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Sustainable Development Report

Contents

INTRODUCTION FROM THE CHIEF EXECUTIVE OFFICER

Dear Colleagues and Friends,

The Sakhalin-2 Project is the world's biggest international shelf oil and gas project ever implemented in the harsh environment of Sakhalin Island in the Russian Far East. The Project is based on a Production Sharing Agreement (PSA), and is uniquely organised. In 1999, first oil was produced from the Molikpaq offshore platform installed at the Piltun–Astokhskoye field during Phase 1. In Phase 2, two more offshore platforms were constructed and started up. The Project includes some 300 km of offshore pipelines that connect all three platforms to shore, more than 1,600 km of onshore oil and gas pipelines, an onshore processing facility, an oil export terminal, and Russia's first liquefied natural gas (LNG) plant. Our Sakhalin-2 Project is probably the most innovative and technically advanced in Russia, and is contributing to a comprehensive upgrade of the country's oil and gas industry.

On 18 February 2009, Russian President Dmitry Medvedev attended the official inauguration of the first Russian LNG plant built by our Company in the southern part of Sakhalin Island. The strategic importance of the Sakhalin-2 Project for the entire Asia–Pacific was seen in the distinguished guests at the ceremony, including Taro Aso, the Prime Minister of Japan, Prince Andrew, Duke of York, Maria van der Hoeven, the Minister of Economic Affairs of the Netherlands, and other high–ranking officials and guests from Russia and countries that are co–partners in the Project from the UK, the Netherlands, and Japan.

On 29th March 2009, the first scheduled Russian LNG cargo was successfully loaded from the Sakhalin-2 LNG plant onto the LNG carrier, the Energy Frontier. The first Sakhalin LNG was delivered to two of the Company's founding customers – Tokyo Gas and Tokyo Electric.

As always, safety and reliability remain the main priorities for Sakhalin Energy during construction, start–up and operation of Sakhalin-2.

On 31st May 2009, Train 2 of the LNG plant and related facilities at the Lunskoye–A (LUN–A) platform and onshore processing facility started up.

On 22nd July 2009, Sakhalin Energy exported its 200th oil cargo. The Sakhalin Island, a PRISCO–owned tanker on long–term charter to the Company, delivered some 100,000 tonnes of oil produced at the Company's offshore facilities in the Sea of Okhotsk to a refinery in South Korea.

Since the beginning, our Company has based its activity on a strategy of sustainable development, which

allows us to achieve our business goals while taking into consideration potential environmental and social impacts on our employees and on local communities. It is fair to say that such an approach means no operational or technological decision is made without adequate environmental and social assessments of their potential impact. We rely on best international practice and standards in managing and gauging environmental, health, safety and social impact.

In 2008 and 2009, our Company won several prestigious Russian and international awards in recognition of our efforts in environmental protection, charity, engagement with Sakhalin indigenous peoples, and public relations. You will find more information about these projects in this Report.

In November 2009, Sakhalin Energy reached a new level of social responsibility and transparency by joining the UN Global Compact. The Company assumed a strict commitment to consistently advance 10 key principles of the Compact in the areas of human rights, labour, the environment, and anti–corruption. By joining the Global Compact, businesses express their support for the idea that business practice based on these universal principles promotes greater sustainability, fairness, and representation on the global market, and contributes to the creation of prosperous and successful communities. The 10 principles of the Global Compact are based on:

- The Universal Declaration of Human Rights
- The International Labour Organisation's Declaration on Fundamental Principles and Rights at Work
- The Rio Declaration on Environment and Development
- The United Nations Convention Against Corruption.

Since 2001 our Company has issued annual reports covering our social activities as well as our charitable and environmental efforts. Relying on our analysis of international and Russian best practice, in 2009 Sakhalin Energy took a major decision to follow the leading companies in Russia and abroad and publicly disclose our non–financial reports, based on best international standards. Our new report is presented in the most advanced format, in accordance with the principles and indicators of sustainable development.

We are delighted to present the first result of this work. We hope you will recognise this full disclosure as an important milestone for our Company — beneficial for our shareholders, lenders, employees, and the general public. This report reflects the critigue we got from key stakeholders during special public consultations and dialogues held by Sakhalin Energy in 2009 and 2010.

This Report is not a goal in itself; rather, it is a tool for more effective communication with our customers and partners, non–governmental organisations, local communities, authorities, and even competitors. We welcome your feedback and your comments on this Report. Your input will enable us to develop our business in a more efficient and responsible way, and consider social and environmental factors in our development. With this report, we aim to demonstrate and prove once again our social responsibility in the most advanced sense of the term.

All our efforts are targeted at harmonious and sustainable development, public benefit, and environmental protection.

Andrei GALAEV
Chief Executive Officer

ABOUT THE REPORT

General Information

After joining the United Nations Global Compact in 2009, the Company made the crucial decision to change to non–financial public reporting based on the best international standards used by the world's leading companies.

This report describes the Company's sustainable development performance in 2009 according to the principles and indicators of the Global Reporting Initiative (GRI). The target audience for this report includes the internal and external stakeholders listed in Section *Stakeholder engagement*. In preparing this report, the Company held two rounds of consultations with stakeholders, according to the AA1000SES international standard. This complements the GRI and recommends logical and systemic interaction between a modern, socially responsible company and its stakeholders. Detailed information about the consultations is presented in Section *Stakeholder engagement*.

The report is published on the Company's public website and is circulated among the principal stakeholders. The Company wellcomes the opinions, suggestions, and comments of all stakeholders on its sustainable development report. To respond, you may use any of the following options:

- Complete the feedback form attached to this report and send it to the address indicated
- Fill out the feedback form on the Company's public website (www.sakhalinenergy.com) or
- Fill out the feedback form at one of the Company's information centres (a list of information centres is provided in Appendix 5: *List of Company information centres*).

Definition of Report Contents

The main approach to presenting information in the Company's performance report was to provide of balanced coverage of three main areas of sustainable development: economy, ecology, and social policy. An important criterion for deciding whether or not to include certain information was the principle of materiality, which involves evaluating the significance and impact of specific events, factors, and indicators on the Company and its main stakeholders. It is essential to take into account the materiality and information about events when making strategic and immediate decisions on sustainable development.

This is why the Company shares and uses the main principles of international reporting on sustainable development, such as:

GRI Principle	Definition

Materiality	Sakhalin Energy seeks to disclose in this Report all the topics and indicators relating to its sustainable development performance. To identify these issues and to determine and avaluate their materiality, the Company analyses the internal and external factors of its operations that affect the economy, the environment, and the social sphere, including the Company's mission and vision, strategy and development, questions, expectations, and stakeholder concerns, etc.
	The Company used a series of balanced methods and tools, especially the following:
	• Identify and analyse public needs, interests, expectations, and concerns in the course of public, group, and individual consultations (a detailed annual report on completed consultations, issues raised, and the Company's response is available on the Company's public website)
	• Public opinion polls (as a minimum, annual sociological surveys of the population and/or experts' opinion in areas where the Company operates, as well as opinion polls of Company personnel); as a rule, a specialised contractor was enlisted to conduct public opinion surveys. In 2009, 800 individuals in 22 communities on Sakhalin Island were surveyed. Some of the objectives accomplished by this survey include:
	  • public opinion on individual aspects of implementing the Sakhalin-2 Project, possible impact on the population, and the socioeconomic state of communities
	  • public attitude towards the Sakhalin-2 Project, Sakhalin Energy, its contractors and subcontractors, and concerns over the Sakhalin-2 Project and the operations of Sakhalin Energy
	  • public information needs on Project implementation and the operations of Sakhalin Energy, and related matters.
	• Media analysis which is conducted by the Company on a regular basis.
	
	Additionally, we analysed issues raised in reports by other oil and gas companies

Stakeholder inclusiveness	The Company determines and analyses in a systematic and logical manner the range of stakeholders by groups and issues of mutual interest. Section *Stakeholder engagement* of this report presents information on stakeholder engagement, including approaches, principles, and the results of engagement processes. The principal document guiding the Company's stakeholder engagement is the Public Consultation and Disclosure Plan, developed according to Guidance Note F: Guidance for Preparation of an Information Campaigns and Public Consultation Plan of the International Finance Corporation (IFC). It is updated yearly and is available on the Company's public website. The plan details the process used to identify and analyse stakeholders and describes methods used for stakeholder engagement. Additionally, in preparing this Report, the Company held two rounds of consultations with its stakeholders, according to the principles and provisions of the AA1000SES International Standard. Detailed information about the consultations and their results is presented in the Section *Stakeholder engagement*.

GRI Principle	Definition
Sustainability context	A focus on corporate social responsibility and an adherence to sustainable development principles is at the core of the Company's production operations. The Company developed a sustainable development policy from the outset of its operations. This policy has been applied throughout the entire duration of the Sakhalin-2 Project, by incorporating sustainable development principles in the business plans and operational methods of the Company. Throughout this report, the Company sought to present its contribution to sustainable development in a broader national context and a regional context.
Comprehen-siveness	The report contains information on all structural units of the Company and on all areas affected by the Company's performance on sustainable development, including economic, environmental, and social aspects. In this report, the Company sought to make the most complete disclosure of information possible: • According to GRI principles and indicators, within the boundaries of its operations (primarily the Production Sharing Agreement) • Taking into account the interests and expectations of stakeholders to include specific topics in this report • According to the priorities of shareholders, lenders and Company executive management.

Report Quality Assurance

Balance	The Company sought to make a balanced presentation of its performance, including favourable aspects (accomplishments) and unfavourable aspects (action items). It sought to pay attention to issues disclosed in the report relative to their materiality, interest, and the stakeholders expectations to include specific topics in this report.
Compatibility	In this report, the Company follows the GRI Sustainable Development Reporting Guidelines and their technical protocols, so stakeholders can compare the results of the Company's performance with other companies and organisations. Since this is the first sustainable development report prepared in accordance with GRI Guidelines, the Company's performance indicators can only be compared with future reports.
Accuracy	The Company sought to make an accurate, specific, and sufficiently detailed presentation of its performance results, so that stakeholders can objectively evaluate the results. To this end, the Company used qualitative descriptions and quantitative information based on data from standard financial and statistical reports, reports to relevant oversight agencies, the Russian Party, shareholders and lenders, and from internal reports drawn up according to the procedures and methods adopted by the Company. Where estimates are used, a reference to the source is provided or a rationale is presented for using estimates.

Timeliness

This is the first sustainable development report prepared according to GRI Guidelines. Development of the report was carried out systematically, including special consultations with stakeholders in the course of its development and publication in the second quarter of the year immediately following the reporting year.

Clarity

In preparing sustainable development report, the Company sought to present information in a manner that is understandable and accessible to stakeholders in form and substance.

The report avoids specialised technical terms, acronyms, jargon, or other content likely to be unfamiliar to most stakeholders. The report makes use of charts, graphs and schemata, and provides explanations of abbreviations and terms where appropriate and necessary.

Reliability

Report details are based on data from standard financial and statistical reports, reports to the relevant supervisory agencies, the Russian Party, shareholders and lenders to the Sakhalin-2 Project, as well as internal reports drawn up according to the procedures and methods adopted by the Company.

A number of details reflecting the results of the Company's sustainable development performance have also been verified independently. A corresponding reference is in the report.

Definition of Report Boundaries

The report is corporate wide and contains information on all structural units of the Company and areas affected by the Company's sustainable development performance, including social, economic and environmental aspects.

INTRODUCTION

Sustainable development and corporate Social Responsibility – essential components Sakhalin Energy's strategic development

'Sustainable development meets the needs of the present without compromising the ability of future generations to meet their needs'– this definition in 1987 is from the UN World Commission on Environment and Development (the Brundtland Commission). The essence of this definition is still relevant and is shared by politicians, the public and entrepreneurs worldwide.

'Sustainable development' has become firmly embedded in the activities of the general public and business in developed and major emerging economies. This is mainly because the majority of these countries made significant international commitments in accordance with An Agenda for the 21st Century, adopted by the United Nations Conference on Environment and Development in Rio de Janeiro in 1992, and the Johannesburg Declaration on Sustainable Development, adopted at the World Summit on Sustainable Development in 2002.

Owing to this forward–moving process, flagship companies and corporations are developing and implementing their own corporate sustainability plans. An important stage in the establishment of corporate sustainable development practice was the introduction of the Global Reporting Initiative (GRI) international standard based on the Triple Bottom Line principle: economy of companies, ecology of production, and social policy.

At the corporate level, a sustainable development strategy ensures a gradual fusion of the economic, environmental and social aspects of the Company's operations into a single self–organising system. In this sense, sustainable development presumes and ensures economic effectiveness, environmental safety and social justice, combined with an overall reduction of human pressure on the biosphere.

Sakhalin Energy developed a sustainable development policy from the outset of its operations. The policy reflects the realities of the Company's operations in Russia and envisages the achievement of specific and practicable Company goals. These goals are aimed at facilitating the sustainable development of Sakhalin Island. This policy has been pursued throughout the entire duration of the Sakhalin-2 Project by incorporating sustainable development principles into the business plans and operational methods of the Company.

The starting point of the Company's sustainable development policy is the following seven principles. Sakhalin Energy has followed them since its inception:

- Minimise environmental impact
- Use resources efficiently
- Maximise profitability
- Maximise benefits to the community
- Respect and protect the rights of personnel and the population
- Interact and work with the shareholders
- Provide quality service to clients.

These principles are incorporated into the Company's sustainable development policy. The main commitments Sakhalin Energy has made in connection with its sustainable development policy are the following:

- Carry out business responsibly and efficiently to deliver a robust project that maximises benefits to shareholders, the Russian Federation and the Sakhalin community
- Contribute to the present and future needs of the society of Sakhalin Island while keeping a balance among economic development, environmental protection and social responsibility
- Work with stakeholders to identify ways to contribute to the wider long–term economic, environmental and social benefits of the Sakhalin Oblast.

To us, corporate social responsibility (CSR) is a measure to realise the Company's sustainable development policy in stakeholder engagement. As a socially responsible company, since 2001 Sakhalin Energy

published information on its performance, demonstrating to the public at large that it pays constant and specific attention to environmental and social aspects. This minimises the Company's exposure to the risks of internal and external conflicts and to evnvironmental sanctions.

As mentioned above, in 2009 the Company took a major step towards improving the format of its public reporting: a transition to international standards in sustainable development reporting and stakeholder engagement, as part of the Global Reporting Initiative and AA1000 Accountability (AA1000SES standard). In many ways, this is connected with the successful completion of the major construction works of Phase 2 of the Project and the beginning of the operational phase, aligned with the stable production and delivery of oil and liquefied natural gas to consumers in 2009. We hope that this modern, standardised way of non–financial reporting will enable our stakeholders in Sakhalin, the Russian Federation, and interested parties globally to regularly receive even more objective, concreate and comprehensive information on our operations.

Sustainable development and Corporate social responsibility, use of international standards

It is common knowledge that at the turn of the 21st century a universal goal for the advancement of the global community, including individual countries, regions, cities, enterprises and corporations is the transition to 'sustainable development'. This is understood as the preservation of the environment and the conservation of natural resources, in combination with the social and economic welfare of present and future generations. Corporate best practice has demonstrated that sustainable development and CSR are interrelated concepts, and measures of their practical implementation are mostly identical.

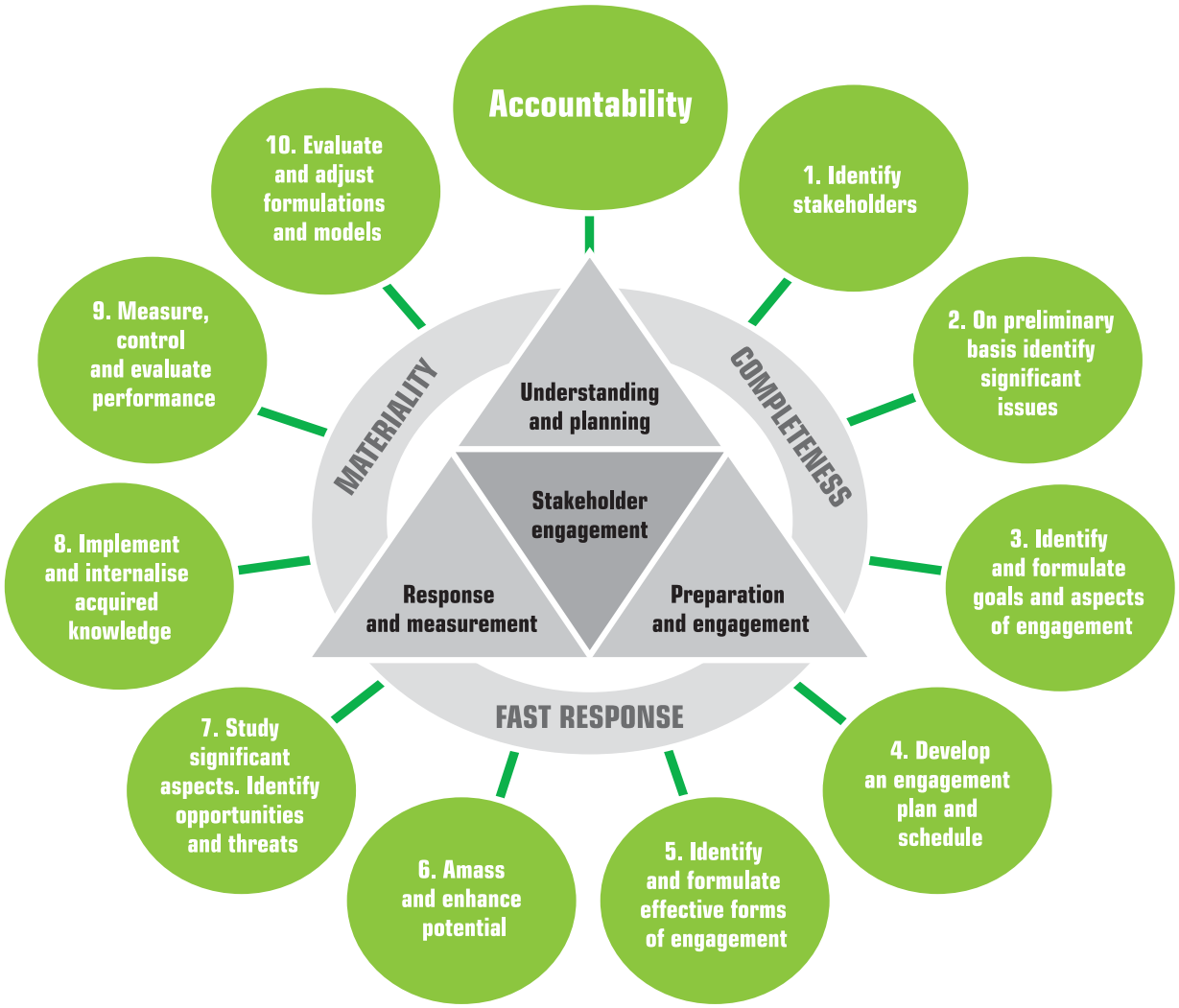
Over the last 15 years, the leading members of the international business community have recognised that CSR encompasses a broad range of business activities in the economic, social and environmental spheres: within the so–called three 'pillars' of social responsibility or three interconnected aspects of sustainable development. CSR is based on compliance with legislation and additional voluntary initiatives by companies, in making their contribution to social development. As shown by the best international and Russian practices, CSR is a system of ethical norms and values for companies; at the same time, it is a system that measures economic, ecological and social activities implemented on the basis of regular stakeholder engagement, aimed at minimising non–financial risks; long–term enhancement of Company image; and comprises corporate business reputation of companies capital growth and competitiveness.

CSR ensures the profitability and sustainable development of companies.

Social responsibility was and remains an important factor in the business reputation, public image, sustainable development and capitalisation of any company. The global financial and economic crisis caused both international and Russian companies to scale back somewhat the scope of their CSR activities, particularly voluntary initiatives of a social and charitable nature. Nevertheless, in the context of decreasing financial capabilities for the implementation of CSR initiatives, the greater part of them are becoming increasingly relevant and even critical for overcoming the crisis. As international practices show, the importance of CSR and sustainable development measures at the recovery stage is not diminished, but, quite the opposite, substantially increases. This applies to all companies that, while undergoing transformation, continue to operate. Sakhalin Energy too, as a socially responsible company in the broadest sense of the concept, continued to focus on this essential component of its business during the crisis year of 2009.

Modern international standards of CSR and non–financial (sustainable development) reporting spell out principles and processes for the effective interaction between the Company and its stakeholders. For instance, AA1000SES, one of the world's most widely used standards and one often used in Russia,

Stages and elements of the system of quality stakeholders engagement



proposes a model of consistent and systemic interaction between a modern socially responsible company and its stakeholders.

Another international standard, the Global Reporting Initiative (GRI), calls for a system of indicators across all areas of sustainable development based on the Triple Bottom Line concept. G3, the third generation of this standard that went into effect at the end of 2006, comprises 121 elements of standard reporting, including nine economic, 30 ecological and 40 social indicators, which primarily enable stakeholders and the public at large to objectively evaluate the level of social responsibility of a company and its contribution to sustainable development. By the end of 2009, international CSR and sustainable development reporting was practiced by over 6,000 leading international companies. Having completed its large–scale infrastructure Phase 2 construction works in 2008–2009, Sakhalin Energy has joined this club of flagship international companies and now uses not only the best CSR and sustainable development practices, but also universally accepted forms of international sustainable development reporting.

The introduction and use of advanced international CSR standards and non–financial reporting will enable Sakhalin Energy to join the ranks of the leading Russian and international companies in this sphere.

ABOUT SAKHALIN ENERGY

Sakhalin Energy Investment Company Ltd. ('Sakhalin Energy' or Company) was set up to implement the Sakhalin-2 Project according to the production–sharing agreement with the Russian Federation. The Company, established in 1994, is developing the Piltun–Astokhskoye and the Lunskoye oil and gas fields, offshore Sakhalin Island in the Sea of Okhotsk in the Russian Far East.

Sakhalin-2 is one of the world's biggest offshore projects to produce and export oil and gas, and one of the most technologically advanced ever implemented by the oil and gas industry. The level of objectives, scope of operations, and scale of the investments, coupled with the harsh environment, unique ecosystem, and the lack of oil and gas infrastructure on Sakhalin Island, and its remoteness from major Russian commercial centres meant the Company had to apply the best practices of the industry and use innovative technologies and efficient managerial solutions. A unique partnership of its shareholders helped Sakhalin Energy to master these tasks.

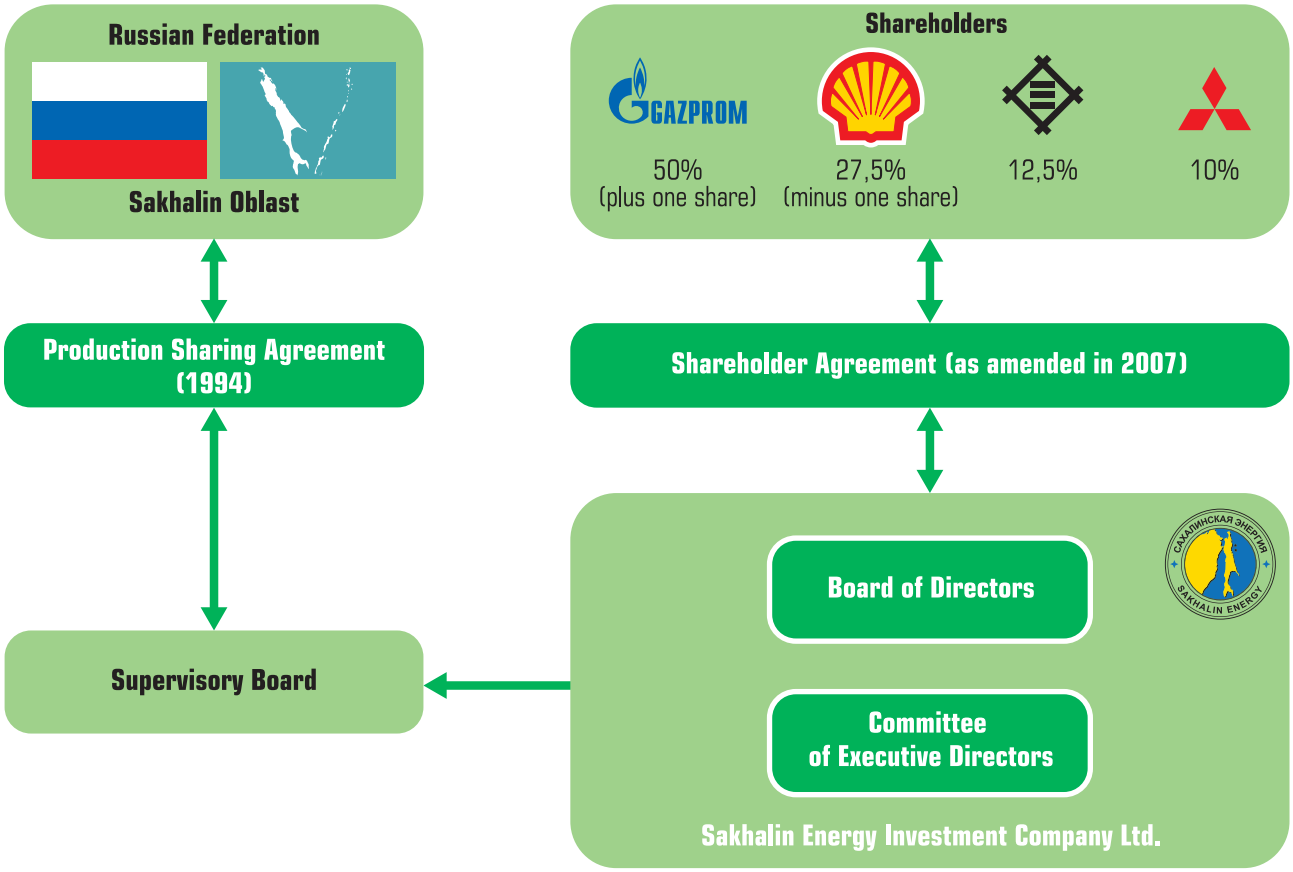
Management Structure

Sakhalin Energy is the investor and operator of the Sakhalin-2 Project.

Sakhalin Energy signed a production sharing agreement (PSA) in 1994 with the Russian Federation, represented by the Russian Government and the Sakhalin Oblast Administration. A PSA is a commercial contract between an investor and the state, allowing the investor to make a long–term investment on a large scale that carries a high risk. In a PSA, the state grants an investor the exclusive right to develop a subsoil field by its own means and at its own risk. The Sakhalin-2 PSA defines the terms and conditions to explore, develop, produce, process and transport hydrocarbons. The PSA provides a framework for contractual relations between an investor and the government. The agreement spells out the production sharing arrangement between the contracting parties, substituting the collection of various taxes, levies and duties, and ensuring a stable taxation regime during the life of the project. According to the PSA conditions, the Russian Federation retains the sovereign right of ownership to the oil and gas fields and Sakhalin Energy invests the funds required to explore and develop the fields.

The PSA allows for complete financial transparency of the Sakhalin-2 Project. The Russian Federation approves the estimates of expenditures and has the right to audit the investor's expenses. In addition, the parties bear mutual responsibility for compliance with the rules established by the PSA.

The Sakhalin-2 PSA describes a specific tax regime for Project development. The majority of the taxes and custom duties are substituted by production sharing. This effectively means that instead of a mineral resources tax, property tax and some other taxes and levies, Sakhalin Energy pays royalties (fees for subsoil use), starting from first oil production. In addition, as soon as the investor recovers the production costs, production profits are shared by Sakhalin Energy and the Russian government. The specific shares of each party depend on Project economics. The Company also pays the Russian profits tax, at a rate, which according to the PSA exceeds the currently effective profits tax rate generally established for tax payers not eligible to PSA conditions. This means the Russian Federation share of the Sakhalin-2 Project is made up of tax receipts, royalties and a share of production profits.



The Company's shareholders, which retain their shares through subsidiary structures, are Gazprom (50% +1 share), Shell (27.5% –1 share), Mitsui (12.5%) and Mitsubishi (10%). These major international companies have extensive knowledge and experience in the construction and operation of oil and gas infrastructure facilities, and in the production and transportation of hydrocarbons.

The responsibilities of the Supervisory Board (SvB) for Project implementation are spelled out in the PSA. The Board makes fundamental decisions relating to the PSA. Among its decisions, the Board approves development and work programmes and budgets, LNG sales agreements, procurement procedures, and training and employment plans for Russian Nationals. The Board also reviews the annual report of the Company and appoints auditors on behalf of the Russian Party. The Board comprises six representatives of Sakhalin Energy and six representatives of the Russian Party, including two government representatives of the Sakhalin Oblast and four from the Russian Federation.

Shareholders appoint the Board of Directors to manage Sakhalin Energy. The Board of Directors is made up of executive and non–executive directors of the Company. All board members are appointed by shareholders. Charles Watson is the Chairman of the Board of Directors.

The Committee of Executive Directors, headed by the Chief Executive Officer, directly manages the Company. The Committee sets out the everyday activities of Sakhalin Energy through business plans and strategies, and solutions for their implementation. As of 1 April 2010, the Company had six executive directors who are department heads in charge of key functions: Chief Executive Officer, Production Director, Technical Director, Finance Director, Legal Director, and Director of Human Resources.

