.76% | 4.76% | 4.76% |

The following reconciles the outstanding share options granted under the employee share option plan at the beginning and end of financial year:

| | 2007 | | 2006 | |
|---|---|---|---|---|
| | Number of options | Weighted average exercise price USD | Number of options | Weighted average exercise price USD |
| Balance at the beginning of year | 4,689,152 | 11.86 | 4,689,152 | 11.09 |
| Granted during the year | 2,045,304 | 4.5 | - | - |
| Cancelled during the year | (4,689,152) | (11.86) | - | - |
| **Balance at the end of the financial year** | **2,045,304** | **4.5** | **4,689,152** | **11.09** |

As of 31 December 2007 the market price of the share options was lower than USD 4.5 per share. In July 2008, share options (SOP III) issued in July 2007 were cancelled.

In addition to the above share options, in August 2007 a number of executives were granted an option to purchase 105,000 shares at par value of 0.01 EUR as a reward and compensation for their services to the Group. The options vested at the date of grant and were exercised immediately by the grantees. The Group recognized a charge of USD 440 thousand in relation to the granting of these share options.

#### *(ii).* Dividends

Holders of the ordinary shares are entitled to dividends upon the decision of the general shareholders' meeting if the net assets of the Company exceed the total value of the paid in capital and reserves, which have to be maintained by law and the Articles of Association. No dividends to ordinary shareholders were declared in 2007 and 2006.

#### *(iii).* Minority interest

USD 9 million in minority interest is attributable to a 10% minority interest in the net assets of Kirov tyre plant. (2006: USD 8 million).

#### *(iv).* Legal reserves

In relation to legal reserves refer to Note (viii) of the Parent financials statements.

### 27. RETIREMENT BENEFIT OBLIGATION

#### *(i).* Defined benefit plans

At 31 December 2007 employees of Vredestein Banden B.V. (Netherlands) and Vredestein GmbH (Germany) participated in defined benefit plans. The benefits of the defined benefit pension plans in the Netherlands and Germany are based primarily on years of service and employees' compensation. The funding policy for the plans is consistent with local requirements in the countries where the funds were established. Awarded pension rights for the defined benefit pension plan of Vredestein Banden B.V. are financed by means of annual premiums paid to the pension fund. The defined benefit pension plan of Vredestein Banden B.V. is wholly funded. The defined benefit pension plan of Vredestein GmbH is partly funded.

The amounts recognised in the consolidated balance sheet in respect of the Group's defined benefit obligations were as follows:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| *Defined benefit obligation* | | |
| Balance at beginning of the year | (124) | (116) |
| Service costs | (3) | (3) |
| Payments by employees | (5) | (6) |
| Interest costs | (6) | (5) |
| Actuarial gains | 14 | 18 |
| Foreign exchange losses | (14) | (12) |
| **Balance at end of the year** | **(138)** | **(124)** |

| *in million USD* | **31 December 2007** | **31 December 2006** |
|---|---|---|
| *Plan assets* | | |
| Balance at beginning of the year | 98 | 78 |
| Contribution by employer | 9 | 8 |
| Contribution by employees | 4 | 4 |
| Expected return on plan assets | 5 | 4 |
| Actuarial losses | (9) | (4) |
| Foreign exchange gain | 11 | 8 |
| Balance at end of the year | 118 | 98 |
| Funded status | (20) | (26) |
| Unrecognised loss | (14) | (8) |
| **Net balance pension liability** | **(34)** | **(34)** |

The amounts recognised during the period in the statement of income for 2006 were as follows:

| *in million USD* | **Year ended 31 December 2007** | **Year ended 31 December 2006** |
|---|---|---|
| Service costs | 3 | 3 |
| Interest costs | 6 | 5 |
| Expected return on plan assets | (5) | (4) |
| **Total cost recognised** | **4** | **4** |

The amounts were recorded in cost of goods sold, administrative and distribution expenses.
The major categories of plan assets, and the expected rate of return at the balance sheet date for each category, are as follows:

| | **Expected return** | | **Fair value of plan assets** | |
|---|---|---|---|---|
| | **2007 %** | **2006 %** | **31.12.2007 million USD** | **31.12.2006 million USD** |
| Equity securities | 7.65% | 7.25% | 41 | 22 |
| Government bonds | 4.65% | 4.25% | 77 | 74 |
| Property investment funds | - | - | - | 2 |
| **Weighted average expected return** | **5.45%** | **5%** | **118** | **98** |

The overall expected rate of return is a weighted average of the expected returns of the various categories of plan assets held. The directors' assessment of the expected returns is based on historical return trends and analysts' predictions of the market for the asset in the next twelve months.

The actual return on plan assets was a loss of USD 4 million (2006: gain of USD 2.6 million).

The plan assets are managed through a strategic allocation fund. The portfolio contains bonds (65%) and investments (35%) such as stocks, commodities, hedge funds, real estate, high yield bonds and private equity. The market value of the shares in the strategic allocation fund is USD 116 million. In addition, the plan assets include USD 2 million in cash.

The history of defined benefit obligation, plan assets and experience adjustments:

| *In million USD* | 31.12.2007 | 31.12.2006 | 31.12.2005 |
|---|---|---|---|
| Present value of defined benefit obligation | 138 | 124 | 116 |
| Fair value of plan assets | (118) | (98) | (78) |
| Deficit | 20 | 26 | 38 |
| Experience adjustments on plan liabilities | 14 | 18 | (6) |
| Experience adjustments on plan assets | (9) | (4) | - |

The Group has only a three year history of experience adjustments, since the defined benefit plan was acquired as part of the acquisition of Vredestein Banden B.V. in April 2005.

The Group expects to make a contribution of USD 7.8 million (2006: 7.6 million) to the defined benefits plans during the next financial year.

## 28. LOANS AND BORROWINGS

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| *Non-current* | | |
| Unsecured bank loans | - | 24 |
| Secured borrowings | - | 8 |
| Secured bank loans | 253 | 207 |
| | **253** | **239** |
| *Current* | | |
| Current portion of secured bank loans | 488 | 148 |
| Unsecured bank loans | 2 | 103 |
| Unsecured borrowings | - | 153 |
| Unsecured bonds issued | - | 11 |
| | 490 | 415 |
| Bank overdraft | 35 | 26 |
| | **778** | **680** |

For more information about the Group's exposure to interest rate and foreign currency risk, refer to Note 32(v).

### *(i).* Terms and debt repayment schedule

**31 December 2007**

| *in million USD* | Total | Under 1 year | 1-5 years | Over 5 years |
|---|---|---|---|---|
| ***Secured bank loans:*** | | | | |
| RUR, fixed at 8,30-15% | 321 | 252 | 18 | 51 |
| EUR, variable at Euribor+1.25% | 57 | - | - | 57 |
| EUR, variable at Euribor+2.25% | 140 | 15 | 125 | - |
| EUR, variable at Euribor+4% | 9 | 9 | - | - |
| EUR, variable at Euribor+5.25% | 15 | 15 | - | - |
| EUR, fixed at 9.59% | 132 | 132 | - | - |
| USD, fixed at 13% | 65 | 65 | - | - |
| CHF, fixed at 3.2% | 2 | - | - | 2 |
| ***Unsecured bank loans:*** | - | - | - | - |
| RUR, fixed at 9-11,75% | 2 | 2 | - | - |
| ***Bank overdraft:*** | - | - | - | - |
| RUR, fixed at 9-13,8% | 7 | 7 | - | - |
| EUR, variable at Euribor+2.25% | 28 | 28 | - | - |
| | **778** | **525** | **143** | **110** |

The Group has adopted a policy of ensuring that 60 per cent of the EUR variable borrowings at Euribor+2.25%, provided by ING/ABN-Amro are hedged by interest rate swaps denominated in Euros. The fixed interst rates on the interest rate swaps are 2.98% and 3.13%, depending on the contract. The swaps mature over the next four years matching the maturity of the related loan. As of 31 December 2007 the Group had interest rate swaps with notional contract amounts of USD 115 million (2006: USD 87 million). At 31 December 2007 the fair value of the interest rate swaps is USD 3 million (2006: USD 2 million).

### *(ii).* Security

The following assets are pledged to secure the bank loans (at carrying amount):

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Owned property, plant and equipment | 195 | 120 |
| Leased property, plant and equipment | 34 | 36 |
| Inventories | 115 | 80 |
| Accounts receivables | 94 | 86 |
| Ordinary Shares – Group companies | 158 | 54 |

### *(iii).* Unsecured borrowings

Pursuant to First and Second loan agreements dated June 28, 2005, between the Group and Emerging Markets Structured Products B.V. ("EMSP"), EMSP granted two loans to the Group in the aggregate amount of USD 175 million, with 9.25% interest rate (paid semi-annually). The loan agreement implied an option to the Group to declare new interest rate for the period starting from June 30, 2006 to June 30, 2007 at its own discretion.

In 2006 the Group exercised this option and declared a rate of 9.00% and ESMP, exercised its put-option and required the Group to prepay partially the First Loan agreement in the amount of 20 million USD.

As of 31 December 2006, the aggregate principle amount outstanding under both loan agreements totalled USD 153 million bearing 9.00% interest (paid semi-annually).

In June 2007 the Group had fully repaid the loans.

***(iv).* New credit lines**

During the first five months of 2007, the Group has entered into new credit lines with several banks in order to replace the short-term loans and to be able to repay the EMSP loan (refer above). Two eighteen-month facilities have been provided by Sberbank in the amount of RUR 1 685 million (USD 65 million), secured by the securities of Group companies and RUR 315 million (USD 12 million) secured by a pledge of real estate. Bank SG-Vostok has increased the credit line limit from RUR 300 million to RUR 400 million (by USD 4 million) secured by equipment pledge. EUR 50 million Amsterdam Trade Bank facility, maturing in May 2007, has been replaced with similar structure provided by Alfa bank secured by a pledge of equipment and temporary pledge of 51% of the share capital OJSC AV-TO, which has been released in October 2007.

For the Financing of Voronezh-2 investment program and the final payment of the Moscow Tyre Plant acquisition, the Company entered into longer term credit facilities secured by pledge of equipment.

Credit lines with other banks which matured within the first five months of 2007 have been refinanced with similar facilities without an increase in limits.

***(v).* Covenants**

Over the period, the Group was not in compliance with certain financial covenants set out in existing loan agreements as of December 31, 2007. As of the date of approval of the Group's accounts by the EGM, several creditors have filed claims to the courts. Loans in the amount of USD 31 million have been reclassified to current, on the basis of the breaches and claims.

***(vi).* Restructuring**

Subsequent to the year end the Group has commenced an extensive restructuring of its debt obligations. Further information on this is provided in Notes 2(i) and 38.

## 29. FINANCE LEASE LIABILITIES

Finance lease liabilities are payable as follows:

| | 2007 | | | 2006 | | |
|---|---|---|---|---|---|---|
| *USD million* | Minimum lease payments | Future finance charges | Principal outstanding | Minimum lease payments | Future finance charges | Principal outstanding |
| Less than one year | 10 | (3) | 7 | 10 | (4) | 6 |
| Between one and five years | 17 | (2) | 15 | 26 | (5) | 21 |
| | 27 | (5) | 22 | 36 | (9) | 27 |

The finance leases relate to manufacturing equipment. The interest rates implicit in the leases vary from 11 to 17% per annum (2006: from 11 to 17%). Under the terms of the lease agreement, no contingent rents are payable.

## 30. TRADE AND OTHER PAYABLES

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| Trade accounts payable | 146 | 93 |
| Taxes payable, other than VAT | 29 | 19 |
| VAT payable | 15 | 14 |
| Payables to related parties | 13 | 15 |
| Accruals and provisions | 10 | 3 |
| Advances received | 9 | 7 |
| Deferred income | 2 | 1 |
| Other payables | 44 | 51 |
| | 268 | 203 |

Trade accounts payable include the liability to Sibur Holding for raw materials in the total amount of USD 22 million (2006: USD 11 million).

Other payables comprise of employee benefits, sales bonuses accrued and other payables. The average credit period on purchases of raw materials is 30 days (2006: 30 days). No interest is charged on trade payables for this period. Thereafter, interest is charged at 0.04% per day but not exceeding 3 to 10% of the outstanding balance, in accordance with the terms of the individual contracts.

## 31. EARNINGS PER SHARE

The calculation of earnings per share is the net loss for the year divided by the weighted average number of ordinary shares outstanding during the year, calculated as shown below. Diluted earnings per share are computed on the basis of the weighted average number of shares outstanding plus the effect of the stock option plans in effect during the relevant period. However since the effect of the stock option plan is anti-dilutive, the stock option plan had no impact on the earnings per share calculation.

| *in Dollars per share* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Basic and diluted earnings per share | | |
| From continuing operations | (3.57) | 0.01 |
| From discontinued operations | - | (0.08) |
| **Total basic and diluted earnings per share** | **(3.57)** | **(0.07)** |

| *Shares* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| On issue at the beginning of the year | 68,176,803 | 68,140,803 |
| Effect of shares issued | 44,014 | 12,000 |
| Weighted average number of ordinary shares at 31 December 2006 | 68,220,817 | 68,152,803 |

## 32. FINANCIAL INSTRUMENTS

As described in Note 2(i), the Group has borrowed over USD 800 million to finance its modernization and expansion program. Although the Group was operationally cashflow positive in 2006 and 2007, as the majority of the modernization and expansion program was funded by borrowings, this has resulted in substantial gearing, which currently cannot be supported by existing operating cashflows.

### *(i).* Gearing ratio

The Group has a target long term gearing ratio of 72% determined as a proportion of net debt to equity, which is substantially lower than at year end. The gearing ratio at the year end was as follows:

| | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Debt (i) | 800 | 707 |
| Cash and cash equivalents | (22) | (28) |
| **Net debt** | **778** | **679** |
| Equity (ii) | 218 | 410 |
| **Net debt to equity ration** | **357%** | **166%** |

Debt is defined as long-term and short-term borrowings, bank overdrafts and finance lease liabilities.

Equity includes all capital and reserves of the Group.

### *(ii).* Major categories of financial instruments

The Group's principle financial assets and liabilities comprise of the following:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| **Financial assets** | | |
| Trade and other receivables | 250 | 242 |
| Cash and cash equivalents | 22 | 28 |
| Loans and receivables | 6 | 24 |
| | **278** | **294** |
| **Financial liabilities** | | |
| Loans and borrowings | (743) | (654) |
| Trade payables including payables to related parties | (268) | (203) |
| Bank overdrafts | (35) | (26) |
| Finance lease liabilities | (22) | (27) |
| | **(1 068)** | **(910)** |

The main risks arising from the Group's financial instruments are liquidity, interest rate, foreign currency and credit risks.

### *(iii).* Liquidity risk

Liquidity risk is the risk that the Group will not be able to settle all liabilities as they are due.
As described above, the expansion program was primarily financed by loans and borrowings and as a result the Group's financial condition has significantly deteriorated Based on contractual maturities and management's best estimates, the Group's principle financial assets and liabilities mature during the following periods, prior to the restructuring plan:

*2007*

| *in million USD* | 0-6 mths | 6-12 mths | 1-2 yrs | 2-3 yrs | 3-4 yrs | 4-5 yrs | over 5 yrs | Total |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Trade receivables | - | 250 | - | - | - | - | - | **250** |
| Cash and cash equivalents | 22 | - | - | - | - | - | - | **22** |
| Loans issued | 6 | - | - | - | - | - | - | **6** |
| | **28** | **250** | - | - | - | - | - | **278** |
| **Financial liabilities** | | | | | | | | |
| Loans and borrowings | (171) | (289) | (39) | (134) | - | - | (110) | **(743)** |
| Trade and other payables | - | (268) | - | - | - | - | - | **(268)** |
| Bank overdrafts | (35) | - | - | - | - | - | - | **(35)** |
| Finance lease liabilities | (3) | (4) | (8) | (7) | - | - | - | **(22)** |
| | **(209)** | **(561)** | **(47)** | **(141)** | - | - | **(110)** | **(1 068)** |

*2006*

| *in million USD* | 0-6 mths | 6-12 mths | 1-2 yrs | 2-3 yrs | 3-4 yrs | 4-5 yrs | over 5 yrs | Total |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Trade receivables | - | 242 | - | - | - | - | - | 242 |
| Cash and cash equivalents | 28 | - | - | - | - | - | - | 28 |
| Loans issued | - | 11 | 13 | - | - | - | - | 24 |
| Advances | - | - | 27 | - | - | - | - | 27 |
| | 28 | 253 | 40 | - | - | - | - | 321 |
| **Financial liabilities** | | | | | | | | |
| Loans and borrowings | (301) | (114) | (14) | (26) | (134) | (5) | (60) | (654) |
| Trade and other payables | - | (203) | - | - | - | - | - | (203) |
| Bank overdrafts | (26) | - | - | - | - | - | - | (26) |
| Finance lease liabilities | (3) | (4) | (7) | (7) | (6) | - | - | (27) |
| | (330) | (321) | (21) | (33) | (140) | (5) | (60) | (910) |

The table above shows the breached loans as non-current in accordance with the expected repayment schedule. The table does not reflect the expected loan restructuring. In respect of loans and borrowings, the above tables do not include contractual interest payments which are generally payble on a monthly basis.

### *(iv).* Interest rate risk

Interest rate risk is the risk that changes in floating interest rates will adversely impact the financial results of the Group. Interest rate swap denominated in Euro have been entered into to achieve an appropriated mix of fixed and floating rate exposure within the Group's policy. The change in fair value is recognised in the statement of operations as interest income or costs.

The table below details the Group's sensitivity to an increase or decrease in floating rate by 1% on variable rate interest-bearing financial assets and liabilities:

| *in million USD* | 31 December 2007 | 31 December 2006 |
|---|---|---|
| **Net interest charge** | (3) | (2) |

### *(v).* Foreign currency risk

Foreign currency risk is the risk that the financial results of the Group will be adversely impacted by changes in exchange rates to which the Group is exposed. The Group incurs foreign currency risk on sales, purchases and borrowings. Management does not hedge the Group's exposure to foreign currency risk.

The Group has the following foreign-currency denominated financial assets and liabilities:

**2007**

| *in million USD* | USD-denominated | Euro-denominated | RUR-denominated | Other currencies-denominated | Total |
|---|---|---|---|---|---|
| Financial assets | 2 | 150 | 126 | - | 278 |
| Financial liabilities | (69) | (508) | (489) | (2) | (1 068) |

**2006**

| *in million USD* | USD-denominated | Euro-denominated | RUR-denominated | Other currencies-denominated | Total |
|---|---|---|---|---|---|
| Financial assets | 7 | 147 | 167 | - | 321 |
| Financial liabilities | (176) | (347) | (385) | (2) | (910) |

The Group is mainly exposed to the Euro and the Russian Rouble. The table below shows the Group's sensitivity to a 10% increase and decrease in the USD as the reporting currency against the relevant foreign currencies. A positive number below indicates an increase in profit/equity when the USD weakens 10% against the relevant currency.

| *in million USD* | Euro 31 December 2007 | Euro 31 December 2006 | RUR 31 December 2007 | RUR 31 December 2006 |
|---|---|---|---|---|
| Profit and loss | (1) | (4) | (1) | (1) |
| Other equity | 10 | 14 | 15 | 22 |

### *(vi).* Credit risk

The Group does not require collateral in respect of financial assets. Credit evaluations are performed on all customers, other than related parties, requiring credit over a certain amount.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

### *(vii).* Fair values

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price.

