OAO "North-West Telecom"

Consolidated Financial Statements

Year ended December 31, 2006
with Report of Independent Auditors

OAO "North-West Telecom"

Consolidated Financial Statements

For the year ended December 31, 2006

Contents

Independent Auditors’ Report

To the Shareholders and Board of Directors of OAO “North-West Telecom”

We have audited the accompanying consolidated financial statements of OAO “North-West Telecom” and its subsidiaries (“the Company”), which comprise the consolidated balance sheet as at December 31, 2006, and the consolidated income statement, consolidated cash flow statement and consolidated statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management’s Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors’ Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors’ judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC

July 16, 2007

OAO "North-West Telecom"
Consolidated Balance Sheet
as of December 31, 2006

(in thousands Rubles)

	Notes	2006	2005, as restated *(see Note 2)*
ASSETS			
Non-current assets			
Property, plant and equipment, net	6	**28,009,688**	26,642,873
Intangible assets and goodwill, net	7	**2,863,953**	1,832,433
Investments in associates	10	**98,192**	94,655
Long-term investments	11	**10,239,203**	7,947,455
Long-term receivables and other financial assets	12	**203,419**	209,656
Long-term advances given	13	**627,317**	389,085
Total non-current assets		**42,041,772**	37,116,157
Current assets			
Inventories	14	**308,250**	300,092
Accounts receivable, net	15	**1,336,905**	1,181,806
Short-term investments	11	**-**	1,042,626
Other current assets	16	**1,029,502**	1,240,722
Cash and cash equivalents	17	**244,491**	152,091
Total current assets		**2,919,148**	3,917,337
TOTAL ASSETS		**44,960,920**	41,033,494
SHAREHOLDERS' EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Preference shares	19	**621,739**	621,739
Ordinary shares	19	**2,233,765**	2,233,765
Treasury shares	19	**(66,667)**	(56,681)
Unrealized gain on available-for-sale investments		**7,295,093**	5,547,430
Additional paid in capital, retained earnings and other reserves		**16,334,487**	15,435,911
Total equity attributable to equity holders of the parent		**26,418,417**	23,782,164
Minority interest		**-**	8,515
Total shareholders' equity		**26,418,417**	23,790,679
Non-current liabilities			
Long-term borrowings	20	**7,577,611**	8,177,438
Long-term finance lease obligations	21	**136,733**	302,121
Pension liabilities and other long-term benefits	24	**1,636,631**	1,301,953
Deferred revenue		**321,934**	304,857
Deferred income tax liability	29	**3,765,230**	3,108,668
Other non-current liabilities		**2,229**	-
Total non-current liabilities		**13,440,368**	13,195,037
Current liabilities			
Accounts payable, accrued expenses and advances received	22	**2,167,371**	1,614,461
Payables to OAO Rostelecom	35	**421,361**	146,282
Taxes payable	23	**307,215**	694,236
Dividends payable		**17,320**	15,936
Short-term borrowings	20	**81,531**	595,678
Current portion of long-term borrowings	20	**1,937,448**	791,969
Current portion of long-term finance lease obligations	21	**169,889**	189,216
Total current liabilities		**5,102,135**	4,047,778
Total liabilities		**18,542,503**	17,242,815
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		**44,960,920**	41,033,494

General Director ____________ V.A. Akulich   Chief Accountant ___________ M.M. Semchenko

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

OAO "North-West Telecom"

Consolidated Income Statement

For the year ended December 31, 2006

(in thousands Rubles)

	Notes	2006	2005
Revenues	**25**	**20,649,827**	20,541,914
Wages, salaries, other employee benefits and payroll taxes		**(7,094,425)**	(7,323,084)
Impairment of property, plant and equipment, construction in progress and intangible assets	**7**	**-**	(16,559)
Depreciation and amortization	**6, 7**	**(3,774,353)**	(3,024,865)
Materials, repairs and maintenance, utilities		**(2,499,826)**	(2,052,030)
Taxes other than income tax		**(511,198)**	(435,969)
Services of telecommunication operators		**(1,469,395)**	(3,541,880)
Reversal of provision for impairment of receivables	**15**	**191,429**	362,428
Loss on disposals of property, plant and equipment		**(90,370)**	(134,520)
Other operating expenses, net	**26**	**(2,517,569)**	(1,788,806)
Total operating expenses		**(17,765,707)**	(17,955,285)
Operating income		**2,884,120**	2,586,629
Share in result of associates, net	**10**	**986**	9,673
Interest expense, net	**27**	**(688,250)**	(595,154)
Loss from disposal of investments, net	**28**	**(8,189)**	(4,520)
Foreign exchange loss, net		**(15,470)**	(7,960)
Profit before income tax		**2,173,197**	1,988,668
Income tax	**29**	**(902,591)**	(577,801)
Profit for the year		**1,270,606**	1,410,867
Profit for the year attributable to equity holders of the parent		**1,270,580**	1,411,648
Profit (loss) for the year attributable to minority holders of subsidiaries		**26**	(781)
Basic and diluted earnings per share (Rubles) for profit for the year attributable to equity holders of the parent	**30**	**1.13**	1.25

General Director ___________ V.A. Akulich   Chief Accountant __________ M.M. Semchenko

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

OAO "North-West Telecom"
Consolidated Cash Flow Statement
For the year ended December 31, 2006
(in thousands Rubles)

	Notes	2006	2005, as restated (see Note 2)
Cash flows from operating activities			
Profit before tax		**2,173,197**	1,988,668
Adjustment to reconcile income to cash provided by operating activities:			
Foreign exchange loss, net		**15,470**	7,960
Depreciation of property, plant and equipment	**6**	**3,518,914**	2,880,003
Amortization of intangible assets	**7**	**255,494**	144,862
Loss on disposal of property, plant and equipment and other assets		**90,370**	134,520
Share in result of associates	**10**	**(986)**	(9,673)
Loss from disposal of investments	**28**	**8,189**	4,520
Interest expense, net	**27**	**688,250**	595,154
Reversal of provision for impairment of receivables	**15**	**(191,429)**	(362,428)
Impairment of intangible assets	**7**	**-**	16,559
Movement in pension obligations	**24**	**334,678**	73,313
Other non-cash items		**24,523**	(12,302)
Operating profit before working capital change		**6,916,670**	5,461,156
Decrease in accounts receivable		**37,075**	355,920
Decrease in other current assets		**256,340**	294,918
Decrease (increase) in inventories		**(6,740)**	24,784
Increase in accounts payable and accrued expenses		**245,891**	117,656
Decrease in taxes other than income tax and social contributions payable		**(387,954)**	(115,759)
Increase in contingency provision		**9,665**	-
Cash flows generated from operations		**7,070,947**	6,138,675
Interest paid		**(818,282)**	(866,629)
Income tax paid		**(843,470)**	(1,061,421)
Net cash flows from operating activities		**5,409,195**	4,210,625
Cash flows from investing activities			
Purchase of property, plant and equipment and construction in progress		**(4,719,837)**	(5,717,015)
Purchase of intangible assets		**(935,625)**	(244,267)
Purchase and implementation of Oracle EBS		**(146,517)**	(207,849)
Purchase and implementation of Amdocs Billing Suite		**(140,498)**	(200,208)
Purchase of subsidiaries and minority interest, net of cash acquired		**2,651**	(73,357)
Purchase of investments and other financial assets		**(13,676)**	(1,214,104)
Disposal of investments and other financial assets		**1,051,811**	37,878
Proceeds from sale of property, plant and equipment and construction in progress		**149,346**	54,672
Loans given		**(27,967)**	(14,048)
Proceeds from repayment of loans given		**3,026**	11,781
Interest received		**59,199**	96,234
Dividend received		**4,618**	456
Net cash used in investing activities		**(4,713,469)**	(7,469,827)

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

OAO "North-West Telecom"

Consolidated Cash Flow Statement (continued)

	Notes	**2006**	**2005, as restated** *(see Note 2)*
Cash flows from financing activities			
Proceeds from issue of shares		**17,237**	22,355
Acquisition of treasury shares		**(32,179)**	(12,114)
Proceeds from borrowings		**7,970,314**	12,206,305
Repayment of borrowings		**(9,201,970)**	(10,883,919)
Proceeds from bond issue		**1,993,120**	3,061,627
Repayment of bonds		**(450,000)**	(61,627)
Repayment of finance lease obligations		**(218,445)**	(206,638)
Repayment of supplier credits		**(89,491)**	(187,138)
Repayment of promissory notes issued to acquire Amdocs Billing Suite		**(178,384)**	(443,348)
Repayment of promissory notes		**(16,514)**	-
Repayment of other non-current liabilities		**-**	(176)
Dividend paid		**(392,439)**	(337,922)
Net cash from (used in) financing activities		**(598,751)**	3,157,405
Effect of exchange gain (loss) on cash and cash equivalents		**(4,575)**	499
Increase (decrease) in cash and cash equivalents		**92,400**	(101,298)
Cash and cash equivalents at the beginning of year		**152,091**	253,389
Cash and cash equivalents at the end of year		**244,491**	152,091

General Director ____________ V.A. Akulich Chief Accountant ___________ M.M. Semchenko

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

OAO "North-West Telecom"

Consolidated Statement of Changes in Equity

For the year ended of December 31, 2006

(in thousands Rubles)

	Notes	Share capital: Preference shares	Share capital: Ordinary shares	Share capital: Treasury shares	Retained earnings and other reserves	Additional paid-in capital	Unrealized gain on available-for-sale investments	Total	Minority interests	Total equity
Balance at December 31, 2004	**2**	621,739	2,233,765	(60,822)	11,036,332	2,496,388	3,745,996	20,073,398	18,915	20,092,313
Effect of adjustments					824,861		71,552	896,413		896,413
Balance at December 31, 2004 (adjusted)		**621,739**	**2,233,765**	**(60,822)**	**11,861,193**	**2,496,388**	**3,817,548**	**20,969,811**	**18,915**	**20,988,726**
Unrealized gain on available-for-sale investments		-	-	-	-	-	1,686,960	1,686,960	-	1,686,960
Total income and expense for the year recognised directly in equity		**-**	**-**	**-**	**-**	**-**	**1,686,960**	**1,686,960**	**-**	**1,686,960**
Profit (loss) for the year		-	-	-	1,411,648	-	-	1,411,648	(781)	1,410,867
Total income and expense for the year		**-**	**-**	**-**	**1,411,648**	**-**	**1,686,960**	**3,098,608**	**(781)**	**3,097,827**
Dividends paid to equity holders of parent		-	-	-	(335,581)	-	-	(335,581)	-	(335,581)
Purchase of treasury shares		-	-	(12,114)	-	-	-	(12,114)	-	(12,114)
Sale of treasury shares		-	-	16,255	-	6,099	-	22,354	-	22,354
Acquisition of minority interests		-	-	-	(3,836)	-	-	(3,836)	(9,619)	(13,455)
Effect of adjustments		-	-	-	-	-	42,922	42,922	-	42,922
Balance at December 31, 2005 (adjusted)	**2**	**621,739**	**2,233,765**	**(56,681)**	**12,933,424**	**2,502,487**	**5,547,430**	**23,782,164**	**8,515**	**23,790,679**
Unrealized gain on available-for-sale investments		-	-	-	-	-	1,747,663	1,747,663	-	1,747,663
Total income and expense for the year recognised directly in equity		**-**	**-**	**-**	**-**	**-**	**1,747,663**	**1,747,663**	**-**	**1,747,663**
Profit (loss) for the year		-	-	-	1,270,580	-	-	1,270,580	26	1,270,606
Total income and expense for the year		**-**	**-**	**-**	**1,270,580**	**-**	**1,747,663**	**3,018,243**	**26**	**3,018,269**
Dividends paid to equity holders of parent	**31**	-	-	-	(393,825)	-	-	(393,825)	-	(393,825)
Purchase of treasury shares		-	-	(32,179)	-	-	-	(32,179)	-	(32,179)
Sale of treasury shares		-	-	22,193	-	22,536	-	44,729	-	44,729
Acquisition of minority interests		-	-	-	(715)	-	-	(715)	(8,541)	(9,256)
Balance at December 31, 2006		**621,739**	**2,233,765**	**(66,667)**	**13,809,464**	**2,525,023**	**7,295,093**	**26,418,417**	**-**	**26,418,417**

General Director ____________ V.A. Akulich Chief Accountant ___________ M.M. Semchenko

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

1. General Information

Authorization of Accounts

The consolidated financial statements of OAO North-West Telecom and its subsidiaries (hereinafter the "Company") for the year ended December 31, 2006 were authorized for issue by the General Director and the Chief Accountant of the Company on July 16, 2007.

The Company

OAO North-West Telecom is an open joint stock company incorporated in accordance with the laws of the Russian Federation.

The registered office of the Company is 14/26, Gorokhovaya Str., St. Petersburg, Russia.

The Company provides local and intra-regional telephony, telegraph, data transmission services, rent of communication channels and wireless communication services, and bills subscribers for national long-distance and international telephone calls for and on behalf of operators providing such national long-distance and international telephony services on a contractual basis in the North-West Region of the Russian Federation.

Open joint stock company Svyazinvest, a federal holding company controlled by the Russian Federation, owns 50.8% of the Company's voting shares and as of December 31, 2006.

The details of main subsidiaries are disclosed in Note 9. All subsidiaries are duly incorporated in accordance with the laws of the Russian Federation unless stated otherwise.

Presentation of Financial Statements

The consolidated financial statements of OAO North-West Telecom are prepared based on standalone financial statements of the parent and its subsidiaries and associates under unified accounting policies.

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

The consolidated financial statements of the Company are presented in thousands of Russian Rubles, unless stated otherwise.

Liquidity and Financial Resources

As of December 31, 2006 current liabilities of the Company exceeded its current assets by 2,182,987 (December 31, 2005: 130,441). The Company's profits before tax in 2006 and 2005 were 2,173,197 and 1,988,668 respectively. In this connection, a significant uncertainty exists as to the Company's ability to maintain liquidity and the availability of sufficient sources of financing.

In prior year, the Company raised borrowings, both short and long-term, to finance its telecommunication network development, primarily in the form of bank loans, bond issues, equipment supplier credits and capital leases.

Management believes that where necessary, some projects may be deferred or scaled down commensurate with the financing requirements for the Company's current operations.

1. General Information (continued)

Liquidity and Financial Resources (continued)

The Company has an action plan in place to maintain and improve current liquidity level and raise long-term debt to finance the 2007 investment program, including the refinancing of the existing short-term borrowings outstanding (improvement of the current ratio).

- Organization of a syndicated loan for the total amount of 100 000 thousand US Dollars (scheduled in the third quarter of 2007) to refinance short-term debt;
- Placement of the 5th bond issue for the total amount of 3 000 000 Rubles (scheduled in the fourth quarter of 2007) to refinance short-term debt;
- Funding of the 2007 investment program from long-term bank loans obtained under the existing loan facilities.

2. Basis of Presentation of the Financial Statements

Basis of Preparation

These consolidated financial statements have been prepared 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 closing balances, results of operations and cash flows in accordance with IFRS.

The accompanying financial statements have been presented on a going concern basis, which contemplates the realization of assets and the settlement 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 that might result should 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 operations.

The Company has transitioned to IFRS at January 1, 2003 using the provisions of IFRS 1 “First-time Adoption of International Financial Reporting Standards”.

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 at the date of transition even if the corridor approach is used for later actuarial gains and losses.

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

Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except that the Company has adopted those new/revised standards and interpretations mandatory for financial years beginning on or after January 1, 2006.

The changes in accounting policies result from adoption of the following new or amended standards and interpretations:

- IAS 19 (amended 2005) “Employee benefits”;
- IAS 21 (amended 2005) “The Effects of Changes in Foreign Exchange Rates”;
- IAS 39 (amended 2005) “Financial Instruments: Recognition and Measurement”;
- IFRIC 4 “Determining whether an Arrangement contains a Lease”;
- IFRIC 5 “Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds”.

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

IAS 19 (amended 2005) “Employee Benefits”

As of January 1, 2006, the Company adopted the amendments to IAS 19. As a result, additional disclosures are made providing information about trends in the assets and liabilities in the defined benefit plans and the assumptions underlying the components of the defined benefit cost. This change has resulted in additional disclosures being included for the years ending December 31, 2006 and December 31, 2005 but has not had a recognition or measurement impact, as the Company chose not to apply the new option offered to recognize actuarial gains and losses outside of the income statement.