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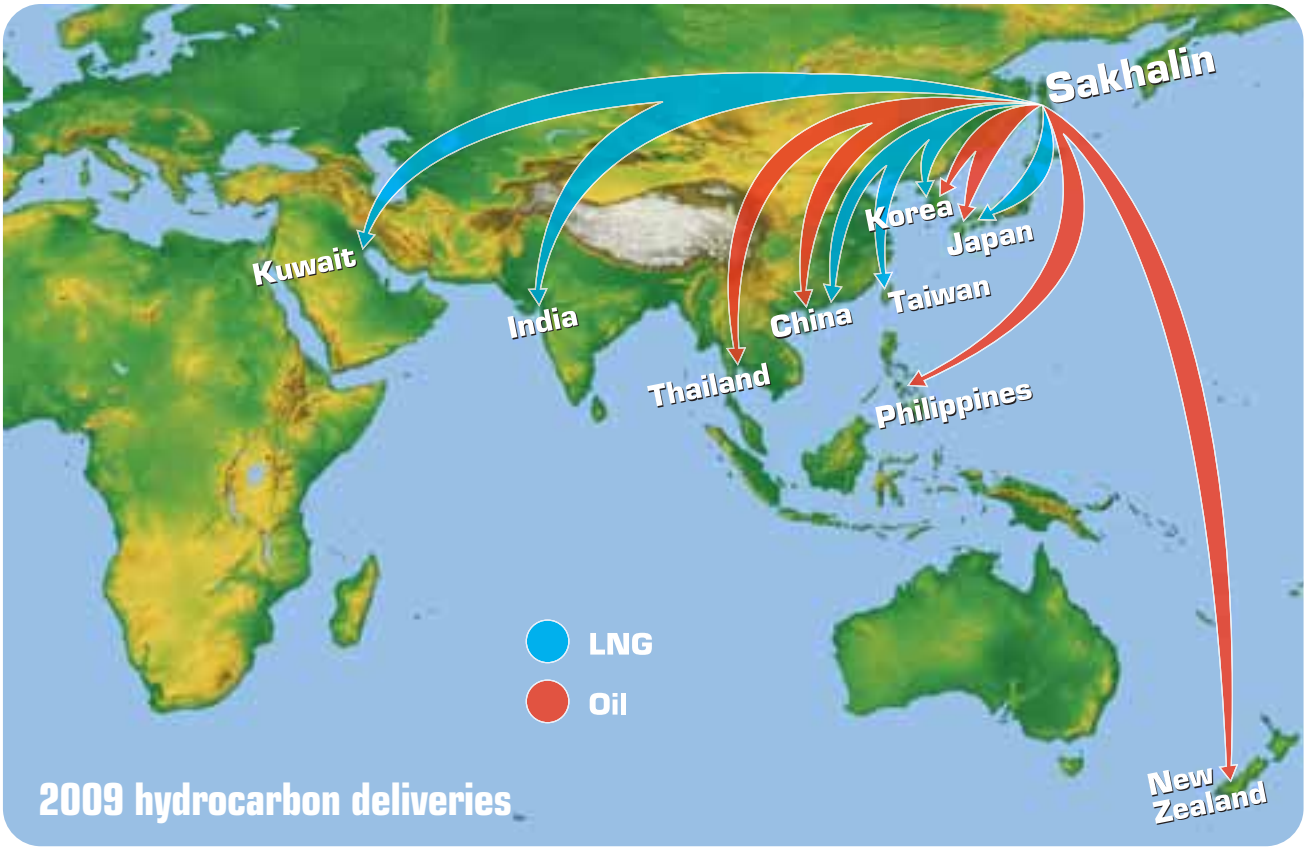


About Sakhalin-2

The license areas of the Sakhalin-2 Project are in the Sea of Okhotsk near the north–eastern coast of Sakhalin Island. The location of the oil and gas fields determines the destination of supplies: most of the liquefied natural gas and an oil blend produced from the Project are sold to the high–growth energy market of the Asia–Pacific region (APR).

The resource base of the Project is formed by two oil and gas fields located about 15 kilometres off the coast of Sakhalin Island. Piltun–Astokhskoye is predominantly an oil field and Lunskoye is a gas and condensate field. The water depth in the fields varies from 28 to 48 metres. The total estimated reserves of the Project fields represent approximately 9% of the hydrocarbons reserves offshore Sakhalin.

THE SAKHALIN-2 PROJECT IS THE FIRST RUSSIAN OIL AND GAS COMPLEX TO SELL TO THE ASIA–PACIFIC MARKET. IN 2009, SAKHALIN ENERGY CELEBRATED ITS 10TH ANNIVERSARY OF OIL SALES TO THE REGION.

The Sakhalin-2 Project is implemented in phases determined by the scope, technological sophistication, required investment, and by the harsh environment and remoteness of the fields from major Russian centres of economic activity. Field development began in 1996 in the Astokh area of the Piltun–Astokhskoye field. In 1999, Sakhalin Energy started seasonal oil production from the Molikpaq (PA–A) ice–resistant offshore platform, the first offshore oil and gas production platform on the Russian shelf. Under Phase 1 of the Project, oil production took place only in ice–free months, for about six months. The 10th production season, the last season during Phase 1, started on 30 July 2008. In late 2008, the Molikpaq platform was successfully switched to year–round operation using the new infrastructure of Phase 2.

Phase 2 of the Project started in 2003, the large–scale integrated development of the Piltun–Astokhskoye and Lunskoye fields, to simultaneously produce oil and gas with an integrated production infrastructure. While similar integrated projects have been implemented in other countries, the construction phase was much longer and facilities were commissioned in succession.

Phase 2 involved constructing and commissioning one of the world's largest oil and gas infrastructure projects to produce oil and gas, liquefy natural gas and transport oil and LNG to customers.

Production facilities of the Sakhalin-2 Project comprise:

- The Molikpaq (PA–A) platform to produce oil and associated

gas in the Astokh area of the Piltun–Astokhskoye field
- The Piltun–Astokhskoye B (PA–B) platform to produce oil and associated gas in the Piltun area of the Piltun–Astokhskoye field
- Lunskoye A (LUN–A) gas production platform, the first and only Russian offshore gas and gas condensate production platform
- TransSakhalin pipeline system, consisting of offshore pipelines connecting three platforms to the shore, and onshore oil and gas pipelines running from north to south of Sakhalin Island to the Prigorodnoye production complex
- An Onshore Processing Facility (OPF), designed to process gas and gas condensate coming from the platforms, for further transportation via the onshore pipeline system
- Booster Station 2 (BS2)
- An Oil Export Terminal (OET) and the Tanker Loading Unit, located 5 km offshore in Aniva Bay
- The first Russian liquefied natural gas plant.

The LNG Plant, along with the LNG jetty/OET, is part of the facilities of the Prigorodnoye Production Complex, where the first Russian specialised seaport for oil and gas exports operates.

More detailed information on the Company and the Project, including the history of development, is available at the Company's public website. Under the Sakhalin-2 Project, unique for its content and the scope of its implementation, the Company set a number of records at Russian and international levels, including for technological achievements, project financing, and unique partnerships with stakeholders (see Appendix 4 *Sakhalin-2 records*).

VITYAZ CRUDE OIL IS A NEW BRAND INTRODUCED BY SAKHALIN ENERGY. IT IS A LIGHT SWEET OIL SIMILAR TO LIGHT OMAN CRUDE OIL.

Liquefied natural gas, or LNG, is natural gas in its liquid form. Natural gas is made up of primarily methane, with low concentrations of other hydrocarbons, water, carbon dioxide, nitrogen, oxygen and some sulphur compounds. During the process known as liquefaction, natural gas is cooled to minus 160° Celsius. Before the gas can be cooled, components such as water vapour, carbon dioxide and heavy hydrocarbons are removed from the gas in various processes. During the subsequent cool down period, the gas becomes a clear, colourless, odourless liquid. In this state, natural gas is reduced in volume by 600 times, so it can be transported by sea in LNG tankers. Less than half the density of water, LNG will float if spilled on water.

LNG is returned to a gaseous state at re–gasification terminals after delivery to customers. LNG is not corrosive or toxic. It can be used for heating and cooking as well as generating electricity and for other industrial uses. LNG can also be kept as a liquid for use as an alternative source of fuel for transport.

Natural gas is the cleanest–burning fossil fuel. LNG is a price–competitive energy source that could help meet the future economic needs of many countries. LNG also offers unrivalled flexibility of delivery compared with natural gas supplied by pipeline.

Company mission, core values and business principles

Mission and vision

The mission and vision of Sakhalin Energy provide the basis for determining the goals and strategies of the Company.

The mission: Sakhalin Energy is committed to being a premier energy supplier, recognised for its operational excellence, reliability and safety. We conduct our business in an ethically, socially and environmentally responsible manner.

The vision: to be the premier energy source for the Asia-Pacific.

The objectives: to commercially develop, operate and sell hydrocarbons from our fields, in keeping with the licenses of the Sakhalin-2 Project, and to develop the required project infrastructure for the benefit of our shareholders, the Russian Federation, the Sakhalin Oblast and the local community.

Values and general business principles

The core values of Sakhalin Energy, such as integrity, transparency and respect for people, underlie all Company activities and form the basis of its General Business Principles. These principles cover business, competition, business integrity, political activities, health, safety and the environment,

THE COMPANY'S EFFORTS TO PROTECT THE ENVIRONMENT HAVE BEEN RECOGNISED BY THE INTERNATIONAL COMMUNITY: THE OIL EXPORT TERMINAL OF SAKHALIN ENERGY WON 'THE ENVIRONMENTAL SAFETY' CATEGORY IN THE OIL TERMINAL 2009 SECOND INTERNATIONAL CONTEST, IN NOVEMBER 2009.

Quality Assurance
Sakhalin Energy uses quality assurance, a formal methodology to assess the quality of products or services provided. Quality assurance includes a review and assessment of services, problem identification, corrective actions to remedy any deficiencies, and evaluation of actions. It assumes necessary precautions have been taken so the entire production of a product or service is within specifications under a wide range of operating conditions. This usually requires creating indicators to master and monitor the production process.

liaison with the local population, and compliance with Russian laws.

The General Business Principles apply to all aspects of Sakhalin Energy activities and determine the conduct of each employee in each subdivision. Over all the years of its existence, the Company has been guided by these General Business Principles, and compliance with

tthose principles is the decisive component of our continued success.

The General Principles are supported by a number of documents, especially the following:

- Statement of General Business Principles
- Code of Conduct
- Sustainable Development Policy
- Grievance procedure
- Conflict of interest policy and procedure.

Application of these principles is supported by control procedures, developed to ensure these principles are understood by employees, so employees can acknowledge their activities are in line with these principles. The control system also includes the responsibility of management to provide employees with safe and confidential methods to express their concerns, ask questions and inform the Company of cases infringing these principles. In turn, employees are responsible for notifying the Company about suspected infringement of the General Business Principles.

Company responsibility and commitments

Sakhalin Energy's commitments extend to six stakeholder groups. Management is responsible to continuously assess the business and prioritise its activities to effectively fulfill its commitments as a single and undivided business objective.

- **To shareholders:** to keep the investments of shareholders safe and to ensure these investments grow at a level competitive with the other industry leaders.
- **To the Russian Party:** to comply with the Company commitments to the Russian Federation and Sakhalin Oblast, and to protect the rights of both under the production–sharing agreement signed between Sakhalin Energy and these parties.
- To **customers**: to engage new customers and to retain existing customers by manufacturing and offering products and services attractive in price, quality and safety, and with a minimum impact on the environment, and delivered with a high level of commercial, technological and environmental competence.
- To **Company staff**: to respect employees rights, to provide employees with decent and safe working conditions and competitive terms of employment; to contribute to career development and deploy the abilities of staff at a maximum; to ensure equal opportunity to employees and to develop their abilities and skills; to encourage employee participation in selecting and planning their work; and to provide employees with the opportunity to inform management of their needs. The efficiency of all Sakhalin Energy employees in their work is considered a pre–condition to commercial success.
- To **business partners**: to establish mutually beneficial relations with contractors and suppliers, and to facilitate application of the General Business Principles of Sakhalin Energy, or similar principles in relations with business partners. Effective application of these principles should be an essential condition for deciding whether to start or continue a business partnership.

People are judged by their actions. Business integrity, due diligence, and mutual respect underlie all activities of Sakhalin Energy staff. We are strongly convinced that the key principles behind the work of any team should include confidence, transparency, professionalism, team spirit, and pride in their work.

Sakhalin Energy is committed to promoting sustainable development in all areas of its activities. This means finding a balance between short–term and long–term interests, and taking into account economic, environmental and social factors in commercial decisions.

Conducting activities in strict compliance with the business principles assists the Company in maintaining its excellent reputation. We call on our staff to demonstrate leadership, responsibility, and team spirit, qualities that promote the success of Sakhalin Energy. We also call on our partners to adopt these principles or to adhere to their own high standards. Management of the Company must serve as an example for all employees in following these principles, and to persuade employees to comply with the spirit and the letter of this document.

Over many years, these principles have been the foundation of our business success, and their further observance guarantees our continued success.

- To the **community**: to conduct business in a socially responsible manner, observing the laws of the Russian Federation and the countries where Sakhalin Energy operates; to express support for basic human rights within the legal business framework; to pay necessary attention to health, safety and environmental issues.

Corporate culture

The corporate culture of Sakhalin Energy is based on its mission and vision, and furthered by its General Business Principles and Code of Conduct.

The Code of Conduct is the main document that ensures greater clarity on the norms and standards of behaviour the Company expects its staff to adopt and to observe, and how to align their personal behaviour with the core values of the Company, such as integrity, due diligence, and respect for people. The Code of Conduct summarizes the main rules, standards and norms of behaviour required to achieve Company goals. The Code details the requirements and guidelines for all Company employees in several areas of potential risk in all Company subdivisions, including:

- Health, Safety and Environment
- Personal and business integrity, including on bribery and corruption, and conflict of interest
- Protection finance and assets
- Staff issues, such as equal opportunity based on skills, job performance, and other work–related characteristics clearly articulated and consistently applied labour standards standards of job performance and management systems inadmissibility of defamation by action, illegal discrimination of staff showing respect and impartiality to staff and external parties, in compliance with the core values and the General Business Principles
- Information management.

An essential component of our corporate culture is internal communications. The Corporate External Affairs department sets up and maintains a corporate culture of excellence and an efficient internal communications system.

- Internal communications include:
  - Conducting opinion polls of Company staff on a wide range of issues
  - Publishing corporate mass media and various information and reference materials
  - Providing general corporate information messages through the daily news screen and e–mail
  - Using general information boards
  - Holding training workshops to explain the Company's new procedures and programmes.

Company staff are regularly informed on the results from meetings of the Committee of Executive Directors, the Board of Directors and the Supervisory Board, and on other important Company events, through internal communications. Over many years, the Company has held regular staff engagement sessions, where members of the Committee of Executive Directors report on the main results of Company activities and current and strategic plans.

SOCIAL AND ECONOMIC BENEFITS OF SAKHALIN-2 PROJECT FOR THE RUSSIAN FEDERATION AND SAKHALIN OBLAST

General

Investments to develop a large–scale project stimulate more business for industries and services outside the oil and gas sector. The activities of Sakhalin Energy to implement the Sakhalin-2 Project boosted the development of many enterprises on Sakhalin Island and elsewhere in Russia, and gave them potential access to international markets. The Project also provided employment opportunities, higher salaries, growing retail trade, better social programmes and more tax revenue. In general, the Project is making a major contribution to the wide–ranging revitalisation and development of the Island's economy, usually referred to as a 'multiplier effect'. According to the Council on the Study of Productive Forces at the RF Ministry of Economic Development, every dollar invested in the construction of the Sakhalin-2 Project resulted in 0.6 dollar added to other sectors of the economy.

Benefits for the Russian Federation

- The Project has transferred US$ 1.299 billion to the Russian Federation (see Section *Financial benefits for the Russian Federation*)
- Russian companies have mastered new technologies and enjoyed new business opportunities (see Section *Russian content*)
- Russian contractors have been awarded contracts of more than US$ 14 billion (see Section *Russian content*)
- Russian businesses have gained invaluable experience working together with international consortiums on complex project management, in line with best international practice.

Benefits for the Sakhalin Oblast

- Paid US$ 100 million to the Sakhalin Development Fund (as committed under the production sharing agreement for Sakhalin-2)
- Generated significant income flows for the budgets of the Sakhalin Oblast and municipal entities (see Section *Financial benefits for the Russian Federation*)
- Contributed to the large–scale upgrade of Island infrastructure worth approximately US$ 600 million (see Section *Development of the regional social infrastructure*)
- Created new employment opportunities, directly and indirectly, and improved the quality of the workforce. During construction, Sakhalin-2 employed about 12,000 Sakhaliners; at the end of 2009, 78% of 5,600 of Sakhalin-2 employees were local residents. From 2003 to 2009, the Sakhalin Oblast had the lowest unemployment rate of any Russian region (1.2 per cent in early 2009)
- Contributed to a higher income and better living standard for local residents
- Sakhalin–based companies have been actively involved in the Project as contractors and subcontractors, building up their capacity and competitiveness (see local content examples in the Section *Russian content*)
- The Company has taken a proactive approach to developing regional social and public initiatives (see Section *Social investment and sustainable development programmes supported by Sakhalin Energy*).

Time period	Russian Party revenue from the Project (US$ million)
1995–2008	931
2009	368
1995–2009	1,299

Financial Benefits for the Russian Federation

When the Project started producing and exporting oil year round, the Company significantly boosted hydrocarbons output, and financial inflows to the Russian Party increased in proportion.

As a result, subsoil royalties in 2009 increased sevenfold to US$ 281 million versus US$ 39 million the previous year.

Sakhalin Energy paid a total of US$ 368 million in taxes and other statutory payments into government budgets at federal, regional, and local levels in 2009, a 75 per cent increase from the year before.

The Russian Federation through 2009 has received a total of US$ 1.299 billion from the Project.

Payments by Sakhalin Energy accounted for 28 per cent of the total amount transferred to the budget from 1995 to 2009.

The Company paid to the Sakhalin Oblast budget RUB 1.79 billion in taxes and other charges in 2009. Some decrease in these payments reflects the completion of construction and a consequent decline in the number of construction workers engaged in the Project.

Receipts from Sakhalin-2 account for a significant part of the budget revenues of most of the municipalities engaged in the Project.

Russian Content

Russian content commitments in the Sakhalin-2 Project as stated in the PSA are a strategic priority for Sakhalin Energy. The Russian content clause of the PSA provides a unique mechanism for Russian companies to get access to the best international technologies, business practices, and managerial skills.

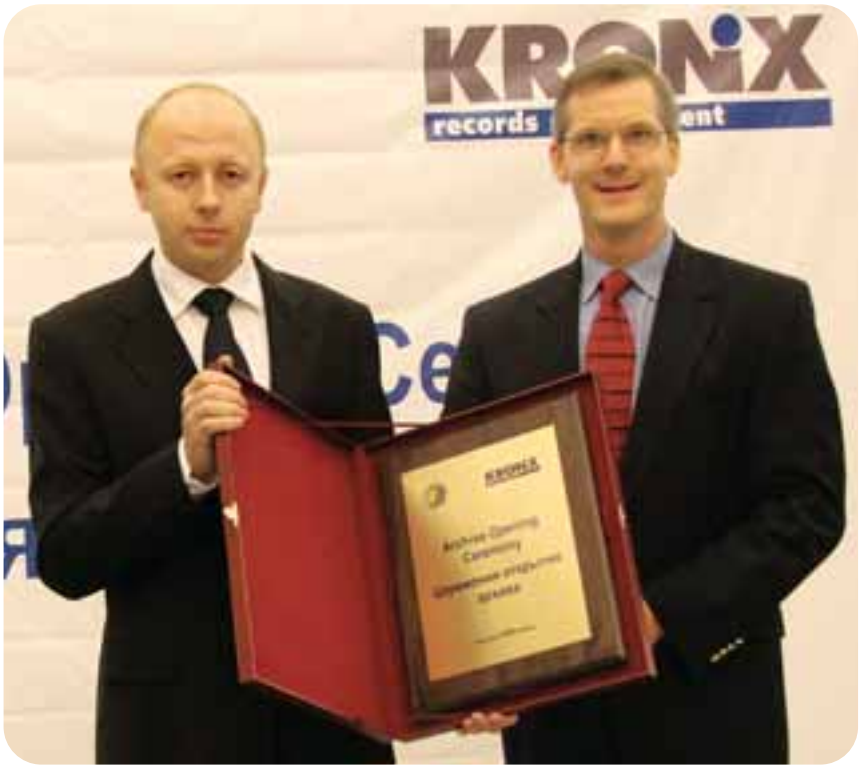
BY THE END OF 2009, RUSSIAN COMPANIES HAVE BEEN AWARDED CONTRACTS WORTH MORE THAN US $14 BILLION.

Russian content is defined as the use of Russian industrial and human resources. It is measured in man–hours and units of supply. Sakhalin Energy is committed to 70% Russian content of its workforce, equipment, supplies, and contracted services over the life of the Project.

Sakhalin Energy is continually working to increase Russian content in the development of Sakhalin-2. To achieve this, the Company developed and introduced a Russian Content Policy and a Russian Content Development Strategy. Both documents are available on the corporate public website. Accordingly, the Company is planning procurement and contracting for Sakhalin-2 over the long term and is identifying opportunities to expand Russian

In June 2009, Sakhalin Energy and Sakhalinremflot signed a US$ 2.7 million long–term contract for the manufacturing and maintenance of lifting equipment for the Sakhalin-2 Project.

'This is not the first order Sakhalinremflot carried out for offshore projects,' Anatoly Moiseev, the General Director, said. 'We are proud to be the first Russian company to offer delivery and management services for special–purpose shipping containers. We were able to mobilise all the necessary resources at short notice and obtain international quality certificates. Already, we have received a number of interesting offers to participate in other offshore projects, which means Russian companies are able to compete with international companies.'



Pioneer in document management

In February 2009, Sakhalin Energy awarded Russian Kronix a contract for the storage of design engineering documents.

The Sakhalin–based enterprise decided to develop the archive business according to the very highest standards. It is now the first private documents archive in the Russian Far East, a pioneer in this market segment.

The Sakhalin archive company had to compete in a tender against bids from major international companies, and was able to prove its ability to collect and store documents that meet rigorous Russian and international standards.

Kronix already had experience in the oil industry. Since 2001, the company performed engineering, office maintenance, procurement and other services for Sakhalin Energy and Exxon Neftegaz Limited. According to Kronix Project Manager Matvey Egorov, the company was aware of the strict qualification criteria applied by Sakhalin Energy in putting together its bid. It surveyed the Sakhalin market of archive services and studied the experience of Moscow–based companies. To obtain the necessary skills, Kronix joined the International Document and Archive Management Association. The company analysed other market opportunities to further develop the document management business in Sakhalin.

content in due course. Another policy priority for Sakhalin Energy under these plans is to extend targeted assistance to Russian businesses to boost their competitiveness.

Apart from creating new jobs, especially during construction, personnel development, and capacity building in hydrocarbons production, the Sakhalin-2 Project opens up other opportunities to Russian companies:

- To improve corporate health standards and services, and the quality of supplies
- To adopt new technology and gain new experience
- To work with international partners and establish joint ventures
- To improve competitiveness in tenders in the Sakhalin Oblast and internationally.

Vendor Development Programme

To boost the competitiveness of Russian companies and share unique experience from the Sakhalin-2 Project, in 2009 the Company continued its vendor development programme. The programme has several training courses to give Russian vendors access to information on working with Sakhalin Energy and other major operators.

The vendor development programme covers three areas:

- Health, safety and environment
- Quality assurance
- Tendering skills.

New horizons for Sakhalin's design engineers

Sakhalingrazhdanproject, a design engineering institute, has been in the Sakhalin Oblast for over half a century. The institute survived the tough economic and political reforms of perestroika and retained its core human resources. However, its workforce shrank from 700 in 1988 to 200 in 1994.

The situation improved when new offshore oil and gas developments offered many new opportunities for design engineering contracts. Sakhalingrazhdanproject has been a Sakhalin Energy contractor for over a decade, and has completed a number of contracts for the Sakhalin-2 Project, including designing construction camps and storage facilities, and developing environmental documents.

Igor Emelyanov, General Director of the Institute, believes the 10–year collaboration of Sakhalingrazhdanproject with Sakhalin Energy has created new project work. Local designers have been able to learn and to practice international design standards of fire safety and earthquake–resistant construction. By working on oil and gas projects on Sakhalin Island, the Institute had to accomodate the requirements of international standards, which are now widely applied in Russia.

To win an international tender and to comply with its demanding requirements, the Institute completed the huge task of implementing the International Quality System. Because health, safety and environment are top priorities for Sakhalin Energy, the Institute applies a systematic approach to health management and has added new environmental support services.

In working with Sakhalin Energy, Sakhalingrazhdanproject also had to master state–of–the art engineering processes and improve working conditions.

Today, Sakhalingrazhdanproject is a stable and rapidly developing company. In the short term, the Institute plans to add new services. The clients of the Institute are yet another demonstration of its credibility. They include the capital construction offices of the Sakhalin Oblast, Yuzhno–Sakhalinsk, and other cities of the Oblast, Sakhalin Energy, Exxon Neftegaz Ltd., Sakhalin Railways, and the Directorate of the Kuril Islands Federal Programme.

MAIN PRODUCTION AND BUSINESS ACHIEVEMENTS

Startup of gas production in the Lunskoye field

Sakhalin Energy started producing gas from the Lunskoye field in January 2009. Lunskoye–A is the first platform to produce offshore gas in Russia.

LUN–A is the first platform in the world equipped with friction pendulum bearings, which protect the platform from seismic loads in the event of an earthquake. The platform is designed for year–round operation in a climate with ice, wind, waves and extremely low temperatures. A similar design was used in PA–B platform.

By the end of 2009, five of the wells in Lunskoye field were producing gas. These are 'big bore' wells, special technology designed for prolific reservoirs like Lunskoye that also have a very high gas flow rate. These are the largest producing gas wells in Russia.

LUN–A, THE FIRST OFFSHORE GAS PLATFORM IN RUSSIA, WAS INSTALLED IN 2006 AT A WATER DEPTH OF 48 METRES

Gas produced from LUN–A is pumped through a multiphase pipeline to the Onshore Processing Facility (OPF) installed seven kilometres inland from the LUN–A pipeline landfall.

Inauguration of the LNG plant

On 18 February 2009, the first LNG plant in the Russian Federation was inaugurated in a ceremony on Sakhalin Island. Russian President Dmitry Medvedev, who addressed the audience, described the plant as 'one of the most innovative, state–of–the–art production facilities that meets the highest standards.' Praising the LNG plant and the project as a whole, President Medvedev also said: 'Russia is one of the world's leading gas producers, and I am confident that this new facility will strengthen our potential for supplying gas and Russia's position as a global energy supplier.'

The high profile of the guests who attended the ceremony was an indication the launch of the LNG plant was a truly global event. About 500 important dignitaries were present during the ceremony. It was President Medvedev's first visit to Sakhalin since assuming office. The presence of Prime Minister Taro Aso of Japan marked the first visit by a Japanese leader to Sakhalin since the end of World War II. Among the honorary guests were Prince Andrew, HRH Duke of York (UK); the Netherlands' Minister for Economic Affairs, Maria van der Hoeven; executives of Gazprom, Shell, Mitsui and Mitsubishi; high–ranking Russian and foreign government officials; and business leaders.

Construction of the LNG plant took five years. About 10,000 workers and engineers from nearly 40 countries were employed during construction, which started in August 2003. The plant was designed and built by CTSD, an international consortium comprising Chiyoda Corporation and Toyo Engineering of Japan and Nipigazpererabotka and Khimenergo of Russia.

The LNG facilities occupy a site of 490 hectares. The LNG plant consists of two gas liquefaction trains (each capable of producing 4.8 million tonnes of LNG per year), an LNG jetty, a chemical laboratory, a central control room, and LNG tanks. Gas from the Lunskoye and Piltun–Astokhskoye fields is piped to the LNG plant after processing by the OPF for transport. The world class Lunskoye field is the main source of gas. In addition to its high heating value, Sakhalin gas is also known for its low level of impurities, and is considered a 'clean gas'.

DMITRY MEDVEDEV: THE CREATION OF THIS FACILITY WILL DEEPEN INTERNATIONAL COOPERATION, WHICH IS ESPECIALLY IMPORTANT TO US TODAY.

The LNG plant removes any water and trace impurities from the gas to prevent freezing or damage to infrastructure. The gas is then cooled to around –160°C, when it turns into a liquid, occupying about one 600th of its original volume and remaining liquid at ambient pressure. The Sakhalin-2 LNG plant uses Double Mixed Refrigerant (DMR) technology that Shell developed for this project. It is the world's most advanced technology, saving energy by taking advantage of Sakhalin's cold climate.

LNG produced by two trains runs to LNG tanks, each with a capacity of 100,000 m^3, for further export by special tankers. Due to the high level of automation of the LNG plant, a team of only 300 people is needed to operate it at the design capacity.

MORE THAN 100 JOURNALISTS COVERED THE CEREMONY, REPRESENTING MORE THAN 60 RUSSIAN AND INTERNATIONAL MEDIA.

Essential completion and status of facilities

The facilities of Phase 2 were essentially completed at the end of 2008. In parallel, the process of gradually starting them up and phasing them into operation began the transition to a fully integrated functioning of the system.

Transfer to full operation

The completed facilities under Sakhalin-2 Phase 2 underwent testing in 2009. The test operating mode is required to tune and conduct final checks on all systems and equipment before transferring them to full operation.

IN MAY 2009, THE COMPANY RECEIVED AN AWARD FOR THE BEST INNOVATIVE OFFSHORE PROJECT FROM THE BOARD OF DIRECTORS OF THE OFFSHORE TECHNOLOGY CONFERENCE, A WORLD FORUM FOR OIL AND GAS TECHNOLOGIES.

In parallel, Russian authorities carried out very thorough checks of the facilities. The final inspections by state body Sakhalin Rostekhnadzor covered all the major facilities of the Phase 2 project, including PA–B and LUN–A platforms, OPF, offshore and onshore pipelines, the LNG plant, OET, and pipeline maintenance depots. Sakhalin Rostekhnadzor issued conclusions certifying the completed facilities complied with technical standards, other regulations, and the design documents. In February 2010, Sakhalin Rostekhnadzor issued an order approving the certificate of compliance for the onshore pipelines.

Issuing the certificates of compliance allowes the Company to apply to state authorities for the necessary approvals for the full operation mode.

In addition to the positive outcome of the state checks, all our facilities were certified to be in compliance with the requirements of the ISO 14001:2004 standard for environmental management systems.

Molikpaq platform (PA–A)

The Molikpaq platform (PA–A), installed in 1998 in the Astokh feature of the Piltun–Astokhskoye field, was the first fixed offshore oil–producing platform in Russia. It began year–round operations during the winter of 2008–2009. Before switching to year–round production, all oil from Molikpaq was produced seasonally.

IN JULY 2009, MOLIKPAQ ACHIEVED AN IMPORTANT HSE MILESTONE – FIVE YEARS OPERATING WITHOUT A LOST TIME INCIDENT.

PA–A reached its design level for oil production in 2009. Molikpaq is currently operating 14 oil production wells, four water injection wells, one gas re–injection well and one cuttings re–injection well.

Lunskoye–A platform (LUN–A)

Production of gas and condensate from LUN–A started in January 2009. The big–bore wells drilled from LUN–A are the largest gas wells in Russia. Each LUN–A well produces enough gas to feed a 2 GW power plant. The prolific gas bearing zone of the Lunskoye reservoir and the very high gas flow rate determine the large diameter of wells. Each well can produce up to 10 million m^3 of gas per day.

