SISTEMA HALS REAL ESTATE DEVELOPMENT GROUP

Independent Accountants' Review Report

Financial Statements
as of June 30, 2006 (unaudited) and
December 31, 2005 and for the six months
ended June 30, 2006 and 2005 (unaudited)

SISTEMA-HALS REAL ESTATE DEVELOPMENT GROUP

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INDEPENDENT ACCOUNTANTS' REVIEW REPORT

To the Board of Directors and Shareholders of JSFC Sistema:

We have reviewed the accompanying statements of assets and liabilities of Sistema-Hals Real Estate Development Group (the "Group"), comprising the real estate business of JSFC Sistema conducted in the Commonwealth of Independent States ("CIS"), as of June 30, 2006 and 2005, and the related statements of operations, cash flows and changes in net assets/(liabilities) for the six months then ended. These financial statements are the responsibility of the Group's management.

We conducted our review in accordance with standards established by the American Institute of Certified Public Accountants for reviews of interim financial information. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards as established by the Auditing Standards Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

The accompanying financial statements were prepared to present the assets and liabilities and related results of operations and cash flows of the Group, as described in Note 1 to the financial statements, and may not necessarily be indicative of the conditions that would have existed or the results of operations and cash flows if the Group had been operated as a stand-alone company during the periods presented.

Based on our review, we are not aware of any material modifications that should be made to accompanying financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche

October 3, 2006
Moscow, Russia

SISTEMA-HALS REAL ESTATE DEVELOPMENT GROUP

STATEMENTS OF ASSETS AND LIABILITIES
AS OF JUNE 30, 2006 (UNAUDITED) AND DECEMBER 31, 2005
(Amounts in thousands of U.S. Dollars)

	Notes	June 30, 2006	December 31, 2005
ASSETS			
Cash and cash equivalents	5	23,289	10,362
Accounts receivable, net	6	8,022	20,929
Taxes receivable	7	25,777	25,058
Prepaid expenses and other assets, net	8	10,831	3,917
Loans and notes receivable	9	12,302	7,708
Costs and estimated earnings in excess of billings on uncompleted contracts	10	33,705	38,348
REAL ESTATE INVESTMENTS, NET			
Real estate developed for sale	11	201,484	124,312
Income producing properties, net	11	50,505	47,580
Total		251,989	171,892
Plant and equipment, net	12	5,690	3,356
Development rights and other intangible assets, net	13	43,269	43,178
Investments in shares	14	2,667	287
TOTAL ASSETS		417,541	325,035
LIABILITIES			
Payables to suppliers and subcontractors	15	37,859	12,148
Billings in excess of costs and estimated earnings on uncompleted contracts	16	66,559	13,996
Accrued expenses and other liabilities	17	58,881	5,198
Taxes payable		1,841	856
Construction obligations	18	21,898	21,898
Loans and notes payable	19	164,590	216,500
Deferred tax liabilities	21	13,332	10,883
TOTAL LIABILITIES		364,960	281,479
COMMITMENTS AND CONTINGENCIES	24	-	-
MINORITY INTERESTS		14,316	14,125
NET ASSETS		**38,265**	**29,431**

See notes to financial statements

SISTEMA-HALS REAL ESTATE DEVELOPMENT GROUP

STATEMENTS OF OPERATIONS
FOR THE SIX MONTHS ENDED JUNE 30, 2006 AND 2005 (UNAUDITED)
(Amounts in thousands of U.S. Dollars)

	Notes	Six months ended June 30,	
		2006	**2005**
REVENUES	25	106,620	33,245
OPERATING EXPENSES	20	(64,627)	(29,349)
OPERATING INCOME		41,993	3,896
OTHER INCOME (EXPENSES):			
Other income, net		268	128
Interest income		846	220
Interest expense, net of amounts capitalized		(2,600)	(2,307)
Losses on foreign currency transactions		(4,819)	(953)
Gain on disposal of an equity investee	14	3,078	-
INCOME BEFORE INCOME TAX AND MINORITY INTERESTS		38,766	984
Income tax expense	21	(4,748)	(1,942)
INCOME/(LOSS) BEFORE MINORITY INTERESTS		34,018	(958)
Minority interests		(2,934)	(3,201)
NET INCOME/(LOSS)		31,084	(4,159)

See notes to financial statements.

SISTEMA-HALS REAL ESTATE DEVELOPMENT GROUP

STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30, 2006 AND 2005 (UNAUDITED)
(Amounts in thousands of U.S. Dollars)

	Six months ended June 30,	
	2006	**2005**
OPERATING ACTIVITIES:		
Net income/(loss)	31,084	(4,159)
Adjustments to reconcile net income/(loss) to net cash provided by/ (used in) operations:		
Depreciation and amortization	1,714	963
Loss on disposal of plant and equipment	191	131
Gain on disposal of an equity investee	(3,078)	-
Profit recognized by the percentage-of-completion method on real estate developed for sale	(34,935)	-
Minority interests	2,934	3,201
Deferred tax expense	2,449	173
Bad debt (reversal)/expense	(87)	2,300
Foreign currency transactions loss/(gain) on non-operating activities	4,413	(2,573)
Changes in operating assets and liabilities:		
Billings in excess of costs on uncompleted contracts	56,398	5,600
Accounts receivable	12,907	(3,912)
Prepaid expenses and other assets	(6,827)	(2,957)
Taxes receivable	(719)	(4,099)
Payables to suppliers and subcontractors	17,321	1,699
Accrued expenses and other liabilities	21,881	(8,219)
Taxes payable	985	328
Net cash provided by/(used in) operating activities	**106,631**	**(11,524)**
INVESTING ACTIVITIES:		
Payments for real estate investments	(59,414)	(14,492)
Proceeds from sale of real estate investments	30,341	-
Purchases of plant and equipment and intangible assets	(3,461)	(4,478)
Proceeds from sale of plant and equipment	331	204
Issuance of short-term loans and notes receivable, net	(4,117)	(1,449)
Purchases of long-term investments	(2,520)	(320)
Proceeds from sale of long-term investments	139	123
Proceeds from sale of an equity investees	3,094	-
Net cash used in investing activities	**(35,607)**	**(20,412)**

STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE SIX MONTHS ENDED JUNE 30, 2006 AND 2005 (UNAUDITED)
(Amounts in thousands of U.S. Dollars)

	Six months ended June 30, 2006	Six months ended June 30, 2005
FINANCING ACTIVITIES:		
Principal payments on long-term borrowings	(30,400)	(41,248)
Proceeds from long-term borrowings	9,546	33,305
(Principal payments on)/proceeds from short-term borrowings, net	(35,946)	23,902
Net transfers from Sistema	-	14,730
Dividends paid to minority shareholders of subsidiaries	(1,922)	-
Net cash (used in)/provided by financing activities	**(58,722)**	**30,689**
Effects of foreign currency translation on cash and cash equivalents	625	(148)
INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	12,927	(1,395)
CASH AND CASH EQUIVALENTS, beginning of the period	10,362	6,540
CASH AND CASH EQUIVALENTS, end of the period	23,289	5,145
CASH PAID DURING THE PERIOD FOR:		
Income taxes	1,594	2,679
Interest, net of amounts capitalized	2,351	2,684

NON-CASH INVESTING AND FINANCING ACTIVITIES:

Non-cash investing and financing activities for the six months ended June 30, 2006 included transfer to Sistema of a share of profit on Pokrovka 40 development project, as described in Note 3, and acquisitions of subsidiaries, as described in Note 4.