IAS 21 (amended 2005) “The Effects of Changes in Foreign Exchange Rates”

As of 1 January 2006, the Company adopted the amendments to IAS 21. As a result, all exchange differences arising from a monetary item that forms part of the Company’s net investment in a foreign operation are recognized in a separate component of equity in the consolidated financial statements regardless of the currency in which the monetary item is denominated and of which Company entity transacts with the foreign operation. This change has had no significant impact as at 31 December 2006 or 31 December 2005.

IAS 39 “Financial Instruments: Recognition and Measurement”

The amendment to IAS 39 in 2005:

- required to include financial guarantee contacts issued;
- permitted the foreign currency risk of a highly probable intra-group forecast transaction to qualify as the hedged item in cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the financial statements;
- restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through profit and loss.

These amendments did not have an effect on the Company’s financial statements.

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

Changes in Accounting Policies (continued)

IFRIC 4 “Determining whether an Arrangement contains a Lease”

IFRIC 4 provides guidance for determining whether arrangements are, or contain, leases that should be accounted for in accordance with IAS 17, if the arrangements comprise a transaction or a series of related transactions, that does not take the legal form of a lease but conveys a right to use an asset in return for a payment or series of payments.

IFRIC 5 “Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds”

IFRIC 5 explains how to treat expected reimbursements from funds set up to meet the costs of decommissioning assets or in undertaking environmental restoration or rehabilitation. As the Company does not currently operate in a country where such funds exist, this interpretation has had no impact on the financial statements.

The adoption of IFRIC Interpretations as of January 1, 2006 has not had a significant impact on the Company in 2006 and 2005.

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:

- IFRS 7 “Financial Instruments: Disclosures”;
- IAS 1 (amended 2005) “Presentation of Financial Statements – Capital Disclosures”;
- IFRIC 8 “Scope of IFRS 2”;
- IFRIC 9 “Reassessment of Embedded Derivatives”;
- IFRIC 10 “Interim Financial Reporting and Impairment”;
- IFRIC 11 “IFRS 2 - Group and Treasury Share Transactions”

IFRS 7 “Financial Instruments: Disclosures” replaces the disclosure requirements of IAS 32 and must be applied for annual reporting periods that commence on or after January 1, 2007.

The amendment of IAS 1 “Presentation of Financial Statements – Capital Disclosures” requires disclosures regarding an entity’s objectives, policies and processes for managing capital. The provisions are effective for reporting periods beginning on or after January 1, 2007.

IFRIC 8 clarifies that IFRS 2 applies to arrangements where an entity makes share-based payments for apparently nil or inadequate consideration. If the identifiable consideration given appears to be less than the fair value of the equity instrument granted, under IFRIC 8 this situation typically indicates that other consideration has been or will be received. IFRS 2 therefore applies. IFRIC 8 becomes effective for financial years beginning on or after May 1, 2006.

IFRIC 9 clarifies, that an entity shall assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. An entity shall apply this interpretation for annual periods beginning on or after June 1, 2006.

(in thousands Rubles)

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

IFRSs and IFRIC Interpretations Not Yet Effective (continued)

Applying IFRIC 10, an entity shall not reverse an impairment loss recognized in a previous interim period in respect of goodwill or an investment in either an equity instrument or a financial asset carried at cost. An entity shall apply this interpretation for annual periods beginning on or after November 1, 2006.

IFRIC 11 addresses the issues whether the certain transactions should be accounted for as equity-settled or as cash-settled under the requirements of IFRS 2, and concerns the accounting treatment for share-based payment arrangements that involve two or more entities within the same group. An entity shall apply this interpretation for annual periods beginning on or after March 1, 2007.

The Company expects that the adoption of the pronouncements listed above will have no significant impact on the Company's result of operations and financial position in the period of initial application. The adoption of IFRS 7 will significantly affect the disclosures relating to financial instruments as presented in the notes to the financial statements.

Restatement of Prior Year Financial Statements

In 2006 the Company engaged an independent appraiser to determine the fair value of investment in unquoted shares in ZAO Russian Industrial Bank (hereinafter ZAO RIB) as of December 31, 2006 and January 1 and December 31, 2005 to ensure fair presentation of changes in equity for 2005. The investment was initially recognized at cost. Based on the findings of the independent appraisal, the investment in ZAO RIB was recognized at fair value as of December 31, 2005 and January 1, 2005 (Note 11).

In accordance with Federal Law "On Communications", the Company is obliged to have all of its linear and cable installations registered. The Company deems it appropriate to claim back value added tax related to its linear and cable installations not registered as immovable property only after they receive state registration. Because the registration process may take considerable time to complete, the Company reclassifies VAT on assets expected to be registered in more than 12 months into non-current assets.

The effect of adjustments to the previous year financial statements can be summarized as follows:

	As previously reported	Effect of adjustment	As restated
Consolidated balance sheet as of December 31, 2005			
Long-term investments	7,796,831	150,624	7,947,455
Long-term receivables and other financial assets	33,614	176,042	209,656
Other current assets	1,416,764	(176,042)	1,240,722
Total assets	**40,882,870**	**150,624**	**41,033,494**
Unrealized gain on available-for-sale investment	5,432,956	114,474	5,547,430
Total equity	**23,667,690**	**114,474**	**23,782,164**
Deferred income tax liability	3,072,518	36,150	3,108,668
Total non-current liabilities	**13,158,887**	**36,150**	**13,195,037**
Consolidated Statement of Changes in Equity for the year ended December 31, 2004			
Unrealized gain on available-for-sale investment	3,745,996	71,552	3,817,548
Consolidated Statement of Changes in Equity for the year ended December 31, 2005			
Unrealized gain on available-for-sale investment	5,432,956	114,474	5,547,430

(in thousands Rubles)

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

Foreign Currency Transactions

The consolidated financial statements are presented in Russian Ruble (RUB), which is the Company’s functional and presentation currency. 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 income statement 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 Rubles 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, 2006 and 2005 were as follows:

Currency	2006	2005
Russian Rubles per US Dollar	**26.3311**	28.7825
Russian Rubles per Euro	**34.6965**	34.1850

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. 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 parent and/or subsidiary 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 income statement.

Acquisition of Minority Interest in Subsidiaries

The difference between the cost and carrying value of additional interest acquired in the net assets of a subsidiary is reported in shareholders’ equity as of the date of transaction as acquisition of minority interest and is charged to retained earnings and reserves. The Company does not remeasure the assets and liabilities of the subsidiary to reflect their fair values at the date of the transaction or for consolidation purposes.

3. Summary of Significant Accounting Policies (continued)

3.2 Associates

Associates are entities in which the Company generally owns 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 by the equity method of accounting 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 income statement 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 obligated to make further payments to, or on behalf of, the associate.

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

3.3 Investments and Other Financial Assets

The Company classifies its financial assets into the following categories: "loans and receivables" and "investments available for sale". When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not classified as "financial assets valued at fair value through profit or loss", directly attributable transaction costs. The Company determines the classification of its financial assets at initial recognition. All regular way purchases and sales of financial assets are recognized on the trade date, which is the date when the asset is delivered to the purchaser. 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 them 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 shall be classified as held for trading, and those that the entity upon initial recognition classifies 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 shall be classified as available for sale.

Such assets 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 and Other Financial Assets (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 three preceding 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 income statement. Reversals of impairment losses in respect of equity instruments are not recognised in the income statement. 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 income statement.

The fair value of investments that are actively traded in organized 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; or 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 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 Interpretation of IFRS in accordance with the specific transitional provisions, if any, in that Standard or Interpretation.

Changes in accounting estimates

As a result of 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

Prior period errors are 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.

3. Summary of Significant Accounting Policies (continued)

3.5 Property, Plant and Equipment

3.5.1 Historical Cost

Property, plant and equipment are recorded at purchase or construction cost, excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value. Such cost includes the cost of replacing part of plant and equipment when that cost is incurred if recognition criteria are met. 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 in accordance with the exemption provided in IFRS 1. At each reporting date management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount, and the difference is recognized as an expense (impairment loss) in the income statement. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

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 routine repairs and maintenance are charged to the income statement as incurred. Social assets are expensed on acquisition. Major renewals and improvements are capitalized, and the assets replaced are retired. Major inspection costs are included in the carrying value of property, plant and equipment if recognition criteria are met.

3.5.2 Depreciation and Useful Life

Depreciation is calculated on a straight-line basis. The depreciation periods, which represent the estimated useful economic lives of the respective assets, are as follows:

Buildings	50 years
Constructions	20 years
Digital switches	15 years
Other telecommunication equipment	10 years
Transportation equipment	5 years
Computers, office and other equipment	3 years
Land	Non depreciable

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

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. Summary of Significant Accounting Policies (continued)

3.5 Property, Plant and Equipment (continued)

3.5.3 Construction in Progress

Construction in progress includes assets under construction or otherwise being brought to a location and condition necessary for them to be operated in the manner intended by management. Construction in progress is recorded as the total of actual expenditures incurred less any impairment in value. No depreciation is charged on construction in progress.

3.5.4 Property, Plant and Equipment Received Free of Charge

Production equipment and other assets attributable to the Company's core business transferred to the Company free of charge outside the privatization process are capitalized at market value at the date of transfer. The corresponding income is fully recognized in the income statement at the date of transfer. In the case when transfers of assets relate to the rendering by the Company of future services to the transferor using the assets transferred, the assets are classified as deferred revenue amounting to the fair value of equipment or other assets transferred. The deferred revenue is taken to the income statement as depreciation is charged on the assets transferred over their useful lives from the date when the Company starts rendering services to the transferor.

Asset contributions that will not generate any future economic benefits for the Company are not recognized.

3.6 Intangible Assets and Goodwill

3.6.1 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 the acquisition of an associate is included in 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.

3. Summary of Significant Accounting Policies (continued)

3.6 Intangible Assets and Goodwill (continued)

3.6.1 Goodwill (continued)

Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognized. 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.

3.6.2 Licenses

The cost of licenses paid to the government for the permission to provide telecommunication services within an identifiable period of time is recognized as intangible asset. Following initial recognition, intangible assets are carried at acquisition cost less any accumulated amortization and any accumulated impairment losses.

3.6.3 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.

3.6.4 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 are accounted for by changing the amortization period, 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 10 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 the indefinite life assessment is no longer supportable, the Company changes the assessment from indefinite to finite and accounts for the change as a change in accounting estimates through starting amortization of the intangible asset.

3. Summary of Significant Accounting Policies (continued)

3.7 Leases

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

Leases where the Company is not transferred substantially all the risks and rewards of ownership of the asset are classified as operating leases.

3.7.1 Finance Leases

At the commencement of the lease term, i.e. the date from which the Company is entitled to exercise its right to use the leased asset, the Company recognizes finance leases as property, plant and equipment at the lower of their fair value or the present value of minimum lease payments, each determined at earlier of the inception of the lease or the date when the parties agree on key terms and conditions of the finance lease. The liability under finance lease is initially recognized at the amount equal to the cost of the assets received under finance lease, 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 the accounting policy of the Company applicable for depreciable and amortized assets. If it is probable that an asset received under a finance lease will have to be returned upon expiration of the lease, the asset is fully depreciated over the shorter of the lease term and its useful life.

3.7.2 Operating Leases

Operating lease payments are recognized as an expense in the income statement on a straight-line basis over the lease term.

3.8 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.

3. Summary of Significant Accounting Policies (continued)

3.8 Financial Instruments (continued)

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. 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 entity’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 derecognized when the rights to receive cash flows from the asset expire or the Company transfers its rights to receive cash flows from the asset.

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

3.9 Inventories

Inventories are recorded at the lower of cost and net realizable value. The cost of inventory is determined on the weighted average basis. The cost of finished goods and work in progress comprises raw material, direct labor, other direct costs and related production overheads (based on normal operating capacity) but excludes borrowing costs. 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.

3.10 Advances Given

Advances given to acquire non-current assets are classified as non-current regardless of the actual date of delivery of the underlying assets and are considered non-monetary assets. Long-term advances given as part of operating activities are also classified as non-current assets.

3.11 Cash and Cash Equivalents

Cash comprises cash at banks and in hand and short-term deposits with an original maturity of three months or less.

3. Summary of Significant Accounting Policies (continued)

3.12 Accounts Receivable and Provision for Impairment of Receivables

Receivables are recognized at original invoice amount less an allowance for any uncollectible amounts. Allowance is made when there doubts that the Company will not be able to collect the debts in full.

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. 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 income statement.

The carrying amount of current receivables is a reasonable approximation of their fair value. The fair value of non-current receivable is calculated using the effective interest rate method.

3.13 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, or 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 be measured in accordance with applicable IFRS Standards and Interpretations.

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

3.14 Loans Given

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

3.15 Loans and Borrowings Received

Loans and borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortized 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 recognized as an adjustment to interest expense over the period of the borrowings.

3. Summary of Significant Accounting Policies (continued)

3.16 Employee Benefits

3.16.1 Current Employment Benefits

Wages and salaries paid to employees are recognized as expense in current period. In addition, the Company creates a provision for future vacations.

3.16.2 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.

3.16.3 Other Pension Plans and Post-Employment Benefits

Under collective bargaining agreements and internal regulations on additional pension benefits, the Company also provides additional benefits for its active and retired employees by using post-employment defined 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: defined contribution plan and defined benefit plan.

The Company's obligation under defined contribution plans are limited to the amount that the Company is prepared to contribute to the fund. In this case, actuarial and investment risks are borne by the employees.

Under defined benefit plans, the Company's obligation is to provide an agreed amount of benefit to current and retired employees. In this case, actuarial and investment risks are borne by the Company.

3.16.3.1 Defined Benefit Plans

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. 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 exceed 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 defined benefit 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 are 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)

3.16 Employee Benefits (continued)

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

3.16.3.2 Defined Contribution Plans

As the Company receives services from employees, the Company accrues its respective commitments under the pension plan by way of recognition of the liability (accrual) less any contributions made as of the date of such accrual, and in correspondence with the recognition of expenses in line "Wages, Salaries, Other Employee Benefits and Payroll Taxes" of the income statement. Where the amount of contribution exceeds the respective liability as of the balance sheet date, the Company recognizes the excess as an asset (prepaid expense) to the extent the prepayment may be offset against future payments or returned to the Company. If contributions under defined contribution plans relate to a service period exceeding 12 months, then at the end of the period in which employees provided services to the Company the amounts related to that period are discounted at a rate established as the market rate of return on AAA corporate bonds ruling at the balance sheet date.

3.17 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 in interest expense.

3.18 Taxation

3.18.1 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.

3. Summary of Significant Accounting Policies (continued)

3.18 Taxation (continued)

3.18.1 Income Taxes (continued)

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 in the period when the asset is realized or liability settled, based on legislation that has 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 utilized.

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.

3.18.2 Deferred Income Tax

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 nor taxable profit or loss.

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 utilized. Deferred tax assets and liabilities are measured at tax rates that are expected to apply in the period when the asset is realized or liability settled, based on legislation that has 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.

3.19 Shareholders’ Equity

3.19.1 Share Capital

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

3. Summary of Significant Accounting Policies (continued)

3.19 Shareholders’ Equity (continued)

3.19.2 Treasury Shares

Where the Company or its subsidiaries purchases the Company’s shares, the consideration paid, including any attributable transaction costs, net of income taxes, is deducted from equity as treasury shares until they are cancelled or reissued. No gain or loss is recognized in the income statement on the purchase, sale, issue or cancellation of the Company’s own equity instruments. Where such shares are subsequently sold or reissued, any consideration received is included in equity. Treasury shares are stated at weighted average cost.

3.19.3 Dividends Declared

Dividends are recognized as a liability and deducted from equity at the balance sheet date only if they are declared 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.

3.20 Minority Interest

Minority interest represents 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.

3.21 Revenue Recognition

Revenue is recognised to the extent that it is probable that the 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 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.

