TNK-BP: TREAD WITH CAUTION

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CASE DESCRIPTION

The primary subject matter of this case concerns the management of international joint ventures. Secondary issues examined include: business in Russia; government's intervention in business and how it affects multinational companies; market entry and modes of market entry decisions;; and dimensions and elements of culture (Fang 2003). The case has a difficulty level appropriate for first or second year graduate level. The case is designed to be taught in one class hour and is expected to require one hour of outside preparation by students.

CASE SYNOPSIS

BP, one of the largest publicly listed oil companies in the world, had been operating in Russia since 1997, initially through minority stakes in Russian oil companies and, since 2003, through TNK-BP, a 50-50 joint venture with AAR, a consortium of Russian investors. This joint venture allowed BP access to extensive oil reserves in Russia and was one of BP's most valuable assets, accounting for 25% of BP's production in 2007.

In 2008, BP and its partners in TNK-BP encountered serious disagreements about how to run the company. A string of government actions including raids by the Russian tax police on both BP and TNK-BP's offices in Russia concluded with the cancelation of TNK-BP's British CEO's work visa by Russian immigration authorities. Although BP and its partners reached an agreement in principle to renew the board of TNK-BP and appoint a new CEO in December 2008, by February 2009 they had not been able to appoint a Chief Executive acceptable to both parties.

INTRODUCTION

In May 2009 TNK-BP, a 50-50 joint venture between BP, one of the major western oil companies, and Alfa Access/Renova, a Russian consortium, was operating without a CEO. Robert Dudley, its previous CEO, had been forced to resign from his post following a bitter dispute between the partners in the joint venture, including raids on the company's offices by tax authorities and the revocation of Mr. Dudley's work visa in Russia. After an agreement in principle and the election of a new board, the new CEO would have to face the challenges of the politicized business environment in Russia, a partner with a history of strained relationships, and declining oil prices. However, nine months after its previous CEO had been ousted TNK-BP was still operating under its COO, Tim Summers, as Interim CEO With his Interim CEO contract recently extended, what tools would Summers need to prevent the mistakes of the past and build a more successful business model for these very different partners?

BRITISH PETROLEUM

British Petroleum had its origin in the early 1900's as the Anglo-Persian Oil Company (APOC). On May 26, 1908 at a depth of 1,180 feet in remote Persia, "a fountain of oil spewed out into the dawn sky" from what was later named the Naphtha Field (www.bp.com). Within a year the Anglo-Persian Oil Company was in business. By 1914 APOC was almost broke but Winston Churchill, then First Lord of the Admiralty, believed Britain needed a dedicated oil supply. He urged his colleagues to "look out upon the wide expanse of the oil regions of the world. Only the British-owned Anglo-Persian Oil Company could protect British Interests," he said. The resolution passed easily and the British government became a major shareholder in the company. No one had long to think of the implications as two weeks later, an assassin killed the Archduke Franz Ferdinand in Sarajevo and six weeks later, Germany attacked France and World War I had begun. By the end of the Great War, "war without oil would be unimaginable." (www.bp.com)

The British Petroleum brand was originally created by a German company as a way to market its products in Britain. During the war, the British government expropriated the company's assets and sold them to Anglo-Persian in 1917. Over the next decade, gas and electricity replaced kerosene for home heating and gasoline-fueled trucks competed with railroads and the automobile age had begun.

In 1935, Persia changed its name to Iran and Anglo-Persian changed its name to Anglo-Iranian. Then in 1939 Britain entered World War II and gasoline was rationed. With the high risk in transporting oil from Iran to the UK, the company increased production at a field in Nottingham, England. The quantities were small but large enough to help the country get by. The field was one of the best-kept secrets of World War II.

After World War II, as Europe rebuilt, Anglo-Iranian invested in refineries all over Europe and began selling gas in New Zealand. Middle Eastern nationalism was rapidly expanding, and Britain's control over Iran was rapidly diminishing. In 1951 the Iranian Parliament nationalized oil operations within the country's borders. Governments around the world boycotted Iranian oil, and within 18 months the Iranian economy was in ruins. Eventually a new arrangement was worked out with a consortium of companies including Amoco and others running the operation with Anglo-Iranian's stake down to 49%. In 1954 the board changed the company's name to The British Petroleum Company.

In the 1960's, expeditions started finding oil in places like Abu Dhabi, Nigeria and Libya. In 1965, BP found enough natural gas in the English Channel to power a medium-sized city. In 1968, a significantly larger discovery was made on the North Slope of Alaska by Arco and Exxon. A year later, BP drilled into the field which was one of the largest reservoirs found on the North American continent. Nobody believed that oil would be found in the North Sea. But in 1970 the "40's field" was discovered, which could produce 400,000 bbls oil per day.

In the 1970's, nationalization of oil fields in the Middle East and North Africa led to a decline in Middle Eastern oil from 80% to 10% of BP's total supply. This spurred the development of the North Sea and Alaskan fields. In 1987, BP bought Sohio and, in the late 1990's, Amoco and Arco. This gave BP new momentum.

By the 21st Century, BP was looking forward and had major long term projects in Russia, the Caspian, and elsewhere. There were also new projects in Angola and the Gulf of Mexico. It was in this time period that TNK-BP was formed to capitalize on the vast Russian reserves in a period of increasing oil prices and increasing demand.

TNK-BP BACKGROUND

With oil resources were naturally and politically limited, the industry was constantly looking for new supplies that were not off limits. Since the collapse of the Soviet Union, Russia had been modernizing its oil infrastructure. Russia had proved oil reserves of 60 billion bbls, mostly in Western Siberia, and also had the world's largest natural gas reserves.

Though Russia had major issues with NATO and the American plan for a missile shield, in the 21st century the power was in pipelines, not warheads. Russia's state-controlled Gazprom provided an increasingly significant proportion of Europe's natural gas supplies and controlled the pipeline network that distributed it. This gave Russia significant leverage over Western Europe's economy. However, this may also have given the West some leverage as Russia needed the revenue, technology and investment to broaden and develop Russia's own economy.
In 2002, energy accounted for nearly 20% of Russia's GDP. For the Russian oil industry, the drivers toward globalization include: "spreading portfolio risk, access to learning and expertise, more certain economic conditions and payment, enhanced ability to raise capital, securing a downstream market for crude oil, high cashflows from domestic operations providing resources for foreign investments and ego" (Dixon, 2004).

Analysts believed Russia had great potential and could eventually produce 10 million bbls of oil per day by 2010. However, Russia had an inefficient infrastructure, widespread government corruption and a lack of pipeline capacity. Some Russian oil companies were therefore quite open to the idea of partnering with western companies. For example, for the Russian partners Alfa Access/Renova (AAR), a western partnership could have provided access to new technology, international capital, world class management skills, and new international markets. (Dudley, 2003) Several factors in Russia helped make such a partnership possible, including: an improved investment climate in Russia; Russia's increased participation in the global economy; and enhanced political cooperation with the U.S. and European Union.

Still, most western oil companies kept their distance from the Russians by getting minority stakes short of management control. BP, however, had had a longer history of working with the Russians, including a 10% investment in Siberian oil company Sidanco in 1997 (the first by a western major in Russia) increasing to 25% and management control in 2000. During that period, TNK (controlled by Alpha Access/Renova) and Sidanco sued and countersued each other over Chernogorneft, a Siberian subsidiary. As part of a 2001 settlement, Sidanco regained control over Chernogorneft while TNK acquired a majority stake in Sidanco. Both BP and the Russians saw the opportunities in a partnership.

