

JSC VENTSPILS NAFTA AND ITS SUBSIDIARIES

(UNIFIED REGISTRATION NUMBER 50003003091)

ANNUAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2010

INCLUDING THE FINANCIAL STATEMENTS PREPARED IN ACCORDANCE WITH
INTERNATIONAL FINANCIAL REPORTING STANDARDS

TOGETHER WITH
THE INDEPENDENT AUDITORS' REPORT

Riga, 2011

CONTENTS

Independent Auditors' Report	2
Supervisory Council of JSC <i>Ventspils nafta</i>	4
Management Board of JSC <i>Ventspils nafta</i>	5
Statement of Management's responsibilities	6
Management report	7
Consolidated income statement	10
Consolidated statement of financial position	12
Consolidated statement of cash flows	14
Consolidated statement of changes in equity	15

Supervisory Council of JSC *Ventspils nafta*

Supervisory Council (as at the date of signing of the financial statements):

Appointed:

Chairman of the Council:	Vladimir Egger
Deputy Chairman of the Council:	Mikhail Dvorak
Members of the Council:	Javed Ahmed Oļegs Stepanovs Rubil Yilmaz Mark Ware Christophe Theophanis Matsacos Rudolf Meroni Michael Hason David Alexander Schlaff Edgars Jansons

The changes in the Council during the period from 1 January 2010 to 27 April 2011 were as follows:

Elected	Dismissed	Name	Position held
20/01/2010	-	Vladimir Egger	Chairman of the Council
20/01/2010	-	Mikhail Dvorak	Deputy Chairman of the Council
20/01/2010	-	Oļegs Stepanovs	Member of the Council
20/01/2010	-	Javed Ahmed	Member of the Council
20/01/2010	-	Rubil Yilmaz	Member of the Council
20/01/2010	-	Mark Ware	Member of the Council
07/07/2010	-	Christophe Theophanis Matsacos	Member of the Council
07/07/2010	-	Rudolf Meroni	Member of the Council
07/07/2010	-	Michael Hason	Member of the Council
07/07/2010	-	David Alexander Schlaff	Member of the Council
07/07/2010	-	Edgars Jansons	Member of the Council
20/01/2010	07/07/2010	Paul Thomas	Member of the Council
20/01/2010	07/07/2010	Gatis Grāvītis	Member of the Council
20/01/2010	07/07/2010	Mārtiņš Kvēps	Member of the Council
20/01/2010	07/07/2010	Valērijs Godunovs	Member of the Council
20/01/2010	07/07/2010	Aleksejs Ovods	Member of the Council

According to the Council's resolution of 31 August 2010 Vladimir Egger has been re-elected as the Chairman of the Supervisory Council and Mikhail Dvorak has been elected as deputy chairman of the Supervisory Council.

Management Board of JSC *Ventspils nafta*

Management Board (as at the date of signing of the financial statements):

Appointed:

Chairman of the Board:

Simon Boddy

Members of the Board:

Boris Bednov
Aleksej Tarasov

The changes in the Board during the period from 1 January 2010 to 27 April 2011 were as follows:

Elected	Dismissed	Name	Position held
28/04/2010	-	Boris Bednov	Member of the Board
28/04/2010	30/12/2010	Alexander Jagdžijanc	Member of the Board
30/12/2010	-	Aleksej Tarasov	Member of the Board
16/06/2010	30/12/2010	Andris Vilcmeiers	Member of the Board
-	28/04/2010	Normunds Staņēvičs	Member of the Board
-	16/06/2010	Ilva Purēna	Member of the Board

According to the Council's resolution of 20 January 2010, Simon Boddy was appointed as the Chairman of the Board.

Statement of Management's responsibilities

The Management Board prepares consolidated financial statements for each financial year which give a true and fair view of the state of affairs of the *JSC Ventspils Nafta* and its subsidiaries (hereinafter also – the Group) as of 31 December 2010, changes in shareholders' equity, cash flows and the results of the Group for the year ended 31 December 2010 in accordance with International Financial Reporting Standards as adopted by the European Union. In preparing those consolidated financial statements, they:

- ◆ select suitable accounting policies and then apply them consistently;
- ◆ make judgments and estimates that are reasonable and prudent;
- ◆ prepare the consolidated financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Management Board is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position, financial performance and cash flows of the Group and facilitate the preparation of financial statements which comply with International Financial Reporting Standards as adopted by the European Union.