3.21.1 Sales Revenue

The Company categorizes the revenue sources in 13 major categories:

1. Local telephone calls;
2. Intra-regional telephone calls;
3. Installation and connecting fees;
4. Fees on assistance services;
5. Documentary services;
6. Cellular services;
7. Radio and TV broadcasting;
8. Data transfer and telematic services;
9. New services (Internet, ISDN, ADSL, IP-telephony);
10. Rent of telephone channels;
11. Services to telecommunications operators;
12. Other telecommunications services;
13. Other revenues.

3. Summary of Significant Accounting Policies (continued)

3.21 Revenue Recognition (continued)

3.21.1 Sales Revenue (continued)

Revenue from all services, except installation and connection fees, is recognized 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, when time driven billing scheme is applied. If fixed payment scheme is applied then revenue depends on the subscription fee only.

Intra-regional Telephone Services

Intra-regional telephone services include the following client services:

- Telephone connections between subscribers of fixed line telephone network within the territory of a constituent entity of the Russian Federation;
- Telephone connections between subscribers of fixed line telephone network and subscribers of mobile communication network where subscriber numbers of the calling party and destination party are included in the numbering capacity within, respectively, geographically identifiable and geographically unidentifiable numbering areas assigned to the same constituent entity of the Russian Federation.

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 in the income statement 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.

Effective January 1, 2006, changes in legislation governing national long-distance /international and intra-regional services have come in force.

Starting from January 1, 2006, the Company does no longer recognize revenue from national long-distance /international telephony services because, under the new regulations, in the Russian Federation these services are now provided only by operators licensed to do so. In 2006, the Company has been providing only intra-regional telephony services based on a relevant license.

In 2005, revenue from intra-regional telephony services were reported as part of national long-distance telephony services (Note 25).

Fees on Assistance Services

Fees on assistance services include fees for services provided to national long-distance /international operators under assistance agreements. These services comprise subscriber billing and invoicing for long-distance calls, delivery of bills, collection of respective cash receivables and some other services.

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.

3. Summary of Significant Accounting Policies (continued)

3.21 Revenue Recognition (continued)

3.21.1 Sales Revenue (continued)

Cellular Services

Revenues from cellular services mainly arise from airtime services subscription fees, value added telecom 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. 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.

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, ADSL, ISDN, 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 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 to Telecommunications Operators

Revenue from telecom operators includes revenue from interconnection services to Russian operators, point of connection maintenance, as well as termination of local and intra-regional traffic of the Company’s partner operators in the Company’s and interconnected operators’ networks.

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.

Other Revenues

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

3.22 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.

3. Summary of Significant Accounting Policies (continued)

3.22 Earnings per Share (continued)

The Company’s preference shares are considered participating equity instruments for the purpose of earnings per share calculations (Note 30).

3.23 Contingent Liabilities and Contingent Assets

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.

3.24 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 Company;
3. the party is a joint venture in which the Company is a venturer (see IAS 31 Interests in Joint Ventures);
4. the party is a member of the key management personnel of the Company 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 Company, or of any entity that is a related party of the Company.

Relationships between the parent and its subsidiaries and between subsidiaries themselves are not disclosed by the Company in its consolidated financial statements.

The Company discloses transactions with related parties who are commercial organizations under the control of the Russian Federation.

3.25 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 favorable and unfavorable outcomes of conditions that existed at the balance sheet date and changes in management estimates subject to uncertainties which was used for accounting of a number of business activities.

3. Summary of Significant Accounting Policies (continued)

3.25 Events after the Balance Sheet Date (continued)

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 the following for each material category of non-adjusting event after the balance sheet date.

3.26 Hedging

Derivative financial instruments are initially recognized at fair value as of the date of the derivative contract and subsequently revalued to fair value. The method of recognition of the resulting gains or losses depends on whether or not the derivative is designated as hedging instrument, and if it is, then on the nature of the item being hedged. Certain derivatives are designated by the Company as cash flow hedges. At the inception of a transaction, the Company documents the relationship between the hedging instruments and hedged items, as well as its risk management objectives and hedging strategies. Also, the Company documents its estimate, both at the inception and in the course of hedging, as to whether the derivates used in the hedging transactions can efficiently compensate for changes in the cash flows generated by the items being hedged.

With respect to cash flow hedging, the effective portion of changes in fair value of derivative instruments designated and qualifying as cash flow hedges, is reported in the income statement in the periods when the hedged item affects profit or loss. If the hedge is treated as a cash flow hedge then the gain or loss on remeasuring the forward contract is recognized in equity. This amount is included in net profit or loss in the same period or periods during which the hedged item (the liability) affects net profit or loss, that is, when the liability is remeasured for changes in foreign exchange rates.

When a hedging instrument expires or is sold, or when hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognized in equity on the hedging instrument should remain there until the forecast transaction is ultimately recognized in profit and loss. If the forecast transaction is no longer expected to occur, then the cumulative gain or loss recognized in equity, if any, should be immediately recognized in profit or loss.

4. Significant Accounting Assumptions and Estimates

4.1 Assumptions

In applying the accounting policies, the Company’s management, apart from accounting estimates, made the following assumptions that significantly affect the amounts reported in the consolidated financial statements:

Classification of Leases

Leases where all significant risks of ownership of the asset are transferred to lessee are classified as finance leases or operating leases, if otherwise. The answer to the question of whether a lease should be classified as finance lease or operating lease depends on the substance of the deal rather than the mere form of agreement. Unless there is substantial evidence to the contrary, if the term of the lease exceeds 75 percent of the useful life of the asset, or if, at inception of the lease, the present value of minimal lease payments amounts to at least 90 percent of fair value of the leased asset, the Company classifies the lease as finance lease.

4. Significant Accounting Assumptions and Estimates (continued)

4.2 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:

Useful life of Property, Plant and Equipment

The Company assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors". These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and on depreciation recognized in profit or loss.

Impairment of Property, Plant and Equipment

The Company assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Company makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of the asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the assets.

The determination of impairment of property, plant and equipment involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment is based on a large number of factors, such as changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists. The determination of the recoverable amount of a cash-generating unit involves the use of estimates by management. Methods used to determine the value in use include discounted cash flow-based methods, which require 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. These estimates, including the methodologies used, may have a material impact on the fair value and ultimately the amount of any property, plant and equipment impairment.

Fair Values of Assets and Liabilities Acquired in Business Combinations

The Company is required to recognize separately, at the acquisition date, the identifiable assets, liabilities and contingent liabilities acquired or assumed in the business combination at their fair values, which involves estimates. Such estimates are based on valuation techniques, which require considerable judgment in forecasting future cash flows and developing other assumptions.

4. Significant Accounting Assumptions and Estimates (continued)

4.2 Estimation Uncertainty (continued)

Impairment of Goodwill

The Company determines whether goodwill is 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 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, 2006 was 46,936 (2005: 46,936). In 2005 the Company recognized impairment of goodwill of 16,559; in 2006, no impairment of goodwill was identified as a result of analysis. More details are provided in Note 8.

Fair Values of Unlisted Available-for-Sale Investments

The fair value of investments that are not actively traded in organized 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 or other valuation models. These valuation techniques are based on assumptions that are not supported by observable market prices or rates. Management believes that the estimated fair values resulting from the valuation technique which are recorded in the balance sheet and the related changes in the fair values recorded in the statement of changes in equity are reasonable and the most appropriate at the balance sheet date. The major assumptions include the following:

- the companies operate and will continue to operate as going concerns;
- the owners will continue to exercise due diligence and manage the companies’ operations in a competent manner;
- the companies will comply will all applicable laws and normative acts;
- the companies have, will have or extend all necessary permits and licenses from relevant federal and regional authorities and organizations whose decisions underline the valuation results;
- all cash flows from operating activities take place during the year to which the respective income and expenses relate;
- all cash flows take place in the middle of the year.

Allowance for Doubtful Accounts

Management maintains an allowance for doubtful accounts to account for estimated losses resulting from the inability of customers to make payments due from them. When evaluating the adequacy of an allowance for doubtful accounts, management bases its estimates on the aging of accounts receivable balances and historical write-off experience, customer credit worthiness and changes in customer payment terms. If the financial condition of customers were to deteriorate, actual write-offs might be higher than expected. As of December 31, 2006, allowances for doubtful accounts have been created in the amount of 327,891 (2005: 603,762). More details are provided in Note 15.

4. Significant Accounting Assumptions and Estimates (continued)

4.2 Estimation Uncertainty (continued)

Pension Obligations

Post-employment benefits are generally satisfied by plans which are classified and accounted for as defined benefit plans. The present value of defined post-employment benefit obligations and related current service cost are determined in accordance with actuarial valuation, which rely on demographic and financial assumptions including mortality, both during and after employment, rates of employee turnover, discount rate, future salary and benefit levels and, to a limited extent, expected return on plan assets. In the event that further changes in the key assumptions are required, future amounts of pension benefit costs may be affected materially. More details are provided in Note 24.

Site Restoration Provisions

Management reviews site restoration provisions at each balance sheet date, and adjusts them to reflect the current best estimate in accordance with IFRIC 1 “Changes in Existing Decommissioning, Restoration and Similar Liabilities”. As of December 31, 2006 no need for a provision was identified.

Litigations

Management exercises considerable judgment in measuring and recognizing provisions and the exposure to contingent liabilities related to pending litigations or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgement is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the final settlement. Because of the inherent uncertainties in this evaluation process, actual losses may be different from the originally estimated provision. These estimates are subject to change as new information becomes available, primarily with the support of internal specialists, if available, or with the support of outside consultants, such as actuaries or legal counsel. Revisions to the estimates may significantly affect future operating results. More details are provided in Note 33.

Current Taxes

Russian tax, currency and customs legislation is subject to varying interpretations and changes occurring frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Company’s entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Company’s entities may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As of December 31, 2006 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Company’s tax, currency and customs positions will be sustained. More details are provided in Note 33.

4. Significant Accounting Assumptions and Estimates (continued)

4.2 Estimation Uncertainty (continued)

Deferred Tax Assets

Management judgment is required for the calculation of current and deferred income taxes. Deferred tax assets are recognized to the extent that their utilization is probable. The utilization of deferred tax assets will depend on whether it is possible to generate sufficient taxable income in respective tax type and jurisdiction. Various factors are used to assess the probability of the future utilization of deferred tax assets, including past operating results, operational plan, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from that estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected. In the event that an assessment of future utilization indicates that the carrying amount of deferred tax assets must be reduced, this reduction is recognized in profit or loss.

5. Segment Information

The Company operates in one industry, i.e. wireline telecommunication services in the territory of the North-West region of Russia. The Company’s structure is based on territorial units, which service the corresponding parts of the Company’s network. Management considers that the Company operates in one geographical and operating segment. Management assesses operating results and makes investment and strategic decisions based on an entity-wide performance analysis.

(in thousands Rubles)

6. Property, Plant and Equipment

	Land, buildings and constructions	**Switches and transmission devices**	**Construction in progress and equipment for installation**	**Vehicles and other property, plant and equipment**	**Total**
Cost					
As of December 31, 2004	**16,224,446**	**9,139,478**	**1,010,984**	**3,386,542**	**29,761,450**
Additions	-	-	5,366,787	-	5,366,787
Additions due to acquisition of subsidiaries	10,639	1,033	64	1,435	13,171
Disposals	(143,662)	(67,806)	(30,966)	(94,972)	(337,406)
Put in operation	1,778,765	2,484,046	(5,562,192)	1,299,381	-
As of December 31, 2005	**17,870,188**	**11,556,751**	**784,677**	**4,592,386**	**34,804,002**
Additions	-	-	5,294,787	-	5,294,787
Additions due to acquisition of subsidiaries	-	605	-	4,435	5,040
Disposals	(190,700)	(234,802)	(54,873)	(274,139)	(754,514)
Put in operation	1,790,310	1,863,130	(4,319,608)	666,168	-
As of December 31, 2006	**19,469,798**	**13,185,684**	**1,704,983**	**4,988,850**	**39,349,315**
Accumulated depreciation					
As of December 31, 2004	**(2,387,514)**	**(2,127,716)**	**-**	**(899,898)**	**(5,415,128)**
Charge for the year	(1,169,928)	(1,072,616)	-	(637,459)	(2,880,003)
Charge on retired assets	27,797	42,872		63,333	134,002
As of December 31, 2005	**(3,529,645)**	**(3,157,460)**	**-**	**(1,474,024)**	**(8,161,129)**
Charge for the year	(1,100,919)	(1,142,855)	-	(1,275,085)	(3,518,859)
Charge on retired assets	28,208	75,841	-	236,312	340,361
As of December 31, 2006	**(4,602,356)**	**(4,224,474)**	**-**	**(2,512,797)**	**(11,339,627)**
Net book value as of December 31, 2004	13,836,932	7,011,762	1,010,984	2,486,644	24,346,322
Net book value as of December 31, 2005	14,340,543	8,399,291	784,677	3,118,362	26,642,873
Net book value as of December 31, 2006	**14,867,442**	**8,961,210**	**1,704,983**	**2,476,053**	**28,009,688**

In 2006, the Company increased construction in progress by 11,899 of capitalized interest (2005: 78,800). In 2006, the capitalization rate was 8% (2005: 9.8%).

As of December 31, 2006 property, plant and equipment amounting to 1,010,881 (2005: 3,251,064) was pledged as security for loans and borrowings (Note 20).

(in thousands Rubles)

6. Property, Plant and Equipment (continued)

As of December 31, 2006 and 2005 the net book value of property, plant and equipment received under finance lease contracts amounted to:

	2006	2005
Land, buildings and constructions	**113,806**	124,712
Switches and transmission devices	**736,018**	785,400
Construction in progress and equipment for installation	**8,379**	26,047
Vehicles and other property, plant and equipment	**-**	172
Total received under finance lease, net book value	**858,203**	936,331

7. Intangible Assets and Goodwill

	Goodwill	Licenses	Software	Client base	Other	Total
Cost						
As of December 31, 2004	**-**	**8,699**	**1,547,372**	**8,347**	**4,549**	**1,568,967**
Additions	-	8,135	506,149	-	483	514,767
Additions due to acquisition of subsidiaries	46,936	-	-	4,054	-	50,990
Disposals		(817)	(83,801)		(21)	(84,639)
As of December 31, 2005	**46,936**	**16,017**	**1,969,720**	**12,401**	**5,011**	**2,050,085**
Additions	-	9,805	1,163,009	-	130,168	1,302,982
Additions due to acquisition of subsidiaries	-	-	72	-	-	72
Disposals	-	(268)	(65,881)	-	(619)	(66,768)
As of December 31, 2006	**46,936**	**25,554**	**3,066,920**	**12,401**	**134,560**	**3,286,371**
Impairment in value						
As of December 31, 2004	-	-	-	-	-	-
Provision for the year	(16,559)	-	-	-	-	(16,559)
As of December 31, 2005	**(16,559)**	**-**	**-**	**-**	**-**	**(16,559)**
Provision for the year	-	-	-	-	-	-
As of December 31, 2006	**(16,559)**	**-**	**-**	**-**	**-**	**(16,559)**
Accumulated amortization						-
As of December 31, 2004	**-**	**(3,361)**	**(118,896)**	**(464)**	**(488)**	**(123,209)**
Charge for the year	-	(2,696)	(137,063)	(3,630)	(1,473)	(144,862)
Charge on disposed intangibles	-	716	66,241	-	21	66,978
As of December 31, 2005	**-**	**(5,341)**	**(189,718)**	**(4,094)**	**(1,940)**	**(201,093)**
Charge for the year	-	(5,299)	(245,999)	(3,913)	(283)	(255,494)
Charge on disposed intangibles	-	236	50,417	-	75	50,728
As of December 31, 2006	**-**	**(10,404)**	**(385,300)**	**(8,007)**	**(2,148)**	**(405,859)**
Net book value as of December 31, 2004	-	5,338	1,428,476	7,883	4,061	1,445,758
Net book value as of December 31, 2005	30,377	10,676	1,780,002	8,307	3,071	1,832,433
Net book value as of December 31, 2006	**30,377**	**15,150**	**2,681,620**	**4,394**	**132,412**	**2,863,953**

7. Intangible Assets and Goodwill (continued)

Oracle E-Business Suite

As of December 31, 2006 software included Oracle E-Business Suite application with net book value of 804,611 (2005: 762,908), including accrued capitalized interest of 131,142 (2005: 120,589). In 2006, capitalization rate was 8% (2005: 9.8%). Under the supply contract, in 2006 the Company acquired 7,638 licenses for nonexclusive use of Oracle E-Business Suite 2003 Professional.