BP's past experience also provided some insight of the potential challenges ahead. Tony Hayward, chief executive of BP, was asked what suggestions he would offer to companies planning to do business in Russia. "My advice," he replied, "would be: tread with caution."

In February 2003, BP invested $6.75 billion in a new joint venture company with Russia's fourth-largest oil company, TNK, pooling the assets of both TNK and Sidanco and giving BP access to the large Samotlor oil field with reserves of 3.7 billion bbls (Grace, 2005) Thus TNK-BP, registered in the British Virgin Islands, was at the time of its formation the largest foreign investment in a Russian company, as well as one of the largest corporate transactions in Russian history. In newly appointed CEO Robert Dudley's 2003 presentation to BP stockholders, he identified the opportunities in Russia as:

1. New reserves to ensure long-term growth;
2. New production region to ensure diversity of supply;
3. Proximity to markets; and
4. Leverage on existing relationships with Russian partners.

TNK-BP had a shareholder agreement that established joint and equal control between BP and Russian partners AAR. The Board was comprised of five representatives from BP and five from AAR. A Senior Management Team consisted of seven representatives from each company. AAR appointed the Chairman and BP appointed the CEO. An audit committee was chaired by Rodney Chase, advisor to BP's CEO.

A compensation committee determined the compensation and performance package for both the CEO and Senior Management. BP's 50% stake in TNK-BP made it the world's largest crude oil producer in 2003.

The partnership had appeared golden for several years, with BP technology and expertise increasing the productivity of existing oil fields. BP became the world's number two Russian exporter, a figure that rivals had yet to match. From fiscal years 2006 to 2007, TNK-BP saw 9% growth, to revenues of $38.7 billion in 2007. By 2008, TNK-BP accounted for 25% of BP's global production. However, during this time the partnership began to show signs of strain. Board meetings became marathon battles with lots of screaming over different visions for corporate policy and strategy. There were also strident disagreements about payment terms to stockholders. When profits decreased 20% due to investments in new developments, necessary after the low hanging fruit of increasing productivity in existing assets, Russian shareholders claimed that CEO Robert Dudley was more focused on the interests of BP than TNK-BP profits. The Board failed to agree on a five-year plan.

In addition, in 2008 BP employees were increasingly coming under attack. (See Exhibit 1 for a timeline of key events.) In March 2008, Russian security services raided the offices of TNK-BP and BP in Moscow. Russia's interior ministry launched an investigation into tax-evasion by one of TNK-BP's former units. AAR demanded the ouster of Robert Dudley and said that the election of a new board at TNK-BP's main listed subsidiary was illegal. Soon visa delays forced BP to withdraw specialists from the country. When immigration authorities refused to issue the CEO a new work visa (because his contract had not been renewed), he was forced to leave the country. However, Mr. Dudley promised to run the company from outside the country, albeit from an undisclosed location. Concern increased considerably when James Owen, an independent C.F.O., resigned on August 4, 2008, and Anthony Considine, TNK-BP Vice President for Downstream, resigned on August 25th.

Even beyond the TNK-BP situation, Russia was exerting nationalistic goals in dealing with Western oil companies, making western access to Russian exploration prospects and fields increasingly difficult. As an editorial by Alan Cowelt in the August 2-3 International Herald Tribune stated, Robert Dudley, CEO of TNK-BP left Russia because of complications with his work visa. Those problems coincided mysteriously—and for the Russian side, conveniently—with broader disputes about the company's investment policies and senior personnel appointments. Since leaving, Dudley had tried to run the company from somewhere outside Russia, even though his partners in the joint venture no longer recognized him as chief executive. BP accused them of enlisting state agencies to pursue their battle—a familiar combination of commercial and government forces in Russia's quest to restrict foreign influence in its oil industry.

TNK-BP OPERATIONS

TNK-BP Operations, led by the Chief Operating Officer, consisted of Upstream, Downstream, Technology, and Field services. Key TNK-BP upstream subsidiaries included Samotlnirneftegas, Nizhnevartovsk NP, TNK-Nyagan, Tyumenneftegas, Orenburgneft, as well as upstream subsidiaries of Sidanco. Key downstream subsidiaries included Ryazan Refinery, Nizhnevartovsk NPO and Orsk Refinery in Russia and Lisichansk Refinery in Ukraine; as well as Sidanco refining subsidiary, Saratov Refinery (Russia).

Political risks were a big part of doing business in Russia, including: governmental control; state monopolies restricting oil transportation and exports; gas transportation; complex bureaucracy, and tax regime – incremental taxes take 90% after $25/bbl. Internally, TNK-BP Operations faced challenges of production overcapacity; government's reluctant support in private investment in infrastructure; outdated infrastructure; and production substantially outpaced by domestic demand growth. The government supported plans to expand export infrastructure but was reluctant to allow private investment in the infrastructure and export systems which needed major upgrade. More specifically, new export routes were required to access higher-growth markets (North America, Asia-Pacific).

Recognizing the risks and challenges that TNK-BP had, CEO Robert Dudley laid out operations strategy priorities in February 2004. The upstream strategy priorities included:

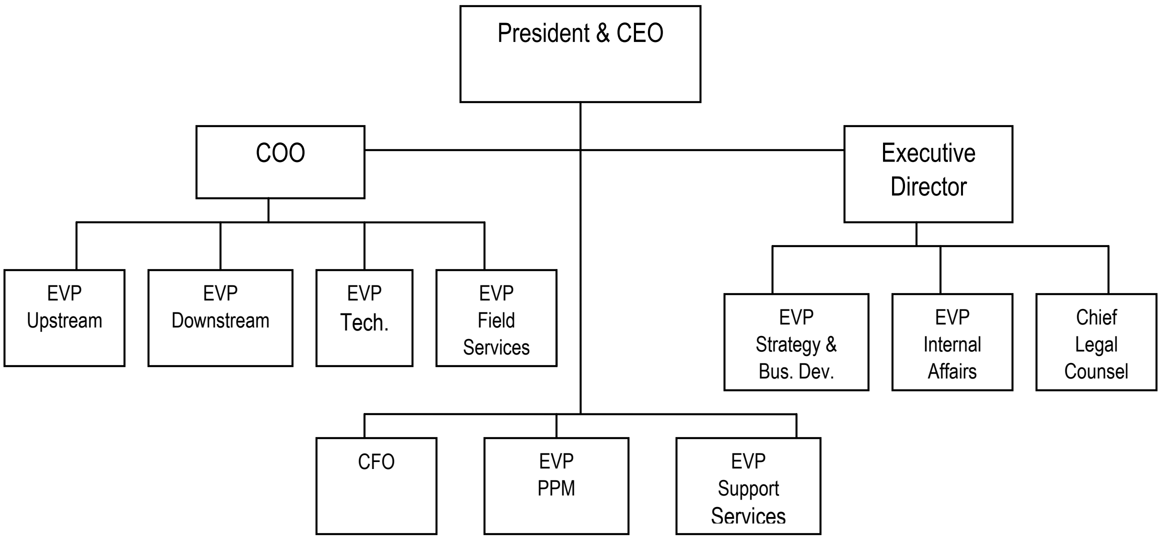
* *Targeted aggressive production growth balanced by reserve replacement of 75% or more of production*
* *Organic growth –continue "brownfield renaissance" through integration of technology*
* *Inorganic growth –acquire assets with synergies and shared infrastructure*
* *Optimized portfolio*
* *Monetized gas reserves and build successful gas business*

The downstream priorities included:

* *Enhanced downstream margins*
* *Maximized exports*

** Expanded presence in key CIS markets (e.g. Central Russia and Ukraine)*
** Explored options for gas exports to China, South Korea, Europe*

TNK- BP Management Structure (TNK-BP General Presentation 2003).



