SISTEMA JSFC
AND SUBSIDIARIES

Consolidated Financial Statements
As of December 31, 2014 and 2013
and for the Years Then Ended

SISTEMA JSFC AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Shareholders of Sistema Joint Stock Financial Corporation

We have audited the accompanying consolidated financial statements of Sistema Joint Stock Financial Corporation and its subsidiaries, which comprise the consolidated statements of financial position as of December 31, 2014 and 2013, and the related consolidated statements of operations and comprehensive income, cash flows and changes in shareholders' equity for the years then ended, and the related notes to the consolidated financial statements and appendix thereto.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with the Russian Federal Auditing Standards and auditing standards generally accepted in the United States of America. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about 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 consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated 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 referred to above present fairly, in all material respects, the financial position of Sistema Joint Stock Financial Corporation and its subsidiaries as of December 31, 2014 and 2013, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche

April 2, 2015
Moscow, Russian Federation

для аудиторских заключений
Россия, г. Москва, ул. Лесная, д. 5

Raikhman M.V., Partner
(Certificate no. 01-001195, dated January 14, 2013)

SISTEMA JSFC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
AS OF DECEMBER 31, 2014 AND 2013
(Amounts in thousands of U.S. dollars, except share and per share amounts)

	Notes	2014	2013
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents		$ 1,288,722	$ 1,537,492
Short-term investments	8	479,341	1,562,547
Assets from banking activities, current portion (including cash and cash equivalents of $843,715 and $1,132,368)	7	2,180,196	3,898,740
Accounts receivable	9	1,163,092	1,630,593
VAT receivable		236,438	335,289
Inventories and spare parts	11	1,244,509	1,131,302
Deferred tax assets	21	245,571	330,388
Other current assets	10	832,060	1,084,547
Current assets of Bashneft	2	-	3,054,728
Total current assets		7,669,929	14,565,626
NON-CURRENT ASSETS:			
Property, plant and equipment	12	7,191,394	11,151,341
Advance payments for non-current assets		84,560	162,978
Goodwill	13	817,537	1,327,779
Other intangible assets	14	1,721,389	2,162,700
Investments in affiliates	16	356,018	365,266
Assets from banking activities, net of current portion	7	1,374,367	2,554,229
Debt issuance costs		42,267	78,348
Deferred tax assets	21	392,866	297,419
Long-term investments	17	316,625	249,071
Other non-current assets		703,525	714,458
Non-current assets of Bashneft	2	-	9,619,779
Total non-current assets		13,000,548	28,683,368
TOTAL ASSETS		$ 20,670,477	$ 43,248,994

See notes to the consolidated financial statements and appendix thereto.

SISTEMA JSFC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
AS OF DECEMBER 31, 2014 AND 2013 (CONTINUED)
(Amounts in thousands of U.S. dollars, except share and per share amounts)

	Notes	2014	2013
LIABILITIES AND EQUITY			
CURRENT LIABILITIES:			
Accounts payable		$ 1,584,251	$ 1,943,133
Liabilities from banking activities, current portion	18	2,180,491	3,864,415
Taxes payable		290,635	490,564
Deferred tax liabilities	21	64,947	114,192
Subscriber prepayments, current portion		390,736	620,281
Accrued expenses and other current liabilities	19	1,315,656	1,567,890
Short-term loans payable		129,938	40,836
Current portion of long-term debt	20	1,598,770	2,102,911
Current liabilities of Bashneft	2	-	2,663,432
Total current liabilities		7,555,424	13,407,654
LONG-TERM LIABILITIES:			
Long-term debt, net of current portion	20	6,534,055	8,375,161
Subscriber prepayments, net of current portion		59,064	101,240
Liabilities from banking activities, net of current portion	18	167,860	772,525
Deferred tax liabilities	21	787,631	902,591
Asset retirement obligations	28	53,715	83,809
Postretirement benefits obligations		45,344	53,943
Property, plant and equipment contributions		41,358	74,174
Other long-term liabilities		475,713	443,032
Non-current liabilities of Bashneft	2	-	3,734,024
Total long-term liabilities		8,164,740	14,540,499
TOTAL LIABILITIES		15,720,164	27,948,153
Commitments and contingencies	30	-	-
Redeemable noncontrolling interests	29	792,766	805,130
SHAREHOLDERS' EQUITY:			
Share capital (9,650,000,000 shares issued; 9,435,902,596 and 9,274,755,045 shares outstanding with par value of 0.09 Russian Rubles, respectively)	24	30,057	30,057
Treasury stock (214,097,404 and 375,244,955 shares with par value of 0.09 Russian Rubles, respectively)		(246,351)	(426,715)
Additional paid-in capital		2,604,913	2,616,608
Retained earnings		4,210,623	8,993,469
Accumulated other comprehensive loss	24	(3,743,402)	(906,718)
Total shareholders' equity		2,855,840	10,306,701
Non-redeemable noncontrolling interests		1,301,707	4,189,010
TOTAL EQUITY		4,157,547	14,495,711
TOTAL LIABILITIES AND EQUITY		$ 20,670,477	$ 43,248,994

See notes to the consolidated financial statements and appendix thereto.

SISTEMA JSFC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(Amounts in thousands of U.S. dollars, except share and per share amounts)

	Notes	2014	2013
Sales		$ 15,886,775	$ 17,623,153
Revenue from banking activities		698,182	878,832
TOTAL REVENUES		16,584,957	18,501,985
Cost of sales, exclusive of depreciation and amortization shown separately below		(7,460,524)	(7,907,148)
Cost related to banking activities, exclusive of depreciation and amortization shown separately below		(760,084)	(523,960)
Selling, general and administrative expenses		(3,431,075)	(3,896,207)
Depreciation and amortization		(2,292,118)	(2,633,548)
Taxes other than income tax		(193,122)	(239,814)
Equity in results of affiliates		73,124	29,866
Impairment of goodwill	15	-	(258,048)
Impairment of other assets	15	(864,629)	(804,545)
Gain on disposal of investment in RussNeft	4	-	1,200,000
Gain from reentry into Uzbekistan	6	181,305	-
Gain on Bitel case resolution	30	-	371,100
Other operating expenses		(99,385)	(273,109)
OPERATING INCOME		1,738,449	3,566,572
Interest income		212,774	182,447
Interest expense		(811,346)	(960,136)
Change in fair value of derivative instruments		-	30,199
Foreign currency transaction loss		(548,596)	(298,264)
Income before income tax		591,281	2,520,818
Income tax expense	21	(453,417)	(842,107)
Net income excluding Bashneft		137,864	1,678,711
Income of Bashneft operations, net of tax effect of $427,716 and $455,637	2	1,517,054	1,540,489
Loss on deconsolidation of Bashneft, net of tax effect of nil	2	(4,969,011)	-
NET (LOSS) / INCOME		(3,314,093)	3,219,200
Noncontrolling interests		(773,539)	(961,672)
NET (LOSS) / INCOME ATTRIBUTABLE TO SISTEMA JSFC		$ (4,087,632)	$ 2,257,528
Including:			
From continuing operations		(278,161)	1,102,161
From Bashneft operations and its deconsolidation		(3,809,471)	1,155,367
OTHER COMPREHENSIVE (LOSS)/INCOME, NET OF TAX			
Currency translation loss		$ (3,886,388)	$ (885,770)
Unrealized (loss)/gain on available-for-sale securities		(52,099)	32,200
Unrealized gain on derivatives		72,899	45,499
Unrecognized actuarial gain		172	5,310
Other comprehensive (loss)/income, net of tax		(3,865,416)	(802,761)
TOTAL COMPREHENSIVE (LOSS)/INCOME		$ (7,179,509)	$ 2,416,439
Including:			
Attributable to noncontrolling interests		(255,193)	738,912
Attributable to Sistema JSFC		(6,924,316)	1,677,527
Weighted average number of common shares outstanding – basic and diluted		9,350,539,484	9,239,817,019
Earnings per share, basic and diluted, U.S. cent			
(Loss)/earnings per share from continuing operations		(2.98)	11.93
(Loss)/earnings per share from Bashneft operations and its deconsolidation		(40.74)	12.50
Total (loss)/earnings per share attributable to Sistema JSFC shareholders		(43.72)	24.43

See notes to the consolidated financial statements and appendix thereto.

