

OJSC “Tattelecom”

Financial Statements

For the Year Ended 31 December 2007

OJSC "TATTELECOM"

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OJSC "TATTELECOM"

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the independent auditors' report set out on pages 2-3, is made with a view to distinguish the respective responsibilities of management and those of the independent auditors in relation to the financial statements of OJSC "Tattelecom" (the "Company").

Management is responsible for the preparation of the financial statements that present fairly in all material respects the financial position of the Company at 31 December 2007, the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

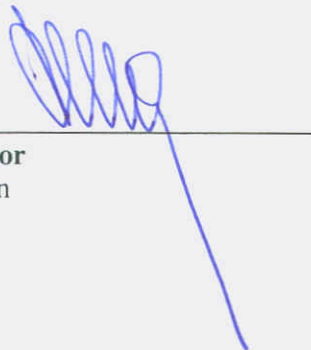
In preparing the financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether IFRS have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Preparing the financial statements on a going concern basis, unless it is inappropriate to presume that the Company will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Company;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Company, and which enable them to ensure that the financial statements of the Company comply with IFRS;
- Maintaining proper accounting records in compliance with legislation and accounting standards of the Russian Federation;
- Taking such steps as are reasonably available to them to safeguard the assets of the Company; and
- Preventing and detecting fraud, errors and other financial irregularities.

The financial statements for the year ended 31 December 2007 were authorized for issue on 15 May 2008 by:



General Director
L.N.Shafigoullin

INDEPENDENT AUDITORS' REPORT

To the Shareholders of OJSC "Tattelecom":

We have audited the accompanying financial statements of Open Joint Stock Company "Tattelecom" ("Tattelecom" or the "Company"), which comprise the balance sheet as of 31 December 2007, and the related statements of income, changes in equity and cash flows 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 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 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.

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 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 accompanying financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2007, and its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards.

Deloitte & Touche

Moscow
15 May 2008

OJSC "TATTELECOM"

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2007 *(in US Dollars and in thousands)*

	Notes	<u>2007</u>	<u>2006</u>
REVENUE	7	193,335	143,593
OPERATING EXPENSES	8	<u>(147,009)</u>	<u>(109,875)</u>
OPERATING PROFIT		46,326	33,718
Interest expense		(5,415)	(1,102)
Interest income		65	19
Foreign exchange gain		<u>5</u>	<u>22</u>
PROFIT BEFORE INCOME TAX		40,981	32,657
INCOME TAX	20	<u>(10,449)</u>	<u>(7,779)</u>
NET INCOME		<u>30,532</u>	<u>24,878</u>

The notes on pages 9 to 36 form an integral part of these financial statements.

OJSC "TATTELECOM"

BALANCE SHEET AS OF 31 DECEMBER 2007 (in US Dollars and in thousands)

	Notes	2007	2006
ASSETS			
LONG-TERM ASSETS:			
Property, plant and equipment	9	377,979	281,232
Intangible assets	10	752	937
Long-term investments	11	1,149	433
Other long-term assets	12	13,554	4,060
		393,434	286,662
CURRENT ASSETS:			
Inventories	13	5,536	3,846
Trade accounts receivable	14	24,909	14,052
Other accounts receivable	15	4,956	5,232
Prepaid income tax		35	761
Prepaid taxes, other than income tax		7,942	1,788
Short-term financial investments	11	510	124
Cash	16	5,305	4,300
		49,193	30,103
TOTAL ASSETS		442,627	316,765
EQUITY AND LIABILITIES			
EQUITY:			
Common shares	17	75,852	75,852
Treasury shares		(2,987)	(2,987)
Cumulative translation reserve		22,809	8,596
Retained earnings		111,020	88,695
		206,694	170,156
LONG-TERM LIABILITIES:			
Long-term borrowings	18	35,528	25,390
Long-term obligations under finance lease	19	1,627	217
Deferred tax liabilities	20	10,680	11,364
Deferred revenue	21	31,623	31,172
Post-retirement benefit obligations	22	4,796	3,953
Fixed assets granted	23	7,329	9,130
Other long-term liabilities		2,055	2,183
		93,638	83,409
CURRENT LIABILITIES:			
Current portion of long-term borrowings	18	83,270	29,194
Short-term obligations under finance lease	19	1,263	647
Trade accounts payable	24	38,144	14,134
Taxes payable		1,977	1,861
Other accounts payable	25	10,429	11,271
Deferred revenue, current portion	21	7,212	6,093
		142,295	63,200
TOTAL EQUITY AND LIABILITIES		442,627	316,765

The notes on pages 9 to 36 form an integral part of these financial statements.

OJSC "TATTELECOM"

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2007 (in US Dollars and in thousands)

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Income before tax	40,981	32,657
Adjustments for:		
Depreciation of property, plant and equipment	26,152	19,854
Amortization of intangible assets	1,075	632
(Gain)/ loss on disposal of property, plant and equipment	(1,377)	4,367
Interest income	(65)	(19)
Interest expense	5,415	1,102
Increase in allowance for doubtful receivables	5,372	422
Increase in tax provision	29	292
Increase in allowance for obsolete inventory	161	55
Impairment of other non-current assets	474	-
Depreciation of fixed assets granted	(471)	(755)
Foreign exchange gain	(5)	(22)
Operating cash inflow before changes in working capital:	<u>77,741</u>	<u>58,585</u>
Trade receivables	(14,811)	(6,742)
Inventory	(1,514)	(1,553)
Other accounts receivable	629	4,169
Trade accounts payable	21,781	1,398
Other accounts payable	(1,594)	4,170
Taxes payable	(5,014)	(1,734)
Post-retirement benefit obligations	533	327
Deferred revenue	(1,094)	(384)
Cash inflow from operating activities	<u>76,657</u>	<u>58,236</u>
Income taxes paid	(9,992)	(10,623)
Interest paid	(5,047)	(5,678)
Net cash provided by operating activities	<u>61,618</u>	<u>41,935</u>
CASH FLOW FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(103,027)	(40,053)
Purchases of intangible assets	(831)	(851)
Proceeds from sale of property, plant and equipment	504	133
Interest received	65	19
Proceeds from sale of promissory notes and other financial assets	-	181
Purchases of long-term financial investments	(2,773)	-
Net cash used in investing activities	<u>(106,062)</u>	<u>(40,571)</u>

OJSC "TATTELECOM"

STATEMENT OF CASH FLOWS (CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2007
(in US Dollars and in thousands)

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings	162,863	29,371
Repayment of borrowings	(105,544)	(26,128)
Finance lease payments	(3,536)	(1,788)
Dividends paid	(8,016)	(3,021)
Net cash provided by /(used in) financing activities	<u>45,767</u>	<u>(1,566)</u>
NET INCREASE/(DECREASE) IN CASH	1,323	(202)
Effect of exchange rate changes on cash	(318)	19
CASH, beginning of the year	4,300	4,483
CASH, end of the year	<u>5,305</u>	<u>4,300</u>
SUPPLEMENTAL INFORMATION		
Non-cash activities:		
Fixed assets granted	945	109
Fixed assets acquired under finance lease	3,289	805

The notes on pages 9 to 36 form an integral part of these financial statements.