The management consider the carrying amounts of financial assets and liabilities recorded in the consolidated financial statements approximate their fair values with the exception of loans and borrowings in the amount of USD 743 million and finance leases of USD 22 million. The Group is unable to determine the fair value of these financial liabilities as the Group's debt is not publically traded and further funding for the Group is not available on a stand alone basis.

## 33. OPERATING LEASES

Production companies of the Group did not enter into operating lease agreements. Amount of operating lease rentals payable of retail business was negligible.

## 34. COMMITMENTS

At 31 December 2007 the Group has not entered into any non cancellable expenditure commitments (2006: USD 2 million).

## 35. CONTINGENCIES

### *(i).* Insurance

The insurance industry in the Russian Federation is in a relatively early stage of development and many forms of insurance protection common in other parts of the world are not yet generally available. The Group has insured a significant part of the Group's production facilities, including Voronezh tyre plant, Kirov tyre plant, against damage arising from accidents or fire. The insurer, however, will not reimburse the Group for business interruption or any environmental damage arising from accidents on Group property or relating to Group operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

### *(ii).* Taxation contingencies

The taxation system in the Russian Federation is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

Some retail chains which were acquired by the Group were involved in tax optimization programs. Management of the retail chains involved, controlled the transactions. Although the Group is not responsible for the potential violations of the tax legislations, this could result in a possible tax liability that cannot be estimated. Based on the facts available, the risk of a significant economic benefit outflow as result of the potential claims is seen by management as less than probable.

### *(iii).* Factoring arrangements

In 2007 and 2006 the Group used factoring operations to finance its operating activities. Factoring services were rendered by a Bank under non-recourse terms. The total amount of receivables sold in 2007 was USD 62 million (2007: USD 83 million).

## 36. RELATED PARTY TRANSACTIONS

### *(i).* Control relationships

Related parties comprise the shareholders of the Parent Company and all other companies in which the shareholder has a controlling interest or significant influence. Transactions with key management personnel and entities, that are controlled, jointly controlled or significantly influenced by individuals mentioned, are also recognized and disclosed as related party transactions.

### *(ii).* Management remuneration

The remuneration of directors and other members of key management during the year was as follows:

| *in million USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| Short-term benefits | 4 | 3 |
| Termination benefits | 3 | - |
| Share-based payments | 14 | 2 |
| | **21** | **5** |

| *In thousand USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Executives and management** | | |
| **A.Gurin (ceased employment on 31 July 2007)** | | |
| Salaries | 352 | 607 |
| Bonuses | 117 | 202 |
| Related taxes | 838 | 20 |
| Termination benefits | 3 471 | - |
| Share-based payments | 4 770 | 1 179 |
| | **9 548** | **2 008** |
| **S.Bokhanov (commenced employement on 26 June 2006 and ceased employment on 31 May 2007)** | | |
| Salaries | 186 | 433 |
| Bonuses | 37 | 68 |
| Related taxes | 58 | 14 |
| Share-based payments | 1 908 | 511 |
| | **2 189** | **1 026** |
| **R.Oudschoorn** | | |
| Salaries | 392 | 408 |
| Bonuses | 68 | 184 |
| Post employment benefits | 49 | 46 |
| Share-based payments | 1 068 | 315 |
| | **1 577** | **953** |
| **T.Tholens (ceased employment on 8 March 2007)** | | |
| Salaries | 214 | 305 |
| Bonuses | 62 | 165 |
| Post employment benefits | 27 | 31 |
| Share-based payments | 1 068 | 315 |
| | **1 371** | **816** |
| **P.Zolotarev (commenced employment on 1 July 2007)** | | |
| Salaries | 396 | - |
| Bonuses | 317 | - |
| Related taxes | 185 | - |
| Share-based payments | 4 432 | - |
| | **5 330** | - |
| **I.Ivanov (commenced employment on 2 October 2007)** | | |
| Salaries | 161 | - |
| Bonuses | - | - |
| Related taxes | 42 | - |
| | **203** | - |
| **V.Pesochinskiy (commenced employment on 1 July 2007)** | | |
| Salaries | 202 | - |
| Bonuses | - | - |
| Related taxes | 52 | - |
| | **254** | - |

| *In thousand USD* | Year ended 31 December 2007 | Year ended 31 December 2006 |
|---|---|---|
| **Non-executive directors** | | |
| S.Gupta (ceased directorship on 31 July 2007) | - | 100 |
| T.Saudhri (ceased directorship on 06 September 2007) | - | 50 |
| D.Gualtieri (ceased directorship on 30 June 2007) | - | 75 |
| D.Gupta | 102 | 75 |
| H.Pandza (commenced directorship on 26 June 2006) | 86 | 50 |
| M.Ignatiev | 120 | 75 |
| R.Nagapetiantz (commenced directorship on 01 July 2007) | 34 | - |
| H.W.T. Bosh (commenced directorship on 02 October 2007) | 17 | - |
| **Total non-executive directors** | 359 | 425 |

Non-executive directors compensation comprises of annual director fees paid quarterly.

Share based payments included in 2007 remuneration amounts, with the exception of USD 440 thousand, have not been realised, as all share options schemes have been cancelled in 2007 and 2008.

### *(iii).* Transactions with Group companies

During 2007 the Group performed following transactions with related parties:

| *in million USD* | 2007 | 2006 |
|---|---|---|
| **Sales to related parties** | **1** | **-** |
| OAO MTP | 1 | - |
| **Purchases of goods** | **5** | **4** |
| OAO MTP | 5 | 4 |
| **Rent expenses incurred** | **-** | **1** |
| Mr.Gupta | - | 1 |
| **Acquisition of Intangible Assets** | **1** | **-** |
| OAO MTP | 1 | - |
| **Promissory notes** | **7** | **10** |
| OAO MTP | 7 | 10 |
| **Promissory notes interest income** | **1** | **-** |
| OAO MTP | 1 | - |
| **Loans from related parties** | **116** | **9** |
| Alfa-bank | 48 | 9 |
| Amsterdam Trade bank | 68 | - |
| **Loans repaid by related parties** | **-** | **11** |
| Amtel-Development | - | 8 |
| Amtel-Investment | - | 3 |
| **Loans issued to related parties** | **3** | **-** |
| OAO MTP | 3 | - |

### *(iv).* Balances with related parties

As of 31 December 2007 Group companies recorded the following balances with related parties:

| *in million USD* | 2007 | 2006 |
|---|---|---|
| **Long-term interest bearing loans issued to related parties** | **3** | **-** |
| OAO MTP | 3 | - |
| **Trade and other receivables** | **8** | **12** |
| OAO MTP | 8 | 12 |
| **Promissory notes receivable** | **8** | **11** |
| OAO MTP | 8 | 11 |
| **Loans from related parties** | **73** | **88** |
| Alfa-Bank (i) | 73 | 22 |
| Amsterdam Trade Bank (ii) | - | 66 |
| **Payables to related parties other than controlling shareholder** | **13** | **12** |
| Employees | 12 | 7 |
| OAO MTP | 1 | 5 |

(i) The loans from Alfa-Bank consist of a Euro denominated loan in the amount of USD 55 million (2006: nil) with a fixed rate of interest of 9.75% and Rouble denominated loan in the amount of USD 18 million (2006: 22 million) at a rate of 11%. The loans were secured by equipment and goods valued at USD 110 million.

(ii) The loan from the Amsterdam Trade Bank in the amount of USD nil (2006: USD 66 million) was denominated in Euros at a fixed rate of interest of 9.59%. The loan was secured by equipment and goods valued at USD 78 million.

Transactions with related parties were performend on an arm's length basis.

## 37. SIGNIFICANT SUBSIDIARIES

| | Principle Activity | Country of incorporation | Effective ownership interest on 31 December 2007 % | Effective ownership interest on 31 December 2006 % |
|---|---|---|---|---|
| ***Holding companies*** | | | | |
| Amtel Exports PTE Limited | Investing | Cyprus | 100 | 100 |
| Tapistron Limited | Investing | Cyprus | 100 | 100 |
| OAO Amtel-Vredestein | Sales and distribution | Russia | 100 | 100 |
| ***Production companies*** | | | | |
| *Voronezh tyre plant* | | | | |
| OOO Amtel Chernozemye | Tyre manufacturer | Russia | 100 | 100 |
| OAO Shinny Komplex Amtel Chernozemye | Tyre manufacturer | Russia | 100 | 100 |
| OOO Tekhnopark | Investing | Russia | 100 | 100 |
| *Kirov tyre plant* | | | | |
| OOO TD Kirovsky Shinny Zavod | Sales and distribution | Russia | 90 | 90 |
| OOO Vyatskaya Shina | Sales and distribution | Russia | 90 | 90 |
| OAO Shinny Komplex Amtel Povolzhye | Tyre manufacturer | Russia | 90 | 90 |
| *Moscow tyre plant* | | | | |
| Moscow Tyre Plant – M ZAO | Tyre manufacturer | Russia | 100 | 100 |
| Shintekh OOO | Investing | Russia | 100 | 100 |
| *Kemerovo Chemical Fiber Plant* | | | | |
| OOO Khimvolokno Amtel-Kuzbass | | Russia | - | - |
| ***Retail chain*** | | | | |
| OOO AV-TO | Investing | Russia | 100 | 100 |
| OOO Rosshina-Master | Retail outlet | Russia | 100 | 100 |
| OOO Russina-Zapchasti | Retail outlet | Russia | 100 | 100 |
| OOO Lamel | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Ufa | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Region | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Volgograd | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Ekaterinburg | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Perm | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Nizhni Novgorod | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Rostov-on-Don | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Kaluga | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Samara | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Tolgiatty | Retail outlet | Russia | 100 | 100 |
| OOO Nord-Tyre | Retail outlet | Russia | 100 | 100 |
| OOO Nord-Avto | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO St. Petersburg | Retail outlet | Russia | 100 | 100 |
| OOO AV-TO Moscow | Retail outlet | Russia | 100 | 100 |
| | | | 100 | |

| | Principle Activity | Country of incorporation | Effective ownership interest on 31 December 2007 % | Effective ownership interest on 31 December 2006 % |
|---|---|---|---|---|
| ***Wholesale companies*** | | | 100 | |
| OOO TD Megashina | Sales and distribution | Russia | 100 | 100 |
| OOO TD Pigma | Sales and distribution | Russia | 100 | 100 |
| OOO Pigma NN | Wholesale distributor | Russia | 100 | 100 |
| OOO Export Zapchast | Wholesale distributor | Russia | 100 | 100 |
| OOO Servis Avtomobiley | Wholesale distributor | Russia | 100 | 100 |
| OOO Pigma Voronezh | Wholesale distributor | Russia | 100 | 100 |
| OOO Roznichnaya Torgovlya | Wholesale distributor | Russia | 100 | 100 |
| | | | 100 | |
| ***Vreredestein Group*** | | | 100 | |
| Vredestein Banden B.V. | Tyre manufacturer | The Netherlands | 100 | 100 |
| Vredestein Consulting B.V. | Consultancy | The Netherlands | 100 | 100 |
| N.V. Vredestein SA | Sales office | Belgium | 100 | 100 |
| Vredestein GmbH | Sales office | Germany | 100 | 100 |
| Vredestein (UK) Ltd | Sales office | UK | 100 | 100 |
| Vredestein France SA | Sales office | France | 100 | 100 |
| Vredestein Italia Srl | Sales pffice | Italy | 100 | 100 |
| Vredestein Norge A/S | Sales office | Norwey | 100 | 100 |
| Vredestein GesmbH | Sales office | Austria | 100 | 100 |
| Vredestein Iberica SA | Sales office | Spain | 100 | 100 |
| Vredestein Daeck AB | Sales office | Sweden | 100 | 100 |
| Vredestein Maloya AG | Sales office | Switzerland | 100 | 100 |
| Vredestein USA | Sales office | USA | 100 | 100 |
| Vredestein Kft | Sales office | Hungary | 100 | 100 |
| ***Other companies*** | | | 100 | |
| Melina Investments | Investing | BVI | 100 | 100 |
| OOO Amtel – Logistics Center | Investing | Russia | 100 | 100 |
| OOO Amtelshinprom | Investing | Russia | 100 | 100 |

## 38. SUBSEQUENT EVENTS

### *(i).* Completion of MTP-M sale

As described in Note 8 the Group has completed the disposal of the Moscow Tyre Plant-M, its 100% subsidiary in March 2008. The total transaction value was $77 million which comprised the amount paid for 100% of the shares of MTP-M including all intercompany debts due to the Group companies, as well as external MTP-M debts which have been assumed by the buyer. The proceeds have been utilised to reduce the existing Group's debt to Sberbank, which holds a pledge over MTP-M shares, and to fulfil certain obligations related to the 2006 MTP-M acquisition from OJSC Moscow Tyre Plant.

### *(ii).* Announcement and termination of Sibur Transaction

On 30 June 2008 the Group entered into an agreement with OJSC SIBUR Holding ("SIBUR Holding") and OJSC SIBUR-Russian Tyres ("SRT") setting out the terms and conditions on which it was proposed that the Group would acquire the entire issued share capital of SRT (the "Transaction Agreement") and SIBUR Holding would become a principle shareholder in the combined group.

Closing of this acquisition was subject to a number of conditions precedent set out in the Transaction Agreement. These conditions needed to be fulfilled by 30 September 2008 unless they were waived by the relevant parties. These conditions included the execution of subscription letters in respect of US$100 million of new shares in the Company and US$50 million new shares which were to be subscribed by SIBUR Holding. On 30 September 2008, these and certain other conditions were not fulfilled and the Agreement was terminated in accordance with its terms.

### *(iii).* Suspension from Trading on UKLA

In accordance with the UK Listing Rules and due to the size of the possible Transaction with Sibur, its impact on the Group and the fact that, OJSC SIBUR-Russian Tyres ("SRT") is privately held, Amtel-Vredestein GDRs have been suspended from trading from the date of the announcement of Sibur Transaction (i.e. 30 June 2008).

### *(iv).* Suspension of production at Kirov and Voronezh

Starting the second half of October 2008, production at the Kirov and Voronezh manufacturing facilities has been suspended until the beginning of December as a result of the working capital shortage faced by the Group. The production was further suspended in January with uncertain restart date due to uncertainty of market situation and availability of working capital. The production suspension does not affect Vredestein Banden BV where production is at its normal levels. The Group continues to explore a number of options to reduce the high levels of debt under which the Russian part of the Group continues to operate. The options being explored include the sale of certain of the Group's assets and/or divisions or the Group as a whole.

### *(v).* Payment acceleration requests

As part of the terminated Sibur transaction, described above, the Group was in the process of renegotiating all of its principal repayments due under the existing credit facilities. The principal repayments due prior to 31 December 2012 were supposed to be deferred to 31 December 2012 and interest up to 30 June 2009 was supposed to be capitalised, the capitalised interest to be repaid on a quarterly basis commencing on 31 March 2011. The total value of loans and borrowing to be deferred was USD 480 million. This restructuring was subject to agreement of all the financing banks and completing merger with SRT prior to end of December 2008, which conditions have not been satisfied.

During last quarter of 2008, due to termination of Sibur transaction, the Group has received payment acceleration requests from SRT and several of the banks lending to its Russian operations under its existing facilities. Some of the banks and SRT claims have been filed with the courts in Russia and the Netherlands. The Group will be unable to fulfil these requests unless an alternative settlement solution can be agreed. The Group is currently in discussions with SRT and the lenders and hopes to negotiate a standstill agreement which will enable it to pursue value realisation options. Please refer to the Note 2(i).

***(vi).* Plans to sell Dutch operation unit and changes in the composition of Executive Board**

The Dutch subsidiary of the Group, Vredestein Banden B.V. ("VBBV") continues as going concern due to the separate financing arrangements it has in place with a consortium of Dutch banks secured on assets and shares of VBBV. In order to ensure the long term sustainability of VBBV, the Group is conducting a sale process for VBBV and several potential bidders are conducting due diligence following the submission of preliminary offers. In connection with this process, the Group and VBBV are also in discussions with finance providers of VBBV. The Group is determined to conclude a successful sale of VBBV in the near term providing maximum value to all stakeholders. However, there can be no certainty that the sale of VBBV will be successfully concluded. Due to a potential conflict of interest in respect to a possible sale of VBBV, Mr R.H. Oudshoorn, Mr K.T. Hettema and Mr M.A.A. Luyten, who are also managers of VBBV, confirmed their intention to resign from the Executive Board of the Group. These resignations became effective from Monday 15th December 2008. After their resignations and the prior resignation of Mr I. Ivanov, the Executive Board of the Group comprises two members, being Mr P. Zolotarev as CEO and Director A, and Mr V. Pesochinsky as a Director B.

Amsterdam, 31 December 2008

The consolidated statements were prepared on 31 December 2008 by the Executive Board of Directors.

| | |
|---|---|
| Petr Zolotarev<br>Director A | Vadim Pesochinskiy<br>Director B |

## AMTEL-VREDESTEIN N.V.

### STATUTORY BALANCE SHEET BEFORE APPROPRIATION OF NET RESULT FOR THE YEAR AS AT 31 DECEMBER 2007

| *In million USD* | Notes | 2007 | | 2006 | |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| Non-current assets | | | | | |
| Financial fixed assets | (vi) | 305 | | 459 | |
| | | | 305 | | 459 |
| *Current assets* | | | | | |
| Trade and other receivables | (vii) | 118 | | 156 | |
| | | | 118 | | 156 |
| | | | **423** | | **615** |
| *Shareholders' equity* | *(viii)* | | | | |
| Issued capital | | 1 | | 1 | |
| Additional paid in capital | | 474 | | 460 | |
| Legal reserve | | 13 | | 13 | |
| Foreign currency translation reserve | | 58 | | 22 | |
| Retained earnings | | (94) | | (89) | |
| Net result for the period | | (243) | | (5) | |
| Total equity | | | 209 | | 402 |
| *Current liabilities* | | | | | |
| Short-term intra-Group loans | | 211 | | 206 | |
| Other paybles – intra-Group | | 2 | | 1 | |
| Other paybales - external | | 1 | | 6 | |
| | | | 214 | | 213 |
| | | | **423** | | **615** |

## AMTEL-VREDESTEIN N.V.

### NOTES TO THE 2007 STATUTORY COMPANY BALANCE SHEET AND STATEMENT OF OPERATIONS

| *In million USD* | 2007 | 2006 |
|---|---|---|
| Share in results from participating interests, after taxation | (197) | (4) |
| Other result after taxation | (46) | (1) |
| **Net loss** | **(243)** | **(5)** |

### *(i).* General

The separate Company only financial statements are part of the annual report 2007 consolidated financial statements of Amtel-Vredestein N.V. with reference to the separate statement of operations, Amtel-Vredestein N.V., use has been made of the exemption pursuant to Section 402 of Book 2 of the Netherlands Civil Code.

### *(ii).* Principles for the measurement of assets and liabilities and the determination of the result

For setting the principles for the recognition and measurement of assets and liabilities and determination of the result for its separate financial statements, Amtel-Vredestein N.V. makes use of the option provided in section 2:362 (8) of the Netherlands Civil Code. This means that the principles for the recognition and measurement of assets and liabilities and determination of the result (hereinafter referred to as principles for recognition and measurement) of the separate financial statements of Amtel-Vredestein N.V. are the same as those applied for the consolidated EU-IFRS financial statements. Participating interests, over which significant influence is exercised, are stated on the basis of the equity method. These stand alone EU-IFRS financial statements are prepared according to the standards laid down by the International Accounting Standards Board and adopted by the European Union (hereinafter referred to as EU-IFRS) and Title 9 of the Dutch Civil Code. Please see pages 11 to 22 for a description of these principles.

### *(iii).* Going Concern

Refer note 2(i).