Piltun–Astokhskoye–B platform (PA–B)

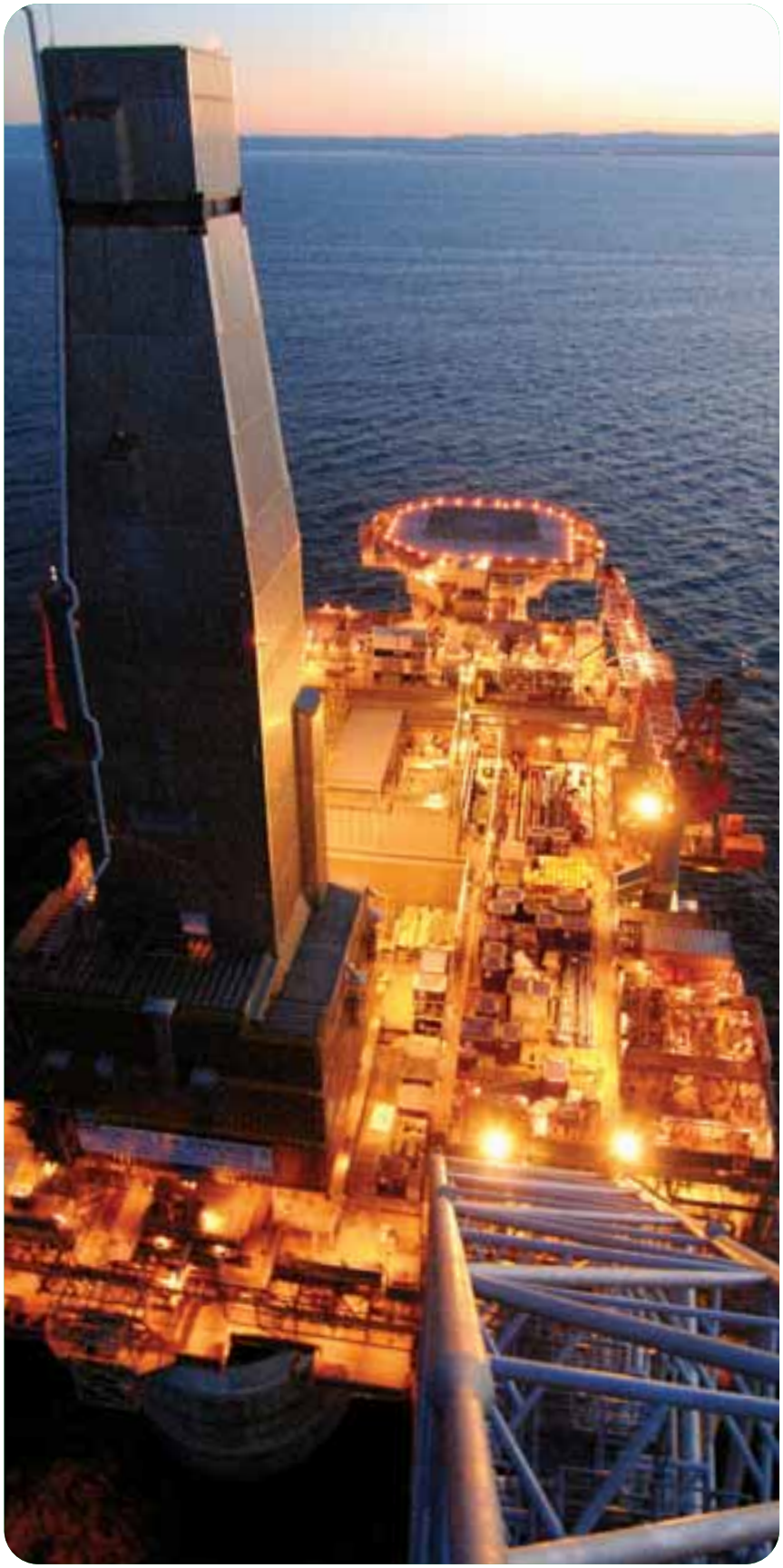
PA–B produced first oil in December 2008. By the end of the following year, six oil wells were operating on the platform.

THE SUCCESSFUL TRANSPORTATION AND INSTALLATION OF THE PA–B TOPSIDES WEIGHING 28,000 TONNES SET A NEW WORLD RECORD IN 2007.

The average daily capacity of each PA–B production well is some 10,000 bbls (1.3 thousand tonnes) of oil.

Onshore processing facility (OPF)

The main function of the Onshore Processing Facility (OPF) is the primary processing of natural gas and condensate coming from the Lunskoye field for transport by pipeline to the Oil Export Terminal and the LNG plant. The OPF also



includes a 100 MW power generation unit that supplies power to LUN–A.

In January 2009, gas started flowing from the OPF to the LNG plant via the TransSakhalin pipeline system.

LNG plant

The LNG plant was inaugurated on 18 February 2009. LNG train 1 produced first LNG soon after that, and the first LNG cargo was offloaded later on. LNG train 2 started operations in late May. The Sakhalin-2 LNG plant is the sixth–largest LNG facility in the world in production capacity. Sakhalin Energy plans to optimise the LNG production systems, which may allow raising plant capacity by several percent.

IN JUNE 2009, THE LNG PLANT RECEIVED 'AN INNOVATIVE PROJECT' AWARD FROM THE JAPANESE MINISTRY OF LAND USE, INFRASTRUCTURE, TRANSPORT AND TOURISM.

TransSakhalin pipeline system

The onshore facilities of the project are linked by the TransSakhalin pipeline system, which includes over 300 km of offshore and over 1,600 km of onshore oil and gas pipelines, 104 block valve stations, and five pipeline maintenance depots. There are also two booster stations, one at the OPF and the other about halfway between the OPF and the Prigorodnoye complex in the south of the island.

The oil pipeline was commissioned in late 2008, and the gas pipeline in January 2009. In April, the operation and maintenance services of the TransSakhalin pipeline system were handed over to Sakhalin Energy's contractor, GazpromTransgazTomsk (GTT). GTT specialists were directly involved in testing and commissioning the pipelines. Engaging GTT in these two tasks allows Sakhalin Energy to tap the wealth of experience of its major shareholder, Gazprom. GTT will also provide maintenance services to Booster Station 2, which will be commissioned in 2010.

Restoring the onshore pipeline right of way (ROW)

Construction of the onshore pipeline involved a range of activities to restore the pipeline ROW, control erosion and stabilise river banks. By 2009, these activities were almost fully completed within the pipeline ROW.

High precipitation in the summer of 2009 caused minor landslips and washouts in some parts of the ROW. The heavy rainfall also caused some damage to river banks of the rivers in the Makarov district. An action plan was put in place to repair the damage from the heavy rains. By year end, all high priority repairs of the ROW were completed. Late in the year, winter works on repairs of the river banks in the Makarov district began.

A complete survey of the ROW was also carried out at that time to gauge the success of biological reinstatement of the ROW, which included recultivating the grass. The survey revealed some areas requiring recultivation, and a plan was enacted to finish the work in 2010.

Well drilling programme

Drilling continued in 2009 from PA–B and LUN–A with 'zero discharge', meaning all drilling waste was injected in special cuttings re–injection wells which were completed first. No wells were drilled from the Molikpaq (PA–A) platform in 2009.

As of year end, eight wells were producing in the Piltun area: six producing wells, one dedicated cuttings reinjection well, and one water injection smart well.

As of year end, six wells of the LUN–A platform were in operation, five wells for producing gas and one well for reinjecting cuttings.

A SMART WELL IS DRILLED IN THE SHAPE OF A FISH HOOK. SMART WELLS SUBSTANTIALLY REDUCE FIELD DEVELOPMENT COSTS AND INCREASE OIL PRODUCTION. THANKS TO THE UNPARALLELED SKILLS OF THE DRILLING CREW AND IMPECCABLE COORDINATION, THE DRILLING TIME OF THE SMART WELL FELL FROM A PLANNED 77 DAYS TO A RECORD 41 DAYS.

Implementing plans to produce and export hydrocarbons

Crude oil

Once the PA–B offshore oil platform went into operation and the LUN–A platform started gas condensate production, crude oil exports increased. Oil produced from the Molikpaq and the PA–B is blended with gas condensate from the Lunskoye field. Gas condensate makes up 25% to 30% of the crude oil blend. Due to its low sulfur content and high amount of light and medium–light hydrocarbon fractions, this blend of crude is used to produce petrol, kerosene, diesel fuel, and source materials for the petrochemicals industry. The blend also has a low flow threshold (below –60°C) and requires no heating during transport via pipeline. The blend derives its name from 'Vityaz Crude', which has been in the market for the last decade. The new crude is called Vityaz Blend.

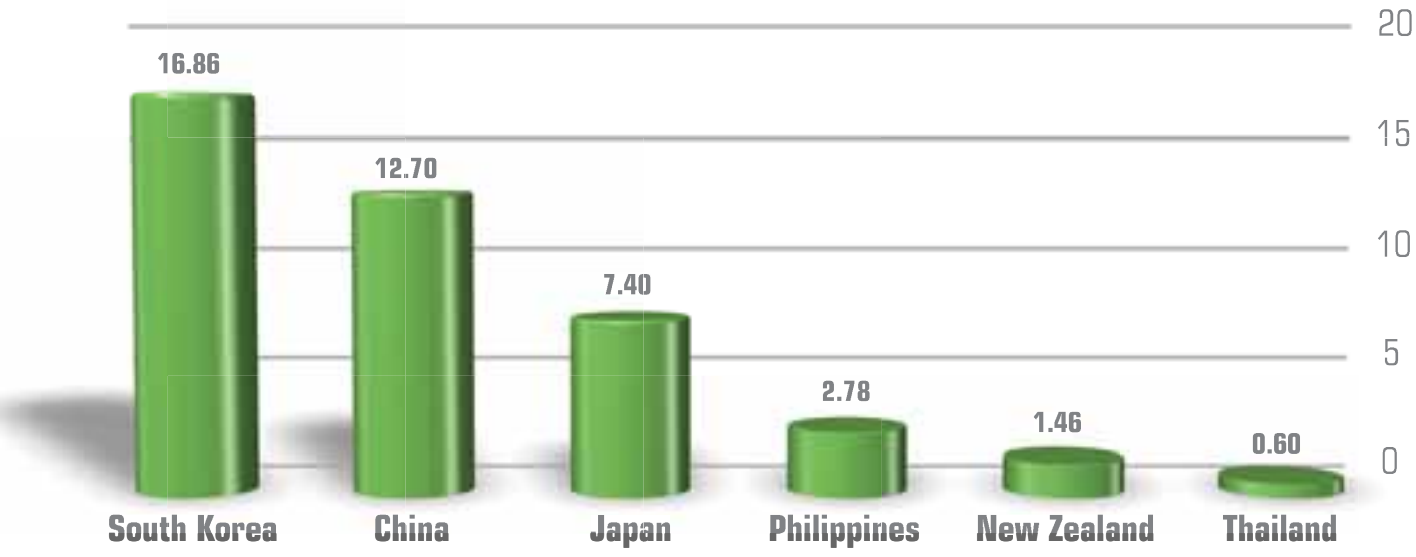
In 2009, the Company produced and offloaded over 5.5 million tonnes of oil and condensate, almost four times the oil export volume the previous year. The Company exceeded its 2009 targets for oil production and exports by 11%.

Buyers of Vityaz include power companies and refineries in Japan, South Korea, China, the Philippines, Thailand and New Zealand.

To transport the oil, Sakhalin Energy secured the tankers 'Governor Farkhutdinov' and 'Sakhalin Island' under long–term charter contracts with Primorsk Shipping Corporation. In October 2009, the Company signed a long–term charter contract with Primorsk Shipping Corporation for another tanker 'Zaliv Aniva'. These three Aframax class tankers, each with a gross deadweight over 100,000 tonnes are rated Ice 2 (ICE–1C as per international classification). They are double hulled and equipped with a bow loading facility to load hydrocarbons from the Tanker Loading Unit.

IN 2009, SAKHALIN ENERGY SURPASSED ITS PLANNED ESTIMATES FOR EXPORTS OF CRUDE OIL BY 11% AND LNG BY 47%.

2009 Vityaz Blend sales by country (mn barrels)



LNG

In March 2009, the first LNG cargo was offloaded from the LNG plant for Japanese buyers Tokyo Gas and Tokyo Electric. The startup of the second process trains of the LUN–A platform, the OPF, and the LNG plant allowed the Company to gradually ramp up LNG production to 5.3 million tonnes of LNG by the end of 2009, a 47% increase over plan.

Such a successful performance while in the midst of commissioning and start up of a production facility is well above international standards. This impressive feat was achieved mostly due to the detailed and highly efficient coordination of the commissioning effort. The end result has been the reliable operational readiness of all equipment, including the process facilities of the offshore platforms, the OPF and the LNG plant. In addition, the timely commissioning of gas wells, a high drilling rate, and a better–than–expected performance of the reservoir contributed to the success of the effort.

Almost all the annual output of LNG (98% of the LNG produced by both process trains) was contracted for the next 20–25 years. A total of 13 LNG sales contracts were signed, with 10 Japanese companies and the rest with South Korean state–owned company Kogas, Shell Eastern Trading, and Gazprom Global LNG. Thanks to these last two contracts, buyers of Russian LNG last year included India, China, Taiwan, and even Kuwait.

When the LNG plant reaches its design capacity, Sakhalin Energy will be producing some 5% of the world's LNG output.

Sakhalin-2 LNG is transported to customers by LNG tankers chartered by the Company under long–term charter contracts or by the ships provided by the buyers. Whenever additional cargoes are needed to transport LNG to buyers, the Company charters tankers in the spot market. Three 'grand' class LNG tankers were custom–built in Japan to transport Sakhalin LNG: 'Grand Elena', 'Grand Aniva', and 'Grand Mereya'. The first two tankers belong to a consortium of Russia's largest shipping company, Sovkomflot, and Japan's Nippon Yusen Kabushiki Kaisha. The owner of the third LNG tanker is a Russian–

EACH 'GRAND' CLASS LNG TANKER HAS FOUR SPHERICAL TANKS CAPABLE OF HOLDING 145,000 M³ OF LNG. THE TANKERS CAN BREAK ICE UP TO 40 CM THICK. THERE ARE ONLY 10 LNG TANKERS OF THIS KIND IN THE WORLD.

2009 Sakhalin LNG sales by country (thousand tonnes)

Japanese consortium set up by Primorsk Shipping Corporation, Mitsui OSK Lines and K Line.

Sakhalin Energy sets the most stringent requirements for vessels calling at Prigorodnoye Port to take oil and LNG on board. All oil and LNG tankers must be equipped with special ice detection radar. They must also have additional chain stoppers to secure reliable mooring during cargo–handling operations. These mandatory Company requirements greatly reduce environmental risk and in some aspects are stricter than the recommendations of the International Organisation of Offshore Terminal Owners for loading safety.

To prevent alien species from dissemination with ballast waters from calling ships, the Company developed a procedure for ballast water discharge from LNG and oil tankers in Aniva Bay. Among the measures in the procedure, all calling ships are required to change ballast water offshore, also required by the International Maritime Organisation (IMO). The Company closely controls and monitors compliance with this mandatory requirement. For this task, the Company uses an integrated monitoring system, widely considered to be the most innovative in Russia and the world.

New phase of project financing

In October 2009, Sakhalin Energy and a consortium of international commercial banks signed an agreement for an additional $1.4 billion in Sakhalin-2 Project financing. The loan was insured by Nippon Export and Investment Insurance (NEXI), an export credit agency owned by the Japanese government.

The funds are to finance completion of the full scope of the Sakhalin-2 Phase 2 project, including the drilling programme, enabling the project to reach full production capacity.

THE $6.7 BILLION FINANCING SECURED FOR PHASE 2 IS THE HIGHEST EVER IN RUSSIAN PROJECT FINANCING.

The Project financing for Sakhalin-2 Phase 2 project including this loan now totals $6.7 billion.

Project financing is often used by the oil and gas industry to develop major infrastructure assets. Debt is repaid from the cash flow generated by the asset financed. Securing additional Project financing despite difficult financial market conditions shows the confidence a wide range of business interests and the international financial community have in Sakhalin Energy, a confidence grounded in the viability of the project and its economic and financial strengths.

STAKEHOLDER ENGAGEMENT

Stakeholder engagement strategy and principles

Sakhalin Energy considers regular and constructive engagement with the public and key stakeholders, together with broad and transparent disclosure, as important elements of its successful operation and implementation of the Sakhalin-2 Project.

To this end, since the launch of the Project in 1994, the Company has engaged with the following stakeholders:

- National and municipal authorities
- Residents of communities directly affected by Project operations and other Sakhalin communities
- Stakeholders in Japan, especially on Hokkaido Island
- Public organisations and other non–government organisations (NGOs) locally, regionally, nationally and internationally
- Mass media locally, regionally, nationally and internationally and other stakeholders.

The General Business Principles of Sakhalin Energy call for transparency and open stakeholder engagement. The Company follows these principles in achieving its goals and its engagement approaches:

- Engagement shall be constructive, purposeful and open, as inclusive as possible and practicable, and shall incorporate as diverse a range of views and interests as possible
- Engagement shall be aimed at building solid, positive relationships with the community and other stakeholders, to provide effective mechanisms for the exchange of views about previously identified issues and the ways in which Sakhalin Energy manages them, and to create conditions so that emerging issues of concern are brought to the Company's attention and addressed in a timely manner
- Engagement shall be documented and the relevant summary reports shall be published, where possible, with the exception of issues relating to personal information and the privacy of individuals.

Sakhalin Energy complies with the requirements of Russian legislation concerning public consultations and strives to follow best international practices for information campaigns and public consultations. The Company is developing and constantly improving tools for effective stakeholder engagement and communication. The Company's information campaign and public consultation strategy have been evolving for more than a decade on the basis of engagement with Sakhalin Island residents and other stakeholders and have been shaped by taking resident's opinions into account.

The main document of the Company regulating stakeholder engagement and information disclosure is the Public Consultation and Disclosure Plan, which was developed according to Guidance Note F: Guidance for the Public Consultation and Disclosure Plan of the International Finance Corporation (IFC). It is updated every year and is available on the Company's public website. The plan details the process of identifying and analysing stakeholders, and describes methods of engagement. The Company publishes an annual report on stakeholder engagement on its public website.

Additionally, in 2009 the Company prepared and released 50 Energy TV programmes, broadcast by local Sakhalin television channels, held four media briefings, and arranged eight media tours for representatives of national and Sakhalin–based mass media.

Stakeholder engagement in 2009

In 2009, the Company continued its public consultations and stakeholder engagement on a variety of issues. Core activities included:

- As in previous years, a series of regular public community meetings were held to update communities on the latest developments in the Company's performance and progress on the Sakhalin-2 Project; 17 public meetings were held in different parts of the island, attended by some 300 representatives of Sakhalin communities
- Company engagement with representatives of Sakhalin indigenous minorities, as part of the Sakhalin Indigenous Minorities Development Plan (see Section *Sakhalin indigenous minorities*)
- An information campaign continued, including publishing information in local mass media, mailing notices, and circulating information materials. These messages were aimed at raising public awareness about safety issues at the Company's facilities, the measures necessary for preventing emergencies, and emergency response measures
- Information centres were opened across the entire island on the premises of local libraries (see Section *Company information centres*)
- Stakeholders were informed throughout the year via the Company's public website, with access to more than 2,500 documents, including press releases, articles, and reports, the monthly corporate newspaper Vesti, information centres, disclosure reports, and materials circulated in communities via radio, print, and television.

Community liaison officers

The Company employs a unique system of engagement with affected communities – a network of community liaison officers. In 2002, following social impact assessment of the Sakhalin-2 Project on the island community and taking into account best international practices, the Company proposed setting up this network to establish and maintain effective engagement with local authorities and communities, and to identify and address any Project related concerns in a timely and effective manner. Key activities of these officers include:

In 2009, the Company decided to publish its first non–financial report on sustainable development, prepared according to the guidelines of the Global Reporting Initiative (GRI) and the AA1000 Stakeholder Engagement Standard.

As part of this process, in November 2009, the Company held a first round of consultations with stakeholders to learn their major interest and expectations, in order to include them in the 2009 report.

Representatives of local and regional public organisations attended these consultations, including those with an environmental and social focus, the Sakhalin indigenous minorities, executive and legislative authorities of the Sakhalin Oblast, and social institutions.

In addition to these consultations, during a meeting of the Western Gray Whale Advisory Panel in December 2009, Sakhalin Energy met with representatives of international environmental organisations in Geneva, Switzerland, as part of its preparation of the Sustainable Development Report.

In April 2010, the Company held the second round of consultations with stakeholders, to present the Company's answers to comments and proposals voiced during the first round. Answers and the preliminary commitments of the Company were mailed to all participants in advance.

The list of participants consultation results are published in Appendices 2 and 3.

THE COMPANY'S COMMUNITY LIAISON SYSTEM RECEIVED A HIGH RATING AFTER AN INSPECTION BY REPRESENTATIVES OF AEA. SINCE 2001, THIS AGENCY HAS BEEN AN INDEPENDENT CONSULTANT TO THE LENDERS OF THE SAKHALIN-2 PROJECT. EXPERTS NOTED THE SPECIAL ROLE OF THE COMMUNITY LIAISON OFFICERS IN ESTABLISHING AND MAINTAINING EFFECTIVE COLLABORATION BETWEEN THE COMPANY AND THE LOCAL POPULATION. COMMUNITY LIAISON OFFICERS HAVE ALSO RECEIVED LETTERS OF APPRECIATION FROM THE ADMINISTRATIONS OF MUNICIPALITIES IN THE SAKHALIN OBLAST AND FROM NGOS.

- Open hours for community residents
- Regular meetings with government and municipal authorities and other special interest groups
- Coordination of the district information centres
- Annual public community meetings

Community Liaison Officers are also responsible for engaging with community within the framework of the grievance procedure. Effective and prompt resolution of community grievances is critical for building trust between a community and an industrial project.

The organisation of community liaison officers consists of a coordinator and four officers. Each officer oversees one discretionary zone of Sakhalin Island. A district centre in each zone has opened an office where the community liaison officer is based. Details of the activities of these officers are described in the Company's PCDP and Public Consultation and Disclosure Reports available on the Company's public website.

A project to develop business approaches to human rights has been ongoing since 2005, undertaken by John Ruggie, Special Representative of the UN Secretary General for Business and Human Rights. In 2008, the UN Council on Human Rights and the largest international business associations approved practical principles and recommendations for the business community. These principles are developed by Ruggie under his UN mandate, and formulate new standards for organising the complaints review process during business operations.

Tests of those principles are taking place from 2009 to 2011. The results will be used to develop recommendations for the global business community.

Sakhalin Energy was selected in 2009 as one of five international companies to test these principles and recommendations. The Company is honoured to represent Russian business and the international oil and gas industry in this process. International experts involved in the project have said 'the procedure for handling complaints in place at Sakhalin Energy is one of the most advanced in the industry'.

Company information centres

In 2009, the Company completed setting up the network of 20 information centres, a core element of the Company's effective engagement with the public. The network offices are based in district and rural libraries in communities along the route of the TransSakhalin pipeline system and near other Project facilities.

THE JOINT PROJECT TO SET UP INFORMATION CENTRES IN LIBRARIES HAS EXTENDED THE COMPANY'S ENGAGEMENT WITH THE GENERAL PUBLIC. NOW THE LATEST INFORMATION ABOUT THE COMPANY AND THE SAKHALIN-2 PROJECT IS AVAILABLE IN SMALL COMMUNITIES, NOT ONLY IN THE REGIONAL CENTRE.

The information centres are equipped with information boards, computer and office equipment, and have Internet access, which accomplishes the Company's objectives and enhances the capacity of the libraries.

Visitors to the centres are helped by library employees, who have taken a Company-organised training workshop.

A total of 1,500 queries from the local community were registered at the information centres by the end of 2009. The most frequently asked questions were about employment opportunities, requests for additional information about the Sakhalin-2 Project, and opportunities to participate in the Company's social programmes and public initiatives.

Community grievance procedure

As a core element of safeguarding human rights and more effectively engaging communities, in 2003 Sakhalin Energy developed a procedure to address community grievances related to the Sakhalin-2 Project. The main benefits of the community grievance procedure lie in its simplicity and effectiveness. A complaint can be filed in one of seven ways, including anonymously.

Informing residents about the community grievance procedure is essential to public engagement. Sakhalin Energy regularly stages an extensive public information campaign on who can file complaints, and how. The Company also developed information materials, including a leaflet on the grievance procedure that contains recommended steps to file a complaint about the Sakhalin-2 Project.

Detailed information on addressing grievances is available in the annual report on the Company's Public Consultation and Disclosure on the Company's public website.

Engaging Sakhalin Indigenous Peoples

The Company regularly engages Sakhalin indigenous minorities, mostly those living in the north–eastern part of Sakhalin Island. Consultation activities and contributions to development of indigenous minority communities are detailed in the Sakhalin Indigenous Minorities Development Plan, developed in 2005 and 2006 according to the World Bank Operational Directive 4.20. An essential component in its preparation was the involvement of representatives from indigenous minorities.

The only indigenous minority community that could have been adversely affected from Project construction was the reindeer herders living in Val in the Nogliki district. To lessen the impact of construction on this group and to identify the most acceptable methods of engagement, intensive consultations were held with reindeer herders during the construction phase.

The Company held consultations in 2009 with indigenous minorities on implementing the Development Plan, how to make information available,

the Plan's effectiveness, listening to their concerns and ideas for potential projects, and reminding the population about the grievance procedure and how to use it.

The Development Plan is described in more detail in the Section *Sakhalin indigenous minorities*.

Interaction with NGOs

Sakhalin Energy collaborates with representatives of local, national, and Far Eastern NGOs, and maintains regular contact with NGOs in Japan and internationally.

Public organisations and other NGOs are regularly updated on the progress of the Project, and discuss all issues of interest with Company representatives.

Consultations take place in different formats, including personal and group meetings, and by written correspondence. The most important meetings held in 2009 with key NGOs from the island, region, federation, and internationally were the following:

- The Western Gray Whale Advisory Panel, as part of efforts to find the best solution for minimising any adverse impact on Gray Whales. During meetings with the Panel, Company representatives met with representatives of the WWF, the Pacific Environment and Resources Centre, the International Foundation for Animal Welfare, and other international NGOs (see Section *Western Gray Whales*)
- The Wild Salmon Centre and the Sakhalin Salmon Initiative, as part of a programme of the same name (see Section *Social investment and sustainable development programmes supported by Sakhalin Energy*)
- Stakeholders in Japan: fishermen associations on Hokkaido Island, Hokkaido Island authorities, and other local stakeholders on oil spill response, preserving Steller's Sea Eagles, and biodiversity.

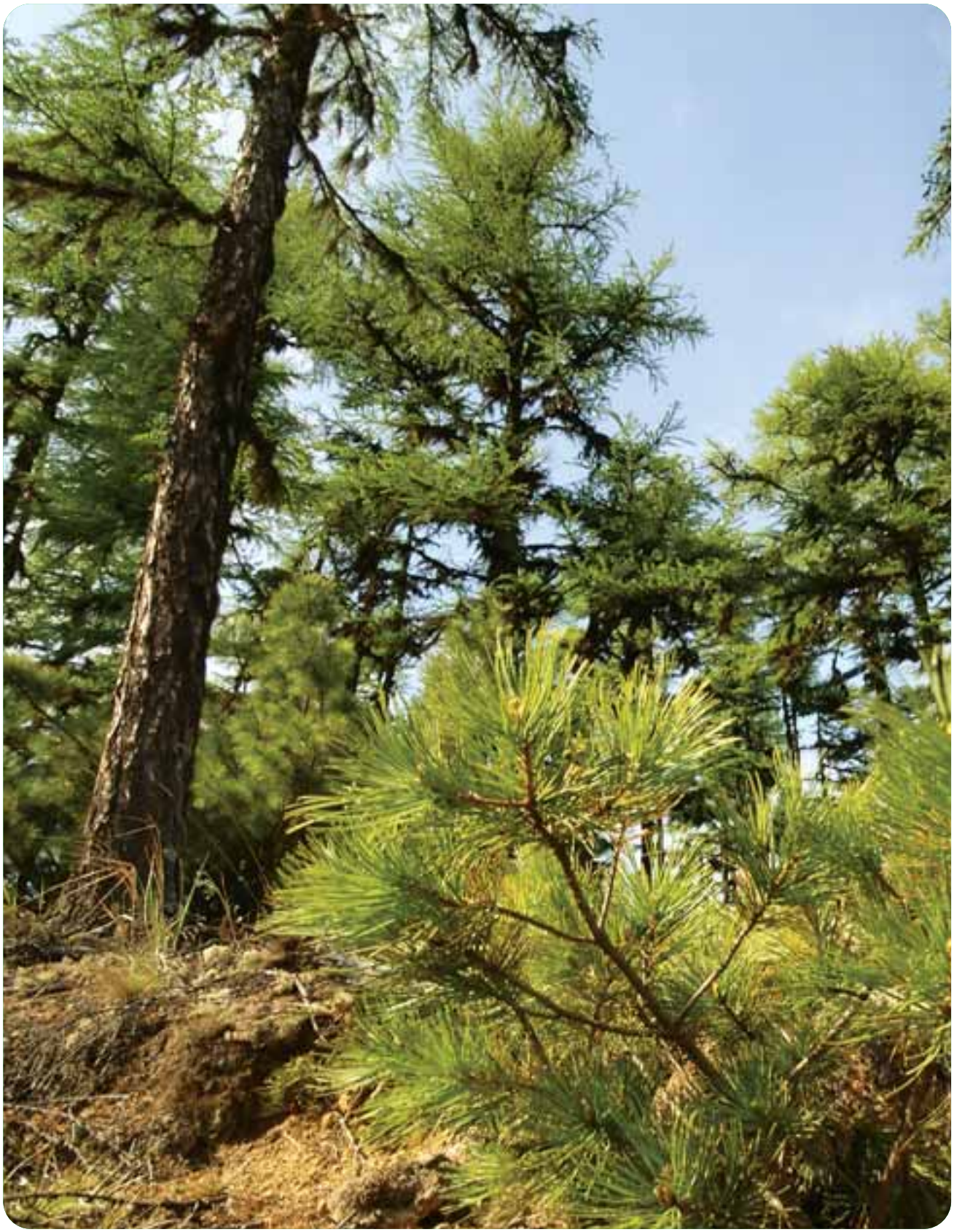
Engaging Japanese stakeholders

Japanese stakeholder engagement is important to the Company, due to the proximity of Sakhalin Island to Hokkaido Island in Japan. Experts, business, NGOs, fishermen and other stakeholders in Japan are concerned with the environmental impact of the Sakhalin-2 Project, notably oil spill response, preserving biodiversity, and protecting and preserving the Steller's Sea Eagle.