In 2006, the Company began a phased implementation of Oracle E-Business Suite in relation to non-current asset accounting. During 2006 the software has been implemented in 10 branches of the Company. Full implementation of the software is expected to be completed in 2009.

The Company amortizes the asset starting from the in-service date pro rata to the number of licenses used over the useful life of 10 years.

Amdocs Billing Suite

As of December 31, 2006, software also included Amdocs Billing Suite with net book value of 930,114 (2005: 615,810) including accrued capitalized interest of 66,759 (2005: 25,838). In 2006, capitalization rate was 8% (2005: 6%). The software was acquired with a view to implement a unified computerized settlement system. The Amdocs Billing Suite-based unified computerized settlement system implementation project is expected to take 4 to 5 years to complete.

Amdocs Billing Suite was delivered in December 2004 by OOO IBM Eastern Europe/Asia to whom the Company transferred 18 promissory notes with nominal value of 625,716 in consideration for the provision of software. Promissory notes were repaid by June 1, 2006.

The Company will commence amortizing this asset from the date of software implementation pro rata to the cost of implemented modules over their estimated useful life that is to be determined before the in-service date. Until then, management intends to periodically assess the asset for impairment.

Communication Network Operating Support Systems

As of December 31, 2006 included in software was a communication network operating support system product (SEPSS) with net book value of 442,299 (2005: 83,006), including capitalized interest of 20,204 (2005: – nil). In 2006 capitalization rate was 8%.

The SEPSS software project is being implemented with a view to computerize network accounting, network and service management processes and is expected to take 3-4 years to complete. Software implementation has started in May 2006. The main SEPSS supplier is OOO Step Lodgic.

The Company will commence amortizing this asset from the date of software implementation pro rata to the cost of implemented modules over their estimated useful life that is to be determined before the in-service date. Until then, management intends to periodically assess the asset for impairment.

Unified Pre-Billing System HP Open View IUM

In December 2006 the Company purchased HP Open View IUM for 208,470, with a view to implement unified automated system Amdocs Billing Suite. A unified pre-billing function is necessary to ensure centralized settlements with interconnected operators and to transfer data to Amdocs Billing Suite.

The HP Open View IUM implementation project is expected to take 3-4 to complete. The main supplier is OOO Paladin Invent.

(in thousands Rubles)

7. Intangible Assets and Goodwill (continued)

Unified Pre-Billing System HP Open View IUM (continued)

The Company will commence amortizing this asset from the date of software implementation pro rata to the cost of implemented modules over their estimated useful life that is to be determined before the in-service date. Until then, management intends to periodically assess the asset for impairment.

Network Operation and Management Optimization Program

In 2006, the Company started a phased implementation of a network operation and management optimization program. As of December 31, 2006 the project cost was 129,910. System design and implementation activities have started in October 2006. The Company expects to complete implementation by 2010.

The Company will commence amortizing this asset from the date of software implementation pro rata to the cost of implemented modules over their estimated useful life that is to be determined before the in-service date. Until then, management intends to periodically assess the asset for impairment.

8. Impairment of Assets

Impairment Testing of Goodwill

The Company recognizes goodwill resulted from acquisition in 2005 of OOO Novgorod Datacom that was subsequently restructured through the merger with another Company’s subsidiary OOO Novgorod Deitacom. As of December 31, 2006, the carrying value of goodwill attributable to OOO Novgorod Deitacom was 30 377. The recoverable amount of the goodwill was determined based on its value in use estimated using cash flow projections based on five year budget plans approved by management. Cash flows beyond 5 year period were extrapolated based on average industry-wide profitability indices and using 5% growth rate that is the long-term average growth rate assessed for these cash generating units. Cash flow projections were made using a 14% discount rate (2005: 22%).

As of December 31, 2006, no impairment of goodwill was identified (2005: 16,559).

Impairment Testing of Intangibles Not Yet Available for Use

The Company performed impairment tests of intangible assets not yet available for use. These assets include Oracle E-Business Suite, Amdocs Billing Suite, SEPSS, HP Open View IUM and Network Operation and Management Optimization Program totaling 1,735,522 as of December 31, 2006 (2005: 1,288,962). As a result of analysis made as of December 31, 2006 and 2005, no impairment was identified.

9. Subsidiaries

The consolidated financial statements include the assets, liabilities and financial results of OAO North-West Telecom and its subsidiaries as listed below:

		Equity interest/voting stock	
Subsidiary	**Core activity**	**2006**	**2005**
ZAO AMT	Consulting services	**100%**	100%
OOO Artelecom Service	Lease of the Company’s assets	**100%**	83%
OAO Kolatelecom	Communication services	**50%**	50%
OOO Parma Inform	Communication services	**100%**	100%
ZAO IK Svyaz	Finance services	**100%**	100%
OOO Novgorod Deitacom	Communication services	**100%**	100%
ZAO SPiC	Information services	**100%**	40%

(in thousands Rubles)

9. Subsidiaries (continued)

All of the above companies are Russian legal entities duly incorporated under Russian laws, and have the same financial year as the Company.

In December 2006, following the OAO North-West Telecom Board of Directors’ decision (Minutes No. 19 - 01/30 (06) of November 3, 2006), the Company purchased additional 2,406 registered ordinary shares in ZAO SPiC representing 60% equity interest for 2,631. As a result, the Company has increased its participation in ZAO SPiC to 100%. Expenses directly attributable to the ZAO SPiC acquisition totaled 81. The shares were acquired with a view to expand services available to OAO North-West Telecom subscribers. Management believes that the fair value of identifiable assets, liabilities and contingencies of ZAO SPiC approximates their book value.

In March 2006, OOO Artelecom Service bought 17% of its equity interest from OAO Rostelecom . The transaction is classified in the Company’s consolidated financial statements as acquisition of minority interest and recognized as transaction involving shareholders’ equity. The acquisition cost of the share in OOO Artelecom Service amounted to 9,253 and was fully paid in cash by the Company. As a result, OOO Artelecom Service has become a wholly-owned subsidiary of the Company.

No equity interests in subsidiaries were disposed of in 2006.

10. Investments in Associates

As of December 31, 2006 and 2005 the Company’s investments in associates included:

		2006		**2005**	
Associate	**Core activity**	**Voting stock**	**Carrying value**	**Voting stock**	**Carrying value**
ZAO WestBaltTelecom	Communication services	**28%**	**57,198**	28%	49,055
SZAO Medexpress	Insurance	**25%**	**40,994**	35%	29,294
ZAO Severnaya Kliringovaya Palata	Payment and clearing systems	**-**	**-**	20%	16,306
Others		**24-40%**	**57**	24-40%	57
Impairment of investments in associates			**(57)**		(57)
Total			**98,192**		94,655

All of the above companies are Russian legal entities duly incorporated in accordance with Russian law, and have the same financial year as the Company.

The carrying value of investment in associates reported in these consolidated financial statements reflects the Company’s share in net assets of the associate.

In September 2006, the Company purchased 43,156 new shares of SZAO Medexpress registered common stock for 12,731. The total number of shares in the ownership of OAO North-West Telecom after the purchase is 197,572, and the Company’s equity interest is 25%. The shares have been purchased to retain a majority interest in SZAO Medexpress.

(in thousands Rubles)

10. Investments in Associates (continued)

Disposals of associates in 2006 are presented below:

Associate	Core activity	Carrying value	Proceeds	Sale/disposal of equity interest at the trade date, %
ZAO Severnaya Kliringovaya Palata	Settlement and clearing systems	16,306	2,182	20%
Total		**16,306**	**2,182**	**20%**

Details of gain/loss from sales or other disposals of interest are provided in Note 28.

Movement in investments in associates for the years ended December 31, 2006 and 2005 is presented below:

	2006	2005
Investments in associates as of January 1	**94,655**	85,046
Reclassification of ZAO SPiC from other long-term investments	**7,834**	-
Share in loss of ZAO SPiC for 11 months 2006	**(6,772)**	-
Share in profit of other associates, net of income tax	**7,758**	9,673
Reclassification of ZAO SPiC to subsidiaries	**(1,062)**	-
Purchase of additional shares in SZAO Medexpress	**12,731**	-
Sale of investments in associates	**(16,306)**	-
Dividends received	**(646)**	(64)
Investments in associates as of December 31	**98,192**	94,655

In 2006 share in result of associates (net) comprises 986 (in 2005: 9,673).

The carrying value of investments in associates reported in the consolidated financial statements reflects the Company's interest in the net assets of the associates.

The table below shows aggregated information on the major associates:

Associate	Equity interest	Assets	Liabilities	Sales revenue	Net profit / loss
2005					
ZAO WestBaltTelecom	28%	229,561	(54,367)	169,255	25,159
SZAO Medexpress	35%	411,662	(327,964)	470,255	6,971
ZAO Severnaya Kliringovaya Palata	20%	264,409	(182,879)	13,733	2,489
2006					
ZAO WestBaltTelecom	28%	242,799	(38,521)	219,274	31,616
SZAO Medexpress	25%	722,592	(558,616)	698,846	(15,724)

All of the above companies are Russian legal entities duly incorporated in accordance with Russian law, and have the same financial year as the Company.

(in thousands Rubles)

11. Investments

As of December 31, 2006 and 2005 investments included:

	2006	2005, as restated *(See Note 2)*
Long-term investments available-for-sale	**10,239,203**	7,947,455
Total long-term investments	**10,239,203**	7,947,455
Short-term investments held to maturity	**-**	1,042,626
Total short-term investments	**-**	1,042,626
Total investments	**10,239,203**	8,990,081

As of December 31, 2006 and 2005, long-term investments available for sale included the following:

	2006		2005, as restated *(See Note 2)*	
Company	**Equity interest**	**Fair value**	**Equity interest**	**Fair value**
OAO Telecominvest	**15%**	**10,051,765**	15%	7,763,961
ZAO Russian Industrial Bank	**9%**	**170,788**	9%	159,036
Other long-term investments		**35,881**		59,124
Impairment in value of other investments		**(19,231)**		(34,666)
Total investments available for sale		**10,239,203**		7,947,455

Similar to the prior year the Company engaged independent appraiser to determine the fair value of an unquoted equity investment in OAO Telecominvest as of December 31, 2006. Based on: (a) fair value as determined by an independent appraiser using income, market comparison and cost approaches; (b) independent appraiser's conclusions as to the amount of any potential discount for minority interest; (c) commercial offers from potential buyers received as of the date of these financial statements; and (d) Board of Directors' approval (Minutes No. 19-01/17 (07) of July 9, 2007) of the sale of 15% stake for 410,000 US Dollars (Note 37), as of December 31, 2006 the investment was reported at fair value of 10,051,765 (2005: 7,763,961).

Unrealized gain on investments available for sale recognized in 2006 totaled 1,747,663 (2005: 1,729,882 – as restated – Note 2)).

As of December 31, 2005 short-term investments held to maturity mainly included bank deposits maturing within 6 months in the amount of 1,033,550 bearing interest of 7-8% p.a. The deposits were withdrawn in 2006.

(in thousands Rubles)

12. Long-Term Accounts Receivable and Other Financial Assets

As of December 31, 2006 and 2005 long-term accounts receivable and other financial assets comprised the following:

	2006	**2005, as restated** *(See Note 2)*
Long-term VAT receivable	**165,004**	176,042
Long-term loans given	**23,215**	25,180
Long-term accounts receivable	**11,645**	8,434
Other long-term financial assets	**3,555**	-
Total	**203,419**	209,656

As of December 31, 2006 and 2005, long-term loans given are reported at amortized cost using the effective interest rate of 17.4-20% (2005: 17.4-20%).

13. Long-Term Advances Given

As of December 31, 2006 and 2005 long-term advances given included the following:

	2006	**2005**
Advances to equipment suppliers	**271,242**	27,087
Advances to intangible assets	**241,812**	234,925
Advances to capital contractors	**98,223**	120,965
Other advances given	**16,040**	6,108
Total	**627,317**	389,085

14. Inventories

As of December 31, 2006 and 2005 inventories comprised the following:

	2006	**2005**
Cable, materials, and spare parts for telecommunications equipment	**95,828**	125,565
Tools, work clothes, fittings etc.	**25,908**	28,425
Finished goods and goods for resale	**9,775**	8,444
Construction materials, fuel and other inventories	**176,739**	137,658
Total	**308,250**	300,092

The cost of inventories expensed in 2006 was 729,631 (2005: 710,771).

In 2006 and 2005, no inventory impairment provision was created.

As of December 31, 2006 no inventories have been pledged as security for borrowings.

(in thousands Rubles)

15. Accounts Receivable

As of December 31, 2006 and 2005 accounts receivable were as follows:

	2006	**2005**
Trade receivables – telecommunication services	**1,553,968**	1,686,056
Other receivables	**110,828**	99,512
Provision for impairment of receivables	**(327,891)**	(603,762)
Total	**1,336,905**	1,181,806

The Company identified accounts receivable by the following major customer groups:

	2006	**2005**
Residential customers	**571,998**	802,797
Social security organizations – tariff compensation	**189,773**	479,684
Corporate customers	**702,518**	316,444
Government customers	**89,679**	87,131
Total trade receivables – telecommunication services	**1,553,968**	1,686,056

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 Rubles, in effect at the time the calls are made. In certain cases the Company managed to collect penalties for payment delays and to enforce reimbursement in arbitration court.

As of December 31, 2006, the debt of social security organizations with regard to tariff compensation related to granting privileges to certain categories of subscribers amounted to 12% of total accounts receivable (2005: 28%).

In 2006, the Company recovered from the federal government 212,742 through legal action in settlement of the above accounts receivable.

In December 2006, the Company assessed the probability of recovery of accounts receivable related to compensation due from social organizations, and taking into account potential judicial enforcement of debts, created a provision for impairment of receivables of 189,773 (2005: 479,684) or 100% of the total amount due from social security organizations as of December 31, 2006.

The following table summarizes changes in the provision for impairment of receivables:

	2006	**2005**
Balance as of January 1	**603,762**	1,029,883
Reversal of provision	**(191,429)**	(362,428)
Write-off of accounts receivable	**(84,442)**	(63,693)
Balance as of December 31	**327,891**	603,762

Income accrued in 2006 in relation to the reversal of the provision for impairment of receivables of 191,429 (2005: 362,428) was included in "Reversal of Provision for Impairment of Receivables" in the consolidated income statement.

(in thousands Rubles)

16. Other Current Assets

As of December 31, 2006 and 2005 other current assets comprised the following:

	2006	2005, as restated *(See Note 2)*
VAT receivable	**501,166**	766,769
Prepaid income tax	**219,591**	172,115
Prepayments and advances	**77,029**	81,549
Deferred expenses	**60,878**	81,560
Other prepaid taxes	**26,077**	15,757
Settlements with personnel	**19,677**	17,117
Other settlements and current assets, less provision	**125,084**	105,855
Total	**1,029,502**	1,240,722

17. Cash and Cash Equivalents

As of December 31, 2006 and 2005 cash and cash equivalents comprised the following:

	2006	2005
Cash at bank and on hand	**244,404**	152,005
Short-term deposits with original maturities of three months or less	**87**	86
Total	**244,491**	**152,091**

As of December 31, 2006 the Company had no restricted cash.

As of December 31, 2006 Cash at bank and on hand comprised of amounts denominated in Russian Rubles.

The total figures of cash and cash equivalents shown on the face of the balance sheet as of December 31, 2006 and in the cash flow statement for 2006 and as of December 31, 2005 and for 2005, are equal. The Company applies the same policy to determine the structure and amount of cash and cash equivalents in the balance sheet and cash flow statement.

18. Significant Non-Cash Transactions

In 2006 the Company acquired property, plant and equipment on finance lease terms in the amount of 6,600 (2005: 11,468) and on a free of charge basis in the amount of 24,523 (2005: 12,302).

Non-cash transactions have been excluded from the consolidated cash flow statement.