### *(iv).* Principles for the valuation of assets and liabilities and the determination of the result

The principles for the valuation of assets and liabilities and the determination of the result are the same as those applied to the consolidated statement of operations.

### *(v).* Result from participating interests

The share in the result of participating interests consists of the share of Amtel-Vredestein N.V. in the result of these participating interests. Results on transactions, where the transfer of assets and liabilities between Amtel-Vredestein N.V. and its participating interests and mutually between participating interests themselves, are not incorporated insofar as they can be deemed to be unrealized.

### *(vi).* Financial fixed assets

| *In million USD* | 2007 | 2006 |
|---|---|---|
| Participating interests in Group companies | 111 | 278 |
| Accounts receivable from Group companies | 190 | 172 |
| Other receivables | - | 6 |
| Deferred tax assets | 4 | 3 |
| | **305** | **459** |

The movements of the participating interests in Group companies (refer to note 37) can be shown as follows:

| *In million USD* | 2007 | 2006 |
|---|---|---|
| Position as at 1 January | 278 | 280 |
| Result | (197) | (5) |
| Foreign currency translation | 30 | 3 |
| **Position at 31 December** | **111** | **278** |

## *(vii).* Trade and other receivables

| *In million USD* | 2007 | 2006 |
|---|---|---|
| Accounts receivable from group companies | 113 | 156 |
| Other receivables | 5 | - |
| | **118** | **156** |

***Movement in accounts receivable from group companies***

| *In million USD* | 2007 | 2006 |
|---|---|---|
| Opening balance | 156 | 170 |
| Net movement | (43) | (14) |
| Closing balance | **113** | **156** |

## *(viii).* Shareholders' equity

| *In million USD* | Share Capital | Additional paid in capital | Foreign currency translation reserve | Legal Reserve | Retained Earnings | Net result for the year | TOTAL |
|---|---|---|---|---|---|---|---|
| Balance at 31 December 2005 | 1 | 457 | (11) | 12 | (7) | (81) | 371 |
| Appropriation of result for the prior period | - | - | - | - | (81) | 81 | - |
| Legal reserve | - | - | - | 1 | (1) | - | - |
| Equity settled employee benefits | - | 3 | - | - | - | - | 3 |
| Translation result | - | - | 33 | - | - | - | 33 |
| Loss for the period | - | - | - | - | - | (5) | (5) |
| **Balance at 31 December 2006** | **1** | **460** | **22** | **13** | **(89)** | **(5)** | **402** |
| Appropriation of result for the prior period | - | - | - | - | (5) | 5 | - |
| Legal reserve | - | - | - | - | - | - | - |
| Equity settled employee benefits | - | 14 | - | - | - | - | 14 |
| Translation result | - | - | 36 | - | - | - | 36 |
| Loss for the period | - | - | - | - | - | (243) | (243) |
| **Balance at 31 December 2007** | **1** | **474** | **58** | **13** | **(94)** | **(243)** | **209** |

In specific circumstances legal reserves must be created in accordance with Part 9, Book 2 of the Dutch Civil Code. The legal reserves comprise the translation reserve, and development costs reserve. If a legal reserve has a negative value no payments can be made from the other reserves up to the level of the negative value(s).

*Issued capital*

The authorised capital of Amtel-Vredestein N.V. amounts to USD 3 million (2006: USD 3 million), divided into 222,148,650 ordinary shares of EUR 0.01 each, of which 68,281,803 ordinary shares have been issued (2006: 68,176,803). In 2007, 105,000 ordinary shares were issued to the management (2006: 36,000).

*Foreign currency exchange translation reserve*

Exchange differences resulting from the conversion of foreign entities (including group loans to foreign units). In the case of the sale of a participating interest, the associated accumulated exchange differences are transferred to the other reserves.

*Legal reserve*

Legal reserve has been recognised in respect of research and development cost which were capitalised as a part of intangible fixed assets.

*Retained earnings*

The General Meeting of Shareholders will be asked to approve the results for the 2007, net loss: an amount of USD 243 million. No dividend will be declared.

### *(ix).* Board of Directors

*Option schemes*

Members of the Executive Board were awarded an option scheme to obtain shares in Amtel-Vredestein N.V. – refer note 26(ii) .

*Personnel*

During the period under review, the Company has a Board of Supervisory Directors who received fixed remuneration – refer note 36(ii).

### *(x).* Off-balance sheet commitments

Reference to consolidated financial statements.

### *(xi).* Tax entity

Amtel-Vredestein N.V. forms a fiscal entity together with its Dutch subsidiaries for corporation tax purposes; the standard conditions stipulate that each of the companies is liable for the corporation tax payable by all companies belonging to the fiscal entity.

***(xii).* Share in results from participating interests**

This concerns the share of Amtel-Vredestein N.V. in the loss of its participating interests, of which an amount of USD 243 million concerns group companies (2006: USD 4 million).

***(xiii).* Emoluments of directors and supervisory directors**

The emoluments, including pension obligations as intended in Section 2:383(1) Netherlands Civil Code, which were charged in the financial year to Amtel-Vredestein N.V. and group companies, amounted to USD 21 million (2006: USD 5 million) for Directors and former Directors – refer note 36(ii).

There were no loans, prepayments and guarantees granted to the company's directors and company's supervisory directors.

***(xi).* Provisions in the articles of association governing the appropriation of profit**

Under article 39 of the company's articles of association, the profit is at the disposal of the General Meeting of Shareholders, which can allocate said profit either wholly or partly to the formation of – or addition to – one or more general reserve funds.

The Company can only make payments to the shareholders and other parties entitled to the distributable profit insofar as the shareholders' equity is greater than the paid-up and called-up part of the capital plus the legally required reserves.

***(xii).* Commitments**

Under Section 2:403 of the Dutch Civil Code the company accepts liability for the debts incurred by a Dutch group company. The relevant declaration has been filed for perusal at the office of the Trade Register within whose jurisdiction the group company falls.

***(xiii).* Subsequent events**

Refer note 38 of the consolidated financial statements.

Enschede, 31 December 2008

The consolidated statements were prepared on 31 December 2008 by the Executive Board of Directors.

| | |
|---|---|
| Petr Zolotarev<br>Director A | Vadim Pesochinskiy<br>Director B |

Enschede, 31 December 2008

**The Supervisory Board**

Rafael Nagapetyants (Chairman)

Hendrik W. ten Bosch

Daniel Gupta

Hubert Pandza

Maxim Ignatiev

**ANNUAL REPORT 2007**

KEY RESULTS

Amtel-Vredestein sold over 19 million tyres in 2007. This included over 14 million PCT in the *Premium* "A", *Value* "B" or Discount "C" segments – a 9% increase over the previous year. Net revenue from the Company's core PCT business grew 20% to $612.4 million. Sales grew steadily across most businesses in 2007, with healthy top line and margin growth at the Company's Russian manufacturing subsidiaries and good performance of Vredestein Banden operations.

Gross profit on a continuing operations basis improved to $234 million in 2007 from $185 million in 2006 – an increase of 26.5%. However, the gross profit margin remained broadly the same at 23.5% in 2007 versus 23.1% in 2006.

Net loss for 2007 was $243 million, versus $5 million in 2006, principally due to significant asset impairment charges, additional non-cash tax charge related to $12 million deferred tax asset write down, increased costs, including interest expense and other factors.

CHAIRMAN'S FOREWORD

Dear Stakeholders,

2007 was one of the most difficult years in the history of Amtel-Vredestein N.V. It was a year in which the Company's growth was superseded by two fundamental weaknesses: our huge debt incurred to finance the expansion of previous years, and our resulting inability to adjust structural costs in line with global market volatility. The challenges faced in 2007 – over-capacity, rising costs, growing competition – intensified and significantly weakened our business.

Obviously, this is unsustainable and runs contrary to our projections from 2006, and that raises a critical point. Deleveraging the Company is crucial, and we are working intently to achieve that goal. But our objective is not just to manage the debt; our fundamental goal is to transform the Company for the long haul, to structure it for sustained profitability and growth. Major actions to accomplish this included negotiations with creditors on debt restructuring and with market peers on possible business combinations. We've made good progress in these complex negotiations over the past few months, and continue to be hopeful that a solution can be found soon that is in the best interests of the Company and its stockholders.

In 2007, we laid out and began to implement a turnaround plan aimed at strengthening our competitive position, deleveraging the Company and achieving strong business results for years to come. The last two points of the plan led to some difficult and painful decisions that required sacrifices from virtually everyone with a stake in the Company:

- We announced plans to dispose of the Moscow Tyre Plant, making redundant the workforce and relocating the equipment to other production facilities. The reason for this was the limited demand for MTP brand tyres, and the high cost of operations there due to its Moscow location, which made it inefficient to continue there.
- We suspended the Voronezh II project due to a shortage of funds that made it impossible to complete the new tyre complex. Production at Voronezh II is scheduled to start late 2008 - 2009, provided we settle our most acute issues.

- We suspended further expansion of our AV-TO retail unit and are going through a careful evaluation of our current retail asset portfolio.
- We started to look more openly to potential strategic and restructuring options the company may face

In view of the challenging market environment, which was generally more difficult than the previous year, our operational achievements are particularly gratifying. 2007 brought a yield of $997 million in sales (22% growth vs. 2006) and over 19 million in units of tyres sold. The Company continued to demonstrate the steady growth of PCT output in line with our strategy to focus on the high-margin product range. Key factors behind this growth are our continued efforts to reestablish the Vredestein brand on the Russian market – and its booming premium segment – along with surging demand from OEM partners we are well-suited to satisfy. Specifically, last year was marked with exclusive contract the company has signed to supply Amtel tyres for Renault Logan and Fiat Albea passenger cars produced in Russia.

This year demonstrated the first results of the technological integration of the business. Amtel Russian plants started production of the completely new Planet-3 tire, which was developed in cooperation with the Vredestein design center. We expect continued effort in 2008 as we launch new products and expand our brands.

Amtel-Vredestein N.V. continues to place a high priority on operational safety, environmental protection and R&D. In doing so, we've taken ambitious initiatives and in 2007 obtained further certification of full compliance with the ISO 14001:2004 standard of systems on ecological management for our Kirov facility. This positions us as a responsible manufacturer and enables to respond to anticipated future regulations that are getting more stringent each year. With our R&D consistently on track, in 2007 we kept modernizing our production toolbase, making it more efficient and effective, and thus confirmed our commitment to industrial risk prevention and environmental protection.

We recognize that our stockholders have shared the pain as the Company has struggled over the past year. We appreciate your patience and advice, and we are committed to continue looking for ways of making your investment in Amtel-Vredestein N.V. a profitable one. Managing the significant financial burden of the past is a daunting task and success cannot be guaranteed. But it also gives us an opportunity to lead this unique company into a new era of growth and success in providing the world with innovation in transportation. I am confident that we'll emerge from these challenging times stronger, smarter, and a better global competitor.

Rafael Nagapetyants
Chairman of the Supervisory Board

CEO INTERVIEW

**Facing Challenges**
an interview with Chief Executive Officer and Chairman of the Executive Board Petr Zolotarev

*Amtel-Vredestein faced one of its most challenging years in 2007, even as our core passenger tyre business remained strong. But growth stalled due to the significant amount of debt it had accrued in recent years, and the Company faced challenges of over-capacity, growing raw material costs, and increased competition.*

*The Company is taking many necessary steps to solve this problem. These include not only working with creditors to manage the debt, but to fundamentally reshape the business to compete for the long haul. CEO Petr Zolotarev, who joined the company in July 2007, here explains the situation and how he intends to restructure the Company for sustained profitability and growth.*

**Q: What are the main achievements and disappointments that characterized 2007?**

"Although we delivered strong operational results in our core passenger tyre business last year, there are a number of reasons why 2007 proved difficult for us. Some of the challenges we faced relate to our market position – over-capacity, rising costs for doing business and for the raw materials that are essential for what we do, plus growing competition as markets continue to shift and develop. Each of these factors intensified last year.

But the biggest problem is simply that the Company's debt incurred to finance its rapid expansion and development over the past few years has put a strain on the Company's liquidity. When coupled with investments that did not pan out as hoped – like acquiring the Moscow Tyre Plant and retailer AV-TO – it created a difficult predicament for us.

Despite this, our central business remains strong. In 2007, our net sales rose by 22% from $817.4 million in 2006 to $997.4 million. Our net revenue from passenger car tyre sales grew 21%, to $615.8 million. The Company sole a total of 14.2 million passenger tyres last year, up from 13 million the year before, which is a 9.3% increase."

**Q: How does the Company plan to manage its debt, to let these strong fundamentals step out of its shadows?**

"The restructuring of our debt is going to be a major priority for 2008 I'm happy to report that we've made good progress in recent months in these very complex discussions with our advisors and creditors. Despite a number of attempts not leading to practical results including the agreed merger with SIBUR Russian Tyre I'm still hopeful that we can find a solution that will be in the best interest of all creditors, the Company and its shareholders. The very existence of the company and continuation of production through 2008 can be considered a partial success. We also have not ruled out broader strategic options, including possible business combinations with other market peers. We've begun some conversations to explore different possibilities."

**Q: What has the Company done in regard to its loss-producing assets?**

"In light of our position, and the overall competitiveness of our market, we realized last year that we would need to urgently resolve several issues relating to the underperforming assets within the Company.

"Among the main issues was the Moscow Tyre Plant, which Amtel-Vredestein acquired in 2006.

The cost of doing business in a major city like Moscow, plus the limited market demand for the tyre brands produced there, outweighed any benefits the plant could provide. So in March 2008 we sold the plant for $77 million, with proceeds going to reduce the company's existing debt and to fulfill certain obligations related to the acquisition of the plant. As part of the deal, we are still considering various options to relocate some of the plant's equipment, including possibly moving it to our other facilities.

We are currently still assessing our strategy regarding retailer AV-TO. Until we have chosen a clear path forward regarding this division, we have suspended any further expansion."

**Q: What global and domestic market trends do you anticipate will play the biggest roles in 2008?**

We anticipate an increasingly more difficult business environment that will be characterized by significantly higher raw materials costs, inflationary pressure on consumer behavior and tougher competition.
On the positive side, car sales in Europe are growing, and in Russia, sales of foreign cars are continuously growing at a steady rate, which is a good sign as we continue to emphasize our lines of premium and mid-range tyre brands. Sales of discount tyres appear to be slowing, and we are continuing to scale back our presence in this market segment."

**Q: What impact will the ever-growing cost of raw materials play in the future?**

"The cost of raw materials continues to rise, as most of the materials our industry uses are closely linked to oil prices, which as everyone knows skyrocketed in 2007 and continue to be highly volatile. This is an unfortunate fact of life for our business. These increases continue to put pressure on our margins, and some of these cost increases must be passed on to the consumer. However, our continuing emphasis on the higher-level "A" and "B" market segments rather than the lower margin "C" segment will help us manage this situation.

**Q: Could you give us an update on the Company's plans for its Voronezh II project?**

"The development of our Voronezh II facility is one of our most important projects going forward. While test production there began in May 2007, a shortage of funds has made it hard to complete the new complex when we would have liked. At this point, the mixing hall has been built, but the mixers and downstream equipment have yet to be installed. We have pushed back our full start-up date to some time after a solution for the Company's debt problems will be found.

This is going to be one of the most advanced tyre manufacturing facilities in Europe when it is completed, and will begin by making our Amtel brand of tyres. Soon after it will expand to make Vredestein and Maloya tyres for Europe. We will have invested about $124 million in the facility, which we are designing based on our Vredestein Banden plant in the Netherlands. It will be able to produce over 2.5 million passenger and truck tyres a year, which in addition to our existing manufacturing capacity at the Amtel-Chernozemye facility will make it a core element of our future.

**Q: How are the Company's brands currently positioned in the market? And can you explain new brands that have been launched, and what old lines have been abandoned?**

"Our core brands remain strong, and are known across Europe for their value and performance. They include our high-performance Vredestein tyres, as well as our well-known midpriced brands Amtel and Maloya.

We are not content to rest on our laurels, and have unveiled some new brands that we expect will follow our tradition of proven success. In September 2007, we introduced our new Nord-Trac Xtreme and Icetrac tyres in Moscow. These are each designed especially to handle snowy and icy road conditions with exceptional traction and control.

Among our other brands, we are confident about the future of our specialized agricultural and industrial tyres. In 2007, we continued our effort to remain an industry leader in bicycle tyres. We introduced three new tyre brands after extensive research and design, and with the help of the Cannondale-Vredestein Mountainbike Racing team.

**Q: In the face of all this market uncertainty, the company continues to produce outstanding tyres for a variety of market segments. How is it able to continue to perform at such a high level?**

"A great deal of Amtel-Vredestein's success can be attributed to our passionate commitment to research and development. This enables us to always push the envelope of what we can do, and to pass these innovations onto consumers.

Consumers know quality when they see it. In January, *Forbes* magazine published its list of the 50 best Russian brands based on retail sale volume from July 2006 to June 2007. Amtel is the only Russian tyre listed, in 34$^{th}$ place, up from 49$^{th}$ place in the previous year's list. And auto producers have also noticed the quality of our work. Even though it remains a relatively small portion of our business, more and more auto-makers are turning to us for original equipment, including a deal we signed last year to provide for Renault Logan and Fiat Albea car made in Russia.

**Q: What can we expect from Amtel-Vredestein in 2008 and afterwards?**

"We are committed to continue to pursue the course we have begun to follow, to not only alleviate our debt load, but to go further. We are not in the business of managing debt – we are in the business of making high quality tyres for a variety of consumers and markets. We are in the business of deploying the best research and development to manufacture outstanding products in the safest and most environmentally responsible way we can.

And at this critical moment in the Company's history, obviously a short-term task is to stabilize the Company. However our long-term goal remains to fundamentally transform the Company for the long-haul. We want to make it an operation for sustained profitability and growth for a long time to come."

## CORPORATE GOVERNANCE

Amtel-Vredestein aspires to the highest standards of ethical conduct and shareholder advocacy. These standards consist of a forthright approach to all corporate communications; reporting results and important information with accuracy and in a timely manner; as well as maintaining full compliance with all the laws, rules and regulations in each of the jurisdictions that govern the Company's businesses.

The Company regards it as a top priority to strengthen the trust placed in it by its shareholders. This includes openness to the investment community with a high degree of financial and operational transparency, and the existence of effective oversight mechanisms for the internal and external audit process.

The Company pursued several corporate governance goals in 2007. The first was to achieve a proper balance between entrepreneurship and control. The second was to facilitate performance-driven management, and provide leadership to ensure integrity and transparency in the decision-making process. The third was to enable the Board and management to pursue objectives in the best interests of the Company and its shareholders, and to create long-term value. The Company focused on these goals despite a challenging financial position, and the degree of ambiguity that presented.

Board structure optimization

One of the most visible manifestations of the Company's commitment to strong corporate governance principles is the composition of its Board of Directors and board committees. All their members are senior professionals educated in the Netherlands, Russia, the United States and United Kingdom. The key positions on the Board are held by specialists with an extensive experience of working for both Russian and multinational companies. In 2007, the Company's Supervisory board consisted of three independent members, and we are committed to further optimize the Board structure to achieve full compliance with the Dutch Code of Corporate Governance.

Financial reporting optimization

Transparency in financial reporting is another important aspect of corporate governance. Amtel Vredestein N.V. endorses financial reporting transparency by releasing semi-annual and annual reports under IFRS. While the Company has not been able to present semi-annual accounts over 2008, due to the restructuring efforts that are being undertaken, it aims to continue this past practice again in the future, also in order to fulfil its obligations under the relevant implementation rules of the Transparency Directive

We are convinced that creating value for our shareholders and adhering to the highest standards of corporate governance are essential to maintaining the trust of the investment community and maximizing the returns we generate for all our shareholders.

