Joint Stock Company
Central Telecommunication Company

Consolidated Financial Statements

For the year ended December 31, 2005
with Independent Auditor's Report

JSC CenterTelecom

Consolidated Financial Statements

For the year ended December 31, 2005

Contents

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Independent Auditors' Report

To the Shareholders and Board of Directors of JSC Central Telecommunication Company

1. We have audited the accompanying consolidated balance sheet of Joint-Stock Central Telecommunication Company (a Russian open joint-stock company – hereinafter "the Company"), as at December 31, 2005 and the related consolidated statements of operations, cash flows and changes in equity for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of OJSC "Russian Telecommunications Network" (a Russian open joint-stock company – hereinafter "RTS"), a wholly-owned subsidiary, which statements reflect total consolidated assets of 986,633 thousand roubles as at December 31, 2005, total consolidated revenues of 970,359 thousand roubles and consolidated pre-tax loss of 83,942 thousand roubles for the year then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for RTS, is based solely on the report of other auditors.

2. Except as discussed in paragraph 3 and 4 below we conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

3. As described in Note 2 "Basis of Presentation of the Financial Statements" and Note 5 "Property, Plant and Equipment", the Company transitioned to International Financial Reporting Standards (IFRS) at January 1, 2003 and applied an exemption in IFRS 1, First-time Adoption of International Financial Reporting Standards, which permits an entity to measure property, plant and equipment at the date of transition to IFRS at fair value and use that fair value as deemed cost. However, we were not able to satisfy ourselves as to whether the carrying amounts of property, plant and equipment as at January 1, 2003 were representative of fair value. Accordingly, we were unable to determine whether the carrying value of property, plant and equipment as of December 31, 2005 and 2004, complies with the requirements of IFRS. Further, we were unable to satisfy ourselves as to the related (i) depreciation expense for the years presented and (ii) deferred tax balances as at the reporting dates and deferred tax expense for the years presented.

4. As described in Note 24 "Pension Liabilities", the Company provides certain long term benefits to its employees. The Company engaged an independent actuary to estimate its obligations regarding such benefits as of December 31, 2005, 2004 and 2003. We were unable to obtain sufficient support for the actuarial assumptions and significant underlying data used. We were therefore unable to satisfy ourselves with respect to the pension obligation as of the balance sheet dates, the related expense for the defined benefit pension plan for the years presented, and related disclosures.

5. The Company accounted for the purchase of subsidiaries based on historical cost of their net assets. The Company did not identify and estimate the fair value of the acquired assets and liabilities as required by IFRS 3, Business Combinations. We were not able to quantify the respective adjustments to the financial statements for the year ended December 31, 2005. In addition, we were unable to satisfy ourselves as to whether the carrying amounts of non-current assets in subsidiaries are not in excess of their recoverable values.

6. In our opinion, based on our audit and the report of other auditors, except for the effects on the financial statements of such adjustments, if any, which might have been determined to be necessary had we been able to satisfy ourselves as to the matters referred to in paragraphs 3 and 4 above, and except for the effects on the financial statements of the matter referred to in paragraph 5 above, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Joint-Stock Central Telecommunication Company as at December 31, 2005, and the consolidated results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC

June 16, 2006

JSC CenterTelecom

Consolidated Balance Sheet

As of December 31, 2005

(in thousands of roubles)

	Notes	2005	2004
ASSETS			
Non–current assets			
Property, plant and equipment, net	**5**	**30,176,743**	30,008,572
Intangible assets and goodwill, net	**6**	**4,096,394**	3,422,106
Investments in associates	**8**	**20,081**	15,927
Long–term investments	**10**	**25,621**	13,662
Long–term accounts receivable and other assets	**11**	**221,546**	317,594
Long–term advances given	**12**	**951,182**	1,108,682
Deferred income tax asset	**30**	**105,787**	–
Total non–current assets		**35,597,354**	34,886,543
Current assets			
Inventories, net	**13**	**513,628**	577,518
Accounts receivable, net	**14**	**1,877,457**	2,068,164
Other current assets	**15**	**1,556,475**	2,028,065
Income tax prepaid		**82,877**	78,625
Cash and cash equivalents	**16**	**994,627**	1,417,214
Total current assets		**5,025,064**	6,169,586
TOTAL ASSETS		**40,622,418**	41,056,129
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Share capital	**18**	**6,900,165**	1,219,366
Unrealized gain on available–for–sale investments		**–**	4,517
Treasury shares		**(2,808)**	–
Retained earnings		**4,384,797**	10,854,657
Total equity attributable to equity holders of the parent		**11,282,154**	12,078,540
Minority interest		**14,366**	23,974
Total equity		**11,296,520**	12,102,514
Non–current liabilities			
Long–term borrowings	**19**	**6,824,529**	13,003,785
Long–term finance lease obligations	**20**	**1,562,302**	1,775,171
Pension Liabilities	**24**	**850,420**	565,000
Deferred revenue		**833,884**	794,390
Long–term Income tax payable	**23**	**10,604**	10,973
Long–term other tax payable	**23**	**14,589**	13,373
Deferred income tax liability	**30**	**–**	147,720
Other long–term liability		**34,398**	4,231
Total non–current liabilities		**10,130,726**	16,314,643
Current liabilities			
Accounts payable, accrued expenses and advances received	**21**	**2,277,667**	3,039,662
Payables to Rostelecom		**190,533**	191,543
Income tax payable		**42,739**	181,413
Other taxes payable	**22**	**1,098,858**	1,070,193
Dividends payable	**32**	**8,273**	15,241
Short–term borrowings	**19**	**2,263,764**	3,604,397
Current portion of long–term borrowings	**19**	**12,570,338**	3,864,032
Current portion of long–term finance lease obligations	**20**	**743,000**	672,491
Total current liabilities		**19,195,172**	12,638,972
Total liabilities		**29,325,898**	28,953,615
TOTAL EQUITY AND LIABILITIES		**40,622,418**	41,056,129

The accompanying notes form an integral part of these consolidated financial statements.

JSC CenterTelecom

Consolidated Statement of Operations

for the year ended December 31, 2005

(in thousands of roubles, except per share amounts)

	Notes	2005	2004
Revenues	**26**	**28,700,650**	26,029,080
Wages, salaries, other benefits and payroll taxes		**(10,197,813)**	(9,713,189)
Depreciation and amortization	**5,6**	**(4,860,503)**	(4,243,356)
Materials, repairs and maintenance, utilities		**(2,719,610)**	(2,500,376)
Taxes other than income tax		**(774,186)**	(625,344)
Interconnection charges		**(4,003,521)**	(4,055,981)
Provision for impairment of receivables	**14**	**(296,524)**	(831,322)
Gain/(loss) on disposal of property, plant, and equipment		**(56,664)**	9,318
Other operating expenses	**27**	**(3,525,341)**	(3,312,229)
Operating profit		**2,266,488**	756,601
Share of result of associates		**3,049**	2,282
Interest expense, net	**28**	**(2,607,604)**	(1,879,617)
Gain from Investments	**29**	**8,872**	297,358
Foreign exchange gain, net		**78,354**	59,845
Other income and expenses, net		**22,357**	(83,614)
Loss before income tax		**(228,484)**	(847,145)
Income tax expense	**30**	**(420,735)**	(154,074)
Loss for the year		**(649,219)**	(1,001,219)
Attributable to:			
Equity holders of the parent		**(649,862)**	(1,009,223)
Minority interests		**643**	8,004
Net Loss for the year		**(649,219)**	(1,001,219)
Loss per share			
- basic and diluted, for loss for the year attributable to equity holders of the parent	**31**	**(0.309)**	(0.480)

The accompanying notes form an integral part of these consolidated financial statements.

JSC CenterTelecom
Consolidated Cash Flow Statement
for the year ended December 31, 2005
(in thousands of roubles, except per share amounts)

	2005	2004
Cash flows from operating activities:		
Loss before income tax	**(228,484)**	(847,145)
Adjustments for:		
Depreciation and amortization	**4,860,503**	4,243,356
Loss/(gain) on disposal of property, plant and equipment	**56,664**	(9,318)
Provision for impairment of receivables	**296,524**	831,322
Provision for obsolescence of inventory	**585**	–
Share of result of associates	**(3,049)**	(2,282)
Gain from investments	**(8,872)**	(297,358)
Interest expense, net	**2,607,604**	1,879,617
Foreign exchange gain, net	**(78,354)**	(59,845)
Operating cash flows before working capital changes	**7,503,121**	5,738,347
Increase in accounts receivable	**(88,097)**	(1,082,994)
Decrease/(increase) in other current assets	**508,014**	(317,244)
Decrease/(increase) in inventories	**66,168**	(28,848)
Increase/(decrease) in accounts payable and accrued expenses	**346,365**	(13,670)
Increase in taxes payable other than income tax	**43,253**	45,656
Increase in pension liabilities	**285,420**	200,000
Cash flows generated from operations	**8,664,244**	4,541,247
Interest paid	**(3,015,619)**	(1,839,446)
Income tax paid	**(804,770)**	(431,940)
Net cash flows from operating activities	**4,843,855**	2,269,861
Cash flows from investing activities:		
Purchase of property, plant and equipment	**(4,945,677)**	(7,112,382)
Purchase of intangible assets	**(126,451)**	(74,289)
Purchase of Oracle E–Business Suite software	**(164,888)**	(274,271)
Purchase of Amdocs Billing Suite software	**(172,778)**	–
Proceeds from sales of property, plant and equipment	**70,690**	98,230
Purchase of subsidiaries, net of cash acquired	**(141,377)**	(1,372,349)
Proceeds from sale of subsidiaries, net of cash disposed	**–**	174,391
Purchase of investments and other financial assets	**74,938**	(82,583)
Proceeds from disposal of investments and other assets	**8,605**	122,947
Interest received	**2,480**	62,639
Dividends received	**214**	20
Net cash flows from investing activities	**(5,394,244)**	(8,457,647)
Cash flows from financing activities:		
Purchase of treasury shares	**(2,808)**	–
Proceeds from borrowings	**5,268,646**	8,156,516
Repayment of borrowings	**(6,517,620)**	(5,791,976)
Proceeds from debt securities issued	**–**	5,555,477
Repayment of debt securities	**(608,633)**	–
Proceeds from promissory notes	**5,025,556**	1,202,651
Repayment of promissory notes	**(1,247,405)**	(1,052,123)
Repayment of finance lease obligations	**(750,952)**	(650,277)
Repayment of vendor financing obligations	**(234,547)**	(508,280)
Repayment of promissory notes for Amdocs Billing Suite Software	**(687,613)**	–
Increase (decrease) in other non–current liabilities	**30,168**	(11,808)
Dividends paid	**(146,168)**	(347,379)
Dividends paid to minority	**(822)**	(390)
Net cash flows from financing activities	**127,802**	6,552,411
Net increase/(decrease) in cash and cash equivalents	**(422,587)**	364,625
Cash and cash equivalents at the beginning of the year	**1,417,214**	1,052,589
Cash and cash equivalents at the end of the year	**994,627**	1,417,214

The accompanying notes form an integral part of these consolidated financial statements.

JSC CenterTelecom

Consolidated Statement of Changes in Equity

For the year ended December 31, 2005

(in thousands of roubles)

		Share capital							
	Notes	**Preference shares**	**Ordinary shares**	**Treasury shares**	**Retained earnings**	**Unrealized gain on available–for–sale investments**	**Total equity holders of parent**	**Minority interest**	**Total equity**
Balance at December 31, 2003		304,840	914,526	–	12,606,161	2,624	13,828,151	358	13,828,509
Effect of adjustments		–	–	–	(394,984)	–	(394,984)	23,115	(371,869)
Balance at December 31, 2003 (adjusted)		304,840	914,526	–	12,211,177	2,624	13,433,167	23,473	13,456,640
Loss for the year		–	–	–	(1,009,223)		(1,009,223)	8,004	(1,001,219)
Dividends to equity holders of parent	**32**	–	–	–	(347,297)	–	(347,297)	–	(347,297)
Dividends of subsidiaries to minority shareholders							–	(390)	(390)
Acquisition of minority interest in existing subsidiaries							–	(10,479)	(10,479)
Minority interest arising on acquisition of subsidiaries							–	3,366	3,366
Unrealized gain on available–for–sale investments		–	–	–	–	1,893	1,893	–	1,893
Balance at December 31, 2004		**304,840**	**914,526**	**–**	**10,854,657**	**4,517**	**12,078,540**	**23,974**	**12,102,514**
Loss for the year					**(649,862)**		**(649,862)**	**643**	**(649,219)**
Dividends to equity holders of parent	**32**	–	–	–	**(139,199)**	–	**(139,199)**	–	**(139,199)**
Dividends of subsidiaries to minority shareholders		–	–	–	–	–	–	**(822)**	**(822)**
Purchase of treasury shares	**18**	–	–	**(2,808)**	–	–	**(2,808)**	–	**(2,808)**
Realized gain on available–for–sale investments		–	–	–	–	**(4,517)**	**(4,517)**	–	**(4,517)**
Acquisition of minority interests in existing subsidiaries		–	–	–	–	–	–	**(9,429)**	**(9,429)**
Share capital increase		**1,420,180**	**4,260,619**	–	**(5,680,799)**	–	–		–
Balance at December 31,2005		**1,725,020**	**5,175,145**	**(2,808)**	**4,384,797**	**–**	**11,282,154**	**14,366**	**11,296,520**

The accompanying notes form an integral part of these consolidated financial statements.

1. General Information

Authorization of Accounts

The consolidated financial statements of JSC CenterTelecom and its subsidiaries – (hereinafter "the Company") for the year ended December 31,2005 were authorized for issue by the General Director and the Chief Accountant of the Company on June 16, 2006.

The Company

The Company is an open joint stock company incorporated in accordance with the laws of the Russian Federation.

The registered office of the Company is Russia, Moscow region, city of Khimki, Proletarskaya st. 23.

The Company's principal activity is providing telephone services (including local, long-distance and international calls), telegraph, data transfer services, rent of communication channels and wireless communication services on the territory of Central Federal District of the Russian Federation.

Open joint-stock company Svyazinvest, controlled by the Russian Government, as a holding company, as of December 31, 2005 owned 50.69% of the Company's ordinary voting stock.

Information on the Company's main subsidiaries is disclosed in Note 7. All subsidiaries are incorporated under the laws of the Russian Federation, unless otherwise stated.

Presentation of Financial Statements

The consolidated financial statements of JSC CenterTelecom are prepared on the basis of standalone financial statements of the parent and its subsidiaries and associates prepared under unified accounting policy.

The measurement and presentation currency of the Company is the Russian Rouble, which is the national currency of the Russian Federation.

The consolidated financial statements of the Company are presented in thousands of Russian Roubles.

Tariff Setting

Tariffs relating to intercity traffic are regulated by the government and tariffs for international traffic are regulated by OJSC "Rostelecom" which is controlled by OJSC "Svyazinvest" holding.

In 2005 the Company revised its tariffs for telephone services with the aim to reduce the effect of cross-subsidization between domestic long-distance and local services by changing the tariffs for local telephone calls.

In general, the Company increased tariffs in 2005 and 2004 as follows:

Customer Group	Urban areas (%)		Rural areas (%)	
	2004	2005	2004	2005
Residential	26.32%	33.33%	29.41%	36.36%
Corporate	16.00%	37.93%	16.00%	37.93%
State organizations	16.00%	37.93%	16.00%	37.93%

1. General Information (continued)

Tariff Setting (continued)

New regulations supporting the implementation of the Federal Law on Communications are effective from January 1, 2006. These regulations affect the principles of provision of fixed line telecommunication services and change licensing requirements to the Company (see also Note 37 on tariffs for telecommunication services).

Liquidity and Financial Resources

As of December 31, 2005, the Company's current liabilities exceeded its current assets by 14,170,108 (December 31, 2004 – 6,469,386). The Company incurred pre-tax losses of 228,484 and 847,145 in 2005 and 2004, respectively. As a result, there may be some doubts about the Company's ability to attract further financing and to pay its existing debts as they fall due.

To date, the Company has significantly relied upon short-term and long-term financing to fund the improvement of its telecommunication network. This financing has historically been provided through bank loans, bonds, vendor financing, and finance leases.

If needed, management believes that certain projects may be deferred or curtailed in order to fund the Company's current operating needs. Management believes it will be able to delay payment for certain operating costs to manage its working capital requirements, if necessary.

Through 2006, the Company anticipates funding from a) cash generated from operations; b) bonds placement in the domestic market; c) financing from domestic and international lending institutions.

As described in Note 37, the Company has received a tax assessment for 2,353,512. The Company disagrees with the assessment and is appealing it in court.

2. Basis of Presentation of the Financial Statements

Basis of Preparation

These financial statements have been prepared and presented in accordance with International Financial Reporting Standards ("IFRS").

These financial statements are prepared based on the statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation, with adjustments and reclassifications recorded for the purpose of fair presentation of ending balances, results of operations and cash flows in accordance with IFRS.

These financial statements have been presented on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. Accordingly, the financial statements do not include any adjustments related to the recoverability and classification of recorded asset amounts or any other adjustments that might result if the Company either be unable to continue as a going concern or if the Company was to dispose of assets outside the normal course of its operating plan.

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

2. Basis of Presentation of the Financial Statements (continued)

Basis of Preparation (continued)

The Company transitioned to IFRS as of January 1, 2003 using the provisions of IFRS 1, "First-time Adoption of International Financial Reporting Standards", which is effective for periods starting on or after January 1, 2004. IFRS 1 applies to first-time adopters of IFRS including companies that previously applied some, but not all IFRS, and disclosed this fact in its most recent previous financial statements.

The Company has applied an exemption permitted by IFRS 1 which allows an entity to measure property, plant, and equipment at the date of transition to IFRS at fair value and use that fair value as deemed cost. The Company has also applied the exemption permitted by IFRS 1 which allows an entity to recognize all cumulative actuarial gains and losses on employees defined benefit plans at the date of transition even if the corridor approach is used for actuarial gains and losses.

Management estimates that the carrying value of all of the Company's property, plant and equipment is broadly comparable to their fair values. However, management intends to engage an independent appraiser to support these fair values and as a result, the reported carrying amount of property, plant and equipment may be adjusted. It is expected that the appraisal will be completed in the near future.

The Russian economy was considered hyperinflationary until prior to January 1, 2003. As such, the Company applied IAS 29 "Financial Reporting in Hyperinflationary Economies" by restating non-monetary items, including components of equity (except for the property, plant and equipment, for which fair values as at January 1, 2003 have been used as deemed cost) to the measuring units current at January 1, 2003 by applying the relevant inflation indices to the historical cost. These restated values were used as a basis for accounting in subsequent periods.

The accounting policies adopted are consistent with those of the previous financial year except that the Company has adopted those new/revised standards mandatory for financial years beginning on or after January 1, 2005.