SISTEMA JSFC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(Amounts in thousands of U.S. dollars)

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) / income	$ (3,314,093)	$ 3,219,200
Income of Bashneft operations	(1,517,054)	(1,540,489)
Loss on deconsolidation of Bashneft	4,969,011	-
Net income excluding Bashneft	137,864	1,678,711
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation and amortization	2,292,118	2,633,548
Equity in results of affiliates	(73,124)	(29,866)
Deferred income tax expense	36,338	140,292
Foreign currency transaction loss	548,596	298,264
Gain from disposal of investment in RussNeft	-	(1,200,000)
Gain on Bitel case resolution, net of cash received of $125,000	-	(246,100)
Gain on reentry into Uzbekistan	(181,305)	-
Gain on disposal of property, plant and equipment	(26,731)	(7,226)
Gain on disposal of subsidiaries	(139,082)	-
Amortization of connection fees	(23,019)	(60,309)
Allowance for loan losses	260,417	212,081
Dividends received from affiliates	70,369	65,247
Non-cash compensation to employees	79,430	54,158
Impairment of goodwill	-	258,048
Impairment of other assets	864,629	804,545
Other non-cash items	19,937	(15,057)
Changes in operating assets and liabilities, net of effects from purchases of businesses:		
Trading securities	267,153	(406,687)
Accounts receivable	(44,241)	(240,586)
VAT receivable	(17,192)	(174,951)
Inventories and spare parts	(490,362)	(171,320)
Other current assets	(114,574)	(93,381)
Accounts payable	560,603	533,948
Subscriber prepayments	(11,593)	110,112
Taxes payable	(5,394)	109,503
Accrued expenses and other current liabilities	281,592	(54,127)
Net cash from operating activities excluding Bashneft	4,292,429	4,198,847
Net cash from operating activities of Bashneft	2,755,291	2,629,988
Net cash provided by operating activities	7,047,720	6,828,835
CASH FLOWS FROM INVESTING ACTIVITIES:		
Payments for purchases of property, plant and equipment	(2,362,652)	(2,455,276)
Proceeds from sale of property, plant and equipment	80,332	39,592
Payments for purchases of intangible assets	(539,930)	(539,117)
Payments for businesses, net of cash acquired	(392,409)	(34,664)
Proceeds from sale of subsidiaries, net of cash disposed	150,000	561,402
Purchase of investments in affiliated companies	(201,582)	(63,753)
Payments for purchases of long-term investments	(836,916)	(105,000)
Proceeds from sale of long-term investments	511,227	1,286,292
Payments for purchases of short-term investments	(1,327,702)	(1,337,304)
Proceeds from sale of short-term investments	1,622,718	1,047,317
Payments for purchases of other non-current assets	-	(44,879)
Increase in restricted cash	-	(15,819)
Net decrease/(increase) in loans to customers of the banking segment	664,089	(70,458)
Net cash used in investing activities excluding Bashneft	(2,632,825)	(1,731,667)
Net cash used in investing activities of Bashneft (net of cash disposed of $961,733)	(3,256,540)	(1,158,995)
Net cash used in investing activities	$ (5,889,365)	$ (2,890,662)

SISTEMA JSFC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013 (CONTINUED)
(Amounts in thousands of U.S. dollars)

	2014	2013
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from/(principal payments on) short-term borrowings, net	$ 185,838	$ (231,036)
Net decrease in deposits from customers of the banking segment	(701,620)	(177,105)
Proceeds from long-term borrowings	2,850,171	1,900,322
Principal payments on long-term borrowings	(2,274,350)	(2,539,405)
Acquisition of noncontrolling interests in existing subsidiaries	(67,432)	(299,184)
Dividends paid	(1,198,028)	(1,225,440)
Proceeds from capital transactions with shares of existing subsidiaries	41,141	69,002
Net cash used in financing activities excluding Bashneft	(1,164,280)	(2,502,846)
Net cash provided by/(used in) financing activities of Bashenft	885,338	(580,164)
Net cash used in financing activities	(278,942)	(3,083,010)
Effect of foreign currency translation on cash and cash equivalents	(1,938,436)	(293,247)
Net (decrease)/increase in cash and cash equivalents	(1,059,023)	561,916
Cash and cash equivalents at the beginning of the year, including Bashneft	3,191,460	2,629,544
Cash and cash equivalents at the end of the year, including Bashneft	2,132,437	3,191,460
Less: cash and cash equivalents of Bashneft at the end of the year	-	(521,600)
Cash and cash equivalents at the end of the year	$ 2,132,437	$ 2,669,860
Comprising:		
Non-banking activities	1,288,722	1,537,492
Banking activities	843,715	1,132,368
CASH PAID DURING THE YEAR FOR:		
Interest, net of amounts capitalized	$ (876,692)	$ (1,160,300)
Income taxes	(377,298)	(735,797)
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Acquisition of intangible assets	-	670,300
Equipment and licenses acquired under capital leases	203,904	223,628
Amounts owed for capital expenditures	401,206	124,826
Payables related to business acquisitions	1,760	345

See notes to the consolidated financial statements and appendix thereto.

SISTEMA JSFC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(Amounts in thousands of U.S. dollars, except share amounts)

	Share capital		Treasury stock		Additional paid-in capital	Retained earnings	Accumulated other compre-hensive Loss	Shareholders' equity	Non-redeemable non-controlling interests	Total equity	Redeemable non-controlling interests
	Shares	Amount	Shares	Amount							
Balances at January 1, 2013	**9,650,000,000**	**30,057**	**(440,425,038)**	**(501,109)**	**2,859,491**	**7,110,467**	**(326,717)**	**9,172,189**	**4,109,505**	**13,281,694**	**731,661**
Net income/(loss)	-	-	-	-	-	2,257,528	-	2,257,528	1,021,588	3,279,116	(59,916)
Other comprehensive (loss)/income	-	-	-	-	-	-	(580,001)	(580,001)	(229,192)	(809,193)	6,432
Settlements under long-term motivation program	-	-	65,180,083	74,394	(13,262)	-	-	61,132	-	61,132	-
Accrued compensation cost	-	-	-	-	54,158	-	-	54,158	-	54,158	-
Business combinations, disposals and capital transactions of subsidiaries	-	-	-	-	(283,779)	-	-	(283,779)	237,429	(46,350)	27,547
Change in fair and redemption value of noncontrolling interests	-	-	-	-	-	(99,406)	-	(99,406)	-	(99,406)	99,406
Dividends declared by Sistema JSFC	-	-	-	-	-	(275,120)	-	(275,120)	-	(275,120)	-
Dividends declared by subsidiaries	-	-	-	-	-	-	-	-	(950,320)	(950,320)	-
Balances at December 31, 2013	**9,650,000,000**	**30,057**	**(375,244,955)**	**(426,715)**	**2,616,608**	**8,993,469**	**(906,718)**	**10,306,701**	**4,189,010**	**14,495,711**	**805,130**
Net (loss)/income	-	-	-	-	-	(4,087,632)	-	(4,087,632)	852,476	(3,235,156)	(78,937)
Other comprehensive (loss)/income	-	-	-	-	-	-	(5,128,557)	(5,128,557)	(974,348)	(6,102,905)	(54,384)
Settlements under long-term motivation program	-	-	122,129,298	132,811	(141,239)	-	-	(8,428)	-	(8,428)	-
Accrued compensation cost	-	-	-	-	79,430	-	-	79,430	-	79,430	-
Business combinations, disposals and capital transactions of subsidiaries	-	-	39,018,253	47,553	50,114	-	-	97,667	(491,574)	(393,907)	-
Change in fair and redemption value of noncontrolling interests	-	-	-	-	-	(120,957)	-	(120,957)		(120,957)	120,957
Dividends declared by Sistema JSFC	-	-	-	-	-	(574,257)	-	(574,257)		(574,257)	-
Dividends declared by subsidiaries	-	-	-	-	-	-	-	-	(889,068)	(889,068)	-
Deconsolidation of Bashneft	-	-	-	-	-	-	2,291,873	2,291,873	(1,384,789)	907,084	
Balances at December 31, 2014	**9,650,000,000**	**30,057**	**(214,097,404)**	**(246,351)**	**2,604,913**	**4,210,623**	**(3,743,402)**	**2,855,840**	**1,301,707**	**4,157,547**	**792,766**

See notes to the consolidated financial statements and appendix thereto.

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

1. BASIS OF PREPARATION

Sistema Joint Stock Financial Corporation (the “Company”, together with its subsidiaries, the “Group”) invests in, and manages a range of companies which operate in the telecommunications, oil and energy, high technology, banking, timber, real estate and other sectors. The Company and the majority of its consolidated subsidiaries are incorporated in the Russian Federation (“RF”).

The controlling shareholder of the Company is Vladimir P. Evtushenkov. Minority holdings are held by certain top executives and directors of the Company. The rest of the shares are listed on the London Stock Exchange in the form of Global Depositary Receipts (“GDRs”) and on the Moscow Exchange.

Below are the Group’s significant entities and their principal activities as of December 31, 2014:

Significant entities	Short name	Principal activity	Beneficial ownership as of December 31, 2014	2013
Sistema Joint Stock Financial Corporation	Sistema	Investing and financing		
Mobile TeleSystems	MTS	Telecommunications	53%	53%
Sistema Shyam TeleServices Limited	SSTL	Telecommunications	57%	57%
MTS Bank	MTS Bank	Banking	87%	87%
RTI	RTI	Technology	85%	85%
Detsky mir-Center	Detsky mir	Retail trading	99%	100%
Medsi	Medsi	Healthcare services	75%	75%
Targin	Targin	Oilfield services	100%	100%
Bashkirian Power Grid Company (Note 5)	BPGC	Energy transmission	91%(1)	79%(1)
LesInvest (Note 3)	LesInvest	Timber	100%	-
Leader-Invest	Leader-Invest	Real estate	100%	100%

(1) Voting interests as of December 31, 2014 and 2013 – 93%.

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

In determining and applying accounting policies, judgement is often required in respect of items where the choice of specific policy, accounting estimate or assumption could materially affect the reported results of operations or financial position of the Group.