Sakhalin Energy held a number of public consultations and meetings throughout 2009 in Japan:

- February and November: the Company met with Japanese fishing industry organisations and stakeholders along the shore of the Sea of Okhotsk; these meetings were attended by the Japanese Bank for International Cooperation (JBIC), one of the leading Project lenders
- June, August, and September: At public environmental forums, Company management made presentations on the status of Project implementation and environmental issues
- September: The Company met with Japanese experts on biodiversity issues.

MANAGING NON–FINANCIAL RISKS IN HEALTH, SAFETY, ENVIRONMENT AND SOCIAL ISSUES



General principles for managing non–financial issues

Health, safety, the environment (HSE), and social issues are an integral part of Company business activities, in line with its commitment to do no harm to people, to protect the environment, and to contribute to sustainable development, including bringing benefits to the inhabitants of Sakhalin Island and to other key stakeholders. HSE approaches and social performance (SP) management are embedded in the Company's values and general business principles (see Section *Company mission, core values and business principles*).

The steps the Company has taken to implement these principles in HSE and social issues are briefly outlined below in the sections on management.

Health, Safety, Environment and Social Action Plan (HSESAP) was developed for Phase 2 of the Sakhalin-2 Project, in keeping with the international and Russian Federation standards and international best practices. The Plan consolidates commitments from the Environmental, Health and Social Impact Assessments, including supporting documentation and addenda. It also details the measures agreed between the Company and the Phase 2 senior lenders to eliminate, mitigate, or manage any adverse HSE and social impacts to acceptable levels that have been identified. The Plan is available to the public on the Company's public website.

Structure and content of managing non–financial risk

Sakhalin Energy takes a systematic approach to managing its HSE and social performance, to ensure compliance with Russian federal law, adopt international standards, and continuously improve performance.

The Company's integrated HSE and Social Performance Management System lists the controls Sakhalin Energy uses to manage HSE and social issues and risks. Sakhalin Energy sees managing these risks as critical to business success. The Company will continue to maintain, develop, and improve the Management System consistent with relevant international best practice.

The Management System is based on the Plan–Do–Check–Act methodology of the management system standards ISO 14001 and OHSAS 18001:

- Establish objectives and processes to deliver results consistent with the Company's HSE and Social Performance policy
- Implement the processes
- Monitor and measure processes against policy, objectives, legal and other requirements, and report the results
- Take actions to continually improve HSE and social performance.

Sakhalin Energy conducted three impact assessments on the environment, social issues and health (ESHIA), to determine potential risks and impacts from the Sakhalin-2 Project. Assessments were conducted in accordance with Russian regulatory requirements, best industry practice, and international standards. The Company involved local resources and international experts and organisations. In keeping with international standards on impact assessments, public consultations were held to discuss potential impacts and measures. In a short time period, from September 2001 to November 2002, over 5,000 Sakhalin residents were interviewed in 52 towns and villages. The first ESHIA was completed and published in 2003. In 2005, the assessment was updated, and the reports posted at the Company's public website.

Hazards and risk management

The Company manages HSE risk and social issues to reduce major risks to 'as low as reasonably practicable' (ALARP), and to continuously improve. ALARP is the point where the cost in time or money of implementing further risk reduction measures becomes grossly disproportionate to the benefit obtained, or the reduced risk.

Detailed processes identify hazards and aspects of HSE and social issues, assess risks and impacts, and determine appropriate design and management controls in accordance with:

- Russian Federation requirements
- Project lender requirements
- Adopted international standards and best industry practices.

Impact assessment

As a key component to managing non–financial risks, the Company conducts impact assessments prior to any major new project or before making major modifications to existing facilities. Stakeholder consultations are integral to any impact assessment the Company does, and impact assessment documents are made available for public consultation.

Impact management measures are designed to mitigate negative impact and enhance the benefits from Project activities. Sakhalin Energy strives to eliminate or mitigate any impacts to the lowest possible level, or to compensate for them. The following measures were developed to apply to potentially negative impacts that have been identified:

- Eliminate impact
- Provide compensation
- Reduce likelihood of occurrence
- Expand opportunities
- Reduce impact
- Prevent impact.

IMPACT ASSESSMENT IS THE PROCESS OF FORECASTING AND MANAGING IMPACTS THROUGH PROJECT DESIGN, IMPLEMENTING IMPACT MITIGATION MEASURES, AND EXPANDING FAVOURABLE OPPORTUNITIES. IMPACT ASSESSMENT DEALS WITH ENVIRONMENTAL AND SOCIAL EFFECTS, AND THE IMPACT ON THE HEALTH OF STAFF AND THE COMMUNITY FROM CURRENT OR PLANNED COMPANY BUSINESS.

Previous environmental and social impact assessments including addenda and special studies have contributed to Company standards, while current Company activities are based on management plans and programmes.

Risk assessment matrix

Another important risk management tool the Company uses is the risk assessment matrix to classify actual and potential consequences, determine significance, and guide appropriate risk management.

The risk assessment process falls under the Company's hazards and effects management methodology. The Company has modified the risk assessment matrix since the Company's inception, to classify incidents and to audit. To secure funding, the Company and the Phase 2 senior lenders have agreed on the methods based on this matrix.

Consequences of a breach or a risk fall into five categories: social impact, damage to health, assets, the environment, or reputation, by selecting the appropriate risk description in the respective matrix column.

A detailed description of the matrix and methodology are provided in the Plan.

Innovative Approach and Risk Assessment Practice

The Company's methodology of risk assessment is probably the most advanced available. Risks are determined and analysed consistently, structurally, and systematically, not only by category of damage inflicted to health, assets, environment and reputation, which is a common practice, but also by social impact such as on the population or on community life.

Objectives and annual improvement plans

Every year the Chief Executive Officer of Sakhalin Energy approves the Company's strategic objectives for the next five years, the specific parameters and results of Company activities, as well as HSES action plans.

The corporate HSE, corporate social performance, and supplementary plans provide detailed actions, timelines, and resources by subdivision and level of organisation.

The effectiveness of results and plans are gauged and controlled with regular reports and assessments.

Audits and inspections

Audits and inspections are an integral part of the management system, to verify that internal control systems required to manage HSE and social risks, and comply with Sakhalin Energy policy, standards, procedures and Company processes are available and effective. The results of audits and inspections are subject to control to reduce risks and improve processes, to assist in providing external reports, to inform management on the audits, and to submit compliance reports to stakeholders and the Business Assurance Committee.

The Business Assurance Committee approves and adopts the audit programme, following an approach based on risk assessment. The Committee then regularly analyses implementation of the Plan and its basic results, weak points of the management system, non–compliance items, and the themes and status of the open results. The auditee is responsible for the follow up, elimination of identified non–compliances, and respective actions. Audit plans referto the specific facility or contract part of the annual audit plans for individual asset teams or contractors.

Corrective and preventive actions

The importance of any non–compliance or weaknesses revealed in an audit is determined with a risk assessment matrix. If the audit indentifies issues requiring remedial actions, a corrective plan is developed.

The Company takes corrective and preventive actions to address incidents, including grievances, draws up non–conformance reports and lessons learned, records findings of assurance activities, and assumes other commitments.

Actions taken to eliminate the causes of actual and potential non–compliance suit the magnitude of the problem and are commensurate with the HSE and social risks encountered, and subject to appropriate risk assessment.

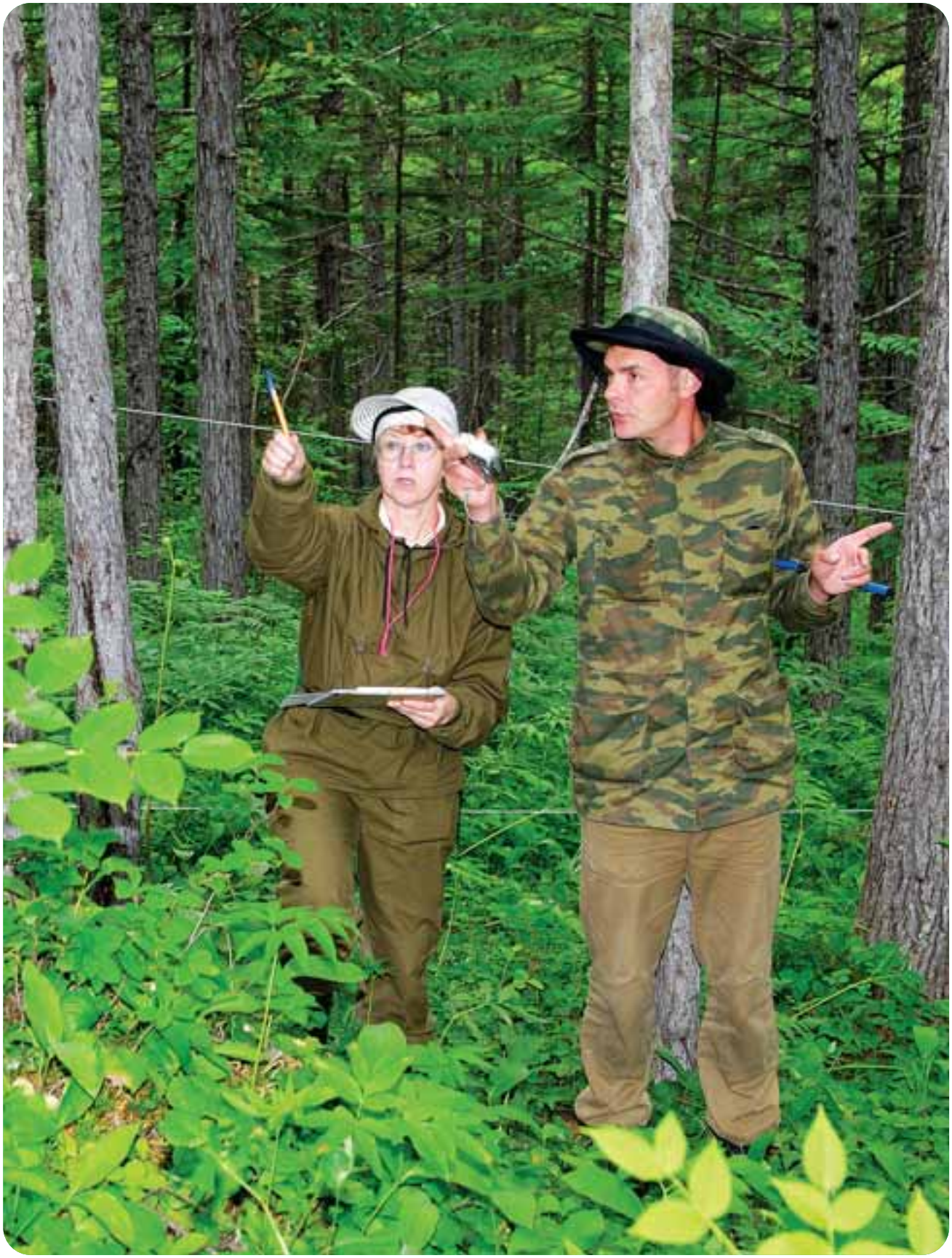
Management reviews

Regular reviews are conducted of regulatory compliance and performance monitoring and reporting, incident and non–conformance reporting and learning, the status of corrective and preventive actions, and outcomes of assurance activities.

Sakhalin Energy conducts an annual management review to ensure the continued suitability, adequacy, and effectiveness of the management system, and takes action to improve. The reviews include:

- Evaluating trends and lessons learned from performance, incident investigations, audits; compliance with legal requirements and changes in legal and other requirements; status of corrective and preventive actions, results of consultations
- Completing a self assessment of the Management System
- Assessing opportunities to improve and changes needed in the Management System.

ENVIRONMENTAL PROTECTION, ECOLOGICAL AND INDUSTRIAL SAFETY



Policy

Sakhalin Energy's commitment to protect the environment is reflected in its health, safety and environment policy.

We care…

Sakhalin Energy Investment Company Ltd. Commitment to Health, Safety and Environment

We are all committed to:

- Pursue the goal of no harm to people
- Protect the environment
- Use material and energy efficiently to provide our products and services
- Develop energy resources, products and services consistent with these aims
- Publicly report on our performance
- Play a leading role in promoting best practice in our industry
- Manage HSE matters like any other critical business activity
- Promote a culture in which all Sakhalin Energy employees share this commitment.

In this way we aim to have an HSE performance we can be proud of, to earn the confidence of customers, shareholders and society at large, to be a good neighbour and to contribute to sustainable development.

Sakhalin Energy Investment Company Ltd. Health, Safety and Environment Policy

The Company:

- Has a systematic approach to HSE management designed to ensure compliance with the law and to achieve continuous performance improvement;
- Sets targets for improvement and measures, appraises and reports performance;
- Requires contractors to manage HSE in line with this policy;
- Will use its influence to promote this or an equivalent policy in company related activities which are not under its direct control;
- Includes HSE performance in the appraisal of all staff and rewards accordingly.

… all of us have a role to play.

Each of us has a right and duty to intervene with unsafe acts and conditions or when activities are not in compliance with this HSE Policy and Commitment.

Goals and performance

The Health, Safety and Environmental Management Committee of Sakhalin Energy, comprising the HSE General Manager and the Committee of Executive Directors and chaired by the CEO, oversees the Company's HSE management.

Our environmental management system is based on the HSE policy and standards of Sakhalin Energy and our Shareholders, the legal requirements of the Russian Federation, primarily our government–approved Environmental Monitoring Project and relevant permits and licenses, and commitments to lenders and other interested parties.

Sakhalin Energy is committed to continuously improving its environmental performance. To demonstrate this commitment, management prepares plans that set out expectations, milestones and targets for the year, and measurements of their performance. During 2009, each asset and project team developed plans consistent with and supportive of the corporate plan. Performance objectives were introduced to the workforce, including key contractors. The Health, Safety and Environment Management Committee met regularly during 2009 to review HSE priorities, action plans, milestones, incidents and investigations, evolving HSE issues, and the key environmental performance indicators.

Sakhalin Energy continuous efforts led to one of the most impressive results in the industry in oil spills prevention. Whilst in 1999-2009 the company produced almost 149,700,000 barrels (20,100,000 tonnes) of Vityaz oil, total oil spilled constituted slightly over four barrels (slightly over 0.5 tonne).

Notable achievements and activities in 2009 included the following:

- Project-wide **ISO14001:2004** certification was granted in early 2009, more than a year ahead of schedule. Regular internal and external audits were carried out to maintain focus and ensure improvement plans were implemented.
- Continued, extensive engagement with key stakeholders on protecting the critically endangered **Western Gray Whale** that feeds offshore northeast Sakhalin. Following a recommendation from the Western Gray Whale Advisory Panel convened under the IUCN, the Company decided to postpone its planned 4D seismic survey. Although fewer whales were sighted offshore Sakhalin in 2008, their numbersrebounded in 2009 to previous lrvels, and the Panel has now agreed the seismic survey can proceed in 2010.
- Sakhalin Energy's **Biodiversity Action Plan** (BAP) was well-received at the fourth meeting of the Sakhalin Biodiversity Group in September. The group expressed their support for the plan and its implementation. Members of the Group recommended using Sakhalin Energy's BAP as a basis for a regional BAP for Sakhalin Oblast.
- Planting approximately 140,000 trees during the **Djimdan River Restoration Project**, which aims to stabilise the tree population of previously denuded areas, to help rivers recover from increased sediment loads.

Industrial environmental monitoring

Sakhalin Energy maintains permits for air emissions, wastewater discharge, and waste disposal in accordance with Russian environmental legislation. The Company commissioned one of the largest integrated oil and gas projects in the world in 2009.

During the transition from construction to operations, monitoring results were considered in engineering and technical assessment of the Project facilities, and where necessary modification of existing equipment, or in some cases installation of new equipment, was carried out to reduce the amount of emissions and wastes. The Company makes appropriate payments to Russian authorities in accordance with the legislation, permits and licenses under which it operates.

Waste management

Waste management is done in accordance with Company policies, Russian Federation legislation and regulations, and approved programmes for the generation, use, decontamination, transport, and disposal of waste.

Managing water resources and effluents

The total volume of water drawn or received in 2009 from natural sources was 31,943 thousand m^3. The water was used to supply Company facilities. The total volume of discharged water was 26,119 thousand m^3.

Of the amount discharged to surface water bodies, such as the sea, rivers and creeks, 25,331 thousand m^3 (99.5 %) was related as standard clean water (not subject to treatment) and the rest was treated. Where necessary, the Company prepared an action plan to improve the effectiveness of wastewater treatment, including upgrades to the discharge system.

Table: Tonnes of waste per class* managed during 2009

Waste movement	Class 1	Class 2	Class 3	Class 4	Class 5	TOTAL
Waste at sites on 1 January 2009	0	0.297	11.954	515.700	0.350	528.301
Waste generated in 2009	0.915	18.200	462.233	22653.893	1465.646	24600.877
Use by Company for its production needs	0	0	201.618	0	0	201.618
Transferred to other parties for use	0	7.212	106.632	1683.431	491.674	2288.949
Transferred to other parties for decontamination	0.912	0.186	152.771	419.815	0	573.684
Transferred to other parties for final disposal at licensed landfills	0	0.028	0	2363.347	946.322	3309.697
Stored at Company assets	0	0	0	0	0	0
Disposed at Company assets	0	0	0	18703.000	0	18703.000
Waste at sites end 2009	0.003	11.071	13.166	0	28.000	52.240

** According to Russian Federal law, hazardous waste includes classes 1, 2, 3, and 4. Non-hazardous waste is class 5 only.*

Environmental monitoring results showed no adverse impact on water environment from Company's discharges.

Air emissions

The amount of air emissions from Company's stationary sources in 2009 was 33 thousand tonnes, including carbon monoxide – 23,71 thousand tonnes, nitrogen oxides – 5,93 thousand tonnes, sulfur dioxide – 0,10 thousand tonnes, solids – 2,34 thousand tonnes.

As per Sakhalin Statistical Office data, total amount of air emissions from stationary sources in Sakhalin Oblast in 2009 was 116 thousand tonnes, main components emitted being carbon monoxide, nitrogen oxide, sulphur dioxide, solids.

In 2009, Company's contribution to Sakhalin Oblast total emissions was 28.4 %. Total air emissions increased in 2009 in comparison with those in 2008 due to commissioning and start-up activities.

Biodiversity

The Company's Biodiversity Action Plan (BAP) sets out its approach to fulfill its commitments to manage biodiversity and ecological impacts from operations. The independent environmental consultant to the Project lenders described Sakhalin Energy's BAP as 'a clear, concise, comprehensive, and thoroughly researched document. It draws on the best available evidence from peer–reviewed scientific literature, coupled with knowledge and understanding of national and international policy and legislative frameworks, and presents a reasoned account of the relationships between Sakhalin Energy's activities and the biodiversity / ecosystems of Sakhalin and how any detrimental impacts might be assessed and mitigated'.

Sakhalin Energy is proud of this recognition of its achievements, and will continue to set industry standards on protecting and managing biodiversity.

The BAP describes the framework and rationale to support the monitoring programmes that Sakhalin Energy, its stakeholders, government authorities, and Project lenders believe are important, not only for environmental protection, but because it makes good business sense. Key criteria for prioritisation

Table: Aggregated 2009 water use data, thousand m^3

Water intake	31,943
Wastewater discharge	26,119
including	
discharge to surface water bodies	25,446
discharge to land, drainage fields	672

were the social and ecological value placed on species and habitats, and the protection afforded them by legislation. Other criteria include:

- Threatened species or ecosystems
- Areas of 'natural' or relatively intact habitat
- Habitats and areas supporting high species / habitat diversity
- Environments sensitive to potential impact
- Species and habitats where significant declines in populations and area have been documented and may be worsening
- Areas and habitats considered important for providing and maintaining ecological processes and ecosystem function.

Using these criteria, Sakhalin Energy's Biodiversity Action Plan identifies (in summary) the following biodiversity priorities:

For species:

- Relevant species protected under law
- Coastal and wetland birds of the Chaivo bar
- Certain breeding birds of the coniferous forest
- Certain breeding birds of river valley mixed woodland
- Salmonid fish populations of selected river systems.

For habitats:

- Certain forests
- Certain tracts of peatland and swamps
- Certain river catchments
- Shallow coastal lagoon systems and fringing wetlands
- Areas of Aniva Bay and the northeast Sakhalin shelf.

Details of monitoring programmes for these species and habitats carried out in2009 are presented in the following sections.

Terrestrial ecosystems

Flora and vegetation

The location of Sakhalin Island is extremely important for floral zonation. Scientists have divided the Island into two main areas: north–Sakhalin and south–Sakhalin. The northern flora belong to the Okhotsk–Kamchatka province of the Boreal floral region, and the southern to the Sakhalin–Hokkaido province of the East Asian floral region. The flora of Sakhalin are less numerous than the neighbouring Japanese island of Hokkaido or the mainland Russian territories of Khabarovsk or Primorye, and comprise approximately 1520 species, 1230 of which are indigenous. Nevertheless, Sakhalin Energy recognizes the importance of this scientific classification and works within these environmental conditions.

Our monitoring shows that in general, plant communities within the vicinity of the LNG plant have maintained their structure and composition. Comparing 2009 with 2008 data indicates that no habitats of protected plants were destroyed or severely affected. As a direct result of this research, several new locations of protected species were discovered, and currently nine species of Red Data Book seed plants and two species of Red Data Book lichens have been registered in the area surrounding the LNG plant.

The vegetation of Sakhalin Island has been significantly modified through previous human activity. Originally, the island was characterised by coniferous forests, where Yezo spruce, Sakhalin fir, and Cajander's larch were the dominant species, with Japanese dwarf pine and the Kurile bamboo found on the upper parts of the mountain range. Between the world wars, the southern region was severely clear–cut, leaving only small areas of old–growth fir forests on the Susunaiskiy Ridge between Dolinsk and Yuzhno–Sakhalinsk, with fragments remaining on the Krillion Peninsula in the southwest. Similarly, most of the northern half of the island has been clear–felled by the Russian timber industry. Although much of the island has been replanted, this has not kept pace with the rate of forest loss, and in many areas the establishment of new forest has been limited.

This fragmentation of areas of contiguous habitat is considered to be one of the main causes of biodiversity loss. Regarding the Sakhalin-2 Project, it was not possible for some sections of the onshore pipeline to avoid certain blocks of forest habitat, especially in the more mountainous areas to the west of the onshore processing facility and in the Makarov area. Following construction, the priority in relation has been to prevent or minimise further potential deterioration of intact blocks of habitat that may have been initially affected by the Project. Sakhalin Energy's Biodiversity Action Plan targets these areas to determine and assess the extent of Project–related disturbance and to establish appropriate mechanisms to mitigate observed impacts. A survey was conducted of old growth dark coniferous forests along the pipeline right–of–way in 2009, to delineate locations of this forest type within the Project footprint, and to create permanent plots for long–term monitoring and assessment. As a direct result of this work, mitigation measures have been employed, including closing access roads and reinstatement where these roads are no longer required.

Although reinstatement of land that was disturbed during Project construction has been very successful in some areas, it has been less successful in others. Seeding of grasses and other plants has not led to expected results at all sites. Addressing this will take several years, and consequently the Company has an active programme to complete biological reinstatement. In many cases re–seeding is needed to establish stable vegetation cover.

Soils and geomorphology

Impacts generally mitigated during typical construction projects include:

- Soil erosion and sediment release to land and water
- Soil mixing, compaction, and topsoil loss leading to reduced fertility and biodiversity loss
- Alteration of natural drainage.

In most instances, soils on Sakhalin tend to be boggy, fragile, and podzolised, although soil type varies across the Island according to vegetation, relief, and climate. Although some impact on soils during construction will persist into the operations phase of the Project, subsidence may continue to occur where soils used to backfill the pipeline trench often undergo natural settlement. The Company is monitoring the condition of soils around the major facilities during operations, to verify that controls designed to mitigate potential impacts, such as pollutant accumulation due to atmospheric deposition, maintenance, and other industrial activities are effective.

Operations monitoring of soils around the LNG plant started in 2008, while operations monitoring along the right–of–way and around the onshore processing facility started in 2009. It is too early in the natural cycle to draw conclusions on the temporal dynamics of soil composition and structure. Along the right–of–way, monitoring identified several areas where erosion, swamping, and sagging of poorly compacted soil, which slow the development of vegetation cover, were happening. Corrective actions have been designed and are being implemented. Monitoring will continue in 2010.

River systems are alive and complex , and many have important ecological value. In developing Phase 2 of the Project, Sakhalin Energy recognised the importance of potential impacts of pipeline construction and operation on the hydrology and morphology of rivers. If left unaddressed, such impacts could, over different timescales, damage river ecosystems. Increased sediment loads could smother plants and reduce their rates of photosynthesis, and in the future cause decrease in invertebrate and herbivorous fish populations. Fish stocks could be affected by changes in water quality and habitat loss. Sakhalin Energy has therefore taken wide mitigation measures, including using horizontal directional drilling (HDD) for all high–value fishery rivers during construction. The Company continues to monitor geomorphic and hydromorphic processes during operations to manage pipeline integrity and environmental disturbance.

Monitoring geomorphic processes during the operations phase of the Project began in 2009, part of a long–term programme to assess the integrity of onshore pipelines and the landscapes they pass through. Aerial observations of the Gornaya River crossing showed the 2009 summer floods had damaged left riverbank protection structures and scoured a

new channel, affecting the pipeline and right–of–way. This incident highlighted the importance of these surveys and of predicting hydromorphic events before they occur.

Hydromorphological monitoring at river crossings showed river channelling and erosion in certain places. This is a natural and expected process in hydrologically energetic locations; the environmental management objective is to keep such potential effects to a minimum, whilst recognizing the natural process of denudation and peneplanation. When comparing data from 2004–2006 and 2008–2009, considerable variations are noted for the Malaya, Tym, Pobedinka, Leonidovka, Nituy (northern anabranch), and Gornaya river crossings, as well as for steep slopes in the basins of the Lesnaya, Krasnaya, Rybnaya, and Kirpichnaya rivers. An extensive repair programme was designed and successfully executed, and monitoring of the Gornaya and other crossings will continue in 2010.

Terrestrial mammals

The mammal populations of Sakhalin Island are less diverse compared with the mainland of the Russian Far East. The population levels and distribution of many species have responded to human–induced pressures, so that highly adaptable species tend to dominate. Those with more restricted ecological requirements were either never present in the first place, or are significantly fewer, or have been completely lost from the island fauna a long time before Sakhalin Energy started operations.

Rodents and shrews are highly sensitive to disturbances and respond quickly to environmental changes. For this reason they are used as indicator species, so that the health of small mammal communities in total, and the potential impacts of industrial activities on them, can be indicated by the size and demographic characteristics of rodent and shrew populations.

In 2009, three species of rodent and five species of shrew were recorded in the area of the onshore processing facility. The northern red–backed vole was clearly dominant in the community, which is typical for rodent communities in undisturbed or slightly disturbed areas of northern Sakhalin. Although differences were noted in the morphological characteristics, none of these were significant abnormalities, and are likely to be due to the intra–population dynamics of separate species.

Three species of rodent and four species of shrew were recorded in the area around BS–2 in 2009, with most species represented by only a few individuals. Three species of rodent and three species of shrew were observed in the area around the LNG plant.

Birds

The wide variety of terrestrial habitats on Sakhalin Island, including wetland and coastal habitats, support a range of distinct bird assemblages. The Red Data Book (RDB) of endangered species for Sakhalin Oblast lists about 105 bird species. The largest part, approximately 70%, of Sakhalin's rare bird fauna are species of wetland birds, such as lake swamp and littoral marine. This reflects the large presence of these habitats across the island and especially the dynamic and productive coastal ecosystem in the north–east part of

the Island. Terrestrial species, representative of the mountainous and forested interior of the Island and human–influenced habitats, such as commercial forestry or agricultural land, make up the remaining 30% of the rare bird fauna.

The Company monitored species of rare and protected birds in 2009 within the zone of influence of Sakhalin Energy's facilities as required by the Environmental Monitoring Project (officially referred to as the System of Industrial Ecological Control and Local Monitoring). A total of 26 protected bird species were recorded in the 2 km zone of influence along the pipeline right–of–way. Nesting species numbered 16, namely Japanese snipe, Japanese robin, cinnamon russet sparrow, mandarin duck, white–tailed and Steller's Sea Eagles, European hobby, Siberian spruce grouse, black–billed capercaillie, Sakhalin dunlin, Aleutian tern, long–toed stint, great gray owl, Eurasian pygmy–owl, boreal owl, and northern hawk owl. Also found in adjacent territory were nesting sites of Japanese white–eye, osprey, reed bunting, long–billed murrelet, and Japanese waxwing, species that could also nest in the zone of influence.

The status of populations of most protected species in 2009 did not deteriorate along the right–of–way compared with previous years. A gradual recovery in the number of species that depend on meadow habitats was noted, probably due to reinstatement of the right–of–way.

At the Chayvo bar along the right–of–way, 10 protected species were observed, dominated by Sakhalin dunlin and Aleutian tern. The locations of nesting sites and the number of colonies of dunlin had not changed compared with 2008. However, nesting sites of Aleutian tern along the pipeline route were more variable compared with previous years.

In the area of the LNG plant, 16 protected species were observed, five of them, the white–tailed eagle, besra sparrow–hawk, Japanese snipe, Japanese robin, and reed bunting were nesting within the zone of influence. In 2009, the population of Japanese snipe increased compared with the previous year, probably due to their use of recultivated sites. Six nesting sites of Japanese snipe were found in the floodplain of Goluboi creek, within the territory of the LNG plant.

In the area of the onshore processing facility, 26 protected bird species were observed, 15 nesting at a distance of up to 6 km from the facility. The immediate vicinity of the processing facility is inhabited by Siberian spruce grouse, and their numbers have not changed compared with previous years. Construction of access roads in forested areas and the large number of voles probably contributed to an increase in the numbers of northern hawk owl, boreal owl, and Eurasian pygmy–owl.