See notes to financial statements.

STATEMENTS OF CHANGES IN NET ASSETS
FOR THE SIX MONTHS ENDED JUNE 30, 2006 AND 2005 (UNAUDITED)
(Amounts in thousands of U.S. Dollars)

	Six months ended June 30,	
	2006	**2005**
Beginning balance	29,431	15,798
Net income/(loss)	31,084	(4,159)
Net transfers (to)/from Sistema (Note 3)	(22,250)	14,730
Ending balance	**38,265**	**26,369**

See notes to financial statements.

1. BASIS OF PRESENTATION

The financial statements of Sistema-Hals Real Estate Development Group (the "Group") are presented on a carve-out basis to include the historical operations of the Real Estate business segment of JSFC Sistema ("Sistema"). In August 2006, Sistema has completed the corporate reorganization of its Real Estate business segment by consolidating ownership of the segment's entities under Sistema-Hals JSC, except that Pokrovka 40 LLC (Note 3), remains majority owned by Sistema. Pokrovka 40 will be transferred to the buyer of the office complex that the Group has developed at Pokrovka St. 40, Moscow, upon closing of the sale.

The Group is engaged in real estate development, project and construction management, real estate asset management and facility management, primarily focused on the "Class A" and "Class B" segments of the Moscow office market, shopping centers, high-end housing, single family houses, apartment buildings and land development. The Group's revenues are derived principally from the following activities: (i) sale of completed development projects, both commercial and residential, as well as the sale of rights to land; (ii) project and construction management activities for infrastructure and other construction and development projects; (iii) rental income from completed development projects held as investments; and (iv) facility management services.

Business operations of the Group are conducted in the Russian Federation (hereinafter referred to as the "RF") and the CIS, primarily in Moscow, the Moscow Region and Saint-Petersburg. All significant operating entities of the Group are incorporated in the CIS.

During the six months ended June 30, 2006 and 2005, Sistema did not charge the Group for any management services, including corporate oversight, financial, legal, corporate communications or human resources. Costs incurred by Sistema to provide such services to the Group have not been significant during these periods. However, these financial statements may not necessarily be indicative of the conditions that would have existed or the results of operations and cash flows if the Group had been operated as a stand-alone company during the periods presented.

During the six months ended June 30, 2006 and 2005, majority of the Group's borrowings was provided by Sistema. Significant portion of this financing was of a short-term nature. In August and September 2006, the Group obtained loans from international financial institutions for the term of one year (Note 26), that it expects to use, in part, to refinance borrowings from Sistema. Management believes, on the basis of cash flow forecasts, that the total facilities available to the Group will be sufficient to cover all of the Group's current obligations.

All significant transactions within the Real Estate business segment of Sistema, balances and unrealized gains (losses) on such transactions have been eliminated in these financial statements.

(Amounts in thousands of U.S. Dollars unless otherwise stated)

The beneficial ownership and proportion of voting power of Sistema in significant operating entities of the Group as of June 30, 2006 and December 31, 2005 were as follows:

Operating entities	**Ownership interest**		**Voting power**	
	June 30, 2006	**December 31, 2005**	**June 30, 2006**	**December 31, 2005**
Mosdachtrest	56%	56%	60%	60%
Sistema-Temp	100%	100%	100%	100%
Kuntsevo-Invest	81%	81%	81%	81%
Landshaft	100%	100%	100%	100%
Landshaft-2	100%	100%	100%	100%
City-Hals	100%	100%	100%	100%
Hals-Stroy	100%	100%	100%	100%
Beijing-Invest	90%	90%	90%	90%
Sistema-Hals Nord-West	76%	76%	76%	76%
Organizator	51%	51%	51%	51%
PSO Sistema-Hals	51%	51%	51%	51%
Hotel Korona-Intourist	100%	100%	100%	100%
Pokrovka 40	97%	-	97%	-
Terra	99%	99%	99%	99%
Yalta Fish Processing Plant	98%	98%	98%	98%
Kaskad	100%	100%	100%	100%

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements have been prepared in conformity with the accounting principles generally accepted in the United States of America (“U.S. GAAP”). The Group’s entities maintain accounting records and prepare their statutory financial statements in Russian rubles (“RUB”) in accordance with the requirements of accounting and tax legislation in Russia.
The accompanying financial statements differ from the financial statements prepared for statutory purposes in Russia in that they reflect certain adjustments, not recorded in the Russian statutory accounting books of the Group’s entities, which are appropriate to present the financial position, results of operations and cash flows in accordance with U.S. GAAP.

The accompanying financial statements as of June 30, 2006 and December 31, 2005 and for each of the six months ended June 30, 2006 and 2005 have been prepared by the Group, without audit. These financial statements should be read in conjunction with the audited financial statements and the notes thereto included herein. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position as of June 30, 2006 and December 31, 2005, results of operations and cash flows for each of the six months ended June 30, 2006 and 2005 and are not necessarily indicative of the operating results for the full year.

Use of estimates – The preparation of the financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and amounts of revenues and expenses of the reporting period. Actual results could differ from those estimates.

Concentration of business risk – The Group's principal business activities are within the RF. Laws and regulations affecting businesses operating in the RF are subject to rapid changes. Russian land and property legislation is complicated, often ambiguous and contradictory at the federal and regional levels. In particular, it is not always clear which state bodies are authorized to enter into land leases with respect to particular land plots, construction approval procedures are complicated and prone to challenge or reversal, and construction and environmental rules often contain requirements that are impossible to comply with in practice. As a result, the risk exists that the Group's ownership of and/or lease rights to land and buildings might be challenged by government authorities or third parties.

The construction industry in general is subject to unique risks in respect to the means of financing, the legal and political risks and the financial risks associated with construction projects which transpire over a prolonged period of time. The Group is also reliant on a limited number of general contractors and subcontractors to undertake its commitments for construction in the timeframe required to avoid penalties and other associated costs.

Foreign currency translation – The Group follows a translation policy in accordance with Statement on Financial Accounting Standards ("SFAS") 52, "Foreign Currency Translation".

Management believes that the USD is the functional currency of the Group, as the majority of its revenues, costs and capital expenditures are either priced, incurred, payable or otherwise measured in USD. In addition, the Group maintains significant portion of its debt instruments in USD. To the extent settlements are required to be in RUB, the Group sets prices and values in USD and performs the settlements in RUB using the then prevailing exchange rate of the Central Bank of Russia. As such, during the six months ended June 30, 2006 and 2005, the Group remeasured its assets, liabilities, income and expense items in USD. Monetary assets and liabilities were translated into USD at the rate in effect as of the balance sheet date; non-monetary assets and liabilities and income and expense items were translated at the rate prevailing on the date of the transaction. Exchange gains and losses arising from the remeasurement of monetary assets and liabilities not denominated in USD were included in gains/(losses) on foreign currency transactions in the statements of operations. The official exchange rates quoted by the Central Bank of Russia as of June 30, 2006 and December 31, 2005 were 27.08 and 28.78 rubles per 1 USD, respectively.