Management considers that certain accounting estimates and assumptions relating to business combinations and disposals, property, plant and equipment, intangible assets and goodwill, provisions and contingent liabilities and impairment are the Group’s critical accounting estimates.

A discussion of these estimates together with the summary of the Group’s significant accounting policies is provided in appendix A1 to the notes to these consolidated financial statements.

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

2. DECONSOLIDATION OF BASHNEFT

In September 2014, a civil claim was filed with the Moscow Court of Arbitration by the Prosecutor General’s Office of the Russian Federation seeking the transfer to the Russian Federation of all shares in Bashneft held by the Group. The civil claim asserted that the transfer of Bashneft from the property of the Russian Federation into the property of Bashkortostan in 1992-1993 had been unlawful, as no requisite consent had been obtained from the federal authorities, and therefore all subsequent transactions with Bashneft shares should be considered null and void. In November 2014, the court ruled in favour of the plaintiff and ordered the transfer of the Bashneft shares held by the Group to the Russian Federation. The transfer of the shares took place in December 2014.

The Group deconsolidated Bashneft in December 2014 and recognized a loss upon loss of control, measured as the difference between the carrying amount of noncontrolling interests in the former subsidiary (including accumulated other comprehensive income attributable to the noncontrolling interests) at the date Bashneft was deconsolidated and the carrying amount of its assets and liabilities. The Group also removed the amount previously accumulated in the translation adjustment component of equity and attributable to Bashneft and reported it as part of the loss on transfer of Bashneft shares to the Russian Federation.

The loss on deconsolidation of Bashneft recognized in the consolidated statement of operations and comprehensive income for the year ended December 31, 2014 is measured as follows:

Net assets as at deconsolidation date	$	4,061,927
Noncontrolling interests		(1,384,789)
Accumulated currency translation adjustment		2,291,873
Loss on deconsolidation of Bashneft		4,969,011
Tax effect		-
Loss on deconsolidation of Bashneft, net of tax	$	**4,969,011**

Bashneft results were separately presented in the consolidated statements of operations and comprehensive income for the years ended December 31, 2014 and 2013 as follows:

		2014		2013
Revenues	$	16,224,383	$	17,783,111
Income from Bashneft, before income taxes		1,944,770		1,996,126
Income tax expense		(427,716)		(455,637)
Income from Bashneft, net of tax effect		1,517,054		1,540,489

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

Additionally, the assets and liabilities pertaining to Bashneft have been presented separately within the consolidated statement of financial position as of December 31, 2013 as follows:

Cash and cash equivalents	$	625,417
Accounts receivable		593,016
Inventories and spare parts		716,847
Other current assets		2,659,069
Intragroup balances		(1,539,621)
Current assets of Bashneft		**3,054,728**
Property, plant and equipment		8,794,360
Other non-current assets		941,695
Intragroup balances		(116,276)
Non-current assets of Bashneft		**9,619,779**
Accounts payable		(1,351,326)
Debt, current portion		(367,147)
Other current liabilities		(1,096,320)
Intragroup balances		151,361
Current liabilities of Bashneft		**(2,663,432)**
Debt, long-term portion		(2,419,639)
Other long-term liabilities		(1,344,437)
Intragroup balances		30,052
Long-term liabilities of Bashneft	$	**(3,734,024)**

The Group retains no continuing involvement with Bashneft after it has been deconsolidated, other than routine transactions in the normal course of business.

In December 2014, the Group filed a claim with the Moscow Court of Arbitration for the recovery of RUB 70.7 billion losses from Ural-Invest, a legal successor of the seller of the Bashneft shares to the Group. In February 2015, the court upheld the Group's claim. In March 2015, the Group and Ural-Invest signed a settlement agreement. In accordance with its terms, all assets owned by Ural-Invest of RUB 46.5 billion, will be transferred to the Group, which will invest RUB 4.6 billion of this amount into the projects of Ural charitable fund. In March 2015 the Moscow Court of Arbitration approved the settlement agreement between the Group and Ural-Invest. The transfer of assets did not occur as of the date of the issuance of the consolidated financial statements and therefore the Group did not recognize the gain in the consolidated statement of operations and comprehensive income.

3. BUSINESS COMBINATIONS

Business combinations in 2014

LesInvest – In September 2014, LesInvest, a wholly owned subsidiary of the Group, acquired 100% of the share capital of OJSC Segezha Pulp and Paper Mill and LLC Derevoobrabotka-Proekt (together with their subsidiaries – "LesInvest Group"), a leading manufacturer of sack paper and paper sacks and exporter of timber products and ply wood, for a total cash consideration of $287 million. The Group sees high growth potential for the LesInvest Group business, to be unlocked by improving operating efficiency and upgrading production facilities. The following table summarizes consideration paid and the amounts of the assets acquired and liabilities assumed that were recognized at the acquisition date:

Property, plant and equipment	**$**	110,917
Inventories		109,876
Deferred tax assets		76,047
Other assets		117,367
Accounts payable and other liabilities		(127,000)
Cash consideration paid	**$**	**287,207**

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

The purchase price allocation of LesInvest Group was not finalized as of the date of these consolidated financial statements, as the Group had not completed the valuation of individual assets and liabilities of LesInvest Group. The Group's consolidated financial statements reflect the allocation of the purchase price based on a preliminary fair value assessment of the assets acquired and liabilities assumed.

Other acquisitions – The information on other business combinations which took place in 2014 is summarized below:

Acquiree	Principal activity	Date of acquisition	Interest acquired	Acquiring segment	Purchase price
SMARTS-Ivanovo	Mobile operator	December	100%	MTS	7,480
SMARTS-Ufa	Mobile operator	December	100%	MTS	7,040
Penza-GSM	Mobile operator	December	100%	MTS	34,121
Step Group	Grain production	December	85%	Corporate	63,965
Total					**$ 112,606**

The following table summarizes the amounts of the assets acquired and liabilities assumed relating to such acquisitions at the acquisition date:

Current assets	$ 25,935
Property, plant and equipment	78,467
Rights to use radio frequencies	25,759
Goodwill	29,247
Other non-current assets	5,061
Current liabilities	(32,722)
Non-current liabilities	(9,546)
Noncontrolling interests	(9,595)
Purchase price	$ **112,606**

The purchase price allocations of SMARTS-Ivanovo**,** SMARTS-Ufa and Penza-GSM were not finalized as of the date of these financial statements as the Group had not completed the valuation of the individual assets of each entity. The Group's consolidated financial statements reflect the allocation of the purchase price based on a preliminary fair value assessment of the assets acquired and liabilities assumed. The excess of the consideration paid over the value of net assets in the amount of $29 million was preliminarily allocated to goodwill which was attributable to the MTS segment. Goodwill is mainly attributable to the expected synergies from combining the operations of MTS and acquired companies.

In December 2014, Krasnodar Agro, a wholly owned subsidiary of the Group, acquired 85% of the voting shares of the five grain producers in Krasnodar region (Step Group).

Pro forma results of operations (unaudited)

The following pro forma financial data for the years ended December 31, 2014 and 2013 give effect to the acquisition of LesInvest Group as if it had occurred as of January 1, 2013:

	2014	2013
Revenues	$ 17,130,212	$ 19,199,485
Net income	(3,346,547)	3,052,629

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

The pro forma information is based on various assumptions and estimates. The pro forma information is neither necessarily indicative of the operating results that would have occurred if the Group acquisitions had been consummated as of January 1, 2013, nor is it necessarily indicative of future operating results. The pro forma information does not give effect to any potential revenue enhancements or cost synergies or other operating efficiencies that could result from the acquisitions. The actual results of operations of these companies are included into the consolidated financial statements of the Group only from the respective dates of acquisition.

The following amounts of revenue and earnings of LesInvest Group since the acquisition date in September 2014 are included into the consolidated statement of operations and comprehensive income for the year ended December 31, 2014:

		2014
Net revenues	$	151,227
Net income		14,178

The results of operations of other acquired businesses have not been included because the effects of these business combinations, individually and in aggregate, were not material to the Group's consolidated results of operations.

Business combinations in 2013

SITRONICS-Nano – In May 2013, the Group acquired an additional 12.3% ownership interest in SITRONICS-Nano, previously an affiliate, from RUSNANO for cash consideration of RUB 2 billion ($61.1 million at the acquisition date) increasing its voting interest to 62.1%. Simultaneously, the Group and RUSNANO amended existing call and put option agreements. Under the amended agreements, the Group had a call option to acquire RUSNANO's shares in Sitronics-Nano for RUB 6.1 billion plus 7.63% p.a. at any time till November 1, 2017. RUSNANO had a put option to sell its remaining shares in SITRONICS-Nano for RUB 8.1 billion not earlier than October 31, 2016 and not later than November 1, 2017. This acquisition allowed the Group to secure its rights for use of 180 and 90 nanometre equipment that has been leased from SITRONICS-Nano.