The changes in accounting policies result from adoption of the following new or revised standards:

- IFRS 2 "Share-Based Payment";
- IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations";
- IAS 1 (revised) "Presentation of Financial Statements";
- IAS 2 (revised) "Inventories";
- IAS 8 (revised) "Accounting Policies, Changes in Accounting Estimates and Errors";
- IAS 10 (revised) "Events after the Balance Sheet Date";
- IAS 16 (revised) "Property, Plant and Equipment";
- IAS 17 (revised) "Leases";
- IAS 24 (revised) "Related Party Disclosures";
- IAS 27 (revised) "Consolidated and Separate Financial Statements";
- IAS 28 (revised) "Investments in Associates";
- IAS 31 (revised) "Interests in Joint Ventures";
- IAS 32 (revised) "Financial Instruments: Presentation and Disclosure";
- IAS 33 (revised) "Earnings per Share";
- IAS 39 (revised) "Financial Instruments: Recognition and Measurement".

The principal effects of these changes in policies are discussed below.

2. Basis of Presentation of the Financial Statements (continued)

Basis of Preparation (continued)

IAS 1 (revised) "Presentation of Financial Statements" and IAS 27 "Consolidated and Separate Financial Statements"

Minority interests in net assets of the Company's subsidiaries are presented within equity, separately from parent shareholders' equity. Previously, minority interests were presented separately from liabilities and equity in the Company's consolidated balance sheet.

IAS 39 "Financial Instruments: Recognition and Measurement" (amended 2004)

The gains and losses on re-measurement of financial assets available-for-sale to fair value are recognized as a separate component of equity. A gain or loss on an available-for-sale financial asset is recognized directly in equity, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognized, at which time the cumulative gain or loss previously recognized in equity is recognized in profit or loss. However, interest calculated using the effective interest method is recognized in profit or loss. Dividends on an available-for-sale equity instrument are recognized in profit or loss when the Company's right to receive payment is established.

IFRSs and IFRIC Interpretations not yet Effective

The Company has not applied the following IFRSs and IFRIC Interpretations that have been issued but are not yet effective:

- IAS 19 (amended 2004) "Employee Benefits";
- IAS 39 (amended 2005) "Financial Instruments: Recognition and Measurement";
- IFRS 6 "Exploration for and Evaluation of Mineral Resources";
- IFRS 7 "Financial Instruments: Disclosures";
- IFRIC 4 "Determining whether an Arrangement contains a Lease";
- IFRIC 5 "Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds".

The Company expects that the adoption of the pronouncements listed above will have no significant impact on the Company's financial statements in the period of initial application.

Management Estimates

The preparation of financial statements requires management of the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates with regard to those financial statements relate to the valuation and useful lives of property, plant and equipment, intangible assets, deferred taxation, provision for bad debt reserve and pension liabilities as discussed in Notes 5, 6, 13, 14, 24 and 30 .

Estimation Uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

2. Basis of Presentation of the Financial Statements (continued)

Estimation Uncertainty (continued)

Impairment of Goodwill and Intangible Assets

The Company determines whether goodwill and intangible assets not yet available for use are impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill only is allocated. Estimating the value in use requires the Company to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at December 31, 2005 was 1,275,838 (2004: 1,207,063) and carrying amount of intangible assets not yet available for use at December 31, 2005 was 2,612,411 (2004: 2,078,708). More details are provided in Note 6.

Correction of Errors and Reclassifications

In 2005 the Company determined and presented its obligations existing under the defined benefit plans in accordance with IAS 19, “Employee Benefits”. The Company engaged an actuary to perform a valuation of the pension obligations and recorded the defined benefit obligation as of December 31, 2005 and made other adjustments to the comparatives as of December 31, 2003 and 2004.

(in thousands of roubles)

2. Basis of Presentation of the Financial Statements (continued)

Correction of Errors and Reclassifications (continued)

The Company introduced the following reclassifications to the 2004 presentation:

Consolidated balance sheet as at December 31, 2004	As previously reported	Effect of reclassifications	After reclassifications	Description of reclassifications
Intangible Assets and Goodwill	3,328,070	(52,608)	**3,275,462**	Reclassification of Long–term Advances Given from Intangible Assets
Long–term Advances Given	1,056,076	52,606	**1,108,682**	Reclassification of Long–term Advances Given from Intangible Assets
Accounts Receivable, net	1,936,643	126,495	**2,063,138**	Reclassification of Accounts Receivable from Other Current Assets
Other Current Assets	2,369,709	(347,319)	**2,022,390**	Reclassification of Accounts Receivable and Prepaid Profit Tax from Other Current Assets
Prepaid Income Tax	–	78,625	**78,625**	Reclassification of Prepaid Income Tax from Other Current Assets and net off prepaid income tax against income tax payable
Deferred Revenue	617,789	176,601	**794,390**	Reclassification of Deferred Revenue from Other Long–Term Liabilities and Accounts Payable and Accrued Liabilities
Accounts Payable and Accrued Liabilities	3,176,723	(167,576)	**3,009,147**	Reclassification of Deferred Revenue from Accounts Payable and Accrued Liabilities
Other Taxes Payable	1,395,882	(323,614)	**1,072,268**	Reclassification of Income Tax Payable from Other Taxes Payable
Income tax payable	–	181,413	**181,413**	Reclassification of Income Tax Payable from Other Taxes Payable and net off of income tax liability against prepaid income tax
Short–term borrowings	4,572,646	(973,278)	**3,599,368**	Reclassification of Current Portion of Long–Term Borrowings from Short–Term borrowings
Current portion of short–term borrowings	2,900,072	973,278	**3,873,350**	Reclassification of Current Portion of Long–Term Borrowings from Short–Term Portion of Long–Term borrowings
Other long–term liabilities	13,254	(9,023)	**4,231**	Reclassification of Deferred Revenue from Other Long–term Liabilities

(in thousands of roubles)

2. Basis of Presentation of the Financial Statements (continued)

Correction of Errors and Reclassifications (continued)

Consolidated Statement of Operations for 2004	**As previously reported**	**Effect of reclassifications**	**After reclassifications**	**Description of reclassifications**
Wages, salaries, other benefits and payroll taxes	9,413,121	96,319	**9,509,440**	Reclassification of Wages and Salaries from Other Operating Expenses
Other operating expenses	3,471,798	(188,991)	**3,282,807**	Reclassification of Interest Expense, Wages and Salaries, Income Tax Expense, and Other Income and Expenses from Other Operating Expenses
Interest expense, net	2,032,987	10,000	**2,042,987**	Reclassification of Interest Expense from Other Operating Expenses
Other income and expenses, net	0	81,709	**81,709**	Reclassification of Other Operating Expenses from Other Income and Expenses
Income tax expense	126,069	963	**127,032**	Reclassification of Income Tax Expense from Other Operating Expenses

(in thousands of roubles)

2. Basis of Presentation of the Financial Statements (continued)

Correction of Errors and Reclassifications (continued)

The Company introduced the following adjustments to the 2004 reported financial statements.

Consolidated balance sheet as at December 31, 2004	After reclassifications	Effect of adjustments	As restated	Description of adjustments
Fixed Assets	30,000,961	7,611	**30,008,572**	Elimination of gain on disposal of equipment
Intangible Assets and Goodwill	3,275,462	146,644	**3,422,106**	Capitalization of interest relating to Oracle software
Long-term accounts receivable and other financial assets	323,626	(6,032)	**317,594**	Correction of loans given to employees due to change in accounting estimate
Accounts Receivable, net	2,063,138	5,026	**2,068,164**	2004 gains and losses identified in the second half of 2005
Other Current Assets	2,022,390	5,675	**2,028,065**	2004 gains and losses identified in the second half of 2005
Long-term borrowings	12,972,648	31,137	**13,003,785**	Effect from change in accounting estimate relating to bonded loans
Pension Liabilities	–	565,000	**565,000**	Accrual of pension liabilities as at December 31, 2004
Deferred Tax Liabilities	122,849	24,871	**147,720**	Cumulative effect on Deferred Tax Liabilities
Accounts Payable and Accrued Liabilities	3,009,147	30,515	**3,039,662**	2004 gains and losses identified in the second half of 2005
Other Taxes Payable	1,072,268	(2,075)	**1,070,193**	2004 gains and losses identified in the second half of 2005
Short-term borrowings	3,599,368	5,029	**3,604,397**	Correction due to change in accounting estimate
Current portion of short-term borrowings	3,873,350	(9,318)	**3,864,032**	Correction due to change in accounting estimate
Retained Earnings	11,345,410	(486,236)	**10,859,174**	Cumulative Effect on Retained Earnings

(in thousands of roubles)

2. Basis of Presentation of the Financial Statements (continued)

Correction of Errors and Reclassifications (continued)

Consolidated Statement of Operations for 2004	After reclassifications	Effect of adjustments	As restated	Description of adjustments
Revenue	26,047,204	(18,126)	**26,029,080**	Revenue recognized from prepaid cards correction and 2004 gains and losses identified in the second half of 2005
Wages, salaries, other benefits and payroll taxes	9,509,440	203,749	**9,713,189**	2004 gains and losses identified in the second half of 2005 and accrual of pension liabilities
Materials, repairs and maintenance, utilities	2,499,688	688	**2,500,376**	2004 gains and losses identified in the second half of 2005
Interconnection charges	4,048,930	7,051	**4,055,981**	2004 gains and losses identified in the second half of 2005
Taxes other than income tax	627,418	(2,074)	**625,344**	2004 gains and losses identified in the second half of 2005
Gain on disposal of property, plant, and equipment	1,150	8,168	**9,318**	Elimination of incorrect consolidated adjustment and 2004 gains and losses identified in the second half of 2005
Gain from sales of subsidiaries, associates and other investments	274,243	23,115	**297,358**	Correction of gain from disposal of subsidiary
Other operating expenses	3,282,807	29,422	**3,312,229**	Effect from change in accounting estimate relating to bonded loans and 2004 gains and losses identified in the second half of 2005
Interest expense, net	2,042,987	(163,370)	**1,879,617**	Additional interest capitalization and effect from change in accounting estimate relating to loans given to employees and bonded loans
Other expenses, net	81,709	1,905	**83,614**	Effect from change in accounting estimate relating to bonded loans and 2004 gains, losses identified in the second half of 2005
Income tax expense	127,032	27,042	**154,074**	Cumulative effect on deferred tax

2. Basis of Presentation of the Financial Statements (continued)

Correction of Errors and Reclassifications (continued)

As a result of the adjustments the net loss for 2004 increased by 91,252.

The effect on loss per share from these adjustments equalled 0.043 roubles per share.

3. Summary of Significant Accounting Policies

3.1. Principles of Consolidation

The consolidated financial statements of the Company represent the financial statements of the Group of companies, i.e. the parent and its subsidiaries, presented as if the Company operated as a single economic entity.

Subsidiaries

Subsidiaries, which are those entities in which the Company has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. The Control is a power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Company and are no longer consolidated from the date that control ceases. All intercompany transactions, balances and unrealized gains on transactions between Company companies are eliminated; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. In case of necessity, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Company.

Acquisition of Subsidiaries

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Company. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest.

The excess of purchase consideration over the fair value of the Company's share of identifiable net assets is recorded as goodwill. If the cost of the acquisition is less than the fair value of the Company's share of identifiable net assets of the subsidiary acquired the difference is recognized directly in the statement of operations.

Minority interest is the interest in subsidiaries not held by the Company. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair value of the identifiable assets and liabilities of the subsidiary at the acquisition date and the minorities' portion of movements in equity since the date of the combination. Minority interest is presented within the shareholders' equity.

Losses allocated to minority interest do not exceed the minority interest in the equity of the subsidiary unless there is a binding obligation of the minority to fund the losses. All such losses are allocated to the Company.

Acquisition of Minority Interest in Subsidiaries

The difference between the cost of the additional interest in a subsidiary and the minority interest's share of the assets and liabilities is reflected in the consolidated statement of shareholders' equity at the date of the purchase of the minority interest as a charge to retained earnings. The Company does not remeasure the assets and liabilities of the subsidiary to reflect their fair values at the date of the transaction.

3. Summary of Significant Accounting Policies (continued)

3.2. Investments in Associates

Associates are entities in which the Company generally has between 20% and 50% of the voting rights, or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognized at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Company's share of net assets of the associate. The Company's share of its associates' profits or losses is recognized in the statement of operations, and its share of movements in reserves is recognized in equity. However, when the Company's share of losses in an associate equals or exceeds its interest in the associate, the Company does not recognize further losses, unless the Company is obliged to make further payments to, or on behalf of, the associate.

Unrealized gains on transactions between the Company and its associates are eliminated to the extent of the Company's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Joint Ventures

Entities that are controlled jointly by the Company and a limited number of other shareholders are accounted for under the equity method.

3.3. Investments

The Company's investments are classified as either loans and receivables or available-for-sale investments, as appropriate. When investments are recognised initially, they are measured at fair value plus directly attributable transaction costs. The Company determines the classification of its investments upon initial recognition. All purchases and sales of investments are recognised on the settlement date, which is the date that the investment is delivered to or by the Company.

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Company has the positive intention and ability to hold to maturity. During the period the Company did not hold any investments in this category.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

(a) those that the entity intends to sell immediately or in the near term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;

(b) those that the entity upon initial recognition designates as available for sale; or

(c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which are classified as available for sale.

Loans and receivables are carried at amortised cost using the effective interest method. Gains and losses are recognised in income when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

3. Summary of Significant Accounting Policies (continued)

3.3. Investments (continued)

Available-for-sale investments are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the other categories. After initial recognition available-for-sale investments are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the statement of operations. Reversals of impairment losses in respect of equity instruments are not recognised in the statement of operations. Impairment losses in respect of debt instruments are reversed through profit or loss if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the statement of operations.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis.

3.4. Changes in Accounting Policies, Accounting Estimates and Errors

Change in Accounting Policies

The Company changes an accounting policy only if the change is required by a Standard or an Interpretation of IFRS or results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the Company's financial position, financial performance or cash flows.

The Company accounts for a change in accounting policy resulting from the initial application of a Standard or an Interpretation in accordance with the specific transitional provisions, if any, in that Standard or Interpretation.

Changes in Accounting Estimates

As a result of the uncertainties inherent in business activities, many items in financial statements cannot be measured with precision but can only be estimated. Estimation involves judgments based on the latest available, reliable information. An estimate may need revision if changes occur in the circumstances on which the estimate was based or as a result of new information or more experience.

When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate. The effect of a change in an accounting estimate is recognized prospectively by including it in profit or loss in the period of the change, if the change affects that period only or the period of the change and future periods, if the change affects both.

Prior Period Errors

The Company corrects material prior period errors retrospectively in the first set of financial statements authorized for issue after their discovery by restating the comparative amounts for the prior period presented in which the error occurred or if the error occurred before the earliest prior period presented by restating the opening balances of assets, liabilities and equity for the earliest prior period presented.

Prior period error is corrected by retrospective restatement except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the error.

(in thousands of roubles)

3. Summary of Significant Accounting Policies (continued)

3.5. Foreign Currency Transactions

The measurement and presentation currency of the Company is the Russian Rouble, which is the national currency of the Russian Federation. Transactions in foreign currencies are initially recorded in the measurement currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the measurement currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to the consolidated statement of operations as foreign exchange gains (losses). Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction.

Assets and liabilities settled in Roubles but denominated in foreign currencies are recorded in the Company's consolidated financial statements using the same principles as for assets and liabilities denominated in foreign currencies.

The exchange rates as of December 31, 2005 and 2004 were as follows:

Currency	**2005**	**2004**
Russian Roubles per US dollar	**28.78**	27.75
Russian Roubles per Euro	**34.19**	37.81
Russian Roubles per Japanese yen	**0.25**	0.27

3.6. Property, Plant and Equipment

3.6.1 Property, Plant and Equipment

Property, plant and equipment are recorded at purchase or construction cost less accumulated depreciation and any impairment in value. For the property, plant and equipment acquired prior to January 1, 2003, fair values as at January 1, 2003 have been used as deemed cost (refer to Note 2) in accordance with the exemption provided in IFRS 1. The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. Impairment losses are recognized in the statement of operations.

Interest costs on borrowings to finance the construction of property, plant and equipment are capitalized, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

Expenditure for continuing repairs and maintenance are charged to the statement of operations as incurred. Social assets are expensed on acquisition.

3. Summary of Significant Accounting Policies (continued)

3.6. Property, Plant and Equipment (continued)

3.6.2 Depreciation and Useful Life

Depreciation is calculated on property, plant and equipment on a straight-line basis from the time the assets are available for use, over their estimated useful lives as follows:

Buildings	50 years
Constructions	20 years
Analogue switches	15 years
Digital switches	15 years
Other telecommunication equipment	15 years
Transportation equipment	5 years
Computers, office and other equipment	4-5 years
Land	not depreciated

The asset's residual values, useful lives and depreciation methods are reviewed, and adjusted as appropriate, at each financial year-end.

Depreciation of an asset begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 and the date that the asset is derecognised.

The depreciation charge for a period is usually recognized in the statement of operations. However, sometimes, the future economic benefits embodied in an asset are absorbed in producing other assets. In this case, the depreciation charge constitutes part of the cost of the other asset and is included in its carrying amount.

The period of validity of the Company's operating licenses is significantly shorter than the useful lives used for depreciation of the cost of property, plant and equipment. Based on the Russian licensing legislation and prior experience, management believes that the operating licenses will be renewed without significant cost, which would allow the Company to realize the cost of its property, plant and equipment through normal operations.

3.6.3 Construction in Progress

Construction in progress is recorded as the total of actual expenditures incurred by the Company from the beginning of construction to the reporting date less any impairment in value.

3.6.4 Assets Received Free of Charge

Equipment transferred to the Company free of charge by its customers and other entities outside the privatization process is capitalized at market value at the date of transfer. A corresponding income is fully recognized in the statement of operations. In the case when transfers of equipment relate to the rendering of future services to the transferee the equipment is considered as deferred revenue which is recognised as income on the same basis that the equipment is depreciated.

Equipment contributions that will not generate any future economic benefit for the Company are not recognized.

3. Summary of Significant Accounting Policies (continued)

3.7 Intangible Assets

3.7.1 Goodwill

Goodwill represents the excess of the cost of an acquisition over the net fair value of the Company's share of the identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate at the date of acquisition. Goodwill on an acquisition of a subsidiary is included in intangible assets. Goodwill on an acquisition of an associate is included in the investments in associates. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Company are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Company at which the goodwill is monitored for internal management purposes; and
- is not larger than a segment based on either the Company's primary or the Company's secondary reporting format determined in accordance with IAS 14 "Segment Reporting".

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

An impairment loss recognized for goodwill is not reversed in a subsequent period.

3.7.2 Licenses

Cost of licenses paid to Government for permission to provide telecommunication services within identifiable period of time is recognized as intangible assets.
Following initial recognition, intangible assets are carried at historical cost less any accumulated amortisation and any accumulated impairment losses.