During the six months ended June 30, 2006 and 2005, the Russian ruble was not a fully convertible currency outside of the territory of the RF. The translation of ruble denominated assets and liabilities into USD for the purpose of these financial statements does not indicate that the Group could realize or settle in USD the reported values of the assets and liabilities.

Revenue recognition – The Group's revenues are principally derived from i) real estate development, ii) project and construction management, iii) real estate asset management, iv) facility management. The Group records revenues as follows:

(i) Revenues from real estate development activities are recognized in accordance with the provisions of SFAS 66 "Accounting for Sales of Real Estate" or AICPA Statement of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts" ("SOP 81-1").

When the Group undertakes real estate development projects at its own risk, it recognizes revenues from sales of real estate when a) a sale is consummated; b) the buyer's initial and continuing investments are adequate to demonstrate a commitment to pay; c) the Group's receivable is not subject to future subordination; d) the Group has transferred to the buyer the usual risks and rewards of ownership and does not have a substantial continuing involvement with the project. A sale is not considered consummated until (a) the parties are bound by the terms of a contract; (b) all consideration has been exchanged; (c) any permanent financing for which we are responsible has been arranged; and (d) all conditions precedent to closing have been performed. Revenues from development of office buildings, apartments, condominiums, shopping centers and similar structures are recognized prior to consummation of sale by the percentage-of-completion method if (a) construction is beyond a preliminary stage; (b) the buyer is committed to the extent of being unable to require a refund except for nondelivery of the property; (c) sales prices are collectible; (d) aggregate sales proceeds and costs can be reasonably estimated.

Investments in real estate developed for sale where the sale is not consummated are accounted for under the deposit method in accordance with SFAS 66, except for those investments in development of office buildings, apartments, condominiums, shopping centers and similar structures, where criteria for revenue recognition have been met as of the balance sheet date. Such investments are accounted for by the percentage-of-completion method.

In those instances, when the Group acts as a contractor under construction contracts with third parties, it applies the percentage of completion method to the respective contracts where and as soon as it is able to reliably estimate the stage of progress to completion of the project, costs to complete the project and contractual revenues. Progress towards completion is measured by the percentage of costs incurred to date to the estimated total costs at completion for each contract (the “cost-to-cost” method). On most of its contracts, the Group is not able to reliably estimate costs to complete the project and contractual revenues until the project is at least 30% complete. Until the 30% completion point, the Group carries the projects at cost. The Group does not recognize revenue on contracts until reasonably dependable estimates of costs to complete the project and contractual revenues can be made.

(ii) The Group provides project and construction management services to municipal governments on certain socially important infrastructure projects. The Group’s remuneration for such services was determined as a percentage of project costs incurred by third parties and approved by the municipal government. Based upon the guidance in Emerging Issues Task Force Consensus 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent (“EITF 99-19”), management has concluded that the Group’s services under such contracts do not transfer to the Group full risks and rewards associated with the projects. Therefore, the Group recognizes as revenues only its fees from project management services. Fees are recognized as the project costs are incurred and approved by the municipal government.

(iii) Revenues from real estate asset management include rental revenues, revenues from sale or assignment of rights to land plots and residential units. Rental revenues are recognized over the lease term on a straight-line basis. Revenues from sale or assignment of rights over real estate are recognized when substantially all the risks and rewards of ownership have been passed to the buyer.

(iv) Revenues from service contracts for facility management are recognized on the accrual basis over the periods when services are provided.

Change orders and claims – Once contract performance is underway, the Group may experience changes in the conditions, client requirements, specifications, designs, materials and/or work schedule (“change orders”). Generally a change order will be negotiated with the customer to modify the original contract to approve both the scope and the pricing of the change. When a change order becomes a point of dispute between the Group and its customer, the Group then considers it as a claim. Costs related to change orders and claims are recognized when they are incurred. Change orders are included in total estimated contract revenues when it is probable that the change order will result in a bona fide addition to the relevant contract value and can be reliably estimated. Claims are included in total estimated contract revenue only to the extent that contract costs related to the claim have been incurred and when it is probable that the claim will result in a bona fide addition to contract value and can be reliably estimated.

Estimated losses on uncompleted contracts and changes in contract estimates – The Group provides for estimated losses on uncompleted contracts in the periods in which such losses are identified. The cumulative effects of revisions to contract revenue and estimated completion costs are recorded in the accounting period in which the amounts become evident and can be reasonably estimated. These revisions may include such items as the effects of change orders and claims, warranty claims, other contractual penalties and contract closeout settlements.

Costs and billings on uncompleted contracts – Costs related to the Group's performance under construction contracts (including estimated earnings from uncompleted contracts) is recorded net of billings on those contracts. Billings when in excess of costs and estimated earnings on uncompleted contracts are recorded as liabilities.

Income producing properties – The Group has a number of developments where it generated or expects to generate economic benefits through retaining title to or lease rights for the property and receiving rental revenues. Such properties primarily consist of residential and commercial buildings and land which is, or will be, leased on either a short-term or long-term basis.

Income producing properties are depreciated on a straight-line basis over estimated useful lives of the assets (buildings and land improvements – 20 to 40 years; leasehold improvements – the lesser of the remaining life of the asset or term of the lease).

Financial instruments – The Group's financial instruments primarily comprise cash and cash equivalents, short-term and long-term investments, receivables, payables and debt. The estimated fair value of short-term financial instruments as of June 30, 2006 approximated their carrying value as reflected in the balance sheet. The fair value of long-term loans and notes payable which have variable interest rates based on market rates approximate the carrying amount of those financial instruments. The fair value of the Group's long-term loans and notes payable to Sistema and its subsidiaries is not practicable to estimate based on the related party nature of the underlying transactions. The fair value of long-term investments was not determined due to quoted market prices not being readily available and valuations not being obtained due to the excessive costs involved.

Cash and cash equivalents – Cash and cash equivalents include cash on hand, amounts on deposit in banks and cash invested temporarily in various instruments with maturities of three months or less at the time of purchase.

Loans and notes receivable – Loans and notes receivable with original maturities in excess of three months are being accounted for at amortized cost. Management annually assesses the realizability of the carrying values of loans and notes receivable and, if necessary, records impairment losses to write the investments down to fair value.

Investments in shares – The Group's share in net assets and net income of Amiral B.V., Telecom Development, Sibmost and Kamenny Ostrov, in which the Group holds 20-50% of voting shares and has the ability to exercise significant influence over their operating and financial policies ("affiliates") is accounted for using the equity method of accounting. During the six months ended June 30, 2006 and 2005, the Group's share in the net income/(loss) of these entities was insignificant.

Investments in corporate shares where the Group owns less than 20% voting interest are accounted for at cost of acquisition.

Accounts receivable – Accounts receivable are stated at their net realizable value after deducting an allowance for doubtful accounts. Such provisions reflect either specific cases or estimates based on evidence of collectibility.

Prepaid expenses – Prepaid expenses are primarily comprised of advance payments for services to vendors.