The Company understands that a sterling reputation for adhering to the highest standards is not granted, but only earned over an extended period. As we strive **to rethink our business** and meet the challenges of tomorrow, we are also determined to retain this trust and reputation through an unwavering commitment to our principles.

*Below we specify the areas where we focus our major efforts to enhance corporate governance in the Company.*

**General**

The provisions of the Corporate Governance Code (the "Code) took effect on January 1, 2005 and apply to annual reports for financial years starting on or after January 1, 2004. Dutch companies whose shares or depositary receipts are listed on a government-recognized stock exchange must discuss compliance with the Code in their annual report. If a company does not apply the best practice provisions of the Code, it must explain the reasons for any deviations.

Each year Amtel-Vredestein reviews and updates the Code – a document that details the Company's level of compliance with the Dutch Code of Corporate Governance, which is prepared as a separate addendum to the Annual report and can be easily accessed on the corporate website.

The Company complies with the Code, but, in the following areas, deviates from the best practice provisions included therein:

**Risk management and control**
The Company is aware of the necessity of the creation of an internal risk management and control system for the Group as a whole. The Audit Committee has already approved the Enterprise-wide Risk Management function development plan and budget. The Company is going to implement it after stabilizing its financial position (best practice provision II.1.3). The Executive Board shall declare in the next annual report that the internal risk management and control systems are adequate and effective and shall provide clear substantiation of this. In doing so, it shall describe any significant changes that have been made and any major improvements that are planned, and shall confirm that they have been discussed with the audit committee and the Supervisory Board (best practice provision II 1.4).

Internal control efficiency assessment is documented in the form of internal audit reports and internal audit working papers. Both sources so far reveal control inefficiencies and respective uncovered risks. Remediation is documented in the form of corrective actions plan, the execution of which is placed under tight control.

**Share options and awards**
The Code states that options to acquire shares are a conditional remuneration component, and become unconditional only when the Executive Board members have fulfilled predetermined performance criteria after a period of at least three years from the grant date. The Company does not apply this best practice provision because arrangements were established and approved by the Company prior to listing. The Company is going to produce a separate internal policy on this matter, which is subject to approval of the Supervisory Board (best practice provision II.2.1).

Best-practice provision II.2.3 of the Code treats the allocation of shares for no financial consideration as a form of variable remuneration. According to the Code, the purpose of a variable element should be to reinforce the Executive Board members' long term commitment to the company and the furtherance of its interests. This can be achieved by requiring Executive Board members who are allocated shares for no financial consideration to undertake to retain them for at least five years or until termination of their employment. Since these shares are allocated for no financial consideration, the best-practice provision requires that allocation be dependent on the achievement of clearly quantifiable and challenging targets, which have been defined in advance. The performance criteria must be stated in the remuneration report. II.2.3 Shares granted to EB members without financial consideration shall be retained for a period of at least five years or until at least the end of the employment, if this period is shorter. The number of shares to be granted shall be dependent on the achievement of clearly quantifiable and challenging targets specified beforehand.

The Company has not applied this best practice provision in the past because some arrangements were established and approved by the Company prior to listing. Going forward the Company is going to produce a separate internal policy under this matter, which is subject to decision of the Supervisory Board.

According to best practice provision II 2.14, the Company shall state in the notes to the annual accounts, in addition to the information to be included pursuant to article 2:383d of the Dutch Civil Code, the value of any options granted to the Executive Board and the personnel and shall indicate how this value is determined. The Company intends to apply this best practice provision and disclose information about options in the notes to its 2007 annual accounts.

**Regulations for transactions in securities in other companies**
One of the recommendations of best-practice provision II.2.6 of the Code is that the Supervisory Board should adopt regulations embodying rules on the ownership of and transactions in

securities by the Executive Board members other than those issued by their 'own' company. These regulations should be posted on the company's website. An Executive Board member shall give periodic notice, but in any event at least once a quarter, of any changes in his holding of securities in Dutch listed companies to the compliance officer or, if the company has not appointed a compliance officer, to the chairman of the Supervisory Board. An Executive Board member who invests exclusively in listed investment funds or who has transferred the discretionary management of his securities portfolio to an independent third party by means of a written mandate agreement is exempted from compliance with this last provision. The Company is not in compliance with this best practice provision II 2.6. The Company is not in compliance with this best practice provision as this provision is not relevant to the Company's business.

**Conflicts of interest**
All transactions in which there are conflicts of interest with Executive Board members shall be agreed on terms that are customary in the sector concerned. Decisions to enter into transactions in which there are conflicts of interest with Executive Board members that are of material significance to the Company and/or to the relevant board members require the approval of the Supervisory Board. Such transactions shall be published in the annual report, together with a statement of the conflict of interest and a declaration that best practice provisions II.3.2 to II.3.4 inclusive have been complied with. The Company applies this best practice provision and formalized this procedure in the By-Laws of the Executive Board. In 2007, conflicts of interest have arisen with members of the Executive Board that were of material significance to the Company and/or any of the members of the Executive Board being the following: - for the purpose of internal adjustment of inter-group debts the Company entered into the Transfer, Surety and Novation Agreements, pursuant to which all of the Company's obligations under Loan Agreement with Petrokommerts Bank # 20.2-07/20094 dated June 26, 2007 with the credit amount of $65 million have been transferred to OJSC "Amtel-Vredestein", a subsidiary of the Company.

**Independence of all but one Supervisory Board member**
All Supervisory Board members, with the exception of not more than one person, shall be independent within the meaning of best practice provision III.2.1. The Company is not in compliance with this best practice provision because of its current shareholding structure and arrangements between shareholders. In 2008 as for the date of adoption of 2007 Annual Report, the Supervisory Board of the Company consists of three independent and two dependent members. Further information about the composition of the Supervisory Board can be found on page 38 up to and including 39 of this report.

According to best practice provision III.2.2 a Supervisory Board member shall be deemed to be independent if the criteria of dependence as set out in the code do not apply to him.

The Company is not in compliance with this provision. One member of the Supervisory Board is affiliated with one of the current shareholders of the Company; another is a relative of the former SB Chairman

**Retirement schedule**
The Supervisory Board shall draw up a retirement schedule in order to avoid, as far as possible, a situation in which many Supervisory Board members retire at the same time. The retirement schedule shall be made generally available and shall, in any event, be put on the Company's website. The Company intends to apply this best practice provision III.3.6, as it is laid down in the By-Laws of the Supervisory Board, and develop and post to its website a rotation plan for the Supervisory Board members.
The Company is not in compliance with this provision so far. However, it is going to draw up a retirement schedule for the SB members upon improvement of its distressed financial condition and return to normal business operations.

**Internal Committees**
Principle III.5 requires the appointment of an audit committee, a remuneration committee and a selection and designation committee in case the Supervisory Board consists of more than four members. Our Supervisory Board consists of five members. The Company applies this best practice provision. The Supervisory Board has two key committees: the Audit Committee and a Remuneration & Nomination Committee (the latter being a combined remuneration committee and selection and appointment committee). The Company has adopted Regulations of the Remuneration and Appointment Committee and Charter of the Audit Committee, which have been posted on the Company's website (further information can be found on pages 40 - 46 of the annual report).

**Prior approval transactions between the Company and legal or natural persons who hold at least ten percent of the shares in the Company**
All transactions between the Company and legal or natural persons who hold at least ten percent of the shares in the Company shall be agreed on terms that are customary in the sector concerned. Decisions to enter into transactions in which there are conflicts of interest with such persons that are of material significance to the Company and/or to such persons require the approval of the Supervisory Board. Such transactions shall be published in the annual report; together with a declaration that best practice provision III.6.4 has been observed. The Company shall apply this best practice provision **III.6.4**. However, we've considered disclosing the fact of existence of some financing agreements with OJSC Alfa-Bank, which is affiliated with our shareholder. All these agreements are made on arm's length terms in the ordinary course of business.

**Further information on compliance with the Code**
Further information on compliance with the Code and the reasons for (partial) deviation of the abovementioned best practice provisions can be derived from the "Code" Corporate Governance of Amtel-Vredestein N.V. as attached to this annual report.

## Capital and shares

### Capital structure, shares

The authorised and issued capital of Amtel-Vredestein solely consists of ordinary shares. The 68,281,608 issued ordinary shares, which are all registered shares, are not listed on a stock exchange.

### Global Depositary receipts

Over 75% of the issued ordinary shares are held by Bank of New York Mellon. Bank of New York Mellon issues global depositary receipts ("GDRs") in exchange for these shares. The global depositary receipts are listed on the London Stock Exchange.

The GDRs can be exchanged, without any restrictions, for the underlying shares. An administrative fee may be charged for this.

### Issue of shares

According to its Articles of Association ("Articles") Amtel-Vredestein's authorised capital is EUR 2,346,428.50. New shares in excess of this amount can only be issued if the Articles are amended. An amendment has to be passed by notarial deed, which requires a declaration of no objection to be issued by the Minister of Justice.

Share issues are to be decided by the General Meeting of Shareholders ("General Meeting"), which may also delegate its authority. In 2005 the General Meeting resolved to delegate authority to the Supervisory Board to issue new ordinary shares or to grant rights to take up new ordinary shares, both with and without a right of first refusal for existing shareholders for a period of five years (ending on 14 April 2010).

On 29 August 2008 the General Meeting resolved, conditional upon the closing of the Transaction with OJSC SIBUR Holding to amend the Articles to enlarge the authorized share capital from EUR 2,346,428.50 to EUR 10,000,000 and to extend the authority of the Supervisory Board for a period of three (3) years as the corporate body to resolve to issue and/or grant rights to subscribe for (depositary receipts of) shares and to limit or exclude the pre-emptive rights with respect to such issuance and/or granting of rights to subscribe for (depositary receipts of) shares. The Supervisory Board is authorized to resolve to issue as many (depositary receipts of) shares as may be issued up to the maximum of the authorised share capital of the Company as it will read after execution of the notarial deed of amendment of the Company's Articles mentioned above. However on 30th of September 2008 Subscription agreement concluded with OJSC SIBUR Holding lapsed due to expiration of certain deadlines and the authorisation above may not be required.

**Transfer of shares and depositary receipts and transfer restrictions**

Shares are transferred by means of a deed of transfer between the transferor and the transferee. To become effective, Amtel-Vredestein has to acknowledge the transfer, unless Amtel-Vredestein itself is a party to the transfer. Pursuant to the Articles, there are no restrictions for the transfer of ordinary shares.

There are no restrictions for the transfer of GDRs pursuant to the Articles or the Depositary agreement.

Amtel-Vredestein is not aware of the existence of any agreement under which transfer of ordinary shares or global depositary receipts for such shares is restricted.

**Repurchase of shares**

Amtel-Vredestein may acquire fully paid ordinary shares at any time for no consideration, or, subject to certain provisions of Dutch law and its Articles, if (i) the shareholders' equity minus the payment required to make the acquisition, does not fall below the sum of called-up and paid-up share capital and any statutory reserves, and (ii) Amtel-Vredestein and its subsidiaries would thereafter not hold Shares or hold a pledge with an aggregate nominal value exceeding ten percent of the aggregate nominal value of the Company's issued share capital.

An acquisition of ordinary shares for a consideration should be authorised by the General Meeting. Such authorisation may apply for a maximum period of 18 months. Each year, the General Meeting is asked to approve the Executive Board's authority to repurchase shares. The current authorisation is valid until 29 December 2008. When repurchasing shares the Executive Board is to observe the following price ranges: between par value and 110% of the opening price at the stock exchange date on the date of purchase.

**Shareholders' structure**

The issued share capital on 31 December 2007 was 68,281.303 shares. On 31 December 2007 the following persons had an interest in Amtel-Vredestein and notified this to the Netherlands Authority for the Financial Markets in accordance with chapter 5.3 of the Dutch Financial Supervision Act.

| Shareholders | Directors | Shares/GDRs | Percentage |
|---|---|---|---|
| JP Morgan Chase & Co | | 8,069,555 (GDRs) | 11.84% |
| ABH Financial Limited | | 6,000,000 (Shares) | 8.80% |
| | R.H. Oudshoorn | 28,000 (GDRs) | 0.04% |
| | K.T. Hettema | 20,000 (GDRs) | 0.03% |
| | P. Zolotarev | (options lapsed on 2/7/08) | |

Amtel-Vredestein understands that the actual shareholders' structure is different than above which have been made public in the relevant public registers of the Netherlands Authority for the Financial Markets and is not based on any other sources known to Amtel-Vredestein.

**Voting rights on shares and GDRs**

**Voting rights on shares**

Each Person with Meeting Rights (as defined in Amtel-Vredestein's Articles shall be entitled to attend the General Meeting, to address the meeting and to exercise his voting rights. The Executive Board must be notified in writing of the intention to attend the meeting. The Executive Board must receive such notice not later than on the date mentioned in the notice of the meeting.

Each share shall give the right to cast one vote at General Meetings of Shareholders. Unless the Articles require a greater majority, all resolutions shall be adopted by an absolute majority.

Amtel-Vredestein is not aware of any contract under which voting rights on any class of its shares is restricted.

**Voting on GDRs**

Although the GDRs do not formally have any voting rights, holders of GDRs, in practice, can provide voting instructions in respect of the shares underlying their GDRs. More detail in respect of the GDRs and the rights of GDR holders is provided on pages 35 - 36 in the Executive Board Report.

The GDRs and the depositary structure would prevent a small minority of shareholders, which coincidentally may form the majority in the meeting, from taking decisions purely to suit themselves in the absence of other parties at the General Meeting.

**Other provisions**

**Special rights of control**

No special rights of control referred to in article 10 of the EU Directive on takeover bids are attached to any share.

**Amendments to the Articles**

A resolution to amend the Articles of Amtel-Vredestein, may be adopted by absolute majority of the votes cast at a General Meeting at which at least one third of the issued share capital is represented.

**Payments to Executive Board members upon the execution of a public offer**

The employment contracts with the members of the Executive Board provide for severance payments, which are to become due in case of termination of the contract in connection with a public bid defined in section 5:70 of the Dutch Financial Supervision Act.

If the Company initiates the termination of the employment agreement for a Dutch resident Executive Board member and if the termination is for a reason other than an urgent reason (cf. Section 7:677 of the Dutch Civil Code (*Burgerlijk Wetboek*), the Company and the Executive Board member will observe the provisions laid down in the Code. For this reason, the neutral Sub-District Court formula will serve as a basis for the calculation of the severance payment.

If the Company initiates termination of the employment agreement for Russian resident Executive Board member and if the termination is "without cause" as defined in the employment agreements, such member is entitled to severance benefits as set forth in the employment agreement.

If the Company initiates termination of the employment agreement of the CEO at the election of the Supervisory Board, without Cause, upon not less than sixty (60) days prior written notice of termination; (ii) due to a change of control of the Company; or, without cause within one year following a change of control of the Company, the CEO shall receive a lump sum payment by the Company in an amount equal to three times his annual base salary.

With respect to the amounts due, there is no difference as to whether termination of the contract would be in connection with a public bid or not.

**Appointment and dismissal of Executive Board members**

The General Meeting shall appoint the Executive Directors and may at any time suspend or remove any managing director. The Supervisory Board is also entitled to suspend a member of the Executive Board, but such suspension can be terminated at ant time by the General Meeting.

The Supervisory Board may make a nomination for Executive Board members to be appointed. If a resolution of the General Meeting is taken in accordance with a nomination of the Supervisory Board an absolute majority of votes cast is required for appointment of such member(s). If the General Meeting wishes to appoint a member of the Executive Board other than in accordance with the nomination by the Supervisory Board, such a resolution may only be taken by absolute majority in a meeting at which at least one third of the issued share capital is represented. If this quorum is not met, but an absolute majority of the votes cast at the meeting is in favour of the proposal an new General Meeting can be called at which the proposal can be adopted by absolute majority without any quorum being required.

Executive Directors are appointed for a maximum period of four years starting on the day after the day of the General Meeting where they are appointed and ending on the day of the annual General Meeting to be held in the fourth year after their appointment. Each managing director is eligible for immediate reappointment.

**Appointment and dismissal of Supervisory Board members**

The General Meeting shall appoint the members of the Supervisory Board and may at any time suspend or remove any such member. The members of the Supervisory Board will need to fit the profile as set out in the By-Laws Supervisory Board (as available on Amtel-Vredestein's website). If the General Meeting wishes to dismiss or suspend a member of the Supervisory Board other than in accordance with the proposal by the Supervisory Board, such a resolution may only be taken by absolute majority in a meeting at which at least one third of the issued share capital is represented. If this quorum is not met, but an absolute majority of the votes cast at the meeting is in favour of the proposal a new General Meeting can be called at which the proposal can be adopted by absolute majority without any quorum being required.

The Supervisory Board may make a nomination for Supervisory Board members to be appointed. If a resolution of the General Meeting is in accordance with the nomination of the Supervisory Board an absolute majority of votes cast is required for appointment. If the General Meeting wishes to appoint an executive director other than in accordance with the nomination by the Supervisory Board, such a resolution may only be taken in accordance with the same attendance and quorum rules as set out in the previous paragraph.

Members of the Supervisory Board are appointed for a maximum period of four years starting on the day after the day of the General Meeting where they are appointed and ending on the day of the annual General Meeting to be held in the fourth year after their appointment. Each director is eligible for immediate reappointment, save that such reappointment can - in principle - only take place twice.

**Dividends and other distributions**

The distributable profits shall be at the disposal of the General Meeting at the proposal of the Supervisory Board by a resolution adopted with a majority of seventy five percent (75%) of the votes cast by the Supervisory Board members present or represented and with due observance of the relevant provisions in the Articles.

The Company may make distributions to shareholders and other persons entitled to distributable profits only to the extent that the equity exceeds the sum of the paid and called-up part of the share capital and the reserves which must be maintained by law (after adoption of the annual accounts demonstrating that the distributions are permitted). In calculating the appropriation of profits, the shares held by the Company in its own share capital shall not be taken into account.

Amtel-Vredestein may make interim distributions of profits provided the provisions set out in the Articles are duly observed.

MARKETS

**Growing international demand for tyres**

The world tyre market continues to show stable annual growth. Sales of passenger car tyres (PCT) are projected to grow at a compounded annual rate of just over 3%, according to Global Industry Analysts, Inc. According to recent figures from the International Rubber Study Group, by 2010 the worldwide passenger car tyre market will reach nearly 1.17 billion units. The European market by that time will be at 385 million, the second-largest in the world. In 2006, European tyre sales reached 200 million, representing approximately 30% of the world market.

**European car sales continue significant growth**

Automobile sales in Europe showed healthy growth in 2007. According to the European Automobile Manufacturers' Association, production in Europe increased by 5.3% in 2007, with passenger cars accounting for 87% of the production. The biggest growth was in eastern Europe, with new European Union member states posting a 25.2% increase in auto production. In Europe, demand for new vehicles rose 1.8%, even though it was somewhat restrained by rising oil prices, tax changes, and a global credit crunch and declining purchasing power.

Forecasts from PricewaterhouseCoopers point to Russia becoming the second largest market in Europe for passenger cars after Germany with demand increasing to 2.7 million vehicles a year by 2010.

Although the growth rate in the auto market has shown some signs of slowing down, it is not expected to dramatically do so in Russia. On April 11, the director of the automotive division of Ernst & Young, Ivan Bonchev, told *Kommersant* that while there is a "modest slowdown in growth," he believed it "would not be serious." He predicted that total new Russian auto sales in 2008 would pass the 2 million mark.