As a result of the transactions, the Group obtained control over SITRONICS-Nano and accounted for this business combination by applying the acquisition method. The following table summarizes the consideration paid for SITRONICS-Nano and the assets acquired and liabilities assumed recognized at the acquisition date, as well as the fair value of the noncontrolling interests in the investee:

Current assets	$	73,231
Net investment in the lease		518,916
Current liabilities		(76,700)
Non-current liabilities		(18,829)
Noncontrolling interests		(187,164)
		309,454
Fair value of previously held interest		(248,309)
Cash consideration	**$**	**61,145**

As part of this business combination, the Group recognised a revaluation gain resulting from the remeasurement of its previously held interest. The difference in the amount of $22.4 million between the fair value of previously held interest and the carrying value of the Group's investment has been recorded within other operating expenses, net in the consolidated statement of operations and comprehensive income. The fair value of previously held interest and the noncontrolling interests in SITRONICS-Nano were estimated based on the amount of consideration in the transaction described above.

In May 2014, following the issuance of additional shares in Mikron, a subsidiary of RTI, such put and call option agreements between the Group and ROSNANO were amended (Note 5).

4. DISPOSALS

Disposals in 2014

NIIDAR-Nedvizhimost – In 2014, the Group sold its 100% interest in NIIDAR-Nedvizhimost, a subsidiary of RTI which managed rental property, for a total cash consideration of $150.0 million. As a result of this transaction, the Group recognized gain on disposal of subsidiaries of $139.1 million, included in other operating expenses in the consolidated statement of operations and comprehensive income.

Disposals in 2013

SG-trans – During 2013, the Group completed a reorganisation of its transportation assets. As a result of the reorganization, SG-trans, which was acquired in 2012 was split into two legal entities: SG-trading which comprised the non-core non-transportation assets and SG-trans which retained all the core transport assets. In April 2013 the Group sold a 70% stake in SG-trans to Financial Alliance, an affiliate of the Group, for cash consideration of RUB 12 billion ($380.2 million at the disposal date), thereby reducing its direct ownership in SG-trans from 100% to 30%.

Upon disposal, the Group deconsolidated SG-trans and accounted for its remaining interest using the equity method. As a result of the transaction, the Group recognized a gain of $4.0 million in the consolidated statement of operations and comprehensive income.

In July 2013, the Group further sold additional 15% of SG-trans to Unirail, a shareholder of Financial Alliance, for a cash consideration of RUB 2.5 billion ($76.4 million) with no gain or loss recognized as a result of this transaction.

RussNeft – In July 2013, the Group sold its 49% stake in RussNeft, the Group's affiliate, for cash consideration of $1,200 million. Prior to the disposal, the Group has been accounting for this investment using the equity method. As of the disposal date, the carrying value of the Group's investment in RussNeft was nil. Accordingly, the Group recognized a $1,200 million gain on this disposal being the difference between the consideration received and the carrying value of investment disposed.

5. CAPITAL TRANSACTIONS OF SUBSIDIARIES

Transactions in 2014

MTS Bank – In December 2014, the Group participated in additional share issue of MTS Bank for $309.0 million. The transaction resulted in no change in noncontrolling interests and additional paid-in capital.

Mikron – In May 2014, Mikron issued additional shares representing 25.1% of its share capital in exchange for 37.7% interest in SITRONICS-Nano, owned by OJSC RUSNANO. Upon completion of the transaction, the Group's effective ownership in Mikron decreased to 53.0%. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests and an increase of additional paid-in capital by $44.1 million. Simultaneously, the Group and RUSNANO substituted their existing put and call option agreements on RUSNANO's share in SITRONICS-Nano for new put and call option agreements on its 25.1% share in Mikron. The terms of the option agreements remained unchanged.

Business-Nedvizhimost – In April 2014, MTS sold a 49% stake in Business-Nedvizhimost, a company which owns and manages a real estate portfolio in Moscow, to the Company for $91.8 million. This transfer of ownership interest within the Group resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by $47.4 million.

NVision – In January 2014, the Group acquired an additional 38.75% stake in NVision from minority shareholders for $82.5 million, $37.5 million of which was paid in cash and $45.0 million in the Company's treasury shares. Upon completion of this transaction, the Group's ownership in NVision was 88.75%. The transaction was accounted for directly in equity and resulted in an increase of noncontrolling interests by $42.0 million and a decrease of additional paid-in capital by $121.8 million. In December 2014, the Group acquired the remaining 11.25% stake in NVision for approximately $10.0 million. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by $13.8 million and a decrease of additional paid-in capital by $24.0 million.

Transactions in 2013

Business-Nedvizhimost – In December 2013, MTS sold a 51% stake in Business-Nedvizhimost to the Company for RUB 3.2 billion ($98.5 million as of the transaction date). This transfer of ownership interest within the Group resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by $42.7 million.

RTI – In December 2013, RTI issued 4,687,500,000 common shares with par value of 1 Russan ruble which were acquired by existing shareholders, the Company and the Bank of Moscow, for cash consideration of RUB 6.0 billion ($183.9 million as of the purchase date) in proportion to their existing ownership interests. The Bank of Moscow received a put option to sell its 703,125,000 shares acquired upon their issuance to the Group at a price of $27.5 million plus 8.25% p.a. not earlier than December 26, 2016 and not later than December 26, 2018. As a result of this put option, the Group classified the underlying noncontrolling interests as redeemable.

Targin – In September 2013, the Company acquired a 100% stake in Bashneft Services Assets, (renamed to Targin in July 2014) from Bashneft for RUB 4.1 billion ($126.8 million as at transaction date). This transfer of ownership interest within the Group resulted in a decrease of noncontrolling interests and an increase of additional paid-in capital by $24.4 million.

MTS – In September-December 2013, the Group acquired 0.6% of MTS ordinary shares on the open market for $120.0 million. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by $23.0 million and a decrease of additional paid-in capital by $97.0 million.

Detsky mir – In September 2013, Detsky mir purchased 25%+1 of its own shares from Sberbank for cash consideration of $140.0 million. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by $5.4 million and a decrease of additional paid-in capital by $134.6 million. The Group took a long-term loan from Sberbank to fund the purchase. Simultaneously the Group has pledged these shares to Sberbank as security against the loan.

SITRONICS-N – In September 2013, the Group undertook restructuring of certain RTI assets. Upon completion of a series of transactions, SITRONICS, a subsidiary of RTI, spun off two companies, SITRONICS-N and RTI Microelectronics, with allocation of all its major assets and liabilities to these companies. To complete the restructuring process a 100% stake in SITRONICS was sold to SITRONICS-N for 1 RUB. In October 2013, the Company acquired a 100% stake in SITRONICS-N from RTI for RUB 1.0 billion ($31.0 million as at transaction date). This transaction resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by $11.0 million.

Mikron – In August 2013, Mikron issued 691,962 ordinary shares which were purchased by the RF for cash consideration of RUB 465 million ($14.1 million). This transaction was accounted for directly in equity and resulted in an increase of noncontrolling interests by $5.2 million and an increase of additional paid-in capital by $8.9 million.

MTS Bank – In April 2013, MTS acquired a 25.0945% stake in MTS Bank through the purchase of its additional share issuance for RUB 5 billion ($123 million). Upon completion of the transaction, the Group's effective ownership in MTS Bank decreased from 99% to 87%. This transfer of ownership interest within the Group resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by $105 million.

Capital transactions of Bashneft and its subsidiaries

UPC – In September 2014, the Group terminated a contract for the acquisition of a 98% stake in UPC from Bashneft. As a consequence of this transaction, Bashneft obtained control over UPC. This resulted in the Group's ownership in UPC decreasing from 99.0% to 78.0% and the Group's ownership in Ufaorgsintez decreasing from 86.5% to 78.7%. These transactions resulted in an increase of noncontrolling interests in the amount of $4.8 million and a decrease of additional paid-in capital by $20.9 million.

Bashneft-Polyus – On 23 May 2014, in accordance with an order from the Federal Agency for Subsoil Use ("Rosnedra") the Trebs and Titov oilfield license was transferred from Bashneft to its subsidiary Bashneft-Polyus. This transaction resulted in an increase in noncontrolling interests in the amount of $113.0 million with a corresponding decrease in the Group's constructive obligation to OJSC LUKOIL in the amount of $139.1 million and an increase in additional paid-in capital by $26.1 million.

Sistema-Invest – In May 2014, the reorganization of CJSC Sistema-Invest ("Sistema-Invest") was completed. 38,139,925 ordinary shares of Bashneft previously held by CJSC Bashneft-Invest, wholly-owned subsidiary of Bashneft created through a spinoff from Sistema-Invest, and 8,885,866 preferred shares bought back from the shareholders were cancelled. The transactions were accounted for directly in equity and resulted in a decrease of noncontrolling interests by $694.6 million and an increase of additional paid-in capital by $199.4 million. The Group's ownership in Bashneft increased from 75.0% to 78.8% and in BPGC – from 79.3% to 91.0%.

Ufaorgsintez – In March 2014, pursuant to the terms of a voluntary tender offer originally announced in December 2013, Ufaorgsintez completed the acquisition of its ordinary shares for a total consideration of $26.5 million. As a result, the Group's ownership in Ufaorgsintez increased from 76.8% to 86.5%. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by $49.5 million and an increase of additional paid-in capital by $22.5 million.