Value-added taxes – Value-added taxes (“VAT”) related to sales are payable to the tax authorities either on an accrual or a cash basis (members of the Group are applying different methodologies, as allowed by Russian tax law) based upon invoices issued to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that are reclaimable after the balance sheet dates is recorded in taxes receivable. Non-reclaimable VAT is included into the cost of construction as it is a cost necessarily incurred in the completion of the relevant object.

Plant and equipment – Plant and equipment with a useful life of more than one year is capitalized at historical cost. Cost includes major expenditures for improvements and replacements which extend useful lives of the assets or increase their revenue generating capacity. Repairs and maintenance are charged to the statements of operations as incurred.

Items of plant and equipment that are retired or otherwise disposed of are eliminated from the balance sheet along with the corresponding accumulated depreciation. Any gain or loss resulting from such retirement or disposal is included in the determination of net income.

Plant and equipment is depreciated on the straight-line basis over 3 to 5 years.

Development rights and other intangible assets – Development rights acquired by the Group are stated at acquisition cost. The costs of development rights will be amortized on a straight-line basis from the date when the project starts generating revenues until the development period expires. Development rights as of June 30, 2006 and December 31, 2005, comprise rights to develop residential property in the Western Kuntsevo district of Moscow. The development period for this project expires in 2012. Amortization of other finite-life intangible assets is computed on a straight-line basis.

Impairment of long-lived assets – The Group periodically evaluates the recoverability of the carrying amount of its long-lived assets in accordance with SFAS 144, “Accounting for the Impairment or Disposal of Long-Lived Assets”. Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, the Group compares undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, the Group records impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets. Management does not believe there should be any impairment charge recorded relating to the Group’s investments in long-lived assets during the six months ended June 30, 2006 and 2005.

Construction obligations – Construction obligations represent obligations to construct apartments assumed as a result of the acquisition of rights to develop residential property in the Western Kuntsevo district of Moscow.

Income taxes – Income taxes have been computed in accordance with the laws of the RF. The standard income tax rate in the RF for the six months ended June 30, 2006 and 2005 was 24%.

Deferred income taxes are accounted for under the liability method and reflect the tax effect of all significant temporary differences between the tax bases of assets and liabilities and their reported amounts in the financial statements. A valuation allowance is provided for deferred tax assets if it is more likely than not that these items will either expire before the Group will be able to realize the benefit, or the future deductibility is uncertain.

Retirement benefit and social security costs – The Group contributes to the RF state pension fund, social insurance fund, medical insurance fund on behalf of all of its current employees. In accordance with the current RF legislation, all social contributions are calculated by the application of a regressive rate from 26% to 2% to the annual gross remuneration of each employee. The contributions are expensed in the period in which they are incurred.

Borrowing costs – The Group capitalizes interest on borrowings during the active construction period of its capital projects. Capitalized interest is added to the cost of the underlying assets and is amortized over the useful lives of the assets. For the six months ended June 30, 2006 and 2005, capitalized borrowing costs were USD 3,779 thousand and USD 3,666 thousand, respectively. Other borrowing costs were recognized as an expense in the period in which they were incurred.

Advertising costs – The Group expenses the cost of advertising in the period in which they are incurred.

Minority interests – Minority interests represents share in book value of net assets of the Group’s entities proportional to equity interests in those entities owned, directly or indirectly, by shareholders other than Sistema and its subsidiaries.

Dividends and distributions – Dividends and distributions to shareholders are recognized at the date they are declared. Distributable retained earnings of the Group are based on amounts extracted from statutory accounts of individual entities and may differ from amounts calculated on the basis of U.S. GAAP.

Comprehensive income – Comprehensive income consists of net income/(loss) and other comprehensive income/(loss). Other comprehensive income/(loss) refers to revenues, expenses, gains and losses that are not included in net income, but rather are recorded directly in net assets/(liabilities). For the six months ended June 30, 2006 and 2005, the Group had no items of other comprehensive income/(loss), and, accordingly, comprehensive income is the same as net income.

New accounting pronouncements – In March 2005, the FASB issued Interpretation No. 47, “Accounting for Conditional Asset Retirement Obligations – an interpretation of FASB Statement No. 143.” This Interpretation clarifies that the term “conditional asset retirement obligation” as used in FASB Statement No. 143, “Accounting for Asset Retirement Obligations”, refers to a legal obligation to perform an asset retirement activity, in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity.
The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Uncertainty about the timing and (or) method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists to make a reasonable estimate of the fair value of the obligation. Interpretation No. 47 is effective for the Group beginning January 1, 2006. The adoption of Interpretation No. 47 did not have a material impact on the Group’s financial position or results of operations.

In March 2005, the SEC released Staff Accounting Bulletin 107, "Share-Based Payments", or SAB 107. The interpretations in SAB 107 express views of the SEC staff regarding the interaction between FAS No. 123R and certain SEC rules and regulations, and provide the SEC staff's views regarding the valuation of share-based payment arrangements for public companies. In particular, SAB 107 provides guidance related to share-based payment transactions with nonemployees, the transition from nonpublic to public entity status, valuation methods (including assumptions such as expected volatility and expected term), the accounting for certain redeemable financial instruments issued under share-based payment arrangements, the classification of compensation expense, non-GAAP financial measures, first-time adoption of FAS No. 123R in an interim period, capitalization of compensation cost related to share-based payment arrangements, the accounting for income tax effects of share-based payment arrangements upon adoption of FAS No. 123R, the modification of employee share options prior to adoption of FAS No. 123R.

In May 2005, the FASB issued FAS No. 154, "Accounting Changes and Error Corrections", which replaces APB Opinion No. 20, "Accounting Changes" and FAS No. 3, "Reporting Accounting Changes in Interim Financial Statements". FAS No. 154 changes the requirements for the accounting and reporting of a change in accounting principle and is applicable to all voluntary changes and to changes required by an accounting pronouncement if such pronouncement does not specify transition provisions. FAS No. 154 requires retrospective application to the prior periods' financial statements of changes in accounting principle. In cases when it is impracticable to determine the period-specific or cumulative effects of an accounting change, the statement provides that the new accounting principle should be applied as of the earliest period for which retrospective application is practicable or, if impracticable to determine the effect of a change to all prior periods, prospectively from the earliest date practicable. This Statement is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

In June 2005, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue No. 05-6, "Determining the Amortization Period for Leasehold Improvements." As part of a business combination, the acquiring entity will often assume existing lease agreements of the acquired entity and acquire the related leasehold improvements. The issues are whether the "lease term" should be reevaluated at consummation of a purchase business combination and whether the amortization period for acquired leasehold improvements should be reevaluated by the acquiring entity in a business combination. The consensus reached by EITF No. 05-6 is effective for leasehold improvements that are purchased or acquired in reporting periods beginning June 29, 2005. The adoption of EITF No. 05-6 did not have a material impact on the Group's financial position and results of operations.

In February 2006, the FASB issued FAS No. 155, "Accounting for Certain Hybrid Financial Instruments, an amendment to FAS No. 133 "Accounting for Derivative Instruments and Hedging activities" and FAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". FAS No. 155 addresses application of FAS No. 133 to beneficial interests in securitized financial assets and permits to remeasure fair value for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, requires to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, amends FAS No. 140 to eliminate the prohibition on a qualifying special purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument, and clarifies certain other derivatives classification issues. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that starts after September 15, 2006, and is not expected to have a material impact on the Group's financial position and results of operations.