Sakhalin Island's geographical position makes it a potential migratory bridge for birds travelling between Japan and the Far East

mainland. A large number of the Sakhalin Oblast RDB are also listed in the Japan–Russia Migratory Bird Treaty (1973). Notable among these is the Steller's Sea Eagle, one of the largest birds in the world with a wingspan of up to 2.4 m. In Japan, it is a designated 'natural monument' species and is protected according to the 'Law for the Conservation of Species'.

The Steller's Sea Eagle breeds along the Okhotsk Sea in Far East Russia, and about 2,000 migrate to Japan every winter, mainly to the eastern part of Hokkaido Island in Japan. As a result, Japan is very interested in conserving the habitat and population of the sea eagle on Sakhalin.

Sakhalin Energy launched its Sea Eagle Research Programme in 2004 to ensure preservation of the Steller's Sea Eagle (SSE) and the white–tailed sea eagle, which is listed in the Red Books of Sakhalin and the Russian Federation. Surveys focus on north–eastern Sakhalin, including lagoon areas and the lower parts of rivers crossed by the pipeline.

In April 2009, the Company completed the first survey, during the early nesting period, to assess the condition of breeding areas and to identify active nests. These 'early–season' data were used to inform the annual update of our SSE impact mitigation plan. A second, more extensive survey was carried out in July and August at the end of the nesting period, to assess population and breeding characteristics.

To date, 274 nesting areas, including 619 nests of Steller's Sea Eagle, and nine areas containing18 nests of the white tailed sea eagle were recorded. About 40% of the areas were active and 33% more were occupied. The eagles bred 108 chicks. The breeding success of the SSE population was higher than in previous years, 0.67 chick per breeding pair. Bear predation rates were much lower than from 2005 to 2008, and the number of nests destroyed was less than 10%. Bear protection previously installed on some of the nesting trees most likely helped reduce predation rates.

Within the zone of potential impact around operating assets where disturbance may be caused by human and industrial activities, 165 eagle nests were identified in 61 breeding areas. In 38 occupied areas, 26 were active, and the eagles successfully raised 31 nestlings during 2009. Breeding success within the zone of influence was 0.82 chick per breeding pair, higher than outside the zone. Although this demonstrates the success of Sakhalin Energy's SSE impact mitigation plan, and the condition of the population is considered satisfactory overall, some of the population indices may be considered

low. For example, juveniles made up only 15% of the population, and the breeding success rate in 2009 was lower than in 2004, so protection measures will be maintained to ensure the conservation of this RDB species.

River ecosystems

Rivers

Linked to hydromophologic monitoring, assessment of benthic organisms living in the sediments of rivers and streams crossed by Sakhalin Energy's onshore pipelines is an important measure of water quality and habitat integrity. Compared to other aquatic groups like fish stocks, benthic organisms tend to be more stable over time, characterize a local situation, are sensitive to environmental disturbance, and provide useful 'early warning' signals of potential control failures and impacts to river communities.

River benthos surveys were conducted during August and September 2009, on 27 watercourses crossed by Sakhalin Energy's onshore pipelines, and on one watercourse located within the zone of influence of the onshore processing facility. This was the first survey carried out under the operations phase. In total, 292 benthic samples were taken at 146 stations, comparing upstream and downstream characteristics, including abundance, biomass, diversity of species and groups, and indicator species. It is difficult to conclude any technogenic influence on the patterns in these data from the first year of monitoring.

Water quality and sediment characteristics were monitored in 25 rivers during the spring high water period in 2009, when snow melt and runoff introduce allogenic materials (that is, not typical to this area) to the watercourse, and during the summer low water period, when concentration effects may cause water quality to deteriorate when benthos growth rates peak.

Data indicated that, in some rivers, the reduced flow from the upstream control station towards the downstream control station was due to riverbed deformation. Physical and chemical properties of surface water of all monitored water bodies complied with standard criteria during all periods of monitoring. Oxygen levels in the rivers during both periods were considered normal, and seasonal fluctuations of suspended solids were recorded in accordance with the hydrological regime. Concentrations of substances such as ammonium ions, nitrites, nitrates, and phosphates were relatively low. Overall, these results indicate that our river crossings have not affected water quality outside of normal conditions.

Sakhalin Taimen

The Sakhalin taimen is one of the world's largest and most ancient

species of salmon. It is a migratory species, and is found only in Sakhalin, the Amur Basin in Russia, and northern Hokkaido Island in Japan. Based on historical and recent data on species abundance across its range, the International Union for Conservation of Nature (IUCN) has listed the taimen as critically endangered.

Because it occupies the highest trophic level in Sakhalin rivers, the taimen is an ideal indicator species to gauge the health of freshwater ecosystems. Studies were conducted in 2009 to provide evidence of successful natural reproduction, to estimate the density of juveniles, to identify habitat types that are most important for spawners and juveniles, and to assess any impact from construction on the populations and habitats of this species.

From August to September, the study surveyed seven river basins. The highest indices of the average density of taimen juveniles in 2009 were observed in the Nabil River (0.1242 pcs/m^2) and in the Severnaya Khandasa River (0.0254 pcs/m^2).

Wetlands

Wetlands are a very important and complex habitat on Sakhalin Island. They support vital ecological processes such as water regulation and purification, and provid sanctuary for birds (including rare and protected species) during seasonal migrations. Sakhalin Energy has gone to great lengths to protect these wetlands and limit the Project's impact on them. Many experts have provided advice and wetlands management is a key part of Sakhalin Energy's Biodiversity Action Plan.

The Company's onshore pipelines right-of-way (ROW) passes through wetlands in places, affecting less than 0.5% of the total area of Sakhalin wetlands. Sakhalin Energy established a long-term monitoring programme to (a) control processes of wetland recovery within the ROW and in adjacent areas, and (b) assess and treat any long-term negative impacts on wetlands, which may occur as a result of construction or subsequent operation of the onshore pipelines.

A good understanding of wetlands is important because of the wetland's fragility. When affected, wetlands can take a very long time to recover, which is why they remain a focus for the Company. At the time of writing it is difficult to say what long term impact the pipeline construction has had. Preliminary results from the monitoring programme show soil and vegetation are slowly recovering, in line with expectations. The level of influence on areas adjacent to the ROW was lower than expected. The Company plans to continue monitoring wetlands in the future to mitigate any possible negative impact.

Marine ecosystems

Ballast water

Operation of the LNG plant and oil export terminal at the port of Prigorodnoye have led to increased vessel traffic in Aniva Bay. Tankers arriving at the port for LNG and oil cargoes took on ballast water in other parts of the world where marine flora and fauna differ from those in Aniva Bay. Thus, ballast water that is not 'exchanged' prior to arrival at the port may contain species that are 'alien' to local marine ecosystems and have the potential to become invasive. Recognising the importance of the risks faced by invasive species in ballast water Sakhalin Energy has taken a proactive approach to dealing with this issue.

A ballast water risk assessment was undertaken for the port of Prigorodnoye, and controls put in place to manage the potential effects of ballast exchange in Aniva Bay. Sakhalin Energy monitors the effectiveness of these controls by conducting surveys of marine plankton and benthos. In 2008, baseline studies were conducted of the community composition of zoo-, phyto-, and ichthyo–plankton in the Prigorodnoye area. Seasonal patterns were indicated by changes in the relative abundance of different species and groups and their biomass. In addition to plankton, baseline assessments of benthos and marine fouling were also completed from 2007 to 2008.

In 2009, established monitoring stations took samples of plankton, benthos, and marine fouling characteristics. A few species that had not been recorded during the baseline studies were identified, but none were invasive alien species.

Offshore monitoring

Sakhalin Energy monitors benthos, sediment and water quality around its platforms, pipelines, and other offshore infrastructure, to see if industrial activities such as dredging, dumping, drilling, and discharges have caused any changes.

Dredging works were undertaken in Aniva Bay during construction of the LNG jetty and the materials offloading facility. Dredged material was deposited at an approved site about 25 km due south of the LNG jetty. Prior to dredging and dumping, baseline characteristics for chemical and biological parameters in the water column and seabed were determined, against which potential change could be later compared.

The disposal site in Aniva Bay has been monitored annually during and after construction to assess benthic re–colonisation and recovery. Data show that initial effects on the benthic community were caused by sediment deposition. Benthic samples collected in the autumn and winter of 2004 showed benthic biodiversity significantly decreased across all groups of organisms. However, subsequent monitoring showed a rapid re–colonisation of the disposal area, and recent results indicate many of the species expected in the area are now present, providing evidence of a recovery in benthic fauna.

Overall, the results from 2009 surveys around the platforms, pipelines, and other offshore infrastructure indicate ecological conditions are good at many monitoring stations, where benthos community composition and distribution are stable and species diversity is high. Benthos recovery is generally well underway within the post–construction impact zone around offshore facilities, although biomass and density remain lower at some locations. Concentrations of pollutants in sea water did not exceed baseline levels, and concentrations of hydrocarbons and most heavy metals in bottom sediments were within background values, and less than concentrations that may lead to biological effects.

Western Gray Whales

The western Pacific population of gray whales is one of only two surviving populations of this species. Both populations were brought to near extinction by commercial whaling during the 19th and 20th centuries. The eastern Pacific population, which migrates annually from Mexico and Alaska to Chukotka and Kamchatka, has recovered considerably following an international ban on hunting and now numbers about 20,000. By comparison, the western Pacific population remains extremely small, approximately 136.

Although unconfirmed, it is thought the western population overwinters and breeds in the South China Sea. The whales then migrate to feeding grounds off the northeast coast of Sakhalin during late spring to autumn. Sakhalin Energy has done significant research and monitoring to better understand the population status and ecology of the Western Gray Whale. Earlier work began in 1997, and an extensive joint research and monitoring programme was initiated by Sakhalin Energy and Exxon Neftegas started in 2001, supported by a large team of

independent Russian and international scientists. This programme is also subject to third-party verification by the IUCN's Western Gray Whale Advisory Panel (WGWAP). The establishment of this independent advisory body was initiated by Sakhalin Energy in 2004 and represents an unprecedented step in the oil and gas industry.

Much of what is known about this population is the direct result of this detailed research. The monitoring programme currently comprises five main components: acoustics, benthos or food source, whale behaviour, distribution, and photo–identification.

After an observed decline in whale densities in 2008, distribution and photo–ID surveys conducted in 2009 demonstrated that whale abundance increased and was similar to the previously observed levels. The cause of the 2008 anomaly has not yet been fully established. One possible reason is their food supply. Analysis of long–term datasets for amphipod biomass in the Piltun feeding ground indicates a large decrease in biomass in 2006 compared with 2002 to 2005. Amphipod biomass then increased in 2007 to 2008, and this upward trend was maintained the next year. In 2009, amphipod biomass reached the level of 2004 to 2005, but was still lower compared with 2002 to 2003. In short, current analysis of amphipod data does not clearly reflect the 2008 anomaly in whale densities, but understanding these fluctuations is key to understanding the densities and distribution of the Western Gray Whale population.

Because of the change in whale abundance in 2008 and the need for further scientific study, Sakhalin Energy agreed with the WGWAP to postpone execution of a seismic survey planned for 2009. Meanwhile, the Seismic Task Force of the WGWAP, comprising Panel members and scientific experts, continued their extensive work to develop mitigation and monitoring methods to minimise disturbance of the whales during the 2010 seismic survey. When 2009 distribution surveys found that whale densities in the Piltun area offshore Sakhalin had returned to pre–2008 levels, Sakhalin Energy and the WGWAP agreed the seismic survey should proceed in 2010. Preparations are underway for the survey to take place in June 2010.

At the eighth meeting of the WGWAP in Geneva, Switzerland, the chairman of the Panel noted:

'Seismic surveys are taking place every year on the Sakhalin shelf, but this [Sakhalin Energy] project is unique in terms of what has been invested in mitigation and monitoring. We hope it will come to be regarded as a good model for other companies in Sakhalin and other parts of the world.'

Sakhalin Energy met with the Panel twice in 2009. In addition, the seismic survey task force and the

photo identification task force each met twice.

A total of 117 whales were identified offshore Sakhalin in 2009 compared to 98 in 2008. A near–record 10 calves were identified. Photo–identification effort from 2007 on shows evidence of fairly active whale migration between the feeding areas in northeastern Sakhalin and newly–identified ones in southeastern Kamchatka. In general, results from the 2009 surveys indicate the population is stable and routine mitigation measures appear adequate and effective.

This is a unique project, and Sakhalin Energy and its shareholders are committed to ensuring continued best practice consistent with their stated objectives for environmental management.

Oiled wildlife rehabilitation programme

Sakhalin Energy's Oil Spill Response plans set out the organisation and responsibilities for preparedness and response. The plans were developed in compliance with Russian Federation legislation and comprise required procedures, guidelines, checklists and other information so that the Company can plan, respond to, and manage oil spills coming from Sakhalin Energy operations.

Our oil spill response plans take into account key sensitivities and contain appropriate measures to ensure ecological interests are safeguarded. In keeping with our commitment to biodiversity and in line with international best practice, Sakhalin Energy is implementing an oiled wildlife rehabilitation programme. As part of its integrated oil spill response plan, the Company developed a plan that details how an oiled wildlife incident response should be initiated, implemented, and managed by Sakhalin Energy.

The plan describes measures aimed at prevention of and response to oiled wildlife, the required response capability, resources and procedures, and protocols for coordination and cooperation between corporate and third–party capabilities and resources.

Priority areas for wildlife protection in the event of an oil spill include the coastal bays and lagoons that sustain migrating birds, seabirds and other wildlife, spawning rivers, and wetlands.

Sakhalin Energy bought specialist equipment that is held in readiness should it ever need to be deployed.

Training and awareness

Sakhalin Energy believes education is critical to securing support for environmental management and biodiversity conservation. Training, development and competence assurance processes are well established within the Company's management system; basic environmental awareness training is delivered during HSE induction, while training needs for task–specific competencies are addressed in more targeted programmes. Capacity building inside and outside the organisation is encouraged.

Monitoring and follow–up

Sakhalin Energy's monitoring programmes improve our understanding of the environment in which we operate. We have a systematic approach to collect data, analyse and report to facilitate informed decision–making. Different programmes are derived from specific objectives. Baseline monitoring provides a reference point for identifying trends and is an indicator of sustainable development. Measurements help us assess compliance with our standards, permits and licenses, while effects assessments help us determine the success of our industrial controls and mitigation plans. Monitoring programmes are reviewed regularly to improve information collection, accommodate changes to scope, and introduce new methods and techniques.

Sakhalin Energy's management system also requires reporting incidents and non–compliance, which are subject to investigation, corrective action and close–out. Our process of corrective action is necessary to ensure our operating requirements are met, our performance continually improves, and the likelihood of future incidents is minimised.

In addition, all business processes and activities are audited periodically, depending on the activity risk profile and previous performance. Audits enable the Company to verify the effectiveness of internal controls intended to manage our environmental risks.

HUMAN RESOURCES MANAGEMENT AND DEVELOPMENT

HR management and HR policy approaches

As part of its social responsibility and commitment to sustainable development, the Company is building up its human resources capacity and provides good remuneration to its employees. Dividing of the Sakhalin-2 Project into two phases, construction and operation, determines the corresponding approaches the Company has taken to HR management.

Basic human values, such as integrity, honesty, and respect for others, are top priorities for Sakhalin Energy. We encourage diversity and respect the personalities of all employees.

The Company implements its HR tasks and objectives through its HR policy, which is based on a detailed HR strategy and tactics in all areas.

The HR policy is a comprehensive strategic policy governing the Company's relations with its employees. The HR Director leads development of the Company's HR policy and determines its key objectives.

The key objectives of the Company's HR policy are:

- To improve the staff structure of the Company's business units
- To develop an effective motivation and incentive system
- To develop and maintain the Company's organisational structure; to promote employee loyalty and responsibility; to improve labour discipline and working standards
- To deploy employee training and talent development programmes
- To establish and enhance the corporate culture.

To achieve these objectives, the Company has adopted policies, guidelines, procedures and other regulations, which are in line with Russian law and the best international HR management practices. The basic documents regulating HR management are:

- The Code of Conduct
- Internal Working Rules
- Diversity and Inclusiveness Policy
- Conflict of Interest Procedure
- Harassment and Discrimination Procedure
- Whistle Blowing Policy
- Whistle Blowing Procedure
- Grievance and Inquiry Procedure for Sakhalin Energy Personnel
- Learning and Development Guideline
- Recruitment Procedure for Russian National Staff
- Employees' Personal Data Confidentiality Policy
- Occupational Health Standard.

General

At the end of 2009, the Company employed 1,916 people, 80 per cent of them Russian nationals or about 1,500 people. A total of 1,871 were based in Sakhalin sites and offices; the rest worked in the Moscow office. Full-time employment contracts with the Company were held by 1,347 people or 70 per cent of total number of employees. At the end of 2009, the Company employed 982 Sakhalin residents, 141 of whom held executive positions.

In December 2009, Aleksandr Khoroshavin, governor of the Sakhalin Oblast, awarded Sakhalin Energy Employer Credibility Certificate No. 001.

The Company's efforts were recognised to ensure the labour rights of its employees, stated in its declaration submitted to the State Labour Inspectorate of the Sakhalin Oblast. The initiative to declare job activities under the respective part of the law was launched in the Sakhalin Oblast only this year. The main objective of the initiative is to promote socially responsible business practices.

The Company was the first in the region to be awarded this certificate, indicating that the holder respects employees' rights and is in compliance with the labour law.

The per cent of Russian nationals in the Company's work force is expected to reach 90 per cent over the next few years. Russian citizens held 264 executive positions or 64 per cent of the total in 2009 while 67 executives were women. By 2018, Russians are expected to hold 75 per cent of executive positions. The Company has an action plan to achieve these goals. In addition to the proactive approach to training and promoting Russian nationals who are already employed, the action plan calls for hiring new highly-skilled Russian specialists and arranging internships as a resource of technicians for the Company.

The Company carried out a massive recruitment drive mostly in the construction phase. As the Sakhalin-2 Project reached the operation phase, its workforce decreased and will be sustained at this level. Yet the Company is currently hiring, as it replaces expatriate employees with Russian nationals, including engineers, technicians and operators. In 2009, employee turnover was 4.46%.

In 2009, the average age of the Company's employees was 36 years. Employees below 35 years of age account for two–thirds of the Company's payroll; most of them majored in oil and gas engineering at leading Russian universities.

In 2009, 28% of the Company's employees worked rotating shifts. They were accommodated in fully furnished shared housing facilities, such as hotels and shift camps. The Company makes every effort to provide a high quality of accommodation for its employees (see Section *Housing policy*).

Labour safety and protection

Sakhalin Energy is committed to pursuing the goal of doing no harm to people and promoting a culture where employees share this commitment. We aim to have an HSE performance we can be proud of, to earn the confidence of customers, shareholders and society at large, to be a good neighbour, and to contribute to sustainable development.

To achieve this commitment, Sakhalin Energy has a systematic approach to HSE management designed to ensure compliance with the law and achieve continuous improvement. We also require our contractors to manage safety in line with this policy.

Performance

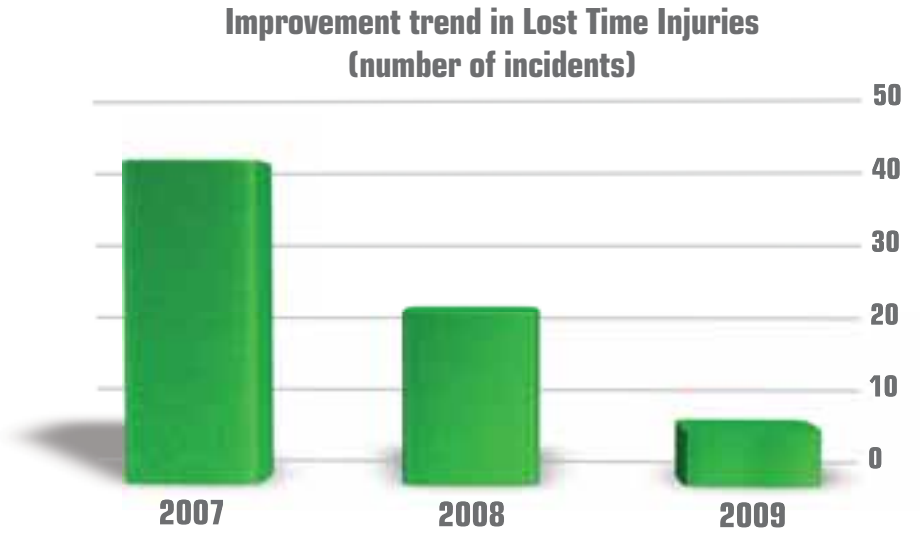
The Company has continuously improved its safety performance through its relentless focus on labour protection and industrial safety.

Ensuring safety is a complex activity that involves a number of key areas such as road safety, behavioural safety, operational safety, and safe start–up of facilities with the introduction of hydrocarbons during commissioning.

The 2009 results show a significant leap forward in safety performance. Sakhalin Energy achieved zero fatalities or significant incidents, the number one safety priority for the Company.

Sakhalin Energy also recorded another significant safety achievement in 2009: road accidents involving vehicles of the Company and its contractors dropped sharply. By late 2009, close to 500 motor vehicles involved in the project operated for more than 10 months free of road injuries. On 23 February 2010, the Company entered its second year without injuries from road accidents. From February 2009 to February 2010, vehicles involved in the project travelled nearly 19 million km.

Although there were seven lost–time injuries in 2009, this is still a major improvement from 41 injuries recorded in 2007.



The Company achieved its progress by emphasising road safety, behavioural safety, operational safety, and the safe start–up of facilities by introducing hydrocarbons during commissioning.

Road safety

A critical review in 2007 of the Company's approach to road safety led to fundamental changes in leadership focus and the implementation of controls. The Company launched a CEO–led road safety programme for Company and contractor personnel that covered seven areas:

1. Visible and leading by example senior management
2. Rigorously implementing road safety standards, tailored to the road safety culture in Russia
3. Improving defensive driving skills
4. Consistent consequence management for violating safety rules
5. Systematically reducing exposure
6. Installing in–vehicle monitoring systems in all vehicles to monitor driver behaviour
7. Influencing the community through partnership activities in conjunction with the Global Road Safety Partnership.

Acting as a responsible citizen, in 2005 Sakhalin Energy joined efforts with the government of Sakhalin Oblast, GIBDD and the public to establish the Sakhalin Road Safety Partnership. This organisation, in which Sakhalin Energy plays an important role, implements long-term projects to improve road safety on the island. As a result of joint actions taken by the Company, the State and the public, the accident rate on Sakhalin roads has dropped significantly. The rate of drivers who use safety belts whilst driving is higher on Sakhalin today than anywhere in Russia. The activity of the Sakhalin Road Safety Partnership and Sakhalin Energy's internal road accident prevention programme were highly praised by the International Energy Institute and honoured with an award as the best international project in terms of safety.

Operational safety

While still in the construction phase, Sakhalin Energy introduced 'HSE Golden Rules' which are mandatory for Company personnel and contractors. With the transition from construction to operations, the risk profile of Sakhalin Energy changed, but the risk levels did not become lower. With process safety becoming even more important, the Company updated and detailed its internal safety rules to match its new focus. The most serious hazards critical to life safety were identified, and the Company's new '10 Life Saving Rules' were established.

To also address the increased risks associated with the introduction of hydrocarbons during commissioning, the Company introduced the 'Go Live!' training programme to improve hazard recognition and adjust risk perception for workers near hydrocarbon.

Sergey ROZINOV,
a Senior Process Engineer at the Onshore Processing Facility (left), receives the CEO safety award from Andrei GALAEV,
Sakhalin Energy CEO (right)

The Company also put in place a programme to identify improvement opportunities in worksite hazard management and to leverage best practices across Sakhalin Energy. The staff–swap programme allows operational personnel to move between different assets to conduct facilitated reviews.

Behavioural safety

The goal of behavioural safety at Sakhalin Energy is for the staff and contractors to want to do the right thing, because they see the value in it, not because they are told to do it. In addition to systematically identifying and controlling risks, the Company introduced several initiatives and ongoing activities in 2009 to kickstart the HSE management system.

All staff and contractors undergo observation and intervention training as part of the Company's behavioural safety programme. To better understand the safety culture of contractors and inside the Company, Sakhalin Energy deployed the Energy Institute's Hearts and Minds tool. The tool also helped the Company take further action to strengthen the culture of safety.

To help maintain high safety awareness and to recognise HSE leaders at all levels, Sakhalin Energy created a monthly CEO Health, Safety and Environment Award. The award is given to individuals and departments of the Company and its contractors, for actions and behaviour that exemplify our values. The award is not only for single achievements, but also for systematic work and initiatives in labour safety and environmental protection.

To make safety visible and relevant for all staff and contractors, Sakhalin Energy holds a Safety Day each year, where everyone reflects on how they can further improve their safety behaviour – in the field, in the office and at home.

'DO THE RIGHT THING!' – IS THE MESSAGE OF SAFETY DAY

Safety Day at the LNG plant

Protecting the health of personnel

Sakhalin Energy supports a structured and efficient approach to manage and protect the health of our personnel. After developing minimum health management standards, these standards were well–maintained at the assets and in the project groups in 2009. The outcome: assets and project groups made a satisfactory contribution to the health performance scorecard.

As part of its revised medical emergency response processes, the Company completed a gap analysis for all relevant sites, in order to develop and implement new training modules and medical emergency response manuals at new operational sites.

Medical fitness for high–risk groups emerged as a significant issue. Based on a review of non–accidental deaths in earlier years, the Company developed an additional health screening programme focusing on cardio–vascular diseases. Medical fitness screening for all workers continued, including a risk assessment for heart attack.

An internally promoted Wellness Campaign supported the programme. The campaign

encourages personnel to maintain a healthy state of body and mind, especially through deliberate effort. To further encourage a healthy lifestyle, the Company built a sports and leisure centre in Yuzhno-Sakhalinsk for Sakhalin Energy employees. The centre comprises sports amenities, a gym, a swimming pool, and leisure facilities. Sports and health facilities are also in every camp and permanent accommodation for the Prigorodnoye complex personnel in Korsakov. Moscow office employees get compensation towards sport club membership fees.

Alcohol and drug awareness programmes were developed with the help of materials from Alcoholics Anonymous in Yuzhno–Sakhalinsk, in line with the Company's alcohol breath–testing programme at operational sites and the Yuzhno offices. Random drug tests were conducted at offshore installations. The Company also recognised World No Tobacco Day on 31 May.

The Company recognises sexually–transmitted diseases, including HIV/ AIDS, as an issue that poses health, social, and reputational risks. A joint community health initiative addresses the issue, and in 2009 carried out a pre–hospital care project, first aid training, an HIV / AIDS awareness campaign and conference, and a billboard campaign.

The Influenza Contingency Action and Communication Plans progressed in 2009. Due to an Influenza A (H1N1) level six alert, the stock of personal protection equipment on remote sites was increased, regular communication alerts were sent, and all employees and contractors arriving from affected areas were monitored.

Under the Staff Development and Russian Content policy, the international training programme for Russian physicians continued. A total of nine Russian physicians successfully completed refresher training abroad.

Housing policy

The Company provides comfortable housing for all its employees who come to Sakhalin to work. Non–local employees and their families live in fully–furnished housing. The Company covers all moving and relocation expenses for new employees and their families.

To accommodate engineering and operating staff, the Company built shift camps at each project site. The camps offer comfortable facilities for work, leisure, and sport.

Recruitment, motivation and assessment

The Company has adopted a number of documents regulating recruitment, employee assessment, and employee motivation. The documents establish mandatory procedures for selecting and approving candidates, evaluating personal and professional skills, and planning personal and professional growth.

The Company's recruiting process is conducted in four main stages:

Prigorodnoye staff housing

In 2009, a new housing facility was commissioned in Korsakov to accommodate employees of the Prigorodnoye complex.

Until recently, LNG plant personnel lived in a temporary camp near the plant site.

The housing facility consists of five buildings and accommodates 100 people. It has all the amenities for comfortable work and leisure, including gym, library and lecture room, conference hall, canteen, sauna, Jacuzzi, tennis court, volleyball court and even a special barbecue site.

- Attraction
- Screening
- Selection
- Hiring.

Sakhalin Energy posts all vacancies at its corporate website where an applicant questionnaire is conveniently available. The Company also uses mass media, recruiting agencies, and employment agencies to announce vacancies and invite candidates for interviews and to events.

To help new employees get off to a good start, Sakhalin Energy adopted an adjustment procedure to ensure high employee performance from day one, and faster promotion and career growth:

The procedure includes:

- Arranging workplaces for new employees
- Ongoing briefings, feedback, and mentoring
- Arranging and conducting the first meeting with the Company; introducing an employee to the direct supervisor
- Arranging and performing induction, information management, and other sessions to help new employees adapt.

The employee motivation system adopted by Sakhalin Energy provides for:

- Competitive salaries equal to or higher than average wages in the Russian oil and gas industry
- Transparent bonus schemes in all personnel categories
- Competitive benefits to attract a highly–skilled workforce
- Career planning for employees
- Training programmes
- An ongoing career planning and performance evaluation cycle, including regular monitoring setting and achieving targets, evaluation and feedback; as well as identifying improvement areas and setting target for the next period
- Regular monitoring of the financial aspects of the labour market.

To keep wages competitive, the Company annually reviews employees remunerations based on performance.

Our compensation policy, practice and methods are aimed at rewarding and encouraging operational performance and personal achievement in the short and long term. The incentive programme is designed to reward special achievements based on a standard integrated approach in all Company business units.

The Company offers an employee benefits package that includes compensation, perks, and additional privileges that goes beyond Russian labour law.

The package includes:

- Voluntary health insurance
- Health benefits
- Free or discounted travel packages and health resort accommodations for employees and their children
- Round–trip vacation travel for employees and their children
- Lump sum cash allowances for difficult personal situations.

Employing disabled people

The Company offers employment opportunities to disabled people. These individuals receive priority in the selection process for any vacancies, provided they meet the qualification eligibility criteria and taking into account workplace limitations. All Company offices are equipped for the disabled. The Company has been a partner with the Government Employment Agency of the Sakhalin Oblast since 2005. As of end 2009, the Company employed eight disabled people.

HR training and development

Corporate approaches

To maintain a high level of skills and highly-motivated employees, which are necessary to succeed in a highly competitive industry domestically and internationally, the Company needs to pay constant attention to professional growth and development. Our top priority is to achieve performance excellence at all levels by tapping the full potential of employees.