Riga, 27 April 2011

On behalf of the Supervisory Council:

On behalf of the Management Board:

Vladimir Egger

Chairman of the Supervisory Council

Simon Boddy

Chairman of the Management Board

Management report**Dear shareholders, clients and cooperation partners,**

In 2010 *JSC Ventspils nafta* and its subsidiaries continued work on the improving operational efficiency of group companies, optimizing expenses and improving corporate governance. In 2010 the largest shareholder of *JSC Ventspils nafta* took a significant role in bringing the international experience of seasoned professionals to the Supervisory Councils of the parent company and its holdings.

In 2010 the largest *JSC Ventspils nafta* shareholder *Euromin Holdings (Cyprus) Limited* increased its shareholding in by over 1.5%, to 49.5%.

On January 20, 2010, and July 7, 2010 the Supervisory Council of *JSC Ventspils nafta* was re-elected with Mr. Vladimir Egger becoming Chairman of both of these Councils.

On January 20, 2010 Mr. Simon Boddy was elected Chairman of the Management Board of *JSC Ventspils nafta*.

The Management Board of *JSC Ventspils nafta* has three members. During the year four members either resigned or were dismissed and four new members were elected by the Supervisory Council.

The registered and paid-up share capital of *JSC Ventspils nafta* in the financial year was LVL104,479,519, comprised of 104,479,519 shares with a nominal value of LVL 1 per share. Part of the *JSC Ventspils nafta* share capital is listed on NASDAQ OMX Riga.

During the financial year the price of *JSC Ventspils nafta* shares on the NASDAQ OMX Riga ranged from LVL 0.91 to LVL 1.89, the average price being LVL 1.34. The market capitalization of *JSC Ventspils nafta* at the end of 2010 was LVL 146.27 million compared to LVL 98.21 million at the end of 2009. It should be noted that market value may not be representative due to the low level of turnover in the company's shares – the average daily turnover in 2010 was approximately LVL 10 thousand, this is only 0.01% of the market capitalization. During 2010 1,492,345 shares with a value of LVL 2.22 million were traded on the NASDAQ OMX. This is an increase of 50% over 2009.

Share price of *JSC Ventspils nafta* – January 1 to December 31, 2010 (Currency LVL)

The unaudited consolidated turnover of the *JSC Ventspils nafta* Group in 2010 was LVL 53 million and unaudited net loss was LVL 25.27 million. Due to impairments made by *JSC Latvian Shipping Company* and impairment of *LASCO Investment Ltd* debt made by *JSC Ventspils nafta* which all are according to the International Financial Reporting Standards *JSC Ventspils nafta* Group's previously unaudited 2010 results reported to NASDAQ OMX Riga differ from the actual unaudited results by more than 10%.

The parent company *JSC Ventspils nafta*'s unaudited net profit was LVL 3.64 million, this is LVL 2.5 million more than in 2009. In 2010 *JSC Ventspils nafta* as a parent company implemented a cost cutting programme resulting in a reduction of administrative expenses from LVL 2.45 million in 2009 to LVL 1.47 million in 2010. The management of *JSC Ventspils nafta* will continue working on the reduction of administrative expenses in 2011.

Management report (cont'd)

In the fourth quarter of 2010, in order to reduce foreign currency exposure, the *JSC Ventspils nafta* management converted the long-term loan to the company *Euromin Holdings (Cyprus) Limited* from USD 90 million to the equivalent amount in Euro (EUR 67.96 million). In line with this conversion the variable element of the interest rate was changed from 3 month US dollar Libor to 3 month Euro Libor. There were no delays in interest payments during the financial year.

On 17 December 2010, *JSC Latvian Shipping Company* lost control over *LASCO Investment Ltd*. The insolvency of *LASCO Investment Ltd* was announced on January 3, 2011. *LASCO Investment Ltd* is a significant debtor of *JSC Ventspils nafta* – as at December 31, 2010 the principal amount of this debt was LVL 27.6 million and the accrued interest was in excess of LVL 1.02 million. Please, see Note 30 (b) for details. As at 31 December 2010, *JSC Latvian Shipping Company* deconsolidated *LASCO Investment Ltd*. However, *JSC Latvian Shipping Company* plans to regain a control over *LASCO Investment Ltd* in the future.