In July 2006, the FASB issued Interpretation No. 48, “Accounting for Uncertainty in Income Taxes”, of SFAS No. 109, “Accounting for Income Taxes”. The Interpretation applies to all tax positions that are within the scope of SFAS No. 109 and requires the two-step approach for recognizing and measuring tax benefits. The Interpretation establishes a “more-likely- than-not” recognition threshold that must be met before a tax benefit can be recognized in the financial statements. To meet this threshold, the enterprise must determine that upon examination by the taxing authority, the tax position is more likely to be sustained than not, based on the technical merits of the position. Once the recognition threshold has been met, enterprises are required to recognize the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement with the taxing authority. In both steps, enterprises must presume that the taxing authority has full knowledge of all relevant information. The Interpretation also requires enterprises to make explicit disclosures at the end of each reporting period about uncertainties in their income tax positions, including a detailed rollforward of tax benefits taken that do not qualify for financial statement recognition. The Interpretation is effective for fiscal years beginning after December 15, 2006, and should be applied to all tax positions upon initial adoption. The cumulative effect of applying the provisions of the Interpretation should be reported as an adjustment to the opening balance of retained earnings for that fiscal year.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (“SFAS 157”). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. This Statement is required to be adopted by the Group on July 1, 2008. The Group is currently assessing the impact of the adoption of this Statement.

In September 2006, the FASB issued SFAS No. 158, Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R) (“SFAS 158”). SFAS 158 requires companies with publicly traded equity securities that sponsor a postretirement benefit plan to fully recognize, as an asset or liability, the overfunded or underfunded status of their benefit plan(s). The funded status is measured as the difference between the fair value of the plan’s assets and its benefit obligation. SFAS 158 also requires companies to measure their plan assets and benefit obligations as of year-end balance sheet date. SFAS 158 is becoming effective for fiscal years ending after December 15, 2006; the provision to require measurement at the entity’s year-end balance sheet date will be effective for fiscal years ending after December 15, 2008. The Group does not expect the adoption of SFAS 158 to have a material impact on its financial position or results of operations.

3. DISPOSAL OF THE OFFICE PART OF POKROVKA 40 DEVELOPMENT PROJECT

During the six months ended June 30, 2006, the Group has entered into a series of related transactions in order to arrange for disposal of the office part of a real estate complex, developed by the Group at Pokrovka St, 40. In April 2006, the Group has established a special-purpose entity, Pokrovka 40, where Sistema-Hals and subsidiaries own 36.4%, Sistema and subsidiaries own 60.6% and the ultimate buyer of the office building owns 3%. The shareholders contributed USD 30,000 thousand to the share capital of Pokrovka 40, in proportion to their ownership interests, that will be used to acquire rights for the office building from Hotel Korona-Intourist. During the six months ended June 30, 2006, the buyer has refunded contributions of Sistema and Sistema-Hals to the share capital of Pokrovka 40, and entered into a binding contract to acquire their ownership interests in that entity upon satisfactory transfer of the title for the completed office building to Pokrovka 40.

(Amounts in thousands of U.S. Dollars unless otherwise stated)

Upon entrance into a binding contract with the buyer, the Group started recognizing revenues and profits from the office part of Pokrovka 40 development project based on percentage of completion of the project. During the six month period ended June 30, 2006, revenues related to the office part of the complex amounted to USD 63,200 thousand. The profit share to be retained by Sistema and its subsidiaries amounted to USD 22,250 thousand.

4. ACQUISITIONS OF SUBSIDIARIES

During the six months ended June 30, 2006, the Group has acquired additional 50% interest in TRK Kazan, thus increasing its ownership interest in this entity to 100% and 51% interest in NPTC Transtekhproekt. The effect of these transactions on the financial statements for the six months ended June 30, 2006 was not significant.

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Cash and cash equivalents on deposit with:		
Third parties	13,584	3,732
Moscow Bank of Reconstruction and Development ("MBRD"), a subsidiary of Sistema	9,705	6,630
Total	**23,289**	**10,362**

The Group had nil and USD 500 thousand of time deposits classified as cash equivalents as of June 30, 2006 and December 31, 2005, respectively.

6. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net of provision for doubtful debts, as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Trade receivables from third parties	7,308	6,267
Trade receivables from Sistema subsidiaries	816	14,958
Less: provision for doubtful debts	(102)	(296)
Total	**8,022**	**20,929**

As of December 31, 2005, trade receivables from Sistema subsidiaries include USD 14,442 thousand due from MGTS for reimbursement of construction costs incurred.

(Amounts in thousands of U.S. Dollars unless otherwise stated)

7. TAXES RECEIVABLE

Taxes receivable as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
VAT receivable	24,280	22,608
Other taxes receivable	1,497	2,450
Total	**25,777**	**25,058**

8. PREPAID EXPENSES AND OTHER ASSETS, NET

Prepaid expenses and other assets, net of provision for doubtful debts, as June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Advance payments to third parties	4,774	3,233
Other receivables from Sistema subsidiaries	4,188	276
Prepaid expenses	1,875	1,111
Other assets	2,401	1,597
Less: provision for doubtful debts	(2,407)	(2,300)
Total	**10,831**	**3,917**

Management assesses the likelihood of the performance of services in respect of advances paid on an annual basis. This assessment identified advances paid for construction of residential property for which the receipt of services is unlikely and, accordingly, has provided for those advances paid.

9. LOANS AND NOTES RECEIVABLE

Loans and notes receivable as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Loans and promissory notes receivable from subsidiaries of Sistema	8,177	7,258
Loans and promissory notes receivable from third parties	4,125	450
Total	**12,302**	**7,708**

(Amounts in thousands of U.S. Dollars unless otherwise stated)

10. COSTS AND ESTIMATED EARNINGS IN EXCESS OF BILLINGS ON UNCOMPLETED CONTRACTS

Costs and estimated earnings in excess of billings on uncompleted contracts as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Accumulated costs and earnings	60,614	102,345
Less: amounts billed	(26,909)	(63,997)
Total	**33,705**	**38,348**

11. REAL ESTATE INVESTMENTS, NET

Real estate investments, net of accumulated depreciation, as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Real estate developed for sale	**201,484**	**124,312**
Income producing properties:		
Buildings and constructions	54,791	51,290
Construction in progress	-	130
	54,791	**51,420**
Less: accumulated depreciation	(4,286)	(3,840)
Total	**50,505**	**47,580**
Total	**251,989**	**171,892**

Depreciation charge for the six months ended June 30, 2006 and 2005 amounted to USD 1,175 thousand and USD 658 thousand, respectively.

(Amounts in thousands of U.S. Dollars unless otherwise stated)

12. PLANT AND EQUIPMENT, NET

Plant and equipment, net of accumulated depreciation, as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Plant and equipment	4,837	3,114
Other assets	2,609	2,136
	7,446	**5,250**
Less: accumulated depreciation	(1,756)	(1,894)
Total	**5,690**	**3,356**

Depreciation charge for the six months ended June 30, 2006 and 2005 amounted to USD 463 thousand and USD 279 thousand, respectively.