We are committed to the ongoing professional development of our workforce. Our HR policy aims to provide training and development opportunities to all employees. The Company has adopted special procedures to do this and uses them to prepare annual and strategic training and development plans. Employees and management supervise the performance of these plans.

Survey of personnel motivation and corporate culture

The Company launched an employee opinion survey in late 2009 to look into the most significant aspects of employee motivation and corporate culture, in line with best corporate practices. The survey included career and professional development, wages, benefits, and corporate communications.

The objective of the survey was to get employee feedback on these issues for use in developing the Company's development strategy. The survey motto was 'Everyone's voice will be heard! Our future and our success are in your hands!'

Findings and recommendations will be presented to the Committee of Executive Directors in 2010.

Sakhalin Energy has unique entree to training resources. The Company has established close relations with more than 20 educational institutions and training centres of its major shareholder, Gazprom, which are integrated into Gazprom's system of continuing education. This integration gives Sakhalin Energy access to the knowledge and experience of top specialists at the Russian gas giant. Company employees also have access to remote learning from another shareholder, Shell, under Shell's Open University initiative.

On–the–job training, conventional training, and workshops are available on a wide range of subjects:

- Operation and maintenance for technical and engineering personnel
- Health, safety and environment (HSE) and statutory briefings
- Special technical courses and in other professional areas, such as finance, contracts, and human resources
- Management and business administration
- PC, Internet, and Intranet training and other IT courses
- Long–term educational programmes for certification (CIMA, ACCA, CIPS)
- Training for graduates of educational institutions
- General training programs and language courses for Russians and expatriates.

More than 1,800 people participated in workshops, training, and skills improvement sessions in 2009. Sakhalin Energy invested more than RUB 150 million in personnel training in 2009.

Apprenticeships

An apprenticeship programme for Sakhalin residents has been in place since 2003. By the end of 2009, 150 people had been trained based on this programme; many now work at the LNG plant, the onshore processing facility, and the offshore

A TOTAL OF 10 GRADUATES OF THE YUZHNO–SAKHALINSK FUEL AND ENERGY COLLEGE, EIGHT MEN AND TWO WOMEN, COMPLETED A YEAR–LONG TRAINING PROGRAMME FOR PROCESS UNIT OPERATORS AT SAKHALIN ENERGY'S PROFESSIONAL TRAINING CENTRE. THE CENTRE WAS SET UP SEVERAL YEARS AGO IN PARTNERSHIP WITH THE COLLEGE. TODAY, THESE YOUNG SAKHALINERS HAVE STARTED WORKING AT THE LIQUEFIED NATURAL GAS PLANT.

facilities. A total of 10 more specialists went through the programme in September 2009. In hiring, Russian residents get priority, especially from Sakhalin, where the Company operates. This is not only commitment under the PSA but is first and foremost part of the Company's HR policy.

Another Company objective is to provide job training in skills which are new to Russia, such as operating gas liquefaction process. While this specialty was previously done by expatriate employees, by early 2010, the first three Russian specialists completed the required certification to operate this technology.

Operational internship programme

To enlarge its talent pool, Sakhalin Energy adopted an operational internship programme for undergraduates of Russian universities. The objectives of the programme are:

- To give students an opportunity to work in a large international corporation
- To teach students best business practices
- To identify students with high potential who may become eligible candidates for permanent or temporary jobs in the Company.

The internship programme was launched in 2000 to allow students to put their theoretical knowledge into practice and to develop practical skills. The internship lasts four to eight weeks and takes place during regular working hours in accordance with Russian law.

In 2009, 45 students completed an internship at Sakhalin Energy.

Developing the talent pool

To continue developing the potential of Company personnel, and to train managers and specialists to respond to changes in all areas and work efficiently in current market conditions, the HR Directorate sees developing the talent pool as a high priority. Developing the pool of talent shortens the adaptation period of specialists upon promotion, reduces the risks of mistakes in filling positions, and ensures insufficiently–trained employees are replaced with well–trained employees in a timely manner.

The objectives of developing the talent pool for smooth succession are:

- To train executives and employees able to manage the Company's operations under changing conditions; to sustain management continuity and succession, as well as vertical and horizontal staff rotation
- To ensure scheduled replacement of expatriate employees with highly–skilled local personnel in accordance with the Sakhalin-2 PSA
- To smoothly fill executive vacancies with internal candidates possessing top professional and managerial skills
- To reduce the adjustment period for executive positions
- To improve employee motivation for professional and personal growth by creating opportunities for career growth
- To reduce personnel turnover
- To lower personnel–related costs.

SOCIAL INVESTMENT AND CONTRIBUTION TO REGIONAL SUSTAINABLE DEVELOPMENT

Company principles and approaches to Social Investment and Sustainable Development

Sakhalin Energy has made social investments through its charitable and sponsorship programmes since the Sakhalin-2 Project began. Aware of its responsibility to develop society, the Company strives to improve and develop the territory where it operates. Implementing socially relevant programmes in the Sakhalin region has been a priority for the Company since it was founded in 1994.

IN EARLY 2009, SAKHALIN ENERGY WON THE REGIONAL COMPETITION, 'PHILANTHROPIST OF THE YEAR' FOR THE FIFTH TIME. AT THE AWARDS CEREMONY ON 20 MARCH, THE COMPANY RECEIVED AN AWARD IN THE CATEGORY 'CORPORATE PHILANTHROPIST OF THE YEAR'.

Following public consultations, since 2005 the Company has focused its social programmes on education, biological diversity, business, infrastructure and healthcare. A variety of projects have been carried out under these programs, ranging from financing Internet centres at rural libraries on Sakhalin to constructing and equipping healthcare institutions and sponsoring foster care.

The Company invested RUB 65.7 million (US$ 2.27 million) in social programmes in the Sakhalin Oblast, in 2009 alone.

The Company supports projects as part of its social investment programme, according to its sustainable development policy and procedure for implementing social investment and sustainable development projects on the basis of project evaluation criteria. The amount of finance for projects and programmes is approved annually by the Company's shareholders. The decision to support a particular project is made within the budget limit by the relevant competent bodies of the Company – Social Investments and Sustainable Development Committee, supervisory boards of corporate programmes, etc.

Our social programmes and projects have won recognition at

In the Corporate Donor of Russia 2009 competition for charitable projects, and the Second Annual Survey of Corporate Philanthropy, conducted by Vedomosti newspaper, Forum of Donors and PriceWaterhouseCoopers, Sakhalin Energy ranked among the most effective corporate philanthropists in Russia. The Company took third place among Russia's most prestigious national projects on the effectiveness of its corporate charitable programmes. The Sakhalin Salmon Initiative project, presented by Sakhalin Energy for this competition, received 'Best Programme Illustrating the Policy of Corporate Philanthropy and Principles of the Company's Social Investments'. The Company's programme to support charitable initiatives of company's employees was nominated for 'Best Programme (Project) Facilitating aCulture of Philanthropy in Society'

ON 28 JANUARY 2009, SAKHALIN ENERGY RECEIVED THE MOST PRESTIGIOUS RUSSIAN AWARD IN PUBLIC RELATIONS – 'THE SILVER ARCHER' NATIONAL PRIZE, BESTOWED ANNUALLY ON THE BEST PROJECTS IN RUSSIA. THE AWARD INCLUDED A RANGE OF SOCIAL PROJECTS SAKHALIN ENERGY IMPLEMENTED ON SAKHALIN ISLAND. PRESENTED AS PART OF A JOINT PROGRAMME, 'BREAKING STEREOTYPES', THESE MULTIFACETED SOCIAL PROJECTS REINFORCE THE COMPANY'S CORPORATE REPUTATION AND BUILD TRUST AMONG THE PEOPLES OF SAKHALIN.

regional, federal and international levels. Over the last few years Sakhalin Energy has been named winner of the regional competition Philanthropist of the Year. The Company's programmes have won and been nominated in several categories of Corporate Donor – a prestigious Russian competition for best practice in social investment.

Development of the regional social infrastructure

Sakhalin Energy aims to develop the socio–economic fabric of the region, given that high regional development indicators are key to the Company's long–term sustainable development. As part of infrastructure modernisation and sustainable development programmes, we have supported projects to develop the island's social infrastructure.

We launched our programme to upgrade social infrastructure in 2001 and largely completed it by 2007, although some activities continued in 2008 and 2009. The programme envisages:

- Constructing new roads
- Reconstructing existing roads
- Repairing bridges and culverts
- Modernising ports
- Modernising airports
- Modernising health care facilities.

From 2001 to 2009, the Company invested over US$ 600 million modernising the infrastructure of the Island.

The Company provided financial support for the following projects which started up in 2009:

- Opening of a new sports and health complex in Aniva. The Sakhalin Oblast administration and Sakhalin Energy jointly financed the construction and sport equipment
- Reopening of Spartak stadium in Yuzhno–Sakhalinsk; reconstruction of the stadium was financed from the Oblast budget with a financial contribution from Sakhalin Energy

Sakhalin Energy funds new polyclinic

In early 2009 a polyclinic in the city of Korsakov opened, one of Sakhalin Energy's recent social projects, implemented jointly with the administration of the Korsakov city district and the Korsakov Central District Hospital.

The three floors of the centrally–located polyclinic can accommodate 200 patients per shift. The polyclinic has a medical prevention centre diagnostics, X–ray imaging departments, and a dental office.

The clinic took three years to build, at a cost to Sakhalin Energy of over US$ 5 million.

The company paid for modern medical equipment for several other healthcare facilities in the Korsakov District in 2009.

Sports and health complex opens its doors

In July 2007, the Sakhalin Oblast administration, the Aniva municipal district and Sakhalin Energy signed an agreement to jointly finance reconstruction of social facilities within the municipality. One of them was the long–awaited sports and health complex in Aniva which opened early in 2009.

The new three–story building houses a wrestling room, a gym and fitness hall, and a hall for team sports. The local junior and youth sports schools are also located there. The Sakhalin Oblast administration, the Aniva municipal district, and Sakhalin Energy allocated RUB 48 million for the sports and fitness complex, with RUB 10 million coming from Sakhalin Energy.

- Opening of a children's dental surgery in Poronaysk
- Purchasing of new medical equipment for the Korsakov Central District Hospital
- Opening of dental surgery in the village of Ozersk, Korsakov municipal district.

Social investment and sustainable development programmes supported by Sakhalin Energy

Social investments on the island include large projects, such as the partnership programmes Sakhalin Salmon Initiative, and What to do in Emergency Situations, as well as smaller projects. For several years, our social investment and sustainable development strategy have been based on partnering. The approach is reciprocal: in addition to projects initiated by the Company as part of its own policy, local stakeholders and local initiatives can define, develop and propose socially–important projects.

The Company sponsors competitive grant programmes that offer organisations and initiative groups throughout the Oblast the opportunity to receive funding for small–scale projects, a programme to support charitable initiatives of employees, and many others.

Partner project: Sakhalin Salmon Initiative

The Sakhalin Salmon Initiative (SSI) started in 2004. The project was initiated by the non–profit organisation the Wild Salmon Centre of the US. Sakhalin Energy started financing of development the concept and the strategy for the Initiative the following year. The goal of the programme is to support the preservation and rational use of wild salmon and salmon ecosystems, and to facilitate sustainable economic and social development on Sakhalin Island. Sakhalin Energy and the Wild Salmon Centre signed an agreement in 2008 to finance a four–year programme that runs through 2011 to preserve wild salmon on Sakhalin Island, with a budget of US$ 8.8 million, of which Sakhalin Energy provides US$ 4.4 million.

Activities are carried out by the Wild Salmon Centre and the Sakhalin Salmon Initiative, an autonomous, non–profit organisation created in 2007 and directed by a coordination committee. The committee is staffed by representatives from the government of the Sakhalin Oblast, regional and federal agencies, research organisations, businesses, fisheries, communities of Sakhalin indigenous minorities, and local and international NGOs. Projects of the initiative fall under six priority areas: salmon basin councils, monitoring salmon rivers, education and awareness, preservation of salmon habitats, creation of the Salmon Park educational and recreational zone, and development of sustainable fishing.

The following activities were carried out in 2009:

- Two extensive research expeditions
- Ongoing comprehensive monitoring of the abundance and biodiversity of salmon populations and their habitats in Sakhalin rivers
- Salmon basin councils in six districts tackled poaching and restored migration routes to salmon spawning sites, which were disrupted by destructive cyclones in the summer of 2009

THE SAKHALIN SALMON INITIATIVE WON 'THE CORPORATE DONOR 2009', A RUSSIA–WIDE COMPETITION FOR SOCIAL INVESTMENT IN THE CATEGORY OF 'BEST PROGRAMME ILLUSTRATING PRINCIPLES OF CORPORATE CULTURE AND FACILITATING DEVELOPMENT OF CORPORATE STANDARDS FOR COMPANY'S PUBLIC SERVICE ACTIVITIES', ESTABLISHED BY THE RUSSIAN UNION OF INDUSTRIALISTS AND ENTREPRENEURS.

- Preliminary evaluation was completed on ecological certification of salmon fishing, according to the criteria of the Marine Sponsor Council (MSC); in the long term, this certification will allow the fishermen of Sakhalin to benefit from the rising demand for seafood caught using the principles of rational nature management

- A series of cultural events, including an ecological forum, Salmon 2009, an ecological educational gathering the Salmon Festival, along with grant–financed projects
- Financing secured for the first international salmon camp attended by junior ecologists from the USA and Sakhalin
- Around 200 children went on educational trips to study the life of salmon in their natural habitat.

Information about specific activities is available on the Initiative's website: http://sakhsalmoninitiative.org/

Partner project: What to do in emergency situations

Sakhalin is one of the few Russian regions where many kinds of natural disasters are possible – earthquakes, avalanches, forest fires, blizzards, and tsunamis. Since 2005, Sakhalin Energy has been working in partnership with Emercom and the Department of Education in the region to teach local children what to do in an emergency using game–playing techniques.

Programme accomplishments over the period 2003 to 2009 include:

- 23 cartoons were created, featuring a memorable character Senya, broadcast by local television channels, instructing children how to act in an emergency
- A colourful comics book for first–graders in the Sakhalin Oblast was published
- According to the results of a themed competition, 12 schools on the island received modern equipment for life safety for use in classrooms: PCs with specialised software, multimedia equipment, and visual aids.

SAKHALIN ENERGY RECEIVED A LETTER OF APPRECIATION IN JANUARY 2009 FROM THE SAKHALIN OBLAST ADMINISTRATION FOR ASSISTING WITH EMERGENCY PREVENTION. THE COMPANY WAS REWARDED FOR ITS FOUR–YEAR CORPORATE PROGRAMME 'WHAT TO DO IN EMERGENCY SITUATIONS', WHICH INSTRUCTED CHILDREN AND ADULTS.

We are proud the programme has attracted a great deal of interest outside Sakhalin, notably:

- Senya cartoons are broadcast in 10 Russian regions
- Following an expert review of the series, the Emergency Psychological Aid Centre of the Russian Emercom Central Administration described What to do in Emergency situations as 'an interesting and relevant solution to the problem of life safety education'; since 2009, Senya cartoons have been available on the children's website of the Russian Emercom: http://www.spas–extreme.ru/
- In mid–December 2009, the Far Eastern Regional Centre of Emercom invited Sakhalin Energy to take part in an exhibition as part of the annual meeting of the Far Eastern rescuers in Birobidzhan.

Competitive corporate programme 'Small grants – Big deeds'

Small Grants – Big Deeds is a charitable project that supports local initiatives in districts of the Sakhalin Oblast in operation since 2003. Grants are available on a competitive basis to initiative groups, non–profit and nongovernmental organisations, and institutions in the Sakhalin Oblast for social, environmental, cultural, and educational initiatives targeting specific local problems. Over the years, the programme has helped bring to life 200 projects in 47 island communities.

In 2009, 13 grant projects were implemented with Company funds, including:

- Central library system of Yuzhno–Sakhalinsk, 'Through Culture to Peace and Accord'
- 'Green Necklace of Sakhalin' by the municipal educational institution of advanced education for children, the Poronaysk Centre for Children's Creativity
- 'The Sea Teaches Us,' by the municipal educational institution of advanced education for children, the Uglegorsk Centre for Children's Creativity.

'Small grants – Big deeds' is the first project of its kind in the Sakhalin Oblast. We are thankful to all participants for their endeavours, their readiness to progress and study together, and for their small but exciting projects, which have in most cases become significant.

Educational grants programme

For the seventh year in a row, Sakhalin Energy has a grant programme in place for students leaving Sakhalin schools to pursue higher education. Eleventh–graders of the Sakhalin Oblast schools and graduates of oil and gas technical schools are eligible to participate. Winners are awarded educational grants before they leave school and enroll at a university. The grants include scholarships and trips to the university and back home. Scholarship recipients who study an oil and gas discipline have the opportunity to get practical or pre–graduation training at Sakhalin Energy.

The annual budget of the programme is close to RUB 6 million.

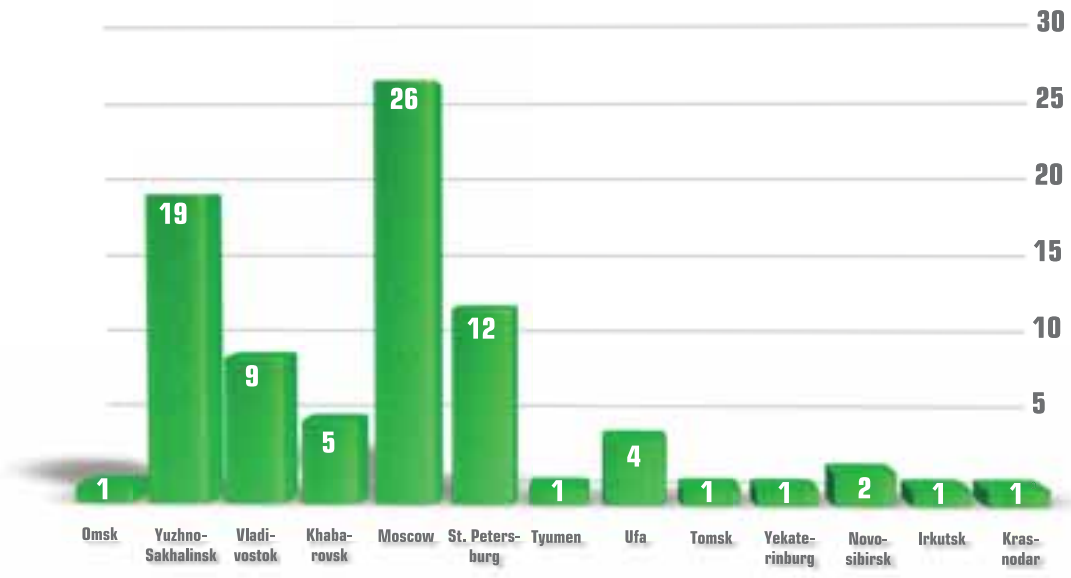
A total of 82 grants have been awarded since 2003, including 12 grants in 2009.

Programme to support volunteer charitable initiatives of employees

Employee involvement in the community is a crucial element of our corporate culture. In support of employee efforts, a company programme, Support of Charitable Initiatives of Sakhalin Energy Employees, continued in 2009, based on a widely–used international model of corporate social investment that is relatively new in Russia. The Company doubles the funds employees donate to a socially important project. The programme's motto is 'Hurry up For Good Deeds.'

The programme gives employees an opportunity to take part directly in a strategic corporate social programme, understand the Company's approaches and principles in this domain, apply their knowledge and skills in their own project, act as initiators and

Cities where scholarship holders pursue education



creators of charitable ideas, and practice their communications and project planning skills.

Since 2008, over 300 employees have taken part in the programme. As a rule, employees focus on the most vulnerable social groups: children in orphanages and social shelters, children left without parental care, children with disabilities, and the elderly.

Projects implemented in 2009 include:

- Audio books for a library for blind children
- New Year's celebration for children with disabilities at the Preodoleniye Rehabilitation Centre
- 'New Year's Miracle' – a celebration for children from the Rehabilitation Centre in Yuzhno–Sakhalinsk and the Pravda village orphanage, organised by employees at the Olympia Park Entertainment Complex
- Sports gear purchased for children with disabilities at the social rehabilitation centre, and a sports festival at the Nadezhda Social Rehabilitation Centre (Poronaysk).

Sakhalin indigenous minorities

Profile of the Sakhalin Indigenous Minorities Development Plan (SIMDP)

Sakhalin is home to about 3,500 representatives of indigenous minorities (about 0.7% of the island's population) belonging to four major ethnic groups: Nivkhs, Uilta (Orok), Evenkis and Nanais.

We have been working with Sakhalin's indigenous minorities since the Company was established in 1994. The Company's social initiatives support cultural, sports and educational projects. In the first stage, the Company worked mainly with reindeer herders who were directly affected by construction of the Sakhalin 2 Project, and key stakeholders.

Since 2005, we have been working with all Sakhalin's indigenous minorities groups as part of our corporate Sakhalin Indigenous Minorities Development Plan. The plan is a trilateral programme implemented jointly by Sakhalin Energy, the government of the Sakhalin Oblast,and the Regional Council of Authorised Representatives of Sakhalin Indigenous Minorities.

IN 2009, THE PROGRAMME TO SUPPORT CHARITABLE INITIATIVES OF COMPANY EMPLOYEES 'HURRY UP FOR GOOD DEEDS' WAS NOMINATED FOR BEST PROGRAMME (PROJECT) FACILITATING A CULTURE OF PHILANTHROPY IN SOCIETY, ANNOUNCED BY THE RF PUBLIC CHAMBER COMMISSION FOR DEVELOPMENT OF PHILANTHROPY AND IMPROVEMENT OF NGO LEGISLATION.

The document was drawn up with the participation of the three parties, following extensive consultations in areas densely populated by Sakhalin's indigenous minorities, and is based on best Russian and international practices. The Plan is the only document of its kind on Sakhalin Island.

Key tasks of the Development Plan include:

- Prevent or minimise potentially adverse impacts of the Sakhalin-2 Project on indigenous peoples
- Contribute to improving the quality of life of Sakhalin's indigenous minorities, through social development programmes that address their cultural specificity
- Assist the potential development of Sakhalin indigenous minorities, by encouraging their active involvement in managing the implementation of the Plan, and other similar programmes.

First book of ABCs for the children of Uilta

In September 2009, Sakhalin Energy was invited to attend the All–Russian Practical Research Conference in Yakutsk, titled 'Native Languages of Indigenous Minorities of the Russian Federation in the Russian Education System'. Representatives of 13 Russian regions, 15 municipalities of the Republic of Sakha, and guests from five countries, attended. A Sakhalin Energy representative delivered a report on collaboration as part of the Development Plan, including working together to preserve the native languages of Sakhalin indigenous minorities.

Publication of the first book of the Uilta alphabet is one of the outstanding projects of the Development Plan, aimed at preserving the unique language and culture of the Northern Sakhalin peoples.

The Uilta language is on the brink of extinction: the number of native speakers is no more than 20 or 30 people. Until recently, other members of this group were having difficulty learning their native tongue. A Cyrillic–based script for the Uilta language was developed by a famous Japanese linguist, Professor Dziro Ikegami. In 1993, this project was approved by the Language Studies Institute of the Russian Academy of Sciences. It took a large team of scientists and native speakers several years to prepare the book of ABCs of the Uilta language. Preparing the book for publication proved equally challenging. For example, the Cyrillic script lacks certain characters that convey specific phonemes: this is why the developers of the electronic version had to come up with special software to replace the missing characters. The scientific community highly rated the ABC book's publication.

This is an excerpt from the conference recommendations from the authorities: 'Spread the positive experience of implementing the Development Plan… in the spheres of social, cultural and educational development of the indigenous minorities of the Sakhalin Oblast, which is shared by Sakhalin Energy, the Sakhalin Oblast Administration and the indigenous peoples.'

The first five–year Development Plan covering 2006 to 2010 envisaged annual financing for the development programmes for Sakhalin indigenous minorities of US$ 300,000. The Company stated that this Plan is the first of a series that will last for the duration of the Sakhalin-2 Project.

Progress reports of the Plan are published and widely circulated among representatives of Sakhalin indigenous minorities. Regular independent monitoring of the Plan by outside experts is envisaged. Monitoring reports are published on the Company's public website.

Development programmes under the Plan are implemented along the following lines:

- Social development
- Competitive mini grants
- Support of traditional economic activities.

Efforts along all three lines continued in 2009, factoring in the positive and negative feedback from the interim evaluation of the Plan conducted in 2008. The evaluation is available on the Company's website and has been circulated in areas densely populated by Sakhalin indigenous minorities.

From 2006 to 2009, Sakhalin Energy financed over 200 projects approved by the governing bodies of the Plan.

SIMDP Social development programme

Initial consultations preceding preparation of the Plan identified the need for social development programmes in support of education, health care and ethnic culture, which remains relevant. These programmes are implemented in close cooperation with the relevant departments of the regional authorities and district administrations, and educational, health care and cultural institutions.

Activities financed under the social development programme as part of the Development Plan include:

- Procuring equipment for remote paramedical and obstetrical stations in areas densely populated by indigenous minorities
- Setting up a mobile dental office
- Conducting medical checkups by airborne units in areas densely populated by indigenous minorities, to detect and treat diseases in a timely fashion by a multi–disciplinary team of doctors from the regional centre
- Providing additional university scholarships: tuition was paid for 140 students from Sakhalin indigenous minorities
- Focusing on the potential development of local organisations and communities; seminars and training sessions were held on a wide range of issues.

SIMDP Competitive mini-grants programme

One of the strategic goals of the Development Plan is for representatives of indigenous peoples to independently manage the plan or its separate programmes. In this context, the competitive programme of mini grants offers a way to achieve this goal. As one step towards this goal, all funding decisions for mini grants are made by the Council of the Mini-Grants Fund, staffed exclusively by representatives of the Sakhalin indigenous minorities.

The objective of the popular annual mini-grant competitions is to encourage and support initiatives and proposals from representatives of

Implementing the Development Plan continues to interest the Russian national authorities and the Russian and international communities, reflected in these events and activities in 2009:

• In April 2009, the 6th Congress of Indigenous Minorities of the North, Siberia and the Far East of the Russian Federation gave Sakhalin Energy a laureate for the Vitus Bering international prize in the category, Best Industrial Company. The prestigious award was established by the Association of Indigenous Minorities of the North, Siberia and the Far East of the Russian Federation and the Batani Russo–Danish Foundation. The award comments on expresses appreciation to the partners of Sakhalin indigenous minorities that have made the greatest contribution to the socioeconomic and cultural development of these minority groups

• In October 2009, as part of the Development Plan, the State Duma of the Russian Federation hosted a photography exhibition titled, Sakhalin Indigenous Minorities to promote the unique culture and traditions of these minority groups. The United Nations Special Representative on Human Rights and Fundamental Freedoms of Indigenous People attended the event while on an official visit to Moscow. Also attending were the representatives of indigenous minorities of the North, specialised committees of the State Duma and the Federation Council, regional authorities, and the scientific community.

the indigenous peoples. The Mini-Grants Fund makes up 10% of the budget of the Development Plan.

SIMDP Programme to support traditional economic activities

Projects to revive the traditional economic activities of the indigenous population of the island are extremely important for preserving age–old traditions. Such programmes include a revival of Nivkhi dog breeding, assistance for the Uilta reindeer herders and support for communities of Sakhalin indigenous minorities.

The programme supporting traditional economic activities aligns with the goal of entrepreneurs among the indigenous peoples, who want to develop their businesses for the benefit of their communities. The programme is also designed to gradually increase the competitiveness of products made by the indigenous peoples.

Nivkhinka club: from generation to generation

The Nivkhinka Club was created over a decade ago at the Nogliki Museum of Local Studies. Two dozen like–minded individuals (the oldest is now over 80) rallied around the idea of preserving the national and cultural heritage of the Nivkhi.

A Nivkhi settlement was located on the shore of the Sea of Okhotsk in the Nyivo Bay until the mid–20th century. Eventually all the residents were resettled in the nearby community of Nogliki. The bay shore remains a favourite location for Sakhalin indigenous peoples to practice their traditional crafts. Members of the Nivkhinka Club live there for long periods in the summer and autumn. They come with their children, grandchildren and great grandchildren. Fishing, hunting sea animals, harvesting wild plants, sewing traditional clothing and footwear – all these skills are passed on to future generations of the Nivkhi.

One of the projects Sakhalin Energy finances to support traditional economic activities as part of the Development Plan is to establish a seasonal base for the Nivkhinka club at Nyivo Bay. This project involves buying boat motors and power generators and improving living conditions.

2010 PLAN

In 2010, Sakhalin Energy's major operating tasks will be to complete the transition of the commissioned facilities from trial operation mode to full–scale operations and to reach the scheduled performance level.

The LNG plant, the Piltun area of the Piltun–Astokhskoye field and the Lunskoye field are scheduled to reach their design capacity. The Astokh area reached its design capacity to producing hydrocarbons in 2009.

An important task to be performed at the final stage of the facilities commissioning is to fine–tune all the systems and equipment and to ensure complete synchronization of the complex infrastructure deployed by Sakhalin Energy. By completing this task, the Company will ensure reliable and efficient operation of all production processes.

The drilling programme to be carried out at the PA–B and LUN–A platforms is another Company priority. At the Piltun area, the Company will proceed with water injection to sustain formation pressure.

The Company will embark on a large–scale upgrading programme in 2010 for the Molikpaq platform

(PA–A), which has been operating for 10 years. The programme will enable the Company to build new wells from its first platform. A 4D seismic survey has been scheduled at the Astokh area to determine the area's current status after 10 years of operation, to plan new wells and eventually to improve oil recovery.

Large–scale construction required to ensure efficiency of the Project and to transfer facilities to full–scale operations is over. In 2010 the Company will complete construction and commission its BS 2. BS 2 will enable additional gas volumes to be transferred through the pipeline, thus boosting the LNG output.

As agreed, shortly Sakhalin Energy will pay royalty in the form of gas; it will also transfer entitlement gas of the Russian party under the PSA. To deliver the gas to Gazprom, which was appointed by the government to sell the Russian share in royalties and entitlement gas, the Company has to build two gas transfer terminals. Construction of the southern gas transfer terminal near Troitskoye village has already started. Sakhalin Energy expects major construction work to be completed by the end of 2010 to commission the gas transfer terminal in 2011 and to start gas supplies to the Yuzhno–Sakhalinsk thermal power plant. Construction of the northern gas transfer terminal near Boatasino settlement will be coordinated with Gazprom plans. The northern gas transfer terminal will transfer gas to the Sakhalin–Khabarovsk–Vladivostok pipeline under the Russian Far East gas supply programme.