3.7.3 Software and Other Intangible Assets

Software and other intangible assets acquired separately are measured on initial recognition at cost. The cost of other intangible assets acquired in a business combination is their fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

3. Summary of Significant Accounting Policies (continued)

3.7 Intangible Assets (continued)

3.7.4 Useful Life and Amortization of Intangible Assets

The Company assesses whether the useful life of an intangible asset is finite or indefinite and, if finite, the length of, or number of production or similar units constituting, that useful life. An intangible asset is regarded by the entity as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity.

Intangible assets with finite lives are amortized over the useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired.

Amortization periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates.

The cost of licenses and software is depreciated on a straight-line basis over the estimated useful life equal to the term of the licenses or the right to use the software. Useful life of other intangible assets is approximately 5 years.

Intangible assets with indefinite useful lives are not amortized, but tested for impairment annually either individually or at the cash-generating unit level. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

3.8 Borrowing Costs

The borrowing costs are capitalized by the Company as part of the cost of the asset when it is probable that they will result in future economic benefits to the entity and the costs are directly attributable to the acquisition, construction or production of a qualifying asset including construction in progress.

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization on that asset is determined as the actual borrowing costs incurred on that borrowing during the period.

To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization is determined by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average of the borrowing costs applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs capitalized during a period shall not exceed the amount of borrowing costs incurred during that period.

3. Summary of Significant Accounting Policies (continued)

3.9 Leases

Leases where all the risks and rewards of ownership of the asset are transferred from lessor to leasee are classified as finance leases.

Leases where the lessor retains substantially all the risks and rewards of ownership of the asset are classified as operating leases.

3.9.1 Finance Leases

At the commencement of the lease term, or the date from which the lessee is entitled to exercise its right to use the leased asset, the Company recognizes finance leases as assets and liabilities in their balance sheets at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. At the commencement of the lease term, the asset and the liability for the future lease payments are recognized in the balance sheet at the same amounts except for any initial direct costs of the lessee that are added to the amount recognized as an asset.

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

The depreciation policy for depreciable leased assets is consistent with that for depreciable assets that are owned, and the depreciation recognized is calculated in accordance with accounting policy of the Company applicable for depreciable assets. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset is fully depreciated over the shorter of the lease term and its useful life.

3.9.2 Operating Leases

Operating lease payments are recognised as an expense in the statement of operations on a straight-line basis over the lease term.

3.10 Inventories

Inventories are recorded at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.
The cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Cost of inventory is determined on the weighted average basis.

3.11 Advances Given

Advances given to acquire non-current assets are classified as non-current and considered non-monetary asset. Long-term advances given for operating activities are also classified as non-current assets.

3. Summary of Significant Accounting Policies (continued)

3.12 Financial Instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets comprise cash and cash equivalents; an equity instrument of another entity; a contractual right to receive cash or another financial asset from another entity, or to exchange financial assets or financial liabilities with another entity under conditions that are potentially favorable to the Company; or a contract that will or may be settled in the Company's own equity instruments and is a non-derivative for which the Company is or may be obliged to receive a variable number of the Company's own equity instruments, or a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments. For this purpose the Company's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the Company's own equity instruments.

Financial liabilities include contractual obligations to deliver cash or another financial asset to another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Company; or a contract that will or may be settled in the Company's own equity instruments and is a non-derivative for which the Company is or may be obliged to deliver a variable number of the Company's own equity instruments or a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments.

The Company recognizes a financial asset or a financial liability on its balance sheet when, and only when, the Company becomes a party to the contractual provisions of the instrument.

When a financial asset or financial liability is recognized initially, the Company measures it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

The Company classifies its financial assets and financial liabilities as current or non-current based on term of its maturity taking into account other factors that limit the Company's ability to realize assets within 12 months or existence of call options in financial liabilities valid within 12 months after the balance sheet date.

Financial asset is derecognised when the rights to receive cash flows from the asset expired or the Company transferred its rights to receive cash flows from the asset.

Financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

3.13 Cash and Cash Equivalents

Cash and cash equivalents represent cash on hand and in the Company's bank accounts, as well as cash deposits and short-term investments with original maturities of three months or less.

3.14 Accounts Receivable and Provision for Impairment of Debt

Accounts receivable are recognized at original invoice amount less an allowance for any uncollectible amounts. Allowance is made when there is objective evidence that the Company will not be able to collect the debts.

Provision for impairment of receivables is created based on the historical pattern of collections of accounts receivable and specific analysis of recoverability of significant accounts.

3. Summary of Significant Accounting Policies (continued)

3.14 Accounts Receivable and Provision for Impairment of Debt (continued)

Provision for impairment is also created for other accounts receivable except advances given based on the assessment of the Company's ability to collect the debts.

Provision for impairment is recognized in the statement of operations.

The carrying amount of current accounts receivable is a reasonable approximation of their fair value.

The fair value of non-current accounts receivable is calculated using the effective interest method.

3.15 Non-current Assets Held for Sale and Discontinued Operations

A discontinued operation is a component of the Company that either has been disposed of, or is classified as held for sale, and represents a separate major line of business or geographical area of operations, is part of a single co-coordinated plan to dispose of a separate major line of business or geographical area of operations or is a subsidiary acquired exclusively with a view to resale.

The Company classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.

The Company measures a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

Immediately before the initial classification of the asset (or disposal group) as held for sale, the carrying amounts of the asset (or all the assets and liabilities in the group) are measured in accordance with applicable IFRSs.

The Company presents and discloses information that enables users of the financial statements to evaluate the financial effects of discontinued operations and disposals of non-current assets (or disposal groups).

3.16 Troubled Debt Restructurings

A troubled debt restructuring occurs when the Company grants a concession to the debtor in the forms of modification of the terms of the debt, including the extension of the maturity date, change of payment schedule or reduction of the face amount of the debt, or in the form of transfer of the assets or an equity interest in the debtor in satisfaction of the debt. The Company recognized a loss in the amount of the difference between the fair value of the assets and/or equity interest received and the recorded amount of the receivable. This loss will be recognized in full in the period the restructuring takes place.

3.17 Loans Given

Loans given are recognized at the amortized cost, using the effective interest method less provision for impairment or uncollectibility. Loans given are recorded as the non-current assets unless the repayment is expected within 12 months after the balance sheet date.

3.18 Loans and Borrowings Received

Loans and Borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortised cost using the effective interest method; any difference between the fair value of the consideration received (net of transaction costs) and the redemption amount is recognised as an adjustment to interest expense over the period of the borrowings.

3. Summary of significant Accounting policies (continued)

3.19 Employee Benefits

3.19.1 Current Employment Benefits

Wages and salaries paid to employees are recognized as expense in current period.

3.19.2 Unified Social Tax

Under provisions of the Russian legislation, social contributions are made through a unified social tax ("UST") calculated by the Company by the application of a regressive rate (from 26% to 25%) to the annual gross remuneration of each employee. The Company allocates the UST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund vary from 20% to 19% depending on the annual gross salary of each employee.

The Company's contributions relating to the UST are expensed in the year to which they relate.

3.19.3 Other Pension Plans and Post-Employment Benefits

Under collective bargaining agreements and internal regulations on additional pension benefits, the Company also provides benefits for its employees by using post-employment benefit plans. The majority of the Company's employees are eligible to participate under such post-employment benefit plans based upon a number of factors, including years of service, age, and compensation.

The Company uses two types of pension plans: plans with defined contributions and plans with defined benefits.

Defined contribution plan limit the Company's legal or constructive obligation to the sum that it agrees to invest into the fund. In such case, the employees of the Company bear actuary and investment risks.

According to plans with defined benefits, the Company undertakes to provide the agreed benefits to its actual and former employees. In such case, the Company bears actuary and investment risks

Plans with Defined Benefits

The Company determines the present value of the defined benefit obligation and the fair value of any plan assets on each reporting date separately for each plan. The obligations are valued by professionally qualified independent actuaries hired by the Company using the projected unit credit method. The assets of the defined benefit plans are valued by professionally qualified actuaries or independent appraisers.

Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses for each individual plan at the end of the previous reporting year exceeded 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plans.

Upon introduction of a new plan or improvement of an existing plan past service cost is recognized on a straight-line basis over the average period until the amended benefits become vested. To the extent that the benefits are already vested immediately, past service costs is immediately expensed.

Gains or losses on the curtailment or settlement of pension benefit obligations are recognized when the curtailment or settlement occurs.

3. Summary of Significant Accounting Policies (continued)

3.19 Employee Benefits (continued)

3.19.3 Other Pension Plans and Post-Employment Benefits (continued)

Defined Contribution Plans

As the employees of the Company render services, the Company accrues obligations to the fund by acknowledgement of obligations (accrued obligations) less the total of payments made as of accrual date. Should the total of payments exceed the obligations as at reporting date, the company recognizes such excess as an asset (deferred expenses) to the extent that such prepayment can be credited against upcoming payments or returned to the Company. If payments under defined contribution plans relate to the period of rendering services exceeding 12 months after the end of the period in which the employees rendered the services of the Company, the amounts relating to such period are discounted at the rate defined as the market rate of return on high-grade corporate bonds, effective at the reporting date.

3.20 Income Taxes

Tax expense (tax income) is the aggregate amount included in the determination of profit or loss for the period in respect of current tax and deferred tax.

Current tax is the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable).

Current tax liabilities (assets) for the current and prior periods are measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the entity expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Any such previously recognized reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Deferred tax assets and liabilities are not discounted.

3. Summary of Significant Accounting Policies (continued)

3.21 Shareholders' Equity

3.21.1 Share Capital

Ordinary shares and non-redeemable preference shares with discretionary dividends are both classified as equity.

3.21.2 Dividends

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared at Shareholders' meeting before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorized for issue.

3.22 Minority Interest

Minority interest is the interest in subsidiaries not held by the Company. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair values of identifiable assets and liabilities of the subsidiary at the acquisition date, and the minorities' portion of movements in net assets since the date of the combination. Minority interest is presented separately from liabilities and shareholders' equity.

3.23 Revenue Recognition

Revenue is recognised to the extent that it is probable that economic benefits will flow to the Company and the revenue can be reliably measured.

Revenue is recognized in the amount of cash or cash equivalents received in the form of cash or receivable. However, when the inflow of cash or cash equivalents is deferred, the fair value of the consideration may be less than the nominal amount of cash received or receivable. When the arrangement effectively constitutes a financing transaction, the fair value of the consideration is determined by discounting all future receipts using an effective interest rate.

3.23.1 Revenue from Customers

The Company categorizes the revenue sources in fourteen major categories:

1. Long distance calls - domestic;
2. Long distance calls - international;
3. Local telephone calls;
4. Installation and connecting fees;
5. Documentary services;
6. Cellular services;
7. Radio and TV broadcasting;
8. Data transfer and telematic services;
9. New services;
10. Rent of telephone channels;
11. Services for national operators;
12. Services for international operators;
13. Other telecommunications services;
14. Other revenues.

3. Summary of Significant Accounting Policies (continued)

3.23 Revenue Recognition (continued)

3.23.1 Revenue from Customers (continued)

Long Distance Calls (domestic and international)

Revenues from long distance services depend on time of call, duration of call, destination of call, type of service used, subscriber category and the applied rate plan. Customers of the Company use the service via installed fixed telephone, as well the service could be accessed by means of pay-phone. The Company charges long distance fees on a per-minute basis. The Company recognizes revenues related to the long distance services in the period when the services are rendered.

Local Telephone Calls

Revenue from the local telephone services depends on the duration of the telephone connections and subscription fee, while time driven billing scheme is applied. If fixed payment scheme is applied then revenue depends on the subscription fee only. Customers of the Company use the service via installed fixed telephone, as well the service could be accessed by means of pay-phone. The Company recognizes revenues related to the monthly network fees for local services in the month the service is provided to the subscriber.

Installation and Connection Fees

Installation and connection fees for indefinite period contracts are paid by a combination of a fixed cash amount and by the contribution of fixed assets consisting of cable and duct, commonly referred to as the “last mile”. Revenue received in the form of cash is recognized when the installation and connection are complete. For installation and connection fees paid in the form of fixed assets, revenue is deferred and recognized as income on the same basis that the fixed assets are depreciated.

Documentary Services

Revenues from telegraph services comprise fees for telegram transmissions and other wire line data transmission services. The Company recognizes revenues related to telegraph services in the period when the services are rendered.

Cellular Services

Major revenues from cellular services arise from airtime services including local, intercity long distance and international long distance calls, subscription fees, value added services, outbound and inbound roaming. The Company recognizes revenues related to mobile telecommunications services in the period when the services are rendered.

Radio and TV Broadcasting

The Company maintains a wireline radio broadcasting network. The revenues comprise monthly fees from subscribers and installation fees for wireline radio sets. The Company recognizes the revenues related to radio broadcasting in the period when the services are rendered.

3. Summary of Significant Accounting Policies (continued)

3.23 Revenue Recognition (continued)

3.23.1 Revenue from Customers (continued)

Data Transfer and Telematics Services

The Company recognizes revenues related to data transfer and telematics services in the period when the services are rendered.

New Services

Major revenues from new services include internet services, ISDN, ADSL, IP-telephony, intelligent network services. The Company recognizes revenues related to new services in the period when the services are rendered.

Rent of Telephone Channels

Major revenues are recognized from the following services: rent of intercity and international, digital, analogue, and telegraph channels. The Company recognizes revenues from the rent of channels in the period when the services are rendered.

Services for National Operators

Revenue from national service providers includes two different groups.

The first group of revenues represents services rendered to the Company's partners for termination of long-distance traffic of its operators-partners in the network of the Company.

The second group of revenues from national operators represents services rendered to interconnected telecom operators that transfer local, intercity and international traffic of their customers via network of the Company.

Major revenues are recognized from the services rendered to operators for transit of local, intercity and international traffic. Further, the Company generates revenue from interconnection to the network (one time fees), rent of channels, rent of equipment, data transfer and Internet services.

The Company recognizes revenues from national operators in the period when the services are rendered.

Services for International Operators

The revenues represents services rendered to interconnected international telecom operators that transfer international traffic of their customers via network of the Company.

The Company recognizes revenues from international operators in the period when the services are rendered.

Other Telecommunication Services

Other telecommunication services primarily consist of revenues received by public switched telephone network (PSTN) stations from the rent of direct lines and local junctions, as well as subscription fees for wired-radio outlets. The Company recognizes revenues related to other services in the period when the services are rendered.

3. Summary of Significant Accounting Policies (continued)

3.23 Revenue Recognition (continued)

3.23.1 Revenue from Customers (continued)

Other Revenues

Other revenues primarily consist of revenues received from manufacturing of the telecommunication equipment and its technical support, transportation services, recreation services and sale of products and services provided by auxiliary units.

3.24 Barter Transactions

When goods or services are exchanged or swapped for goods or services which are of a similar nature and value, the exchange is not regarded as a transaction which generates revenue. When goods are sold or services are rendered in exchange for dissimilar goods or services, the exchange is regarded as a transaction which generates revenue. The revenue is measured at the fair value of the goods or services received, adjusted by the amount of any cash or cash equivalents transferred. When the fair value of the goods or services received cannot be measured reliably, the revenue is measured at the fair value of the goods or services given up, adjusted by the amount of any cash or cash equivalents transferred.

3.25 Earnings per Share

The Company calculates basic earnings per share amounts for profit or loss attributable to equity holders of the parent entity and, if presented, profit or loss from continuing operations attributable to those equity holders. Basic earnings per share are calculated by dividing profit or loss attributable to equity holders of the parent entity (the numerator) by the weighted average number of shares outstanding (the denominator) during the period.

The Company's preference shares are considered participating equity instruments for the purpose of earnings per share calculations (see Note 31).

3.26 Provisions

Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Where the Company expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain.

If the effect of time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a borrowing cost.

3. Summary of significant Accounting policies (continued)

3.27 Contingent Assets and Contingent Liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company or a present obligation that arises from past events but is not recognized because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation or the amount of the obligation cannot be measured with sufficient reliability. The Company does not recognize a contingent liability. A contingent liability is disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company. The Company does not recognize a contingent asset. A contingent asset is disclosed where an inflow of economic benefits is probable.

3.28 Contractual Commitments

Contractual commitments comprise legally binding trading or purchase agreements with stated amount, price and date or dates in the future.

The Company discloses significant contractual commitments in the Notes to the financial statements.

The asset or liability under contractual commitments are not recognized in the financial statement until any of the parties performs in accordance with the contract and until any of the party became legally liable to pay or entitled to receive the payment under the terms of the contract.

3.29 Related Party Transactions

The Company defines the following terms to specify the related party: a party is related to the Company if:

1. directly, or indirectly through one or more intermediaries, the party controls, is controlled by, or is under common control with, the Company (this includes parents, subsidiaries and fellow subsidiaries), has an interest in the entity that gives it significant influence over the entity or has joint control over the entity;
2. the party is an associate (as defined in IAS 28 Investments in Associates) of the entity;
3. the party is a joint venture in which the entity is a venturer (see IAS 31 Interests in Joint Ventures);
4. the party is a member of the key management personnel of the entity or its parent;
5. the party is a close member of the family of any individual referred to in 1 or 4;
6. the party is an entity that is controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in 4 or 5; or
7. the party is a post-employment benefit plan for the benefit of employees of the entity, or of any entity that is a related party of the entity.

Relationships between the parent and its subsidiaries and between subsidiaries themselves are not disclosed by the Company

3. Summary of significant Accounting policies (continued)

3.30 Events after the Balance Sheet Date

The Company adjusts the amounts recognized in its financial statements to reflect adjusting events after the balance sheet date. Events that require an entity to adjust the amounts recognized in its financial statements are caused by favourable and unfavorable outcomes of conditions that existed at the balance sheet date and change in management estimates subject to uncertainties which was used for accounting of a number of business activities.

If non-adjusting events after the balance sheet date are material, their nondisclosure could influence the economic decisions of users taken on the basis of the financial statements. Accordingly, the Company discloses the nature of the event and an estimate of its financial effect, or a statement that such an estimate cannot be made for each material category of non-adjusting event after the balance sheet date.

4. Segment Information

Management believes that the Company operates in one geographical and operational segment, namely rendering services of electric connection on the territory of the Central region of the Russian Federation. Management evaluates the results of operations and takes investment and strategic decisions based on the analysis of the results at the level of the whole Company.