19. Share Capital

The Company has the following outstanding shares:

	Number of shares outstanding (thousands)		Number of treasury shares (thousands)	Shares outstanding		
	Preference shares	Ordinary shares		Preference shares	Ordinary shares	Treasury shares
As of December 31, 2004	250,370	881,045	(7,083)	621,739	2,233,765	(60,822)
Treasury shares purchased			(1,465)			(12,114)
Treasury shares sold			1,945			16,255
As of December 31, 2005	250,370	881,045	(6,603)	621,739	2,233,765	(56,681)
Treasury shares purchased			(1,236)			(32,179)
Treasury shares sold			1,609			22,193
As of December 31, 2006	**250,370**	**881,045**	**(6,230)**	**621,739**	**2,233,765**	**(66,667)**

19. Share Capital (continued)

The nominal value of all issued shares is 1 Ruble each. The difference between the nominal and carrying value of shares reflects the effect of inflation in periods preceding January 1, 2003. All issued shares were fully paid up.

The ordinary shareholders are entitled to one vote per share. 22% of all shares issued as of December 31, 2006 were ordinary shares and 78% were Class A preference shares.

Class A preference shares give the holders the right to participate in annual shareholders' meetings without voting rights except in instances where decisions are made in relation to re-organisation and liquidation of the Company, and where changes and amendments to the Company's Charter which restrict the rights of preference shareholders are proposed.

Each preference share pays a guaranteed dividend determined as the higher of 10% of the net income as reported in the Company's Russian statutory financial statements divided by the number of preference shares, or dividend per ordinary share. In instances when preference shareholders receive a dividend of less than 10% of the net income reported in the Company's Russian statutory financial statements, ordinary shareholders receive no dividend. Preference shareholders have the right to participate in annual shareholders' meetings and vote on all issues within the authority of the meeting starting from the meeting following the annual general shareholders' meeting which took the decision not to pay or to pay only a part of dividend on preference shares.

Distributable earnings of entities comprising the Company are limited to their retained earnings, as mandated by the statutory accounting rules. Statutory retained earnings of the Company as of December 31, 2006 and 2005 amounted to 6,843,562 and 6,598,589 respectively.

In accordance with the Russian legislation, dividends may only be declared to the shareholders of the Company from net income for the year as reported in the Company's Russian statutory financial statements. The net income of the Company for 2006 and 2005 was 2,426,248 and 1,843,471, respectively.

Treasury shares represent ordinary or preference shares of the Company held by subsidiaries.

Dividends were declared in 2007 in respect of 2006 to holders of ordinary shares and preference shares of 0.357 Rubles per ordinary share (2005: 0.265 Rubles) and 0.858 Rubles per preference share (2005: 0.652 Rubles). The total amount of dividends declared is disclosed in Note 31.

In September 2001 the Company signed a depositary agreement with JP Morgan Chase Bank regarding placement of American Depositary Receipts (ADRs), Level 1. In accordance with the depositary agreement, each ADR represents 50 ordinary shares of the Company. As of December 31, 2006, 1,082,726 ADRs represented 54,136,300 deposited shares, which constituted 6.14% of all ordinary shares issued.

(in thousands Rubles)

19. Share Capital (continued)

The Company's shareholding structure as of December 31, 2006 was as follows:

	Ordinary shares (thousands shares)	%	Preference shares (thousands shares)	%	Total (thousands shares)
OAO Svyazinvest	447,231	50.8%	-	-	447,231
Other entities	351,208	39.9%	162,897	65.1%	514,105
Individuals	41,847	4.7%	84,243	33.6%	126,090
Russian Federal Property Fund	37,754	4.3%	5	0.002%	37,759
Treasury shares	3,005	0.3%	3,225	1.3%	6,230
Total	**881,045**	**100%**	**250,370**	**100%**	**1,131,415**

20. Borrowings

As of December 31, 2006 and 2005 outstanding borrowings included:

	Effective interest rate	2006	2005
Short-term borrowings			
Bank loans (Rubles)	13-15.5%	**3,070**	530,438
Interest payable on bank loans, bonds, promissory notes and vendor financing		**78,461**	65,240
Total short-term borrowings		**81,531**	595,678
Long-term borrowings			
Bank loans (Rubles)	8.25 – 10.5%	**1,500,079**	2,200,079
Bank loans (Euro)	5.7-7%	**1,876,868**	1,860,757
Total bank loans		**3,376,947**	4,060,836
Bonds (Rubles)	7.5-9.25%	**6,032,061**	4,479,068
Vendor financing (Rubles)	7%	**-**	110
Vendor financing (US Dollars)	7-8.2%	**8,499**	257,723
Vendor financing (Euro)	7.5-10.8%	**50,638**	111,286
Total vendor financing		**59,137**	369,119
Promissory notes (Rubles)	23%	**2,496**	5,390
Promissory notes (US Dollars)	6%	**3,762**	12,574
Promissory notes (Euro)	8-11.9%	**22,064**	26,200
Total promissory notes		**28,322**	44,164
Other loans (Rubles)	15.4-15.5%	**9,907**	6,743
Other loans (US Dollars)	9.4%	**8,685**	9,477
Total other loans		**18,592**	16,220
Less: Current portion of long-term borrowings		**(1,937,448)**	(791,969)
Total long-term borrowings		**7,577,611**	8,177,438

Long-term borrowings include accrued interest of 5,607 as of December 31, 2006 (2005: 5,231). As repayment of the interest is expected not earlier than in 2008, it was classified as long-term borrowings.

(in thousands Rubles)

20. Borrowings (continued)

As of December 31, 2006, long-term borrowings had the following maturity structure:

Maturity date	Bank loans	Bonds	Vendor financing	Promissory notes	Other	Total
2007	813,080	1,048,921	44,064	20,522	10,861	1,937,448
2008	2,017,293	2,989,640	14,484	5,305	159	5,026,881
2009	458,695	495,617	203	-	159	954,674
2010	37,518	498,757	216	-	159	536,650
2011	50,361	999,126	170	-	635	1,050,292
After 2011	-	-	-	2,495	6,619	9,114
Total	**3,376,947**	**6,032,061**	**59,137**	**28,322**	**18,592**	**9,515,059**

The Company's borrowings as of December 31, 2006 and 2005 were denominated in the following currencies:

	2006	2005
Russian Rubles	**7,602,703**	7,278,444
US Dollars	**21,357**	285,993
Euro	**1,972,530**	2,000,648
Total	**9,596,590**	9,565,085

Bank Credits and Loans

Short-term borrowings as of December 31, 2006 primarily represent bank loans obtained to finance working capital from AKB Sberbank RF (OAO), AKB Provsvyazbank (ZAO), Barenzbank (ZAO).

In 2006 the Company obtained and repaid short-term loans from AKB Sberbank RF (OAO), AKB Bank of Moscow (OAO), KB Citibank (ZAO), AKB Svyaz-Bank (OAO), Bank Uralsib (OAO), ABGP Gazprombank.

In 2006 the Company had open the following contracts but loan raising under these contracts was not performed yet as of December 31, 2006:
- ZAO Raiffeisenbank: a non-revolving loan facility of 500,000;
- ZAO ING Bank (Eurasia): a non-revolving loan facility of 500,000;
- OAO Bank St. Petersburg: a loan facility of 190,000;
- OAO AKB Svyaz Bank: a loan facility of 260,000;
- AKB Sberbank RF: a revolving loan facility of 289,000.

Long-term borrowings as of December 31, 2006 primarily represent bank loans obtained under loan contracts signed prior 2006 with AKB Sberbank RF (OAO), ZAO Commertsbank (Eurasia), Vnesheconombank, Citibank N.A. and Citibank International PLC as well as under the loan provided by ZAO Raiffeisenbank Austria in 2006.

Citibank N.A
In December 2005, a 50,000 thousand Euro syndicated loan agreement was signed between the Company, Citibank N.A., Citibank International PLC and the original lenders. The Company has fully drawn down the credit facility. Transaction costs totaled 553 thousand Euro. Interest rate is fixed at Euribor+ 2% p.a. The agreement expires on March 24, 2009. Interest is accrued and payable on a quarterly basis. As of December 31, 2006 the outstanding syndicated loan was 1,732,969 (2005: 1,692,063), including interest accrued. The loan is not collaterized with property, plant and equipment.

20. Borrowings (continued)

Bank Credits and Loans (continued)

Vnesheconombank
A long-term credit facility was granted to the Company in 1995-1996 by the Russian Federation Ministry of Finance to finance telecom equipment purchases from various foreign vendors. Vnesheconombank acted as credit agent on behalf of the RF Government. The contractual currency is Euro. As of December 31, 2006 the total amount due to Vnesheconombank was 161,248 (2005: 170,419), including short-term portion of 18,465 (2005: 11,802) and interest of 3,815 (2005: 3,505). The liability was recognized at amortized cost with the use of effective interest rate of 7%. The loan is secured by property, plant and equipment with net book value of 74,615 (2005: 78,679).

Restrictions and Covenants

Under the existing borrowing arrangements the Company has to comply with certain conditions, including maintenance of certain financial performance standards.

Under the loan agreements the Company agrees to maintain the following financial performance standards (computed based on IFRS financial statements):

Citibank N. A. (syndicated loan):
- Net debt to EBIDTA ratio – maximum 3:1;
- EBITDA to net interest ratio – minimum 4:1;
- Net debt to net capitalization – maximum 1

Commerzbank (Eurasia) (ZAO):
- Debt to equity ratio – maximum 1:2;
- Net debt to EBIDTA ratio – maximum 2:1;
- EBITDA to net interest ratio – minimum 5:1;
- Equity - minimum 300 000 thousand Euro equivalent

AKB Gazprombank (ZAO):
- Long-term debt to EBITDA – maximum 3:1

In addition to obligations related to financial performance standard compliance, the Company is liable under agreements whereby banks may demand early repayment in the following instances:

Loan agreement with Commerzbank (Eurasia) (ZAO):
- Evidence of bankruptcy;
- Liabilities to third parties of over 300 000 overdue for over 15 days;
- Change of ownership of over 50% shares in the Company

Loan agreement with Raiffeisen Bank Austria (ZAO):
- Threat of court proceedings, rulings or decisions of a court of other government authority against the Company for an amount exceeding 150 000;
- Overdue taxes, duties and other tax and social security liabilities exceeding RUR 150 000;
- Evidence of bankruptcy;
- Disposal/transfer of assets exceeding 10% of total Company's assets, during a fiscal year;
- Receipt by the Bank of a debt collection order for an amount exceeding 150 000; a court or other relevant order to seize or block the Company's bank account or other property valued over 150 000, if such debt collection order or court order is not cancelled prior to execution, or such seizure or block is not lifted within 3 working days.

20. Borrowings (continued)

Bank Credits and Loans (continued)

Restrictions and Covenants (continued)

Loan agreements with AKB Sberbank (OAO):
- Monthly receipts to the settlement account of the Company – minimum 900 000;
- The Company goes into insolvency (bankruptcy); a third party bankruptcy proceedings against the Company;
- Decision on restructuring or liquidation;
- Loss of collateral;
- Prosecution brought against the Company or claim on the Company's assets in the amount exceeding US$ 5,170 thousand

RF Ministry of Finance:
- Reorganization of the Company;
- Delay in performing obligations under a contract (debt restructuring agreement) for over one month

Loan agreement with Citibank N.A.:
- Any of the Borrower's assets is expropriated, arrested, sequestrated, attached, or becomes subject of judicial decision or similar court procedures in a relevant jurisdiction (not applicable where such event or circumstance does not prevent the Borrower from making payments in accordance with financial documents or does not affect the operational activity of the Borrower);
- A tax payment request is served (not applicable if the amount payable does not exceed 10 000 thousand Euro; or the borrower can prove to be contesting payment in good faith);
- Happening of an event or circumstance constituting a breach of obligations under another contract or instrument that is binding on the Borrower or his assets (not applicable if the total liability of the Borrower does not exceed 10 000 thousand Euro).

In addition, the loan agreement with Citibank N.A. imposes the following restrictions:
- Asset sales in a year < 10% of total assets;
- Equity acquisitions in a year < 50 000 thousand Euro;
- Investment programs in a year < 200 000 thousand Euro;
- Loans and guarantees given < 10 000 thousand Euro;
- Dividends for a year < 100% of net profit for the year

Any departure by the Company from the above restrictions is subject to prior approval of the principal lenders. The Company monitors compliance with restrictions and covenants and obtains waivers from the principal lenders if necessary.

(in thousands Rubles)

20. Borrowings (continued)

Bonds

The table below shows movements in bonds payable for the period from December 31, 2005 through December 31, 2006:

Bonds payable as of December 31, 2004	**1,500,288**
3rd bond issue	3,000,000
Issue costs	(27,252)
Amortization of issue costs	28,698
Amortization of premium	(22,666)
Bonds redeemed under the offer attached to 2nd issue	(61,227)
Placement of bonds redeemed under the offer attached to 2nd issue	61,227
Bonds payable as of December 31, 2005	**4,479,068**
Repayment of the 2nd bond issue	(450,000)
4th bond issue	2,000,000
Issue costs	(6,500)
Amortization of issue costs	9,493
Bonds payable as of December 31, 2006	**6,032,061**

As of December 31, 2006 the Company had outstanding 2nd, 3rd and 4th issue bonds. The 2nd issue bonds carry 16 coupons of which 12 have been repaid as of December 31, 2006. In 2006, the Company fully met its coupon obligations at 7.5% p.a. in the total amount of 112,200. Coupon payment per bond was 18.7 Rubles. The nominal bond value is repayable in installments as follows: 30% - in October 2006, 30% – on April 4, 2007. 40% are repayable on October 3, 2007, i.e. 1456 days from the date of placement. As of December 31, 2006 the outstanding bond balance was 1,048,921.

In March 2005, the Company registered the issue of 3,000,000 certified coupon bonds with par value of 1,000 Rubles each carrying 24 interest bearing coupons. Payments under the first coupon are due on the 91st day from the date of bond placement, and other coupon payments are effected every 91 day. The interest rate under coupons 1 through 12 is set at 9.25% p.a. The Board of Directors will establish the interest rate for coupons 13-24 outstanding by February 2008. The bonds mature in February 2011, in 2184 days from the date of placement. The nominal bond value is repayable in installments as follows: 30% - February 25, 2010, 30% – August 26, 2010, and 40% - February 24, 2011. Under the terms of the issue, bondholders are entitled to early redemption in February 2008. In 2006 the Company fully met its coupon obligations at 9.25% p.a. in the total amount of 276,720. Coupon payment per bond was 23.06 Rubles. As of December 31, 2006 the outstanding loan totaled 2,989,640.

In October 2006, the Company registered the issue of 2,000,000 certified coupon bonds with part value of 1,000 Rubles each carrying 20 interest bearing coupons. Payments under the first coupon are due on the 91st day from the date of bond placement, and other coupon payments are effected every 91 day. The interest rate under coupons is set at 8.1% p.a. The nominal bond value is repayable in installments as follows: 25% – December 10, 2009; 25% – December 9, 2010; 50% – December 8, 2011. The issue contains no offer to purchase bonds from bondholders at fixed dates within 12 months from the date of these financial statements. The Bond Resolution and Prospectus provide an option for early redemption at the Company's initiative on 728th day from the date of placement. Bond premium payable on early redemption is 20 Rubles per bond. As of December 31, 2006 the outstanding loan totaled 1,993,500.

(in thousands Rubles)

20. Borrowings (continued)

Vendor Financing

Vendor	Currency	Maturity	Agreed interest rate	2006	2005
IBM East Europe/Asia	USD	2006	Discount	**-**	219,904
AKB Svyaz –Bank (OAO)	EUR	2007-2008	7.5%	**44,871**	89,263
Verisel-Telecom	USD	2006	0%	**7,541**	17,646
Lucent Technologies	EUR	2006	6.6%-9%	**-**	12,713
Siemens	EUR	2007-2008	0%, EURIBOR+2.5%, 7.5%	**5,766**	9,309
Inlain Technologies	USD	2006	LIBOR+4%	**-**	8,581
Iskratel	USD	2005-2006	0%, 6%, 6.5%	**-**	7,473
FGUP LONIIS	USD	2006	0%	**-**	2,949
Kvant-Intercom	USD, RUR	2005, 2011	0%, 9%	**959**	1,230
Others	USD, RUR	2005-2006	0%	**-**	51
Total				**59,137**	369,119

The liability to OOO IBM East Europe/Asia was represented by liability under promissory notes issued by the Company in 2004 as a security for Amdocs Billing Suite software delivery. As of December 31, 2006 the debt was fully repaid.