And based on recent years, the Russian market remains sound. In Russia, positive growth in new sales since 2003 has never dropped below 50%, according to AutoStat, and last year came in at 63%. In that time, the market grew 6.7 times over – 9.4 times in terms of revenue.

**Rise in foreign car sales in Russia drives demand for premium tyres**

Sales for foreign cars continue to grow at a steady pace. In early April, the Association of European Business in Russia (AEB) reported that in the first quarter of 2007, foreign car sales had increased 74 percent over the previous year. The magazine AutoReview reported late in 2007 that for the first half of last year, nearly all foreign car producers increased their sales in Russia. Altogether, they amounted to 68% of the market for new cars – 710,600 passenger cars, which marks a 71% increase over the first half of 2006. At the same time, sales of domestic Russian brands declined during that time by 25% to 325,400 units.

This growth builds on a breakthrough year for the Russian market in 2006. Nearly 2 million passenger cars were sold in Russia in 2006, and in that the AEB revealed that foreign sales increased by 65% that year to over 1 million cars. In massing that important "million" milestone, foreign cars for the first time captured a majority of the Russian market.

Foreign car sales are linked to demand for premium tyres in Russia such as those produced by Amtel-Vredestein. The company estimates that by 2010, the passenger car tyre market for "A-class" tyres in Russia will amount to 14.9 million units, up from an estimated 10.2 million in 2007. This category includes foreign competitors such as Michelin, Goodyear, Bridgestone, and Pirelli. The market share of "B-class" tyres – which includes Kama, Hankook, Cordiant, and Matador -- is expected to grow to 16.4 million tyres in 2010, up from an estimated 12.5 million last year. This is a particularly strong category for Amtel-Vredestein, which estimates it holds a 37 percent market share in the "B-class."

**Sales of Discount tyres likely to continue to decline**

In the coming years, it is expected that the PCT market share for "C-class" discount tyres – where most Russian producers are active – will continue to shrink. In 2010, the company estimates the total market will amount to 12.7 million tyres, down from an estimated 14.1 million tyres last year.

Experts disagree over the future market share of each sector. Last year, Ernst & Young predicted that the share between premium "A-Class," value-for-money "B-Class," and discount "C-class" would become equal by around 2009, with each class accounting for about a third of the market. Other analysts anticipate the arrival of such a scenario may take a little longer, possibly until between 2010-2011, when foreign auto assembly plants based in Russia are expected to reach production capacity.

**Raw materials costs continue to rise**

Performance-related factors in the tyre manufacturing industry worldwide are inextricably linked to the price of raw materials, which continue to rise year after year.

Most of the materials used by the industry are extensively linked to the petrochemical industry. In particular, oil prices (based on NYMEX prices for Light Sweet Crude) began the year down, but quickly began a rapid recovery. By the end of the year, the price of oil had nearly doubled.

Rising demand and costs for synthetic rubber reflect similar trends to that for natural rubber over the past 3-4 years. Over 97% of natural rubber is produced in the Asiatic region. The International Rubber Study Group estimates that by 2010, global production of natural rubber will amount to 10,634,000 tonnes. Projections for synthetic rubber are expected to follow consumption levels closely, especially in the long-term.

Synthetic rubber production processes are also deeply connected to the petrochemical industry, and products used are directly linked to fluctuations in world prices for petroleum. These are often volatile and sensitive to world events. As prices soared in 2007, the knock-on effect was to increase synthetic rubber prices around the world.

Increases in the costs of raw materials inhibits margin growth in the short term, but ultimately leads to price increases across the tyre manufacturing industry worldwide.

BRANDS

**Amtel-Vredestein boasts a strong portfolio of brands**

*Vredestein* tyres are famous for their exceptional performance in all weather conditions, and are suited for a wide variety of luxury automobiles, including Audi, Mercedes, BMW, and Porsche. A tour de force of function and style, the Vredestein brand is the result of years of investment in research & development, and the use of state-of-the-art production techniques.

*Amtel* is the leading value-for money tyre brand in Russia, while *Maloya*, the Company's medium-priced brand, is an ever-popular choice across Europe for vans as well as passenger cars.

**New AV models and specifications in 2007**

More than 100 new tyre specifications have been added in recent years to the Company's fast-growing portfolio of tyre brands.

In September 2007, the Company unveiled its new *Nord-Trac Xtreme* tyre at the Moscow International Motor Show. This winter tyre was designed especially for Russia's extreme weather conditions. It is a low-noise tyre designed for high-powered cars, with a rubber tread with a special soft component that guarantees perfect traction on the most difficult roads. It was designed in cooperation with Italy's Giugiaro Design firm, and is a significant addition to the Company's line of premium tyres.

Also at the Moscow show, Amtel-Vredestein introduced its new *Icetrac,* which is built for snowy and icy roads. It features a mathematically optimised pattern of studs in 12 rows around the tyre to ensure excellent traction and perfect control. Among other advantages, the tyres are effectively self-cleaning, have a maximum zone of contact with the road, and enhanced durability.

**Amtel leads the Russian market for price and reliability**

Amtel is among the leading tyre brands in Russia, known for its outstanding value for money. The Amtel *Planet* line of tyres is suited for summer driving, while Amtel's *NordMaster* is designed for even the harshest Russian winters. Both lines are renowned for their reliability and safe-handling. With a high brand-awareness among consumers, it is one of Russia's best-known brands as well, according to market research agency GFK.

In 2007, the winter range was expanded with the addition of Icetrac tyre – a Vredestein A-segment sub-brand to be marketed in Russian Federation. Production of Icetrac tyres was launched at Kirov facility in 2007. Demand is growing and the additions were well received. Two sizes were also added to Amtel's *Planet DC* range in 2006 -- which beginning in 2007 are fitted on all Renault Logans manufactured in Russia . Two recent models added to the winter range in 2006 - the *NordMaster 2* and the *NordMaster CL,* Amtel's first unspiked winter tyre for use in cities in Southern Russia – were successfully expanded in 2007.
Several new models of Vredestein T-Track Si summer tyre were tested at Voronezh 2 facility; after the project was temporarily suspended the production resumed at Kirov factory.

Sales of Amtel tyres have been steady thanks to Russia's strong passenger car market. The brand performed very well in the value-conscious "B-class" segment of the market, where the Company's sales accounted for 37% of that market segment in 2007.

**The Swiss precision engineering of Maloya**

Maloya tyres are aimed at the upper-medium price range, and are well-known for their Swiss pedigree of precision and performance. Originally manufactured in Switzerland, Maloya tyres are now made in The Netherlands and at Amtel-Vredestein's plant in Kirov, Russia.

The brand includes a range of summer and winter tyres for passenger cars, as well as a popular range of all-season light truck tyres that keep vans transporting heavy loads at high speeds no matter the weather.

**Taganca**

Taganca tyres are one of Russia's best-known legacy discount brands, offering a wide choice of tyres at low prices. The brand was acquires together with Moscow Tyre Plant. However, 2007 revealed general inefficiency of business operations at Moscow Tyre Plant and virtually low demand for Taganca tyres, which made the Company rethink the destiny of the renowned brand. The production of Taganca was terminated and the brand was added to historical array of the Company's portfolio.

**Agricultural tyre brands continue to grow**

Agricultural tyre sales in 2007 sold well, primarily due to an improved range of products and by selling more premium products in the higher-class market segment. In the original equipment market the Company realized growth of 22.5% over the previous year. In the replacement market, the Company's market share is growing, thanks AV's unique *Traxion+* radial tractor tyres.

The agricultural sector of the market has changed fundamentally in recent years. Thanks to an ever-expanding global population that needs to be fed, and the brisk growth of the biofuels industry, agriculture is growing fast. Farming is increasingly more specialized and professionally-run, while farms themselves have increased in size. The result is a need for innovative machinery and equipment to meet demand. The industry is always searching for machinery that will improve efficiency and maximise yields by saving time, fuel, and reducing labour costs.

Thanks to our active product development program, in cooperation with the agricultural machinery industry, the assortment of of our tractor and other machine tyres in the premium market segment is growing. A recent tractor tyre test organised by several trade magazines in Germany reported outsstanding results for the *Traxion+*. During various industry exhibitions in Europe last year, we introduced the new *Flotation Trac* tyre.

**Industrial tyres that meet specialty needs**

The Company's range of industrial tyres provides performance and value for money for industrial vehicles, for fast traffic (up to 130 km/h), for slow traffic (up to 20 km/h) or for specific grassland and horticultural machinery. Our tyres are a combination of an innovative tread design, strong carcass, riding comfort and, of course, long lifespan.

**Space saver in the boot**

Spare tyres are not often needed, but they can be a life-saver when they are. The Company's focus on functional design extends to the compact design of its Space Master spare tyres – now original equipment in many models by Audi, Mercedes, Porsche and Volkswagen. The innovative design takes up a minimal amount of space when stored in the car boot, but once inflated by the included compressor, assumes the same diameter as the original, fitted tyre.

**Bicycle tyres that are a tour de force**

As more and more people put a priority on quality of life and exercise, the Company has developed a line of Vredestein bicycle tyres to help them lead an active lifestyle. The line includes a range of tyres for children's bikes as well as bicycles for trekking, touring, mountain riding, mopeds/scooters, and racing bikes.

In 2007 Vredestein Two Wheel Tyres continued concentrating on the sportive market segment. After ample market analysis and expansive input of the bike-riders from the Cannondale-Vredestein Mountainbike Racing Team three new MTB-tyres were developed:
The Tiger Claw XC-G that performs at its best on a dry hard surface; The Black Panther – a fast all-mountain tyre and The Bull Lock that performs exceptionally well in mud.

Before introducing above mentioned MTB-tyres they were subjected to an extensive testing programme. The tyres are meant for professional use, each one with specific qualities for different terrain conditions.
In March the official introduction of these tyres took place in Cannes as well as the Press presentation of the Cannondale-Vredestein Racing Team.
The sponsoring of the award-winning Predictor-Lotto Professional Cycling Team and the Cannondale-Vredestein Mountainbike Racing Team has contributed to higher brand recognition and a large amount of free publicity in 2007.

**Scooter tyres racing ahead**

Our *Staccata* and *Tornante* are the first *sports* and all-weather *touring* scooter tyres developed in collaboration with top Italian industrial designer Giugiaro Design.

Both tyres feature innovative and creative characteristics – including aggressive, sleek lines that give the tread a powerful look. The designs of the Staccata and Tornante are in keeping with developments in the scooter market, where design, comfort, safety and performance have become just as important as they are for passenger car tyres.

AV-TO

Amtel-Vredestein is now Russia's leading player in the three key sectors of tyre manufacture, distribution and retail -- giving the Company a unique strength with a capability to deliver unbeatable benefits in automotive and retail markets.

Amtel-Vredestein's decision to enter the retail sector in 2005 was based on two factors. First and foremost, to secure retail distribution and market recognition for its tyre brands in Russia, and second to establish a leading retail brand capable of capturing significant market share in a highly fragmented sector.

**Number One in Tyre Retail**

As of 31 December, AV-TO operates 92 multi-brand tyre sales and service centers under one unified brand in 13 cities throughout Russia, including , Kaluga, Maloyaroslavets, Moscow, Nizhny Novgorod, Perm, Rostov-on-Don, Samara, Salavat, St.Petersburg, Sterlitamak, Tolyatti, Volgograd, and Ufa. With the total number of 92 stores in 13 cities and the total number of over 400 thousand tyres sold in 2007 AV-TO is the largest tyre retailer in Russia.

In addition to Amtel and Vredestein brands (representing approximately 25 - 30% of AV-TO sales), AV-TO stores offer a full range of tyres, auto parts and accessories by other leading international producers. And many of its locations provide a full range of services including exhaust systems, break replacements, fluid changes and car washes.

However reaching profitability of the chain may require further expansion focusing on strengthening AV-TO's brand and buying power, product range and quality of services, as well as exploiting commercial opportunities in new sectors, like internet trade and new retail formats.

**A leading auto parts distributor**

Acquired in the second half of 2006 LLC Trade House "Pigma" operates 2 branches in Nizhniy Novgorod and Voronezh supplying a wide range of auto parts to a diverse customer base. AV-TO sells more than 27,000 auto components from approximately 40 producers to over 1500 customers throughout Russia and CIS. However, this business is not profitable and may not be considered as core business for a tyre company.

**Now a leading tyre distributor**

Tyre wholesale distributor LLC Trade House "Megashina", in addition to Amtel and Vredestein brands also distributes tyres from other leading international brands like Goodyear, Pirelli and Kumho (under Marshal brand) to over 1500 customers specialising in tyre sales, including tyre retailers, auto dealers and auto service stations. As of December 31, "Megashina" operates branches and warehouses in 14 major cities of Russia including Moscow, St. Petersburg, Nizhny Novgorod, Ekaterinburg, Chelyabinsk, Perm, Novosibirsk, Krasnoyarsk, Novokuznetsk, Rostov, Krasnodar, Samara and Voronezh. The total number of tyres sold by Megashina in 2007 exceeded 3mln units.

PEOPLE

Amtel-Vredestein's total workforce today amounts to about 9,500 dedicated employees working in 14 countries. The Company is proud of the work they do every day as the Company continues to steer a course to become one of Europe's premier high-quality passenger car tyre producers. Our success so far is the result of the cooperative effort and exemplary performance of our people at every level.

**Sustaining an optimal workforce**

In 2007, Amtel-Vredestein continued to follow through on plans to make its Russian plants more effective and its staffing levels consistent with standards throughout the tyre manufacturing industry for companies with similar production outputs. Over the course of the year, the Company reduced its total workforce by 4.5%, or about 425 positions. Most of the restructuring was at the Kirov plant, due to labour market problems there, and in the Company's AV-TO division, as work continued to optimize that division's organizational structure.

Last year, the Company reached a 3.5% absence rate, which is the lowest in Company history. On the job accidents in 2007 were down 80% compared to 2006.

**Investing in education**

Amtel-Vredestein remains proud of its outstanding training programmes for our personnel, which has raised the efficiency of plants throughout the Company and increased our capacity to produce top-quality products.

In 2007, more than 50% of Company employees, from a variety of positions and divisions within the company, participated in at least one of our training and development programmes. Whether they studied full-time or part-time, the programmes offered them a chance to build on their existing experience and acquire new skills.

Beyond in-house training sessions, about 25 people attended the Tyre Technology Course, which is a special course regularly organized by Vredestein Consulting at the Enschede factory.

Also, the Company unveiled its "Healthy Nutrition" project at several of the Company's plants, and has met with great success.

Education will remain a primary focus of the company. It is a critical component of our commitment to quality production, to maintaining a knowledgeable staff, and to achieving and maintaining the necessary quality and production standards.

**Preparing Voronezh-II**

The Company is continuing plans to launch its state-of-the-art Voronezh-II project later in 2008 - early 2009, which presents several unique staffing challenges. This plant – which will produce high-quality Vredestein tyres – is the product of close cooperation between our Dutch and Russian management teams, and Voronezh-II will have an organisational structure based on the model used by Vredestein at its Dutch plants. New staff has been hired and trained in accordance with Vredestein's high standards – including training programmes in Enschede with the new equipment they will be using. A new compensation and human resources development policy has also been implemented, focusing on high efficiency and productivity.

QUALITY, SAFETY & ENVIRONMENT

*Dutch quality and engineering applied to next generation of tyres for Russia*

Amtel-Vredestein has centralised the Company's Research and Development resources to its Enschede facility in The Netherlands. The move resulted in the development of a new tyre for Russia – the Amtel *Planet 3* – which was launched in June 2007. Amtel *Planet 3* tyres are inspired by the technology and design of *Maloya Crono* tyres and have a prominent "Designed by Vredestein" insignia.

*Certification goal set for all production sites*

Additionally, Amtel-Vredestein's goal is to further improve the overall quality of its design, management and production systems. The company achieved ISO/TS 16949 certification for its factories in Enschede and in Kirov in 2006 and confirmed its compliance in 2007. Its Voronezh plant is scheduled to follow in 2008.
Another significant achievement of 2007 was obtaining the ecological certification ISO/TS 14001. Amtel-Vredestein was the first to pass these stringent audit requirements, and was accredited for ISO/TS 14001 first among Russian tyre manufacturers, having proved its reputation as a responsible producer. Having all these certifications in place proves not only AV's high reputation and status among its peers, but also inspires the Company to review its relationship with suppliers and opt for better quality and environmentally safe materials. It also gives us an advantage in competing on the OE market by minimizing risk.

*Technology transfer improves efficiency*

In order to maximise co-operation within the international Research and Development groups, top Russian engineers have participated in a technology transfer programme at the Enschede facility. Now, strategies for all brands—Amtel, Maloya and Vredestein—are part of one comprehensive product development plan.

Amtel-Vredestein has also begun to collaborate with Dutch universities on two impressive PhD programmes to further increase technological research activities.

The Company continues to implement a policy of standardisation, which entails unifying the quality, choice of materials and construction basics for all tyres produced within the Group. This policy has prompted the Russian divisions of the Company to adopt the world market practice of specifications versus GOST practices widely used in Russia.

**Eliminating contact with hazardous substances**

Multiple actions have been taken to guarantee the health of Enschede plant workers. Virtually all hazardous substances have been eliminated from production processes, and Amtel-Vredestein is now working on alternatives to aromatic oils and complying, well in advance, with new European standards.

Concurrently, the Company is busy creating these same conditions for its plants in Kirov (Amtel-Povolzhye) and Voronezh (Amtel-Chernozemye).
The concept of a "green tyre" – a tyre produced without hazardous substances – is becoming more and more popular in Russia as consumers grow more sophisticated in terms of quality of life issues, and as the income level continues to rise.

**Setting a standard for environmental safety**

Environmental procedures have been undertaken throughout most of Europe to ensure that tyres are properly recycled. In The Netherlands, the Company has been the frontrunner in efforts to implement a reliable system for removing tyre waste and preventing unnecessary environmental harm.

Vredestein Banden and other manufacturers and importers charge each wholesaler/retailer €2 for every new tyre purchased a cost that is then passed along to customers. This money, constantly flowing between tyre manufacturers and sellers, is invested into an end-of-life tyre fund that sustains the operating costs of a government-approved recycling programme, and therefore guarantees that used tyres are disposed of properly. The recycling programme is functioning so well in The Netherlands that other countries in Europe now look to it as an example.

FACILITIES

Amtel-Vredestein in 2007 operated four tyre production facilities, in Enschede (The Netherlands), and in Kirov, Voronezh, and Moscow in Russia. Each of these facilties continued to undergo investment and reorganization to improve the quality of their production and efficiency in 2007. Amtel-Vredestein has been improving its production and management systems by working to obtain ISO TS certification at all of its factories.

**Amtel-Povolzhye, Kirov**

Production at the Amtel-Povolzhye Tyre Complex in Kirov has successfully catered to ever-growing demand in Russia and Europe. The facility is one of the most dynamically developing plants in the Russian tyre industry. After becoming part of the Amtel-Vredestein Group in 2003, the Company invested $40 million into bringing the quality of production up to international standards and began manufacturing premium tyres in 2005.

In September, the Complex received the ISO 14001:2004 Ecology Certificate and the Certificate of Accordance with the ISO/TS 16949:2002 quality standard. Amtel-Povolzhye is the first tyre plant in Russia to receive this Certificate in Quality Management, which is given for meeting strict criteria. This includes that the plant meets international standards of safety requirements, implements improvements in technological processes on an on-going basis, and guarantees reliable high quality production.

Audit certification for ISO 14001:2004 confirmed that Amtel-Povolzhye meets international ecological requirements in full. Application of the integrated environmental system ensures ecological safety in tyre production, optimization of resource conservation and prevention of environmental pollution at every stage of production.