(in thousands of roubles)

5. Property, Plant and Equipment, net

	Land, buildings and constructions	Switches and transmission devices	Vehicles and other	Construction in progress and equipment for installation	Total
Cost					
At December 31, 2003	**10,230,722**	**11,927,712**	**3,235,442**	**2,006,371**	**27,400,247**
Additions	–	–	–	9,699,848	9,699,848
Additions due to acquisition of subsidiaries	–	820,559	103,710	13,107	937,376
Disposals	(59,614)	(204,803)	(76,628)	(6,395)	(347,440)
Disposals due to sale of subsidiaries	(50,378)	(26,487)	(10,380)	(2,558)	(89,803)
Transfers	3,370,500	3,989,711	875,728	(8,235,939)	–
At December 31, 2004	**13,491,230**	**16,506,692**	**4,127,872**	**3,474,434**	**37,600,228**
Additions	–	(25,237)	–	5,018,527	4,993,290
Additions due to acquisition of subsidiaries	90,279	15,189	108,119	38,561	252,148
Disposals	(114,696)	(110,310)	(133,151)	(42,541)	(400,698)
Disposals due to sale of subsidiaries	–	–	(3,173)	–	(3,173)
Transfers	2,469,534	3,289,824	574,196	(6,333,554)	–
Reclassification	26,126	(42,382)	16,256	–	–
At December 31, 2005	**15,962,473**	**19,633,776**	**4,690,119**	**2,155,427**	**42,441,795**
Accumulated Depreciation					
At December 31, 2003	**(369,586)**	**(1,292,725)**	**(1,423,401)**	–	**(3,085,712)**
Charge for the year	(1,208,835)	(2,556,092)	(446,869)	–	**(4,211,796)**
Charge due to acquisition of subsidiaries	–	(582,178)	(64,191)	–	**(646,369)**
Disposals	49,099	158,021	60,964	–	**268,084**
Disposals due to sale of subsidiaries	48,683	26,335	9,119	–	**84,137**
At December 31, 2004	**(1,480,639)**	**(4,246,639)**	**(1,864,378)**	–	**(7,591,656)**
Charge for the year	(1,262,649)	(3,045,464)	(485,171)	–	**(4,793,284)**
Charge due to acquisition of subsidiaries	(33,326)	(14,162)	(57,200)	–	**(104,688)**
Disposals	85,420	92,662	46,494	–	**224,576**
Disposals due to sale of subsidiaries	–	–	–	–	–
Reclassification	(9,466)	11,500	(2,034)	–	–
At December 31, 2005	**(2,700,660)**	**(7,202,103)**	**(2,362,289)**	–	**(12,265,052)**
Net book value as of December 31, 2003	**9,861,136**	**10,634,987**	**1,812,041**	**2,006,371**	**24,314,535**
Net book value as of December 31, 2004	**12,010,591**	**12,260,053**	**2,263,494**	**3,474,434**	**30,008,572**
Net book value as of December 31, 2005	**13,261,813**	**12,431,673**	**2,327,830**	**2,155,427**	**30,176,743**

Banks borrowings are secured by properties with the carrying value as of December 31, 2005 of approximately 5,344,954 (2004 - 6,553,289) (see Note 19).

The total of property, plant and equipment, referred to above, includes the cost of property, plant and equipment with depreciation accrued for 100% (completely amortized), which are still in operation, with an initial cost of 4,617,784 as of December 31, 2005 (2004 – 3,964,350).

(in thousands of roubles)

5. Property, Plant and Equipment, net (continued)

The net book value of plant and equipment held under finance leases at December 31, 2005 and 2004 amounted to:

	2005	2004
Land, buildings and constructions	**1,913**	–
Switches and transmission devices	**2,443,448**	2,218,805
Construction in progress and equipment for installation	**168,906**	227,401
Vehicles and other	**933,272**	916,632
Total net book value of plant and equipment held under finance leases	**3,547,539**	3,362,838

Leased assets are pledged as security for the related finance lease obligations (see Note 20).

The net book value of property, plant and equipment, which were received on vendor financing terms, amounted as of December 31, 2005 to 214,514 (2004 – 213,319).

In 2005, the Company increased construction in progress by the amount of capitalized interest totalling 404,233 (2004 – 364,281). Capitalization rate in 2005 was 14.91% (2004 -12.55%).

(in thousands of roubles)

6. Intangible Assets

	Goodwill	Licenses	Software	Total
Cost				
At December 31, 2003	**29,319**	**14,224**	**1,041,078**	**1,084,621**
Additions	–	2,778	1,230,726	1,233,504
Additions due to acquisition of subsidiaries	1,177,744	–	454	1,178,198
At December 31, 2004	**1,207,063**	**17,002**	**2,272,258**	**3,496,323**
Additions	–	9,530	650,863	660,393
Additions due to acquisition of subsidiaries	70,863	–	54	70,917
Disposals	–	–	(452)	(452)
At December 31, 2005	**1,277,926**	**26,532**	**2,922,723**	**4,227,181**
Impairment				
At December 31, 2004	–	–	–	–
Accrued provision	(2,088)	–	–	(2,088)
At December 31, 2005	**(2,088)**	**–**		**(2,088)**
Accumulated amortization				
At December 31, 2003	**–**	**(2,347)**	**(37,257)**	**(39,604)**
Charge for the year	–	(3,123)	(31,278)	(34,401)
Charge due to acquisition of subsidiaries	–	–	(212)	(212)
At December 31, 2004	**–**	**(5,470)**	**(68,747)**	**(74,217)**
Charge for the year	–	(4,353)	(50,324)	(54,677)
Charge due to acquisition of subsidiaries	–	–	(8)	(8)
Disposals	–	–	203	203
At December 31, 2005	**–**	**(9,823)**	**(118,876)**	**(128,699)**
Net book value at December 31, 2003	**29,319**	**11,877**	**1,003,821**	**1,045,017**
Net book value at December 31, 2004	**1,207,063**	**11,532**	**2,203,511**	**3,422,106**
Net book value at December 31, 2005	**1,275,838**	**16,709**	**2,803,847**	**4,096,394**

Oracle E-Business Suite (OEBS)

As of December 31, 2005 software includes OEBS software with a book value of 1,549,000 (2004 – 1,193,788), including 164,888 of expenses for implementation (2004 – 180,235). In accordance with the supply contract, the Company purchased non-exclusive licenses for 18,049 users of E-business Suite 2003 Professional among other license applications.

The Company will commence amortizing the value of the mentioned software from the date of its implementation, proportionally to the quantity of licenses used, over the useful life of the licenses. Full implementation of Oracle E-Business Suite software is expected to be completed by 2008.

Amdocs Billing Suite

As of December 31, 2005 software also includes Amdocs Billing Suite software with a book value of 1,063,411 (2004 – 884,920), including interest capitalized totalling 43,832 (2004 – 0). The capitalization rate in 2005 was 5.98%.

This software was purchased for the purpose of the implementation of unified automated settlements system.

6. Intangible Assets (continued)

The project of implementation of the unified automated settlements system Amdocs Billing Suite is expected to last 4-5 years.

The Company's Board of Directors approved the purchase of Amdocs Billing Suite software on November 19, 2004.

Amdocs Billing Suite software was supplied in December 2004 by LLC IBM Eastern Europe/Asia, in exchange for zero coupon 18 promissory notes for the total amount of 1,093,751.

The Company will commence amortizing this asset from the date of software implementation, proportionally to the value of implemented modules. Until then the Company annually tests this software for impairment.

In 2005 the Company increased the value of intangible assets by the amount of capitalized interest totalling 234,156.

Total expenses of the company on research and development projects amounted to 6,443 in 2005 (2004 – 239). Research and development expenses of 5,874 were written off in 2005 due to absence of positive results.

(in thousands of roubles)

7. Consolidated Subsidiaries

The consolidated financial statements include the assets, liabilities and financial results of the following subsidiaries:

Subsidiary	Main activity	Ownership, %		Voting shares, %	
		2005	**2004**	**2005**	**2004**
CJSC Vladimir Teleservice	Communication Services	**100%**	**100%**	**100%**	**100%**
LLC Mobilcom	Communication Services	**100%**	**100%**	**100%**	**100%**
LLC Teleport Ivanovo	Communication Services	**100%**	**100%**	**100%**	**100%**
LLL Telecom Terminal	Repair and maintenance services	**100%**	**100%**	**100%**	**100%**
LLC Telecom Stroi	Construction Services	**100%**	**100%**	**100%**	**100%**
OJSC RTS	Communication Services	**100%**	**100%**	**100%**	**100%**
CJSC ATS	Communication Services	**100%**	–	**100%**	–
LLC Tver Telecom	Communication Services	**85%**	**85%**	**85%**	**85%**
LLC Vladpage	Communication Services	**75%**	**75%**	**75%**	**75%**
CJSC TsentrTelecomService	Communication Services	**74,9%**	**74,9%**	**74,9%**	**74,9%**
OOO Svyaz–Service–Irga	Repair and maintenance services	**70%**	**70%**	**70%**	**70%**
LLC Vladimirskii Taksofon	Communication Services	**51%**	**51%**	**51%**	**51%**
CJSC Telecom Ryazanskoi oblasti	Communication Services	**50,9%**	**50,9%**	**50,9%**	**50,9%**
LLC Operatorski Tsentr[1]	Communication Services	**100%**	–	**100%**	–
LLC TeleNET[1]	Communication Services	**100%**	–	**100%**	–
LLC Ortes[2]	Communication Services	**100%**	**100%**	**100%**	**100%**
CJSC Rosnet International[2]	Communication Services	**99%**	**99%**	**99%**	**99%**
CJSC Restel[2]	Communication Services	**100%**	**100%**	**100%**	**100%**
LLC Rosnet Neva[2]	Communication Services	**100%**	**100%**	**100%**	**100%**
RTN (UK) Limited, Great Britain[2]	Communication Services	–	**100%**	–	**100%**
RTN–Leasing, Gibraltar[2]	Communication Services	–	**100%**	–	**100%**
Alarini Enterprises Limited, Cyprus[2]	Communication Services	–	**100%**	–	**100%**
Real Plus Construction, Cayman Islands[2]	Communication Services	–	**100%**	–	**100%**

All the above companies except for specifically mentioned otherwise are Russian legal entities registered in accordance with the Russian legislation, and have the same financial year as the Company.

[1] Subsidiary is under control of CJSC ATS
[2] Subsidiary is under control of OJSC RTS

(in thousands of roubles)

7. Consolidated Subsidiaries (continued)

Acquisition of CJSC "ATS"

In November 2005 the Company acquired a 100% stake in CJSC "ATS" for 150,513. Expenses relating to acquisition of CJSC "ATS" were reflected in the price of acquisition and equalled 7,572. The Company determined December 1, 2005 to be the acquisition date. The major activity of CJSC "ATS" is telephony services, data transmission and telematic services.

The Company's allocation of the acquisition price is as follows:

Acquisition price	
Paid in cash	142,941
Transaction costs	7,572
Total paid	**150,513**
Assigned value of identifiable assets and liabilities	
Property, plant and equipment, net	110,853
Intangible assets, net	36
Long-term investments	2,808
Other Non-current Assets	31,816
Accounts receivable	17,720
Cash and cash equivalents	9,136
Other current assets	37,413
Current liabilities	(83,396)
Long-term liabilities	(46,735)
Total net assets	**79,651**
Company's share in acquired net assets	100%
Assigned value of acquired share in identifiable net assets	79,651
Goodwill	**70,862**
Impairment of goodwill from the date of acquisition to December 31, 2005	–
Amount of goodwill at December 31, 2005, net	**70,862**

Cash outflow on the acquisition of ZAO "ATS" is as follows:

Net cash acquired in the result of acquisition	**9,136**
Total consideration	**(150,513)**
Net cash outflow	**(141,377)**

Loss of CJSC "ATS" for 2005 from the date of acquisition was 1,999.

(in thousands of roubles)

7. Consolidated Subsidiaries (continued)

Other Acquisitions and Disposals of Subsidiaries

In January 2005 the Company increased its stake in OJSC "Aerocom" from 76% to 100% by aquiring minority interest for 7,937. Costs directly attributable to the acquisition amounted to 1,689.

In May 2005 the Company increased its stake in OJSC "Aerocom" from 99.6% to 100% by aquiring minority interest for 911.

In 2005 due to loss of control over CJSC "TeleRoss-Voronej", which was performed through the majority of votes in Board of Directors, the company reclassified investments in CJSC "TeleRoss-Voronej" from investments in subsidiary companies to investments in associate companies.

In 2005 OJSC "RTS" purchased from the Company two of its subsidiaries - CJSC "CenterTelecomService Moskovskoi oblasti" and OJSC "Aerocom" and merged with them. OJSC "RTS" issued 426,857 ordinary shares to the Company as consideration for the acquisition. Subsequent to this reorganization of its subsidiaries the Company continues to recognize assets and liabilities at the book value determined by the Company at original acquisition.

8. Investments in Associates and Joint Ventures

Investments in associates at December 31, 2005 and 2004 comprised the following:

		2005		2004	
Associate	**Activity**	**Voting shares, %**	**Carrying value**	**Voting shares, %**	**Carrying value**
CJSC TeleRossVoronej	Communication Services	**50%**	**592**	–	–
Joint venture (see Note 9)	Cellular Services	**30%**	**14,579**	30%	14,579
CJSC SK Kostars	Insurance Services	**28%**	**4,277**	28%	2,815
OJSC Telecommunications company Rinfotels	Communication Services	**26%**	**1,225**	26%	1,348
CJSC Belgorodskaya Sotovaya Svyaz	Cellular Services	**30%**	–	30%	–
CJSC Smolenskaya Sotovaya Svyaz	Cellular Services	**40%**	–	40%	–
Impairment reserve			**(592)**		(2,815)
Total			**20,081**		15,927

All the above companies are Russian legal entities registered in accordance with Russian legislation and have the same financial year as the Company.

(in thousands of roubles)

8. Investments in Associates and Joint Ventures (continued)

The Company has investments in the following associates whose net assets were negative as of December 31, 2005 and 2004:

Name	Activity	Voting share, %	Net assets as of December 31 2005	Net assets as of December 31 2004
CJSC Smolenskaya Sotovaya Svyaz	Cellular services	40%	**(234,071)**	(120,005)
CJSC Belgorodskaya Sotovaya Svyaz	Cellular services	30%	**(272,358)**	(132,876)

In 2005 due to loss of control over CJSC "TeleRoss-Voronej", which was exercised through the majority of votes in Board of Directors, the company reclassified investments in CJSC "TeleRoss-Voronej" from investments in subsidiary companies to investments in associates.

Due to decrease of income and operational losses the company accrued 100% impairment reserve for CJSC "TeleRoss-Voronej" in 2005. CJSC "TeleRoss-Voronej" operated on the basis of licenses, granted powers of attorney as well as technological agreements giving the right to sign contracts on behalf of LLC "SZ Sovintel". In October 2004 LLC "SZ Sovintel" called off powers of attorney for the representative functions, ceased sales through CJSC "TeleRoss-Voronej", which lead to decrease of income.

Gain/loss from sale of shares in associates is presented in Note 29.

Movement in investments in associates for the years ended December 31, 2005 and 2004 is presented below:

	2005	2004
Investments in associates as of January 1	**15,927**	30,721
Acquisition of associates	–	2,815
Share of income/(loss), net of income tax and of dividends received	**1,468**	(367)
Reclassification	**462**	(5,435)
Disposal of associates	–	(8,992)
Impairment reserve recovery	**2,816**	–
Impairment reserve	**(592)**	(2,815)
Investments in associates as of December 31	**20,081**	15,927

(in thousands of roubles)

8. Investments in Associates and Joint Ventures (continued)

The following table illustrates summarised financial information of the major associates:

Associate	Voting shares	Assets	Liabilities	Revenues	Net income (loss)
2005					
CJSC TeleRossVoronej	**50%**	**23,762**	**(2,899)**	**3,674**	**(308)**
CJSC Smolenskaya Sotovaya Svyaz	**40%**	**4,272**	**(585,357)**	**79,982**	**(114,066)**
CJSC Belgorodskaya Sotovaya Svyaz	**30%**	**351,286**	**(680,986)**	**101,928**	**(139,482)**
CJSC SK Kostars	**28%**	**5,895**	**(8,486)**	**10,976**	**3,269**
OJSC Telecommunications company Rinfotels	**26%**	**408,628**	**(1,185)**	**10,850**	**146**
2004					
CJSC TeleRossVoronej	50%	8,148	(6,614)	12,288	771
CJSC Smolenskaya Sotovaya Svyaz	40%	160,232	(280,237)	30,959	(42,395)
CJSC Belgorodskaya Sotovaya Svyaz	30%	181,723	(306,806)	40,033	(68,454)
CJSC SK Kostars	28%	26,801	(10,377)	19,366	(4,744)
OJSC Telecommunications company Rinfotels	26%	6,856	(1,669)	11,243	636

All the above companies are Russian legal entities registered in accordance with Russian legislation and have the same financial year as the Company.

9. Investments in Joint Venture.

The company owns 30% stake in a joint venture with LLC “Topsnabinvest” and LLC “Bowling-Center” established for the purpose of producing, development, and commercial use of the communal system of the radiotelephone network in CDMA standard in Ivanovo. The joint venture agreement was signed on November 29, 2002 for the period of 8 years.

(in thousands of roubles)

9. Investments in Joint Venture (continued)

The share of the Company in assets, liabilities, revenues and expenses of this joint venture are accounted for using the equity method. Additional information relating to this joint venture as of December 31, 2005 and 2004 and for the years then ended is presented below:

	2005	2004
% of ownership	**30%**	30%
Non-current assets	**39,992**	41,911
Current assets	**11,400**	17,039
Current liabilities	**(2,796)**	(10,354)
Total net assets	**48,596**	48,596
Share in net assets	**14,579**	14,579
Revenue	**11,891**	19,209
Operating expenses	**(10,056)**	(10,616)
Other income and expenses	**(192)**	36
Total net income	**1,643**	8,629
Total share in net income	**493**	2,589

Any net income is distributed during the financial year, therefore net assets and the Company's share of net assets are shown after distribution.

10. Long-term Investments

As of December 31, 2005 and 2004, the Company's investments comprised the following:

	2005		2004	
Company	**Ownership interest**	**Carrying value**	**Ownership interest**	**Carrying value**
OJSC Svyazintech	**18%**	**20,603**	–	–
OJSC Sanatorium Krugozor, Pyatigorsk	**2.47%**	**2,008**	2.47%	2,008
OJSC Bank Tulskii Promishlennik	**0.80%**	**588**	0.80%	588
CJSC Oskoltelecom	**12.41%**	**474**	12.41%	474
OJSC AKB Svyaz-Bank	**1,28%**	**449**	1.28%	449
Other	**0.2%-6.6%**	**1,499**	0.1%-12.41%	10,143
Total investments available-for-sale	**–**	**25,621**	–	13,662

Management believes that the carrying amount of these investments approximates their fair values.

(in thousands of roubles)

10. Long-Term Investments (continued)

Purchase of share in OJSC "Informatsionnye Tehnologii Svyazy" (OJSC "Svyazintech")

In accordance with the decision of the Board of Directors at 9.02.2005, the Company acquired 18% of shares in OJSC "Svyazintech" for 27. In August 2005 the Company purchased additional newly issued 2,057,652 ordinary shares of OJSC "Svyazintech" for 20,577 in order to maintain its 18% share.

OJSC "Svyazintech" was established in 2005 for the implementation of Amdocs billing software in the companies of OJSC "Svyazinvest" Group (the parent company).

11. Long-Term Accounts Receivable and Other Assets

As of December 31, 2005 and 2004 long-term accounts receivable and other assets comprised the following:

	2005	2004
Long-term VAT receivable	**199,885**	299,130
Long-term loans given to employees	**20,034**	18,279
Other assets	**1,627**	185
Total	**221,546**	317,594

As of December 31, 2005 and 2004 long-term loans given to employees are accounted at amortized cost using the effective interest of 21%.