UPC – In September 2013, the Company acquired a 98% stake in United Petrochemical Company ("UPC") from Bashneft for RUB 6.2 billion ($192.0 million as at transaction date), which resulted in a decrease of noncontrolling interests and an increase of additional paid-in capital by $41.4 million.

6. REENTRY INTO UZBEKISTAN

Following unsuccessful tenders on sale of Uzdunrobita equipment, the representatives of the Republic of Uzbekistan and MTS commenced negotiations in relation to the return of MTS to the market. In July 2014, MTS signed a settlement agreement with the Republic of Uzbekistan eliminating all mutual claims ("Settlement Agreement"). International arbitration proceedings between MTS and the Republic of Uzbekistan in the International Center for Settlement of Investment Disputes, Member of the World Bank Group (ICSID), were discontinued following the submission of a joint application by the both parties.

The government authorities provided certain guarantees to MTS in relation to the protection of any future investment in the Republic of Uzbekistan to encourage the return of MTS to the market. Also, the Republic of Uzbekistan established a legal entity, Universal Mobile Systems LLC ("UMS"), with such entity having no legal connection to the previously liquidated entity, Uzdunrobita. UMS was granted 2G, 3G and LTE licenses and received frequencies, numbering capacity and other permits required for the launch of operations.

In September 2014, a 50.01% ownership interest in UMS was transferred to the Group by a state-owned enterprise established and managed by the State committee for communications, development of information systems and telecommunications technologies of the Republic of Uzbekistan, which retained the remaining 49.99% in UMS.The Group concluded that, upon receiving the 50.01% ownership interest, the Group obtained control over UMS and consolidated the entity. The Group estimated the fair value of the entity's assets and liabilities, as well as the noncontrolling interests in UMS as of the date of the transfer, and recognized a gain from reentry into Uzbekistan pursuant to the Settlement Agreement in the amount of $181 million.

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

The Group has determined that the Settlement Agreement primarily addressed two separate elements – the elimination of all mutual claims and guarantees granted to MTS in connection with its reentry into the Republic of Uzbekistan. The Group concluded that the aforementioned consideration of $181 million related to, in its entirety, a financial incentive to encourage the reentry into the Republic of Uzbekistan and as such, recognition in continuing operations was appropriate. No element was allocated to the non-satisfaction and elimination of mutual claims as this was deemed to have minimal value.

The following table summarizes the amounts of the assets and liabilities recognized at the date of obtaining control, as well as the fair value of the noncontrolling interests at that date:

Property, plant and equipment	$	119,211
Intangible assets		132,333
Other non-current assets		31,610
Noncontrolling interests		(101,849)
Gain from reentry into Uzbekistan	$	**181,305**

7. ASSETS FROM BANKING ACTIVITIES

Assets from banking activities, net of an allowance for loan losses, as of December 31, 2014 and 2013 consisted of the following:

		2014		2013
Cash and cash equivalents	$	843,715	$	1,132,368
Loans to customers		2,597,696		4,842,982
Investments in securities (trading)		368,567		551,513
Loans to banks		131,919		161,229
Investments in securities (available-for-sale)		87,652		154,356
Other investments		85,956		127,096
Less: allowance for loan losses		(560,942)		(516,575)
Assets from banking activities, net		3,554,563		6,452,969
Less: amounts maturing after one year		(1,374,367)		(2,554,229)
Assets from banking activities, current portion	**$**	**2,180,196**	**$**	**3,898,740**

Major categories of loans to customers as of December 31, 2014 and 2013 comprise the following:

		2014		2013
Corporate customers	$	1,294,744	$	2,739,345
Individuals		1,302,952		2,103,637
Total	**$**	**2,597,696**	**$**	**4,842,982**

As of December 31, 2014, 79.7% and 0.6% of the balance of loans to corporate customers and individuals, respectively, were evaluated individually for impairment (2013: 80.0% and 0.5%).

The following table presents the effective average interest rates by category of loans as of December 31, 2014 and 2013:

	2014			2013		
	RUB	USD	Other	RUB	USD	Other
Loans to customers						
- corporate customers	10.5%	8.8%	9.2%	10.8%	7.0%	9.8%
- individuals	19.0%	4.4%	6.5%	23.4%	8.3%	4.2%
Loans to banks	7.9%	0.01%	0.01%	4.5%	0.1%	0.1%

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

The movement in the allowance for loan losses in 2014 and 2013 was as follows:

	2014	2013
Allowance for loan losses, beginning of the year	$ 516,575	$ 329,803
Additions charged to operating results less recovery of allowance	423,121	248,032
Amounts written off against the allowance	(162,705)	(37,185)
Currency translation adjustment	(216,049)	(24,075)
Allowance for loan losses, end of the year	**$ 560,942**	**$ 516,575**

8. SHORT-TERM INVESTMENTS

Short-term investments as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Bank deposits with original maturities exceeding three months	$ 202,644	$ 647,077
Trading securities	97,550	499,437
Available-for-sale securities	74,149	354,838
Promissory notes and loans	104,998	61,195
Total	**$ 479,341**	**$ 1,562,547**

Promissory notes and loans to third parties are primarily denominated in USD and bear interest rates varying from 4.0% to 6.0% as of December 31, 2014.

The effective interest rates on bank deposits with original maturities exceeding three months as of December 31, 2014 are between 1.0% and 5.3% (December 31, 2013: 4.2% and 14.0%).

9. ACCOUNTS RECEIVABLE

Accounts receivable, net of provision for doubtful accounts, as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Trade receivables	$ 1,246,580	$ 1,808,403
Less: provision for doubtful accounts	(83,488)	(177,810)
Total	**$ 1,163,092**	**$ 1,630,593**

Write-off of trade receivables against provision for doubtful accounts in 2014 and 2013 amounted to $134.7 million and $96.5 million respectively.

10. OTHER CURRENT ASSETS

Other current assets as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Prepaid expenses and other receivables	$ 564,594	$ 763,791
Tax advances and overpayments	121,360	136,164
Advances paid to third parties	242,184	246,727
	928,138	**1,146,682**
Less: provision for doubtful accounts	(96,078)	(62,135)
Total	**$ 832,060**	**$ 1,084,547**

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

11. INVENTORIES AND SPARE PARTS

Inventories and spare parts as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Finished goods and goods for resale	$ 405,243	$ 593,500
Raw materials and spare parts	232,248	377,292
Work-in-progress	89,506	151,434
Costs and estimated earnings in excess of billings on uncompleted contracts	531,052	116,984
	1,258,049	**1,239,210**
Less: long-term portion	(13,540)	(107,908)
Total	**$ 1,244,509**	**$ 1,131,302**

12. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, net of accumulated depreciation, as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Switches, transmission devices, network and base station equipment	$ 9,066,682	$ 14,083,007
Buildings and leasehold improvements	1,392,585	2,166,179
Power and utilities	496,303	760,686
Other plant, machinery and equipment	1,495,420	2,620,291
Construction in progress and equipment for installation	897,260	1,576,285
Land	148,238	160,973
	13,496,488	**21,367,421**
Less: accumulated depreciation	(6,305,094)	(10,216,080)
Total	**$ 7,191,394**	**$ 11,151,341**

Depreciation expense for the years ended December 31, 2014 and 2013 amounted to $1,778.6 million and $2,089 million respectively.

Impairments of property, plant and equipment for the years ended December 31, 2014 and 2013 amounted to $290.4 million and $285.9 million respectively (Note 15).

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

13. GOODWILL

The carrying amounts of goodwill attributable to each reportable segment are as follows:

	MTS	SSTL	RTI	MTS Bank	Other	Total
Balance as of January 1, 2013						
Gross amount of goodwill	1,441,836	339,059	278,449	67,919	95,636	2,222,899
Accumulated impairment loss	(48,261)	(339,059)	-	(67,919)	-	(455,239)
	$ 1,393,575	**$ -**	**$ 278,449**	**$ -**	**$ 95,636**	**$ 1,767,660**
Impairment (Note 15)	-	-	(258,048)	-	-	(258,048)
Disposals	(722)	-	-	-	(67,816)	(68,538)
Currency translation adjustment	(93,958)	-	(17,210)	-	(2,127)	(113,295)
Balance as of December 31, 2013						
Gross amount of goodwill	1,343,717	300,047	254,291	63,068	25,693	1,986,816
Accumulated impairment loss	(44,822)	(300,047)	(251,100)	(63,068)	-	(659,037)
	$ 1,298,895	**$ -**	**$ 3,191**	**$ -**	**$ 25,693**	**$ 1,327,779**
Business combinations (Note 3)	29,247	-	-	-	-	29,247
Currency translation adjustment	(524,502)	-	(1,335)	-	(13,652)	(539,489)
Balance as of December 31, 2014						
Gross amount of goodwill	829,716	293,424	147,937	36,691	12,041	1,319,809
Accumulated impairment loss	(26,076)	(293,424)	(146,081)	(36,691)	-	(502,272)
	$ 803,640	**$ -**	**$ 1,856**	**$ -**	**$ 12,041**	**$ 817,537**

14. OTHER INTANGIBLE ASSETS

Intangible assets other than goodwill as of December 31, 2014 and 2013 consisted of the following:

	2014			2013		
	Gross carrying value	Accumu-lated amortization	Net carrying value	Gross carrying value	Accumu-lated amortization	Net carrying value
Amortized intangible assets:						
Billing and telecommunication software	$ 974,142	(603,303)	370,839	1,053,559	(580,156)	473,403
Operating licenses	704,536	(214,352)	490,184	768,488	(157,778)	610,710
Radio frequencies	203,419	(101,034)	102,385	301,042	(149,954)	151,088
Acquired customer base and customer relationships	225,495	(136,714)	88,781	468,497	(247,643)	220,854
Software and other	855,003	(376,890)	478,113	973,084	(481,941)	491,143
	2,962,595	**(1,432,293)**	**1,530,302**	**3,564,670**	**(1,617,472)**	**1,947,198**
Unamortized intangible assets:						
Trademarks	184,811	-	184,811	206,135	-	206,135
Numbering capacity with indefinite contractual life	6,276	-	6,276	9,367	-	9,367
Total	**$ 3,153,682**	**(1,432,293)**	**1,721,389**	**3,780,172**	**(1,617,472)**	**2,162,700**

Impairments of intangible assets other than goodwill for the years ended December 31, 2014 and 2013 amounted to $nil and $298.2 million respectively (Note 15).