Next Level of Number of Positions

TNK	29	42%
Sidanco	11	16%
BP	24	35%
External hire	5	7%

After the first full year since the joint venture was begun in 2003, TNK-BP Management successfully executed the strategy by a number of measures. As a result, the Chief Operating Officer reported production growth of 13%--72 million tons in 2004; a decrease in unit/lifting costs; replacement of 127% of production through reserves addition; and significant improvement in downstream netbacks through the opening of new distribution channels. Riding on the success, TNK-BP management again set aggressive milestones for 2005 to accelerate the progress. Key objectives included: production growth better than industry average; replacing 100% production with new reserves; maintaining a strong cost discipline through flat lifting costs; and improving capital efficiency. With a strong focus on investment in the infrastructure, improving capital utilization, and maintaining cost discipline, TNK-BP delivered another good year in 2007 in terms of production growth, technology improvement, and downstream expansion. Downstream expanded five refineries in Russia and Ukraine, became a major retailer of fuels in Russia and Ukraine, and 1600 TNK and BP branded sites. Production and Reserve Growth included oil production 30% higher than at the start of operations, a 132% organic replacement rate, the addition of 2.5 billion barrels of new proved reserves, and the development of new major projects in West and East Siberia, increasing share of gas in the production. Technology improvements included a focus on water injection, a waterflood program to increase recovery, an exploration drilling success rate of more than 60%, and refinery modernizations to produce lighter and cleaner products.

Despite months of acrimonious conflict between BP and its Russian partner, AAR, TNK-BP once again delivered strong performance in the first half of 2008. Tim Summers, Chief Operating Officer, reported four consecutive quarters of production growth, rapid early brownfield optimization, consolidation and development of new projects, and two new greenfields coming on line in 2009 (see Exhibit 3 for upstream performance data).

INDUSTRY OVERVIEW

The roots of the modern oil industry can be traced to the United States during the late 19th century when John D. Rockefeller, after investing in a Cleveland oil refinery during the Civil War, founded Standard Oil in 1870. In 1880, Standard refined 95% of all oil in the US. In 1911, the government determined that Standard was a monopoly and broke it up into 34 companies. Some of those companies survived into the 21st century, including ExxonMobil and Chevron.

With the rapid expansion of the auto industry, oil demand increased quickly. In the 1930s, the oil giants invested substantially in Texas exploration. Shortly thereafter, the legacy companies of Chevron, Texaco, Exxon and Mobil expanded their hunt for reserves outside the US, in particular buying oil rights in Saudi Arabia.

In 1960, the Organization of Petroleum Exporting Countries (OPEC) was formed in Baghdad during a meeting of the top oil producing countries of Iraq, Iran, Saudi Arabia, Kuwait and Venezuela. In 2008; OPEC membership stood at 13 countries (Algeria, Angola, Ecuador, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, United Arab Emirates and Venezuela). OPEC nations accounted for two-thirds of the world's oil reserves, and, as of March 2008, 35.6% of the world's oil production, which gave OPEC considerable influence over the world oil market.

As of Fall 2008, the five largest major integrated oil and gas listed companies by market capitalization were ExxonMobil, Petrochina, Royal Dutch Shell, BP and Chevron. Despite several oil price shocks and maximum prices well over $140/bbl in mid-2008 that resulted in record profits, big oil faced a crisis. Production declined in mature regions such as Alaska and the North Sea where the majors were represented, and in fact fell at all seven of the major western oil companies as few new fields were being discovered. Politics played a significant role as western oil companies were squeezed out of many oil- and gas-rich areas from the Caspian region to South America. The majors were forced to renegotiate contracts on less favorable terms and often lost battles with stronger state-owned oil companies. According to the *International Herald Tribune* (August 16-17, 2008), "…the unpleasant reality is that the giants that once dominated the global oil scene have lost much of their influence – and with it, their ability to increase supplies from traditional sources." In a world that consumed 86 million bbls/day, the market was so tight that the smallest shortfalls pushed up prices.

The global oil industry had been changing dramatically in preceding decades. In the 1970s, western corporations such as ExxonMobil, BP, Royal Dutch Shell, Chevron, Total, Conoco-Philips and Eni controlled over half of the world's production. By 2008, those companies controlled only 13% of production and less than 10% of global reserves.

Henry Lee, an energy expert at Harvard's Kennedy School of Government, said that western companies had "become small players." The 10 largest holders of petroleum reserves were state-owned companies such as Saudi Arabia's Aramco, Russia's Gazprom and Iran's National Oil Company (NIOC). In fact, in 2007, every firm in the top ten reserve holders in the world in 2006 (except Lukoil) was a state-owned oil company. Exhibit #2 shows these top ten companies in terms of liquid petroleum reserves in 2006 and 2000.

ExxonMobil was ranked fourteenth, BP seventeenth, Chevron nineteenth, ConocoPhillips twenty-third and Shell twenty-fifth in 2006. These five companies controlled 3.8% of the world's liquid reserves while the top ten companies in the table above (mostly state-owned) controlled 80.6% of total world liquid reserves. Additionally, the ten companies in the chart above had an average reserve to production ratio (RPR) of 78 years, while the five large international private oil companies previously mentioned had a ratio of eleven years (RPR=(reserves economically recoverable under existing conditions)/(yearly production)). This data suggests that the ten companies would be major forces in the world oil market seven times longer than the five major private international oil companies, reflecting a troubling trend for the energy security of western and other oil importing nations.

Exhibit #3 table shows the top ten companies by petroleum liquids production. In 2006, seven of the top ten producing companies were state-owned while three were private. A company needs access to both oil accumulations and technology to produce hydrocarbons. The private international oil companies had the most access to state-of-the-art technologies, which was one of the key reasons oil producing nations entered production-sharing agreements with private international oil companies.

The technical efficiency and upstream capital expenditures was far greater for the private major international oil companies than for the state-owned oil companies. According to a study of the industry, the efficiency score for the five private major oil companies was 0.73 while for the state-owned companies efficiency was 0.27 (Eller, Hartley & Medlock. 2007). Part of this inefficiency is shown in the number of employees necessary to extract the same amount of oil (See Exhibit #4).

The western majors invested much more in upstream capital expenditures (CAPEX) and this had implications for additions to the world reserve and production base. This was not only a problem for the state-owned oil companies, but rather a problem for the world. The most inefficient firms, which were reinvesting proportionately less CAPEX in finding new oil reserves, were in control of most of the world's oil reserves. With market demand expected to increase 30% by 2030, the world would most likely face an increased future shortage of available oil to market due to the increased share of world oil reserves held by inefficient and low budget state oil companies.

According to the International Herald Tribune, "Experts say the new oil order has unsettling implications for the future of the global supply because the private Western companies are far better than most national oil companies at finding and extracting petroleum. They have developed the world's most advanced exploration technologies, and can muster huge financial resources to develop new fields. Yet instead of drawing on this expertise, many of the world's exporting states have decided to spurn it in favor of keeping full control of their oil. As the power and clout of Western companies erode, many experts predict that the role of national oil companies will keep growing, making the world increasing[ly] dependent on these government-controlled entities." (Eller, Hartley, Medlock III, 2007) As Bruce Bullock, the director of the energy institute at Southern Methodist University said, "We are going to depend on the Venezuelan, the Nigerian, or the Iranian oil companies for the future of our oil supplies. This is a troubling trend." One country where trouble became increasingly manifest was Russia.