Liability under interest-free vendor financing agreements as of December 31, 2006 was initially recognized at fair value based on discount rate of 7% to 8.2%. Subsequently the liability has been carried at amortized cost.

Promissory Notes

In 2000-2003 the Company issued promissory notes to finance its current operations and restructure liabilities. Notes issued are accounted for at amortized cost using the effective interest rate of 23% for Ruble denominated notes, 6% for US dollar denominated notes and 8-11.9% for Euro denominated notes.

21. Finance Lease Obligations

The Company has finance lease contracts for telecommunication equipment and vehicles. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments as of December 31, 2006 and 2005 are as follows:

	2006		2005	
	Minimum lease payments	Present value of minimum lease payments	Minimum lease payments	Present value of minimum lease payments
Current portion	**222,317**	**169,889**	281,487	189,216
1 to 5 years	**157,826**	**136,733**	374,584	302,121
Total minimum lease payments	**380,143**	**306,622**	656,071	491,337
Less amounts representing finance charges	**(73,521)**	**-**	(164,734)	-
Present value of minimum lease payments	**306,622**	**306,622**	491,337	491,337

(in thousands Rubles)

21. Finance Lease Obligations (continued)

In 2006 and 2005, the Company's primary lessors were OAO RTC-Leasing and OAO Leasing Telecom. In 2006, the effective interest rate on lease liabilities ranged from 11% to 45% p.a. (2005: 13% to 45% p.a.).

OAO RTC-Leasing purchases telecommunication equipment from domestic and foreign suppliers and leases the equipment. The Company's obligations to OAO RTC-Leasing under capital leases as of December 31, 2006 comprised 338,916 (2005: 571,914), including 271,291 (2005: 422,154) of principal amount and 67,625 (2005: 149,760) of interest payable.

Pursuant to agreements concluded with OAO RTC-Leasing, the lessor is entitled to adjust the lease payment schedule in the event of change of certain macroeconomic conditions, in particular, change in the refinancing rate of the Central Bank of the Russian Federation.

OAO Leasing Telecom purchases vehicles from domestic and foreign suppliers and leases the vehicles. The Company's obligations to OAO Leasing Telecom under the contracts as of December 31, 2006 were 40,059 (2005: 68,338), including 34,398 (2005: 54,869) of principal amount and 5,661 (2005: 13,469) of interest payable.

As of December 31, 2005 finance lease obligations of 9,307 were denominated in foreign currencies, mainly US Dollar and Euro. As of December 31, 2006 finance lease obligations were denominated in Russian Rubles.

22. Accounts Payable and Accrued Liabilities

Accounts payable and other current liabilities of the Company as of December 31, 2006 and 2005 comprised the following:

	2006	**2005**
Accounts payable to equipment suppliers and capital contractors	**547,971**	113,535
Trade accounts payable	**541,854**	454,493
Salaries and wages	**515,715**	628,935
Advances received from subscribers	**369,393**	348,719
Other accounts payable and current liabilities	**192,438**	68,779
Total	**2,167,371**	1,614,461

As of December 31, 2006 and 2005, accounts payable of 241,459 and 40,052, respectively, were denominated in foreign currencies, mainly Euro and US Dollars.

Other accounts payable include outstanding payables to insurance providers, trade union contributions and agent fees payable.

23. Taxes and Social Charges Payable

As of December 31, 2006 and 2005 the Company had the following current taxes payable:

	2006	**2005**
Unified social tax	**134,649**	213,862
Assets tax	**101,322**	90,540
Personal income tax	**33,529**	20,733
Value added tax	**31,754**	364,937
Other taxes	**5,961**	4,164
Total	**307,215**	694,236

(in thousands Rubles)

23. Taxes and Social Charges Payable (continued)

Payment of value added tax of 27,779 (2005: 245,149) is conditional upon collection or write-off of the respective trade accounts receivable.

24. Pension Liabilities and Other Employee Benefits

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

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 specific formula. According to the formula the benefits depend on the number of parameters for each branch of the Company, including the relative pay of participants and their past service in the Company at retirement. The benefits are not vesting and are subject to the employee retiring from the Company on or after the abovementioned ages.

Non-government pension fund Telecom-Soyuz, which is related to the Company (Note 35), maintains the defined benefit pension plan. The Company funds the pension plan on a pay-as-you-go basis upon agreement with the pension fund.

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

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

As of December 31, 2006 there were 26,794 working employees participating to the defined benefit pension plan of the Company and 16,965 pensioners eligible to the other post-employment benefit plans provided by the Company (2005: 27,647 and 14,014 respectively).

As of December 31, 2006 and 2005 net liabilities under defined benefit and other post-employment benefit plans comprised the following:

	2006	**2005**
Present value of defined benefit obligation	**2,741,726**	1,960,447
Fair value of plan assets	**(40,831)**	(136,885)
Present value of unfunded obligation	**2,700,895**	1,823,562
Unrecognized past service cost	**(594,417)**	(694,318)
Unrecognized actuarial gains /(losses)	**(469,847)**	172,709
Net pension liability in the balance sheet	**1,636,631**	1,301,953

The present value of defined benefit obligation includes the Company’s liabilities under other long-term employee benefits such as jubilee and long-service benefits in amount 62,023 and 169,592 respectively (2005: 32,693 and 110,213 respectively).

(in thousands Rubles)

24. Pension Liabilities and Other Employee Benefits (continued)

The amount of net expense under the defined benefit and other post-employment benefit plans recognized in 2006 and 2005 were as follows:

	2006	2005
Current service cost	**121,137**	111,842
Interest cost on benefit obligation	**138,340**	135,375
Expected return on plan assets	**(6,263)**	(10,359)
Net actuarial losses/(gain) recognized in the year	**67,281**	(6,565)
Amortization of past service cost	**99,901**	49,740
Past service cost immediately recognized	**-**	78,740
Losses/(gains) on curtailments and settlements	**28,795**	(9,260)
Net expense for the defined benefit plan	**449,191**	349,513
Actual return on plan assets	**29**	8,482

Changes in the present value of defined benefit obligations in 2006 and 2005 were as follows:

	2006	2005
Defined benefit obligations at January 1	**1,960,447**	1,470,205
Current service cost	**121,137**	111,842
Interest cost on benefit obligation	**138,340**	135,375
Past service cost	**-**	431,065
Benefits paid	**(42,568)**	(27,818)
Liabilities extinguished on settlements	**(168,028)**	(196,199)
Actuarial (gains)/losses on obligation	**732,398**	35,977
Defined benefit obligations at December 31	**2,741,726**	1,960,447

Changes in the fair value of plan assets during 2006 and 2005 were as follows:

	2006	2005
Fair value of plan assets at January 1	**136,885**	66,960
Expected return	**6,263**	10,359
Actuarial gains/(losses)	**(6,234)**	(1,877
Benefits paid	**(42,568)**	(27,818)
Liabilities extinguished on settlements	**(168,028)**	(186,939)
Contributions by employer	**114,513**	276,200
Fair value of plan assets at December 31	**40,831**	136,885

The Company expects to contribute 153,108 to its defined benefit pension plans in 2007.

The major categories of plan assets as a percentage of the fair value of total plan assets are as follows:

	2006	2005
Russian equities	**9.2%**	1.5%
Russian corporate bonds	**34.2%**	22.7%
Russian government bonds	**30.8%**	39.0%
Russian corporate promissory notes	**24.9%**	33.1%
Other assets	**0.9%**	3.7%

(in thousands Rubles)

24. Pension Liabilities and Other Employee Benefits (continued)

As of December 31, 2006 and 2005 the principle actuarial assumptions of defined benefit pension and other post-employment benefit plans were as follows:

	2006	2005
Discount rate	**7%**	7%
Expected return on plan assets	**8.5%**	9.69%
Future salary increases	**9.2%**	8.15%
Relative pay increase (career progression)	**1%**	1%
Rate used for calculation of annuity value	**6%**	6%
Increase in financial support benefits	**5%**	5%
Staff turnover	**5%**	10%
Mortality tables (source of information)	**USSR 1985/86**	USSR 1985/86

The overall expected rate of return on assets is determined based on the market prices prevailing on that date and the structure of the plan assets portfolio. There has been change in the expected return on plan assets due some decrease in return on corporate promissory notes and decrease in their share in total plan assets in 2006.

Amounts for the current and previous four periods are as follows:

	2006	2005	2004	2003	2002
Present value of defined benefit obligation	**2,741,726**	1,960,447	1,470,205	1,647,759	1,146,114
Plan assets	**(40,831)**	(136,885)	(66,960)	(274,598)	(204,058)
Deficit/surplus	**2,700,895**	1,823,562	1,403,245	1,373,161	942,056
Experience adjustments on plan liabilities, gain/(loss)	**(219,983)**	(52,625)	301,343	(71,539)	(154,385)
Experience adjustments on plan assets, gain/(loss)	**(6,234)**	(1,877)	(23,963)	11,287	19,690

25. Revenues

By revenue type	2006	2005
Local telephony services	**9,315,719**	8,129,287
National and international long distance telephony services	**-**	4,237,324
Intra-regional telephony services	**1,412,985**	1,596,621
Services to national operators	**4,701,883**	1,909,839
New services (Internet, ISDN, ADSL, IP-telephony)	**1,537,237**	1,096,955
Other communication services	**1,046,150**	1,027,737
Installation and connecting fees	**410,427**	747,619
Radio and TV broadcasting	**351,779**	329,136
Data transfer and telematic services	**541,279**	288,094
Rent of telephone channels	**301,440**	263,408
Documentary services	**34,084**	49,640
Other revenues	**996,844**	866,254
Total	**20,649,827**	20,541,914

(in thousands Rubles)

25. Revenues (continued)

Since 2006, in accordance with the recently enacted legislation, the rules for rendering intra-regional, national long distance and international telephony services have been changed.

Starting from 2006, the Company no longer provides national long-distance and international telephone services since, in accordance with the new rules, only operators licensed to provide national long-distance and international telephony services are entitled to provide such services in the territory of the Russian Federation. Since 2006, the Company provides intra-regional telephony services to subscribers based on a relevant license.

In 2005, revenues from intra-regional connections were not shown separately, as the Company used rates approved for all national long-distance telephony services with no separate rate set for intra-regional services.

In 2005, revenue from intra-regional telephony services of 1,596,621 was included in revenue from national long-distance telephony services. For the sake of comparability, the Company made the following reclassification of 2005 revenues:

By type of revenue	As previously classified	Reclassification	After reclassification
National/international long-distance telephone services	6,618,885	(2,381,561)	4,237,324
Intra-regional telephone services	-	1,596,621	1,596,621
Services to national operators	1,124,046	785,793	1,909,839
New services (Internet, ISDN, ADSL, IP-telephony)	1,097,808	(853)	1,096,955

In March 2006 the Company submitted bids and won a contract for taxophone-based universal communication services in Kaliningrad and Archangelsk regions. Since August 2006 the Company has started to provide taxophone-based universal communication services in Arkhangelsk region, and since October 2006, in Kaliningrad region.

The Company identifies revenue by the following major customer groups:

By customer group	2006	2005
Residential customers	**10,035,585**	12,195,232
Corporate customers	**8,958,454**	6,708,207
Government customers	**1,655,446**	1,637,190
Social security organizations – tariff compensation	**342**	1,285
Total	**20,649,827**	20,541,914

(in thousands Rubles)

26. Other Operating Expenses

	2006	2005
Security and fire protection services	**352,749**	305,774
Agency fees	**328,077**	203,797
Rental expenses	**204,678**	225,354
Universal service fund payments	**182,728**	142,516
Membership fees, charities and labor union contributions	**153,564**	90,053
Advertising expenses	**152,864**	78,824
Contributions to Non-Commercial Partnership	**130,000**	144,099
Post services	**125,062**	74,184
Audit and consultancy services	**124,506**	120,373
Transportation services	**107,550**	119,660
Property insurance	**105,564**	124,611
General administration and management	**96,828**	88,229
Business travel and representation expenses	**83,206**	84,854
Lending charges	**58,745**	60,991
Remuneration of the Board of Directors and Audit Commission	**53,468**	42,351
Training	**30,838**	34,079
Collection of written-off receivables	**(5,965)**	(334,001)
Other expenses	**233,107**	183,058
Total	**2,517,569**	1,788,806

Other expenses mainly include social costs, stamp duty and other operating expenses.

27. Interest Expense, Net

	2006	2005
Interest income	**(62,955)**	(95,443)
Interest expense	**734,027**	714,724
Interest expense accrued on financial lease	**98,112**	139,157
Less: capitalized interest (Notes 6 and 7)	**(80,934)**	(163,284)
Total	**688,250**	595,154

28. Loss from Investments, Net

	2006	2005
Loss on sale of ZAO Severnaya Kliringovaya Palata (Note 10)	**14,124**	-
Loss (gain) on sale of other investments	**(1,994)**	3,113
Loss (reversal of loss) on impairment of investments	**(375)**	3,181
Dividend income	**(3,566)**	(1,774)
Total	**8,189**	4,520

(in thousands Rubles)

29. Income Tax

Income tax charge for the years ended December 31, 2006 and 2005 comprised the following:

	2006	2005
Current income tax expense	**799,389**	885,076
Adjustments to current income tax for previous years	**(3,565)**	(3,000)
Deferred income tax expense (income)	**106,767**	(304,275)
Total income tax expense	**902,591**	577,801

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

	2006	2005
Profit before tax	**2,173,197**	1,988,668
Statutory income tax rate	**24%**	24%
Theoretical tax charge at statutory income tax rate	**521,567**	477,280
Increase (decrease) resulting from the effect of:		
Non-taxable income	**(25,837)**	(13,034)
Expenses not deductible for income tax purposes	**406,861**	323,407
Deferred tax asset recognized for defined benefit pension obligation	**-**	(207,428)
Other	**-**	(2,424)
Total income tax charge for the year at the effective rate of 41.5% (2005: 29%)	**902,591**	577,801

In the December 2005 the Company changed terms of agreement with NPF Telecom-Soyuz which maintains the defined benefit pension plan of OAO North-West Telecom. The changes imply that the Company's contributions to non-state pension fund are accounted at employees' personal accounts. Accordingly the Company received a right to deduct such expenses, previously non-deductible, for income tax purposes. Due to this fact in 2005 the Company recognized deferred tax asset in the amount of 207,428 for the defined benefit pension plan obligations maintained by NPF Telecom-Soyuz.

The composition of deferred income tax assets and liabilities as of December 31, 2006 and 2005 and their movement in 2006 was as follows:

	2006	2005
Tax effect of deferred tax assets:		
Accounts payable and accrued expenses	**98,865**	205,544
Accounts receivable	**10,745**	13,725
Finance lease	**41,142**	25,473
Pension liabilities	**263,273**	207,428
Deferred tax assets, total	**414,025**	452,170
Tax effect of deferred tax liabilities:		
Property, plant and equipment	**(1,515,383)**	(1,620,599)
Investments in associates and other investments	**(2,454,774)**	(1,901,358)
Intangible assets	**(209,098)**	(38,816)
Other	**-**	(65)
Deferred tax liabilities, total	**(4,179,255)**	(3,560,838)
Total net deferred tax liabilities (assets)	**(3,765,230)**	(3,108,668)

(in thousands Rubles)

29. Income Tax (continued)

The movement in net deferred tax asset (liability) for the years 2006 and 2005 is presented below:

	2006	2005
Deferred tax assets (liabilities) as of January 1, net	**(3,108,668)**	(2,841,904)
Deferred tax income (expense), recognized in income statement	**(106,767)**	304,275
Deferred tax related to acquired subsidiaries	**2,100**	(2,165)
Deferred tax income (expense) related to change in fair value of investment available-for-sale, recognized in equity	**(551,895)**	(568,874)
Deferred tax assets (liabilities) as of December 31, net	**(3,765,230)**	(3,108,668)

30. Earnings Per Share

The calculation of basic and diluted earnings per preferred and ordinary share is presented below (earnings per share data are stated in Rubles):

	2006	2005
Weighted average number of preference shares outstanding (thousands)	**250,370**	250,370
Weighted average number of ordinary shares outstanding (thousands)	**881,045**	881,045
Adjusted for weighted average number of treasury shares (thousands)	**(5,803)**	(6,813)
Weighted average number of ordinary and preference shares outstanding (thousands)	**1,125,612**	1,124,602
Net income	**1,270,606**	1,410,867
Earnings per share (basic/diluted)	**1,13**	1,25

31. Dividends Declared and Proposed for Distribution

Dividends declared in 2006 based on 2005 results

The annual shareholders' meeting held on June 30, 2007 approved the following dividends based on 2005 results:

Dividends on ordinary shares – 0.265 Rubles per share	233,477
Dividends on preference shares – 0.652 Rubles per share	163,241
	396,718

The number of shares used to compute dividend per share was determined as the number of shares outstanding as of the balance sheet date.