12. Long-Term Advances Given

As of December 31, 2005 and 2004 long-term advances given to suppliers of equipment comprised the following:

	2005	2004
Advances given for capital constructions	**611,654**	1,056,074
Advances given to subcontractors (related to acquisition and implementation of Oracle E-Business Suite software (Note 6))	**339,528**	52,608
Total	**951,182**	1,108,682

13. Inventories

Inventories at December 31, 2005 and 2004 comprised the following:

	2005	2004
Cable, materials and spare parts for telecommunications equipment	**194,384**	216,737
Construction materials, fuels and instruments	**92,839**	128,840
Finished goods and goods for resale	**16,710**	26,489
Other inventories	**210,280**	205,452
Provision for inventory obsolescence	**(585)**	–
Total	**513,628**	577,518

Provision for inventory obsolescence is recorded as other operating expenses in the consolidated statement of operations.

(in thousands of roubles)

14. Accounts Receivable, net

Accounts receivable as of December 31, 2005 and 2004 comprised the following:

	2005	2004
Trade receivables – telecommunication services	**3,795,294**	3,909,046
Trade receivables – other	**283,191**	152,864
Provision for impairement of receivables	**(2,201,028)**	(1,993,746)
Total	**1,877,457**	2,068,164

Accounts receivable for telecommunication services detailed by major customer groups were as follows:

	2005	2004
Residential customers	**1,232,784**	1,091,593
Corporate customers	**865,213**	859,937
Government customers	**158,223**	174,882
Tariff compensation from the state budget	**1,822,265**	1,935,498
Total	**4,078,485**	4,061,910

The Company invoices its governmental and corporate customers on a monthly basis. For residential customers, the Company sends monthly payment requests and substantially relies upon these customers to remit payments based on the received payment requests. All customer payments are based upon tariffs, denominated in roubles, in effect at the time the calls are made.

As of December 31, 2005 debt for tariff compensation from the state budget related to granting privileges to certain categories of subscribers amounted to 48,3% of total accounts receivable (2004 – 52,4%).

The following summarizes the changes in the provision for impairment of trade and other receivables:

	2005	2004
Balance at January 1	**(1,993,746)**	(1,247,545)
Provision for the year	**(296,524)**	(831,322)
Acquisition of subsidiares	**(79,873)**	(11,961)
Trade receivables write-off	**169,115**	97,082
Balance at December 31	**(2,201,028)**	(1,993,746)

15. Other Current Assets

As of December 31, 2005 and 2004 other current assets comprised the following:

	2005	2004
VAT receivable	**1,026,751**	1,269,407
Deferred expenses	**209,686**	202,625
Prepayments and advance payments	**162,375**	206,130
Other prepaid taxes	**30,226**	28,941
Receivables from fixed assets' sale	**23,102**	12,522
Settlements with personnel	**11,192**	10,602
Short-term loans given	**11,358**	28,924
Other receivables and current assets	**81,785**	268,914
Total	**1,556,475**	2,028,065

(in thousands of roubles)

16. Cash and Cash Equivalents

As of December 31, 2005 and 2004 cash and cash equivalents comprised the following:

	2005	2004
Cash at bank and on hand	**992,427**	1,416,586
Short-term deposits with maturity up to three months	**2,200**	628
Total cash and cash equivalents	**994,627**	1,417,214

Interest rate on short term deposits is 9.5 % per annum.

17. Significant Non-Cash Transactions

In 2005 the Company received telecommunication equipment under leasing terms in the amount of 609,291 (in 2004 – 1,413,383).

The Company received equipment contributions in 2005 in the amount of 62,271 (2004 – 22,758).

Non-cash transactions above have been excluded from the consolidated statement of cash flows.

18. Share Capital

The total number of outstanding shares comprises:

	Number of shares authorised (thousands)	Treasury shares (thousands)	Number of shares outstanding (thousands)	Par value	Carrying value	Treasury shares (thousands roubles)	Carrying value
As at December 31, 2003	**2,104,000**	–	**2,104,000**	**631,200**	**1,219,366**	–	**1,219,366**
Preference	525,993	–	525,993	157,798	304,840	–	304,840
Ordinary	1,578,007	–	1,578,007	473,402	914,526	–	914,526
As at December 31, 2004	**2,104,000**	–	**2,104,000**	**631,200**	**1,219,366**	–	**1,219,366**
Preference	525,993	–	525,993	1,577,979	1,725,020	–	1,725,020
Ordinary	1,578,007	(240)	1,577,767	4,733,301	5,175,145	(2,808)	5,172,337
As at December 31, 2005	**2,104,000**	**(240)**	**2,103,760**	**6,311,280**	**6,900,165**	**(2,808)**	**6,897,357**

All shares have a par value of 3 Roubles. The difference between the total par value and the total carrying value of share capital represents the effects of inflation accumulated trough January 1, 2003.

The ordinary shareholders are entitled to one vote per share.

(in thousands of roubles)

18. Share Capital (continued)

Preference shares give the holders the right to participate in general shareholders' meetings without voting rights except in instances where decisions are made in relation to re-organization and liquidation of the Company, and in relation to changes and amendments to the Company's charter which restrict the rights of preference shareholders. The preference shares have no rights of redemption or conversion but carry non-cumulative dividends per share of 10% of the Russian accounting net income for the year. If the Company fails to pay the above mentioned dividends, or has no profits in any year, the preferred shareholders have the right to vote in the general shareholders' meeting. Owners of the preferred shares have the right to participate in and vote on all issues within the competence of general meetings following the annual general meeting at which a decision not to pay (or to pay partially) dividends on preferred shares has been taken. Annual amount of dividends on preference shares may not be less than dividends on ordinary shares. The preference shareholders participate in earnings along with ordinary shareholders. Accordingly, the Company's preferred shares are considered participating equity instruments for the purpose of earnings per share calculations (refer to Note 31).

In case of liquidation, the property remaining after settlement with creditors, payment of preferred dividends and redemption of the par value of preferred shares is distributed among preferred and ordinary shareholders proportionately to the number of owned shares. Accordingly, the Company's preferred shares are considered participating equity instruments for the purpose of earnings per share calculations (refer to Note 31).

Distributable earnings of the Company are limited to the retained earnings, as mandated by the statutory accounting rules. Statutory retained earnings of the Company as of December 31, 2005 and 2004 amounted to 8,623,963 and 8,123,566 respectively.

In accordance with the Russian legislation, dividends may only be declared to the shareholders of the Company from net income as shown in the Company's Russian statutory financial statements. The Company reported net income of 668,504 and 397,711 in its statutory financial statements in 2005 and 2004, respectively.

Dividends were declared in 2005 in respect of 2004 to holders of ordinary shares and preference shares of rouble 0.0630084 per ordinary share (2004 – rouble 0.124867 per ordinary share) and rouble 0.0756115 per preference share (2004 –rouble 0.285662 per preference share). See also Note 32.

On April 9, 2001, the Company placed Level 1 American Depository Receipts (ADR). Each depository receipt is equal to 100 ordinary shares of the Company. At the end of 2005 the Company registered 417,494 ADR and deposited 41,749,400 ordinary shares, which amounted to 2.65% of all issued ordinary shares.

The following table represents ADR registration for 2003-2005:

	ADR (quantity)	**Ordinary Shares Equivalent (quantity)**	**Ordinary Shares %**	**Charter Capital %**
December 31, 2003	249,361	24,936,100	1.58%	1.19%
Decrease 2004	(17,433)	(1,743,300)		
December 31, 2004	231,928	23,192,800	1.47%	1.10%
Increase 2005	185,566	18,556,600		
December 31, 2005	**417,494**	**41,749,400**	**2.65%**	**1.98%**

(in thousands of roubles)

18. Share Capital (continued)

Currently ADR are traded on the following stock markets:

Stock market	CUSIP(WKN)	ADR ticker	ISIN
Over-the-counter (OTC) market (USA)	15548M108	CRMUY	US15548M1080
Frankfurt Stock Exchange (FSE)	798404	CRMUy.F	US15548M1080
Berlin Stock Exchange (BerSE)	798404	CRMUy.BE	US15548M1080

The Company's shareholding structure as of December 31, 2005 was as follows:

	Ordinary shares		Preference shares		
	Number (thousands)	**%**	**Number (thousands)**	**%**	**Total**
OJSC "Svyazinvest"	799,868	50.69%	–	–	**799,868**
Other legal entities	666,862	42.26%	432,677	82.26%	**1,099,539**
Individuals	69,288	4.39%	93,316	17.74%	**162,604**
ADR holders	41,749	2.65%	–	–	**41,749**
Treasury shares	240	0.02%	–	–	**240**
Total	**1,578,007**	**100.00%**	**525,993**	**–**	**2,104,000**

Treasury stock represents ordinary shares of the Company, held by a subsidiary of the Company.

(in thousands of roubles)

19. Borrowings

As of December 31, 2005 and 2004 borrowings comprised the following:

	Interest rate	Maturity date	2005	2004
Short-term borrowings				
Bank loans:				
Bank loans (Roubles)	11% - 15%	2006	1,593,161	1,717,165
Bank loans (US Dollars)	11.4% - 11.8%	2006	1,775	3,352
Bank loans (Euro)	8%-9%	2006	75,655	90,167
Total bank loans			**1,670,591**	**1,810,684**
Accrued interest on bonds (Roubles)	11.9% - 15.4%	2006	**428,769**	**378,504**
Vendor financing:				
Vendor financing (Roubles)	18.3%	–	–	18,967
Vendor financing (US Dollars)	9.00%	2006	44	–
Vendor financing (Euro)	6% - 6.5%	2006	501	2,478
Total vendor financing			**545**	**21,445**
Promissory notes:				
Accrued interest on promissory notes (Roubles)	9.9-15%	2006	162,039	1,393,764
Accrued interest on promissory notes (US Dollars)	6%	2006	1,820	–
Total promissory notes			**163,859**	**1,393,764**
Total short-term borrowings			**2,263,764**	**3,604,397**

(in thousands of roubles)

19. Borrowings (continued)

	Interest rate	Maturity date	2005	2004
Long-term borrowings				
Bank loans:				
Bank loans (Roubles)	12% - 14.5%	2006-2010	6,348,054	5,516,386
Bank loans (US Dollars)	7,5% - 11.8%	2006-2010	125,593	338,092
Bank loans (Euro)	5.75% - 9%	2006-2007	428,914	765,716
Bank loans (Japanese yen)	4.80%	–	–	5,830
Total bank loans			**6,902,561**	**6,626,024**
Bonds (Roubles)	9.79%	2006	**7,508,966**	**8,114,606**
Vendor financing:				
Vendor financing (Roubles)	12%	2006-2007	1,770	13,607
Vendor financing (US Dollars)	9% - 9.14%	2006-2010	25,307	30,227
Vendor financing (Euro)	6% - 9%	2006-2007	89,415	233,860
Total vendor financing			**116,492**	**277,694**
Promissory notes:				
Promissory notes (Roubles)	9.9% - 18%	2006-2007	4,404,733	669,928
Promissory notes (US Dollars)	6.00%	2006	378,751	1,068,183
Total promissory notes			**4,783,484**	**1,738,111**
Loans from related parties (OJSC "Svyazinvest", Note 35)			–	29,000
Restructured loans from customers - connection fees (Roubles)			83,364	82,382
Less: Current portion of long-term borrowings			(12,570,338)	(3,864,032)
Total long-term borrowings			**6,824,529**	**13,003,785**

As of December 31, 2005 short-term borrowings included interest payable in the amount of 683,740 (2004 – 428,766).

As of December 31, 2005 bank loans and vendor financing are secured by equipment with the carrying value of 5,334,954 (2004 - 6,553,289).

(in thousands of roubles)

19. Borrowings (continued)

As of December 31, 2005, long-term borrowings had the following maturity schedule:

Maturity date	Bank loans	Bonds	Vendor financing	Promissory notes	Other	Total
2006	2,418,297	7,508,966	68,271	2,574,804	–	12,570,338
2007	428,876	–	28,961	2,208,681	1,496	2,668,014
2008	2,345,268	–	–	–	15,893	2,361,161
2009	1,266,200	–	–	–	750	1,266,950
2010	443,920	–	19,260	–	–	463,180
2010 and after	–	–	–	–	65,225	65,225
Total	**6,902,561**	**7,508,966**	**116,492**	**4,783,485**	**83,364**	**19,394,868**

The Company's borrowings are denominated in the following currencies:

Currency	2005	2004
Russian Roubles	**20,530,856**	17,934,309
Euro	**594,485**	1,092,221
US dollars	**533,290**	1,439,854
Japanese yen	–	5,830
Total	**21,658,631**	20,472,214

The Company has not entered into any hedging arrangements in respect of its foreign currency obligations or interest rate exposures.

Short-Term Borrowings

Bank Loans

OJSC Vneshtorgbank

In 2005 the Company entered into a loan agreement with Vneshtorgbank. The loan matures in 2006. The total amount of 1,551,401 was outstanding as of December 31, 2005. The loan bears interest at 11% per annum. The loan is denominated in Roubles. The loan is not secured.

19. Borrowings (continued)

Long-Term Loans and Borrowings

Bank Loans

Sberbank

Long-term borrowings from Sberbank mostly represent rouble denominated loans received in 2003-2005. The loans mature in 2006-2010. The loans bear interest of 12-15%. As of December 31, 2005, the outstanding amount was 5,207,950. The loans are secured with property, plant and equipment valued at 2,894,255.

OJSC Vnesheconombank

In 1995-1996, the Ministry of Finance of the Russian Federation provided long-term financing to the Company to purchase telecommunications equipment from various foreign vendors. Vnesheconombank acted as the agent on behalf of the Government of the Russian Federation. The loan is denominated in Euro. At December 31, 2005 the outstanding amount of principal part of loan was 382,272..The principal debt outstanding is presented as short-term portion of long-term liabilities. The interest under these agreements is accrued at a floating rate Plafond C, which in 2005 approximated 5-6 %, plus 2 % per annum. Interest payable as of December 31, 2005 is included in short-term liabilities and equalled to 75,582. The loan is not secured.

As described in Note 33 "Contingencies and operating risks" in July 2005 the Company received a claim for immediate repayment of the outstanding amount overdue to the bank. As of December 31, 2005 the outstanding amount is included in the current-portion of long-term loans and borrowings.

OJSC Vneshtorgbank

In 2002-2005 the Company entered into several loan agreements with Vneshtorgbank. The loans mature in 2006-2008. The total amount of 419,099 was outstanding as of December 31, 2005. The loans bear interest of 6-13% per annum. The loans are secured with property, plant and equipment valued at 373,578

OJSC AKB Promsvyazbank

Long-term borrowings from Promsvyazbank mostly represent rouble denominated loans received in 2004-2005. The loans mature in 2006-2010. As of December 31, 2005 the outstanding liability under these agreements amounted to 650,000. Interest is accrued at 12.5-14.5% per annum. The loans are secured by property, plant and equipment valued at 1,107,745.

OJSC Vneshtorgbank 24 (Guta-Bank)

In 2001-2004 the Company entered into long-term loan agreements with Guta-Bank. The loans mature in 2006-2007. The amounts payable under the agreements are denominated in Russian roubles and US dollars. Interest for loans denominated in Russian roubles is accrued at 14-15% per annum, for loans, denominated in dollars – LIBOR + 7%. As of December 31, 2005 the outstanding liability under these agreements amounted to 30,000 for loans, denominated in Russian roubles and 70,999 for loans, denominated in US dollars. The loans are secured by property, plant and equipment valued at 43,021.

19. Borrowings (continued)

Long-Term Loans and Borrowings (continued)

Bank Loans (continued)

Russian Development Bank

Long-term borrowings from Russian Development Bank represents a rouble denominated loan for the total amount of 142,000 received in August 2005. The loan matures on July, 31 2007. The loan bears interest at 14%. As of December 31, 2005 the outstanding amount was 142,000. The loan is secured with property, plant and equipment valued at 89,562.

Bonds

In September 2003 the Company registered the issue of interest-bearing bonds 03 series with a par value of 1,000 Roubles each for the total amount of 1,959,028. Bonds have 6 coupons. Payments against the first coupon are made on the 183-rd day from the date of issue; interest per other coupons is payable every subsequent 183-rd day. The bonds attract effective interest at 15.19% per annum. The bonds mature in 1,095 days from the date of issue in September 2006.

In September 2003 the Company offered to buy back its 03 series bonds at 101.5% of par value in September – October 2004. Bonds for the total amount of 1,284,820 were repurchased and issued back in September – October 2004 for the same amount. Re-issued bonds bear effective interest rate of 13.71 % per annum. The cost of placement of these bonds was 14,702. Unredeemed bonds bear effective interest rate 11.33% per annum.

In September 2004 the Company also published an irrevocable offer to buy back 03 series bonds on September 19, 2005. None of these bonds were submitted for repurchase.
The outstanding amount of 03 series bonds as at December 31, 2005 equaled to 1,990,641 and was classified as current portion of long-term loans and borrowings.

In June 2004 the Company registered and issued interest-bearing bonds series 04 with a par value of 1,000 Rubles each for the total amount of 5,518,581. The bonds mature in 1,830 days from the date of issue. Bonds have 10 coupons. Payments against the first coupon is made on the 183-rd day from the date of issue; interest per other coupons is payable every subsequent 183-rd day. The effective interest rate is determined at 15.37% per annum.

In August 2004 the Company announced an irrevocable offer to repurchase 04 series bonds in November 2006. Accordingly, the outstanding liability of 5,518,581 was classified as a current portion of long-term debt as at December, 31 2005.

Vendor Financing

Mashpriborcom

In 1997 the Company entered into several agreements with Mashpriborcom under which it delivered telecommunication equipment to the Company. In accordance with agreements the liability matures in 2007. The amounts payable under these agreements are denominated in Euro. The agreements bear interest at 6%. The amount outstanding as of December 31, 2005 was 55,503. The agreements are secured with property, plant and equipment valued at 55,044.

19. Borrowings (continued)

Vendor Financing (continued)

Iskratel

In 2003-2004 the Company entered into several agreements with Iskratel, under which it delivered telecommunication equipment to the Company. The agreements mature in 2006-2007 and their amounts are denominated in Euro. The agreements bear interest of 9%. As of December 31, 2005 the outstanding long-term liability under these agreements amounted to 28,270. The liability is not collateralized.

Promissory Notes

LLC IBM East Europe/Asia

In December, 2004 the Company purchased Amdocs Billing Suite software from IBM Eastern Europe/Asia. In this connection the Company issued US dollar denominated promissory notes in the amount of 1,093,751. The outstanding amount as at December 31, 2005 was 380,571 (2004 – 692,699). The loan bears an effective interest rate of 5.97% per annum. The liability is not collateralized.