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

Amortization expense recorded on other intangible assets for the years ended December 31, 2014 and 2013 amounted to $513.5 million and $544.6 million, respectively. The estimated amortization expense for the five years ending December 31, 2019 and thereafter is as follows:

Year ending December 31,		
2015	$	367,272
2016		306,060
2017		214,242
2018		122,424
2019		61,212
Thereafter		459,092
	$	**1,530,302**

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

15. IMPAIRMENT OF OTHER ASSETS

Impairment of other assets recognized by the Group in the years ended December 31, 2014 and 2013 comprised the following:

		2014		2013
Impairment of long-lived assets in India	$	290,438	$	-
Impairment of 180 and 90 nm equipment and intangible assets		-		357,906
Impairment of system integration intangible assets		-		125,747
Impairment of other long-lived assets		175,386		106,753
Impairment of available-for-sale securities		135,000		-
Provision for cash and deposits in Delta Bank (Ukraine)		92,517		-
Provision for doubtful accounts		103,625		134,392
Inventory obsolescence		30,442		46,504
Other		37,221		33,243
Total impairments of other assets	**$**	**864,629**	**$**	**804,545**

Impairment of long-lived assets in India – As of December 31, 2014, following the continuing operating losses incurred by SSTL, the Group carried out a review of the recoverable amount of its long-lived assets attributable to the SSTL segment. The Group concluded that the segment's fixed assets with a carrying value of $290.4 million were impaired and recognized a loss in the consolidated statement of operations and comprehensive income for the year ended December 31, 2014, which was allocated to the SSTL segment.

The segment's remaining long-lived assets mostly comprise spectrum and licenses with the total carrying value of $306.3 million. The Group conducted their impairment analysis based on the available market data. The market data utilizes the data of the recent spectrum auction in India. The auction in March 2015 demonstrated significant demand for spectrum in the 800 MHz spectrum bands in the circles of SSTL operations at prices significantly higher than the carrying value of equivalent bands owned by SSTL. Therefore, the Group has concluded that the carrying value of SSTL spectrum and licenses was not impaired as of December 31, 2014.

Impairment of 180 and 90 nm equipment and intangibles assets – As of December 31, 2013 the Group carried out a review of the recoverable amount of long-lived assets used in the production of microchips. As a result of this impairment review, an impairment charge of $357.9 million was recognized in the consolidated statement of operations and comprehensive income for the year ended December 31, 2013, which was allocated to the RTI segment.

As of December 31, 2014, the Group identified indicators that the carrying amounts of 180 and 90 nm equipment with a total carrying value of $108.4 million may not be recoverable. These indicators included lower than expected revenue and profitability levels. The Group carried out review that supported the carrying value of the equipment and indicated that no additional impairment is required.

The estimated fair value of such long-lived assets was determined based on unobservable inputs (“Level 3” of the hierarchy established by U.S. GAAP guidance). When calculating the future cash flows used in the assessment of the fair value of long-lived assets, the Group considered historical and projected revenue and operating costs, market conditions, asset ages, asset utilization and other relevant information. The key assumptions used in the fair value calculations included pre-tax discount rate of 25.0%-56.3% depending on the business line (2013: 21.5%-43.8%), compound annual growth rate during the projected twelve-year period of 21.8% (2013: 11.7%), growth rate after that period of 2.3% (2013: 2.3%).

Impairment of system integration intangible assets – During the year ended December 31, 2013, the Group identified indicators that the carrying amounts of long-lived assets attributable to NVision, a subsidiary of RTI, may not be recoverable. These indicators included lower than expected revenue and profitability levels and downward revisions to management’s forecasts for the NVision business.

Subsequent to its acquisition by the Group in 2012, NVision experienced a significant decrease in purchases made by its key customers and, as a result, revenue forecasts were substantially reduced as compared to those existing at the acquisition date. Based on the revised forecasts, the Group determined that the carrying value of the NVision asset group exceeded its undiscounted cash flows. The Group then compared the fair value of the asset group to its carrying value and determined the impairment loss. The impairment loss was allocated to the carrying values of the long-lived assets, but not below their individual fair values. The Group estimated the fair value of the assets primarily using an income approach based on unobservable inputs (“Level 3” of the hierarchy established by U.S. GAAP guidance), with the key assumptions including a discount rate of 16.5% and 3-7% of revenue royalty payments for the trademark. The decline in the fair value of the NVision reporting unit and its intangible assets, as well as fair value changes for other assets and liabilities in the two-step goodwill impairment test, resulted in an implied fair value of goodwill being substantially below its carrying value.

As a result of the impairment review, for certain intangible assets with a carrying value of $129.1 million the Group concluded that the fair value amounted to $3.3 million and recorded an impairment charge of $125.7 million in the consolidated statement of operations and comprehensive income for the year ended December 31, 2013. The Group also recorded an impairment charge on goodwill of $258.0 million based on its implied fair value. The relevant impairment charges were allocated to the RTI segment.

Provision for cash and deposits in Delta Bank (Ukraine) – As of December 31, 2014, MTS Ukraine, a subsdiary of MTS, held $90.2 million in current accounts and deposits in Delta Bank, the fourth largest bank in Ukraine. In December 2014, Delta Bank delayed customer payments and put limits on cash withdrawals. In March 2015, the National Bank of Ukraine adopted a resolution declaring Delta Bank to be insolvent. The Group treated Delta Bank’s insolvency as a recognized subsequent event and provided against the full amount of deposited funds ($90.2 million) and related interest ($2.3 million).

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

16. INVESTMENTS IN AFFILIATES

Investments in affiliates as of December 31, 2014 and 2013 consisted of the following:

	2014		2013	
	Voting power	Carrying value	Voting power	Carrying value
MTS Belarus	49.0%	$ 107,237	49.0%	$ 165,174
OZON	21.6%	91,080	-	-
SG-trans (2013: SG-trans and Financial Alliance, Note 4)	50.0%	83,555	50.0%	133,551
Concept Group	40.0%	18,913	-	-
Other		55,233		66,541
Total		**$ 356,018**		**$ 365,266**

Investment in OZON – In April 2014, the Group acquired a 21.6% of ownership interest in OZON Holdings Limited ("OZON"), a leading Russian e-commerce company, through an additional share issuance for $150.0 million. The Group has the right to nominate two out of eight representatives to the board of directors. Management concluded that, upon completion of the acquisition, the Group gained significant influence over OZON and therefore adopted equity method of accounting for this investment. The Group also obtained a call option for an additional 4.6% stake in OZON exercisable through August 2015. The difference between the equity investment carrying amount of $91 million and underlying equity in net assets as of December 31, 2014 of $26.0 million represents equity-method goodwill, mainly attributable to the expected synergies from commercial arrangements and co-branding programs.

Investment in Concept Group – In October 2014, the Group acquired a 40% of ownership interest in Rangecroft Ltd, a holding company of Concept Group, one of Russia's leading fashion clothing retailers, for $26.0 million, and obtained a call option to acquire another 14.2% of its share capital exercisable till October 2017. In accordance with the shareholders agreement, the Group has the right to nominate three out of nine representatives to the board of directors and, if the call option is exercised, up to five of the nine representatives. A number of key operating decisions for Concept Group, including an approval of an operating budget, require seven out of nine votes; such operating decisions represent participating rights of the shareholders. As a consequence of this, the Group has concluded that it does not have control over the investee and has therefore adopted the equity method of accounting for this investment.

Merger of SG-trans and Finance Alliance – In January 2014, SG-trans and Finance Alliance merged into a single legal entity named SG-trans. The Group retained 50% beneficial interest in the newly established entity.

The financial position and results of operations of significant affiliates as of and for the year ended December 31, 2014 were as follows:

	(unaudited)			
	MTS Belarus	OZON	SG-trans	Concept Group
Total assets	$ 303,315	192,860	641,193	91,607
Total liabilities	(94,102)	(71,403)	(453,119)	(65,646)
Net income/(loss)	194,317	(77,690)	12,059	5,792

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

The financial position and results of operations of significant Group affiliates as of and for the year ended December 31, 2013 were as follows:

		(unaudited)	
		MTS Belarus	**Financial Alliance[1]**
Total assets	$	379,050	1,480,703
Total liabilities		(96,580)	(1,185,979)
Net income/(loss)		145,975	13,435

[1] Including SG-trans amounts.