RUSSIAN POLITICAL, SOCIAL AND CULTURAL BACKGROUND

"In the State Duma there are still people who think that Western firms are imperialists: sharks, come to plunder the Motherland." – An un-named Russian analyst (Dixon, 2004).

In the mid-1980s, Soviet Premier Mikhail Gorbachev began a series of reforms that collectively came to be known as *perestroika*. Gorbachev intended these reforms to revitalize the Soviet Union. At the same time, he embarked on the policy of *glasnost*, or "openness," with the West, a marked departure from the secretive Soviet policies of the past. Rather than revitalizing the Soviet state, however, *perestroika* and *glasnost* had the effect of destabilizing the regime. *Glasnost* revealed the Western world to the Communist bloc, and the temptations of the West proved too alluring to many millions living the dramatically different and drab existence of a centrally planned economy.

In 1989 the Berlin Wall fell, an act inconceivable to most only a few years before. Such an event would have been impossible without Gorbachev's reforms, and in the West (and many parts of the Soviet bloc as well), he was hailed as a benefactor. There were many within Russia, however, who considered these developments a betrayal and a submission to the corrupting influences of the West, which was ever vigilant to encircle and destroy the Soviet Union. Among those who generally held this view were the Soviet Union's staunchest defenders, the KGB (the Soviet state security apparatus), whose *raison d'etre* during the Soviet era was service to the State, best achieved through surveillance and suppression of dissent from all within its reach.

In August 1991, in an effort to save the Soviet Union from these corrupting influences, various members of the government and KGB attempted to overthrow Gorbachev. The coup failed, and ultimately precipitated the collapse of the Soviet Union. The day before the coup was suppressed, a relatively unknown member of the KGB, Lieutenant Colonel Vladimir Putin, resigned from the service.

In the following years, under Russian President Boris Yeltsin, Russians experienced not only the collapse of the Soviet empire, but the stripping away of satellite states and the "security belt" they afforded, the loss of perceived super-power status, and the chaotic upheaval of transition to a capitalistic society. In short, in the span of less than a decade, many of the features of daily life in the Soviet Union were swept away, replaced by the opportunities and uncertainties of dramatic change. This transition was frightening to many and challenging to most. Russia's Real GDP shrank by 40% in the decade between 1989 and 1998, culminating with a bail-out by the International Monetary Fund.

Many citizens of the former Soviet republics were ill-prepared for the challenges a capitalistic society brought, but not all. At this time a small number of opportunistic and well-connected individuals maneuvered to grab much of the country's natural resources, oftentimes convincing ordinary citizens to sell them the "worthless" privatization deeds representing ownership shares in formerly collectivized land or industry for a bottle of vodka or a few coins. These opportunistic individuals, soon known collectively as oligarchs, built up astonishing fortunes seemingly overnight.

In 1995 Russian President Yeltsin signed a decree disbanding the KGB. In its stead was created the FSB (loosely translated as the Federal Security Service). While the name had changed, much of the security apparatus remained in place, with many members of the KGB moving to the FSB. Many other members of the KGB moved into private security positions, protecting the newly rich Russian oligarchy from the rampant crime that gripped Russia during the 1990s.

In 1998, Boris Yeltsin placed Vladimir Putin in charge of the FSB, and a year later, made him Prime Minister. On New Year's Eve 1999, Yeltsin resigned the presidency of Russia, handing the reins of power to Putin. Just prior to becoming president, Putin told his former colleagues at the FSB: "A group of FSB operatives, dispatched under cover to work in the government of the Russian Federation, is successfully fulfilling its task" (*The Economist*, 25 August 2007). It was reported that Putin appeared to be only half-joking.

As President, Putin identified his key priorities as restoring effective management to the country, consolidating political power, and neutralizing any competing sources of influence within Russia, such as the media, parliament and the oligarchs. To assist with these goals, Putin surrounded himself with trusted former colleagues from the KGB. The four key lieutenants who assisted Putin in administering Russian state affairs in the early 21st century all hailed from St. Petersburg (Putin's hometown), and formerly served within the KGB intelligence or counterintelligence units. These individuals were Deputy Prime Minister Igor Sechin, who officially controlled the flow of documents but also oversaw economic issues; Viktor Ivanov, responsible for the Kremlin personnel; Nikolai Patrushkev, head of the FSB; and Sergie Ivanov, the Deputy Prime Minister. Perhaps most striking of all, these individuals not only enjoyed political clout, but controlled considerable financial resources. Consider the following:

> ** Igor Sechin was the chairman of Russia's largest state-run oil company, Rosneft;*
> ** Viktor Ivanov was the chairman of the board of both Aeroflot and Almaz-Antey, Russia's primary producer of air-defense systems;*
> ** Sergei Ivanov oversaw both the military-industrial complex and the newly established aircraft-industry monopoly.*

During Putin's tenure as Russian president, annual economic growth averaged 7%, initially driven by high oil prices and a cheap ruble and later by domestic consumption and investment. In fact, exports of natural resources, in particular oil and gas, accounted for 80% of Russia's exports and 30% of government revenues. In May 2008, Vladimir Putin transferred the presidency to Vladimir Medvedev, while assuming the position of prime minister. During 2008 and into 2009, the global economic and financial crisis and especially lower oil prices took a toll on the Russian economy that was expected to contract by 4% in 2009.

Central to the understanding of the TNK-BP dynamic was the perception of the West, as viewed by Russia. Growing European (and particularly American) influence in the former Soviet bloc, and especially within Russia itself, was viewed by many Russians as an attempt to impose Western culture, philosophy or attitudes on a mostly unwilling people. The government did not discourage this view, but in fact frequently encouraged it with its pointed dislike of NATO encroachment, missile-defense systems, and western companies acquiring or exploiting assets within Russia and its sphere of influence. Deputy Prime Minister Sechin, for example, affirmed that only Gazprom and Rosneft would be allowed to develop the oil and gas reserves beneath Russia's Arctic continental shelf. http://www.russiaprofile.org/page.php?pageid=Business+New+Europe&articleid=a1217228548 Given these sentiments, there was little sympathy within Russia itself for the challenges BP or any other western company experienced when trying to do business within Russia.

It is important, too, to understand the long tradition of collectivism within Russian society, dating back to the time of the tsars. This collective instinct, which tended to ignore the importance of individuals, was at odds with the individualistic approach associated with Western traditions. Such a seemingly innocuous difference could assume potentially dramatic effect when one or both cultures were not inclined to collaborate fully. Along similar lines, the concept of *blat*, a kind of personal networking common within Russia, must be taken into account. *Blat*, in the words of one study, is "an essential lubricant of life" (Hutchings & Michailova,2004) within Russia, and any outsider attempting to do business in Russia without *blat* would be at a distinct disadvantage compared with those who enjoy its benefits.

Financial Overview and Significance of TNK-BP to BP, PLC

"Russians are not thieves. Russians are not bureaucrats by nature. It is just that the previous Soviet period makes them traditionally do what was the norm in this country." -- An un-named Russian Analyst (Dixon, 2004).

TNK-BP was a joint venture owned 50% by BP and 50% by a group of prominent Russian investors, Alfa, Access/Renova groups (AAR). It operated primarily in Russia and the Ukraine and employed about 71,000 people.