The Amtel-Povolzhye plant takes its ecological responsibilities very seriously. With a dedicated laboratory for ecological monitoring and control, it keeps constant watch over air quality, noise levels, thermal emissions and other variables throughout all stages of production. The plant undertakes annual reviews of its environmental protection policy, including waste reduction, emissions control and waste disposal, consistent with Russian and international standards. It is fully compliant with Russian legislation regulating the use of natural resources, paying tens of millions of rubles each year in expenses related to environmental protection.

Amtel-Povolzhye produces more than 20 models of Vredestein tyres and more than 50 models of Amtel tyres, with a total production annually of approximately 7.2 million tyres and holds original equipment supply contracts with GM-AvtoVAZ and KIA as an original equipment supplier.

The quality of Vredestein tyres produced in Kirov fully complies with the original European standards produced at the Company's plant in Enschede, The Netherlands, and the plant has won numerous awards in different competitions, including gold medals in "The Best Tyre on the Russian Roads" contest from 2001 to 2005.

**Amtel-Chernozemye, Voronezh**

The Amtel-Chernozemye Tyre Production Complex is one of the largest tyre manufacturers in Russia. Founded in 1960, it was the first tyre plant in Russia to produce large-diameter tyres for road-building machinery. It was acquired by Amtel-Vredestein in 1999.

High quality production is the top priority of the plant and all passenger and light truck tyres meet Russian (GOST) quality control standards. The tyres also conform to the international rules of the United Nations Economic Commission for Europe and the plant has ISO 9001:2000 certification.

Amtel-Chernozemye was named winner of *Best Plant* at the international exhibition *Tyres, Rubber and Rubber Goods* in 2005, as well as winning a *Best Tyre on Russian Roads* gold medal the same year. In 2006, the plant's tyres were listed among the *100 Best Products in Russia*.

The nature and complexity of tyre production imposes particular responsibilities on tyre producers, particularly regarding the environmental safety of production processes. Environmental control at Amtel-Chernozemye is undertaken by a specialist laboratory, accredited by the Russian standards and certification agency, GOST R, and covers all manufacturing and production processes, as well as supporting functions and infrastructure.

The plant is also quite committed to its social responsibilities. Among its various community programmes, it offers full support of the Bobrovsky Residential School for Orphans and the No.5 Residential School for Sick Children in Voronezh, in co-operation with the Administration of the Voronezh Oblast.

*Voronezh II begins test production in 2007*

In May, Amtel-Chernozemye began test production at its new factory, months earlier than planned. By the time the factory is completed, the company plans to have invested approximately $124 million in Voronezh, including new equipment, tooling, molds, production planning and management systems. The new 44,000 square meter facility is modeled after the Company's Vredestein Banden plant in Enschede, Holland, and was designed in cooperation with the company's Dutch designers.

The company will begin production of its Amtel tyres. Once new rubber mixing equipment is installed, the Company expects to begin production of Vredestein and Maloya tyres for export to Europe, as well as for domestic distribution. Voronezh II will be among the most technologically advanced tyre factories in Europe. It will initially produce approximately 2.5 million passenger car and light truck tyres per year, bringing the total annual capacity at Amtel-Chernozemye to over 7 million tyres. The completion of the project is scheduled for late 2008 – early 2009.

**Vredestein Banden, The Netherlands**

Founded in 1946, the Vredestein Banden factory in Enschede currently manufactures a complete range of high performance and ultra high performance passenger car tyres.

As smaller size and higher volume Vredestein tyre production is shifted to Russia, the Netherlands-based factory will continue to improve its production mix by concentrating on the flexible manufacture of larger, high margin tyres in numerous specifications.

The plant received ISO 9001:2000 standard certification in 2003 and last year was awarded ISO TS status – the highest certification available. All of its control systems adhere to the highest international standards at every stage of production – from verification of supplier compliance with certification standards to final product quality tests and evaluation.

The Enschede facility produces tyres for all types of performance cars from 13" to 20" including tyres capable of supporting speeds of up to 300 kilometres per hour. Its tyres are sold and distributed throughout Europe, North America and South-East Asia.

Currently, the plant's output is approximately five million tyres and is capable of producing over one hundred specifications daily, which underlines its efficiency and flexibility. In addition, it produces hi-tech tractor and implement tyres for the most powerful tractors in the market. It also focus on low profile radial tractor tyres up to 42", and radial flotation tyres for agricultural vehicles.

The Company's commitment to the environment leads it to install dust extractors and filters as well as systems for water purification, and undertakes extensive re-cycling at the plant to reduce potentially harmful processes (such as atmospheric pollution and wastewater).

Amtel-Vredestein is very conscious of its responsibility to operate its business in a socially responsible manner. Close attention is paid to labour safety. A comprehensive assessment of working conditions is undertaken every year, and any issues arising are dealt with promptly. All equipment meets exacting labour safety standards, and each plant holds all necessary operating licences.

**Moscow Tyre Plant, Russia**

In March 2008, OJSC Amtel-Vredestein, a subsidiary of Amtel-Vredestein N.V., announced the completion of the sale of its wholly-owned subsidiary CJSC "Moscow Tyre Plant-M. The reason for disposal of MTP plant was limited demand for MTP branded tyres and high cost of production due to central Moscow location, making it not economical to continue manufacturing there.

As part of the transaction, Amtel-Vredestein N.V. is considering various options in relation to the existing equipment within MTP-M, including a possible sale of the equipment and relocating it to other Amtel-Vredestein N.V. plants for internal use.

EXECUTIVE BOARD REPORT



**Developments in 2007**

2007 has been another challenging year for Amtel-Vredestein N.V. The Company has come to a point where both accomplishments and disappointments should be analyzed in a bold and practical way to ensure a better future.
While still digesting the acquisitions of the previous years, the Company has been forced to manage a highly leveraged business, and to consider various restructuring options.

The Company started the process of disposing of the Moscow Tyre Plant, facility that proved inefficient to operate in the long run. Flexible manufacturing capacity will be especially important as the prospects of economic recovery remain uncertain.

In 2007 the performance of our PCT market hit the forecast and amounted to 14.2 Mio units. The product mix sold continued to improve thanks to the ongoing success of our top products highly appreciated by our consumers. As the demand was positive, strong gains were recorded in both B and C segments.

Our marketing activities were rejuvenated in 2007, especially in the second half or the year, after almost a standstill in 2006. In 2007 we improved our product mix and targeted our resources to better market our B segment brands. To accomplish this, we've started optimization of our AV-TO retail and wholesale division and launched an extensive advertising campaign.

One of the opportunities we've started to explore is the position of our premium Vredestein brand on the Russian market. We expect to further realize an increased awareness of the brand and, obviously, increase sales, market share and profitability. Capitalizing on the brand's European heritage as well as on the accelerating "flight to quality" trend among Russian consumers, we will reinforce Vredestein's position as a tyre offering superior performance to stylish and passionate drivers.

We have made both broad and deep changes to our leadership team and organizational structure. Our current management team has the right skills, the right experience, the right mindset and the right incentives to execute a significant turnaround of our Company.

As a result of changes in the Company's shareholding in 2007, Amtel-Vredestein no longer has a majority shareholder – the Bank of New York Mellon reports a free-float of nearly 80%.

**AV-TO to be restructured**
After a significant investment in AV-TO in 2006, Amtel-Vredestein faced serious difficulties in managing the Russian retail and wholesale network in 2007. The purchase of Pigma and Megashina made the situation even more complex. While wholesale tyre distribution business increased client penetration it also made relationships with other industry players more challenging. This, together with underperformance of the Pigma spare part distribution business, put restructuring of the AVTO division at the top of the Company's agenda. It's imperative that we optimize our infrastructure and distribution network and reconsider the Company's general acquisition strategy to optimally leverage growth opportunities while also reducing strategic risks.

**Voronezh II suspension**
Despite promises to complete Voronezh II production complex in 2007, the high level of debt made it impossible to raise financing to put the facility into operation. However, the Company continues hope for successful continuation of this project as following completion of this project, the Company will have a modern production and distribution platform from which it can ensure sustainable growth for its shareholders.

**Moscow Tyre Plant disposed**
In 2006 Amtel-Vredestein purchased the Moscow Tyre plant with purpose to meet the rising demand for tyres in Russia. Unfortunately the acquired facility showed performance materially different from planned. There was limited demand for MTP Taganka brand and high costs of production attributable to Moscow location made it not economical to produce tires of other brands at MTP. The new management decided to utilize MTP's equipment to upgrade other production units and to sell MTP for better use to a developer who can utilize central Moscow location. The transaction was completed in March 2008.

**State-of-the-Art R&D**
In recent years Amtel-Vredestein has sharpened its focus on research and development to continually introduce unique premium products. Unique in design, unique in construction is our vision for the contemporary tyre. An example of this strategy is all season tyre Quatrac3 launched in 2007 with a very specific tread pattern.
Our teams worldwide are trained in tyre technology as well as in other professional skills. They are continuously fed with tyre and market related information by our Tyre Information Centre at Enschede (NL) via electronic newsletters, Tyre Technology Seminars, factory visits and technical sessions at local meetings in the various countries.

**A strong focus on our dealer network**
We further developed our network of Preferred Dealers across Europe and Russia. Our premium products are serviced by professionals, and only by professionals. We believe that the millions of motorists should be advised in their choice for the right tyre by a tyre specialist. With a tyre being a SAFETY product, our customers-end users deserve the assistance of trustworthy professionals. That is why you will not find our premium products in department stores throughout Europe.
Presence at all relevant car and tyre shows allows the public to know, see and feel our products. Year on year, our wave of communication with the market starts at the Geneva Car Show in February. In 2007 we were happy to display the unique Giugiaro version of the Ford Mustang.

The car was displayed on our Ultrac Sessanta 20' ultra high performance tyres, for this specific occasion embellished with orange stripes on the tread. The Quatrac3 all season tyre was displayed in preview and attracted many visitors, as well as other new products such as our Runflat winter tyre.

In the beginning of March we organized an international press and dealer event at Cannes and in the wonderful Esterel surroundings of this area at the Côte d'Azur. All could try out the new Black Panther, Bull Lock and Tiger Claw mountain bike tyres, guided by the (world) champions of our Vredestein-Cannondale professional MBK Team. It was an overwhelming event with an enormous group of riders and a large coverage in the international press.

At the Rai Car Show in Amsterdam, Vredestein was simply the most remarkable exhibitor from the tyre business. Again the unique Giugiaro Mustang was displayed, together with our newest tyres. But our, sometimes special 'green' Vredestein tyres were also on display under various prototypes of 'green' car projects, from various Universities. As we are supporting several studies and projects in the Netherlands, but also in Germany and other countries leading to develop more environmental friendly vehicles.

Amtel-Vredestein participated in a variety of car and tyre shows in a long list of countries, from Bologna (Italy) via Moscow (Ru) to Las Vegas (USA).

**PASSENGER CAR TYRES**

The Company's core PCT business continued its steady growth in 2007 – sales increasing 20% to $612,2 mln. The Company sold a total of 14,2 mln. passenger car tyres, up from 13 mln. in 2006, which is a 9% increase. We achieved a fast growing turnover and margin mainly due to the improved product mix by selling more premium products in the high market segment. Amtel has become one of the leading tyre brands on the Russian market. The Amtel *Planet* line is designed for summer driving, while its *NordMaster* line is built for Russia's harsh winter conditions. Both lines are well-known for their reliability and safe handling.

The Company unveiled its new *Nord-Trac Xtreme* tyre at the Moscow International Motor Show in September 2007. This product is designed especially for Russia's extreme winter weather conditions, with a special rubber tread that guarantees perfect traction under the most difficult road conditions, and low-noise qualities to ensure a comfortable ride. It was designed in cooperation with Italy's Giugiaro Design firm, and is a major addition to Amtel-Vredestein's line of premium tyres.

Also at the Motor Show, the Company reintroduced its *Icetrac* tyres, a premium segment tyre aimed at the Russian market. This model is designed for snowy and icy roads, featuring a mathematically-optimal pattern of studs in 12 rows around the tyre to ensure excellent traction and perfect control. In addition, they feature a maximum contact area with the road for enhanced durability. Production of these tyres was launched last year at the Company's Kirov facility.

These new additions were well-received by the driving public, and demand for Amtel-Vredestein tyres continues to grow. Two new sizes were added to Amtel's *Planet DC*, which beginning in 2007 has been fitted as original equipment on all Renault Logan's manufactured in Russia. The new models added to the winter range are the *NordMaster 2* and the *NordMaster CL* (which is the Company's first unspiked winter tyre for use in southern Russia).

**AGRICULTURAL TYRES**

In 2007, sales of agricultural tyres were very successful. In the original equipment market The Company achieved growth of 22,5 % over the previous year, and enjoyed fast growing demand in the replacement market as well, especially for our unique Traxion+ radial tractor tyres and Flotation implement tyres. A tractor tyre test organised by a well-known magazine in Germany showed outstanding results for the Traxion+. And during various exhibitions in Europe, the Company introduced the new Flotation Trac, which immediately earned recognition.

The agricultural sector has changed fundamentally in recent years. Due to the the expanding world population and the ever-growing demand for food, agricultural businesses are booming. Also, the bio-energy business is growing very fast, also feeding increased demand for agricultural products. Agriculture is becoming increasingly more specialised and professional, and farms themselves have increased significantly in size. These factors will demand future innovation in machinery to cope. This is positive for the industry since it means agricultural machinery manufacturers are continually improving products in order to meet market demand.

Farmers are always looking for machinery that will improve efficiency and maximise yields by saving time, fuel and labour costs. Factors like like soil compaction, traction power, rutting, speed and comfort are what discerning customers look for. Due to our active product development, in cooperation with the agricultural machinery industry, the assortment of our tractor and implement tyres in the premium market segment, has expanded.

## INDUSTRIAL TYRES

Market targets for industrial tyres have been realised in turnover as well as in margin. In the original equipment market segment, sales were above target. Especially in the small agro/horticulture tyre segment leading manufacturers of agricultural machineries prefer to fit Vredestein for haymaking machines, pickups and tillage equipment based on Vredestein's reputation for quality. Sales in the slow traffic market segment were slightly below target while small speed tyres were level.

All industrial tyres are delivered via our central warehouse in Europe, so that we can guarantee reliable and flexible deliveries of a wide range of high quality products. Based on our good reputation as a producer and reliable supplier of high quality products, a growing number of leading manufacturers are choosing to partner with Vredestein.

## TWO-WHEEL TYRES

In 2007, Vredestein Two-Wheel Tyres continued concentrating on the sporting market segment. After extensive market analysis and expansive input from riders on the Cannondale-Vredestein Mountainbike Racing Team, three new MTB-tyres were developed: *The Tiger Claw XC-G*, *The Black Panther*, *The Bull Lock.*

Before introduction to the market, the new MTB-tyre brands were subjected to an extensive testing programme. Each line is meant for professional use, with specific qualities for different terrain conditions.

In the racing segment the carbon rim is continuing to gain in popularity. This results in a growing demand for tubes. In the past, only 21 mm wide tubes were requested. As broader tyres offer more comfort and have lower rolling resistance they are increasing in demand. With the introduction of the *Fortezza Pro TriComp* 23 mm we believe we can meet this extra demand.

In the high-end *Tour Trek City* segment we introduced the pliable *Girando 37-622* for recreational on-road use. This tyre is meant to be taken as a spare tyre on long bicycle tours.

For extension of the distribution network we found partners worldwide which fit the Vredestein philosophy. For better geographic division in the Netherlands, we teamed up with Juncker Bike Parts, a part of the Accell Group.

Our sponsorship of the Predictor-Lotto Professional Cycling Team and the Cannondale-Vredestein Mountainbike Racing Team has contributed to higher brand recognition and a large amount of free publicity for the Company in 2007.

## EARNINGS AND FINANCIAL RESULTS

Sales grew steadily across most businesses in 2007, with healthy top line and margin growth at the Company's Russian manufacturing subsidiaries and good performance of the Vredestein Banden operations.

During the period, the Company announced that it had begun equipment tests for the production of tyres at Voronezh II – an investment project expected to greatly expand the Company's tyre complex in Voronezh. Completion of this project was suspended due to the lack of financing and is expected to resume upon improvement of the Company's distressed financial position.

The Company's AV-TO retail and wholesale division ("AV-TO") delivered higher sales due to the expansion and the consolidation of the wholesale business unit which took place in 2006. However, the business performance of the unit failed to meet expectations and management's current estimate of AV-TO's economic value is significantly lower than the value attributed to the assets at the time of acquisition in 2006. This led to the Company to recognise a significant impairment of assets in this business unit. AV-TO has also contributed to a significant proportion of the Company's loss for the period and put additional pressure on the Company's results due to significant associated costs.

The Company repaid a $155 million credit linked note in June 2007 from operational cash flow and short-term borrowings. This, combined with significant deterioration of Russian and international debt markets in second half of 2007, led, among other reasons, to the Company abandoning its proposed Eurobond offering and curtailed the Company's ability to make further borrowing for working capital and investment purposes as well as plans to refinance its debt. This led to the Company starting discussion with lenders to its Russian operations in respect of debt restructuring.

**Net Sales up 29.4% (on a continuing operations basis)**

Consolidated revenues rose by 29.4% year on year to $994 million in 2007 from $768 million in 2006 on a continuing operations basis, boosted by our core PCT segment strong performance, as well as good trading in other tyre segments. This revenue increase can be primarily attributed to increased sales to the original equipment market, as well as to increased sales through the Company's AV-TO unit due to the acquisitions of auto parts and tyre wholesale businesses Pigma and Megashina, and to the increased number of retail stores in the Company. Generally, the demand for Amtel-Vredestein tyres rose steadily during the period.

Sales from the Company's Russian operations grew 30% to $439 million. Sales from European operations via the Company's Vredestein Banden subsidiary grew 18% to $402 million.

**Consolidated gross profit margin growth curtailed by AV-TO**

Gross Profit on a continuing operations basis improved to $234 million in 2007 from $187 million in 2006, an increase of 25.1%. However, the Gross Profit Margin remained broadly the same at 23.5% in 2007 versus 24.3% in 2006. Though the Company showed positive margin development in its passenger car tyre business, lower than expected margins at AV-TO were made worse by the introduction of wholesale operations unit resulting from the acquisition of Pigma and Megashina.

**AV-TO and Pigma contributed significantly to sales; also losses**
AV-TO and Pigma contributed $254 million to sales (on a stand alone basis) during 2007 – a 141.9% increase in sales from $105 million in 2006; however it also contributed a $161 million loss in 2007 versus a $9 million loss in 2006 due to poor operational results and $122 million of write-downs relating to goodwill and other intangible assets acquired during 2006. AV-TO's results in 2007 were impacted significantly by the wholesale businesses, Pigma and Megashina, acquired in late 2006.

**EBITDA was affected by the negative contribution from AV-TO***

EBITDA calculated on comparable basis decreased 25.3%: $59 million in 2007 versus $79 in 2006; primarily due to a negative contribution of $26 million from AV-TO. Additional factors impacting EBITDA were provisions created for bad debts and other balance sheet items totalling to $21 million, $14 million non-cash cost related to cancellation of stock option plan issued to the previous management team and stock option expense issued to current CEO and cancelled in 2008, *significant $9 million consulting expense related to refinancing and restructuring attempts* and $3 million in redundancy payments to outgoing management. Operational EBITDA adjusted to those extraordinary items is in line with the Company's expectations.

**Profitability was seriously affected by asset impairment and growing interest expense**
Net Loss for 2007 was $243 million, versus $5 million in 2006, principally due to significant asset impairment charges, additional non-cash tax charge related to $12 million deferred tax asset write down, increased costs, including interest expense, and other factors discussed above.