OJSC "TATTELECOM"

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2007 (in US Dollars and in thousands)

	Common shares	Treasury shares	Cumulative translation reserve	Retained earnings	Total
At 1 January 2006	75,852	-	(4,875)	66,838	137,815
Effect of translation to presentation currency	-	-	13,471	-	13,471
Net income	-	-	-	24,878	24,878
Total income and expenses recognized during the year	-	-	13,471	24,878	38,349
Dividends	-	-	-	(3,021)	(3,021)
Acquisition of treasury shares from minority shareholders	-	(2,987)	-	-	(2,987)
At 31 December 2006	75,852	(2,987)	8,596	88,695	170,156
Effect of translation to presentation currency	-	-	14,213	-	14,213
Net income	-	-	-	30,532	30,532
Total income and expenses recognized during the year	-	-	14,213	30,532	44,745
Dividends	-	-	-	(8,207)	(8,207)
At 31 December 2007	75,852	(2,987)	22,809	111,020	206,694

The notes on pages 9 to 36 form an integral part of these financial statements.

OJSC "TATTELECOM"

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

1. NATURE OF BUSINESS

OJSC "Tattelecom" ("Tattelecom" or the "Company") is the largest telecommunications operator in the Republic of Tatarstan, the region of the Russian Federation. OJSC "Tattelecom" was established on 22 July 2003 as a result of privatization of State Unitary Enterprise for Communications Management (GUP UES) "Tattelecom" pursuant to Resolution of the Cabinet of Ministers of the Republic of Tatarstan No. 350 as of 2 July 2003 and Resolution of the Ministry of Land and Property Relations of the Republic of Tatarstan No. 87 as of 8 July 2003. The Company has a head office and 7 branches: Almetyevsky, Arsky, Buisky, Nizhnekamsky, Chistopolsky, Kazansky and Naberezhno-Chelninsky zonal telecommunication nodes. The Company's head office is located at 57 N. Ershova street, 420061, Kazan, Republic of Tatarstan, Russian Federation.

Reorganization – In the second quarter of 2006, OJSC "Svyazinvestneftekhim", a controlling shareholder of OJSC "Tattelecom" and OJSC "Kazan City Telephone Network" ("KGTS"), completed the Company's reorganization through OJSC "KGTS" merger by OJSC "Tattelecom" (collectively – the "Group"). In the course of reorganization the share capital of OJSC "Tattelecom" was increased through issuance of additional common shares and their subsequent swap for common and preferred shares of KGTS. The reorganization was recorded at historical cost of the assets and liabilities of the Group's entities. The Company's equity for prior years was restated to account for the reorganization, as if it was completed at the beginning of the earliest period presented in the financial statements.

Financial results and cash flows of the Group over the periods prior to the reorganization could have differed from the information presented in the financial statements, had the Group operated during those periods as a single entity.

As of 31 December 2007, the Company's major shareholders were as follows:

	As of 31 December 2007	
	Number of shares	% of ownership
OJSC "Svyazinvestneftekhim"	18,182,331,372	87.2%
Other (individually less than 5%)	2,661,645,028	12.8%
Total	20,843,976,400	100%

The ultimate shareholder of OJSC "Svyazinvestneftekhim" is the Republic of Tatarstan.

The average number of the Company's employees in 2007 and 2006 was 7,100 and 6,800, respectively.

OJSC "TATTELECOM"

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 *(in thousand of US Dollars, unless otherwise stated)*

2. STATEMENT OF COMPLIANCE

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). International Financial Reporting Standards include standards and interpretations approved by the International Accounting Standards Board ("IASB"), including International Accounting Standards ("IAS") and interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC").

3. ADOPTION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Company adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC") of IASB that are relevant to its financial statements for the year ended as of 31 December 2007.

- IFRS 7, *Financial Instruments: Disclosures*;
- Amendments to IAS 1, *Capital Disclosures* ;
- IFRIC Interpretation 7, *Applying the Restatement Approach under IAS 29 "Financial Reporting in Hyperinflationary Economies*;
- IFRIC Interpretation 8, *Scope of IFRS 2*;
- IFRIC Interpretation 9, *Reassessment of Embedded Derivatives*;
- IFRIC Interpretation 10, *Interim Financial Reporting and Impairment*.

The effects of adoption of these standards and interpretations are not material to the Company's financial position or results of its operations, however, the Company is required to disclose additional information in its financial statements.

The main effect of the above-mentioned changes include the following:

IAS 1, Presentation of Financial Statements (amendments)

In accordance with IAS 1 (as amended) the Company provided additional disclosures to enable users of the financial statements to evaluate the Company's principle objectives, policies and procedures for managing capital (Note 27).

IFRS 7, Financial Instruments: Disclosures

In accordance with IFRS 7, the Company provided additional disclosures that enable users of the financial statements to evaluate the significance of the Company's financial instruments and the nature and extent of risks arising from those financial instruments.

Another four IFRIC interpretations became effective for the current year financial statements. These are: IFRIC Interpretation 7, *Application of Approach Which Requires Restatement of Financial Statements in Accordance with IAS 29, Financial Reporting in Hyperinflationary Economies*; IFRIC Interpretation 8, *Scope of IFRS 2*; IFRIC Interpretation 9, *Reassessment of Embedded Derivatives* and IFRIC Interpretation 10, *Interim Financial Reporting and Impairment*. The adoption of these Interpretations has not led to any changes in the Company's accounting policies or additional disclosures in the financial statements.

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

At the date of authorization of these financial statements, the following Standards and Interpretations were in issue but not yet effective:

	Effective for annual reporting periods beginning on or after
IAS 1, <i>Presentation of Financial Statements (amended)</i>	1 January 2009
IAS 23, <i>Borrowings Costs (amended)</i>	1 January 2009
IAS 27, <i>Consolidated and Stand-alone Financial Statements (amended)</i>	1 July 2009
IAS 28, <i>Investment in Associates (amended)</i>	1 July 2009
IAS 31, <i>Interests in Joint Ventures (amended)</i>	1 July 2009
IAS 32, <i>Financial Instruments: Disclosures (amended)</i>	1 January 2009
IFRS 2, <i>Share-based Payments (amended)</i>	1 January 2009
IFRS 3, <i>Business Combinations (amended)</i>	1 July 2009
IFRS 8, <i>Operating Segments</i>	1 January 2009
IFRIC Interpretation 11, <i>IFRS 2: Group and Treasury Share Transactions</i>	1 March 2007
IFRIC Interpretation 12, <i>Service Concession Arrangements</i>	1 January 2008
IFRIC Interpretation 13, <i>Customer Loyalty Programmes</i>	1 July 2008
IFRIC Interpretation 14 (an interpretation of IAS 19), <i>The Limit on a Defined Benefit Asset Minimum Funding Requirements and their Interaction</i>	1 January 2008

IFRS 8 becomes effective with respect to annual periods beginning on or after 1 January 2008. This IFRS replaces IAS 14, *Segment reporting*, and requires identification of operating segments on the basis of internal reports, which are regularly monitored by the chief executive responsible for taking operating decisions in order to allocate the resources to segments and assess their performance.

IAS 23 (amended) becomes effective with respect to annual periods beginning on or after 1 January 2009. Amendments to IAS 23 prohibit immediate expensing of borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. This provision relates to qualifying assets which require an extended period of time for their preparation for maintenance or sale. The Company should capitalize such borrowing costs. According to management estimates, amendments to IAS 23 will have no effect upon the Company's financial results as the Company has already applied the policy of borrowing costs' capitalization (refer to Significant Accounting Policies – Borrowing costs).

IFRIC 13 addresses how companies granting their customers loyalty award credits (often called 'points') when buying goods or services should account for their obligation to provide free or discounted goods or services if and when the customers redeem the points. This interpretation is mandatory for annual periods beginning on or after 1 July 2008.

The impact of adoption of these standards and interpretations on the financial statements for future periods is currently being assessed by the Company's management.