LLC Brokerage Company "Region"

In 2005 the Company issued promissory notes to LLC "Region" to finance its working capital. The promissory notes mature in January 2007 and bear effective interest rate of 9.8% per annum. The outstanding amount as at December 31, 2005 was 1,327,033.

LLC Brokerage Company "North-West Investment Center"

In 2005 the Company entered into several promissory notes agreements with LLC "North-West Investment Center" to finance its working capital. The promissory notes mature in 2006-2007 and bear effective interest rates of 9-15.6% per annum. The outstanding amount of principal part of promissory notes as at December 31, 2005 was 2,309,202. Interest payable as of December 31, 2005 is included in short-term liabilities and equalled to 156,560.

OJSC "Vneshtorgbank"

In July 2004 the Company entered into several promissory notes agreements with OJSC "Vneshtorgbank" to finance its working capital. The promissory notes mature in 2006 and bear effective interest rate of 17-18% per annum. The outstanding amount as at December 31, 2005 was 758,793.

(in thousands of roubles)

20. Finance Lease Obligations

The Company has finance lease contracts for telecommunication equipment. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments as of December 31, 2005 and 2004 are as follows:

	2005		2004	
	Minimum lease payments	**Present value of payments**	**Minimum lease payments**	**Present value of payments**
Current portion	**1,192,641**	**743,000**	1,132,393	672,491
2 to 5 years	**2,104,960**	**1,562,302**	2,427,529	1,775,171
Total minimum lease payments	**3,297,601**	**–**	3,559,922	–
Less amounts representing finance charges	**(992,299)**	**–**	(1,112,260)	–
Present value of minimum lease payments	**2,305,302**	**2,305,302**	2,447,662	2,447,662

In 2005 and 2004, the Company's primary lessors were OJSC "RTC-Leasing" and LLC "Promsvyazleasing". In 2005, the effective interest rate on lease liabilities ranged from 19% to 42% per annum (2004 – 15% to 48% per annum).

OJSC "RTC-Leasing" purchases telecommunication equipment from domestic and foreign suppliers and provides such equipment to the Company under finance lease agreements. The Company's obligations under finance leases to OJSC "RTC-Leasing" as of December 31, 2005 amounted to 2,219,854 (2004 – 2,275,991).

OJSC "RTC-Leasing" is entitled to adjust the lease payment schedule in the event of a change in certain economic conditions, in particular, a change in the refinancing rate of the Central Bank of the Russian Federation.

As of December 31, 2005 and 2004 finance lease obligations denominated in foreign currency, amounted to 67,879 and 152,588, respectively, and were mainly in US dollars.

21. Accounts Payable, Accrued Expenses and Advances Received

As of December 31, 2005 and 2004, the Company's accounts payable, accrued expenses and advances received comprised the following:

	2005	2004
Trade accounts payable and accrued expenses	**834,322**	579,048
Advances received from subscribers	**465,895**	444,857
Accounts payable for capital investments	**457,692**	1,633,963
Salaries and wages	**471,479**	305,841
Other accounts payable	**48,279**	75,953
Total	**2,277,667**	3,039,662

Accounts payable for capital investments in the amount of 225,067 and 117,527 included in trade payables as of December 31, 2005 and 2004, respectively, are denominated in foreign currency, mainly Euro and US dollars.

(in thousands of roubles)

22. Taxes Payable

As of December 31, 2005 and 2004, taxes payable comprised the following:

	2005	2004
Value-added tax	**902,858**	845,639
Property tax	**160,090**	149,203
Unified social tax	**11,058**	14,216
Other taxes	**24,852**	61,135
Total	**1,098,858**	1,070,193

Included in value added tax payable is the amount of 571,997 (2004 – 580,528), which represents deferred value added tax, that is only payable to the tax authorities when the underlying receivables are recovered or written off. Starting January 1, 2006 amendments to Tax Code relating to rules of determination of the taxable base were introduced. These are described in Note 37 "Subsequent events".

23. Long-Term Taxes Payable

Long-term taxes payable comprises overdue debt repayments for various taxes which were restructured for the period of up to 10 years in accordance with regulation #1002 of the Government of Russian Federation dated September 3,1999 "On procedure and time limits of restructuring of tax payables of legal entities" and in accordance with regulation #442 of the Administration of the Tula Region dated August 9, 2002. "On procedure of restructuring in 2002 of payables (principal debt, fines and penalties) of legal entities before regional tax budget that forms territorial road fund"; Regulation of Heads of Administration of the Vladimir region #368 dated June 26, 2001 and #168 dated July 12, 2001; Regulation of the Administration of the Voronej region #959 dated August 29, 2001, as shown below.

The following table shows book value and debt maturity:

	2005			2004		
	Federal Budget	**Regional Budgets and other non-budgetary funds**	**Total**	**Federal Budget**	**Regional Budgets and other non-budgetary funds**	**Total**
1-2 years	**3,723**	**1,108**	**4,830**	980	792	1,772
2-3 years	**4,791**	**672**	**5,464**	2,119	684	2,803
3-4 years	**6,211**	**600**	**6,811**	3,684	1,500	5,184
4-5 years	**4,492**	**607**	**5,099**	5,015	1,085	6,100
Over 5 years	**2,587**	**402**	**2,989**	6,466	2,021	8,487
Long-term taxes payable	**21,804**	**3,389**	**25,193**	18,264	6,082	24,346
Short-term portion of long-term taxes payable	**1,572**	**884**	**2,456**	648	137	785
Total taxes payable	**23,376**	**4,273**	**27,649**	18,912	6,219	25,131

(in thousands of roubles)

24. Pension Liabilities

In addition to statutory pension benefits, the Company also contributes to post-employment benefit plans, which covers most of its employees.

Defined Contribution Pension Plans

For employees of certain branches, the Company provides post-employment benefits, which are classified as defined contribution pension plans. Non-government pension fund Telecom-Soyuz, which is related to the Company, maintains the plan.

During 2005 the Company made 316,460 of contributions under all of its defined contribution pension plans (2004 – 62,858) that were expensed.

Defined Benefit Pension Plans

The defined benefit pension plan provides old age retirement pension and disability pension. The plans provide for payment of retirement benefits starting from statutory retirement age, which is currently 55 for women and 60 for men. The benefits are based on a formula specific to each branch of the Company. According to the formula the benefits depend on a number of parameters, including the relative pay of participants and their length of service in the Company at retirement. The benefits do not vest until and are subject to the employee retiring from the Company on or after the above-mentioned ages.

Non-government pension fund Telecom-Soyuz, which is related to the Company (Note 35), maintains the defined benefit pension plan. The Company makes contributions to the pension fund in the amount set forth in the agreement with the pension fund.

The Company further provides other long-term employee benefits such as a death-in-service payments and lump-sum payment upon retirement of a defined benefit nature.

Additionally the Company provides financial support of a defined benefit nature to its old age and disabled pensioners.

As of December 31, 2005 there were 64,893 active participants to the defined benefit pension plan of the Company (as of December 31, 2004 – 67,406).

As of December 31, 2005 and 2004 the net liabilities of defined benefit pension and other post-employment benefit plans comprised the following:

	2005	**2004**
Present value of defined benefit obligation	**1,928,000**	1,836,000
Fair value of plan assets	–	(398,000)
Present value of unfunded obligations	**1,928,000**	1,438,000
Unrecognized past service cost	**(1,397,000)**	(1,340,000)
Unrecognized actuarial (losses)/gains	**319,000**	467,000
Net pension liability in the balance sheet	**850,000**	565,000

As of December 31, 2005 management estimated employees' average remaining working life at 8 years (2004 - 12 years).

(in thousands of roubles)

24. Pension Liabilities (continued)

Defined Benefit Pension Plans (continued)

The amount of net expense for the defined benefit pension and other post-employment benefit plans recognized in 2005 and 2004 was as follows:

	2005	2004
Interest cost	**173,000**	222,000
Service cost	**86,000**	134,000
Expected return on plan assets	**(36,000)**	(34,000)
Actuarial gains	**(24,000)**	–
Amortization of past service cost	**134,000**	135,000
Past service cost recognized in current year	**(69,000)**	–
Curtailment or final settlement effect	**63,000**	–
Net expense for the defined benefit pension plan	**327,000**	457,000

Expenses to defined benefit pension plans were included in line "Wages, salaries, other benefits and payroll taxes" in the consolidated statement of operations.

As of December 31, 2005 and 2004 the principle actuarial assumptions of defined benefit pension plans and other post-employment benefit plans were as follows:

	2005 Per annum	2004 Per annum
Discount rate	**7.00%**	9.18%
Expected return on plan assets	**7.05%**	9.33%
Future salary increases	**8.15%**	9.18%
Relative pay increase (career progression)	**1%**	1%
Rate used for calculation of annuity value	**6%**	6%
Increase in financial support benefits	**5%**	6%
Staff turnover	**7%**	2.5%
Mortality tables (source of information)	**USSR 1985/86**	Russia 1998

Movements in the net assets of defined benefit pension plans and other post-employment benefit plans during 2005 and 2004 were as follows:

	2005	2004
Fair value of plan assets at January 1	**398,000**	353,000
Actual return on plan assets	**52,000**	16,000
Employer contributions	**42,000**	257,000
Benefits paid	**(75,000)**	(228,000)
Settlements	**(417,000)**	–
Fair value of plan assets at December 31	**–**	398,000

Actual return on plan assets for 2005 was 13.5 %.

(in thousands of roubles)

24. Pension Liabilities (continued)

Defined Benefit Pension Plans (continued)

The movements in the net liability for defined benefit pension plans and other post-employment benefit plans recognized in 2005 and 2004 are as follows:

	2005	2004
Net liability at January 1	**565,000**	365,000
Net expense for the year	**327,000**	457,000
Contributions	**(42,000)**	(257,000)
Net liability at December 31	**850,000**	565,000

Other payables to Telecom-Soyuz amounted to 420 and the total amount of pension liability at 31/12/2005 was 850,420.

25. Reduction of staff

Expenses of the Company in the form of compensation to former employees due to reduction of staff in 2006 are expected to be equal to 10,315.

26. Revenues

Revenues for the year ended December 31, 2005 and 2004 comprised the following:

By revenue types	2005	2004
Local telephone calls	**10,818,463**	7,906,535
Long distance calls - domestic	**8,711,225**	9,145,616
Long distance calls - international	**1,733,843**	1,782,194
Installation and connecting fees	**1,422,238**	2,037,887
New services	**1,318,353**	918,873
Services for national operators	**966,084**	730,920
Radio and TV broadcasting	**710,338**	678,310
Data transfer and telematic services	**455,895**	388,046
Cellular services	**267,128**	322,012
Rent of telephone channels	**245,747**	187,603
Documentary services	**56,255**	89,383
Other telecommunication services	**903,168**	813,837
Other revenue	**1,091,913**	1,027,864
Total	**28,700,650**	26,029,080

The Company identifies revenue by the following major customer groups:

Customer groups	2005	2004
Residential customers	**16,976,958**	15,209,039
Corporate customers	**9,583,770**	9,015,268
Government customers	**2,137,160**	1,804,773
Total	**28,697,888**	26,029,080

(in thousands of roubles)

27. Other Operating Expenses

The components of other expenses were as follows:

	2005	2004
Fire and other security services	**(436,017)**	(388,577)
Lease of premises	**(408,258)**	(373,694)
Cost of goods sold	**(258,074)**	(276,438)
Non-commercial partnership expenses (Note 33)	**(215,801)**	(296,677)
Insurance	**(214,896)**	(273,045)
Bank services fees	**(211,766)**	(269,858)
Universal service fund payments	**(204,731)**	–
Transportation services	**(188,432)**	(174,668)
Buildings maintenance	**(130,050)**	(93,710)
Agency fees	**(113,669)**	(21,783)
Audit and consulting fees	**(113,107)**	(144,438)
Advertising expenses	**(110,630)**	(134,669)
Charitable contributions	**(97,062)**	(119,584)
Education expenses	**(91,826)**	(72,204)
Telecommunication equipments maintenance	**(61,426)**	(65,959)
Business travel expenses and representation costs	**(41,463)**	(50,590)
Civil Defense	**(35,256)**	(27,299)
Post services	**(16,108)**	(15,312)
Fines and penalties	**(6,826)**	(21,893)
Payments to Gossvyaznadzor	**–**	(71,718)
Other expenses	**(569,943)**	(420,113)
Total	**(3,525,341)**	(3,312,229)

In 2005 the Company incurred an expense on payments to Universal service fund. These payments are prescribed by Federal Law on Communications and Government Decree # 243 of April 21, 2005. Payments are calculated as 1.2% of the revenues from the telecommunication services less revenues from interconnection services. Related contingency is disclosed in Note 33.

Other expenses include expenses related to social expenditures, billing and cash collection services, cost of documentary, pay phone and other telecommunication services, representation expenses and other operating expenses.

28. Interest Expense, net

Interest expense, net for the years ended December 31, 2005 and 2004 comprised the following:

	2005	2004
Interest income	**9,056**	69,216
Interest expense	**(2,110,136)**	(1,528,900)
Interest expense on finance leases	**(504,758)**	(414,816)
Interest expense on vendor financing	**(1,766)**	(5,117)
Total	**(2,607,604)**	(1,879,617)

(in thousands of roubles)

29. Gain from Investments

Gain from associates and other investments for the year ended December 31, 2005 and 2004 comprised the following:

	2005	2004
Disposal of subsidiaries and associates	–	300,197
Total gain/(loss) from disposal of investments, avalible for sale	**7,042**	(44)
Impairment reserve / (recovery of reserve) on investments	**2,289**	(2,815)
Valuation of investments	**(673)**	–
Dividend income	**214**	20
Total	**8,872**	297,358

30. Income Tax

Income tax charge for the years ended December 31, 2005 and 2004 comprised the following:

	2005	2004
Current income tax expense	**(648,100)**	(533,531)
Deferred tax benefit – origination and reversal of temporary differences	**227,365**	379,457
Total income tax for the year	**(420,735)**	(154,074)

A reconciliation of the theoretical tax charge to the actual income tax charge is as follows:

	2005	2004
Profit before income tax	**(228,484)**	(847,145)
Statutory income tax rate	**24%**	24%
Theoretical tax credit at statutory income tax rate	**54,836**	203,315
Increase (decrease) resulting from the effect of:		
Non-deductible expenses	**(492,559)**	(393,111)
Other	**16,988**	35,722
Total income tax charge for the year at the effective rate of 184% (2004 - 18%)	**(420,735)**	**(154,074)**

(in thousands of roubles)

30. Income Tax (continued)

The composition of deferred income tax assets and liabilities as of December 31, 2005 and 2004 was as follows:

	As at December 31, 2003	Origination and reversal of temporary differences	As at December 31, 2004	Origination and reversal of temporary differences	Acquisition of subsidiaries	As at December 31, 2005
Deferred tax assets						
Property, plant and equipment	–	–	–	–	9,209	**9,209**
Accounts payable and accrued liabilities	159,151	(74,060)	85,091	221,437		**306,528**
Accounts receivable	50,452	79,312	129,764	48,875	16,933	**195,572**
Effect of investments valuation	7,459	66,113	73,572	(2,625)	–	**70,947**
Loans		6,444	6,444	(6,444)	–	–
Other	65,600	(24,687)	40,913	(21,322)	–	**19,591**
Total deferred tax assets	282,662	53,122	335,784	239,921	26,142	**601,847**
Deferred tax liabilities						
Property, plant and equipment	(779,787)	366,936	(412,851)	204,521	–	**(208,330)**
Finance Lease	(30,052)	(5,407)	(35,459)	35,459	–	–
Intangible assets	–	(35,194)	(35,194)	(137,814)	–	**(173,008)**
Loans	–	–	–	(114,722)	–	**(114,722)**
Total deferred tax liabilities	(809,839)	326,335	(483,504)	(12,556)	–	**(496,060)**
Deferred Tax Assets / Liabilities, net	(527,177)	379,457	(147,720)	227,365	26,142	**105,787**

The movement in deferred tax liability and asset for the years ended December 31, 2005 and 2004 was as follows:

	2005	**2004**
Deferred tax liability, at January 1	**(147,720)**	(527,177)
Deferred income tax benefit	**227,365**	380,419
Prior year deferred income tax adjustments		2,172
Deferred income tax assets (liability) of acquired subsidiaries	**26,142**	(3,149)
Recovery of provision for deferred income tax asset		614
Deferred income tax related to unrealized gain on available-for-sale financial assets	**–**	(599)
Net deferred tax asset / liability at December 31	**105,787**	(147,720)

In the context of the Company's current structure, tax losses and current tax assets of the different companies may not be set off against current tax liabilities and taxable profits of other companies and, accordingly, taxes may accrue even where there is a net consolidated tax loss. Therefore, deferred tax asset of one company of the Company is not offset against deferred tax liability of another company.

(in thousands of roubles)

31. Loss per Share

Loss per share is calculated by dividing the net loss attributable to shareholders of the parent by the weighted average number of shares in issue during the period.

The calculation of basic and diluted loss per preferred and ordinary share is presented below (loss per share is stated in Roubles):

	2005	2004
Loss for the year attributable to equity holders of the parent	(649,862)	(1,009,223)
Weighted average number of ordinary shares outstanding (thousands) and other participating instruments (see Note 18)	2,103,980	2,104,000
Basic and diluted loss per share attributable to equity holders of the parent, Russian Roubles	(0.309)	(0.480)

The Company has no dilutive potential ordinary shares; therefore, the diluted loss per share equal basic loss per share.

32. Dividends Declared and Proposed for Distribution

Dividends declared in 2005 based on 2004 results:

Dividends on ordinary shares – 0,063008 Roubles per share	99,428
Dividends on preference shares – 0,075611 Roubles per share	39,771
Total	**139,199**

Dividends paid to shareholders are determined by the Board of Directors and declared and officially approved at the annual shareholders' meeting. Earnings available for dividends are limited to profits determined in accordance with the Russian statutory accounting regulations. Dividends are accrued in the year they are declared and approved.

33. Contingencies and Operating Risks

Operating Environment of the Company

The Russian economy while deemed to be of market status continues to display certain characteristics consistent with that of a market in transition. These characteristics include, but are not limited to, relatively high inflation and the existence of currency controls which cause the national currency to be illiquid outside of Russia. The stability of the Russian economy will be significantly impacted by the government's policies and actions with regards to supervisory, legal, and economic reforms.

Management cannot predict what effect changes in fiscal, political or tariff policies may have on the Company's current financial position or its ability to make future investments in property, plant and equipment. The consolidated financial statements do not include any adjustments that might result from these uncertainties. Related effects will be reported in the financial statements as they become known and estimable.

33. Contingencies and Operating Risks (continued)

Taxation

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Company may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. It is not practical to determine the amount of unasserted claims that may manifest, if any, or the likelihood of any unfavourable outcome. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review.

Tax Claims

On April 2006, the tax authorities completed their audit of the Company's taxes in 2002 and 2003 and delivered a tax assessment in the total amount of 2,353,512, including penalties of 953,419. The most significant part of the assessment relates to taxation of income on settlements between operators.