13. DEVELOPMENT RIGHTS AND OTHER INTANGIBLE ASSETS, NET

Development rights and other intangible assets, net of accumulated amortization, as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Development rights – Kuntsevo properties	43,156	43,156
Other intangible assets	304	137
	43,460	43,293
Less: accumulated amortization	(191)	(115)
Total	**43,269**	**43,178**

Amortization charged for the six months ended June 30, 2006 and 2005 amounted to USD 76 thousand and USD 26 thousand, respectively.

Management estimates that on the basis of the amortization policy referred to in Note 2, the estimated amortization expense is as follows:

Year ended June 30,	
2007	6,657
2008	6,657
2009	6,657
2010	6,657
2011	6,657
Thereafter	9,984
Total	**43,269**

(Amounts in thousands of U.S. Dollars unless otherwise stated)

Actual amortization expense to be reported in future periods could differ from these estimates as a result of new intangible assets acquisitions, changes in useful lives and other relevant factors.

14. INVESTMENTS IN SHARES

Investments in shares, as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Sibmost	2,400	-
Other	267	287
Total	**2,667**	**287**

In January 2006, PSO Sistema-Hals acquired 25% plus one share of Sibmost for USD 2,400 thousand. Sibmost is a leading infrastructure project manager and developer in the Siberian Federal Region.

In May 2006, Sistema-Hals sold its stake in Regiony for USD 3,094 thousand. The gain from disposal amounted to USD 3,078 thousand.

15. PAYABLES TO SUPPLIERS AND SUBCONTRACTORS

Payables to suppliers and subcontractors as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Payables to third parties	35,434	10,568
Payables to Sistema subsidiaries	2,425	1,580
Total	**37,859**	**12,148**

16. BILLINGS IN EXCESS OF COSTS AND ESTIMATED EARNINGS ON UNCOMPLETED CONTRACTS

Billings in excess of costs and estimated earnings on uncompleted contracts as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Amounts billed	90,099	44,820
Less: accumulated costs and earnings	(23,540)	(30,824)
Total	**66,559**	**13,996**

(Amounts in thousands of U.S. Dollars unless otherwise stated)

17. ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued expenses and other liabilities as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Advances received from third parties	45,374	-
Advances received from Sistema subsidiaries	3,114	-
Accrued expenses and other liabilities to third parties	10,301	3,725
Other liabilities to Sistema subsidiaries	92	1,473
Total	**58,881**	**5,198**

18. CONSTRUCTION OBLIGATIONS

Upon acquisition of Kuntsevo-Invest, the Group assumed obligations to construct two residential buildings (15, Elninskaya St. and 9, Aviatorov St.). During the six months ended June 30, 2006, the Group incurred related construction costs in the amount of USD 8,435 thousand. The construction costs will be offset against the respective obligations when the completed buildings will be accepted by the customers and the Moscow City Government.

19. LOANS AND NOTES PAYABLE

The Group's loans and notes payable as of June 30, 2006 and December 31, 2005 consisted of the following:

	June 30, 2006	December 31, 2005
Loans and notes payable to Sistema and its subsidiaries		
Sistema	40,891	45,259
MBRD	107,880	129,572
Other Sistema subsidiaries	3,593	7,609
Total	**152,364**	**182,440**
Loans and notes payable to third parties:		
Elizairing EKS	6,629	-
Commerzbank	-	20,000
West LB Vostok	-	10,400
Other	5,597	3,660
Total	**12,226**	**34,060**
Total loans and notes payable	**164,590**	**216,500**
Current portion of loans and notes payable	132,784	152,857
Non-current portion of loans and notes payable	31,806	63,643

(Amounts in thousands of U.S. Dollars unless otherwise stated)

The Group's activities have historically been financed through the provision of loans and notes by the controlling shareholder and its subsidiaries.

The weighted average interest rate on loans is 8.51% and 10.17% as of June 30, 2006 and December 31, 2005, respectively.

The interest rates on loans and notes obtained by the Group from Sistema and its subsidiaries are fixed and range from 0% to 16%.

The interest rate on the Commerzbank loan was LIBOR+5% (9.84% as of December, 31 2005). The loan was guaranteed by Sistema and has been settled in March 2006.

The interest rate on the West LB Vostok loan was LIBOR+6.8% (11.64% as of December 31, 2005). The loan was guaranteed by MGTS, a subsidiary of Sistema, and has been settled in March 2006.

In June 2006, the Group entered into a loan agreement with Elizairing EKS for a total amount of USD 6,629 thousand. The interest rate under the agreement is 12%. Funds for this loan were provided by MBRD.

The schedule of repayments of long-term debt is as follows:

Year ended June 30,	
2007	132,784
2008	21,075
2009	3,008
2010	7,723
Thereafter	-
Total	**164,590**

20. OPERATING EXPENSES

Operating expenses for the six months ended June 30, 2006 and 2005 comprised the following:

	Six months ended June 30,	
	2006	**2005**
Cost of sales of development projects	45,926	14,578
Payroll and employee related costs	11,280	6,240
Consulting services	467	1,379
Depreciation and amortization	1,714	963
Rent of premises and land	830	738
Security expenses	506	672
Taxes other than income taxes	135	296
Repairs and maintenance	1,182	56
Utilities and energy costs	472	795
Insurance	51	204
Advertising and marketing	248	208
Bad debt (reversal)/expense	(87)	2,300
Other	1,903	920
Total	**64,627**	**29,349**

(Amounts in thousands of U.S. Dollars unless otherwise stated)

21. INCOME TAXES

The Group's provision for income taxes for the six months ended June 30, 2006 and 2005 was as follows:

	Six months ended June 30, 2006	Six months ended June 30, 2005
Current expense	2,299	1,769
Deferred tax expense/(benefit)	2,449	173
Total	**4,748**	**1,942**

The provision for income taxes is different from that which would be obtained by applying the statutory income tax rate of 24% to income/(loss) before income tax and minority interests. The items causing this difference are as follows:

	Six months ended June 30, 2006	Six months ended June 30, 2005
Income tax provision computed on income before taxes at statutory rate	9,304	236
Adjustments due to:		
Non-deductible items	664	79
Non-taxable items	(30)	(114)
Share of profit on Pokrovka 40 development project, retained by the controlling shareholder	(5,340)	-
Taxable losses not carried forward	874	1,820
Currency exchange and translation differences	(724)	(79)
Total	**4,748**	**1,942**

Temporary differences between the Russian statutory tax accounts and these financial statements give rise to the following deferred tax assets and liabilities as of June 30, 2006 and December 31, 2005.

	June 30, 2006	December 31, 2005
Deferred tax assets		
Construction obligations	5,062	5,062
Other	1,089	914
Less: valuation allowance	(6,151)	(5,976)
Total deferred tax assets	**-**	**-**
Deferred tax liabilities		
Development rights	(10,330)	(10,330)
Other	(3,002)	(553)
Total deferred tax liabilities	**(13,332)**	**(10,883)**

(Amounts in thousands of U.S. Dollars unless otherwise stated)

Valuation allowance is primarily attributable to the deferred tax asset relating to construction obligations. The valuation allowance has been recorded, as it is 'more likely than not' that taxable income generated by the respective entity of the Group during the periods when the deductible temporary differences are expected to reverse, will not be sufficient for this asset to realize.