OJSC "TATTELECOM"

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

4. BASIS OF PRESENTATION

Accounting principles – The Company maintains its accounting records and prepares statutory financial statements in Russian rubles in accordance with the laws and accounting and reporting regulations of the Russian Federation.

The accompanying financial statements differ from the financial statements prepared for statutory purposes in Russia in that they reflect certain adjustments, appropriate to present the financial position, results of operations and cash flows in accordance with IFRS, which are not recorded in the Company's accounting books.

The financial statements of the Company are prepared under the historical cost convention, except that property, plant and equipment are carried at deemed cost as of 1 January 2005.

Going concern – The attached financial statements were prepared by the Company's management on a going concern basis, based on the assumption that the Company will continue its activities for the foreseeable future and has no intention or obligation to discontinue or significantly curtail the scope of its activities, and therefore all obligations will be settled in the due course of business.

Reporting on related party transactions – 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 as defined by IAS 24, *Related Party Disclosures*. In considering related party relationship, attention is directed to the substance of the relationship, and not merely the legal form.

Related parties may enter into transactions in which unrelated parties would not enter. Transactions between related parties may be on different terms, conditions and amounts as the transactions between unrelated parties.

Transactions with related parties for the year ended 31 December 2007 and outstanding amounts as of that date are disclosed in Note 26.

Functional and presentation currency – The Company's financial statements are measured in the currency prevailing in the economic environment in which the Company operates (functional currency). The functional currency of the Company is the Russian Ruble ("RUB"). The financial statements are presented in US dollars ("USD").

Transactions with other foreign currencies are translated into the functional currency using the exchange rates prevailing at the date of transactions. Exchange rate differences arising from such transactions and from translation of monetary assets and liabilities denominated in foreign currency at the closing exchange rate are recorded in the income statement.

The financial statements are translated into US dollars as follows:

- Assets and liabilities are translated at closing rates at the balance sheet date;
- The share capital and retained earnings as of the beginning of the reporting period are translated at the historical rates;
- Income and expenses for the period are translated at the average rate for the period.

The exchange rates of the Russian Ruble to the USD as of 31 December 2007 and 2006 were RUB 24.55 and 26.33 to 1 USD, respectively.

OJSC "TATTELECOM"

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

5. SIGNIFICANT ACCOUNTING POLICIES

Significant accounting policies used in preparation of these financial statements are described below.

Property, plant and equipment – Property, plant and equipment items as of 1 January 2005 are recorded at the revalued amounts as of that date. The valuation is confirmed by an independent appraiser. Those values were treated as deemed cost at the date of IFRS adoption. Property, plant and equipment purchased after 1 January 2005 are carried at cost.

The Company incurs costs associated with telecommunications and other equipment which require installation and related works to enable assets to commence revenue generating activities. All costs directly attributable to the construction, preparation and installation of an item to commence revenue generating activities are capitalized.

Significant renovations are capitalized if they extend the life of the asset or significantly increase its revenue generating capacity. Repair and maintenance costs are recognized in the income statement as incurred.

Property, plant and equipment are depreciated on a straight-line basis over their estimated useful lives. The accrual of depreciation charges commences from the month following the one in which the item is ready for use. The Company set the following useful lives of property, plant and equipment:

	<u>Years</u>
Buildings	40
Telecommunications equipment	10
Transmission devices	15
Vehicles	7
Office equipment and other	3-5

Property, plant and equipment items used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the assets may have been impaired. The management believes that no such events took place in 2007.

Items of property, plant and equipment contributed to the Company free-of-charge by the state authorities under programs for the development and upgrading of wire-line telecommunications networks are recorded at fair value as of the date of transfer. The transfer of such assets is recorded as deferred revenue, which is amortized over the useful lives of respective assets.

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

Asset retirement obligations – The Company records asset retirement obligations if it has a legal obligation to incur costs associated with the future retirement of assets. As of 31 December 2007, asset retirement obligations were not significant for the Company's financial statements.

Finance lease – The Company accounts for the leased property in accordance with the requirements of IAS 17, *Leases*. A lease is classified as a finance lease if the terms of the lease transfer substantially all risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

OJSC "TATTELECOM"

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

For finance leases, the present value of future minimum lease payments at the inception of the lease is recorded in the lessee's balance sheet. Amounts due within one year after the balance sheet date are classified as short-term obligations and the remaining balance – as long-term liabilities.

Leased assets are depreciated over their useful lives as determined in accordance with the accounting policy or over the term of the finance lease, if shorter. If there is reasonable certainty that the lessee will obtain ownership by the end of the finance lease term, the asset is depreciated over its useful life. If it is possible that the assets received under finance lease agreements will be returned upon the end of the lease term, such assets are depreciated over their useful life or the lease term, whichever is shorter.

Lease payments under operating leases are recognized as expenses on a straight-line basis over the lease term.

Intangible assets – Intangible assets primarily represent licenses and software products: programs that automate management of subscriber accounts (billing systems) and other software.

Software products and other intangible assets purchased separately are initially recorded at cost of their acquisition. Subsequently, intangible assets are carried at cost, less accumulated amortization and any accumulated impairment loss.

Finite-life intangible assets are amortized over their useful lives and reviewed for impairment whenever any impairment indicators arise.

Licenses and software are amortized on a straight-line basis over their useful lives determined as the license term or the period for which the rights to use the software are granted.

Impairment of long-term assets – At each balance sheet date, the Company's management reviews the carrying amounts of its fixed assets, intangible assets and other long-lived assets to determine whether there is any indication that those assets have suffered an impairment loss. If any indications of the possible impairment have been identified, the asset's recoverable amount is determined. Where it is impossible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash generating unit to which the asset belongs.

If the recoverable amount of an asset (or asset group) is estimated to be less than its carrying amount, the carrying amount of the asset (or asset group) is reduced to its recoverable amount. Any impairment loss is recorded in the income statement.

The Company's management believes that no impairment of long-lived assets of the Company occurred as of 31 December 2007.

Fair value of financial instruments – Financial instruments carried on the balance sheet include cash, short-term and long-term investments, receivables, payables and loans received. The particular recognition methods adopted are disclosed in the individual policy statements associated with each item below.

Short-term financial instruments primarily include cash, short-term investments, receivables, payables, and short-term borrowings. The estimated fair value of short-term financial instruments as of 31 December 2007 approximated their carrying value.

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

Long-term financial instruments primarily comprise long-term borrowings and long-term investments. As of 31 December 2007, the carrying and fair value of long-term financial assets was not significant. The fair value of long-term financial liabilities as of 31 December 2007 was USD 83 million.

Cash and cash equivalents – Cash and cash equivalents consist of petty cash, balances with banks, bank deposits and highly liquid financial investments with original maturities of three months or less, with low risks of a decrease in value.

Accounts receivable – Receivables are stated at their net realizable value after deducting an allowance for doubtful debts. Such allowance reflects either specific cases of delinquencies or defaults or estimates based on evidence of collectability. Concentrations of credit risk with respect to trade receivables are limited due to a highly diversified customer base, which includes a large number of individuals, private businesses and state-financed institutions.

Allowance for doubtful debts is created based on the actual data of accounts receivable collectability and the creditworthiness analysis of the Company's major debtors. Doubtful debt expense is charged to the income statement.

Inventories – Inventories comprise cables, spare parts, telephones and are stated at the lower of cost or net realizable value. Inventories are written off using the first-in-first-out method (FIFO).

Net realizable value represents the estimated selling price determined under the ordinary business terms less marketing costs.

Financial investments – Investments in corporate shares where the Company owns less than 20% of share capital, are accounted for at the cost of acquisition.