The parent company BP PLC had a market capitalization of $161.8 billion, making it the fifth largest major integrated oil company in the world behind Exxon Mobil, Petrochina, Royal Dutch Shell and Chevron. Founded in the early 1900's and headquartered in London, BP operated in Europe, the United States, Canada, Russia, South America, Australasia, Asia and Africa. BP PLC employed 97,600 employees and operated in two segments, Exploration & Production, and Refining & Marketing. The company had net proved reserves of 17.8 billion barrels of oil and gas equivalent.

TNK-BP was a very significant asset to BP PLC. Based on financial statements, in 2007 BP had sales and other operating revenues of $284.365 billion and profit for the year of $21.169 billion. TNK-BP reported financial data under various accounting standards including Russian accounting standards as well as under US GAAP. Financial statements were also filed with the Luxemburg Stock Exchange where the company's Eurobonds were listed. In 2007 TNK-BP reported total revenues of $38.7 billion and net income of $5.3 billion (US GAAP and approved by TNK-BP Audit Committee but prior to Board of Director's approval). These numbers were audited by PricewaterhouseCoopers.

TNK-BP sales and other operating revenues attributed to BP's financial statements were $19.463 billion with profit (after taxes) of $2.271 billion. Therefore BP's share of TNK-BP's sales were 6.8% of BP's total revenues and 10.7% of BP's total profit after taxes. The relevant financial summary tables are shown in Exhibit 7.

TNK-BP was one of the largest contributors to BP PLC's bottom line and was probably the single largest contributor to BP's profits. Therefore resolving the shareholder dispute with the TNK-BP Russian partners and government was of critical importance to BP. This was not an asset that BP could afford to walk away from. Even if compromises had to be made from BP's perspective, it was paramount that BP worked to resolve the "Russian Factor" to the mutual if imperfect satisfaction of all partners and stakeholders.

TNK-BP – SEPTEMBER 2008 RESOLUTION OF ISSUES

According to various sources including the *Miami Herald*, *The International Herald Tribune*, *Business Week*, the *Wall Street Journal* and TNK-BP, a resolution of the ongoing dispute between BP and TNK-BP's billionaire shareholders had emerged based on a September 4, 2008 news release. In this release Robert Dudley, CEO of TNK-BP, stated:

> *"I am pleased that our shareholders have reached agreement in principle on resolving their differences. Implementation of the agreement will allow TNK-BP to develop greater independence and identity and help prepare it for a successful public offering in due course. Becoming a more publicly held company will drive even higher standards of corporate governance and provide a fairer market valuation.…Meanwhile in 2008, we remain on track to deliver our best year of operational and financial performance in our five year history"*
> *(http://www.tnk-bp.com/press/news/2008/9/224/).*

The statement also noted that "TNK-BP remains a strong and competitive Russian oil and gas company and has contributed more than $80 billion in taxes, duties and excise to the Russian government in the five years since its inception. Its five year performance is second to none in the Russian oil and gas industry in terms of organic production growth, replacement of reserves and total shareholder returns."

BP CEO Tony Hayward commented that the agreement was "a sensible means of resolving a situation that could not continue without causing serious damage to what had been an immensely successful joint venture for all concerned. I now look forward to a fruitful conclusion of negotiations so that we can rebuild trust with AAR and resume our record of success for the benefit of all parties. A transparent, responsible approach to governance will be a critical factor in the appeal of TNK-BP to potential future investors."

Viktor Vekselberg of Renova of the AAR Russian shareholder consortium, which owns 50% of TNK-BP, stated that the agreement came after "very difficult negotiations. The main thing is that neither party allowed their emotions to overrule common sense during the conflict." Deputy Prime Minister Igor Sechin, who was involved in the negotiations, said " this will send the right signal to the market" (Stewart, 2008). Perhaps the performance results shown in

Exhibit 8 helped to encourage the TNK-BP shareholders to reach an agreement and end disruption to the highly profitable business. In addition, growing international concern about doing business in Russia, coupled with the major decline in both the Russian stock market and in the ruble's value against the dollar, may have helped spur the Russian side to reach an acceptable agreement and one not too onerous to BP and western perception about investing in Russia. According to the Wall Street Journal (Sept. 4, 2008) and other sources, BP agreed to:

> ** Remove TNK-BP CEO Robert Dudley, a former BP executive and a US citizen, by the end of 2008.*
> ** Ensure that Dudley's replacement spoke Russian, addressing the Russian Shareholders' complaint that top management at the company was too heavily foreign. The new CEO was to be approved by the TNK-BP board.*
> ** Reduce the 14-member Management Board to 4 executives to make decision-making more efficient.*
> ** Restructure and expand the TNK-BP Board of Directors from 10 to 11 directors to break the deadlock between BP and the Russian partners that had paralyzed the board for nearly a year. BP and AAR would each appoint 4 members of the board and there would be 3 independent directors.*
> ** Consider an international IPO of up to 20% of the shares of a TNK-BP subsidiary, addressing another demand of the Russian shareholders.*
> ** BP and TNK would each retain a 50% stake in the parent company, TNK-BP.*

The agreement involved substantial concessions from BP but did result in the company maintaining its 50% stake in TNK-BP, which was a very profitable business and accounted for about one quarter of BP's production and one fifth of its reserves. Extreme pressure from Russian regulators resulted in a court decision that disqualified Mr. Dudley as CEO based on minor paperwork violations related to employee contracts. BP believed this pressure was instigated by the Russian shareholders. AAR's main criticisms were that TNK-BP used too many expensive expatriates, ran the venture to best serve the interests of BP and that BP prevented TNK-BP from expanding abroad. The placement of more Russians in top management positions was expected to strengthen the positions of the two Russian shareholders who also held management posts. BP had in turn accused the Russian partners of wanting high dividend payments at the expense of capital expenditures needed for the future growth of the company.

BP's stock price rose 3% following the announcement of the agreement because it appeared to remove uncertainty over the ultimate outcome. Previously BP's share price had fallen by more than 20% since the dispute intensified in the public eye in May 2008. Prior to the announcement, Standard & Poor's Corporation had cut the long-term credit rating on BP PLC to AA from AA-plus on September 1st, at least in part as the result of the TNK-BP dispute. One school of thought previously believed that BP would be required to give up some of its 50% stake in TNK-BP or perhaps even lose it completely. However, there still remained the possibility that a Russian company like Gazprom could ultimately gain an interest in the company. The 20% IPO agreement was a concession to the Russian shareholders who wanted the IPO as a way to help determine a valuation of the company in case the Kremlin forced the Russian shareholders to sell part of their interest in TNK-BP.

OPPORTUNITIES AND RISKS

BP was again talking positively about the attractiveness of Russia. According to BP spokesman Toby Odone, "We don't have any regrets whatsoever about our Russian investment." Indeed, he noted that BP invested $8.5 billion into TNK-BP five years ago and had already received $10 billion in dividends (*Business Week*, September 4, 2008).