22. RELATED PARTY TRANSACTIONS

During the six months ended June 30, 2006 and 2005, the Group entered into the following transactions with Sistema and its subsidiaries:

	Six month ended June 30,	
	2006	**2005**
Services provided	3,287	598
Services purchased	(148)	(146)
Interest income	444	-
Interest costs	(6,244)	(5,137)

Agreements to act as a developer

In the six months ended June 30, 2006 and 2005, the Group had agreements with Detsky Mir, NIIDAR and MGTS, subsidiaries of Sistema, to act as a developer for projects to redevelop properties owned by these entities.

The Group has an investment agreement with Manezh 13/1, a wholly owned subsidiary of Sistema, for redevelopment of Mokhovaya 13/1 office building, owned by Manezh 13/1. In the year ended December 31, 2005, Sistema decided to appoint a contractor, owned by a director of Sistema-Hals, to perform construction and finishing works under the project. The Group is recognizing a fee related to the supervisory, management and administrative services provided in respect of the Mokhovaya 13/1 redevelopment project, determined as 5% of the total construction costs.

Finance costs

In the six months ended June 30, 2006 and 2005, borrowing costs on the Group's loans from MBRD amounted to USD 6,244 thousand and USD 5,137 thousand, respectively. Interest income on MBRD's promissory notes and deposits with MBRD for the six months ended June 30, 2006 and 2005 amounted to USD 444 thousand and nil, respectively.

Site management services provided

Services provided in the six months ended June 30, 2006 and 2005, included site management revenues of USD 3,287 thousand and USD 598 thousand, respectively. These services are being performed primarily for Sistema and its subsidiary MTS.

Rental revenues

During the six months ended June 30, 2006 and 2005, the Group received rental revenues from Radio Centre, then a subsidiary of Sistema, of USD 205 thousand and USD 312 thousand, respectively.

(Amounts in thousands of U.S. Dollars unless otherwise stated)

Certain single-family houses owned by Mosdachtrest are leased to Sistema's related parties. The amount of rental revenues from these leases has been insignificant for the six months ended June 30, 2006 and 2005.

Related party balances as of June 30, 2006 and December 31, 2005 are disclosed in the corresponding notes to the financial statements.

23. GUARANTEES AND PLEDGES

Warranties and guarantees of work performed – The Group is contractually responsible for the quality of construction works performed subsequent to the date at which the relevant object was handed over, generally for an exploitation period up to 2 years subsequent to handover. Based upon prior experience with warranty claims, which have not been significant, no contingent liabilities have been recorded in the Group's financial statements in relation to warranties and guarantees for work performed.

Pledges – As of June 30, 2006, common shares of the Group's entities have been pledged under borrowings from MBRD as follows:

	Number of shares	**Ownership interest**
Mosdachtrest	7,093	39%
Landshaft	72	72%

As of June 30, 2006, the Group has also pledged title to apartments with the fair value of USD 7,781 thousand and future proceeds on sale of hotel part of Pokrovka 40 real estate complex in amount of USD 4,867 thousand.

As of June 30, 2006, Sistema has guaranteed MBRD's borrowings to the Group in the amount of USD 19,963 thousand.

As of June 30, 2006, MBRD guaranteed PSO Sistema-Hals' obligations to FGUP Dorogi Rossii to provide services in relation to a highway construction project. The guarantee is secured by funds of PSO Sistema-Hals deposited in MBRD in the amount of USD 1,810 thousand.

24. COMMITMENTS AND CONTINGENCIES

a) Licenses

The Group's revenues are derived from operations conducted pursuant to licenses issued by state authorities. Our principal licenses expire in 2007; however, our construction activities remain subject to licensing only until January 1, 2007, according to the Federal Law on Licensing of Certain Types of Activities.

b) Taxation environment

Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include VAT, income tax, unified social tax, together with others. The government's policy on implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established.

Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that is more significant than typically found in countries with more developed tax systems. Generally, tax declarations remain open and subject to inspection for a period of three years following the tax year. Management believes that it has adequately provided for tax liabilities; however, the risk remains that relevant authorities could take a different position with regard to interpretive issues.

c) Russian environment and current economic situation

Over the past decade Russia has undergone substantial political and social changes. As an emerging market, Russia does not possess a fully developed business and regulatory infrastructure that would generally exist in a more mature market economy. The Russian government is attempting to address these issues; however it has not yet fully implemented the reforms necessary to create banking and judicial systems that usually exist in more developed markets. As a result, operations in Russia involve risks that typically do not exist in more developed markets.

d) Industry regulation

Construction and development of real estate in Russia is primarily governed by the Civil Code, the Federal Land Code, the Federal Law on the State Registration of Rights to Immovable Property and Transactions Therewith, construction norms and regulations approved by the Ministry of Industry and Energy, and others. In addition, a new City Construction Code and the Federal Law on Entry into Effect of the City Construction Code came into force on December 30, 2004. Construction and development involves compliance with burdensome regulatory requirements, and authorizations from a large number of authorities at the federal, regional and local levels. In particular, the Federal Agency on Construction, Housing and the Communal Sector, or Rosstroi, the Federal Service for Supervision in the Sphere of Use of Natural Resources, the Federal Service on Ecological, Technologic and Nuclear Supervision and regional bodies of the state architectural and construction supervision are involved in the process of authorizing and supervising real estate development.

In addition, construction is subject to all applicable environmental, fire safety and sanitary norms and regulations.

The Group is constructing a number of cottages without obtaining necessary construction permits. However, management is in the process of addressing this issue and does not foresee that this will adversely affect the Group's financial position or results of operations.

e) Legal proceedings

In the ordinary course of business, the Group may be a party to various legal and tax proceedings, and be subject to claims. In the opinion of management, the Group's liability, if any, in all current and pending litigations or other legal proceedings will not have a material effect upon the financial condition, results of operations or liquidity of the Group, other than as is already reflected in these financial statements.

f) Commitments under construction contracts

The Group has entered into agreements with third parties for construction of objects which will require capital outlays subsequent to June 30, 2006. A summary of significant commitments under construction contracts as of June 30, 2006 is provided below:

Leningradsky 39 – The Group has contracted for construction works, including foundations, shell and core, utilities and other general construction expenditures. Commitments under these contracts amounted to USD 79,771 thousand as of June 30, 2006. In addition, in connection with this project, the Group undertook obligations to provide the Central Army Sports Club ("CSCA") with 17,437 sq.m of residential housing.

MGTS properties – The Group entered contractual agreements for reconstruction of the abovementioned buildings. Commitments under these contracts amounted to USD 19,128 thousand as of June 30, 2006.

Mosdachtrest properties – The Group has contracted for construction works related to Mosdachtrest properties. Commitments under these contracts amounted to USD 18,233 thousand as of June 30, 2006.

Western Kuntsevo properties – The Group has hired a contractor to perform general construction works. Commitments under these contracts amounted to USD 17,250 thousand as of June 30, 2006.