Dividends declared and approved by the annual shareholders' meeting subsequent to year end (Note 37)

Dividend on ordinary shares – 0.357 Rubles per share	314,533
Dividend on preference shares – 0.858 Rubles per share	214,817
	529,350

The number of shares used to compute dividend per share was determined as the number of shares outstanding as of the date of declaration of dividend.

(in thousands Rubles)

31. Dividends Declared and Proposed for Distribution (continued)

Dividends to shareholders are determined by the Board of Directors and officially approved at the annual shareholders' meeting. Earnings available for dividends are limited to the OAO North-West Telecom profits determined in accordance with the federal law "On Joint Stock Companies" and based on financial statements prepared in accordance with the federal law "On Accounting" and Russian accounting and reporting regulations. Dividends for 2006 approved for distribution at the annual shareholders' meeting are reported in Note 37.

32. Operating Lease

As of December 31, 2006 and 2005 minimum lease payments under operating lease agreements were allocated as follows:

	2006	2005
Current portion	**275,658**	171,052
1 to 5 years	**586,594**	205,526
Over 5	**121,986**	-
Total	**984,238**	376,578

The Company's expenses on operating lease recognized in lines "Other Operating Income (Expenses)" and "Services of Telecommunication Operators" of the consolidated income statement totaled, respectively, 204,678 (2005: 225,354) and 256,022 (2005: 203,581) .

	2006	2005
Lease of premises	**131,893**	158,426
Lease of channels from domestic operators	**192,288**	126,200
Lease of other assets	**72,785**	66,928
Lease of channels from OAO Rostelecom	**63,734**	77,381
Total	**460,700**	428,935

33. Contingencies and Operating Risks

Operating Environment of the Company

Whilst there have been improvements in the Russian economic situation, such as an increase in gross domestic product and a reduced rate of inflation, Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

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 unfavorable outcome. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

33. Contingencies and Operating Risks (continued)

Taxation (continued)

As of December 31, 2006 management believes that its interpretation of the relevant legislation is appropriate and that the Company's tax, currency and customs positions will be sustained.

Litigations, Claims and Assessments

Management is unable to estimate what developments may occur in respect of 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 foreseeable future the Company's operations may be affected by the implications of judicial reform. The financial statements do not include any adjustment that may result from these uncertainties.

During the year, the Company was party to 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 or 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.

The only exception to the above is a legal action currently heard in Moscow Arbitration Court brought by OAO North-West Telecom against the Decision of December 8, 2006 to hold the taxpayer (charge payer, tax agent) liable for a tax offense. The Decision was made by the Interregional Inspectorate for Major Taxpayers of the Federal Tax Service of Russia based on the findings of a field tax audit of OAO North-West Telecom for years 2003-2004. Following the tax audit, OAO North-West Telecom was charged additional taxes of 437,222, late payment interest of 77,345, and penalty of 70,165. Additional taxes, interest and penalties charged as a result of the tax audit totaled 584,732. In addition, the tax inspectorate decreased the overstated tax liability by 7,832.

The tax authority charged additional taxes due to alleged errors in calculating doubtful debt provision (compensation for reduced rates applied to certain groups of customers): the tax authority ruled that there were no grounds to classify the receivables as doubtful or bad debt. The total amount of taxes charged by the tax authority on these grounds is 203,121. In addition, OAO North-West Telecom was charged additional taxes in relation to settlements between OAO North-West Telecom and OAO Rostelecom at the Integral Settlement Rate in the period from January 1, 2003 through August 1, 2003 and for absence of settlements for termination of international traffic (free provision of services). The total amount of taxes charged by the tax authority on these grounds is 141,501.

The Company believes that the tax authority had no legal grounds to charge additional taxes, late payment interest and penalties. Thus, as of December 31, 2006 the Company did not accrue provision for contingent liability related to litigations with tax authority. Upon considering the OAO North-West Telecom's application, on July 2, 2007 Moscow Arbitration Court ruled in favor of the Company (Note 37).

Changes in Industry Legislation

New industry provisions under the Federal Law "On Communications" which came into force during 2006 had significant impact on Company's financial position and results of operations. These new industry pronouncements significantly changed the Company's relationships with interconnected operators and long-distance providers, including OAO Rostelecom. During 2006 the Company carried out a campaign of renegotiation of contracts with interconnected operators and long-distance providers. The purpose of contracts renegotiation was to bring the terms of interconnection contracts in compliance with the new industry regulations.

33. Contingencies and Operating Risks (continued)

Changes in Industry Legislation (continued)

Due to the fact that the significant part of the new industry regulations became effective on January 1, 2006 the legal practice regarding application of these provisions is not yet developed. As a result, a disagreement in interpretations of the new provisions by the Company and by the regulator may possibly occur. The management believes that as of December 31, 2006 respective industry regulations are correctly interpreted by the Company and that existing uncertainty in interpretation of new industry provisions will not have a significant impact on the Company's financial position and results of operations in subsequent periods.

Licenses

The Company's major revenues are derived from financial and economic activity carried out in accordance with licenses issued by the Ministry of the Russian Federation on telecommunication and informatization. Main operational licenses and supplementary licenses expire during the period from 2007 to 2029. Management believes that there are no grounds for non-prolongation of existing licenses, suspension or extinguishment of any of the licenses.

Suspension of main operational licenses of the Company or non-prolongation of some or all of licenses may have an adverse effect on the financial results of the Company.

It is also known that the government of the Russian Federation plans to strengthen competition in telecommunication, for the reason of which it may issue additional licenses for national and international long distance telephony services to other operators. At the present time it is impossible to predict consequences, if any, of such changes on the Company's financial and economic activity.

Insurance Coverage

During 2006, the Company did not maintain insurance coverage on a significant part of their property, plant and equipment asset bases, business interruption, or third party liability in respect of property or environmental damage arising from accidents on the Company's property or relating to the Company's operations. Until the Company obtains adequate insurance coverage, there is a risk that the loss of destruction of certain assets could have a material adverse effect on the Company's operation and financial position.

Guarantees and Sureties

As of December 31, 2006 the Company stood as guarantor on two loan facilities provided by Sberbank to ZAO RTK-Leasing, a lessor of telecommunication equipment. The guaranteed obligation totaled 702,072 (2005: 693,993). Company's management believes that the probability of occurrence of the guaranteed event is remote.

34. Contractual Commitments

Capital Investments

As of December 31, 2006 and 2005 the Company had commitments for capital investments into modernization and expansion of its network in the amount of approximately 621,869 and 22,918, respectively.

Acquisition of Property, Plant and Equipment

As of December 31, 2006 and 2005 the Company had contractual commitments to acquire property, plant and equipment of 86,472 and 11,739, respectively.

(in thousands Rubles)

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, 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 as of December 31, 2006 are detailed below.

Sales of Products, Services, Other Assets

During 2006 and 2005 the Company rendered services to the following related parties:

Related party	Type of sale	Price determination method	2006	2005
OAO Rostelecom (a Svyazinvest Group company)	Communication services	Normal commercial terms	**3,275,634**	819,018
Other Svyazinvest Group companies	Communication services	Normal commercial terms	**3,397**	41,389
Telecominvest Group companies	Communication services, rental services	Normal commercial terms	**722,774**	668,138
ZAO WestBaltTelecom	Communication services	Normal commercial terms	**3,353**	6,758
SZAO Medexpress	Staff insurance services	Normal commercial terms	**1,019**	1,329
Others		Normal commercial terms	**5,715**	2,202
Total			**4,011,892**	1,538,834

Purchases

In 2006 and 2005 the Company purchased goods, products, property, plant and equipment and other assets from the following related parties:

Related party	Type of sale	Price determination method	2006	2005
OAO Rostelecom (a Svyazinvest Group company)	Communication services	Normal commercial terms	**135,228**	2,864,008
Non-Commercial Partnership (a Svyazinvest Group company)	Communication services, information services, advertising	Normal commercial terms	**130,000**	144,099
Other Svyazinvest Group companies	Communication services, information services, advertising	Normal commercial terms	**-**	48,653
Telecominvest Group companies	Communication services, rental services, charitable activity	Normal commercial terms	**645,601**	677,771
ZAO WestBaltTelecom	Communication services	Normal commercial terms	**27,486**	-
SZAO Medexpress	Staff insurance services	Normal commercial terms	**34,222**	75,657
Others		Normal commercial terms	**59,668**	63,916
Total			**1,032,205**	3,874,104

(in thousands Rubles)

35. Balances and Transactions with Related Parties (continued)

Accounts Receivable

As of December 31, 2006 and 2005 balances of accounts receivable from related parties were as follows:

Related party	Type of receivable	Price determination method	2006	2005
OAO Rostelecom (a Svyazinvest Group company)	Communication services	Normal commercial terms	**287,067**	2,469
Other Svyazinvest Group companies	Communication services	Normal commercial terms	**106,367**	247,996
Telecominvest Group companies	Communication services, rental services	Normal commercial terms	**52,370**	67,051
ZAO WestBaltTelecom	Communication services	Normal commercial terms	**690**	-
SZAO Medexpress	Staff insurance services	Normal commercial terms	**2,792**	-
Others		Normal commercial terms	**4,435**	855
Total			**453,721**	318,371

Accounts Payable

As of December 31, 2006 and 2005 balances of accounts payable to related parties were as follows:

Related party	Type of payable	Price determination method	2006	2005
OAO Rostelecom (a Svyazinvest Group company)	Communication services	Normal commercial terms	**421,361**	146,282
Telecominvest Group companies	Communication services, rental services	Normal commercial terms	**163,549**	88,125
ZAO WestBaltTelecom	Communication services	Normal commercial terms	**3,159**	-
SZAO Medexpress	Staff Insurance services	Normal commercial terms	**9,544**	9,418
Others		Normal commercial terms	**15,629**	3,213
Total			**613,242**	247,038

OAO Svyazinvest

The Company's parent entity - OAO Svyazinvest - was wholly owned by the Russian Government until July 1997 when the Government sold 25% plus one share of the Charter Capital of OAO 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 OAO Svyazinvest and its subsidiaries.

The Government's influence is not confined to its share holdings in OAO 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.

35. Balances and Transactions with Related Parties (continued)

OAO Rostelecom

OAO Rostelecom, a majority-owned subsidiary of OAO Svyazinvest, is the primary provider of domestic long distance and international telecommunications services in the Russian Federation. The annual expense associated with OAO Rostelecom relates to outgoing traffic of the Company and terminated outside the Company’s network. This expense is included in expenses associated with national long-distance/ international traffic transmission. Further, OAO Rostelecom uses the Company’s network to provide incoming long-distance and international traffic to its subscribers and partner operators.

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 typically lease communication channels at lower rates than those fixed by the Ministry of Antimonopoly Policies for 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.

In the course of its normal activities, the Company enters in transactions with other entities under direct or indirect control of the state.

The Company does not conduct its business or any segments thereof through entities under direct or indirect control of the state.

The Company enters into transactions with entities under direct or indirect control of the state solely on an arm’s length basis.

Entities under direct or indirect control of the state do not affect the Company’s transactions with other entities.

By virtue of the RF Government decrees, the Company is not allowed to disconnect certain entities that have a strategic importance for the state. Rates applied to such customers are also set by the state regulator, however their level is identical to that applied to commercial customers.

(in thousands Rubles)

35. Balances and Transactions with Related Parties (continued)

Transactions with Government Organizations (continued)

In years ended December 31, 2006 and 2005 significant operations between the Company and the Government or entities controlled by Government were as follows:

	December 31, 2006		2006	
Type of operation	**Accounts receivable**	**Accounts payable**	**Income**	**Expense**
Communication services	**105,356**	**104,599**	**8,386,054**	**-**
Interconnection and traffic transmission services	**19,809**	**65**	**63,440**	**-**
Other services, core activity	**979**	**422**	**14,709**	**-**
Other income	**11,564**	**996**	**1,230,539**	**-**
Electricity and heat supply	**3,087**	**13,342**	**-**	**338,200**
Rental expenses	**3,374**	**2,694**	**-**	**157,437**
Other expenses	**8,112**	**65,034**	**-**	**556,619**
Lending costs	**-**	**352**	**-**	**16,253**

	December 31, 2005		2005	
Type of operation	**Accounts receivable**	**Accounts payable**	**Income**	**Expense**
Communication services	115,213	95,613	6,171,979	-
Interconnection and traffic transmission services	310	3	17,965	-
Other services, core activity	3,779	1,548	32,822	-
Other income	9,008	528	105,898	-
Electricity and heat supply	2,694	17,198	-	266,084
Rental expenses	1,810	847	-	131,772
Other expenses	4,688	20,928	-	299,873
Lending costs	272	100	-	16,525

Government subscribers accounted for approximately 9% of total accounts receivable as of December 31, 2006 (2005: 8%). Amounts outstanding from government subscribers as of December 31, 2006 amounted to 152,282 (2005: 137,772).

Other income in 2006 comprises income from services provided to OAO Rostelecom according to the assistance agreement in the amount of 883,712 (2005: 0).

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

Non-Commercial Partnership Center for Research of the Problems in Development of Telecommunications (hereinafter the Partnership) is a related party of OAO Svyazinvest. The Company has an agreement with the Partnership, under which it provides financing for the latter to implement mutually beneficial project on behalf of the Company and other subsidiaries and associates of OAO Svyazinvest. Payments to the Partnership included in other operating expenses in the accompanying consolidated income statement for the year ended December 31, 2006 amounted to 130,000 (2005: 144,099).

Non-government Pension Fund Telecom-Soyuz

The Company signed a number of pension agreements with NPF Telecom-Soyuz (Note 24), a related party of OAO Svyazinvest. Total contributions into the fund in 2006 amounted to 85,386 (2005: 258,525).

35. Balances and Transactions with Related Parties (continued)

Compensation to Key Management Personnel

Key management personnel comprise members of Management Board and Board of Directors of the Company, totaling 20 as of December 31, 2006 and 22 as of December 31, 2005. Total compensation to key management personnel included in the income statement within "Wages, Salaries, Other Benefits and Payroll Taxes" for year ended December 31, 2006 amounted to 41,231 (2005: 41,094).

Compensation to key management personnel consists of contractual salary, performance bonus depending on operating results and payments for non-government pension benefits.

36. Financial Instruments

The Company's principal financial instruments comprise bank loans, finance leases and cash and short-term deposits. The main purpose of these instruments is to raise finance for the Company's operations. The Company has other financial assets and liabilities such as trade receivables and trade payables, which arise directly from its operations.

Foreign exchange risk

Foreign exchange risk is the risk that fluctuations in exchange rates will adversely affect the Company's financial results. Liabilities denominated in foreign currencies (Notes 20, 21, 22) give rise to foreign exchange exposure.

A significant proportion of the Company's borrowings is denominated in US Dollars and Euro, whereas income and expenses are denominated in Russian Rubles. Accordingly, any increase in the Ruble to US Dollar or Euro exchange rate may have an adverse impact on the operating income of the Company. A potential decrease in the Ruble exchange rate will lead to an increase in the actual borrowing costs for the Company and obstruct raising debt financing, including that required to refinance the existing debt.

The Central Bank of Russia has established rigid currency regulation rules to stimulate the commercial use of the Ruble. These rules impose restrictions on conversion of the Ruble into a hard currency and establish requirements as to the conversion of currency revenues into Rubles.