Some believed that though the immediate administrative pressure had eased, it had become apparent that the disagreements were linked to commercial disputes with AAR. Therefore the message could have been that foreign investors in Russia who had a falling out with their local partners could have similar problems in the future. *Business Week* (September 4, 2008) noted that:

> *"[I]indeed, the peace agreement at TNK-BP is in many ways reminiscent of the agreement that paved the way for TNK-BP's creation in the first place. Back in 1999, BP was involved in a public and damaging dispute with the same Russian tycoons over the fate of BP's investment in Siberian oil company Sidanco. After months of threats and name-calling, the two parties not only settled the dispute but also agreed to form a wider partnership that culminated in the creation of TNK-BP. Such flexibility shows that hardened investors in Russia know how to roll with the punches. But after two highly public bust-ups, cynics will inevitably wonder if the latest agreement may one day prove to be as brittle as the previous one."*

Indeed, according the *Wall Street Journal*, "suddenly we're supposed to believe that it's safe to do business in Russia… because BP managed to keep its 50% stake in TNK-BP. Investing in Russia remains a dangerous game and the fact that BP stood to lose a multibillion-dollar investment over a disagreement with Russian shareholders is a signal that markets will have received loud and clear" (September 8, 2008). Russian Deputy Prime Minister Igor Sechin made the comment that the deal was reached "without the involvement of third parties, such as the government," but such comments belied the facts. Moscow's refusal to renew the visas of TNK-BP CEO Robert Dudley and 148 other expatriates certainly did qualify as government involvement, despite assertions to the contrary. Absent the visa issue, it is unlikely that AAR would have had the leverage to get rid of Dudley and, as BP's CEO Tony Hayward noted, renegotiated about 10% of the joint venture terms. It had taken a long time for western investors to understand the risks of investing in Russia and it would probably take a lot longer for Russia to demonstrate that those dangers have passed.

According to a *Wall Street Journal* article dated September 11, 2008, after the previous week's decline Russian stock prices had plummeted by more than 40% from their May highs. While initially Russian officials explained these drops as transitory and driven by weak global markets, the ruble's exchange rate continued to slide against the dollar and started to cause official concern. The increasing weakness in both areas were increasingly attributed to fears about Kremlin pressure on companies such as TNK-BP as well as increased tensions between Moscow and the West after the war in Georgia. Even before the BP issue, Prime Minister Vladimir Putin made a public attack on a major steelmaker, spooking investors. Russia's market collapse had occurred in part because of the global credit crunch and weak foreign markets but it was also believed that Moscow's behavior has been a significant contributor.

CHALLENGES

BP chairman Peter Sutherland, commenting on a memorandum of understanding (MoU) issued by BP and AAR, said that the agreement created “a stable base from which to grow the joint venture to the benefit of everyone involved, including the Russian state for which strong capital investment and continued technical innovation to boost declining oil output are so important". (*The Guardian*, September 8, 2008.) It was hoped that the new CEO would ease the tension between BP and Russian shareholders in the cultural front. BP had agreed to appoint a replacement CEO who speaks Russian. However, he or she still faced political and legal challenges. Besides those, TNK-BP production output had peaked. The world-wide credit crunch didn’t help investment in modernization of the TNK-BP infrastructure. Russia’s tax regime - incremental taxes took 90% after $25/bbl – did little to incentivize oil producers. The new CEO had to understand the company operated in a country playing an increasingly important role in the global economy, where revenue from energy made a large portion of Russia’s GDP, and the Russian government could nationalize, and control a majority interest in TNK-BP - they had the power to set the price and through its legal and political arsenal, de-value the company to a point that met their bid and forced shareholders to sell. Specifically, the new CEO:

** Had to recognize that there was a growing nationalization trend in Russia.*
** Should expect that BP would have to have periodic difficult negotiations with AAR as Russia exerted more control over TNK-BP and changed the rules/contract.*
** Should expect that the Russian government would try to “change the rules” periodically and be prepared for elements of TNK-BP to become less and less favorable to BP.*
** Should anticipate BP could lose part or all of its 50% interest at some point as Gazprom or some other Russian entity was assigned an equity interest in TNK-BP at BP’s expense.*

THE WAY FORWARD

Despite the dispute, TNK-BP had even better results in the first half of 2008. On November 6, TNK-BP said the current global financial downturn would have little impact on plans to develop its resources. To remain financially healthy, TNK-BP had to stay the course to execute its current strategy - aggressive production growth, while making adjustments in how it operated in Russia. On December 22, 2008, TNK-BP elected a completely new board, but as of May 6, 2009, TNK had not appointed a new CEO, with Tim Summers, the Chief Operating Officer, acting as Chairman of the Management Board and eventually Interim CEO. Summers was British and a chemical engineer by training. Trained in England, Summers had began at TNK-BP as a chemical engineer in 1989. He had spent twenty years at BP, both in operational, commercial units and headquarters, including work in the Caspian region and Colombia. During the time that TNK-BP was being formed, Summers had led BP’s 24 international E&P business units in Scotland and was the Executive Assistant to BP Group Chief Executive Lord Browne, until he was hired as COO of TNK-BP in April 2006. Since his appointment as Interim, Summers focused on a prudent approach to TNK-BP’s investments, including reduced capital expenditure, and a flat output. In response to concern about the price of oil and access to global credit, the Board had also decided not to declare dividends for the second half of 2008. When asked how he viewed his own chances of becoming the CEO, Summers said, "(I'm) Fully focused on the job I have at the moment."

What are the main challenges TNK-BP's new Interim CEO faced? What should have been his or her priorities on taking this position? Would fluency in Russian be enough to guarantee the necessary cultural competency in the new Russian environment? How would the drop in world oil prices to around $40-60/bbl affect TNK-BP and especially what impact would it have on AAR's attitude towards TNK-BP? How would it affect the Russian government's attitude? Would BP's attitude towards its Russian venture change?

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APPENDIX

Exhibit 1 Drawn from Wall Street Journal, International Herald Tribune	
Feb 2003	BP announces new Russian oil joint venture called TNK-BP with partner AAR
March 19, 2008	Russian security services raid offices of TNK-BP and BP in Moscow
March 25, 2008	Interior Ministry says it's investigating a tax-evasion case against one of TNK-BP's former units
May 13, 2008	TNK-BP says a Siberian court, acting on a Moscow brokerage's request, has issued an injunction preventing BP specialists from working in Russia
May 30, 2008	AAR demands ouster of TNK-BP CEO Robert Dudley
May 31, 2008	Russian Prime Minister Vladimir Putin says he warned BP of the risks of a 50-50 joint venture in Russia
June 6, 2008	BP CEO Tony Hayward meets Russian Deputy Prime Minister Igor Sechin and some of the venture's Russian shareholders to resolve the dispute
June 8, 2008	Russian official says BP's conflict with AAR likely to worsen
June 9, 2008	Prosecutors in Moscow probe alleged labor violations by TNK-BP
June 10, 2008	CEO Dudley is questioned as a witness by the Russian Interior Ministry in the tax investigation
June 23, 2008	Russia's labor inspectorate fines TNK-BP for employment violations
June 26, 2008	AAR says election of new board at TNK-BP's main listed subsidiary was illegal
June 27, 2008	At EU-Russia summit, EU officials express concern to President Medvedev over the fate of BP's investment in TNK-BP
July 1, 2008	Mr. Dudley warns that visa delays could force all foreign staff to leave Russia by end of July
July 2, 2008	Russia authorities promise to issue 49 work permits promptly. AAR renews push to remove Mr. Dudley
July 11, 2008	BP, AAR fail to resolve differences at TNK-BP Board meeting; BP blocks dividend payout on the joint venture
July 17, 2008	Sixteen TNK-BP employees sue to oust Mr. Dudley; he blames shareholder conflict
July 18, 2008	Immigration authorities say they won't issue Mr. Dudley new work visa without work contract
July 22, 2008	BP pulls last specialists out of Russia
July 24, 2008	CEO Robert Dudley leaves Russia to manage TNK-BP from undisclosed location
Aug. 4, 2008	TNK-BP CFO resigns, citing challenges to working independently while share issues remain unresolved
Sept. 4, 2008	News Release states, TNK-BP shareholders have reached an "agreement in principle"
Dec. 22, 2008	TNK-BP elects new board according to the existing agreement