17. LONG-TERM INVESTMENTS

Long-term investments as of December 31, 2014 and 2013 consisted of the following:

		2014		**2013**
Bank deposits	$	242,006	$	90,727
Loans and notes		51,400		129,638
Other		23,219		28,706
Total	**$**	**316,625**	**$**	**249,071**

The effective interest rates on long-term investments as of December 31, 2014 were between 6.2% and 6.3% for EUR denominated investments (2013: 6.0% – 8.6%).

18. LIABILITIES FROM BANKING ACTIVITIES

Liabilities from banking activities as of December 31, 2014 and 2013 consisted of the following:

		2014		**2013**
Term deposits	$	1,567,548	$	2,561,569
Deposits repayable on demand		537,365		1,859,832
Promissory notes issued and other liabilities		243,438		215,539
		2,348,351		**4,636,940**
Less: amounts maturing within one year		(2,180,491)		(3,864,415)
Total liabilities from banking activities, net of current portion	**$**	**167,860**	**$**	**772,525**

As of December 31, 2014 the fair value of liabilities from banking activities amounted to $2,270 million; as of December 31, 2013 – approximated their carrying value.

The following table presents the effective average interest rates by categories of bank deposits and notes issued as of December 31, 2014 and 2013:

	2014			**2013**		
	RUB	**USD**	**Other**	**RUB**	**USD**	**Other**
Term deposits:						
- corporate customers	14.5%	3.0%	2.9%	7.4%	1.8%	2.1%
- individuals	10.0%	3.7%	3.4%	9.7%	3.7%	2.3%
Promissory notes issued	8.0%	-	-	7.3%	-	-
Deposits repayable on demand:						
- corporate customers	0.5%	-	-	4.9%	-	-
- individuals	0.5%	0.1%	0.2%	0.6%	0.07%	0.1%

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

19. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Customers' advances	$ 546,793	$ 350,896
Accrued payroll	267,971	430,946
Accruals for services	210,924	328,050
Accrued interest on loans	51,805	74,621
Financial instruments at fair value	47,086	13,199
Dividends payable	1,369	6,729
Other	189,708	363,449
Total	**$ 1,315,656**	**$ 1,567,890**

20. LONG-TERM DEBT

Long-term debt as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Loans from banks and financial institutions	$ 5,049,820	$ 5,447,071
Notes and corporate bonds	2,781,512	4,888,603
Capital leases	239,401	80,506
Loans from related parties	37	64
Vendor financing	16,662	31,871
Other borrowings	45,393	29,957
	8,132,825	**10,478,072**
Less: amounts maturing within one year	(1,598,770)	(2,102,911)
Total	**$ 6,534,055**	**$ 8,375,161**

The schedule of repayments of long-term debt for the next five years and thereafter is as follows:

Year ended December 31	
2015	$ 1,598,770
2016	1,185,257
2017	1,469,871
2018	1,022,949
2019	1,148,236
Thereafter	1,707,742
Total	**$ 8,132,825**

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

Loans from banks and financial institutions – Loans from banks and financial institutions as of December 31, 2014 and 2013 consisted of the following:

	Maturity	Interest rate (as at December 31, 2014)	2014	2013
USD-denominated:				
Calyon, ING Bank, Nordea Bank, Raiffeisen Zentralbank Osterreich	2015-2020	LIBOR+1.15% (1.51%)	$ 673,698	$ 798,440
China Development Bank	2015-2018	LIBOR+1.5% (1.86%)	179,421	187,497
Bank of China	2015-2021	LIBOR+1.5%-3.5% (1.86%-3.86%)	170,552	170,615
Skandinavska Enskilda Banken	2015-2017	LIBOR+0.23%-1.8% (0.59%-2.16%)	91,987	129,494
Bank of Moscow	2015	LIBOR+7.5% (7.76%)	82,552	82,552
HSBC Bank and ING BHF Bank			-	12,022
Other			14,230	27,223
			1,212,440	**1,407,843**
EUR-denominated:				
Credit Agricole Corporate Bank and BNP Paribas	2015-2018	EURIBOR+1.65% (1.82%)	33,649	47,574
Bank of Moscow	2015-2017	EURIBOR+5.0% (5.15%)	27,333	-
LBBW	2015-2017	EURIBOR+1.52% (1.69%)	16,995	25,630
Bank of China			-	74,403
Other			12,187	14,398
			90,164	**162,005**
RUB-denominated:				
Sberbank	2015-2021	8.45%-15.0%	3,007,244	2,922,817
Gazprombank	2015-2018	9.0%-10.6%	253,170	294,439
Raiffeisenbank	2015-2016	Mosprime+1.45%-5.25% (23.42%-29.02%), 9.45%	149,568	71,891
Bank of Moscow	2015-2018	CBR+3.0% (11.25%); Mosprime+4.5%-8.85% (28.27%-31.02%);	128,993	256,258
VTB	2015-2018	9.0%-22.75%	86,461	77,571
Unicredit	2016	Mosprime+5.2% (12.17%); 10.1-10.4%	37,179	73,248
Alfa-Bank	2015	9.75%-14.18%	27,143	92,486
Credit bank of Moscow	2016	19.0%	8,888	30,554
Other			30,928	53,560
			3,729,574	**3,872,824**
Other currencies			17,642	4,399
Total			**$ 5,049,820**	**$ 5,447,071**

The fair value of loans from banks and financial institutions, including the current portion, is estimated using discounted cash flows and market-based expectations for interest rates, credit risk and the contractual terms of the debt instruments ("Level 2" of the hierarchy established by the U.S. GAAP guidance). As of December 31, 2014 the fair value of loans from banks and financial institutions, including the current portion, amounted to $4,730 million; as of December 31, 2013 – approximates their carrying value.

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

Notes and corporate bonds – Notes and corporate bonds as of December 31, 2014 and 2013 consisted of the following:

		2014			2013
	Currency	**Interest rate**	**Fair value**	**Carrying value**	**Carrying value**
MTS International Notes due 2020	USD	8.625%	$ 601,019	$ 623,140	$ 747,634
MTS International Notes due 2023	USD	5.00%	369,641	478,500	500,000
Sistema International Bonds due 2019	USD	6.95%	338,193	464,979	487,854
MTS OJSC Notes due 2020	RUB	8.15%	253,296	266,627	458,306
SSTL Bonds due 2019	INR	15.75%	202,111	202,111	206,795
MTS OJSC Notes due 2023	RUB	8.25%	133,313	177,751	305,538
MTS OJSC Notes due 2017	RUB	8.70%	151,181	171,894	294,191
Sistema JSFC Bonds due 2016	RUB	8.75%	113,840	145,949	329,790
MTS OJSC Notes due 2015	RUB	7.75%	131,364	134,045	230,567
Sistema JSFC Bonds due 2016	RUB	7.65%	60,376	65,271	406,985
MTS OJSC Notes due 2016	RUB	8.75%	29,851	31,780	54,627
DM-Center Bonds due 2015	RUB	8.50%	16,238	16,418	35,137
MTS OJSC Notes due 2018	RUB	12.00%	2,298	2,419	117,442
MTS OJSC Notes due 2014	RUB	-	-	-	416,098
Sistema JSFC Bonds due 2014	RUB	-	-	-	296,544
Other			531	628	1,095
Total			**$ 2,403,252**	**$ 2,781,512**	**$ 4,888,603**

All Group RUB-denominated notes and corporate bonds are traded on Moscow Exchange. USD-denominated notes issued by MTS International due 2020 and 2023 and Sistema International due 2019 are traded on the Irish Stock Exchange. The fair values of notes and corporate bonds are based on the market quotes as of December 31, 2014 at the exchanges which they are traded on.

In certain instances the Group has an unconditional obligation to repurchase notes at par value if claimed by the noteholders, where a subsequent sequential coupon is announced. The notes therefore can be defined as callable obligations under the FASB authoritative guidance on debt, as the holders have the unilateral right to demand repurchase of the notes at par value upon announcement of new coupons. The FASB authoritative guidance on debt requires callable obligations to be disclosed as maturing in the reporting period when the demand for repurchase could be submitted disregarding the expectations of the Group about the intentions of the noteholders. The Group discloses such notes in the aggregated maturities schedule in the reporting periods when the noteholders have the unilateral right to demand repurchase. The dates of the announcement for each particular note issue are as follows:

MTS OJSC Notes due 2018	December 2015
MTS OJSC Notes due 2020	November 2015
MTS OJSC Notes due 2023	March 2018

Available credit facilities – As of December 31, 2014, the Group's total available unused credit facilities amounted to $1,344.2 million and related to the following credit lines:

	Maturity	**Interest rate**	**Available till**	**Available amount**
Sberbank	2015 – 2018	9.3% - 18%	2015 – 2018	766,013
CitiBank Europe	2024	LIBOR 6M+0.9%;	2015	300,009
Gazprombank	2016 – 2021	9.75% - 25%	2016 – 2021	198,291
ING Bank Eurasia	2015	Mosprime/LIBOR/ EURIBOR + 1.50%	2015	44,438
Other				35,468
Total				**$ 1,344,219**

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

Covenants – Loans and notes payable by the Group are subject to various restrictive covenants, including, but not limited to compliance with certain financial ratios, limitations on dispositions of assets and transactions within the Group and retention of principal telecom licenses. The adverse court's ruling in respect of the Bashneft shares owned by the Group and their further disposition (Note 2) gave certain lenders the right to call the debt under several loan agreements. The lenders waived their rights to demand early repayment with regard to these covenant violations prior to the issuance date of these consolidated financial statements, and the Group retained noncurrent classification for this long-term debt in its consolidated statement of financial position as of December 31, 2014. As of December 31, 2014, the Group also had $138.5 million of its RUB-denominated long-term debt which was presented within current liabilities in the consolidated statement of financial position because of non-compliance with certain financial ratios by its subsidiaries.