During the financial year, changes took place in the composition of shareholders of *Ventspils nafta termināls Ltd*, as restructuring took place within the *Vitol* Group. On March 23, 2010 the *Ventspils nafta termināls Ltd* shareholder *Euromin Holdings (Cyprus) Limited* transferred its 49% share in *Ventspils nafta termināls Ltd* to *Eurotank Holding Sarl*, which is also a member of the *Vitol* Group. The management of *JSC Ventspils nafta* is of the opinion that this change will have no adverse impact upon *Ventspils nafta termināls Ltd*.

The revenue mix of the Group changed in 2010, with an increase of 13% in reloading revenue, a 52% increase in pipeline revenues and a reduction of 56% in railway revenues. This favourable change in mix, combined with the continuing restructuring programme lead to a 133% increase in gross profits.

The audited turnover of *Ventspils nafta termināls Ltd* was LVL 43.4 million in 2010, which is 27% less than in 2009; the audited net profit in 2010 was LVL 9.67 million, an increase of 46% over 2009

During 2010 *Ventspils nafta termināls Ltd* continued the implementation of various modernisation programmes, optimisation of operating processes and procedures, increasing labour efficiency and the introduction of improved environmental protection standards.

In order to ensure competitiveness and long-term development *Ventspils nafta termināls Ltd* implemented an investment project worth LVL 1 million. The company is now able to produce a new and competitive product – butanized gasoline.

The audited turnover of *LatRosTrans Ltd* increased by 52% to LVL 9.9 million compared to LVL 6.5 million in 2009.

Transportation volumes increased by 49% to 5.635 million tonnes. The audited net losses of *LatRosTrans Ltd* were LVL 1.619 million, this is a 74% improvement over 2009 when losses were LVL 6.132 million.

As in prior years, the largest component of *LatRosTrans Ltd's* costs was amortization of long-term investments and depreciation, LVL 4.965 million 2010 (2009: LVL 5.103 million). Notwithstanding the financial losses the company has achieved a positive net cash flow.

In January 2010, due to dissatisfaction with the performance of the management of *JSC Latvian Shipping Company*, *JSC Ventspils nafta* requested that the Management Board and Supervisory Council of *JSC Latvian Shipping Company* convene an extraordinary shareholders' meeting in order to change the Supervisory Council. The *JSC Latvian Shipping Company* Management Board and Supervisory Council failed to convene any shareholders' meetings until December 17. At the December 17 meeting a new Supervisory Council was elected, the Council then appointed a new Management Board. Moreover, the previous management of *JSC Latvian Shipping Company* has concluded several transactions which the current management is investigating and endeavouring to mitigate and reverse. The *JSC Latvian Shipping Company* Group ended the year 2010 with unaudited losses of USD 142.5 million or LVL 78.4 million.

The audited consolidated financial statements of *JSC Latvian Shipping Company* for 2009 were approved by an extraordinary shareholders' meeting of the *JSC Latvian Shipping Company* on January 28, 2011. The audited consolidated net losses of *JSC Latvian Shipping Company* for 2009 were USD 90.3 million or LVL 45.6. Taking these losses into account the audited consolidated losses of the *JSC Ventspils nafta* Group for 2009 were LVL 17.54 million, while the audited net assets of the *JSC Ventspils nafta* Group were LVL 361 million.

Management report (cont'd)

In addition it should be noted that on January 28, 2011, an extraordinary shareholders' meeting of *JSC Latvian Shipping Company* elected a new Supervisory Council and decided to pursue a claim against the previous members of the Supervisory Council and individual Management Board members for the compensation of losses caused to *JSC Latvian Shipping Company*.

Financial Instruments and Financial risk management related to the operations of *JSC Ventspils nafta Group* are disclosed in Note 31 to the consolidated financial statement.

The Consolidated Annual Report includes (on pages 63 to 79) information on compliance with the corporate governance principles in 2009 and 2010.

The Consolidated Annual report has been submitted to the NASADQ OMX Riga together with *JSC Ventspils nafta* Annual Report for 2010, as well as published on *JSC Ventspils nafta* website www.vnafta.lv.