Management periodically assesses impairment of the carrying values of such investments and records valuation allowances, if required.

Retirement and post-retirement benefits – In Russia, all social contributions, including contributions to the pension fund, are substituted with a unified social tax ("UST") calculated by the application of a regressive rate from 26% to 2% of the annual gross remuneration of each employee. UST is allocated to three social funds, including the pension fund. The rates of contributions to the pension fund vary from 20% to 2% depending on the annual gross salary of each employee. These contributions are recorded in the income statement on an accrual basis.

Other post-employment benefits – In accordance with the collective agreement and the agreement on additional retirement benefits, the Company provides additional retirement benefits for both currently employed and retired employees. Most of the Company's employees are eligible for retirement benefits subject to certain conditions, including years of service, age and salary level.

The Company accounts for the post-retirement benefit plans in accordance with IAS 19, *Employee benefits*. The Company measures liabilities and assets under the defined benefit plans separately for each plan at each balance sheet date. The measurement of liabilities and fair values of the plan assets is confirmed by the independent actuary.

Contributions of OJSC Tatttelecom under the employee retirement benefit plans are managed by an affiliated company – Non-Governmental Pension Fund "Volga-Capital".

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

Value added taxes – Value-added taxes ("VAT") related to sales are payable to the tax authorities on an accrual basis based on the invoices issued to customers. VAT incurred for purchases may be reimbursed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that are not reimbursed, as of the balance sheet dates are recorded in other receivables.

Income taxes – Taxes on income are calculated in accordance with the laws of the Russian Federation. Income tax rate in the Russian Federation ("RF") equals 24%.

Deferred taxes are accounted for using the balance sheet liability method in respect to temporary differences arising from differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used to determine taxable profit.

Deferred tax assets are recognized to the extent that it is probable that taxable income will be available against which deductible temporary differences can be utilized.

Deferred taxes are calculated at rates that are expected to apply to the period when the asset is realized or the liability is settled.

Provisions – Provisions are recognized if the Company has current obligations as a result of past events, and it is probable that an outflow of certain resources will be required to settle the obligations and a reliable estimate of the obligations can be made.

Revenue recognition – Revenue is measured at the fair value of consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of any discounts and sales taxes.

The Company earns service revenues from usage of its local exchange networks and facilities. The principal services rendered by the Company are as follows:

1. Intrazonal telecommunications services;
2. Local telecommunications services (subscription system);
3. Installation and connection services (including access to network);
4. Telegraph services;
5. Lease of cable capacity;
6. Interconnection services to other operators;
7. Value added communication services (Internet, IP telephony, IDSN, ADSL);
8. Other communication services (radio and TV broadcasting, pay phones).

Intrazonal telecommunications services – Revenue is recognized in the period in which the services are rendered. Revenue from intrazonal telecommunications services is calculated based on the time of the call, its length, direction and the type of the subscriber.

Local telecommunications services – Monthly subscribers' fees are recognized in the month in which telephone services are rendered.

Installation and connection fees – Upfront fees received for installation and activation of wire line services, including non-refundable connection fees, are deferred and recognized as revenue over the expected subscriber relationship period. According to management estimates, the subscriber relationship period for wire line voice phone subscribers is 15 years for residential customers and 5 years for all other categories of subscribers.

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Telegraph services – Revenue from telegraph services is received from sending telegrams and other data transmission over telegraph lines. The Company recognizes revenue from telegraph services in the period in which the services are rendered.

Lease of cable capacity – The Company recognizes revenue from the lease of cable capacity in the period in which the service is rendered.

Interconnection services to other operators – Revenue from rendering services to other telecommunications operators is split into two categories. The first category represents revenue from terminating long-distance domestic and international traffic from other operators within the Company's network. The second category represents revenue from connection of operators that transmit long-distance domestic and international traffic of their subscribers through the Company's network.

The Company recognizes interconnection revenues from both categories of services in the period in which they are rendered.

New communication services – Revenue from other services is recognized as follows:

- Revenue from providing internet services is recognized at the date when the service is rendered to a subscriber;
- Revenue from operating leases is recognized on a straight-line basis over the lease term.

Borrowing costs – Borrowing costs directly attributable to items of property, plant and equipment, which take a substantial period of time to get ready for their intended use and require additional expenditures, are capitalized. Capitalized borrowings costs for the years ended 31 December 2007 and 2006 amounted to USD 3.2 mln. and USD 5.6 mln., respectively.

All other borrowing costs are recorded in income statement in the period in which they are incurred.

Dividends – Dividends for distribution to the shareholders are approved by the annual shareholders' meeting based on the recommendations of the Board of Directors. Profit available for distribution is determined based on the statutory accounting records. Dividends are recognized in the period in which they are approved by the shareholders' meeting.

Reclassifications – Certain comparative amounts have been reclassified to conform to the presentation adopted for the year ended 31 December 2007.

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6. KEY ASSUMPTIONS AND ESTIMATES

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

When applying the accounting policies, as described in Note 5, the Company's management made the following significant assumptions:

Impairment of long-term assets – At each balance sheet date, the Company's management reviews the carrying amounts of its fixed assets, intangible assets and other long-lived assets to determine whether there is any indication that those assets have suffered an impairment loss. If any indications have been identified of the possible impairment of an asset, the asset's recoverable amount should be determined. The key assumptions underlying the Company's estimation of impairment losses represent the discount rate and cash flow forecast.

Valuation allowances and provisions – At each balance sheet date the Company considers the necessity to record provisions for obsolete inventories, allowances for receivables and deferred tax assets.

Compliance with tax legislation – The practice of enforcement of tax legislation in the Russian Federation is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Tax declarations, together with other legal compliance areas are subject to review and investigation by a number of authorities, which are enabled by law to impose severe fines, penalties and interest charges. The considerations relating to the compliance with the tax laws may be judgmental from the point of view of interpreting regulatory requirements.

Subscriber life – According to management estimates, the customer relationship period for wire line voice phone subscribers is 15 years for residential customers and 5 years for all other categories of subscribers. The subscriber lives are estimated based on the management's expectations and statistical data for the previous periods.

Post-retirement benefit obligations – The Company's liabilities to pay post-retirement benefits to employees under the defined benefit plans were estimated based on the following assumptions: the discount rate, expected average salary raise and average life expectancy of benefit plan participants upon retirement.

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7. REVENUE

Revenue for the year ended 31 December 2007 consisted of the following:

By type of services	2007	2006
Local telecommunication services	69,070	52,164
Intrazonal telecommunication services	48,560	33,587
Interconnection services to other operators	29,362	18,081
Value added communication services (Internet, IP telephony, IDSN, ADSL)	22,840	15,078
Lease of cable capacity	8,773	6,593
Installation and connection services (including access to network)	4,033	7,295
Telegraph services	1,634	1,388
Other communication services (radio and television broadcasting, pay phones)	322	325
Other	8,741	9,082
Total	193,335	143,593
By classes of customers	2007	2006
Residential subscribers	94,082	72,252
Commercial organizations	82,954	59,352
State organizations	16,299	11,989
Total	193,335	143,593

8. OPERATING EXPENSES

Operating expenses for the year ended 31 December 2007 consisted of the following:

	2007	2006
Payroll expenses, including taxes	(49,602)	(40,005)
Depreciation of property, plant and equipment	(26,152)	(19,854)
Interconnection charges	(25,989)	(14,986)
Materials, repairs and maintenance	(10,880)	(8,126)
Doubtful debt expense	(5,372)	(422)
Taxes other than income tax	(4,328)	(3,950)
Rent	(2,334)	(1,987)
Contributions to the Universal Service Fund	(1,462)	(1,463)
Advertising	(1,461)	(541)
Fees for professional services	(771)	(475)
Amortization of intangible assets	(1,075)	(632)
Impairment of other non-current assets	(474)	-
Insurance	(335)	(614)
Tax provisions	(329)	(292)
Bank charges	(399)	(307)
Gain/(loss) on disposal of property, plant and equipment	1,377	(4,367)
Depreciation of fixed assets granted	471	755
Other expenses	(17,894)	(12,609)
Total	(147,009)	(109,875)

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

9. PROPERTY, PLANT AND EQUIPMENT

Movements of fixed assets and accumulated depreciation for the year 2007 are presented as follows:

	Buildings	Machinery and telecommu- nications equipment	Transmission devices	Vehicles	Office equipment and other	Construction in progress	Total
Cost							
As of 1 January 2006	50,923	46,704	137,339	2,416	8,976	8,171	254,529
Additions	-	-	-	-	-	43,467	43,467
Transfers into operation	1,179	18,248	12,507	213	2,179	(34,326)	-
Disposals	(267)	(719)	(4,360)	(165)	(52)	-	(5,563)
Effect of translation to presentation currency	4,771	4,917	13,051	226	905	160	24,030
As of 31 December 2006	56,606	69,150	158,537	2,690	12,008	17,472	316,463
Reclassification	-	4,404	-	1,264	(5,668)	-	-
Additions	-	-	-	-	-	103,435	103,435
Transfers into operation	1,269	29,725	16,869	2,281	1,602	(51,746)	-
Disposals	(2,568)	(1,310)	(1,664)	(246)	(132)	(21)	(5,941)
Effect of translation to presentation currency	4,062	6,542	12,167	373	523	3,438	27,105
As of 31 December 2007	59,369	108,511	185,909	6,362	8,333	72,578	441,062
Accumulated depreciation							
As of 1 January 2006	(1,090)	(4,331)	(7,951)	(351)	(758)	-	(14,481)
Charges	(1,184)	(7,015)	(9,967)	(978)	(710)	-	(19,854)
Disposals	9	238	727	59	29	-	1,062
Effect of translation to presentation currency	(140)	(623)	(1,040)	(63)	(92)	-	(1,958)
As of 31 December 2006	(2,405)	(11,731)	(18,231)	(1,333)	(1,531)	-	(35,231)
Reclassification	-	(1,031)	-	(103)	1,134	-	-
Charges	(1,290)	(9,696)	(11,615)	(748)	(2,803)	-	(26,152)
Disposals	825	501	343	108	104	-	1,881
Effect of translation to presentation currency	(193)	(209)	(1,799)	(21)	(1,359)	-	(3,581)
As of 31 December 2007	(3,063)	(22,166)	(31,302)	(2,097)	(4,455)	-	(63,083)
Net book value							
As of 31 December 2006	54,201	57,419	140,306	1,357	10,477	17,472	281,232
As of 31 December 2007	56,306	86,345	154,607	4,265	3,878	72,578	377,979

As of 31 December 2007 and 2006, property, plant and equipment with book value of USD 41,733 thousand and USD 37,320 thousand, respectively, were pledged as a collateral for certain loans obtained by Tattelecom (Note 18).

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NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007 (in thousand of US Dollars, unless otherwise stated)

10. INTANGIBLE ASSETS

Movements of intangible assets and accumulated amortization for the year ended 31 December 2007 are presented as follows:

	<u>Licenses</u>	<u>Software</u>	<u>Total</u>
Cost			
As of 1 January 2006	37	985	1,022
Additions	594	257	851
Disposals	(35)	(286)	(321)
Effect of translation to presentation currency	22	90	112
As of 31 December 2006	618	1,046	1,664
Additions	466	365	831
Disposals	(485)	(841)	(1,326)
Effect of translation to presentation currency	44	57	101
As of 31 December 2007	643	627	1,270
Accumulated depreciation			
As of 1 January 2006	(15)	(357)	(372)
Charges	(130)	(502)	(632)
Disposals	35	286	321
Effect of translation to presentation currency	(4)	(40)	(44)
As of 31 December 2006	(114)	(613)	(727)
Charges	(562)	(513)	(1,075)
Disposals	485	841	1,326
Effect of translation to presentation currency	(12)	(30)	(42)
As of 31 December 2007	(203)	(315)	(518)
Net book value			
As of 31 December 2006	504	433	937
As of 31 December 2007	440	312	752

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11. INVESTMENTS

Long-term investments as of 31 December 2007 consisted of the following:

	Ownership interest, %	2007	Ownership interest, %	2006
Ak Bars Bank	0.03%	85	0.03%	79
OJSC Kamaz	0.00%	-	0.00%	6
Loans to employees, long-term portion		1,064		348
Total		1,149		433
Loans to employees, current portion		510		124
Total		1,659		557

Loans to employees are interest-free loans with maturities from 3 years and more. The effective interest rate used to amount for these loans in 2007 is 10.5%.

12. OTHER NON-CURRENT ASSETS

Other non-current assets as of 31 December 2007 consisted of the following:

	2007	2006
Advances for property, plant and equipment	10,223	4,060
Advances for intangible assets	3,331	-
Total	13,554	4,060

13. INVENTORIES

Inventories as of 31 December 2007 consisted of the following:

	2007	2006
Cables and spare parts for telecommunications equipment	4,888	3,232
Finished goods and goods for sale	81	101
Other inventory	1,121	873
Provision for obsolete inventory	(554)	(360)
Total	5,536	3,846

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The change in provision for obsolete inventory is presented below:

	<u>2007</u>	<u>2006</u>
Balance at the beginning of the year	(360)	(299)
Increase in provision for obsolete inventory	(161)	(55)
Effect of translation to presentation currency	(33)	(6)
Balance at the end of the year	<u>(554)</u>	<u>(360)</u>

14. TRADE ACCOUNTS RECEIVABLE

Trade receivables as of 31 December 2007 consisted of the following:

	<u>2007</u>	<u>2006</u>
Due from subscribers for communication services	36,185	19,345
Allowance for doubtful receivables	(11,276)	(5,293)
Total	<u>24,909</u>	<u>14,052</u>

The Company distinguished between the following key groups of debtors for communication services:

	<u>2007</u>	<u>2006</u>
Individuals	13,228	9,921
Corporate	22,957	9,424
Total	<u>36,185</u>	<u>19,345</u>

The movements in allowance for doubtful debts with respect to trade receivables are as follows:

	<u>2007</u>	<u>2006</u>
Balance at the beginning of the year	(5,293)	(4,442)
Doubtful debt expense	(5,372)	(422)
Effect of translation to presentation currency	(611)	(429)
Balance at the end of the year	<u>(11,276)</u>	<u>(5,293)</u>

The average credit period for the Company's subscribers is 30 days. No interest is charged on the outstanding accounts receivable balances. The Company has fully provided for all receivables over 90 days because historical experience is such that receivables that are past due beyond 90 days are generally not recoverable. Trade receivables between 30 and 90 days are provided for based on the estimated irrecoverable amounts, determined by reference to past experience and collections.

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The Company's five largest customers represent 19% (2006: 34%) of the accounts receivable balance as of the year end. The summary below shows the outstanding balances from the largest customers at the respective balance sheet date. The Company does not establish credit limits for its customers.