The Company disagrees with the tax assessment and believes that it has sufficient arguments to successfully defend its position in court. As such, no provision has been made for the above mentioned claim.
However, as of now court perspective of such tax claims seems to be unclear in view of court practice absence.

Insurance Coverage

Insurance business in Russia is still in a formative stage and many types of insurance available in other countries have not become common use in Russia yet. During 2005, the Company did not maintain insurance coverage on a significant part of its property, plant and equipment, business interruption losses, or third party liability in respect of property or environmental damage arising from accidents relating to the Company's property or the Company's operations. Until the Company obtains adequate insurance coverage, there is a risk that losses resulting from destruction of certain assets could have a material adverse effect on the Company's operations and financial position.

Legal Proceeding

The Russian legal system is characterized by (1) inconsistencies between and among laws, Presidential decrees, and Russian governmental, ministerial and local orders, decisions, and resolutions and other acts; (2) conflicting local, regional and federal rules and regulations; (3) the lack of judicial and administrative guidance on interpreting legislation; (4) the relative inexperience in legislation interpretation; and (5) a high degree of discretion on the part of governmental authorities.

Management is unable to estimate what developments may occur in respect if the Russian legal system or the resulting effect of any such developments on the Company's financial condition or future results of operations.
In the nearest future the Company's activity could be subject by judicial reform factors. The Company's financials have no adjustments resulted from these uncertainties.

In July 2005 the Ministry of Finance of the Russian Federation filed a claim against the Company demanding immediate repayment of debts outstanding to Vnesheconombank as of July 12, 2005 in the amount of 457,428 (13,259 thousand euro).

33. Contingencies and Operating Risks (continued)

Legal Proceeding (continued)

During the year the Company was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings of other claims outstanding, which could have a material effect on the result of operations or financial position of the Company and which have not been accrued or disclosed in these consolidated financial statements.

Licenses

Substantially all of the Company's revenues are derived from operations conducted pursuant to licenses granted by the Russian Government. These licenses expire in various years ranging from 2006 to 2012. Suspension or termination of the Company's main licenses or any failure to renew any or all of these main licenses could have a material adverse effect on the financial position and operations of the Company.

The Company renewed these licenses on a regular basis in the past, and believes that it will be able to renew licenses without additional cost in the normal course of business.

The Government of the Russian Federation is in process of liberalization of telecommunications market for which additional licenses on providing DLD/ILD has been granted to a number of alternative operators. It is possible that the Company's future results of operations and cash flows could be materially affected by the increased competition in a particular period but the effect can not be currently determined.

The Decision of the Russian Government # 87 "On Endorsement of the list of the names of communication services entered in licenses and the lists of license terms" of February 18, 2005 (amended as at December 29, 2005 # 837) prescribed types of connection services that are to be included into licenses and list of licensing terms. Licensing terms defined in previously issued licenses are effective unless they contradict the current regulations. The Company considered significant effect of new requirements related to the interconnection settlements, traffic transmission and mobile services on current licensing terms for licenses issued prior to January 1, 2004 and in November 2005, the Company submitted to Federal Service for Communications Supervision (Rossvyaznadzor) its request for changes and amendments to the existing License for provision of local, intercity telecommunications services in order to bring the License terms in compliance with the requirements set by Governmental Decree # 87 dated February 18, 2005. All necessary amendments to the licenses were received.

Optimisation of the Number of Employees

In the framework of increase of operating performance the Company developed the program of optimization of the number of employees for 2006-2008, authorized by the Board of Directors (minutes #21 dated 31.03.2006).

The program provides for a gradual reduction of number of employees from 2006 to 2009. Within 2006 the Company plans to cut down personnel by 7,824. As of December 31, 2005 742 employees were notified about their dismissal. The company accrued contingent liabilities reserve (Note 25).

Guarantees Issued

The Company mainly guaranteed credit line facilities provided by Sberbank to OJSC "RTC-Leasing", a lessor of telecommunication equipment, as of December 31, 2005 (Note 19). The total guarantees amounted to 2,812,210 (2004 – 3,429,572).

(in thousands of roubles)

34. Contractual Commitments

Operating Leases

As of December 31, 2005 and 2004 the contractual commitments under operating lease were 465,097 and 318,222 respectively (net of VAT).

	2005	2004
Current Portion	**161,767**	121,434
From 1 to 5 years	**111,424**	101,569
Over 5 years	**191,906**	95,219
Total	**465,097**	318,222

Capital Investments

As of December 31, 2005 and 2004 the Company had commitments for capital investments in modernization and expansion of its network in the amount of approximately 556,534 and 632,390, respectively.

As of December 31, 2005 and 2004 contractual commitments for acquisition of property, plant and equipment were 27,787 and 180,774 respectively.

35. Balances and Transactions with Related Parties.

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the related party relationships for those related parties with whom the Company entered into significant transactions or had significant balances outstanding at December 31, 2005 are detailed below.

(in thousands of roubles)

35. Balances and Transactions with Related Parties (continued)

Rendering Services

During the year ended December 31, 2005 and 2004 the Company rendered services to the following related parties:

Related Party	Relationship	Type of Sales	Price determination method	2005	2004
OJSC "Rostelecom	Controlled by OJSC "Svyazinvest"	Services of traffic transmission	Calculated rates and tariffs, regulated by MAP	**1,183,894**	1,176,272
CJSC Smolenskaya Sotovaya Svyaz	Associate Company	Telecommunications Services	Arms' length terms	**28,002**	6,082
CJSC Belgorodskaya Sotovaya Svyaz	Associate Company	Telecommunications Services	Arms' length terms	**25,986**	11,831
OJSC Central Telegraph	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**23,232**	12,207
OJSC Telecommunications Company Rinfotels	Associate Company	Telecommunications Services	Arms' length terms	**4,987**	4,296
OJSC AKB Svyaz-Bank	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**2,845**	1,645
OJSC "Natsionalnaya taksophonnaya set"	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**1,628**	2,116
OJSC Smolenskaya generiruyushaya kompaniya	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**450**	325
OJSC Smolenskenergosbyt	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**307**	–
OJSC Kostromskaya gorodskaya telefonnaya set	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**227**	524
CJSC TeleRoss-Voronej	Associate Company	Telecommunications Services	Arms' length terms	**196**	466
OJSC Giprosvyaz	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**54**	–
OJSC Uralsvyazinform	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**52**	96
OJSC Smolenskaya GRES	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**30**	46
OJSC North-West Telecom	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**20**	102
OJSC VolgaTelecom	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**1**	38
CJSC Mobile Telecommunications	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**–**	50
Total:				**1,271,911**	1,216,096

(in thousands of roubles)

35. Balances and Transactions with Related Parties (continued)

Purchases

During the year ended December 31, 2005 and 2004 the following related parties rendered significant amount of services to the Company:

Related party	Relationship	Type of purchases	Price determination method	2005	2004
OJSC "Rostelecom	Controlled by OJSC "Svyazinvest"	Services of traffic transmission	Calculated rates and tariffs, regulated by MAP	**3,116,236**	3,130,662
NPF Telecom Soyuz	Controlled by OJSC "Svyazinvest"	Pension plans	Arms' length terms	**283,000**	96,318
Non-commercial partnership "Center for Research of Problems in Development of Telecommunications"	Controlled by OJSC "Svyazinvest"	Membership fees, agent agreement	Arms' length terms	**215,706**	322,917
OJSC Giprosvyaz	Controlled by OJSC "Svyazinvest"	Design works	Arms' length terms	**32,178**	67,032
CJSC Medexpress	Controlled by OJSC "Svyazinvest"	Voluntary health insurance	Arms' length terms	**17,773**	24,675
OJSC Kostromskaya gorodskaya telefonnaya set	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**16,686**	11,811
CJSC Nauchno-tehnicheskii tsentr KOMSET	Controlled by OJSC "Svyazinvest"	Equipment supply	Arms' length terms	**14,600**	26,010
OJSC MGTS	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**11,027**	5,544
OJSC Smolenskenergosbyt	Controlled by OJSC "Svyazinvest"	Electricity	Arms' length terms	**6,523**	5,567
CJSC COSTARS	Associate Company	Medical insurance	Arms' length terms	**5,383**	2,817
OJSC Link Bank	Controlled by OJSC "Svyazinvest"	Credit organisations services	Arms' length terms	**2,672**	2,315
OJSC AKB Svyaz-Bank	Controlled by OJSC "Svyazinvest"	Credit organizations services, agent agreement	Arms' length terms	**2,444**	50,080
OJSC Investitsionnaya Kompaniya Svyazi	Associate Company	Interest on loans	Arms' length terms	**2,171**	7,731
OJSC Smolenskaya generiruyushaya kompaniya	Controlled by OJSC "Svyazinvest"	Heating	Arms' length terms	**1,353**	1,519
CJSC RusLeasingSvyaz	Controlled by OJSC "Svyazinvest"	Equipment supply	Arms' length terms	**659**	29,827
OJSC Moskovskaya mejdugorodnaya telefonnaya stanziya #9	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**583**	600
OJSC Central Telegraph	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**220**	310
CJSC TeleRoss-Voronej	Associate Company	Telecommunications Services	Arms' length terms	**89**	178
OJSC "Natsionalnaya taksophonnaya set"	Controlled by OJSC "Svyazinvest"	Equipment supply	Arms' length terms	**74**	17,830
CJSC Belgorodskaya Sotovaya Svyaz	Associate Company	Telecommunications Services	Arms' length terms	**18**	3
OJSC Uralsvyazinform	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**12**	27
OJSC North-West Telecom	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**9**	36
OJSC VolgaTelecom	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**2**	14
OJSC Telecommunications Company Rinfotels	Associate Company	Telecommunications Services	Arms' length terms	**–**	283
CJSC Mobile Telecommunications	Controlled by OJSC "Svyazinvest"	Telecommunications Services	Arms' length terms	**–**	281
Total				**3,729,418**	3,804,387

(in thousands of roubles)

35. Balances and Transactions with Related Parties (continued)

Settlements with Related Parties

Accounts Receivable

As of December 31, 2005 and 2004 significant balances of accounts receivable with related parties were as follows:

Related party	Relationship	Type of receivables	2005	2004
Non-commercial partnership "Center for Research of Problems in Development of Telecommunications"	Controlled by OJSC "Svyazinvest"	Membership fees, agent agreement	**105,513**	52,608
OJSC AKB Svyaz-Bank	Controlled by OJSC "Svyazinvest"	Telecommunication services, agent agreement	**64,600**	58,207
CJSC Smolenskaya Sotovaya Svyaz	Associate Company	Telecommunication services	**4,738**	786
OJSC Central Telegraph	Controlled by OJSC "Svyazinvest"	Telecommunication services	**4,020**	5,719
OJSC Giprosvyaz	Controlled by OJSC "Svyazinvest"	Design works	**2,957**	21,042
CJSC RusLeasingSvyaz	Controlled by OJSC "Svyazinvest"	Equipment supply	**2,311**	–
CJSC Belgorodskaya Sotovaya Svyaz	Associate Company	Telecommunication services	**1,693**	2,058
OJSC "Natsionalnaya taksophonnaya set"	Controlled by OJSC "Svyazinvest"	Equipment supply	**1,035**	2,211
OJSC MGTS	Controlled by OJSC "Svyazinvest"	Telecommunication services	**529**	239
OJSC Telecommunications Company Rinfotels	Associate Company	Telecommunication services, rent of premises	**475**	437
OJSC Kostromskaya gorodskaya telefonnaya set	Controlled by OJSC "Svyazinvest"	Telecommunication services	**24**	79
OJSC North-West Telecom	Controlled by OJSC "Svyazinvest"	Telecommunication services	**1**	2
CJSC Nauchno-tehnicheskii tsentr KOMSET	Controlled by OJSC "Svyazinvest"	Equipment supply	**–**	7,936
OJSC VolgaTelecom	Controlled by OJSC "Svyazinvest"	Telecommunication services	**–**	350
Total:			**187,896**	151,674

(in thousands of roubles)

35. Balances and Transactions with Related Parties (continued)

Accounts Payable:

As of December 31, 2005 and 2004 significant balances of accounts payable with related parties were as follows:

Related party	Relationship	Type of payables	2005	2004
OJSC Svyazinvest	Parent company	Interest on loans	–	29,622
OJSC "Rostelecom	Controlled by OJSC "Svyazinvest"	Services of traffic transmission	**190,533**	191,544
CJSC RusLeasingSvyaz	Controlled by OJSC "Svyazinvest"	Equipment supply	**20,276**	12,293
OJSC MGTS	Controlled by OJSC "Svyazinvest"	Telecommunication services	**505**	258
OJSC Link Bank	Controlled by OJSC "Svyazinvest"	Credit organisations services	**219**	193
OJSC "Natsionalnaya taksophonnaya set"	Controlled by OJSC "Svyazinvest"	Telecommunication services, agent agreement	**143**	1,399
OJSC Kostromskaya gorodskaya telefonnaya set	Controlled by OJSC "Svyazinvest"	Telecommunication services	**57**	910
OJSC Moskovskaya mejdugorodnaya telefonnaya stanziya #9	Controlled by OJSC "Svyazinvest"	Maintenance of equipment	**57**	56
OJSC Central Telegraph	Controlled by OJSC "Svyazinvest"	Telecommunication services	**33**	33
OJSC AKB Svyaz-Bank	Controlled by OJSC "Svyazinvest"	Credit organisations services	**14**	11
OJSC Smolenskenergosbyt	Controlled by OJSC "Svyazinvest"	Other services	**12**	–
OJSC Smolenskaya generiruyushaya kompaniya	Controlled by OJSC "Svyazinvest"	Other services	**7**	8
OJSC Uralsvyazinform	Controlled by OJSC "Svyazinvest"	Telecommunication services	**4**	1
NPF Telecom Soyuz	Controlled by OJSC "Svyazinvest"	Pennsion plans	–	33,460
OJSC Giprosvyaz	Controlled by OJSC "Svyazinvest"	Design works	–	14,585
CJSC Nauchno-tehnicheskii tsentr KOMSET	Controlled by OJSC "Svyazinvest"	Equipment supply	–	14,403
OJSC North-West Telecom	Controlled by OJSC "Svyazinvest"	Telecommunication services	–	2
CJSC Mobile Telecommunications	Controlled by OJSC "Svyazinvest"	Telecommunication services	–	1
Total:	-	-	**211,860**	298,779

(in thousands of roubles)

35. Balances and Transactions with Related Parties (continued)

OJSC Svyazinvest

The Company's parent entity - OJSC "Svyazinvest" - was wholly owned by the Russian Government until July 1997 when the Government sold 25% plus one share of the Charter Capital of OJSC "Svyazinvest" to the private sector.

An effectively operating telecommunications and data transmission facility is of great importance to Russia for various reasons including economic, strategic and national security considerations. Consequently, the Government has and may be expected to continue to exercise significant influence over the operations of OJSC "Svyazinvest" and its subsidiary companies.

The Government's influence is not confined to its share holdings in OJSC "Svyazinvest". It has general authority to regulate tariffs, including domestic long distance tariffs. In addition, the Ministry of Information Technologies and Communications of the Russian Federation has control over the licensing of providers of telecommunications services.

As of December 31, 2004 the Company had loans payable to OJSC "Svyazinvest" which were fully repaid in 2005 (ref. to Note 19).

	2005	**2004**
Loans from Svyazinvest as of January 1	**29,622**	30,361
Accrual during 2005	**2,171**	7,731
Repayment during 2005	**(31,793)**	(8,470)
Loans from Svyazinvest as of December 31	**–**	**29,622**

Loans were obtained on commercial terms. The total of interest accrued in 2005 equalled 2,171 (in 2004 – 4,640).

OJSC Rostelecom

OJSC "Rostelecom", a majority owned subsidiary of OJSC "Svyazinvest", is the primary provider of domestic long distance and international telecommunications services in the Russian Federation. The annual expense associated with traffic carried by OJSC "Rostelecom" and terminated outside of the Company's network is stated as interconnection charges. The above mentioned expenses are included in expenses, relating to assurance of international and long-distance traffic transmission. Further, OJSC "Rostelecom" uses the Company's network to provide incoming long-distance and international traffic to its subscribers and partner operators.

(in thousands of roubles)

35. Balances and Transactions with Related Parties (continued)

OJSC Rostelecom (continued)

Transactions undertaken by the Company with OJSC "Rostelecom" reported in the accompanying consolidated financial statements as at December 31, 2005 and 2004 and for the years then ended equalled:

	2005	**2004**
Expenses on traffic transmission and rent of channels of OJSC "Rostelecom"	**(3,116,236)**	(3,130,662)
Revenue from OJSC "Rostelecom"	**1,183,894**	1,176,272
Accounts payable to OJSC "Rostelecom" as of December 31	**190,533**	191,543
Accounts receivable from OJSC "Rostelecom" as of December 31	**–**	–
Expenses on accrual of bad debt reserve from OJSC "Rostelecom" for the year ended December 31	**(356)**	(362)
Bad debt reserve OJSC "Rostelecom" for the year ended December 31	**716**	362

Transactions with Government Organizations

Government organizations are a significant element in the Company's customer base, purchasing services both directly through numerous authorities and indirectly through their affiliates. Certain entities financed by the Government budget are users of the Company's network. These entities generally rent network channels and are charged lower tariffs as approved by the Federal Antimonopoly Agency than those charged to other customers. In addition, the Government may by law require the Company to provide certain services to the Government in connection with national security and the detection of crime.

Government subscribers accounted for approximately 49 % of gross trade accounts receivable as of December 31, 2005 (2004 – 52%). Amounts outstanding from government subscribers as of December 31, 2005 amounted to 1,980,488 (2004 – 2,110,380)

Non-Commercial Partnership Centre for Research of Problems in Development of Telecommunications

Non-commercial partnership Centre for Research of the Problems in Development of Telecommunications (hereinafter "the Partnership") is an entity OJSC "Svyazinvest" controls through its subsidiaries. The Company has an agreement with the Partnership, under which it provides funding for industry research and common administrative activities on behalf of the Company and other subsidiary and associates of OJSC "Svyazinvest". Payments to the Partnership included in other operating expenses in the accompanying consolidated statement of operations for the year ended December 31, 2005 amounted to 215,801 (2004 – 296,677).

NPF Telecom-Soyuz

In 2005 the Company signed several pension agreements with NPF Telecom-Soyuz (see Note 24 "Pension Obligations"). OJSC "Svyazinvest" holds the majority in the Board of Directors of NPF Telecom-Soyuz ("the Fund"). Payments from the Company to the Fund in 2005 amounted to 316,460 (2004 – 62,858).

Compensation to Key Management Personnel

Key management personnel comprise members of the Management Board, the Board of Directors, and Revision Committee of the Company. Total compensation to key management personnel included in "Wages, salaries, other employee benefits and payroll taxes" in the statement of operations amounted to 51,755 and 57,124 for the years ended December 31, 2005 and 2004, respectively, and consists of remuneration for management services.