Riga, 27 April 2011

On behalf of the Supervisory Council:

On behalf of the Management Board:

Vladimir Egger

Chairman of the Supervisory Council

Simon Boddy

Chairman of the Management Board

Consolidated income statement

	2010	2009
	EUR thousand	EUR thousand
Continuing operations		
Revenue	75 913	94 881
Cost of sales	(57 942)	(87 084)
Gross profit	17 971	7 797
General and administrative expense	(6 441)	(7 679)
Other operating income	1 198	1 137
Other operating expense	(3 530)	(4 548)
Share of loss in associate	(53 659)	(32 658)
Impairment of other financial receivables	(4 226)	-
Financial income	8 729	5 771
Financial expense	-	(324)
Loss before tax from continuing operations	(39 958)	(30 504)
Corporate income tax	(2 093)	(600)
Net loss for the year from continuing operations	(42 051)	(31 104)
Discontinued operations		
Profit after tax for the year from discontinued operations	6 098	6 147
(Loss) for the year	(35 953)	(24 957)
Attributable to:		
Non-controlling interest	5 959	1 608
Parent company's shareholders	(41 912)	(26 565)
	(35 953)	(24 957)
Earnings/ (loss) per share (EUR per share) attributable to the Parent company's shareholders:		
Diluted and basic loss per share from continuing operations	(0,46)	(0,31)
Diluted and basic earnings per share from discontinuing operations	0,06	0,06

EUR exchange rate of the Bank of Latvia on 31.December 2010 – 0,702804 LVL.

On behalf of the Supervisory Council:

On behalf of the Management Board:

Vladimir Egger

Chairman of the Supervisory Council

Simon Boddy

Chairman of the Management Board

Consolidated statement of comprehensive income

	2010 EUR thousand	2009 EUR thousand
(Loss) for the year	(35 953)	(24 957)
Other comprehensive (loss)/ income		
- Foreign currency translation resulting from investment in associate	12 727	(589)
- Cash flow hedge reserve from investment in associate	(263)	344
Other comprehensive income/ (loss) for the year, net of tax	12 464	(245)
Total comprehensive (loss)/ income for the year, net of tax	(23 489)	(25 202)
Attributable to:		
Non-controlling interests	5 959	1 608
Parent company's shareholders	(29 448)	(26 810)
	(23 489)	(25 202)

EUR exchange rate of the Bank of Latvia on 31.December 2010 – 0,702804 LVL.

On behalf of the Supervisory Council:

On behalf of the Management Board:

Vladimir Egger

Chairman of the Supervisory Council

Simon Boddy

Chairman of the Management Board

Consolidated statement of financial position

	31.12.2010	31.12.2009
	EUR thousand	EUR thousand
Assets		
Non-current asset		
Intangible assets	37 023	38 146
Property, plant and equipment	182 502	186 570
Investments in associated entities	116 821	151 923
Loan note	67 955	62 621
Other non-current receivables	36 509	-
Other non-current financial assets	357	400
Total non-current assets	441 167	439 660
Current assets		
Inventories	2 573	2 917
Trade accounts receivable	88	40
Receivables from related companies	1 248	43 469
Other receivables	3 820	2 680
Short term deposits	29 749	11 709
Cash and cash equivalents	20 141	23 004
Total current assets	57 619	83 819
Total assets	498 786	523 479

EUR exchange rate of the Bank of Latvia on 31.December 2010 – 0,702804 LVL.

On behalf of the Supervisory Council:

On behalf of the Management Board:

Vladimir Egger

Chairman of the Supervisory Council

Simon Boddy

Chairman of the Management Board

Consolidated statement of financial position (cont'd)

	31.12.2010	31.12.2009
	EUR thousand	EUR thousand
Equity and liabilities		
Equity		
Issued capital	148 660	148 660
Share premium	60 249	60 249
Legal reserve	1 017	1 017
Reserves resulting from investment in associates	(10 242)	(22 706)
Other reserves	221 609	248 182
(Loss) for the year	(41 912)	(26 565)
Equity attributable to equity holders of the parent	379 381	408 837
Non-controlling interest	106 661	105 234
Total equity	486 042	514 071
Non-current liabilities		
Deferred tax liability	2 269	2 260
Deferred income	2 472	545
	4 741	2 805
Current liabilities		
Advances from customers	105	105
Trade accounts payable	1 985	2 655
Payables to related companies	-	38
Taxes payable	626	333
Other liabilities	3 044	2 750
Corporate income tax liabilities	908	65
Deferred income	151	61
Provisions	1 184	596
	8 003	6 603
Total liabilities	12 744	9 408
Total liabilities and equity	498 786	523 479

EUR exchange rate of the Bank of Latvia on 31.December 2010 – 0,702804 LVL.