The Company intends to continue with its environmental initiatives in 2010 and remains committed to socially responsible practices. The Company will also continue to be responsible for its HSE and social commitments and standards, as well as the transparency principle and the policy of open and efficient dialogue with stakeholders. Sakhalin Energy expects to become a global leader in these areas by maintaining compliance to the highest international standards or even setting new standards.

The Company expects to complete its HR motivation survey in 2010, and based on its findings, will take measures to improve the efficiency of its HR management, including improving procedures and guidelines. Later in the year, the Company plans to implement its corporate pension programme that was frequently discussed by Company personnel.

We also plan in 2010 to broaden anti–bribery and corruption efforts and enforce the 'Anti–Bribery and Corruption Procedure' that was developed in accordance with our business principles and Code of Conduct.

In social investment and sustainable development, we will continue giving top priority to social partnerships and socially–oriented initiatives. The Company will proceed with its partnerships, such as the Sakhalin Salmon Initiative, What to Do in Emergency Situations, and grant programmes within the allocated funds.

The Company will also finalise its second Sakhalin Indigenous Minorities Development Plan (SIMDP–2) in 2010, for the period 2011 to 2015. As part of this effort and in line with best international practices, a working group will be formed where the majority will be

representatives of Sakhalin indigenous minorities, and two rounds of large–scale and intensive consultations with all indigenous communities will be held. The SIMDP–2 will be developed and discussed within the framework of the World Bank Operational Directive 4.20 Indigenous Peoples.

Throughout 2010 and 2011, the Company will continue its participation in the UN international initiative testing of the Ruggie's principles, setting new standards for grievance management in business. The test results of the project will be used in developing recommendations for the global business community.

In summary, we will continue to perform scheduled operational and financial activities in accordance with our business principles and Sustainable Development Policy, the principles of UN Global Compact that we joined in November 2009, and to make efforts for further development in this area.

EXTERNAL REVIEW OF THE REPORT

This Sustainable Development Report has been developed in dialogue with Company stakeholders. After two rounds of dialogue with stakeholders during development of the report the Company decided to include answers and commitments for 2010 and beyond, and in the 2009 report add core issues of interest to the public. This feedback represents the initial stage of our external review.

Within three months after publication, the report will go through a process of external verification, a public review of corporate reports done at the highest professional level in the Russian Federation. The results will be presented to stakeholders in a timely manner.

The primary focus of our external review is on the substance and comprehensiveness of the Company performance information in the non–financial report,according to the principles of best and accountable business practices.

LIST OF ACRONYMS

AA1000SES	International Stakeholder Engagement Standard AA1000
ALARP	As Low As Reasonably Practicable
APR	Asian–Pacific Region
BAP	Biodiversity Action Plan
BS2	Booster Station 2 CEO Chief Executive Officer
CEO	Chief Executive Officer
CSR	Corporate Social Responsibility
EHSIA	Environmental, Health, and Social Impact Assessment
EMERCOM	Ministry for Civil Defence, Emergencies and Disaster Response
ERC	Emergency Response Committee
GRI	Global Reporting Initiative
GTT	Gazprom Transgaz Tomsk
HSE	Health, Safety, Environment
IFC	International Finance Corporation
IMO	International Maritime Organisation
INPO	Independent Non–Profit Organisation
IP	Sakhalin Indigenous Minorities of the North or Indigenous Peoples
ISO	International Organisation for Standardisation
IUCN	International Union for Conservation of Nature and Natural Resources
IVMS	In–Vehicle Monitoring System
LNG	Liquefied natural gas
LUN–A	LUN–A (Lunskoye) platform
MHMS	Minimum Health Management Standards
MNR	Ministry of Natural Resources
MPC	Maximum Permissible Concentration
MPE	Maximum Permissible Emission
OET	Oil Export Terminal
OPF	Onshore Processing Facility
OSR	Oil Spill Response
PA–A	Molikpaq (Piltun–A) platform
PA–B	Piltun–B platform
PMD	Pipeline Maintenance Depot
Prisco	Primorsk Shipping Corporation
PSA	Production Sharing Agreement
RAS	Russian Academy of Sciences
RTI	Road Traffic Incident
SIEC&LM	System for Industrial Environmental Control and Local Monitoring
SIMDP	Sakhalin Indigenous Minorities Development Plan
SP	Social Performance
SSI	Sakhalin Salmon Initiative
TEO	Feasibility Study (Technical and Economic Substantiation)
TLU	Tanker Loading Unit
UN	United Nations
WWF	World Wildlife Fund

APPENDIX 1:
GRI STANDARD DISCLOSURES (VERSION 3.0)

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
1. STRATEGY AND ANALYSIS					
Statement from the CEO	1.1	Introduction from the Chief Executive Officer	5-7	+	
Description of key impacts, risks and opportunities	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
A description of the significant impacts the organisation has on sustainability, and associated challenges and opportunities	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
An explanation of the approach to prioritizing these challenges and opportunities	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
Key conclusions about progress in addressing these topics and related performance in the reporting period	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
A description of the main processes in place to address performance and/or relevant changes	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
A description of the most important risks and opportunities for the organisation arising from sustainability trends	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
Prioritization of key sustainability topics as risks and opportunities according to their relevance for long–term organisational strategy	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
Table(s) summarizing: Targets, performance against targets, and lessons learned for the current reporting period	1.2	Introduction from the Chief Executive Officer Introduction	5-7 12-14	+	
Outlook on the organisation's main challenges and targets for the next year and goals for the coming 3–5 years	1.2	Introduction from the Chief Executive Officer Introduction. 2010 plans	5-7 12-14 78	+	
Concise description of governance mechanisms in place to specifically manage these risks and opportunities, and identification of other related risks and opportunities	1.2	Managing non-financial risks in health, safety, environment and social issues	44-46	+	

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
2. ORGANISATIONAL PROFILE					
Name of the organisation	2.1	About Sakhalin Energy	16	+	
Primary brands, products, and/or services	2.2	About Sakhalin-2	18-19	+	
Operational structure of the organisation, including main divisions, operating companies, subsidiaries, and joint ventures	2.3	Management structure	17	+	
Location of headquarters	2.4	Management structure	17	+	
Number of countries where the organisation operates, and names of countries with either major operations or that are specifically relevant to the sustainability issues covered in the report	2.5	About Sakhalin-2	18-19	+	
Nature of ownership and legal form	2.6	Management structure	17	+	
Markets served (including geographic breakdown, sectors served, and types of customers/beneficiaries)	2.7	About Sakhalin-2 Project Implementing plans to produce and export hydrocarbons	18 35-36	+	
Scale of the reporting organisation (number of employees, net sales, total capitalization, quantity of products or services provided, total assets, beneficial ownership (including identity and percentage of ownership of largest shareholders, breakdowns by country/region sales/revenues that make up 5 percent or more of total revenues; Costs by countries/regions that make up 5 percent or more of total revenues; and number of employees)	2.8	Social and economic benefits of Sakhalin-2 Project for the Russian Federation and Sakhalin oblast Main production and business achievements, Human resources management and development, Social investment and contribution to regional sustainable development	27-37 35-37 63-64 70-71	+	

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Significant changes during the reporting period regarding size, structure, or ownership	2.9			+	No significant changes in scope, structure and ownership in 2009
Awards received in the reporting period	2.10	About Sakhalin-2 Project, Essential completion and status of facilities, Approaches to HR Management and HR Policy, Social investment and contribution to regional sustainable development	20 30 32 62 70-77	+	
3. REPORT PARAMETERS					
REPORT PROFILE					
Reporting period for information provided	3.1	About the report	8	+	
Date of most recent previous report (if any)	3.2	Introduction	13-14	+	
Reporting cycle	3.3			+	Annual
Contact point for questions regarding the report or its contents	3.4	About the report	8	+	
REPORT SCOPE AND BOUNDARY					
Process for defining report content	3.5	Definition of report contents	8-10	+	
Boundary of the report	3.6	Definition of report boundaries	11	+	
State any specific limitations on the scope or boundary of the report	3.7	Definition of report contents, Definition of report boundaries	8-11	+	
Basis for reporting on joint ventures, subsidiaries, leased facilities, outsourced operations, and other entities that can significantly affect comparability from period to period and/or between organisations	3.8	Definition of report boundaries	11	+	
Data measurement techniques and the bases of calculations, including assumptions and techniques underlying estimations applied to the compilation of the indicators and other information in the report	3.9	Definition of report contents, Report Quality Assurance	10-11	+	

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Explanation of the effect of any re–statements of information provided in earlier reports, and the reasons for such re–statement	3.10			–	This report is the first one prepared in accordance with GRI standards
Significant changes from previous reporting periods in the scope, boundary, or measurement methods applied in the report	3.11			–	This report is the first one prepared in accordance with GRI standards
GRI CONTENT INDEX					
Table identifying the location of the Standard Disclosures in the report	3.12	GRI standard disclosures (version 3.0)	81-92	+	
ASSURANCE					
Policy and current practice with regard to seeking external assurance for the report	3.13	External review of the report	79	+	
4. GOVERNANCE, COMMITMENTS, AND ENGAGEMENT					
GOVERNANCE					
Governance structure of the organisation, including committees under the highest governance body responsible for specific tasks, such as setting strategy or organisational oversight	4.1	Management structure	16-17	+	
Indicate whether the Chair of the highest governance body is also an executive officer (and, if so, their function within the management of the organisation and the reasons for this arrangement)	4.2			+	The Chair of the highest governance body is not an executive officer
For organisations that have a unitary board structure, state the number of members of the highest governance body that are independent and/or non–executive members	4.3	Management structure	16	+	
Mechanisms for shareholders and employees to provide recommendations or direction to the highest governance body	4.4	Company's mission, core values and business principles. Corporate culture	19-22	+	
Linkage between compensation for members of the highest governance body, senior managers, and executives (including departure arrangements), and the organisation's performance (including social and environmental performance)	4.5			+	There is a unified compensation system acting in the Company based on performance evaluation (including social environmental performance)

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Processes in place for the highest governance body to ensure conflicts of interest are avoided	4.6	Company's mission, core values and business principles. Corporate culture	19-22	+	Avoiding any conflict of interests with regulative authorities/committees have been stipulated in the shareholders agreement
Process for determining the qualifications and expertise of the members of the highest governance body for guiding the organisation's strategy on economic, environmental and social topics	4.7			+	One single system of competence evaluation acting in the Company
Internally developed statements of mission or values, codes of conduct, and principles relevant to economic, environmental, and social performance and the status of their implementation	4.8	Company's mission, core values and business principles	19-21	+	
Procedures of the highest governance body for overseeing the organisation's identification and management of economic, environmental, and social performance, including relevant risks and opportunities, and adherence or compliance with internationally agreed standards, codes of conduct and principles	4.9	Company's mission, core values and business principles	21	+	
Processes for evaluating the highest governance body's own performance, particularly with respect to economic, environmental and social performance	4.10			+	Performance evaluation by the highest governance body takes into consideration economic, environmental, and social performance achieved against the planned performance indicators (on issues management)
COMMITMENTS TO EXTERNAL INITIATIVES					
Explanation of whether and how the precautionary approach or principle is addressed by the organisation	4.11	Hazards and risk management	45	+	
Externally developed economic, environmental and social charters, principles, or other initiatives to which the organisation subscribes or endorses	4.12	Introduction from the Chief Executive Officer	6	+	In November 2006 the Company joined Global Agreement of UN. The Company complies with international environmental, safety and labour protection, and social standards. These standards have been captured in HSESAP which is publicly available and put on the Company's public website

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Memberships in associations (such as industry associations) and/or national/international advocacy organisations in which the organisation has positions in governance bodies	4.13			+	The Company is a member of Russian network of the Global Compact of UN
STAKEHOLDER ENGAGEMENT					
List of stakeholder groups engaged by the organisation	4.14	Definition of report contents, Stakeholder engagement strategy and principles	9 38	+	
Basis for identification and selection of stakeholders with whom to engage	4.15	Stakeholder engagement strategy and principles	38	+	
Approaches to stakeholder engagement, including frequency of engagement by type and by stakeholder group	4.16	Stakeholder engagement strategy and principles	38	+	
Key topics and concerns that have been raised through stakeholder engagement, and how the organisation has responded to those key topics and concerns, including through its reporting	4.17	Appendix 2 *Sakhalin Energy answers and commitments as part of the dialogue with stakeholders while development of the 2009 social development report*	93-103	+	The detailed annual report on public consultations and issues manraised agement is available on the Company's web site
5. MANAGEMENT APPROACH AND PERFORMANCE INDICATORS					
ECONOMIC					
Disclosure on management approach		About Sakhalin Energy	16-21	+	
ASPECT: ECONOMIC PERFORMANCE					
Direct economic value generated and distributed, including revenues, operating costs, employee compensation, donations and other community investments, retained earnings, and payments to capital providers and governments	EC1	Social and economic benefits of Sakhalin-2 Project for the Russian Federation and Sakhalin Oblast, Social investment and contribution to regional sustainable development	24-25 70-77	+	

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Coverage of the organisation's defined benefit plan obligations	EC3			–	Final decision on corporate pension programme is expected in 2010, this question was asked by Company's staff
Significant financial assistance received from government	EC4			+	The Company did not get any financial support from the State in 2009
ASPECT: MARKET PRESENCE					
Procedures for local hiring and proportion of senior management hired from the local community at locations of significant operation	EC7	General, HR training and development	62-63 68-69	+	
ASPECT: INDIRECT ECONOMIC IMPACTS					
Development and impact of infrastructure investments and services provided primarily for public benefit through commercial, in kind, or pro bono engagement	EC8	Social and economic benefits of Sakhalin-2 Project for the Russian Federation and Sakhalin Oblast. Social investment and contribution to regional sustainable development	23-26 70-77	+	
Understanding and describing significant indirect economic impacts, including the extent of impacts	EC9	Social and economic benefits of Sakhalin-2 Project for the Russian Federation and Sakhalin Oblast	23-26	+	
ENVIRONMENTAL					
Disclosure on management approach		Policy Goals and performance Biodiversity Training and awareness Monitoring and follow–up	48 50-61 61	+	
ASPECT: WATER					
Total water withdrawal by source	EN8	Industrial environmental monitoring	49-50	+	
Water sources significantly affected by withdrawal of water	EN9	Industrial environmental monitoring	49-50	+	No water sources significantly affected by withdrawal of water

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
ASPECT: BIODIVERSITY					
Description of significant impacts of activities, products, and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas	EN12	Biodiversity	50-61	+	
Habitats protected or restored	EN13	Biodiversity	50-61	+	
Strategies, current actions, and future plans for managing impacts on biodiversity	EN14	Biodiversity	50-61	+	
ASPECT: EMISSIONS, EFFLUENTS AND WASTE					
NO_X, SO_X, and other significant air emissions by type and weight	EN20	Waste management	50	+	
Total water discharge by quality and destination	EN21	Waste management	49-50	+	
Total weight of waste by type and disposal method	EN22	Waste management	49-50	+	
ASPECT: PRODUCTS AND SERVICES					
Initiatives to mitigate environmental impacts of products and services, and extent of impact mitigation	EN26	Biodiversity	47-61	+	
Percentage of products sold and their packaging materials that are reclaimed by category	EN27			–	This indicator is not applicable for the Company considering its scope of activities
SOCIAL					
LABOUR PRACTICES AND DECENT WORK					
Disclosure on management approach		Approaches to HR management and HR policy	62	+	
ASPECT: EMPLOYMENT					
Total workforce by employment type, employment contract, and region	LA1	General	62-63	+	
Total number and rate of employee turnover by age group, gender, and region	LA2	General	62-63	+ -	Information on staff flow is included in the report

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
ASPECT: LABOUR AND MANAGEMENT RELATIONS					
Percentage of employees covered by collective bargaining agreements	LA4			+	There are no collective agreements.
Minimum notice period(s) regarding operational changes, including whether it is specified in collective agreements	LA5			+	In accordance with Russian labour code (not less than 2 months)
ASPECT: OCCUPATIONAL HEALTH AND SAFETY					
Rates of injury, occupational diseases, lost days, and absenteeism, and number of work–related fatalities by region	LA7	Labour safety and protection	63-64	+	
Education, training, counseling, prevention, and risk–control programmes in place to assist workforce members, their families, or community members regarding serious diseases	LA8	Protecting the health of personnel	65	+	
Health and safety topics covered in formal agreements with trade unions	LA9			+	No agreements with trade unions.
ASPECT: TRAINING AND EDUCATION					
Average hours of training per year per employee, by employee category	LA10	HR training and development	68	+ –	The information on employees trained is included in the report.
Programmes for skills management and lifelong learning that support the continued employability of employees and assist them in managing the end of their career	LA11	HR training and development	68-69	+	
Percentage of employees receiving regular performance and career development reviews	LA12			+	100%
ASPECT: DIVERSITY AND EQUAL OPPORTUNITY					
Composition of governance bodies and breakdown of employees per category according to gender, age group, minority group membership, and other indicators of diversity	LA13			+	As of the end of 2009, the Company employed 982 Sakhalin residents, 141 of whom held executive positions. The percentage of Russian nationals in the Company's personnel is expected to reach 90 per cent over the next few years. As regards executive positions, 264 of them (or 64 per cent) were held by Russian citizens in 2009; 67 executives being women. By 2018, the percentage of Russian executives is expected to hit the 75 per cent level. In 2009, the average age of the Company's employees was 36 years. People below 35 years of age account for two–thirds of the Company's payroll.

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Ratio of basic salary of men to women by employee category	LA14			+	Basic salaries of man and women do not differ
HUMAN RIGHTS					
Disclosure on management approach		Company mission, core values and business principles. Community grievance procedure	19-22 41	+	
ASPECT: INVESTMENT AND PROCUREMENT PRACTICES					
Total hours of employee training on policies and procedures concerning aspects of human rights that are relevant to operations, including the percentage of employees trained	HR3			+ –	100 % of employees are trained on business principles of the Company
ASPECT: NON–DISCRIMINATION					
Total number of incidents of discrimination and actions taken	HR4			+	No registered cases of discrimination during the reporting period.
ASPECT: FREEDOM OF ASSOCIATION AND COLLECTIVE BARGAINING					
Operations identified in which the right to exercise freedom of association and collective bargaining may be at significant risk, and actions taken to support these rights	HR5			+	No operations identified in which the right to exercise freedom of association and collective bargaining may be at significant risk
ASPECT: CHILD LABOUR					
Operations identified as having significant risk for incidents of child labour, and measures taken to contribute to the elimination of child labour	HR6			+	No operations identified involving child labour

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
ASPECT: FORCED AND COMPULSORY LABOUR					
Operations identified as having significant risk for incidents of forced or compulsory labour, and measures to contribute to the elimination of forced or compulsory labour	HR7			+	No operations identified involving forced or compulsory labour
ASPECT: INDIGENOUS RIGHTS					
Total number of incidents of violations involving rights of indigenous people and actions taken	HR9			+	No registered cases of violation of rights of indigenous people and actions taken
SOCIETY					
Disclosure on management approach		Stakeholder engagement strategy and principles Company principles and approaches to social investment and sustainable development	38 70	+	
ASPECT: COMMUNITY					
Nature, scope, and effectiveness of any programmes and practices that assess and manage the impacts of operations on communities, including entering, operating and exiting	SO1	Social investment And contribution to regional sustainable development	70-77	+	
ASPECT: CORRUPTION					
Percentage of employees trained in the organisation's anti–corruption policies and procedures	SO3			+	Prevention of corruption is one of the basic components of Company's Code of Conduct. For 2010 we plan to reinforce preventive measures against bribery and corruption and will adopt the Anti–bribery and Corruption Procedure in Sakhalin Energy which has been developed in accordance with our General Business Principles and Code of Conduct

Aspect	Index GRI	Report clause	Page	Disclosure	Comments and references to other sources
Actions taken in response to incidents of corruption	SO4			+	Prevention of corruption is one of the basic components of Company's Code of Conduct. For 2010 we plan to reinforce preventive measures against bribery and corruption and will adopt the Anti–bribery and Corruption Procedure in Sakhalin Energy which has been developed in accordance with our General Business Principles and Code of Conduct
ASPECT: PUBLIC POLICY					
Total value of financial and in–kind contributions to political parties, politicians, and related institutions by country	SO6			+	No registered cases. The Company does not support any political parties
PRODUCT RESPONSIBILITY					
Disclosure on management approach		Company mission, core values and business principles	20	+	
ASPECT: CUSTOMER HEALTH AND SAFETY					
Life cycle stages in which health and safety impacts of products and services are assessed for improvement, and percentage of significant products and services categories subject to such procedures	PR1			+	Impact on health and safety of production and services are evaluated according to Russian legislation requirements applied in the Company

APPENDIX 2: SAKHALIN ENERGY'S ANSWERS AND COMMITMENTS AS PART OF ITS DIALOGUE WITH STAKEHOLDERS FOR DEVELOPMENT OF THE 2009 SUSTAINABLE DEVELOPMENT REPORT

While developing the 2009 non–financial report, the Company conducted two rounds of dialogue with stakeholders. The dialogues were done in accordance with the Company's principles and international standards.

In November 2009, the Company held the first round of dialogue with stakeholders aimed at listening and listing all their expectations and recommendations in the report. The participants of this dialogue were the representatives of local and regional NGOs including those with a social or environmental focus, the indigenous peoples of Sakhalin, officials, and many other groups.

In addition to this first round of the dialogue, the Company met with representatives of international environmental NGOs in December 2009, during the Western Gray Whales Advisory Panel in Geneva.

In April 2010, the Company held the second round of the dialogue with stakeholders, aimed at providing answers to the questions and suggestions voiced during the first round of dialogue. The Company's commitments and answers to the questions were distributed beforehand to the participants of the dialogue.

The table that lists the questions raised at these meetings, along with the Company's answers to them, is provided below. The questions are placed in the left–hand side, in the order in which they were raised at the meetings. The answers to the questions are placed on the right–hand side. The answers include both those provided at the first round of dialogue in November 2009 and later, for those questions requiring additional study.

The answers were provided by relevant specialists of the Company. The text is just a summary of the Company's position related to the question or issue. Detailed information can be obtained from this report or from other public sources, such as Sakhalin Energy's website, and documents available in the public domain.

No.	Comment, question or pointed remark	Company reply
Yury Ivanovich Andreev, Deputy Chairman of the Regional Council of Veterans		
1	'For whom is the report intended? Is the report intended for internal use?'	Clarification on the report audience is included in the report (see Section *Introduction from the Chief Executive Officer*).
2	'Who will assess the report?'	The report will go through a professional certification process of an authorised and qualified specialist organisation, which will provide an independent assessment (see Section *External review of the report*).
3	'Is the report mandatory?'	The report is not mandatory, it is a voluntary initiative of the Company.
Alla Ivanovna Gafner, Chairman of Stroitel gardening community council		
4	'Gardening land plots are located 1 km from the LNG plant. I have been in contact with the Company for six years, asking for resettlement. Forty senior citizens live in this area. 'We are concerned about the way LNG plant impacts vegetation. We are too close to the plant and our plants and soil are covered with hazardous stuff. 'I consulted with a Rospotrebnadzor specialist and received a confirmation that Sakhalin Energy had created a sanitary protection zone. In 2000, a sanitary protection zone of size 1 km was set by the Chief Medical Officer of Russia. After that, the TEO project was carried out, in 2003, according to the TEO, the zone was 3.5 km wide. But now Sakhalin Energy refers to the fact that the Chief Medical Officer of Russia had set the zone with a size of 1 km.'	The environmental impact of the Prigorodnoye Production Complex is limited by the size of the sanitary protection zone (SPZ) set for this industrial facility in accordance with the RF legislation. According to Item 2.14 of SanPiN 2.2.1/2.1.1 1200–03 Sanitary protection zones and sanitary classification of enterprises, erections and other facilities, the SPZ width for facilities not included in the sanitary classification as well as comprising new technologies which have no domestic analogues is set for each particular case, based on the decision of the RF Chief Medical Officer or his deputy. For the LNG plant and the oil export terminal (hereafter 'the OET') in the Prigorodnoye Port, S.I. Ivanov, the Deputy Chief State Medical Officer of Russia, set the SPZ size as 1,000 m from emission sources (letter dated 16 July 2002). The SPZ size data (3,500 m) was given as an expert opinion regarding a possible variant. Due to that, this value cannot be taken as the approved SPZ size. The legitimacy of taking 1,000 m as the SPZ size for the LNG plant/the OET has been checked many times by the office of the Sakhalin inter–district Prosecutor's Office for Environmental Protection. No violations of existing legislation have been observed. It should be noted that in 2009, based on the instruction of the Federal Supervision Agency for Customer Protection and Human Welfare (Rospotrebnadzor), the Research and Development Institute named after Sysin, which is a State Enterprise, performed a hygienic assessment of the materials in the Inventory Report and the Draft MAE Limits for the Atmospheric Air Emission Sources of the LNG Plant /the OET in the Prigorodnoye Port, Korsakov District, and Sakhalin Oblast. and reissued expert conclusion No. 5. EKZ 2/09, of 14 January 2009, that confirmed the calculated SPZ set at 1,000 m in 2002.

No.	Comment, question or pointed remark	Company reply
5	'The Company offered a compensation package of 100,000 rubles, but it is impossible to buy a land plot with this money. The current prices for the land plots are 700,000 to 800,000 rubles.'	The compensation package was set out by the Company in 2006 and endorsed in 2006/2007 in the course of consultations with the members of Stroitel non–commercial gardening community. A professionally licensed appraiser participated in the elaboration of the compensation package to determine the market price of plots of land. The results of the appraiser's work were not disputed by the stakeholders in the course of creating the compensation package. The assessment was carried out in accordance with the size and nature of particular land plots, and in accordance with appraisal standards and the requirements of existing legislation. As a result of the independent assessment, the average market price of a site in the Stroitel non–commercial gardening community in 2006 was 212,569 rubles. In 2005, the sociological laboratory of the Sakhalin State University performed a study, Assessment of the Parameters of Potential Loss of Value for Gardening Land Plots in Stroitel Non–Commercial Gardening Community in the Prigorodnoye, Korsakov District, due to Construction of the LNG Plant. Within the framework of this study, a price comparison between land plots in the Korsakov (Pervaya Pad, Vtoraya Pad, Tretiya Pad, Nechaevka and Prigorodnoye) and Aniva Districts was carried out. According to the study results, the price of land plots in the Korsakov District in the period of 2003/2005 was 54,109 rubles (maximum price – 125,120 rubles, minimum price – 6,000 rubles). So the amount of compensation offered by the Company was sufficient for purchasing similar land plots in the Korsakov District [Korsakov City District] in the period when the compensation package was offered. According to the Company information, those who wished purchased similar land plots (moreover, some of them had better characteristics), including in the Vtoraya Pad. In summary, we believe that at present the Company has fulfilled and continues to fulfill all its responsibilities to the Stroitel non–commercial gardening community. There is no legal justification for resettlement of the community's members. The Company plans to continue engaging with the community within the framework of effective Russian legislation.
6	'The Company performs air and noise monitoring, but doesn't use expensive chemicals which could reveal negative environmental impact factors (nitrogen dioxide, benzopyrene, formaldehydes, etc.)'	At the request of the owners of the gardening land plots, since 2005 the Company has been continually monitoring the ambient air quality and noise level on the territory of the Stroitel non–commercial gardening community during the summer season from May to October. During the observational period, not a single case of pollutant levels exceeding the maximum permissible concentration was registered in the air or concerning noise level. Monitoring is performed by a licensed organisation, Gydromet, according to the RF–stated rules and standards. Studies of soils, agricultural and gardening production performed by the Company in 2006/2007 by the Sakhalin Research and Development Institute for Agriculture did not reveal any impact on the crops or soil or any deviations from the specified standards. Therefore, arguments concerning the negative impact of emissions generated by the activities of Prigorodnoye Production Complex, used by the members of Stroitel non–commercial gardening community, are of a subjective character and are not confirmed by the results of ambient air quality and noise monitoring. Carrying out an inventory of emission sources and developing a MAE (maximal allowable emissions) volume include identifying a list of substances which may be present in the output of the facility. The emission volume of all identified substances is controlled according to calculations for compliance with the standards approved by the Sakhalin branch of the Federal Environmental, Engineering and Atomic Supervision Service. The preparation of the programme for monitoring the emissions impact on the ambient atmospheric air quality considers those substances that contribute most of all to pollution together with carcinogenic substances. All calculations and assessments for identifying the list of substances present in the plant's emissions are carried out in accordance with the existing regulatory documents and method recommendations.

No.	Comment, question or pointed remark	Company reply
7	'The Company invested US$ 50,000 towards equipping the co–operative with necessary facilities. But the land owners refused, since they think that they need resettling rather than modernisation of their co–operative.'	The Company offered to invest US$ 50,000 in the target social investment programme, which should have been aimed at improving the co–operative infrastructure, in accordance with the recommendations by members. That proposal was not supported by the co–operative's members. Concerning justification for re–settling, see the Company answer above, question No. 5.
Vladimir Ivanovich Vorontsov, Chairman of the Committee for Economic Development, Sakhalin Oblast Duma		
8	'This meeting is a good example of communication between business, authorities and society. 'Sakhalin-1 and Sakhalin-2 Projects as well as further offshore development are important for the region. These projects will contribute to the development of the economy, budgetary recharge, and the development of infrastructure, community, young people and business. 'However, the society is concerned with the state of the environment, we appreciate that the Company takes steps to mitigate its environmental impact: pipeline route change, compensation for damages, investing funds in ecological activities, and so on.'	Information about the Sakhalin-2 Project significance and advantages is included in the report (see Section *Social and economic benefits of Sakhalin-2 project for the Russian Federation and Sakhalin Oblast*). In addition, the report covers activities aimed at environmental protection and ecological monitoring (see Section *Environment protection, ecological and industrial safety*).
9	'I suggest that the audience of such meetings should be increased.'	This will be taken into account during the preparation of the 2010 Company report.
10	'I suggest that the format created within the Company together with its attention to environmental problems should be continued in the future.'	The Company will continue its commitment regarding environmental safety and will adhere to the accepted standards of environmental protection and other issues. This is supported by all shareholders of the Company.
11	'It is necessary to pay more attention to the training of local specialists and to supporting our university, to establish a good, solid oil and gas faculty in collaboration with other operators.'	The Company is implementing several programmes aimed at developing and training local specialists. They include: an educational grant programme, internship programme, and the founding and supporting of a Chair of Sustainable Development at Sakhalin State University, and others. Information on this area of activities is included in the report (see Section *HR training and development*).
Aleksander Vladimirovich Romanov, First Deputy Minister of Natural Resources and Environmental Protection of Sakhalin Oblast/Head of Subsoil Use Administration		
12	'The Sakhalin Oblast Administration has a high opinion of the socio-economic achievements and initiatives of the Company. 'I suggest including in the report the following information: Russian Content, attracting Russian and, primarily Sakhalin-based companies to work on the Project, training workshops carried out by the Company with the participation of Russian companies. 'I also suggest that you include in the report individual cases of Sakhalin companies created from scratch, which then developed and have now become leading companies.'	Information on the Project significance and advantages are included in the report (see Section *Social and economic benefits of Sakhalin-2 project for the Russian Federation and Sakhalin Oblast*). Fulfilment of the requirements for Russian Content is a necessary condition, according to the Production Sharing Agreement, and a priority for Sakhalin Energy. Information on Russian Content and the relevant strategy is included in the report (see Section *Russian content*). Information about the training workshops for Russian companies together with examples of the participation of Sakhalin enterprises are included in the report (see Section *Russian content*). In addition, information on the workshops and examples of the participation of Russian (including Sakhalin-based) companies in the Project are available on the Company public web site.