Exhibit 2 World Liquid Petroleum Reserves (millions of barrels) (Excerpted from *Energy Intelligence Research*, "The Energy Intelligence Top 100: Ranking the World's Oil Companies," 2007 and 2001 Editions)					
Rank 2006	Company	Reserves	Rank 2000	Company	Reserves
1	Saudi Aramco	264,200	1	Saudi Aramco	259,200
2	NIOC	137,500	2	INOC	112.500
3	INOC	115,000	3	KPC	96,500
4	KPC	101,500	4	NIOC	87,993
5	PDV	79,700	5	PDV	76,852
6	Adnoc	56,920	6	Adnoc	50,710
7	Libya NOC	33,235	7	Pemex	28,400
8	NNPC	21,540	8	Libya NOC	23,600
9	Lukoil	16,114	9	NNPC	13,500
10	QP	15,200	10	Lukoil	11,432

Exhibit 3 World Liquids Production ((Excerpted from *Energy Intelligence Research*, "The Energy Intelligence Top 100: Ranking the World's Oil Companies," 2007 and 2001 Editions)					
Rank 2006	Company	Reserves	Rank 2000	Company	Reserves
1	Saudi Aramco	11,035	1	Saudi Aramco	8,044
2	NIOC	4,049	2	INOC	3,620
3	Pemex	3,710	3	Pemex	3,343
4	PDV	2,650	4	PDV	2,950
5	KPC	2,643	5	INOC	2,528
6	BP	2,562	6	ExxonMobil	2,444
7	ExxonMobil	2,523	7	Shell	2,268
8	PetroChina	2,270	8	PetroChina	2,124
9	Shell	2,093	9	BP	2,061
10	Sonotrach	1,934	10	KPC	2,025

Exhibit 4 Total Employees per Million Barrels Equivalent Produced, 2004 (Jaffe & Baker, 2007)			
National Oil Companies	Employees	Private Oil Companies	Employees
Saudi Aramco	11	ExxonMobil	19
PDVSA	16	ConocoPhillips	20
CNOOC	18	Chevron	24
NNPC	20	Shell	27
Petromas	38	BP	27
Statoil	39		
NIOC	43		
ONGC	94		
Rosneft	172		
PetroChina	267		

Exhibit 5
Top Companies Upstream Capital Expenditures, 2006 (billions of dollars)
(Excerpted from *Energy Intelligence Research*, "The Energy Intelligence Top 100: Ranking the World's Oil Companies," 2007 Edition)

Rank	Company	Capex
1	ExxonMobil	14,470
2	Shell	12,046
3	BP	10, 237
4	PetroChina	10,160
5	Total SA	10,040
6	ConocoPhillips	8,844
7	Chevron	8,389
8	Petrobras	7,194
9	EnCana	6,650
10	Statoil	6,423

Exhibit 6: Group income statement (BP Annual Report and Accounts 2007)
Exerpted From Page 96 For the year ended 31 December $ million

	2007	2006	2005
Sales and other operating revenues	284,365	265,906	239,792
Earnings from jointly controlled entities – after interest and tax	3,135	3,553	3,083
Earnings from associates – after interest and tax	697	442	460
Interest and other revenues	754	701	613

5 Segmental analysis (Page 113)

	$ million				
By business	Exploration and Production	Refining and Marketing	Gas, Power and Renewables	Other businesses and corporate	Consolidation adjustment and eliminations
Sales and other operating revenues					
Segment sales and other operating revenues	54,550	250,866	21,369	843	(43,263)
Less: sales between businesses	(38,803)	(2,024)	(2,436)	–	43,263
Third party sales	15,747	248,842	18,933	843	–
Equity-accounted earnings (JV's like TNK-BP)	3,061	538	233	–	–
Interest and other revenues	330	134	123	167	–
Total revenues	19,138	249,514	19,289	1,010	–
Segment results					
Profit (loss) before interest and tax	26,938	6,072	674	(1,128)	(204)
Finance costs and other finance income/expense	–	–	–	–	(741)
Profit (loss) before taxation	26,938	6,072	674	(1,128)	(945)
Taxation	–	–	–	–	(10,442)
Profit (loss) for the year	26,938	6,072	674	(1,128)	(11,387)

Exhibit 7: (BP Annual Report and Accounts 2007 - P.134 Note 26) Excerpted From Page 7
$ million except per share amounts

	2007	2006	2005	2004	2003
Income Statement Data					
Sales and other operating revenues from continuing operations	284,365	265,906	239,792	192,024	164,653
Profit before interest and taxation from continuing operations	32,352	35,158	32,682	25,746	18,776
Profit from continuing operations	21,169	22,311	22,448	17,884	12,681
Profit for the year	21,169	22,286	22,632	17,262	12,618
Profit for the year attributable to BP shareholders	20,845	22,000	22,341	17,075	12,448
Capital expenditure and acquisitions	20,641	17,231	14,149	16,651	19,623
Per ordinary share - cents Capital expenditure and acquisitions Profit for the year attributable to BP shareholders					
Basic	108.76	109.84	105.74	78.24	56.14
Diluted	107.84	109	104.52	76.87	5.61
Profit from continuing operations attributable to BP Shareholders					
Basic	108.76	109.97	104.87	81.09	56.42
Diluted	107.84	109.12	103.66	79.66	5.89
Dividends paid per share-cents	42.3	38.4	34.85	27.7	25.5
Dividends paid per share-pence	20.995	21.104	19.152	15.251	15.658
Ordinary share data					
Average number outstanding of 25 cent ordinary shares (shares million undiluted)	19,163	20,028	21,126	21,821	22,171
Average number outstanding of 25 cent ordinary shares (shares million diluted)	19,327	20,195	21,411	22,293	22,424
Balance sheet data					
Total assets	236,076	217,601	206,914	194,630	172,491
Net assets	94,652	85,465	80,765	78,235	70,264
Share capital	5,237	5,385	5,185	5,403	5,552
BP shareholders' equity	93,690	84,624	79,976	76,892	69,139
Finance debt due after more than one year	15,651	11,086	10,230	12,907	12,869
Net debt to net debt plus equity	23%	20%	17%	22%	22%

Investments in jointly controlled entities((BP Annual Report and Accounts 2007 - P.134 Note 26)