On behalf of the Supervisory Council:

On behalf of the Management Board:

 Vladimir Egger
 Chairman of the Supervisory Council

 Simon Boddy
 Chairman of the Management Board

Consolidated statement of cash flows

	2010	2009
	EUR thousand	EUR thousand
Operating activities		
(Loss) before tax from continuing operations	(39 958)	(30 504)
Profit before tax from discontinued operations	6 098	6 147
Profit before tax	<u>(33 860)</u>	<u>(24 357)</u>
Non-cash adjustments to reconcile (loss)/ profit before tax to net cash flows		
Amortisation and depreciation	12 998	13 230
Decrease in provision for unfinished construction	461	462
Disposal of investment	(6)	7
Impairment of non-current receivables	4 226	-
Interest income	(3 108)	(5 771)
Share of net loss in associate including realised gain from discontinued operations	47 567	26 504
Foreign exchange loss/ (gain)	(5 333)	769
Loss on disposal of property, plant and equipment	504	243
	23 449	11 087
Working capital adjustments:		
Decrease in inventories	344	539
Decrease in trade accounts receivable and receivables from related parties	2 309	48
Increase/ (Decrease) in current liabilities and deferred income	731	(916)
	26 833	10 758
Corporate income tax paid	(542)	(8 596)
Net cash flows from operating activities	26 291	2 162
Investing activities		
Purchase of intangibles and property, plant and equipment	(8 660)	(5 273)
Increase in short term deposits	(18 041)	(10 560)
Proceeds from sale of property, plant and equipment and investment properties	88	12 517
Proceeds from disposal of shares	30	61
Proceeds from sale of subsidiaries	-	39 426
Purchase of shares	(24)	-
Interest received	1 985	5 279
Net cash flows from investing activities	(24 622)	41 450
Financing activities		
Dividends paid	(4 532)	(72 262)
Proceeds from borrowings	-	778
Net cash flows from financing activities	(4 532)	(71 484)
Net decrease in cash and cash equivalents	(2 863)	(27 872)
Cash and cash equivalents at 1 January	23 004	50 876
Cash and cash equivalents at 31 December	20 141	23 004

EUR exchange rate of the Bank of Latvia on 31.December 2010 – 0,702804 LVL.

Consolidated statement of changes in equity

	Attributable to the equity holders of the parent							Non-controlling interest	Total shareholders' equity
	Share capital	Share premium	Legal reserve	Reserves resulting from investment in associates	Other reserves	Total			
	EUR thousand	EUR thousand	EUR thousand	EUR thousand	EUR thousand	EUR thousand	EUR thousand		
Balance as of 31 December 2008	148 660	60 249	1 017	(22 461)	319 539	507 003	104 533	611 536	
Loss for the period	-	-	-	-	(26 565)	(26 565)	1 608	(24 957)	
Other comprehensive loss	-	-	-	(245)	-	(245)	-	(245)	
Total comprehensive (loss)/ income	-	-	-	(245)	(26 565)	(26 810)	1 608	(25 202)	
Dividends declared	-	-	-	-	(71 357)	(71 357)	(906)	(72 263)	
Balance as of 31 December 2009	148 660	60 249	1 017	(22 706)	221 617	408 837	105 234	514 071	
Adjustment of prior year other reserves	-	-	-	-	(7)	(7)	-	(7)	
Adjusted balance as of 31 December 2009	148 660	60 249	1 017	(22 706)	221 609	408 829	105 234	514 064	
Loss for the period	-	-	-	-	(41 912)	(41 912)	5 959	(35 953)	
Other comprehensive income	-	-	-	12 464	-	12 464	-	12 464	
Total comprehensive income/ (loss)	-	-	-	12 464	(41 912)	(29 448)	5 959	(23 489)	
Dividends declared	-	-	-	-	-	-	(4 532)	(4 532)	
Balance as of 31 December 2010	148 660	60 249	1 017	(10 242)	179 697	379 381	106 661	486 042	

EUR exchange rate of the Bank of Latvia on 31. December 2010 – 0,702804 LVL.