**Loans and borrowings continued to increase**
Despite the lack of new borrowings in the second half of 2007, the Company's net debt increased to $778 million as of 31 December 2007, up 14.6% from $679 million calculated as of 31 December 2006 on comparable basis. Most of the debt is attributable to the Russian operations where certain covenant breaches and payment delays have occurred during the period without triggering any repayment demands from the financing banks. Those and consequent breaches are expected to be fully waived upon completion of the contemplated debt restructuring. Vredestein Banden operations were not directly impacted by debt problems on the Russian side due to the ring fenced structure of its financing and good financial performance.

**OUTLOOK FOR 2008**

The Company hopes that its net debt will stabilize in 2008 on more stable and sustainable terms following debt restructuring exercise we intend to contemplate this year. The sought equity injection is intended to overcome overdue payments to suppliers and creditors and complete the expansion of its Voronezh tyre factory.

Sales are expected to keep around $1 billion in 2008 based on current sales trends and scheduled production output despite disposal of Moscow Tyre Plant-M. In case short-term financial issues are resolved, the management also intends to undertake steps towards improvements in gross profit and EBITDA consistent with previous years as it continues to migrate up the value chain via a product mix geared to higher quality, higher priced tyres.

The Company will consider steps to lower its overheads through consolidation and continued cost cutting. However, the profitability of the Company in 2008 will be impacted by its distressed financial position pending completion of debt restructuring and correspondent significant restructuring related costs.

In an attempt to ensure tyre manufacturing business going forward, in early 2008 the Company entered negotiations with SIBUR Russian Tyres (SRT) on possible business combination. The talks have progressed significantly within 1st half 2008 and 30 June 2008 a transaction was announced. The deal was structured as a reverse takeover, where Amtel-Vredestein N.V. acquires all issued and outstanding shares of OJSC SIBUR Russian Tyres from SIBUR Holding and issues new equity with subsequent conversion into GDRs and listing on the London Stock Exchange. However the deal lapsed on 30th September 2008 due to expiration of deadlines for certain conditions precedent which were not met due to significant deterioration of business conditions. Following discontinuation of this transaction the Company's going concern status and its continuing prospects became uncertain; restructuring discussions with the core financing banks of its Russian operations were significantly complicated by discontinuation of the merger with SRT and global financial turmoil. If the Group will be unable to find a strategic solution in short term, the continuity of the Group could become uncertain, in which case the underlying assumption of going concern may no longer be appropriate. In this event, the value of fixed assets, intangible and other assets might become impaired and additional liabilities may be incurred which may require change of accounting basis to liquidation accounts.

*The Company's new management has adopted a more conservative approach to treatment of EBITDA and therefore its calculation in regards to 2007 appears somewhat adjusted compared to previously reported figure

## RISKS AND RISK MANAGEMENT

Locally, Amtel-Vredestein N.V. faces a variety of risks that could also have an impact on business processes and thus affect employees, customers or shareholders. Though the Company has no integrated risk management system in place yet, the management track status of the risks mentioned below, and separate control procedures, which would help the Company to decrease probable impact of risks are being applied. Also, the Company is committed to develop and implement a framework for risk management based on international standards. This framework will allow us to strengthen resilience to disruptions by turning variety of current risk management activities to a systematic exercise.

### Market risk

• Foreign exchange risk: The Company operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to USD, EUR and RUR on sales, purchases and borrowings. Vredestein Banden uses forward contracts and currency options to reduce this risk. Its risk management policy requires at least 50% of sales anticipated for a period of 6-12 months in advance to be hedged.

• Fair value interest rate risk: Vredestein Banden is exposed to interest rate risk because the fair value of derivative financial instruments may fluctuate due to changes in interest rates. This will result in an unrealized profit or loss because derivative financial instruments are not held for sale. The Group holds derivative financial instruments to hedge interest rate risk exposures. Derivative financial instruments are measured at fair value. Publicly quoted market prices and rates are used to define the fair value of derivatives. Hedge accounting is not applied in cash flow hedging in connections with interest rate swaps and caps. Changes in fair values of these derivatives instruments have been recorded in profit and loss. Except for Vredestein Banden, the Group does not have any interest rate hedges.

**Credit risk**

The Company has no significant credit risks for its trade debtors., Credit risk for other debtors is addressed in a series of provisions and write offs for bad and doubtful debts, recorded in financial statements for 2007. Its current policies prevent sales to any customer with a sub-standard credit history. The Company has also installed a strong credit management team, which is responsible for overdue receivables.
Derivative counterparties and cash transactions are limited to high-credit quality financial institutions.

**Liquidity risk**
The majority of the expansion of the Group, which started back in 2002, was financed through loans and borrowing and since some of the investments did not meet the forecasted targets, the Group has continued to be cashflow negative, as at 31 December 2007.
In early 2008 the Group had completed its review of the cash raising alternatives and in June 2008 the Group had reached an agreement with OAO Sibur Holdings ("Sibur") to merge its tyre and rubber goods production and distribution business OAO Sibur Russian Tyres ("Sibur Tyres") with the Amtel Group.
On the basis of the merger agreement the Group has negotiated a deal with main lenders of its Russian operations that principal repayments due under the existing credit facilities were deferred to period till 31 December 2012 and interest up to 30 June 2009 was capitalized. The debt restructuring program and possible merger with SRT was supposed to provide the Group the necessary funds to fulfill its repayment obligations. However, discontinuation of SRT merger discussion renewed financial pressure on the Company and put its going concern status under a question mark.

**Cash flow interest rate risk**

In Russia, Amtel-Vredestein primarily uses fixed-rate debt financing. The variable rate debt is linked to MosPrime Rate, EURIBOR or LIBOR. There is no policy to define the proportion between fixed and variable rate debt. The short-term nature of most of the borrowing increases risk if interest rates are adjusted at refinancing. These fluctuations taken together with a significant portion of the debt denominated in foreign currencies, lead to certain risks and restrictions to the Company when it issues debt. Vredestein Banden B.V. uses variable rate debt to finance its operations. The Company is exposed to the variability in interest payments due to changes in interest rates. Management has established a policy for limiting its exposure to a variability in interest rates to 60% of its interest payments through the use of interest rate swaps and interest caps. The interest rate swaps somewhat insulate the Company from variable rate cash flow exposure from long-term loans by placing it in a pay-fixed, receipt-variable position. Vredestein Banden B.V. makes fixed interest payments to counterparty and receives variable interest payments in return. The interest cap limits the Company's overall exposure to increases in long-term interest rates.

**Risks from acquisitions**

As part of its strategy, Amtel-Vredestein has completed several acquisitions, including Vredestein Banden B.V., Moscow Tyre Plant and various retail and distribution assets. Some acquisitions made in the past were already liquidated or were subjected to significant impairment charges. Acquisitions may fail due to a variety of factors such as valuation mistakes or ineffective integration of operations. The Company may has been unsuccessful in addressing these and other obstacles and may repeat this mistake in future, which could have a material impact on its business, financial condition and results of operations.

**Strategic risks**

Amtel-Vredestein's strategy of prioritizing the "A» and "B" passenger car tyre segments over the C-segment may be unsuccessful. The Company has identified the "A» and "B" segments as the most profitable segments within the Russian passenger car tyre market, and it believes that Russian consumers will pay a premium for high- quality "A" and "B" segment tyres. The Company therefore plans to expand its presence in these segments. However, the Company's strategy of developing production capacity in A and B segment ahead of sales may prove risky. At the same time, the Company plans to decrease its sales of low-margin "C" segment tyres. Despite onrising consumer demand for premium and mid-segment tyres, the Company may face the risk of overcapacity due to general market congestion in the related segments. The tendency to commoditization in A and B segments is seen to grow year on year, causing prices and therefore operating margins to decline.
Any of these scenarios could undermine the Company's strategy; decrease its market share and profit margins in these segments, which could materially adversely affect Amtel-Vredestein's business, financial condition or operating results.

Amtel-Vredestein's strategy of developing and expanding its proprietary tyre retail operation could prove unsuccessful. The Company has acquired numerous retail tyre centre chains – a move that brings with it numerous inherent risks and challenges. The process of re-branding these chains and consolidating them into a cohesive has taken longer than anticipated. Sales and margins achieved at these stores have fallen short of the Company's expectations and continue produce losses. The strategy of using these centers to develop and increase sales of the Company's tyre brands could prove unsuccessful and, thus, adversely affect the Company's business and financial performance.

**Market and operational risks**

The Company relies on a relatively small number of customers in the OE market. The OE market is not the Company's largest market on a historical basis or pro forma basis. However, it believes that the OE market is important to its future success in the replacement market. The Company uses its position in the OE market to establish brand recognition and cultivate customer loyalty, both of which are crucial to generating follow-on sales in the more stable and higher-margin replacement market. Accordingly, loss of a major OEM customer could negatively impact sales, thus having a material adverse effect on the Amtel-Vredestein's business, financial condition or operating results.

Falling efficiency of purchase / sales logistics due to financial distress may constitute another material risk for Amtel-Vredestein. Deteriorating credit standing of the Company distorts normal payment terms with suppliers and customers - a situation which hinders our competitiveness and enforces unfavorable trade terms.

**Debt risks**

Amtel-Vredestein is highly leveraged and must observe certain financial and other restrictive covenants under the terms of its indebtedness. Any failure to comply with such covenants could put the Company into default.

The Company is subject to certain pledges and financial and other restrictive covenants under the terms of its various loan agreements. Vredestein is also subject to certain financial and other restrictive covenants under its syndicated loan facilities with ING Bank N.V. ("ING Bank") and ABN Amro Bank N.V. ("ABN Amro Bank") (the "Syndicated Loans"). Vredestein has pledged substantially all of its assets as collateral for these Syndicated Loans.

Under the terms of the agreements that govern the Company's loan portfolio is subject to certain restrictions limiting its ability to expand its business. Some of those covenants and limitations will be difficult to fulfill given the Company's constrained financial position. This forced the Company to start negotiations with its lenders in respect to terms of possible debt restructuring.

**Raw materials risks**

Amtel-Vredestein's supply of key raw materials is subject to price fluctuations, including highly volatile oil and natural rubber prices. Increases in the prices of synthetic rubber and natural rubber could materially affect the Company's manufacturing costs. The price of synthetic rubber as well as that of many other raw materials, including tyre cord, carbon black and certain chemicals that require derivatives of oil to produce, is sensitive to oil prices, and any increase in world oil prices could inflate the prices for such products.

Due to the nature of Amtel-Vredestein's sales contracts with its distributors and the competitive nature of its business, it may be impossible for the Company to pass these costs along to its customers. As such, increasing costs of natural rubber, synthetic rubber and other raw materials could materially adversely affect the Company's business, financial condition or operating results.

Some of the Group's suppliers are affiliated with its competitors and supply it with certain key raw materials, and they could withdraw or delay such supply to gain a commercial or other advantage over the Company. Any disruptions in deliveries from suppliers of key materials could have a material adverse effect on the Company's business, financial conditions or operating results.

**Sales and marketing risks**
The Company is putting great emphasis on building and differentiating each of its tyre brands and clearly understands the vital importance of pro-active marketing strategy as well as possible risks of financing shortfall. Underfunding of marketing activities may result in decrease of brand awareness and brand recognition of the Company's products, which inevitably leads to lower sales. Thus, insufficient funding of marketing policies may adversely affect the Company's business and financial condition.
Similarly, the Company anticipates a certain negative impact of mild winters across Europe and Russia in recent years. Such climate shift entails falling demand for winter tyres and, thus, may have adverse effect to the Company's business, financial and operating results.

**Product liability risks**

Amtel-Vredestein could be subject to product liability claims and product recalls that may adversely affect its operating results. Any material product defect in the Company's tyres that are sold to third parties could expose the Company to product liability claims or require it to undertake service actions or product recalls. Satisfying such liability claims or undertaking such service actions or recalls could require Amtel-Vredestein to expend considerable resources. Although none of the Company's products has, to date, been subject to material liability claims, service actions or recalls, any such event in the future could materially adversely affect the Company's business, financial condition or operating results.

Additionally, because product quality and the perception thereof significantly influence a customer's decision to purchase tyres, any such liability claims, service actions or recalls could, even if they successfully address the underlying defects, decrease the Company's future sales and profitability, thereby materially adversely affecting the Amtel-Vredestein's business, financial condition or operating results.

**Insufficient insurance risks**

The Company's insurance policies may be insufficient to cover losses arising from business interruption, damage to its property or third party liabilities. The Company has insurance policies covering its real estate, inventory, equipment and vehicles. However, such insurance policies might be insufficient to cover full losses arising as a result of a business interruption or damage to property as a result of fire, explosion, flood or other circumstances. In addition, the Company maintains third party liability insurance for its Russian subsidiaries only where and only to the extent that, Russian law so requires. This is because the market does not provide additional coverage on commercial terms. If the Company suffers material losses or incurs a significant liability, its insurance policies might be insufficient to cover such losses or liability, which could materially adversely affect its business, financial condition or operating results.

**Environmental and regulatory risks**

Compliance with environmental and safety laws and regulations could require Amtel-Vredestein to incur costs or restrict its operations in a manner that could materially adversely affect the Company's business, financial condition or operating results. The Company's business of manufacturing tyres may potentially be damaging to the environment. The Company is subject to a variety of environmental laws and regulations, including those regulating the use, handling, treatment, storage, discharge and disposal of substances and hazardous wastes used by or generated in its manufacturing facilities in Russia and The Netherlands. Amtel-Vredestein must invest financial and managerial resources to comply with such environmental laws and regulations.

The Company will likely be subject to increasingly stringent environmental standards in the future and may be required to make additional capital expenditures relating to environmental matters on an ongoing basis. If the Company fails to comply with current and future environmental laws and regulations, it could be subject to severe penalties, possibly including suspension of production. Environmental laws and regulations could also restrict Amtel-Vredestein's ability to expand its facilities or could require it to acquire costly equipment or incur other significant expenses in connection with its manufacturing processes.

The Company currently believes that compliance with existing laws and regulations and the cost of remediation efforts will not materially adversely affect the Group's business, financial condition or operating results.

**Global Depository Receipts and trading market risks**

The Deposit Agreement for the Global Depository Receipts (GDR) and the relevant requirements of Dutch law limit or exclude the voting rights of GDR holders with respect to Amtel-Vredestein's shares. GDR holders have no direct voting rights with respect to the shares represented by the GDRs and will be able to exercise voting rights with respect to such shares only in accordance with the deposit agreement with the Bank of New York ("Depository"), relating to the GDRs. GDR holders face practical limitations on their ability to exercise voting rights due to the additional procedural steps involved in communicating with them.

For example, both applicable Dutch law and the Company's Articles of Association require the Company to notify shareholders at least 15 days in advance of any shareholders' meeting. The

Company's shareholders will receive such notice directly from the Company and can exercise their voting rights either by attending the meeting in person or voting by proxy. By contrast, GDR holders will receive no such notice directly from the Company. Rather, in accordance with the deposit agreement, the Company will dispatch such notice to the Depository. In turn, the Depository has undertaken, if the Company so requests in writing and at the Company's expense, to mail to each GDR holder, as soon as practicable thereafter, copies of voting materials (if and as received by the Depository from the Company), as well as a statement as to the manner in which GDR holders may give voting instructions. To exercise their voting rights, GDR holders must then instruct the Depository as to how to vote the shares represented by the GDRs that they hold.

Because of this additional procedural step involving the Depository, the process for exercising voting rights may take longer for GDR holders than for holders of shares. GDR holders may not receive voting materials in time to enable them to return timely voting instructions to the Depository. GDRs for which the Depository does not receive timely voting instructions will not be voted in accordance with the instructions of the relevant GDR holder.

Additionally, GDR holders will be unable to instruct the Depository to:
• vote the shares represented by their GDRs on a cumulative basis;
• introduce resolutions on the agenda of shareholders' meetings or request the convocation of shareholders' meetings; or
• appoint members for the Company's Supervisory Board and Executive Board.

GDR holders who wish to take such actions must timely request the cancellation of their GDRs and take delivery of the underlying shares, thus becoming the owner of such shares on the Company's share register.

Future sales of shares or GDRs may affect the market price of the GDRs. Sales or the possibility of sales, of material quantities of shares or GDRs in the public markets could have an adverse effect on the trading prices of the GDRs. The Company's subsequent equity offerings may reduce the percentage ownership of its current shareholders.

**Tax risks**

The taxation system in the Russian Federation is relatively new and is characterized by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances, a tax year may remain open longer.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

Some retail chains acquired by the Group were involved in tax optimization programmes. Management of the relevant retail chains controlled the transactions. Although the Group is not responsible for potential violations of the tax legislation, this all could result in a possible tax liability that cannot be estimated at this stage. Based on the facts available, the risk of a significant economic benefit outflow as a result of potential claims is seen by management as low as and less than probable.

## MANAGEMENT'S REPORT ON INTERNAL CONTROL

The management of Amtel-Vredestein N.V. is responsible for establishing and maintaining an adequate system of internal controls over operational effectiveness, laws and regulations and financial reporting. Therefore, management has assessed the effectiveness of Amtel-Vredestein's internal controls for the full year to 31 December 2007. Management has documented its assessment as criteria set forth in the Dutch Corporate Governance Code attachment under section II.1.4.

**The Executive Board**

Peter Zolotarev (Chairman)

Vadim Pesochinskiy (Director B)

SUPERVISORY BOARD REPORT

INTRODUCTION

It was a transformative year for Amtel-Vredestein N.V. in 2007. The Company made a number of important strategy shifts as it rethought and redefined how it does business, with the goal of creating an organization primed for long-term profitability and sustained growth. This process has been guided by the extraordinary efforts of the Company's new management team.

The Supervisory Board was actively involved throughout this pivotal year in the development and oversight of the Company's evolving strategy. The Board's list of duties includes the approval of certain of the Company's activities, oversight of audit matters for interim and annual results, and preparations for the Annual General Meeting of Shareholders. Its responsibilities fall in with the Company's Articles of Association, Dutch law, and the Dutch Corporate Governance Code – also known as the *Tabaksblat Code* (or simply as "the Code").

THE SUPERVISORY BOARD'S ROLE

The primary purpose of the Supervisory Board is to oversee the business policies and decisions of the Company's Executive Board, and to offer advice that represents the best interests of the Company and its shareholders. It answers only to itself about the quality of its work.

Mr. Sudhir Gupta, founder of the Company, once largest shareholder and Chairman of Supervisory Board, left Amtel-Vredestein to pursue other challenges and ceased to exercise significant influence over the Company's business. At present, Rafael Nagapetyants serves as Chairman of the Board, and Hendrik ten Bosch serves as Vice-Chairman.

CORPORATE GOVERNANCE

Last year, the Executive Board, with the support of the Supervisory Board, continued its efforts to implement provisions from the *Tabaksblat Code* in order to provide shareholders with more reliable and transparent information concerning the Company's business and its management.

Starting from last year's Annual General Meeting, the Executive Board and the Supervisory Board will submit detailed information regarding the Company's corporate governance structure at this year's Annual General Meeting of Shareholders. In addition, all new by-laws and regulations considered by the Executive Board, the Supervisory Board, and various Board subcommittees will be posted on the Company's website, as stipulated by the Code.

COMPOSITION OF THE SUPERVISORY BOARD

The Supervisory Board of the Company may consist of up to 10 members, but never less than three members, as mandated by the Company's Articles of Association.