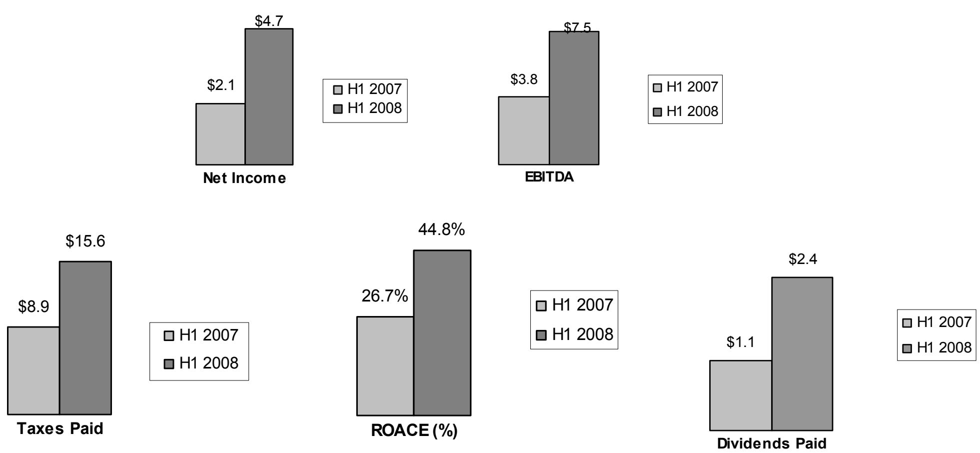
			2007			2006	
	TNK-BP	Other	Total	TNK-BP	Other	Total	TNK-BP
Sales and other operating revenues	19,463	7,245	26,708	17,863	6,119	23,982	15,122
Profit before interest and taxation	3,743	1,299	5,042	4,616	1,218	5,834	3,817
Finance costs and other finance expense	264	176	440	192	169	361	128
Profit before taxation	3,479	1,123	4,602	4,424	1,049	5,473	3,689
Taxation	993	259	1,252	1,467	260	1,727	976
Minority interest	215	–	215	193	–	193	104
Profit for the year[a]	2,271	864	3,135	2,764	789	3,553	2,609
Innovene operations	–	–	–	–	–	–	–
Continuing operations	2,271	864	3,135	2,764	789	3,553	2,609
Non-current assets	12,433	9,841	22,274	11,243	7,612	18,855	
Current assets	6,073	2,642	8,715	5,403	2,184	7,587	
Total assets	18,506	12,483	30,989	16,646	9,796	26,442	
Current liabilities	3,547	1,552	5,099	3,594	1,272	4,866	
Non-current liabilities	5,562	3,620	9,182	4,226	3,370	7,596	
Total liabilities	9,109	5,172	14,281	7,820	4,642	12,462	
Minority interest	580	–	580	473	–	473	
	8,817	7,311	16,128	8,353	5,154	13,507	
Group investment in jointly controlled entities							
Group share of net assets (as above)	8,817	7,311	16,128	8,353	5,154	13,507	
Loans made by group companies to jointly controlled entities	–	1,985	1,985	–	1,567	1,567	
	8,817	9,296	18,113	8,353	6,721	15,074	

TNK-BP INTERNATIONAL LTD

Financial reporting
- TNK-BP International Ltd (TIL) publishes annual and half yearly financial statements on the TNK-BP corporate website and also files financial statements twice a year with the Luxemburg Stock Exchange, where the company's Eurobonds are listed.
- Financial Statements are based on consolidation accounts for the TIL group of companies and are prepared under US GAAP.
- The most significant difference between the two periods is the effect of the divestment of the TIL's interest in Udmurtneft which was sold in August 2006 as part of TNK-BP's portfolio management strategy. In 2006, these assets contributed oil production of 122 thousand barrels/day, and net income benefits of around \$0.4 billion from trading operations, and \$2.0 billion as a one-off gain on divestment.

Financial Highlights			
$ billions	2006	2007	% change
Total Revenues	35.5	38.7	9%
EBITDA	11.2	9.4	-16%
Net Income	6.6	5.3	-21%
Net Income (excluding divestment effect)	4.2	5.3	24%
CAPEX	2.3	3.5	53%
Dividends declared	5.0	2.6	-48%
ROACE (%)	48%	31%	-36%
Note: 2007 TIL accounts is approved by TNK-BP Board Audit Committee but still awaiting formal Board of Directors approval. Hence figures shown for 2007 should be treated as estimates			
Source: TNK-BP First Half 2008 Performance Results			

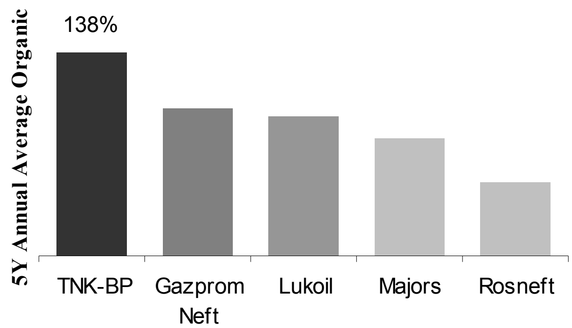
Exhibit 8
Short-term performance indicators
The numbers tell the story. In 2008 TNK-BP had a record first half in terms of income, return on capital, shareholder value and taxes.



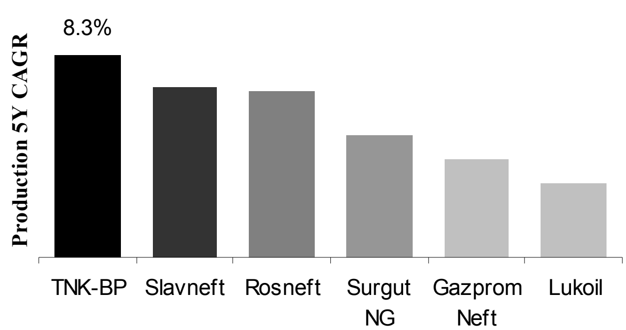
Long-term performance indicators

Since inception, TNK-BP delivered record performance in the industry in terms of production, reserves growth, shareholder return.*

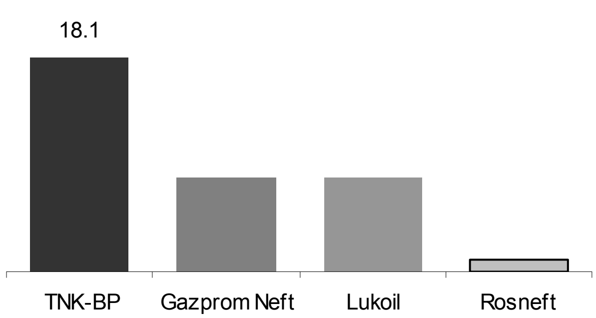
Highest reserve replacement rate



Highest production growth

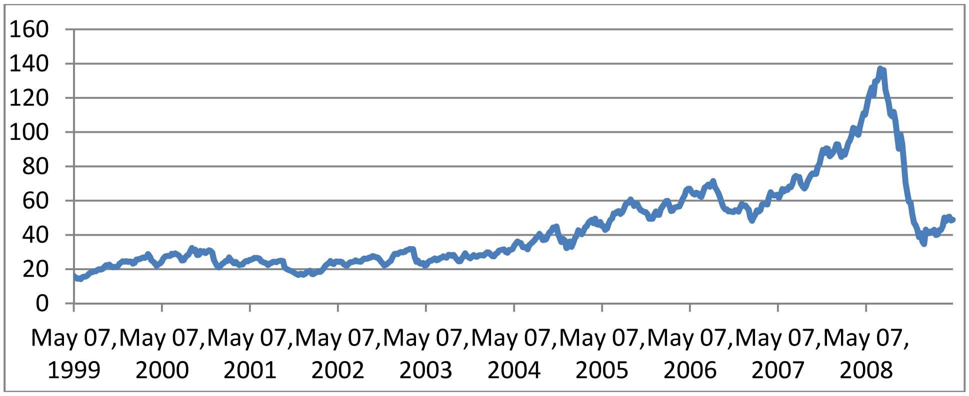


Highest total cash distribution to shareholders



*Through end 2007.
**Exxon Mobil, RD Shell, Chevron, Conoco Phillips

Exhibit 9: Weekly All Countries Spot Price FOB Weighted by Estimated Export Volume (Dollars per Barrel)



Source: U.S. Energy Information Administration