	Client's location	Debt as of the reporting date	
		2007	2006
OJSC "TRK TVT"	RT Kazan	3,170	1,974
OJSC "MSS-Povolzhie"	RT Kazan	817	651
CJSC "MetroTelKazan"	RT Kazan	803	863
LLC "Teleset"	RT Kazan	731	1,441
OJSC MTS' Branch in RT	RT Kazan	714	652
OJSC Vypelkom's, Kazan Branch	RT Kazan	562	1,071
Total		6,797	6,652

Included in the Company's receivable balance as of the year end are debtors with the carrying amount of USD 1,262 thousand (2006: USD 1,945 thousand) which are past due at the respective balance sheet date and which the Company's management still considers recoverable. The Company does not hold any collateral over these balances. The weighted average age of these receivables is 58 days (2006: 57 days).

Aging of past due but not impaired trade receivables is presented below:

	2007	2006
30-60 days	639	1,196
60-90 days	623	749
Total	1,262	1,945

In order to estimate the collectability of trade receivables, the Company considers all the changes in debtors' solvency from the date of issuance of invoice for services to the reporting date. The credit risk concentration is limited due to the Company's diversified client base. The Company's management believes that the total allowance for doubtful debts presented in the financial statements is sufficient to cover the credit risk.

15. OTHER ACCOUNTS RECEIVABLE

Other accounts receivable as of 31 December 2007 consisted of the following:

	2007	2006
Prepayments and advances paid to related parties	2,451	1,907
Prepayments and advances paid to third parties	2,240	3,105
Prepaid expenses	265	220
Total	4,956	5,232

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16. CASH

Cash as of 31 December 2007 comprised the following:

	<u>2007</u>	<u>2006</u>
Current bank accounts, in RUB	4,925	3,955
Cash in transit, in RUB	341	314
Petty cash, in RUB	39	31
Total	<u>5,305</u>	<u>4,300</u>

The Company's cash held in the affiliated bank "AK Bars" as of 31 December 2007 and 2006 amounted to USD 4,432 thousand and USD 3,502 thousand, respectively.

17. SHARE CAPITAL

As of 31 December 2007 and 2006, OJSC "Tattelecom" had 20,843,976,400 issued common shares with par value of 10 kopecks each.

As of 1 January 2006, OJSC "Tattelecom" had 15,885,140 issued common shares with par value of 100 Roubles. As of 1 January 2006, the share capital of OJSC "KGTS" consisted of 1,220,298,800 common shares and 25,880,400 preferred shares with par value of 10 kopecks each.

On 30 November 2005, an Extraordinary General Shareholders' Meeting of OJSC "Tattelecom" was held to address the issues of reorganization through the merger with OJSC "KGTS" and an increase in the share capital of OJSC "Tattelecom" through the issuance of 4,958,836,400 additional common shares with par value of 10 kopecks each. On 24 April 2006, the merger was completed through the exchange of 1 common share of OJSC "KGTS" for 4 ordinary shares of OJSC "Tattelecom". A preferred share of OJSC "KGTS" was exchanged for 3 common shares of OJSC "Tattelecom".

The merger with KGTS, a company under common control, was accounted for at historical cost. The assets and liabilities of the acquired company were combined with the assets and liabilities of Tattelecom. Changes to the financial statements of Tattelecom were applied retrospectively to report the merger with KGTS, as if it had been performed at the beginning of the earliest period presented in the financial statements. The share capital was restated to account for the merger based on the share conversion ratio on the date of acquisition.

In June 2007, Tattelecom declared dividends for 2006 of RUB 0.01007 per share for the total amount of RUB 209,899 thousand (USD 8,551 thousand translated at the rate as of 31 December 2007).

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18. LONG-TERM BORROWINGS

Long-term borrowings as of 31 December 2007 are presented as follows:

	Currency	%	2007	2006
Corporate bonds, 2nd issue	RUB	11.8% – 12.5%	-	23,196
Corporate bonds, 4th issue	RUB	9.88%	62,003	-
Total corporate bonds			62,003	23,196
ABN Amro Bank	RUB	8.37-8.78%	6,122	-
Total unsecured loans			6,122	-
ING Bank (Eurasia)	EUR	7.2%	21,930	2,803
Ak Bars Bank	RUB	4.8-10.5%	12,642	22,697
Bank Societe Generale Vostok	RUB	8.25%	9,986	-
UniCredit Bank	RUB	8.5%	6,115	5,701
Other	Euro, Rubles	Various	-	187
Total collateralized loans			50,673	31,388
Total			118,798	54,584
Less amounts maturing within one year			(83,270)	(29,194)
Total long-term debt			35,528	25,390

Corporate bonds – On 8 November 2007, Tatttelecom floated the fourth issue of non-convertible bearer bonds worth RUB 1,500,000 thousand maturing in 5 years. The nominal value of the bonds was RUB 1,000 (USD 40.74 at the exchange rate as of 31 December 2007).

Following the offering, the rates for the first two coupons were established at 9.88% per annum.

In the second quarter of 2007, the Company fully repaid the second issue of non-convertible bonds.

The debt obligations as of 31 December 2007 have the following maturities:

2008	83,270
2009	14,308
2010	10,995
2011	8,705
2012	1,520
Thereafter	-
Total	118,798

As of 31 December 2007 and 2006, bank loans and credit lines were collateralized by fixed assets with the carrying value of USD 41,733 thousand and USD 37,320 thousand, respectively (Note 9).

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19. FINANCE LEASE OBLIGATIONS

Financial lease obligations as of 31 December 2007 were as follows:

	Minimum lease payments		Present value of minimum lease payments	
	2007	2006	2007	2006
Due within one year	1,794	807	1,263	647
Two to five years	2,039	243	1,627	217
Over five years	-	-	-	-
Less: future finance charges	(943)	(186)	-	-
Present value of lease obligations	2,890	864	2,890	864
Short-term portion			(1,263)	(647)
Long-term portion			1,627	217

During 2004-2007 the Company entered into several finance lease agreements for telecommunications equipment, computer and vehicles. The agreements expire in 2008-2012 and assume the transfer of ownership to Tatt telecom after the last lease payment is effected. The net book value of the leased assets amounted to USD 8,875 thousand and USD 5,036 thousand as of 31 December 2007 and 2006, respectively. Interest expense under these finance lease agreements in 2007 and 2006 amounted to USD 726 thousand and USD 355 thousand, respectively.

20. INCOME TAXES

The Company's income tax expense in 2007 comprises:

	2007	2006
Current income tax	(11,899)	(9,888)
Deferred tax benefit	1,450	2,109
Total	(10,499)	(7,779)

The movement for the year in the Company's deferred tax position is as follows:

	2007	2006
Net deferred liability at the beginning of the year	(11,364)	(12,388)
Deferred tax benefit	1,450	2,109
Effect of translation to presentation currency	(766)	(1,085)
Net deferred tax liability at the end of the year	(10,680)	(11,364)

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The tax effect of the temporary differences that give rise to the deferred tax assets and liabilities as of 31 December 2007 is presented below:

	<u>2007</u>	<u>2006</u>
Deferred tax assets		
Deferred revenue	8,918	8,634
Accrued expenses	2,881	446
Other	5,287	2,574
Total deferred tax assets	<u><u>17,086</u></u>	<u><u>11,654</u></u>
Deferred tax liabilities		
Property, plant and equipment	(20,815)	(20,804)
Other	(6,951)	(2,214)
Total deferred tax liabilities	<u><u>(27,766)</u></u>	<u><u>(23,018)</u></u>
Total deferred tax liabilities, net	<u><u>(10,680)</u></u>	<u><u>(11,364)</u></u>

The income tax expense for the year is different from that which would be obtained by applying the statutory income tax rate to the net income before income tax. Below is a reconciliation of theoretical income tax at 24% to the actual expense recorded in the Company's income statement:

	<u>2007</u>	<u>2006</u>
Income before tax	40,981	32,657
Theoretical income tax at statutory rate of 24%	9,835	7,838
Adjusted for:		
Non-deductible expenses	917	420
Other	(253)	(479)
Income tax expense	<u><u>10,499</u></u>	<u><u>7,779</u></u>

21. DEFERRED REVENUE

Deferred revenue as of 31 December 2007 consisted of the following:

	<u>2007</u>	<u>2006</u>
Deferred revenue from connection fees, current portion	5,534	4,803
Subscriber advances	1,678	1,290
Total current portion	<u><u>7,212</u></u>	<u><u>6,093</u></u>
Deferred revenue from connection fees, long-term portion	31,623	31,172
Total	<u><u>38,835</u></u>	<u><u>37,265</u></u>

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22. POST-RETIREMENT BENEFIT OBLIGATIONS

The post-employment and post-retirement benefit program run by the Company is primarily represented by pension plans. The pension plans cover full-time employees of Tattelcom who make personal contributions to the non-governmental pension fund. Participants of the defined benefit plan are entitled to receive specific post-retirement benefits calculated using a formula. This formula considers certain parameters, including the employees' age and length of service. As of 31 December 2007 and 2006, the Company employed around 7,100 and 6,800 employees, respectively, eligible for certain elements of the post-retirement or long-term social program of the Company, out of them 3,850 employees were the participants in the defined benefit plan.

The defined benefit plan provides for pension benefits upon reaching normal retirement age and disability benefits. In addition, the Company has some long-term employee benefit obligations that are close in nature to defined benefits, in particular, lump sum payments upon death or retirement.

The most recent independent actuarial valuation of the post-retirement and other long-term social programs in accordance with IAS 19 was performed as of 31 December 2007.

The Company's obligations on post-retirement benefits to employees under the defined benefit plans were valued as of 31 December 2007 using the following assumptions:

	<u>2007</u>	<u>2006</u>
Discount rate (% per annum)	6.80%	7.62%
Expected annual salary raise (% per annum)	10.88%	10.88%
Average life expectancy of the plan participants from date of retirement	17 years	17 years

Post-retirement benefit obligations and plan assets as of 31 December 2007 are presented as follows:

	<u>2007</u>	<u>2006</u>
Present value of defined benefit obligations	10,572	7,875
Fair value of plan assets	(5,514)	(4,715)
Present value of unfunded obligations	5,058	3,160
Unrecognised actuarial (losses)/gains	(262)	793
Net liability at the end of the year	<u>4,796</u>	<u>3,953</u>

Movements in the present value of the defined benefit obligations in 2007 were as follows:

	<u>2007</u>	<u>2006</u>
Net liability at the beginning of the year	3,953	3,307
Defined benefit plan expenses	590	469
Employer's contributions	(326)	(142)
Effect of translation to presentation currency	579	319
Net liability at the end of the year	<u>4,796</u>	<u>3,953</u>

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Expenses under the defined benefit plans in 2007 consisted of the following:

	<u>2007</u>	<u>2006</u>
Service cost	328	429
Interest cost	676	534
Expected return on plan assets	(406)	(353)
Actuarial gains recognized	(8)	(141)
Defined benefit plan expenses	<u>590</u>	<u>469</u>

In 2007 and 2006, in addition to the defined benefit plan expenses, the Company paid RUB 11,233 thousand and RUB 15,803 thousand (USD 458 thousand and USD 644 thousand, translated at the exchange rate as of 31 December 2007) under the defined contribution plan.

A non-state pension fund manages the Tattetelecom's pool of investments in plan assets. The fund portfolio consisted of debt instruments (64%) and equity instruments (36%) as of 31 December 2007 (2006: 38% and 62%, respectively). The share of equity instruments within the portfolio is determined as a ratio of equity instruments' value to the total value of equity instruments, state, municipal and corporate bonds within the portfolio as of the relevant date. The share of debt instruments within the portfolio is determined as a ratio of value of state, municipal and corporate bonds to the total value of equity instruments, state, municipal and corporate bonds within the portfolio as of the relevant date.

The calculation of the weighted average expected return on various categories of plan assets is presented below:

	<u>Expected return on plan assets, in %</u>		<u>Expected return on plan assets</u>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Russian companies' equity instruments	9.8	10.72	183	265
Russian state, municipal and corporate bonds	6.8	7.72	223	88
Weighted average expected return	7.88	9.58	406	353

The actual return on plan assets in 2007 was USD 225 thousand (2006: USD 508 thousand).

The Company expects to make a contribution of approximately USD 500 thousand to the defined benefit plans during the next financial year (2007: USD 326 thousand).

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23. FIXED ASSETS GRANTED

In the normal course of business the Company receives telecommunications infrastructure assets in constructed buildings from the authorities of Kazan and the Republic of Tatarstan. Assets granted in 2007 consisted of the following:

	<u>2007</u>	<u>2006</u>
Fixed assets granted at the beginning of the year	9,130	8,963
Fixed assets granted during the year	945	109
Fixed assets disposed during the year	(2,859)	-
Depreciation of fixed assets granted	(471)	(755)
Effect of translation to presentation currency	584	813
	<u>7,329</u>	<u>9,130</u>
Fixed assets granted at the end of the year	7,329	9,130

24. TRADE ACCOUNTS PAYABLE

Trade accounts payable as of 31 December 2007 consisted of the following:

	<u>2007</u>	<u>2006</u>
Payable to related parties	11,117	3,765
Payable to third parties	26,997	10,369
Total	38,144	14,134

The average credit period on purchases of goods/services is 30 days. No interest charge on the outstanding balance for trade payables is accrued during the credit period. The Company has an established financial risk management policy which focuses on budgeting and analysis of cash flows and payment schedules in order to ensure timely payments of all payables within the established timelines.

The table below summarizes the maturity profile of the Company's trade payables as of 31 December 2007 and 2006 based on contractual undiscounted payments:

	<u>2007</u>	<u>2006</u>
Due within three months	20,641	10,333
Due from three to six months	14,914	2,607
Due from six months to twelve months	2,589	1,194
Total	38,144	14,134

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25. OTHER ACCOUNTS PAYABLE

Other accounts payable as of 31 December 2007 consisted of the following:

	<u>2007</u>	<u>2006</u>
Accrued salaries	7,149	5,220
Other accruals	2,937	5,759
Tax provision	343	292
Total	<u>10,429</u>	<u>11,271</u>

26. RELATED PARTY TRANSACTIONS

Remuneration paid to key management personnel

Remuneration to the directors and key executives of Tattelcom (11 employees in 2007 and 15 employees in 2006) for 2007 and 2006 amounted to USD 913 thousand and USD 397 thousand, respectively.

Transactions with other related parties

Receivables from and payables to the related parties as of 31 December 2007 comprise the following:

	<u>2007</u>	<u>2006</u>
Due from subscribers for telecommunication services	7,003	6,227
Other accounts receivable	2,451	1,907
Cash	4,432	3,502
Long-term borrowings	12,642	22,697
Trade payables to related parties	11,117	3,765

Revenue from rendering telecommunications services to affiliated parties (mainly to state-controlled enterprises) and expenses related to services provided by those companies for the year ended 31 December 2007 are as follows:

	<u>2007</u>	<u>2006</u>
Revenues	59,596	29,434
Operating expenses	38,372	20,908

27. RISK MANAGEMENT

The main risks inherent to the Company's operations are those related to capital management, liquidity, market movements in interest rates, credit and foreign currency risk exposures. The Company's risk management policies' description is presented below.