36. Financial Instruments

Foreign Exchange Risk

Foreign exchange risk is the risk that fluctuations in exchange rates will adversely affect items in the Company's statement of operations, balance sheet and/or cash flows. Foreign currency denominated liabilities (see Notes 19 and 20) give rise to foreign exchange exposure.

The Company does not have arrangements to mitigate foreign exchange risks of the Company's operations.

The Central Bank of Russia set up strict rules referring to regulation of transactions in foreign currency with the purpose of stimulation of commercial use of Rouble. This regulation previews restrictions of rouble conversion into hard currency and presents guidelines for conversion of revenue in hard currency into roubles.

As a rule, the company faces foreign exchange risk in respect of liabilities stated in a foreign currency. As at December 31, 2005 Company's liabilities in foreign currency were 1,422,541 (2004 – 2,808,020), including liabilities denominated in US dollars 615,141 (2004 – 1,603,177) and Euro and other currencies 807,401 (2004 – 1,204,843).

For the period from January 1, 2005 to December 31, 2005 exchange rate of the Russian Rouble to US Dollar decreased by approximately 4% and exchange rate of the Russian Rouble to Euro increased by approximately 9%.

(in thousands of roubles)

36. Financial Instruments (continued)

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates may negatively impact the Company's financial results.

The following table presents as of December 31, 2005 and 2004 the carrying amount by maturity of the Company's financial instruments that are exposed to interest rate risk:

	< 1 year	1–5 years	> 5 years	Total
As of December 31,2005:				
Fixed rate				
Short-term obligations	**2,186,531**	**–**	**–**	**2,186,531**
Long-term obligations	**12,184,047**	**6,741,600**	**73,110**	**18,998,757**
Finance lease obligations	**743,000**	**1,562,302**	**–**	**2,305,302**
Loans given	**11,013**	**20,034**	**–**	**31,047**
Short-term deposits	**2,200**	**–**	**–**	**2,200**
Floating rate	**–**	**–**	**–**	**–**
Short-term obligations	**77,233**	**–**	**–**	**77,233**
Long-term obligations	**386,292**	**9,820**	**–**	**396,112**

As of December 31,2004:	**< 1 year**	**1–5 years**	**> 5 years**	**Total**
Fixed rate				
Short-term obligations	3,512,552	–	–	3,512,552
Long-term obligations	3,336,405	12,741,886	101,130	16,179,421
Finance lease obligations	672,491	1,775,171	–	2,447,662
Loans given	28,924	24,311	–	53,235
Short-term deposits	628	–	–	628
Floating rate				
Short-term obligations	91,845	–	–	91,845
Long-term obligations	527,627	160,769	–	688,396

Interest on financial instruments classified as fixed rate is fixed until maturity of the instrument. The other financial instruments of the Company that are not included into the above tables are non-interest bearing and are therefore not subject to interest rate risk.

The Company has no other significant interest-bearing assets, except the assets stated in the table above.

36. Financial Instruments (continued)

Credit Risk

Credit risk is the risk that a counter-party will fail to discharge an obligation and cause the Company to incur a financial loss.

Financial assets, which are potentially subject to credit risk, consist principally of trade receivables. The carrying amount of accounts receivable, net of provision for impairment of receivables, represents the maximum amount exposed to credit risk. The Company has no significant concentrations of credit risk due to significance of the client base and regular monitoring procedures over customers' and other debtors' ability to pay debts. A part of accounts receivable is represented by state and other non-commercial organizations. Recovery of this debt is influenced by political and economic factors, however, management believes that as of December 31, 2005 there is no significant risk of loss to the Company beyond the provision already recorded.

Financial instruments that can potentially lead to concentration of credit risk are mainly presented by trade receivables and other trade receivables. Credit risk, relating to these assets, is unlimited due significance of client base and regular monitoring procedures over customers' and other debtors' ability to pay debts. To manage credit risk the Company places cash in different financial institutions, and the Company's management analyzes risk of default of these financial institutions on a regular basis.

Fair Value

Fair value of a financial instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction (except for forced sale or liquidation). Market prices are considered to be the best evidence of fair value.

Management believes that the carrying values of monetary assets and liabilities approximate their fair values. Balance sheet items denominated in foreign currency have been translated into Roubles using the corresponding exchange rate prevailing at the reporting date.

Carrying value of cash and cash equivalents approximate their fair value due to their short-term character and minimal credit risks.

(in thousands of roubles)

36. Financial Instruments (continued)

Fair Value (continued)

Set out below is the comparison by category of carrying amounts and fair values of all of the Company's financial instruments:

	2005		2004	
Financial instruments	**Carrying amount**	**Fair value**	**Carrying amount**	**Fair value**
Financial Assets				
Investments in associates	**20,081**	**20,081**	15,927	15,927
Long-term investments available for sale	**25,621**	**25,621**	13,662	13,662
Long-term accounts receivable	**221,546**	**221,546**	3,308	3,308
Long-term borrowings given	**20,197**	**20,197**	18,442	18,442
Accounts receivable	**1,877,457**	**1,877,457**	2,068,164	2,068,164
Cash and cash equivalents	**994,627**	**994,627**	1,417,214	1,417,214
Total	**3,159,529**	**3,159,529**	3,536,717	3,536,717
Financial Liabilities				
Long-term bank loans	**4,539,723**	**4,539,723**	4,302,010	4,302,010
Long-term bonds	**20,089**	**20,089**	7,544,187	7,544,187
Long-term promissory notes	**2,208,681**	**2,208,681**	669,928	669,928
Long-term suppliers' credits	**56,036**	**56,036**	487,659	487,659
Long-term finance lease obligations	**1,562,302**	**1,562,302**	1,775,171	1,775,171
Accounts payable	**2,186,986**	**2,186,986**	3,020,036	3,020,036
Short-term bank loans	**1,670,591**	**1,670,591**	1,810,684	1,810,684
Short-term bonds	**428,769**	**428,769**	378,504	378,504
Short-term promissory notes	**163,859**	**163,859**	1,393,764	1,393,764
Short-term suppliers' credits	**545**	**545**	21,445	21,445
Current portion of long-term bank loans	**2,416,479**	**2,416,479**	2,391,177	2,391,177
Current portion of long-term bonds	**7,516,779**	**7,516,779**	601,314	601,314
Current portion of long-term promissory notes	**2,186,348**	**2,186,348**	–	–
Current portion of long-term suppliers' credits	**450,732**	**450,732**	871,541	871,541
Current portion of long-term finance lease obligations	**743,000**	**743,000**	672,491	672,491
Total	**26,150,919**	**26,150,919**	25,939,911	25,939,911

37. Subsequent Events

New provisions of the Federal Law on Communications

The legislative framework for the reform of the Russian telecommunications industry is the Federal Law on Communications of 2004. To implement the Federal Law on Communications, the Russian Government approved new rules and regulations for the interconnection and interaction of telecommunications networks, for the provision of local, intra-regional, DLD, and ILD telephone services, and other regulations for the provision of long-distance services, including licensing requirements for telecommunications operators. The transition to the new system of interaction on January 1, 2006 stems from these new requirements under Russian legislation.

New regulations required in pursuance of the Federal Law on Communications come into force starting January 1, 2006:

1. Decision of the government of the Russian federation no. 161 of March 28, 2005 on endorsing the Rules for connecting electric communication networks and for their interaction (with Amendments and Addenda of June 30, December 29, 2005)
2. Decision of the government of the Russian federation no. 310 of May 18, 2005 on the approval of Rules for Rendering Services of Local, Intra-Zone, Inter-City and International Telephone Communication (approved by Decision of the Government of the Russian Federation No. 310 of May 18, 2005) (with the Amendments and Additions of June 30, December 29, 2005).
3. Decision of the government of the Russian federation no. 241 of April 21, 2005 on the approval of the Rules for state regulation of tariffs on universal communications services (with the amendments and additions of October 24, 2005)
4. Order of the Ministry of Communications no. 97 of August 8, 2005 on Approval of the requirements to public switched telephone networks.
5. Order of the Ministry of Communications no. 98 of August 8, 2005 on Approval of the requirements to traffic transmission in public switched telephone networks.

Changes in Settlements with Rostelecom in 2006

Prior to January 1, 2006 the Company, in accordance with the previously given Addendum #1 to License #24064 for local telecommunication services dated 24.10.2002, rendered domestic long-distance (DLD) and international long-distance (ILD) services (“long-distance services”) to its customers. Revenues and receivables from rendering of the services were recognized as the Company’s revenues and receivables.

Under the previous system of interaction with operators, Rostelecom provided long-distance traffic transit services to the Company. The Company independently billed for long-distance services provided to its local network subscribers through its own subscriber billing systems. The Company settled with Rostelecom for long-distance call transit and termination services, and Rostelecom, in turn, paid the Company for call termination services. The Company performed settlements for international telecommunications services with subscribers by tariffs, set by Rostelecom, and settlements for intercity telecommunications services by tariffs, set by the Federal Antimonopoly Agency.

Starting from 2006 the settlements between the Company and Rostelecom change. Domestic long-distance (DLD) and international long-distance (ILD) services will be rendered by Rostelecom. Revenues and receivables from rendering of the services will be recognized as Rostelecom revenues and receivables.

37. Subsequent Events (continued)

Changes in Settlements with Rostelecom in 2006 (continued)

The Company and Rostelecom signed an agreement for the year 2006 combining elements as of an agency agreement as well as of a service contract, according to which the Company undertakes rendering the following services to Rostelecom:

- Subscriber orders' processing services for access to intercity and international telecommunications services provided through the direct and delay operations.
- Billing processing services for intercity and international telecommunications services.
- Preparation, formation and storage of necessary data and reports;
- Agency services on collection of payments from subscribers and on call centre support in the name and on behalf of Rostelecom.
- Claims administration, documents delivery.

In addition to the above mentioned contract the parties signed the agreement on network interconnections, under which the Company provides Rostelecom the services on traffic transmission and Rostelecom provides the Company connection services.

To comply with the new regulatory requirements, the Company must fulfil a number of conditions, including:

- technical conformity of its network to requirements set for DLD and ILD communication networks, including availability of interconnection points to its network in every federal administrative region of the Russian Federation; and
- operational readiness to provide long-distance services to any local network subscriber.

Changes in settlements with interconnected operators

New legislative pronouncements effective January 1, 2006 significantly changed the scheme of settlements with interconnected operators.

Prior to January 1, 2006 settlements for interconnection services with the operators for local telephone services were of unilateral nature, and for intra-regional, DLD, and ILD telephone services interconnected operators received a part of the revenues from such services depending on the degree of their participation in the provision of a service.

Starting from January 1, 2006 settlements are of a mutual nature and consist of the following:

- point of connection set up;
- user fee for point of connection;
- fee per minute of traffic submitted through the network.

The changes will result in additional revenues from interconnection and traffic transmission as well as in additional costs related to payments to these operators for connection points set up, user fee and traffic transmission in the operators' network.

In order to meet the above mentioned requirements the Company will incur additional capital expenditure to the amount of 434,304.

As of the beginning of April, 2006 the Company signed agreements of interconnection and traffic transmission with OJSC Rostelecom and OJSC Multiregional Transit-Telecom.

37. Subsequent Events (continued)

Changes in Settlements with Interconnected Operators (continued)

Currently the Company is undertaking the necessary renegotiation procedures with interconnection operators. The Company expects to finalize these procedures in July 2006.

Interconnection services are currently included into services regulated by the Government. As a consequence the interconnection fee, including the profitability level, is to be prescribed by the regulating body.

Significant Operator

In accordance with the Order of the Federal Service for Communications Supervision (Rossvyaznadzor) no. 39 on October 21, 2005, no. 40 and 31 on October 24, 2005 and no. 52 on December 22, 2005 the Company is included into the Register of Communications services operators an important position in the general-use communications network (Significant Operator).

An operator occupying an important position in the general-use communications network, is obliged to establish, for the purposes of ensuring indiscriminate access to the market of communications services under similar circumstances, equal conditions for connecting telecommunications networks and for letting through traffic for communications operators rendering similar services, as well as to supply information and to render connection services and the services involved in letting through the traffic to these operators under the same terms and of the same standard, like for his own structural subdivisions and/or for the affiliated persons.

An operator occupying an important position in the general-use communications network on the territories of several subjects of the Russian Federation shall establish the terms for connecting telecommunications networks and for letting through traffic separately on the territory of each subject of the Russian Federation.

The refusal of an operator occupying an important position in the general-use communications network to conclude a contract for connecting telecommunications networks is seen as inadmissible, with the exception of cases when the connection of the telecommunications networks and their interaction contradict the terms of the licenses issued to communications operators, or the legal normative acts determining the construction and the functioning of the uniform telecommunications network of the Russian Federation.

Prices for connection services and for services involved in letting through traffic rendered by operators occupying an important place in the general-use communications network are subject to state regulation. The list of connection services and services for letting through the traffic, the prices for which are subject to state regulation, as well as the procedure for their regulation, are established by the Government of the Russian Federation.

Rendering of Universal Telecommunication Service

Universal communication service is the communication service whose rendering to any user of communication service on the entire territory of the Russian Federation within a fixed term, of the established standard and at a reasonable price is obligatory for operators of the universal service. This service is to be rendered by operators of universal servicing who are selected in accordance with the results of a tender or are appointed in accordance with the Federal Law for every subject of the Russian Federation.

On March 24, 2006 the Company won tenders for provision of telecommunication services by the use of payphones in all (11) lots on the territory of Tula region and in all (6) lots on the territory of Belgorod region. The tenders, along with other, were announced on March 24, 2005.

37. Subsequent Events (continued)

Rendering of Universal Telecommunication Service (continued)

The agreements "On conditions of rendering universal telecommunications services by the use of payphones" for each lot were presented to the Federal communications agency on April 12, 2006.

The Company indicated the date of start of rendering services it the tender document pack of the as January 2007, since required capital investments will be included in the business plan of the next year.

In the Tula region 2,162 coin-box telephones are to be installed in all centres of population, which will require investments at the amount of 980 mln roubles. The total amount of annual compensation of losses, in accordance with the decision of tender committee will be 221,9 mln roubles.

In the Belgorod region 1,240 coin-box telephones are to be installed, and investments are estimated to be 219,5 mln roubles. The total amount of annual compensation of losses will be 130,75 mln roubles.

Cancellation of Charges for Incoming Calls

In March 2006 an amendment to the Federal Law on Communication was approved by the President of RF. According to this amendment effective July 1, 2006 the subscriber will not pay for a telephone connection established as a result of a call by another subscriber, except for the cases specifically mentioned in the Federal Law on Communication.

This change would mainly affect the settlements between the Company and mobile network operators.

Starting from the enforcement of this amendment the Federal Service on Tariffs will set tariffs for intra-regional services between the Company as a significant operator and mobile network operators. Subsequent to that the Company would renegotiate the agreements with these operators.

The Company envisages increase in revenues from intra-regional services in the second half of 2006 and increase in costs related to calls termination on mobile networks.

Tariffs for Telecommunication Services

Under Decree of the Government of the Russian Federation # 627 dated October 19, 2005 settlement rates (including rates for call origination, termination, and transit) for operators occupying a significant position in the public communications network (significant operators) are regulated by the Federal Service for Communications Supervision (Rossvyaznadzor) under the supervision of the Federal Tariff Service (FST) in accordance with the Federal Law on Natural Monopolies.

In November 18, 2005 the Company submitted its proposed tariffs (circular #10-03-06/8252) to Rossvyaznadzor for approval. Owing to the absence of unified methodology on determination of economically justifiable costs and standard profit for the connection services and services of traffic transmission and absence of the order of addressing and consideration of requests of operators the tariffs were not approved by the supervising body.

In December 20, 2005 the Federal Service for Communications Supervision determined the amount of the compensation surcharge to be included in rates for call origination services provided by the Company as a significant operator. The surcharge is set at 0.62 Roubles per minute and is effective starting January 1, 2006. The compensation surcharge is supposed to cover the difference between an operator's income and economically justified costs in providing local and intra-regional communication services.

37. Subsequent Events (continued)

Tariffs for Telecommunication Services (continued)

The following changes of tariffs for local connection are expected to be established in 2006:

- residents - 118%
- organizations – 113%
- for intra-regional communication services – 95%.

Impact of new Rules for Rendering of Telecommunication Services on Financial Statements 2006

The Company's management expects that new rules of provision of telecommunication services will influence both revenues and expenses of the Company, however, the Company cannot reliably measure the effect of such changes on the financial position and financial results of the Company.

Value Added Tax

Federal Law No. 119-FZ dated July 22, 2005, introduced amendments to the Tax Code effective January 1, 2006. According to these amended provisions VAT taxable base on sales of goods (rendering of services) is determined at the earliest of:

- date of goods (services) shipment (rendering);
- date of payment (partial payment) for subsequent delivery of goods (services), transfer of rights of ownership.

Sale of share in CJSC "Smolenskaya sotovaya svyaz", CJSC "Belgordskaya sotovaya svyaz" and CJSC "Lipetsk Mobile"

In February 2006 the Company sold 2,349,200 ordinary shares (40 % of equity interest) of CJSC "Smolenskaya sotovaya svyaz" for 11,390 (400,000 US dollars). The sell was approved by the Board of Directors decision dated December 27, 2005.
In February 2006 the Company sold 30,000 ordinary shares (30 % of equity interest) of CJSC "Belgordskaya sotovaya svyaz" for 10,251 (360,000 US dollars). The sell was approved by the Board of Directors decision dated December 27, 2005.
In February 2006 the Company sold 102,017 ordinary shares (5.9 % of equity interest) of CJSC "Lipetsk Mobile" for 712 (25,000 US dollars). The sell was approved by the Board of Directors decision dated December 27, 2005.

Agreement with Non-Commercial Partnership

In June 2006 the Company's Board of Directors has approves membership's fees to Non-Commercial Partnership Center for Research of the Problems in Development of Telecommunications in the amount of 184,624.

(in thousands of roubles)

37. Subsequent Events (continued)

Dividends

The Board of Directors of the Company proposed the following distribution of profits to the Annual Shareholders' meeting to be held on June 28, 2006:

Dividends for 2005 Proposed for Approval

Dividends on ordinary shares – 0.0674191 Roubles per share	66,850
Dividends on preference shares – 0.1270937 Roubles per share	106,388
Total	**173,238**

Employee Redundancy Program

In accordance with the Employee Redundancy Program for 2006-2008 approved by the Company's Board of Directors, the Company dismissed 742 employees paying compensations totalling 10,315 between December 31, 2005 and the date of the authorisation of the financial statements for the issues.

Bonds Issue

On April 20, 2006 the Board of Directors approved the issue of 3,000,000 interest-bearing bonds, series 05, with par value of 1 each. The bonds have 10 semiannually coupons. Coupon payments are made on each 182nd day starting from the date of placement. The interest rate will be determined based on tender that will be held as at the date of placement. The bonds mature as follows: 10% of par value on 1,274th day, 20% of par value on 1,456th day, 30% of par value on 1,638th day and 40% of par value on 1,820nd day starting from the date of issue.