No.	Comment, question or pointed remark	Company reply
13	'I suggest including in the report information on educational activities, information on the Company's training of its personnel, how many people have been trained, including courses for technicians. It would be interesting to know which areas you intend to tackle in the future according to your plans. I also suggest you covering personnel training work in collaboration with other operators; it is necessary to talk about the activities of the main shareholder in this area, which uses the resources of its educational institutions.'	Personnel training is a priority area for development. Information about the training of personnel, with statistics, and planned areas of development are included in the report (this includes the training of specialists and combined efforts with shareholders) (see Section *HR development and training*).
Natalya Mikhailovna Trefilova, Head of the Representative Office of the Kidsave International, Yuzhno-Sakhalinsk		
14	'I would like to thank the Sustainable Development Fund, since without it Kidsave could not exist. It's a pity that the presentation [during the meeting] did not include information on the work carried out on the adoption of orphans by families; a great deal of money has been spent on that.'	Information has not been included in the report, since the Company didn't collaborate with Kidsave on the projects realised by it in the reporting period (2009 report). Nevertheless, the Company appreciates such a response, it is proud that its participation within the framework of the Sustainable Development Fund has contributed towards the establishment and sustainable development of the significant social activities of this organisation.
15	'The activities of the Company management in the field of social projects are remarkable. I suggest that the Company administration should think about supporting Company employees who volunteer in charitable activities.'	Since 2007, the Company has been realising a programme to support the charitable initiatives of its employees. This programme anticipates co-investment in charitable activities organised by employees. Information on the programme is included in the report (see Section *Programme to support volunteer employees charitable initiatives*).
16	'During contracts awarding, it is necessary to track the social activities of the bidders, potential contractors. That is, to take into account the level of social activity of the company when signing contracts.'	According to Company procedures, each potential contractor should demonstrate high standards in the areas of health, environment and safety, thus demonstrating its social responsibility in carrying out its business activities.
17	'A differential approach to non–commercial organisations (NCOs). According to our information, the Company works with 10 NCOs. The interests of NCOs should be taken into account in making results more effective. For example, the Programme 'Small Grants – Big Deeds'. The money within this programme must not be assigned to administrative needs or personnel. But we are a fully non–commercial organisation, while there are some who partially perform commercial activities and can at least pay salaries to their personnel. As for us, we need to find another job to continue our work on the project during our free time and at weekends. It is necessary to consider the possibility of diversifying the invested funds; for example, it could be not simply a grant, but a compensation of some fixed sum. It might be for expenditures on the salaries and wages of specialists. Recommendations could be written down in the provision for awarding grants, so that the applicant will have the possibility of gaining a certain share from the Project, in order to assign it to administrative needs (wages).'	Non–commercial organisations function as partners and initiators of the greater part of social projects budgeted by the Company. Budgeting for the implementation of social projects that have passed the bid selection is carried out within the framework of the programme 'Small Grants – Big Deeds'. This programme does not provide for the possibility of compensation for the wage expenditures of the participants. This principle will be kept, since the concept of such programmes excludes the mentioned possibility. However, budgeting for a part of the expenditures on wages of the programme participants may be included in the major long–term partnership programmes implemented by the Company or handed over for external or combined administration, such as for the Sakhalin Salmon Initiative, and the Sakhalin Indigenous Minorities Development Plan.

No.	Comment, question or pointed remark	Company reply
18	'We would like to thank you for the simple and convenient method of applying for these grants as well as for the simple and convenient reporting mechanism.'	The Company appreciates this opinion.
Yuri Ivanovich Andreev, Deputy Chairman of the Regional Council of Veterans		
19	'I would like to support this proposal. i.e. the possibility of assigning a share of the grant to the wages of those who will work on that grant.'	The Company's answer see above, question 17.
Natalia Aleksandrovna Lisitsyna, Vice Chairman of Sakhalin Environmental Watch RPO (regional public organisation) Council		
20	'I suppoprt the statement of A.I. Gafner on the Sanitary Protection Zone, re–settlement and the compensation package value.'	The Company's answer see above, question 4.
21	'Why is vegetation monitoring not being carried out?. Vegetation is sensitive to pollution. There is such a thing as 'hygienic and ecological standards.'	Studies of soils and agricultural and gardening production carried out by the Company in 2006/2007 by the Sakhalin Research and Development Institute for Agriculture did not reveal any impact on crops or soil or any deviations from the specified standards. The studies were carried out once and will be continued only if deviations in air quality are identified. Since 2005, the Company has been carrying out continual monitoring of the ambient air quality in the area of the gardening non–commercial community 'Stroitel' during the summer season, from May to October. During the period of observations, not a single case of pollutant levels exceeding the maximum permissible concentration values was registered in the air or concerning noise level on the territory of the gardening non–commercial community 'Stroitel.'
22	'I suggest including in the report information on drilling wastes, on their quantitative and qualitative ratio (what is discharged, what is transported).'	The Company pays particular attention to waste management issues, including drilling wastes. Information on waste management is included in the report (see Section *Waste management*).
23	'Reinstatment along the pipeline's route. You've mentioned that work on the elimination of problems related to cyclones has been completed. We carried out our own checks from May to October, and the problems were still in place. The Watch (Sakhalin Environment Watch) has a full list of problem sites. Besides, biological reinstatement has not yet been carried out everywhere, although the pipeline is already being operated.'	Information on the elimination of problems related to cyclones in 2009 is included in the report (see Section *Restoring the onshore pipeline right of way*). Biological reinstatement along the pipeline's route has been completed. Information on reinstatement and the relevant monitoring programme are included in the report (see Sections *Restoring the onshore pipeline right of way* and *Terrestrial ecosystems*).
24	'I suggest including in the report data on oil spills for the reporting period.'	Information on oil spills is included in the report (see Section *Goals and performance*).
25	'How and why are the facilities operated, if a permit to operate has not been issued by Rostekhnadzor? You may say, of course, that commissioning works continue, but the fact is that the facility is being operated at full capacity.'	The Company performs its activities according to RF regulatory standards, including those related to the commissioning works and operation of facilities. Information on this matter is included in the report (see Section *Transfer to full operation*).

No.	Comment, question or pointed remark	Company reply
Lidia Nikolaevna Yevdokimova, Deputy Head of Korsakov Municipal District, Head of the Department for Social Development		
26	'In 2009, contributions to Korsakov's budget were the lowest. 'It is necessary to pay more attention to social investments in Korsakov town.'	Contributions to the budgets of different levels, related to the Company's activities, are regulated by Russian legislation. The social investments volume is not connected with tax payments, but is rather determined in communication with the Russian party and the Company's shareholders.
27	'The proposal is to review the composition of the Korsakov Partnership Council for Sustainable Development for 2010 in relation to changes in the composition of the Regional Assembly and the course of our life.'	The Korsakov Partnership Council is at the stage of reorganisation. The proposal has been accepted. In 2010, the Council will resume its work in the new format.
Sergei Mikhailovich Pervukhin, Chairman of Piligrim Tourist Regional Club NGO		
28	'It is necessary to create an efficiency indicator system for the large social projects. Transparency of information on the large social projects is important. Where and how much money was directed, in order to see how effectively the money was spent and to understand the level of effectiveness of a particular project for the ecosystem of Sakhalin.'	A system of indicators for large projects has been developed and is being implemented by the Company. In addition, the web site of the Sakhalin Salmon Initiative (SSI) presents data on received funds and their use. The annual report on the breakdown of all expenditures is available for the public. The SSI Coordination Council controls SSI activities. This includes financial efficiency.
Lada Anatolievna Milchenko, Director of Rodnik Ecological Centre		
29	'I suggest including in the report information on the results of projects within the framework of the programme 'Small Grants – Big Deeds)'. It would be interesting to know how successful the projects were, what were the most interesting projects.'	Information on the grant programme 'Small Grants – Big Deeds', project participants and the most interesting projects is available on the Company's public web site. Information on the programme is included in the report (see Sections *Competitive corporate crogramme 'Small grants – Big deeds'* and *Educational grants programme*).
Elena Victorovna Raschupkina-Lopukhina, Head of Knowledge Is Power NGO		
30	'It is necessary to distinguish between social responsibility and philanthropy.'	Sustainable development projects and other social investment projects are included in a common concept of the Company's social responsibility. This principle is an integral component of the Company's business principles.
31	'It is necessary to analyse where funds were invested and their size. I guess that similar expenses could be reflected in many.'	The reports and other information materials of the Company on the distribution of funds between social investment projects and sustainable development projects demonstrate a clear distinction between the different groups of projects.
32	'It is necessary to analyse the failures and those aspects which need to be corrected. There were projects [in Korsakov district], that did not prove worthwhile. The causes of their failure should be analysed in order to avoid future mistakes. This question is not about money, but about the criteria used in approving projects, and who will be responsible for the results.'	When implementing the sustainable development and social investment projects, the Company conducts an analysis of positive as well as negative experiences in the implementation of these projects. The results of the analysis will be taken into account in the future as well, in particular, during the project approval process and interaction with those organisations that implement them. In addition, in July 2009 an independent expert in corporate social responsibility conducted an assessment of the Korsakov Partnership Council and the results of its work (projects) and came to certain conclusions about its strengths and weaknesses. The expert also made recommendations on ways to improve and modernise the Council's activity.

No.	Comment, question or pointed remark	Company reply
33	'What is the responsibility of those who make applications for the grants (if they can't implement the project adequately, and money is lost)? This aspect should be analysed and calculated.'	The contracts signed between the Company and organisations implementing the Project include an obligation on returning money by these organisations that is not properly spent.
34	'Compensation payments for the beach zone in the Prigorodnoye port. The money is quite substantial – about one million dollars. The decision was made to spend the money on a park development. The money has been spent, but there is no park. There is lighting equipment, there is asphalt, but there is no park.'	Construction of the LNG plant/the OET required the closure of the part of the beach in the Prigorodnoye port, which is a popular place of leisure for residents of the town of Korsakov and adjacent districts. Holiday–makers still use the rest of the beach for leisure purposes. As a compensation for the effect on the Prigorodnoye beach, the Company paid US$ 800,000 to the Korsakov District administration for reconstruction of the local park. This alternative was selected after a series of consultations and discussions with the administration and public of the town of Korsakov. An initiative group was established for discussion of the alternatives and decision–making. Sakhalin Energy has fulfilled its obligations. The park reconstruction process was completed in accordance with the agreed responsibilities. Moreover, in December 2007, due to a change in the US$/RUR exchange rate, Sakhalin Energy, on its own initiative, increased the sum from US$ 800,000 to US$ 930,000, which was appreciated by the local administration and the town residents. This asset is a municipal property, so all work was carried out under the control of the Korsakov administration. The Company regularly informed the public of Korsakov town about the progress and scope of work on the park's reconstruction.
35	'Flarings. The Company had promised in its announcements to complete all technological processes and to decrease the flare size to 2–3 m before March. But these promises were not fulfilled. The flare is again 60 m high, with kilometre tails. Reliable information would be desirable.'	The issue of flaring at the LNG plant during the operational stage is covered in the official announcements of the Company and in various informational materials, and it is available at meetings with the public. Additional information can be obtained at the request of interested parties.
36	'Independent experts are very cunning when preparing reports, and 'independent' experts can turn out to be very dependent ones. There is a list of things to be done, and they write that all this has been done, but all this has not been done in practice.'	Experts and independent auditors are selected according to the standard procedures of the Company. Contracts for the supply of materials and services are predominantly assigned according to a competitive bidding procedure. Some auditors are assigned by international credit organisations. If the Company's stakeholders have justifiable complaints relating to assessments given by these independent experts, please inform the Company.
37	'In summer, there was an incident with abandoned open warehouses (involving uncertain substances). I looked on the Company's web site for information, but it wasn't available, and it still isn't.'	Concerning the coverage of its activities, the Company follows the principles of transparency and availability. The Company uses various means to inform interested parties, including the Company's web site, mass media, public meetings, and so on. Regarding the volumes of the Project–related information, the Company's official web site covers aspects of the Company's activities, rather than the activities of its contractors or subcontractors. The incident in question was related to the activity of a subcontractor; that is why it wasn't presented on the web site, but the public was informed about it in due time through the mass media. This is the main channel of communication with the public in similar cases.

38	'I would recommend for other organisations that participate in the 'Small Grants – Bid Deeds' programme not to put salary payments in the application to the Company.'	The Company's answer – see above, question 17.
39	'Where it deals with social responsibility, let the report cover shortcomings as well as advantages.'	The report presents information on the implemented projects together with a brief analysis of positive and negative experiences (see Sections *Environmental protection, ecological and industrial safety* and *Social investment and contribution to regional sustainable development*).
Natalia Vladimirovna Kizimova, Manager of Sakhalin Salmon Initiative Educational Project		
40	'If it were not for the Company, the independent non–commercial organisation *The Sakhalin Salmon Initiative* and the programme would not exist.' She talked about the areas of SSI activities and gave several examples of this projects.	Information on the SSI programme is included in the report (see Section *Partner project: Sakhalin Salmon Initiative*).
Tatiana Petrovna Roon, Director of Sakhalin Regional Museum of Local Lore		
41	'Interaction between the Company and local Sakhalin indigenous minorities should be covered. 'It is necessary to cover interaction with reindeer herders (previous project).'	Information on interaction between the Company and local Sakhalin indigenous minorities is included in the report (see Section *Engaging Sakhalin indigenous peoples)*. Interaction between the Company and reindeer herders is frequently presented in the Company's annual report on information campaigns and public consultations. This report is available on the Company's public web site.
42	'Socio–cultural programmes remain outside the activities of the Company. In Japan the schoolchildren visit other towns in the country to see different cultural values as part of a cultural programme.'	The social investment and sustainable development projects implemented or financed by the Company include a lot of projects aimed at cultural and educational development: computer classes, publishing books and catalogues, projects aimed at the development and preservation of the national culture of local Sakhalin indigenous minorities. Information of these projects is included in the report (see Section *Social investment and contribution to the regional sustainable development*). At the stage of project review, the Company is ready to start a dialogue with cultural organisations, including the Regional Museum of Local History and Culture.
Reeves Randy, Chairman of Western Grey Whale Advisory Panel (WGWAP)		
43	'Russian attitude to environmental issues'. 'It is believed in the West that Russian companies do not pay due attention to the environmental issues. According to an opinion generally held, Shell, being the main shareholder of Sakhalin Energy, used to have a determining influence on the development of responsible policy in this respect, and there are some concerns that, as soon as a Russian company becomes the main shareholder, the opinion of the PSA Russian party will dominate. The Russian party of the PSA is known to be displeased with the expenses for environmental protection and profit loss; it is more interested in economic efficiency. There is a doubt that even if your Company has the best of intentions, the Russian party and the main shareholder will not give you a chance to implement them.'	The Company will continue to follow its commitment regarding the environmental and industrial safety and will adhere to the accepted standards of environment protection and other issues. This is supported by all shareholders of the Company.

No.	Comment, question or pointed remark	Company reply
44	'If the Company sets itself up as a responsible member of society, it would be good to discuss the Company attitude to the problems inherited from the historic industrial development of Sakhalin, as well as the Company's possible intentions to participate in their solution. We mean the impact of previous onshore oil developments, contaminated rivers, rusting pump jacks, etc.'	The Company is implementing the Sustainable Development Policy through the social investment programmes and sustainable development projects which enhance the social, economic and environmental development of the society and the territory of presence. In particular, from 2001 to 2009, Sakhalin Energy invested over US$ 600 million into rehabilitation of the island public infrastructure including: • construction of new roads • reconstruction of existing roads • repairing bridges and culverts • ports modernisation • airports modernisation; and • healthcare facilities modernisation. The information on the Company projects contributing to sustainable development of the territory will be integrated into the report (see Section *Developing regional social infrastructure*).
Finn Larsen, International Union for Conservation of Nature (IUCN)		
45	'I recommend you pay attention to the issue of the way you deal with transparency. Ten years ago, the materials were provided to the whale experts and IUCN quite reluctantly, and most of the data provided were confidential. You have come a long way since then, and today Sakhalin Energy can serve as a model of openness. Such openness is one of the ways to achieve target quality.'	The Company is grateful for this comment. In course of implementing the Sakhalin-2 Project, Sakhalin Energy strives to follow Russian and international best practices on information campaigns and public consultations. The General Business Principles of Sakhalin Energy establish the principles of transparency and open stakeholder engagement. The Company is governed by these principles in achieving the set targets and in its approaches to such cooperation. The information on respective activities will be integrated into the report.
46	'Following the above, I suggest including the information on the amount and type of recommendations given by WGWAP scientists, which the Company has fulfilled.'	The IUCN publishes reports of all meetings on their website http://iucn.org/WGWAP/. On this site, a list of all recommendations is given and their status. To date, the Western Gray Whale Advisory Panel has made 194 recommendations, of which 30 remain open.
Alexey Yurievich Knizhnikov, Oil&Gas sector environmental policy programme coordinator, World Wildlife Fund (WWF Russia)		
47	'Disclose the data on gas flaring on the platforms and tell why it is impossible to totally avoid this.'	Flares are an important safety feature on offshore platforms and are used to burn gas when necessary to ensure the safety of people and the asset. Sakhalin Energy does not flare gas simply to meet production targets, only during emergencies and for safety reasons.

No.	Comment, question or pointed remark	Company reply
48	'Conduct a review of the Project's influence on spawning rivers. The Company has continuously published information on the measures taken to reduce the impact, but it has been a year since the construction was virtually completed, so it would be expedient to assess the condition of spawning rivers and the Project's effect on them.'	Sakhalin Energy has an approved programme for monitoring selected rivers during the post–construction phase. According to results of this monitoring, no significant impact of the Project facilities on the environment has been observed. Information on the monitoring of water bodies is included in the report (see Section *River ecosystems*).
49	'It is necessary to present the measures developed by the Company to save and rehabilitate the birds in case of emergency oil spills. WWF considers this as an important activity for all oil and gas companies and believes that the Company has become the leader in this issue. Perhaps, the results are not as desired by EcoNPO, but this is definitely best practice.'	The Company is grateful for this comment. The Company has developed, together with advice from IFAW, what we believe is a good facility. The plan is available on our public web site. It is our sincere hope that we will never need to implement this plan. Information on the Oiled Wildlife Response Plan is included in the report (see Section *Oiled wildlife rehabilitation programme*).
Grigoriy Arkadievich Tsidulko, Member of WGWAP, Independent whale expert		
50	'Give detailed evaluation of what has been done for OSR, including response on ground, marine and ice marine spills.'	The Company has developed oil spill response plans that comply fully with the Russian Federation legal requirements. These plans are available on the Sakhalin Energy public web site. The plans were all reviewed by an independent organisation at the request of the Project lenders, and their comments have been included. The Company conducts drills and exercises to ensure that responders and equipment are tested regularly.
51	'Provide the clear evaluation of OSRP equipment quantity. We appreciate the Company's efforts in this respect, but there is a doubt that the Company will have sufficient equipment and materials in case of the most pessimistic scenario of events.'	The equipment available is based on the worst–case scenarios as defined by Russian Federation legislation. The equipment is deployed in various locations onshore and on vessels offshore to ensure its availability if needed. Information on OSR plans is available on Company's public web site.

APPENDIX 3:
LIST OF STAKEHOLDERS WHO PARTICIPATED IN DIALOGUES FOR DEVELOPMENT OF THE 2009 SUSTAINABLE DEVELOPMENT REPORT

1. Yu.I. Andreev, Deputy Head of the Regional Council of Veterans
2. A.I. Gafner, Chairman of Stroitel gardening community council
3. V.I. Vorontsov, Chairman of the Committee for Economic Development, Sakhalin Oblast Duma
4. Yu.P. Maltsev, Adviser to the the Chairman of the Committee for Economic Development, Sakhalin Oblast Duma
5. N.M. Gasanova, Adviser to the the Chairman of the Committee for Economic Development, Sakhalin Oblast Duma
6. A.V. Romanov, First Deputy Minister of Natural Resources and Environmental Protection of Sakhalin Oblast/Head of Subsoil Use Administration
7. N.V. Nikitina, Head of design estimate documentation and contracts' activity control department, Ministry of Natural Resources and Environmental Protection, Sakhalin oblast administration.
8. N.M. Trefilova, Head of Kidsave International NGO representative office in Yuzhno-Sakhalinsk
9. E.G. Milainenko, Manager of Kidsave International NGO representative office in Yuzhno-Sakhalinsk
10. O.F. Devyatkina, training specialist in Preodoleniye rehabilitation centre for children with disabilities
11. N.A. Lisitsina, Vice Chairman of Sakhalin Environmental Watch RPO (regional public organization) Council
12. Ye.N. Sapozhnikov, Sakhalin Environmental Watch RPO
13. L.N. Yevdokimova, Deputy Head of Korsakov Municipal District, Head of the Department for Social Development
14. S.M. Pervukhin, Chairman of Piligrim tourist regional club NGO
15. T.V. Pervukhina, grant-manager of Piligrim tourist regional club NGO
16. L.A. Milchenko, Director of Rodnik ecological centre
17. E.V. Raschupkina-Lopukhina, Head of Knowledge Is Power NGO
18. N.V. Kizimova, Manager of Sakhalin Salmon Initiative educational project
19. T.P. Roon, Director of Sakhalin Regional museum of Local Lore
20. I.G. Minervin, First pro-rector of Sakhalin State University
21. To Ken Sik, Head of Management Chair, Sakhalin State University
22. S.K. Kurmanguzhinov, Chairman of Sakhalin IP Regional Council
23. A.A. Voropsey, member of Korsakov Rotary club
24. Reeves Randy, Chairman of Western Grey Whale Advisory Panel (WGWAP)
25. Larsen Finn, International Union for Conservation of Nature (IUCN)
26. A.Yu. Knizhnikov, Oil&Gas sector environmental policy programme coordinator, World Wildlife Fund (WWF Russia)
27. G.A. Tsidulko, Member of WGWAP, independent whale expert.

APPENDIX 4:
SAKHALIN-2 RECORDS

- First PSA in Russia
- First oil and gas operation from marine stationary platforms in Russia
- First simultaneous implementation of several large interconnected green field sub–projects in Russia
- Phase 1 Project financing first funding of its kind in Russia's oil and gas industry
- Largest project finance deal in Russia (2008)
- First offshore platform installed in Russia (Molikpaq)
- Zero to minimal gas flaring, the first system of its kind in Russia (Molikpaq)
- First use of directional hydraulic fracturing, of formation for well completion in Russia (Molikpaq platform)
- First use of indirect fracture of formation for well completion in Russia (the Molikpaq platform)
- First ice class stationary gas production platform installed in Russia – Lunskoye–A platform (Lun–A)
- First concrete gravity base structure in Russia, built for the Lunskoye–A platform (Lun–A)
- Float–over of the Lunskoye–A, 21,800 tonnes topsides in 2006 a world and Russian record in 2006
- Installation of friction pendulum bearings on Lunskoye–A is first use of these bearings in the oil and gas industry anywhere in the world
- Float–over of 28,000 tonnes Piltun–Astokhskoye–B (PA–B) topsides in 2007 broke the float–over record
- First liquefied natural gas (LNG) plant – the first of the kind built in Russia
- First LNG carrier to enter Russian territorial waters – Granosa in 2007
- First time LNG measurement methodology was used in Russia
- First real–time operations centre in Russia
- First use of ISSOW electronic permit to work system in Russia
- First time an oil and gas company created an initiative, the Advisory Panel for the Western Gray Whales protection, under the aegis of IUCN
- First road safety partnership between public administration and business in Russia (Sakhalin Road Safety Partnership).

APPENDIX 5:
LIST OF COMPANY INFORMATION CENTRES

District	Locality	Organisation	Address
Aniva	Troitskoye	Rural library, Branch #07, Unit of Aniva Municipal Centralised Library System	13 Sovetskaya St.
Dolinsk	Vzmorye	Rural library, Branch #06, Unit of Dolinsk Municipal Centralised Library System	22 Pionerskaya St.
	Sovetskoye	Rural library, Branch #10, Unit of Dolinsk Municipal Centralised Library System	122 Tsentralnaya St.
	Dolinsk	Dolinsk Central Town Library, Unit of Dolinsk Municipal Centralised Library System	31 Lenin St.
	Sokol	Rural library, Branch #05, Unit of Dolinsk Municipal Centralised Library System	26 Sovkhoznaya St.
Kholmsk	Kholmsk	Central District Library named after Yury Nikolayev, Branch of Municipal Culture Enterprise Kholmsk Central Library System of Kholmsk Municipality	124 Sovetskaya St.
Makarov	Vostochnoye	Rural library, Branch #02, Unit of Makarov Municipal Centralised Library System	8 Privokzalnaya St.
	Makarov	Makarov Central Library, Municipal Enterprise Makarov Centralised Library System	9a 50 Let Oktyabrya St.
	Novoye	Rural library, Branch #04, Unit of Makarov Municipal Centralised Library System	11–7 Tsentralnaya St.
Poronaysk	Gastello	Rural library, Branch #4, Poronaysk Central Library System, Unit of Poronaysk Municipal Centralised Library System	42– 2 Tsentralnaya St.
	Vostok	Rural library, Branch #13, Poronaysk Central Library System, Unit of Municipal Culture Enterprise Poronaysk Centralised Library System	10a Gagarin St.
Smirnykh	Onor	Rural library, Branch #03, Unit of Municipal Culture Enterprise Smirnykh Centralised Library System	5 Sovetskaya St.
	Pobedino	Pobedino Rural Library, Museum, Branch #04 of Municipal Culture Enterprise Smirnykh Centralised Library System	60 Tsentralnaya St.
	Smirnykh	Smirnykh Central Library, Municipal Culture Enterprise Smirnykh Centralised Library System	12 Lenin St.
	Roschino	Rural library, Branch #06, Municipal Culture Enterprise Smirnykh Centralised Library System	4 Komsomolskaya St.
	Buyukly	Rural library, Branch #07, Municipal Culture Enterprise Smirnykh Centralised Library System	1 Kosmonavtov St.
Tymovsk	Molodezhnoye	Rural library, Branch #17, Unit of Municipal Culture EnterpriseTymovsk Centralised Library System	15 Sovetskaya St.
	Tymovskoye	Central District Library, Municipal Culture Enterprise Tymovsk Centralised Library System	68a Kirovskaya St.
	Yasnoye	Rural library, Branch #13, Unit of Municipal Culture Enterprise Tymovsk Centralised Library System	2 Titov St.
	Kirovskoye	Rural library, Branch #8, Unit of Municipal Culture Enterprise Tymovsk Centralised Library System	70 Tsentralnaya St.

FEEDBACK FORM

DEAR READERS,

You have just read the 2009 Sakhalin Energy Sustainable Development Report (hereinafter – 'Report').

Your opinion on this Report is very important to us and we would greatly appreciate it if you help us to improve the quality of reporting by answering the questions in this Form.

1. After reading Report, do you have a better idea and understanding of Sakhalin Energy's activities in sustainable development?

Yes | Mostly No | Mostly Yes | Unsure | Equal

Please provide comments in support of your answer

2. What is your impression of the information contained in this Report?

Very interesting | Mostly uninteresting | Mostly interesting | Very uninteresting | Equal | Unsure

Please provide comments in support of your answer

3. How do you rate this Report in terms of credibility and objectivity of the information provided?

Very favourable | Mostly unfavourable | Mostly favourable | Very unfavourable | Equal | Unsure

Please provide comments in support of your answer

4. How easy was it to find the required information in Report?

Very easy | Mostly uneasy | Mostly easy | Very uneasy | Equal | Unsure

Please provide comments in support of your answer

5. What Section of Report was the most interesting and valuable to you?

6. What aspects of Sakhalin Energy's activity, in your opinion, should be improved to strengthen the Company's social responsibility efforts?

7. What other information would you like to see in the next Sakhalin Energy Sustainable Development report?

8. Please provide general comments on the Report here:

9. Are you or your organisation interested in participating in dialogues with stakeholders during preparation of 2010 Sakhalin Energy Sustainable Development Report?

Yes (please provide your contact information) | No

10. What other organisations in your opinion should be invited to take part in subsequent dialogues with stakeholders during preparation of the next Sustainable Development Report?

11. Which group of stakeholders do you belong to?

Company's employee	Customer (Buyer)	Representative of public organisation (NGO)
Investor	Partner (Contractor)	Mass media
Shareholder	Representative of authorities	Other group of stakeholders

Please Clarify

Please indicate your contact information below:

Name:	Job title:	Telephone:
Organisation:	Fax:	E–mail:
Address:		

12. Which communication is preferable?

By mail | By E–Mail

Please return the completed Form marked '2009 Sustainable Development Report' to: Sakhalin Energy Investment Company Ltd., 35, Dzerzhinskogo Str., Yuzhno–Sakhalinsk, Sakhalin Oblast, Russian Federation, 693020

You may also email this Form to: Ask-sakhalinenergy@sakhalinenergy.ru or leave it at the Company's Information Centre.

List and addresses of information centres are given in Appendix 5 to the Report.

THANK YOU FOR YOUR FEEDBACK!