Members are appointed by the Annual General Meeting of Shareholders based on nominations made by the Supervisory Board. Current members of the Supervisory Board are as follows:

| | |
|---|---|
| MR. RAFAEL NAGAPETYANTS<br>Chairman<br>Age: 46<br>Nationality: Russian Federation<br>Appointed: 2007 | Managing Director, Corporate Finance Department at Alfa-Bank.<br><br>Degree in International Finance from Moscow Finance Institute; 1995 - Moscow State University PhD. in Law; 1991 - PhD. in Economics. |

| | |
|---|---|
| MR. HENDRIK TEN BOSCH<br>Vice-Chairman,<br>Member Audit Committee<br>Age: 58<br>Nationality: The Netherlands<br>Appointed: 2007 | Member of the Supervisory Board of the Russian subsidiary of Standard Bank of South Africa. Former General Director and Chairman c the Executive Board of ING Bank Eurasia (ZAO). Former General Director and Chairman of the Executive Board of ABN Amro Bank Russia. Degree in Law from Utrecht State University, the Netherlands, 1974 |
| MR. DANIEL GUPTA<br>Chairman Remuneration and Appointment Committee<br>Age: 26<br>Nationality: Russian Federation<br>Appointed: 2005 | Director of Amtel Properties and Development, and is responsible for the company's activities in Russia and CIS.<br><br>Masters Degree in Political Economy and Political Science from the Londor School of Economics. |
| MR. MAXIM IGNATIEV<br>Vice Chairman<br>Member Remuneration and Appointment Committee<br>Age: 47<br>Nationality: Russian Federation<br>Appointed: 2005 | Chairman of the Board of Sport and Fashion Retail Group; Vice-President and co-founder of Russian Fitness Group.<br><br>Degree in Mathematics and Computing from the People's Friendship University named after Patrice Lumumba. |
| MR. HUBERT PANDZA<br>Chairman Audit Committee<br>Age: 60<br>Nationality: Germany<br>Appointed: 2006 | Former Director Russia and Central Asia Business Group and the Group fo Small Business from EBRD's Headquarters in London, former CEO of Deutsche Bank, Moscow |

At the start of 2007, the Supervisory Board had six members: Messrs. Sudhir Gupta, Daniel Gupta, Paul Dominic Gualtieri, Maxim Ignatiev, Tarik Chaudri and Hubert Pandza. Over the course of the year, Messrs. Sudhir Gupta, Tarik Chaudri and Dominic Gualtieri resigned and another three members were appointed to replace them: Messrs. Rafael Nagapetyants, Hendrik ten Bosch and Hubert Hoedl (who resigned in December 2007). At the end of 2007 the Board assumed its current five-member structure, with the people listed above. Of the current members, Messrs. Pandza, Ignatiev, and ten Bosch are independent as defined by the Dutch Corporate Governance Code.

The Supervisory Board held 12 meetings in 2007. Each meeting was attended by all the members, and the minutes were properly recorded.

## COMPOSITION OF THE EXECUTIVE BOARD

As of December 2007, the Executive Board was comprised of six members:

- Petr Zolotarev, CEO of Amtel-Vredestein N.V.
- Vadim Pesochinskiy, CFO of Amtel-Vredestein N.V
- Ilya Ivanov, Deputy Director of Sales and Operations, Amtel-Vredestein N.V.
- Robert H. Oudshoorn, CEO of Vredestein Banden B.V.
- Kornelis (Kees) Hettema, Managing Director of Vredestein Consulting B.V.

- Marc Luyten, Director Corporate Marketing and Sales of Vredestein Banden B.V

Significant changes to the Executive Board took place after the 2007 Annual General Meeting, when the former management team stepped down to pursue opportunities outside of the tyre and automotive industries. A new team led by Mr. Petr Zolotarev was put in place, and the present Board was assembled in October 2007.

To comply with stipulations in the Code and the Company's Articles of Association, newly appointed Executive Board members will be limited to four-year terms.

The Chairman of the Supervisory Board and the Executive Board remain in frequent contact throughout the year, enabling the Supervisory Board to closely monitor the business' operations and financial developments.

## BUSINESS REVIEW

Several key events took place in 2007 that are pivotal to the company's efforts to succeed in the premium passenger car tyre business. The four most important events are that the Company:

- Announced its intention to dispose of the Moscow Tyre Plant (a process completed with the plant's sale in March 2008).
- Postponed the launch of its Voronezh II, with a commitment to complete the installation of new equipment and bring the facility into production operation late 2008 – early 2009.
- Suspended further expansion of its AV-TO retail unit until a careful and thorough evaluation of the division's current retail asset portfolio can be completed, and a strategy for its future can be charted.
- Launched a debt-restructuring program in order to facilitate the financial turnaround.

## COMMITTEES

The Supervisory Board is comprised of two committees – an Audit Committee and a Remuneration and Appointment Committee.

### Audit Committee

The Supervisory Board has delegated to the Audit Committee responsibility for overseeing the financial reporting and internal control of the Company and for maintaining an appropriate relationship with the Company's auditors.

*Role of the Audit Committee*

The main role of the Audit Committee is to encourage and safeguard the highest standards of integrity, financial reporting, risk management and internal control. In doing this, the principal responsibilities of the Audit Committee include:

- reviewing the Company's financial statements;
- reviewing the adequacy and effectiveness of the Company's internal control and risk management;
- recommending to the Supervisory Board the appointment, re-appointment or removal of the internal and external auditors;
- reviewing and monitoring the Company's ethical standards.

*The Composition of the Audit Committee*

| No. | Position | Name | Status | Independent |
|---|---|---|---|---|
| 1. | Chairman | Hubert Pandza | Non-Executive Director | Yes |
| 2. | Member | Rafael Nagapetyants | Non-Executive Director | No |
| 3. | Member | Hendrik ten Bosch | Non-Executive Director | Yes |

During 2007, the following changes in the composition of the Audit Committee have taken place.

1. Dominic Gualtieri has left the Supervisory Board and position of Chairman of the Audit Committee due to his permanent appointment. Hubert Pandza has been elected as new Chairman of the Audit Committee.
2. Rafael Nagapetyants has been elected as a new Audit Committee member. As a representative of a significant shareholder, Alfa Bank, Rafael in the Audit Committee member role will be able to devote sufficient time for assuring that the financial reports show real position of the Company, as well as that the Company's management implement proper corporate governance policies.
3. Tarik Chaudri has left the Supervisory Board for personal reasons. Hendrik ten Bosch has been elected as a new member of the Audit Committee.

For the purposes of the Code, Hubert Pandza is considered by the Supervisory Board to have recent and relevant financial experience. Rafael Nagapetyants joined Supervisory Board in July 2007 and Hendrik ten Bosch served on the Supervisory Board and Audit Committee since October 2007.

The Company's internal and external auditors, as well as certain members of the Executive Board attended most of the meetings during the financial year. The Audit Committee met with the internal and external auditors in separate private sessions during all the Audit Committee meetings throughout the financial year. This provided an opportunity for external and internal auditors to raise matters of concern in confidence.

*Report on the Audit Committee's activities in 2007*

Meetings and Attendance

The Audit Committee met nine times in 2007 and there was full attendance by all members. Members and the auditors participated either in person or via a conference call.

The Committee examined the Group`s track record of past acquisitions, including the performance of entities against that originally envisaged as well as their compliance with appropriate procedures, and agreed that for future acquisitions, a more robust process needs to be in place to ensure alignment with the Group`s overall strategic direction.

To assist the Audit Committee in fulfilling its role, a number of Executive Board members and other executives and advisors were invited to attend some or all of the Audit Committee meetings. These included the Company's CEO, CFO, Director of Internal Audit and the Company's legal counsel, each of whom provided reports to the relevant Audit Committee meeting on their area of responsibility. The Company's external auditors, KPMG and its successor, Deloitte, also attended a number of meetings and presented updates on their activities.

The Audit Committee followed a formal program of issues to review over the course of the year. As its principal guide in the process, the Audit Committee used publications of the Audit Committee Institute, sponsored by KPMG. This review program was designed to ensure that all matters that fall within the Audit Committee's remit are properly reviewed at the appropriate time.

The Audit Committee carried out the following activities during 2007:

*Risk and Controls*

- Reviewed the progress of implementing by the Company of risk management and control system-- including ongoing identification and monitoring of key risks, and the controls implemented by the respective departments in managing these risks;

- Evaluated the overall effectiveness of the system of internal controls through the review of work performed by internal and external auditors and discussions with the key members of the Executive Board;

*Financial Results*

- Reviewed with appropriate officers of the Company and external auditors, the half-yearly financial results and annual audited financial statements of the Company including the announcements pertaining thereto, before recommending to the Supervisory Board for their approval and release of the Company's results to the AFM and the LSE;

*External Audit*

- Reviewed with the external auditors their audit plan for the financial year ended 31 December 2007 to ensure that their scope of work adequately covered the activities of the Company;

- Reviewed the results and issues arising from the external auditor's audit of the year end financial statements and the resolution of such issues highlighted in correspondence to the Committee;

- Reviewed the external auditor's audit performance and independence before recommending to the Supervisory Board their appointment and remuneration;

*Internal Audit*

Reviewed with the internal auditor its annual audit plan for the financial year ended 31 December 2007 to ensure that principal risk areas were adequately identified and covered in the plan;

- Reviewed the recommendations by internal audit, representations made and corrective actions taken by management in addressing and resolving issues as well as ensuring that all issues are adequately addressed on a timely basis;

- Reviewed the results of ad-hoc activities performed by internal audit and the actions taken relating to those activities;

- Reviewed the adequacy of resources and the competencies of staff within the internal audit activity to execute the plan, as well as the audit working programmes used in the execution of the internal auditor's work and results of their work.

Remuneration and Appointment Committee

The Remuneration and Appointment Committee was formed in 2005 and consists of Daniel Gupta and Maxim Ignatiev. The Remuneration and Appointment Committee held two formal meetings (as required) in September and December 2007.

*Role of the Remuneration and Appointment Committee*

The Remuneration and Appointment Committee has no authority to take decisions regarding remuneration but only to make proposals and recommendations to the Supervisory Board regarding the remuneration policy and the remuneration of individual Executive Board members. The current policy was adopted at a General Shareholders' Meeting in October 2005.

*Remuneration Report of the Executive Board*

Full details of the remuneration of Executive Board members for the financial year ended 31 December 2007 are set forth in the 2007 financial statements. The members of the Supervisory Board received compensation for a full year of service in 2007.

REMUNERATION REPORT OF THE SUPERVISORY BOARD

Introduction

In accordance with the Articles of Association, the remuneration of the Executive Board members is the responsibility of the Supervisory Board as a whole. Resolutions on the remuneration proposed by the Supervisory Board should be in line with the remuneration policy for Executive Board members as adopted by the General Meeting of Shareholders.

The Supervisory Board has appointed a Remuneration and Appointments Committee from among its members to prepare proposals, advice and recommendations for the Supervisory Board on the remuneration policy and individual remuneration for the Executive Board members, and to prepare the remuneration report.

Furthermore, the Remuneration and Appointments Committee is to advise the Supervisory Board on the yearly targets for the Executive Board. The remuneration of Supervisory Board members is determined by the General Meeting of Shareholders.

The remuneration policy and any future material changes will be submitted to the General Meeting of Shareholders for adoption. The remuneration policy will be available on the Company's website.

The following is an overview of the remuneration policy for 2007 and subsequent years. It takes into account the best practice provisions of the Code.

REMUNERATION POLICY

Introduction

In accordance with the Articles of Association, the remuneration of the Executive Board members is the responsibility of the Supervisory Board as a whole. Resolutions on the remuneration proposed by the Supervisory Board should be in line with the remuneration policy for Executive Board members as adopted by the General Meeting of Shareholders.

The following is an overview of the remuneration policy for 2008 and subsequent years. Any future material changes in the remuneration policy will be submitted to the General Meeting of Shareholders for adoption.

*Remuneration Policy Statement*

It is essential that the executive remuneration programme rewards the Executive Board members for their ability to achieve operational and financial targets.

In order to achieve this, we will provide a competitive base salary and the opportunity to achieve significant rewards if the Company creates value for its shareholders.

*Employment Agreements*

Executive Board members have an employment agreement with the Company and/or with one of its subsidiaries.

If the Company initiates the termination of the employment agreement for a Dutch resident Executive Board member and if the termination is for a reason other than for urgent reasons (cf. Section 7:677 of the Dutch Civil Code (*Burgerlijk Wetboek*), the Company and the Executive Board member will observe the provisions laid down in the Code. For this reason, the neutral Sub-District Court formula will serve as a basis for the calculation of the severance payment.

If the Company initiates termination of the employment agreement for Russian resident Executive Board member and if the termination is "without cause" as defined in the employment agreements, such member is entitled to severance benefits as set forth in the employment agreement.

If the Company initiates termination of the employment agreement of the CEO (i) at the election of the Supervisory Board, without Cause, upon not less than sixty (60) days prior written notice of termination; (ii) due to a change of control of the Company; or, (iii) without cause within one year following a change of control of the Company, the CEO shall receive a lump sum payment by the Company in an amount equal to three times his annual base salary.

*Term of appointment*

Executive Board members are to be appointed for a period of 4 years. On expiry, the Executive Board member may be re-appointed for successive terms of not more than 4 years.

*Remuneration elements*

The remuneration strategy for the Executive Board shall be aligned with the Company's business strategy to seek profitable growth.

The remuneration of the Executive Board members currently comprises of the following elements: base salary and cash bonus incentives.

The components of base salary and the cash bonus incentive programmes are fixed. The Company considers the bonus incentives to be an important part of the remuneration package of Executive Board members.

*Base salary*

Our guiding principle is that compensation should be comparable to that offered by a reference group of public companies that are roughly similar to the Company in size and complexity.

*Operational Bonus*

The current bonus scheme applicable to the Executive Board members is based on individual financial targets. The quantitative criteria reflect the financial parameters that the Supervisory Board considers to be the most critical annual measures to enable the business to achieve the goals of its objectives. The qualitative targets for the Executive Board are set by the Supervisory Board based upon the approved annual budget.

In accordance with reaching the set qualitative targets, Executive Board members will receive a bonus equal to 50 percent of their respective base annual compensation.

When an employment agreement is terminated by a member of the Executive Board, this member is no longer entitled to any bonus. In case of long lasting absence of a member of the Executive Board as a result of illness or leave of absence, the Supervisory Board is entitled to decide that no cash bonus or only part thereof will be granted. Achievement against the quantitative targets will be assessed following the end of the financial year and on the basis of audited results. The Company does not disclose individual performance targets for Executive Board members.

The current CEO, Mr. Zolotarev, has the right to receive a salary and an annual cash bonus incentive in an amount equal to 100% of his annual base salary and annual bonus for 2008 subject to attaining certain performance indicators established by the Board. The CEO is to receive an annual bonus in the amount of 13,500,000 roubles for 2007. From 2008 onwards, the CEO will receive a bonus equal to 100 percent of annual compensation, subject to annual targets approved by the Supervisory Board. During the first and second quarters of the 2008 calendar year, the CEO is entitled to an advance against the 2008 annual bonus (quarterly amounts equal to 12.5% of the CEO's bonus for 2008).

*Bonus incentive programmes*

- *M& A Bonus Programme*

The M&A Bonus Programme will provide a cash bonus equal to one year's compensation (according to the relevant employment contract). The bonus will be paid either:

- Within 20 days from the date when restructuring agreements are signed with the Company's lenders who hold in total 75% of the Company's total outstanding debt.

Or

- Within 20 days from the date when new shares are issued or existing shares are sold to counterparty where the counterparty becomes controlling shareholder of the resulting entity.

- *Retention Bonus Programme*

The Retention Bonus Programme provides quarterly cash payments equal to 12.5% of the relevant employee's operation bonus for the current year (as per the bonus figures in his/her respective contract) payable at the end of the first and second quarter of the current year during the restructuring period. The retention bonus will be subtracted from the respective annual bonuses outlined above.

- *Severance payments programme*

The Severance Payments Programme provides that in the event a manager is terminated within a one year period following a merger (change of control) and/or without cause, such manager will receive a cash payment equal to one year (or in the case of the CEO, a 3 year) guaranteed portion of his/her compensation.

*Share options and share grants*

In April 2007, the Supervisory Board decided to discontinue the share option programme in its existing form.

As of March 2008, the Company decided to terminate the CEO's share option agreement.

*Allowances and benefits in kind*

Members of the Executive Board benefit from certain allowances and/or benefits in kind. The majority of these allowances and benefits comprise elements based on general local practice (such as a company car, contribution to health care costs, fixed annual cost allowances) or relate to specific international circumstances (such as relocation costs, housing). The latter are often one-off amounts or time-limited.

*Loans*

It is the current policy of the Company not to grant the Executive Board members any personal loans and guarantees.

*Supervisory Board remuneration*

The members of the Supervisory Board are compensated as follows:

(i) Members – EURO 50,000 net for full year of service;
(ii) Vice Chairman and each committee Chair – EURO 75,000 net for full year of service;
(iii) Chairman –EURO 100,000 net for full year of service.

Further, the members of the Supervisory Board will be provided the opportunity to receive an incentive bonus for their work on the Supervisory Board of the Company.

*Indemnification*

The Company has agreed to indemnify Members of the Executive and Supervisory Board with respect to their activities as members of the Executive or Supervisory Board of the Company against expenses (including, without limitation, attorneys' fees, judgments, fines, and amounts paid in settlement) actually and reasonably incurred in connection to any threatened, pending, or completed action, suit, or proceeding whether civil, criminal, administrative, investigative, or otherwise and whether formal or informal, to which the Member was, is, or is threatened to be made a party by reason of facts which include the Member being or having been such a member of the Executive or Supervisory Board of the Company. Any indemnification is subject to AGM approval.

Enschede, 31 December 2008

**The Supervisory Board**

Rafael Nagapetyants (Chairman)

Hendrik W. ten Bosch

Daniel Gupta

Hubert Pandza
Maxim Ignatiev

**AMTELVREDESTEIN**

**AGENDA OF THE EXTRAORDINARY GENERAL MEETING OF SHAREHOLDERS (THE "EGM") OF THE LIMITED LIABILITY COMPANY: AMTEL-VREDESTEIN N.V., WITH ITS STATUTORY SEAT IN ENSCHEDE (THE "COMPANY"), TO BE HELD ON THE 12th DAY OF MARCH 2009 AT 10 A.M. (AMSTERDAM TIME) AT SHERATON AMSTERDAM AIRPORT HOTEL & CONFERENCE CENTER, SCHIPHOL BOULEVARD 101, 1118 BG AMSTERDAM, THE NETHERLANDS.**

1. Opening of the EGM by the Chairman.
2. a. Discussion of the annual accounts, including the report of the Executive Board on the course of Amtel's business and conduct of its affairs during the 12 months ended 31 December 2007.

   b. Proposal to adopt the annual accounts 2007.

   c. Proposal to decide to add the losses incurred during 2007 to the reserves of Amtel.
3. Proposal to approve the management performed by the members of the Executive Board during Fiscal year 2007, including discharge of the members of the Executive Board from liability in respect of the exercise of their duties during Fiscal year 2007.
4. Proposal to approve the supervision performed by the members of the Supervisory Board during Fiscal year 2007, including discharge of the members of the Supervisory Board from liability in respect of the exercise of their duties during Fiscal year 2007.
5. Update by the Supervisory Board and the Executive Board on the course of Amtel's business and the conduct of its affairs including a discussion regarding measures to be taken in relation to Article 2:108a Dutch Civil Code.
6. Questions / any other item with permission of the Chairman.
7. Closing.

Enschede, the 25th day of February 2009
Amtel-Vredestein N.V.
The Executive Board