Capital risk management – The Company manages its capital to ensure that it is able to continue as a going concern while maximizing the return to the shareholders through the optimization of the debt and equity balance. In order to achieve this goal, the Company takes steps and actions aimed to minimize the risks and costs associated with the future financing. The Company has different types of borrowings available for use in order to meet its need in capital, such as bonds' issuance, long-term and short-term borrowings, as well as suppliers' credit.

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The Company did not establish any formal policy with respect to debt to equity ratio. The Company reviews the capital structure on a regular basis in order to determine the necessary actions needed to support the balanced structure of its capital. In such reviews the Company's management considers the cost of capital and risks associated with each category of capital. The Company's targeted debt to equity ratio is 1:1.

The Company's debt to equity ratio as of 31 December 2007 is presented below:

	<u>2007</u>	<u>2006</u>
Borrowings	118,798	54,584
Less: Cash and cash equivalents	(5,305)	(4,300)
Net debt	<u>113,493</u>	<u>50,284</u>
Shareholders' equity	<u>206,694</u>	<u>170,156</u>
Net debt to equity ratio	<u>54%</u>	<u>30%</u>

The fair value of financial instruments

The fair value of financial assets and liabilities is determined as follows:

- The fair value of financial assets and liabilities with standard terms traded in active and liquid markets is determined in accordance with the market quotations;
- The fair value of other financial assets and liabilities (excluding derivative financial instruments) is determined in accordance with publicly accepted model of price calculation on the basis of the discounted cash flows by using prices for existing transactions in the market.

Liquidity risk – Liquidity risk is the risk that Tatttelecom will not be able to settle all liabilities as they become due. The Company has established a detailed budgeting and cash forecasting process to help ensure that it has adequate cash available to meet its payment obligations. The summaries of contractual maturities of the Company's financial liabilities as of 31 December 2007 are presented in Notes 18, 19 and 24.

Interest rate risk – Interest rate risk is the risk that changes in floating interest rates will adversely impact Tatttelecom's financial results. The Company does not use any derivative financial instruments to manage interest rate risk exposure. The Company limits its interest rate risk exposure by maintaining an appropriate mix between fixed and floating rate borrowings.

The table below details the Company's sensitivity to an increase or a decrease of the floating interest rate by 1%. Such sensitivity calculation is used for the Company's management reporting with respect to the interest risk and reflects the management's assessment of a reasonably possible fluctuation of interest rates. The analysis was applied to loans and borrowings (financial liabilities) based on the assumption that amount of debt outstanding as at the balance sheet date will remain outstanding for the next financial year.

If the floating interest rate increased/decreased by 1%, and all other terms and conditions remain constant, income before tax for the year ended 31 December 2007 would decrease/increase by USD 219 thousand (2006: USD 28 thousand).

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Credit risk – Credit risk is the risk that a counterparty may default or not meet its obligations to the Company on a timely basis, leading to financial losses to the Company. Tatt telecom has a diversified client base which allows the Company to be independent from a specific customer (the Company's receivables are distributed among a big number of individuals, budget organizations and legal entities).

There are no significant concentrations of the Company's credit risk with one customer or a group of customers with similar characteristics. The Company defines customers as having similar characteristics in case they are affiliated entities. The credit risk concentration did not exceed 5% of all monetary assets at any time of the current financial year.

Currency risk – Credit risk is the risk that the financial results of the Company will be adversely impacted by fluctuations in the exchange rate of Russian Ruble to other currencies. The Company has transactions denominated in foreign currencies. The Company does not use any derivatives to manage foreign currency risk exposure.

The carrying amounts of the Company's foreign currency denominated monetary assets and liabilities as of 31 December 2007 comprises:

	US Dollar		Euro	
	2007	2006	2007	2006
Assets				
Trade accounts receivable	473	315	-	-
Other non-current assets	3,105	-	137	-
Total assets	3,578	315	137	-
Liabilities				
Borrowings	-	-	(21,930)	(2,803)
Trade accounts payable	(911)	(249)	(10,037)	-
Total liabilities	(911)	(249)	(31,967)	(2,803)
Total net position	2,667	66	(31,830)	(2,803)

The table below details the Company's sensitivity to the fluctuations of the Russian Ruble in relation to USD and EURO by 10%. The sensitivity level of 10% is used during the preparation and review of the management reports on currency risk, and reflects the management's assessment of a reasonably possible change of exchange rates. The analysis was applied to monetary items at the balance sheet dates denominated in respective currencies.

	US Dollar		Euro	
	2007	2006	2007	2006
Decrease in net income for the year	(256)	(6)	(3,055)	(271)
Other equity components	-	-	-	-

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28. COMMITMENTS AND CONTINGENCIES

Capital commitments – Under the agreements effective as of 31 December 2007 and 2006, Tatt telecom does not have any significant capital commitments.

Social commitments – Tatt telecom has entered into a collective agreement with its employees. According to the agreement, Tatt telecom has a commitment to make certain payments to the employees, the amount of which can vary from year to year. No provision for such commitments is recorded in the financial statements, as the future payments under this agreement are not fixed and entirely depend on the Company's management decisions.

Litigation – The Company has been and continues to be the subject of legal proceedings and adjudications from time to time, none of which has had, individually or in the aggregate, a material adverse impact on the financial position and financial performance of the Company.

Russian Federation tax and regulatory environment – Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include value added tax, profit tax, social taxes and others. The government's policy on implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Tax calculations and payments, together with other legal compliance areas (for instance, customs and currency control matters) are subject to review and investigation by various of authorities, which are enabled by law to impose severe fines, penalties and interest charges. These facts create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems. Generally, tax declarations remain open and subject to inspection for a period of three years following the fiscal year end. Management believes that it has adequately provided for tax liabilities; however, the risk remains that relevant authorities could take a different position with regard to interpretive issues. As of 31 December 2007, the Company estimates its possible tax obligations in addition to those already included in the financial statements, at USD 3,159 thousand.

Russian Federation Law and Regulatory Environment for the Telecommunication Industry – New Federal Law on Communications became effective as of 1 January 2006. The Law established new rules for companies providing domestic long-distance and international long-distance communication services (DLD/ILD). The Company signed agent agreements with the licensed DLD/ILD operators (OJSC "Rostelecom" and others). According to these agent agreements, OJSC "Tatt telecom" resells the licensed operators' services for a commission fee determined as a part of revenue from DLD/ILD serviced provided by these operators to the end customers (subscribers). Under the new rules, the DLD/ILD revenues are reported in the financial statements on a net basis, i.e. only the commission amount is shown as revenue from DLD/ILD with no corresponding traffic cost.

Effective 1 July 2006, the Calling Party Pays rule ("the CPP rule") was introduced in Russia for all mobile operators and the majority of fixed line operators. The CPP rule implies that the subscribers pay for all outgoing calls, and all incoming calls are free of charge. Accordingly, the Company started to charge the subscribers for the calls to mobile operators. The respective revenues for the years ended 31 December 2007 and 2006 totalled USD 29,985 thousand and USD 11,782 thousand.

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29. SUBSEQUENT EVENTS

In March 2008, the Company signed a credit line agreement with ABN AMRO Bank for RUB 300 million (USD 12,222 thousand at the exchange rate as of 31 December 2007) with an interest rate of MosPrime + 2.6% per annum.

In April 2008, the Company signed a credit line agreement with Banque Societe Generale Vostok for RUB 300 million (USD 12,222 thousand at the exchange rate as of 31 December 2007) with an interest rate of MosPrime + 2.75% per annum.