The Company is generally exposed to foreign exchange risk with respect to liabilities denominated in foreign currencies. As of December 31, 2006 the Company had currency-denominated liabilities of 2,235,346 (2005: 2,294,617), including liabilities denominated in US Dollars of 214,174 (2005: 287,864); and Euro-denominated liabilities of 2,021,172 (2005: 2,006,753).

Over the period from January 1, 2006 through December 31, 2006 the Ruble increased by approximately 8.5% in relation to the US Dollar and decreased by 1.5% in relation to the Euro.

Liquidity Risk

The Company monitors its risk of a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial investments and financial assets (e.g. accounts receivables, other financial assets) and projected cash flows from operations. The Company's objective is to maintain a balance between continuity of funding and flexibility through the use of bank overdrafts, bank loans, bonds, finance leases. 26% of the Company's debt will mature in less than one year at December 31, 2006 (2005: 23%) based on the balances reflected in the financial statements.

(in thousands Rubles)

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.

Interest rate risk mainly relates to debt instruments with floating interest rate denominated mainly in US Dollar, Japanese Yen and Euro. As of December 31, 2006 approximately 17% (2005: 17%) of total borrowings were obtained with floating interest rate attached to them.

As of December 31, 2006 the outstanding liabilities of the Company were 9,903,212 (2005: 10,055,333), of which approximately 1,715,650 (2005: 1,723,468) were obtained by the Company at a floating rate. The floating rate payable is generally determined based on the European Interbank Offered Rate (EURIBOR).

The following table presents the Company's financial instruments that are exposed to interest rate risk as of December 31, 2006 and 2005:

	< 1 year	1 - 5 years	> 5 years	Total
As of December 31, 2006				
Fixed rate				
Short-term obligations	81,531	-	-	81,531
Long-term obligations	1,185,589	6,604,704	9,116	7,799,409
Finance lease obligations	169,889	136,733	-	306,622
Floating rate				
Short-term obligations	-	-	-	-
Long-term obligations	751,858	963,792	-	1,715,650

	< 1 year	1 - 5 years	> 5 years	Total
As of December 31, 2005				
Fixed rate				
Short-term obligations	593,973	-	-	593,973
Long-term obligations	764,118	6,422,490	59,947	7,246,555
Finance lease obligations	189,216	302,121	-	491,337
Floating rate				
Short-term obligations	1,705	-	-	1,705
Long-term obligations	26,762	1,695,001	-	1,721,763

Credit Risk

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

Financial assets, which potentially subject the Company 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. 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, 2006 there is no significant risk of loss to the Company beyond the provision already recorded.

(in thousands Rubles)

36. Financial Instruments (continued)

Credit Risk (continued)

Financial instruments which potentially subject the Company to a concentration of credit risk consist principally of trade and other accounts receivable. Credit risk associated with these assets is limited due to significance of the Company's client base and regular monitoring procedures over customers' and other debtors' ability to pay debts.

The Company places spare cash on deposits with a number of Russian commercial financial institutions. To manage credit risk the Company places spare cash in different financial institutions, and the Company's management analyzes risk of default of these financial institutions on a regular basis.

Hedging

Given that in December 2005 the Company obtained a syndicated loan of 50,000 thousand Euro, and, accordingly, certain expenses and liabilities of the Company are foreign currency-denominated, a change in the exchange rate of Euro to Ruble may result in a significant increase in the Ruble equivalent of expenses related to the liabilities.

In accordance with the Company's currency policies, risks associated with material currency transactions are hedged. To hedge against risks related to changes in the exchange rate of Euro to Ruble to the extent they affect the discharge of liabilities under the syndicated loan agreement, in September 2006, the Company entered into a forward currency contract for a gross amount of Euro 11,759 thousand to be received in exchange for 408,417 thousand Rubles. The forward currency contract was classified as an instrument to hedge spot exchange rate risk related to the expected future cash flows from the Company's outstanding Euro-denominated loans. The instrument was used to hedge 20% (or 10,000 thousand Euro) of foreign exchange risk attributable to the principal amount of the loan and certain interest amounts calculated at the fixed portion of interest rate (bank margin of 2%).

Net Outstanding Liability under the Syndicated Loan

	2006 (thousands Euro)
Outstanding balance of syndicated loan	**50,000**
Hedged portion of the principal amount	**(10,000)**
Net amount outstanding (open currency position)	**40,000**

To measure foreign exchange risks associated with changes in the exchange rate of Euro to Ruble, the Company estimates potential losses that may result from adverse changes in market indicators based on prior year exchange rate behavior. The volatility index for Euro to Ruble exchange rate is determined based on daily rates for the year.

In the event of a 2.5% change (increase) in the exchange rate, the effect on the income statement in money terms will be 34,000.

Upward/downward adjustment to the Euro/Ruble exchange rate	Effect on income before taxation
2.5%	(34,000)
-2.5%	34,000

The hedged cash flows relate to the following past or future accounting periods:

Year	Amount (thousands Euro)
2006	519
2007	5,281
2008	4,838
2009	1,121

(in thousands Rubles)

36. Financial Instruments (continued)

Net Outstanding Liability under the Syndicated Loan (continued)

The cash flows relate to outstanding loans and the hedged risks and, as such, affect the profit or loss for the period in which the movement in the exchange rate took place. Accordingly, the amounts were not deferred or excluded from the hedging reserve in equity.

As of December 31, 2006, the fair value of the forward contract classified as hedge was 3,555 including 4,115 classified as ineffective portion of the hedge and included in other operating expenses, and 560 classified as effective portion of the hedge included in the currency exchange gain/loss as compensation for the respective exchange loss on the outstanding loan.

Fair Value of Financial Instruments

	2006		2005	
Type of instrument	**Net book value**	**Fair value**	**Net book value, as restated** *(See Note 2)*	**Fair value, as restated** *(See Note 2)*
Financial assets				
Investments in associates	**98,192**	**98,192**	92,215	92,215
Long term investments available for sale	**10,239,203**	**10,239,203**	7,947,455	7,947,455
Long-term accounts receivable	**11,645**	**11,645**	8,434	8,434
Long-term loans given	**23,215**	**23,215**	25,180	25,180
Accounts receivable	**1,336,905**	**1,336,905**	1,181,806	1,181,806
Short-term investments held to maturity	**-**	**-**	1,042,626	1,042,626
Cash and cash equivalents	**244,491**	**244,491**	152,091	152,091
Total	**11,953,651**	**11,953,651**	10,449,807	10,449,807
Financial liabilities				
Long-term bank and corporate loans	**2,571,598**	**2,571,598**	4,061,291	4,061,291
Long-term bond issues	**4,983,140**	**5,073,400**	4,029,068	4,130,115
Long-term promissory notes	**7,800**	**7,800**	28,239	28,239
Long-term vendor financing	**15,073**	**15,073**	58,840	58,840
Long-term obligations under finance lease	**136,733**	**136,733**	302,121	302,121
Accounts payable	**2,913,267**	**2,913,267**	2,470,909	2,470,909
Short-term bank and corporate loans	**81,531**	**81,531**	595,678	595,678
Short-term portion of bank and corporate loans	**823,941**	**823,941**	16,241	16,241
Short-term portion of bond issues	**1,048,921**	**1,049,475**	450,000	445,635
Short-term portion of promissory notes	**20,522**	**20,522**	15,704	15,704
Short-term portion of vendor financing	**44,064**	**44,064**	310,024	310,024
Short-term portion of obligations under finance lease	**169,889**	**169,889**	189,216	189,216
Total	**12,816,479**	**12,907,293**	12,527,331	12,624,013

Fair value of a financial instrument is the amount for which an asset could be exchanged, or 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. Balance sheet items denominated in foreign currency have been translated into Rubles using the corresponding exchange rate prevailing at the reporting date.

37. Subsequent Events

Acquisitions

Pursuant to the Board of Directors' decision (Minutes No. 19-01/30 (06) of November 3, 2006), in January 2007 the Company purchased 61,920 certified ordinary shares in ZAO PTT for 2,571,227. The related transaction costs totaled 1,004. The shares were acquired to take full control of the company. The entry in the Shareholders' Register supporting the transfer of ownership of the securities was made on January 22, 2007.

Sale of Investments

In July 2007 the Company's Board of Directors (Minutes No. 19-01/17 (07) of July 9, 2007) has approved the sale of the Company's 15% stake in OAO Telecominvest comprising 2,449,990 shares with par value of 10 Rubles each. The selling price of the stake is 410,000 thousand US Dollars. The buyer is Renaissance Capital represented by OOO AF Telecom Holding. The stake is being sold as part of the framework subsidiary/associate management strategy: the minority shareholding was insufficient for the Company to exercise a significant influence on the OAO Telecominvest operations, specifically, on making decisions on dividend distribution. The transaction is expected to be closed within three months from the date of approval by the Board of Directors.

Litigation

On July 2, 2007 Moscow Arbitration Court ruled invalid the Decision of December 8, 2006 to hold the taxpayer liable for a tax offense (Note 33).

To date, the court decision has been announced, but not yet documented. The Company's claim was partially satisfied: specifically, the Company's claim for cancellation of the decision in respect of settlements between OAO North-West Telecom and OAO Rostelecom has been dismissed. As for the rest, the court decision is in favor of the Company. The Company believes that the tax authority had no legal grounds to charge additional taxes, late payment interest and penalties, so, it intends to appeal against the dismissal of its claim with respect to episodes related to settlements between OAO North-West Telecom and OAO Rostelecom.

Dividends

Annual dividend per share has been approved at the Company's Annual Shareholders' Meeting on June 22, 2007. the Company's Board proposed that the Board of Directors recommend that the Annual Shareholders' Meeting approve dividend for 2006 of 0.357 Rubles per ordinary share and 0.858 Rubles per preference share (2005: 0.265 Rubles and 0.652 Rubles, respectively), which amounted to 529,350 (2005: 396,718). Following the approval, annual dividend payable to shareholders will be recognized in the 2007 financial statements (Note 31).

37. Subsequent Events (continued)

Settlements with OAO Rostelecom

From January 1, 2007, the Company’s payment arrangements with OAO Rostelecom network, has been changed as stipulated by interconnection agreement due to amendments to Russia tax legislation.

Federal Law No.119-FZ dated July 22, 2005 introduced amendments to the Tax Code effective from January 1, 2007. According to these amendments new rules of VAT offset for non-cash settlements (including settlements using mutual offsets) are set. VAT may be offset only after actual payments of the tax to supplier.

As a result, starting January 1, 2007 settlements between OAO Rostelecom and the Company will be performed in cash without the offset of mutual payables and receivables.

Changes in Industry Legislation

Federal Law No.14-FZ dated February 9, 2007 introduced amendments to Federal Law No.126-FZ “On Telecommunications” dated July 7, 2003. The amendments are effective July, 2007 and comprise the following:

- Mandatory assessment of the conformity of the operator’s communication network to the industry requirements. Such assessment shall be made in the form of an expert examination in accordance with the rules established by the Government of the Russian Federation;
- Registration of operator’s communication networks as a part of a public-use communication network in accordance with rules established by the Government of the Russian Federation.

Communication networks put in operation before the date when these provisions of the Federal Law “On Communications” came into force have to be registered in accordance with the requirements of these provisions by January 1, 2010.

The Company can not reliably measure the effects of these changes on the financial position and results of operations of the Company as the procedures of the mandatory expertise and registration of the networks has not yet been elaborated and approved by the Government of the Russian Federation.

New Tariffs for Telecommunication Services

Pursuant to the Order No.262-s/3 of the Federal Tariff Service of Russia, dated November 14, 2006 from February 1, 2007 new tariffs for local, intra-regional telecommunication services and as well as compensatory allowance on local and intra-regional call initiation in the amount of 0.38 Rubles per minute, were introduced in the North-West region of the Russian Federation.

Monthly payment for local telephone communication services will be comprised of mandatory payments for “Provision of Subscriber’s Line for Permanent Use” and “Provision of Local Telephone Connection Services” (under one of the payment schemes selected).

In accordance with Order No.262-s/3 the Company should introduce following tariff plans effective February 1, 2007:
- For individual subscribers: three obligatory tariff plans (with time-based, fixed and combined fees) and two additional tariff plans (with combined fee);
- For corporate subscribers: one obligatory tariff plan (with time-based fee) and three additional tariff plans (with time-based and combined fees).

Tariff plan on fixed fee terms is primarily aimed at subscribers who make many calls. This tariff plan provides to subscribers unlimited amount of minutes per month for a fixed monthly fee.

(in thousands Rubles)

37. Subsequent Events (continued)

New Tariffs for Telecommunication Services (continued)

The tariff plan with time-based fee stipulates payments for each minute of calls.

The tariff plan with combined fee defines a limited monthly number of minutes provided for a fixed fee and the excess of subscriber's calls over the monthly limit is billed at a reduced per minute price.

The above mentioned tariff plans are introduced in municipalities where technical capabilities for capturing call duration data exist. If these capabilities are absent, subscribers are offered fixed fees at tariffs set by the Federal Service on Tariffs which are effective from February 1, 2007.

Universal Telecommunication Services

In February 2007 the Company won the tenders of the Federal Communication Agency for the right to render universal telecommunication services in the territory of Leningrad and Novgorod regions.

According to the tender terms, the Company is to install 3,432 payphones for rendering universal services in the territory of 3,393 localities in the above regions.

The tariff for local calls in Leningrad Region is set at 0.48 Rubles per minute, in Novgorod Region – 0.45 Rubles per minute.

As of July 16, 2007 the Company has won the tenders for the right to render universal telecommunication services in Arkhangelsk and Kaliningrad regions (March 2006); Komi Republic, Nenets Autonomous District and Vologda Region (December 2006); Karelia Republic, Murmansk and Pskov regions (January 2007); Leningrad and Novgorod regions (February 2007).

The total amount of compensation of losses from the provision of universal telecommunication services as per the tender proposal is 2,519,447. The proposed investment is 5,315,348.

The table below summarizes the above data by area:

Area	Tender date	Services start date	Number of payphones (pcs.)	Investment	Compensation
Arkhangelsk Region	24.03.06	24.09.06	2,874	536,413	401,225
Kaliningrad Region	24.03.06	24.09.06	572	52,258	52,594
Komi Republic	21.12.06	21.06.07	616	460,000	146,033
Vologda Region	21.12.06	21.06.07	3,218	1,116,704	501,049
Nenets AD	21.12.06	21.06.07	43	66,788	62,937
Karelia Republic	18.01.07	18.07.07	662	568,329	203,996
Murmansk Region	18.01.07	18.07.07	166	497,749	118,831
Pskov Region	18.01.07	18.07.07	3,105	762,884	294,216
Novgorod Region	15.02.07	15.08.07	1,832	681,084	297,625
Leningrad Region	15.02.07	15.08.07	1,600	573,139	440,941
Total			**14,688**	**5,315,348**	**2,519,447**

37. Subsequent Events (continued)

Sale of OAO North-West Telecom Shares

On March 15, 2007 the St. Petersburg and Leningrad Regional branch of the Russian Federal Property Fund started an auction to sell the state-owned stake in OAO North-West Telecom. 3.337% of equity shares in the Company were put on auction including 37,753,619 ordinary shares and 5,276 preference shares.

The auction was open to all interested bidders and was set up as open bids. Bids were admitted in the period from December 29, 2006 through March 12, 2007. The opening price for the stake was 1,124,117. The successful bidder was OOO Investment Finance Company Metropol, with a bid price of 1,544,117.

Loan Agreements

During the period from January 1, 2007 to date the Company has entered into the following unsecured revolving credit line agreements with the North-West Bank of AKB Sberbank RF (OAO) for the total amount of 625,000:

– April 27, 2007: revolving credit line for 315,000. The ultimate maturity date is August 24, 2007. Interest rate is established at 6.3% p. a.

– May 17, 2007: revolving credit line for 310,000. The ultimate maturity date is September 13, 2007. Interest rate is established at 6.3% p. a.

Significant Transactions Involving Acquisition of Assets

In July 2007, the Company entered into a service agreement for 416,429 with OAO Informatsionnye Technologii Svyazi (related party, a Svyazinvest Group company) in the context of regional work to implement Oracle E Business Suite.