Moscow City Government – The Group has obligations to manage a number of construction projects which will be completed subsequent to the balance sheet date. The Moscow City Government has the obligation to finance these construction projects, the Group generating commissions based on the agreed upon budget cost of the project.

g) Operating leases

With a few exceptions, the land in Moscow is owned by the Moscow Government. The lease of land in Moscow is subject to a separate regulatory regime administered by the Government. As a general rule, such land lease rights are granted by the Government on the basis of an auction or tender, typically in exchange for either an upfront payment or ongoing consideration in the form of periodic lease payments. Periodic lease payments under land lease agreements in effect during the six months ended June 30, 2006 and 2005 have not been significant.

Mosdachtrest leases numerous cottages to individuals at a discount to market rates as a result of the Moscow Government requirement to make available certain properties to pensioners and others entitled to social benefits. Furthermore, certain residents of Mosdachtrest settlements hold life or long-term leases, which could prevent or delay the Group from developing or redeveloping such settlements. Even if granted the right to develop or redevelop these properties, the Group would be required to transfer these residents to housing of a similar quality.

h) Commitment to maintain production at Yalta Fish Processing Plant

In acquisition of Yalta Fish Processing Plant, the Group assumed obligations to maintain activities and workforce of the plant up to 2008. Management does not expect this commitment to result in significant cash outflows for the Group.

i) Environmental regulations

Environmental laws and regulations impose certain restrictions and encumbrances on the properties that we hold or develop. Some of our land plots under development are located in areas that have special environmental protection. In addition, the development of a project may be subject to certain obligations, including planting of greenery and clean-up measures. These requirements may result in delays of development of our projects or additional costs.

(Amounts in thousands of U.S. Dollars unless otherwise stated)

25. SEGMENT INFORMATION

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", established standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the chief operating decision maker or group in deciding how to allocate resources and in assessing performance.

The Group's operating segments are: Real estate development, Project and construction management, Real estate asset management and Facility management. Activities of the Group's Real estate development segment include identification of investment opportunities, performance of feasibility studies, obtaining necessary construction permits, project financing and marketing activities. The Project and construction management segment is currently primarily acting as a construction manager to oversee compliance by contractors with design specifications and the terms of a particular contract. The Real estate asset management segment is involved in renting of residential and commercial properties that we have developed or acquired. The Facility management segment provides site management services, including security, cleaning, staffing, technical support, repair and renovation, as well as general building maintenance. The Group's management evaluates performance of the segments based on both operating income and income before income taxes and minority interests.

Intersegment eliminations presented below consist primarily of intersegment sales transactions, elimination of capitalized interest on intersegment borrowings and other intersegment transactions conducted under the normal course of operations.

As of and for the six months ended June 30, 2006	Real estate development	Project and construction management	Real estate asset management	Facility management	Total
Net sales to external customers	77,660	13,296	11,242	4,422	106,620
Intersegment sales	418	67	186	601	1,272
Interest income	892	374	-	-	1,266
Interest expense, net of amounts capitalized	(2,647)	(100)	(316)	-	(3,063)
Depreciation and amortization	(192)	(181)	(1,358)	(5)	(1,736)
Operating income/(loss)	32,889	4,858	4,291	325	42,363
Income tax expense	(2,669)	(1,091)	(912)	(76)	(4,748)
Income/(loss) before income tax and minority interests	31,316	4,395	3,553	(498)	38,766
Segment assets	321,637	41,012	82,632	4,800	450,081
Capital expenditures	46,708	1,151	14,653	363	62,875

As of and for the six months ended June 30, 2005	Real estate development	Project and construction management	Real estate asset management	Facility management	Total
Net sales to external customers	12,575	9,435	7,291	3,944	33,245
Intersegment sales	212	3	230	73	518
Interest income	406	15	-	-	421
Interest expense, net of amounts capitalized	(881)	(1,422)	(212)	(5)	(2,520)
Depreciation and amortization	(100)	(67)	(780)	(17)	(964)
Operating income/(loss)	(3,956)	5,443	2,876	(112)	4,251
Income tax expense	(132)	(1,283)	(521)	(6)	(1,942)
Income/(loss) before income tax and minority interests	(6,860)	3,926	4,039	(121)	984
Segment assets	231,012	22,935	82,681	3,657	340,285
Capital expenditures	8,186	100	6,185	21	14,492

(Amounts in thousands of U.S. Dollars unless otherwise stated)

The reconciliation of segment operating income to the income before income tax and minority interests and reconciliation of segment assets to the total assets of the Group are as follows:

	Six months ended June 30,	
	2006	**2005**
Total segment operating income	42,363	4,251
Intersegment eliminations	(370)	(355)
Other income, net	268	128
Interest income	846	220
Interest expense, net of amounts capitalized	(2,600)	(2,307)
Loss on foreign currency transactions	(4,819)	(953)
Gain on sale of equity investee	3,078	-
Income before income tax and minority interests	**38,766**	**984**
Total segment assets	450,081	340,285
Intersegment eliminations	(32,540)	(54,496)
Total assets	**417,541**	**285,789**

26. SUBSEQUENT EVENTS

Transfers to Sistema – In August 2006, to complete the corporate reorganization of Sistema's Real Estate segment, Sistema-Hals acquired from Sistema's subsidiaries outside of the Group a 99% stake in Terra, a 98% stake in Yalta Fish Processing Plant, 100% stake in Kaskad and a 100% stake in Hotel Korona-Intourist for an aggregate consideration of USD 30,300 thousand.

In August 2006, the Group acquired from related parties a 100% stake in Nostro for consideration of USD 26,600 thousand and committed to additionally invest USD 7,200 thousand to settle the debts of that entity. Nostro owns a building located at Sadovnicheskaya st., 75. The difference between the purchase price for the Group and the price paid by the related parties was recorded by the Group as a distribution to the related parties.

Financing – In August 2006, Sistema-Hals entered into a loan facility with Deutsche Bank AG in the amount of USD 140,000 thousand for the term of one year. The loan facility was extended for the Group's general operational needs and refinancing of its existing debt facilities and bears interest rate of 8.65%. The debt is guaranteed by Sistema. The guarantee fee payable by the Group is 3% per annum. The loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios.

In September 2006, Sistema-Hals entered into a loan facility with NOMURA International Plc in the amount of USD 100,000 thousand for the term of one year. The loan facility was extended for the Group's general corporate purposes and working capital needs, refinancing of its existing debt facilities, as well as acquisition and development of real estate assets and bears interest rate of 8.45%. The debt is guaranteed by Sistema. The guarantee fee payable by the Group is 3% per annum. The loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios.

In October 2006, Sistema-Hals entered into a loan facility with UBS AG in the amount of USD 100,000 thousand for the term of one year. The loan facility was extended for the Group's general operational needs and refinancing of its existing debt facilities and bears interest rate of 8.65%. The debt is guaranteed by Sistema. The guarantee fee payable by the Group is 3% per annum. The loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios.

Acquisitions – In October 2006, Sistema-Hals acquired a 19% stake in Kuntsevo-Invest for cash consideration of USD 102 thousand, thus increasing its ownership interest in this entity to 100%.