21. INCOME TAX

The Group's income tax expense for the years ended December 31, 2014 and 2013 was as follows:

	2014	2013
Current provision	$ 417,079	$ 619,643
Deferred income tax expense	36,338	222,464
Total	**$ 453,417**	**$ 842,107**

Income tax expense calculated by applying the Russian statutory income tax rate of 20% to income from continuing operations before income tax differs from income tax expense recognized in the consolidated statements of operations and comprehensive income as a consequence of the following adjustments:

	2014	2013
Income tax expense computed on income from continuing operations before income tax at the Russian statutory income tax rate	$ 118,256	$ 504,164
Adjustments due to:		
Equity in earnings of subsidiaries	147,678	144,647
Other non-deductible expenses	98,094	129,330
Change in valuation allowance	165,819	148,909
Settlements with tax authorities	11,553	(9,108)
Effect of rates different from standard	(43,477)	(44,044)
Currency exchange and translation differences	(5,685)	(10,828)
Non-taxable income	(21,491)	-
Other	(17,330)	(20,963)
Income tax expense	**$ 453,417**	**$ 842,107**

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

The tax effects of temporary differences that give rise to the deferred tax assets and liabilities are presented below:

	2014	2013
Deferred tax assets:		
Tax losses carried forward	$ 1,088,645	$ 855,851
Accrued expenses and accounts payable	165,569	248,061
Property, plant and equipment	243,112	152,210
Intangible assets	143,917	182,846
Other	111,686	209,147
	1,752,929	**1,648,115**
Less: valuation allowance	(1,194,858)	(996,221)
Total deferred tax assets	**558,071**	**651,894**
Deferred tax liabilities:		
Property, plant and equipment	(348,206)	(534,109)
Intangible assets	(219,907)	(218,014)
Undistributed earnings of subsidiaries and affiliates	(124,444)	(208,995)
Other	(79,655)	(79,752)
Total deferred tax liabilities	**$ (772,212)**	**$ (1,040,870)**
Net deferred tax assets, current portion	$ 245,571	$ 330,388
Net deferred tax assets, long-term portion	392,866	297,419
Net deferred tax liabilities, current portion	(64,947)	(114,192)
Net deferred tax liabilities, long-term portion	(787,631)	(902,591)

The Group has the following balances for income tax losses carried forward as of December 31, 2014 and 2013:

Jurisdiction	**Period for carry-forward**	**2014**	**2013**
India	2015-2020	$ 521,547	$ 483,680
Russia	2015-2024	442,370	246,870
Luxembourg	Unlimited	124,728	125,301
Total		**$ 1,088,645**	**$ 855,851**

Management has established valuation allowances against certain deferred tax assets, which are less likely than not to be realized in future periods. In evaluating the Group's ability to realize its deferred tax assets, the Company considers all available positive and negative evidence, including operating results, ongoing tax planning, and forecasts of future taxable income on a jurisdiction by jurisdiction basis. The valuation allowance as of December 31, 2014 and 2013 relates to the following deferred tax assets:

	2014	2013
Tax losses carried forward	$ 850,118	$ 689,731
Sale of investment in Svyazinvest	51,103	65,996
Impairment of long-lived assets in SSTL	128,286	70,194
Other	165,351	170,300
Total	**$ 1,194,858**	**$ 996,221**

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

22. HEDGING ACTIVITIES

The Group regularly enters into variable-to-fixed interest rate swap agreements to manage exposure to changes in variable interest rates related to its debt obligations. The instruments qualify for cash flow hedge accounting under U.S. GAAP. Each interest rate swap matches the exact maturity dates of the underlying debt allowing for highly-effective hedges. Interest rate swap contracts outstanding as of December 31, 2014 mature in 2015, 2018 and 2020

In addition to the above, the Group has also entered into several cross-currency interest rate swap agreements. These contracts hedged the risk of both interest rate and currency fluctuations and assumed periodic exchanges of both principal and interest payments from RUB-denominated amounts to USD- and Euro- denominated amounts to be exchanged at a specified rate. The rate was determined by the market spot rate upon issuance. Cross-currency interest rate swap contracts mature in 2019-2020. The Group entered into cross-currency interest rate swap agreements designated to manage the exposure of changes in variable interest rate and currency exchange rate for 21.7% of its USD- and Euro- denominated bank loans and Eurobonds outstanding as of December 31, 2014.

The following table presents the fair value of the Group's derivative instruments designated as hedges in the consolidated statements of financial position December 31, 2014 and 2013.

	Location		2014		2013
Assets					
Cross-currency interest rate swaps	Other non-current assets	$	389,915	$	55,760
Interest rate swaps	Other non-current assets		142		367
Total			**390,057**		**56,127**
Liabilities					
Interest rate swaps	Accrued expenses and other current liabilities		(47,086)		(13,199)
Total		**$**	**(47,086)**	**$**	**(13,199)**

The following table presents the effect of the Group's derivative instruments designated as hedges (i.e. gain/(loss) recognized) in the consolidated statements of operations and comprehensive income for the years ended December 31, 2014 and 2013. The amounts presented include the ineffective portion of derivative instruments and the amounts reclassified into earnings from accumulated other comprehensive income.

	Location		2014		2013
Interest rate swaps, including ineffective portion of 4,503 and (879)	Interest income / (expense)	$	6,012	$	(5,778)
Cross-currency interest rate swaps, including ineffective portion of (60,252) and nil	Foreign currency transaction loss / (gain)		397,901		(24,397)
Total		**$**	**403,913**	**$**	**(30,175)**

The following table presents the effect of the Group's agreements designated as hedges in accumulated other comprehensive income for the years ended December 31, 2014 and 2013 (net of tax).

		2014		2013
Accumulated gain, beginning of the year	$	46,210	$	807
Fair value adjustments		376,582		21,697
Reclassified into earnings		(303,683)		23,706
Accumulated gain	**$**	**119,109**	**$**	**46,210**

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

As of December 31, 2014, the outstanding hedging instruments were highly effective. $18.0 million of accumulated gain is expected to be reclassified into net income during the next twelve months.

Cash inflows and outflows related to hedging instruments were included in cash flows from operating and financing activities in the consolidated statements of cash flows for the years ended December 31, 2014 and 2013.

23. FAIR VALUE MEASUREMENTS

The following fair value hierarchy table presents information regarding the Group's assets and liabilities measured at fair value on a recurring basis as of December 31, 2014 and 2013:

	Fair value measurements using			
	Quoted prices in active markets for identical assets (Level 1)	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total fair value**
December 31, 2014				
Assets at fair value:				
Trading securities	$ 466,117	$ -	$ -	$ 466,117
Available-for-sale securities	158,370	-	3,431	161,801
Derivative instruments	-	390,057	-	390,057
Total assets	**624,487**	**390,057**	**3,431**	**1,017,975**
Liabilities at fair value:				
Derivative instruments	(12,128)	(59,933)	-	(72,061)
Contingent consideration	-	-	(1,760)	(1,760)
Redeemable noncontrolling interests	-	-	(56,734)	(56,734)
Total liabilities	**$ (12,128)**	**$ (59,933)**	**$ (58,494)**	**$ (130,555)**
December 31, 2013				
Assets at fair value:				
Trading securities	$ 1,050,950	$ -	$ -	$ 1,050,950
Available-for-sale securities	248,534	253,255	7,405	509,194
Derivative instruments	1,575	56,127	-	57,702
Total assets	**1,301,059**	**309,382**	**7,405**	**1,617,846**
Liabilities at fair value:				
Derivative instruments	-	(12,863)	-	(12,863)
Contingent consideration	-	-	(336)	(336)
Redeemable noncontrolling interests	-	-	(89,583)	(89,583)
Total liabilities	**$ -**	**$ (12,863)**	**$ (89,919)**	**$ (102,782)**

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

24. SHARE CAPITAL

As of December 31, 2014 and 2013, the Company had 9,650,000,000 voting common shares with a par value of RUB 0.09 issued, of which 9,435,902,596 and 9,274,755,045 shares were outstanding, respectively.

Dividends declared by the Company in the years ended December 31, 2014 and 2013 are as follows:

	2014	2013
Dividends declared (including dividends on treasury shares of $16,842 and $8,080 respectively)	591,099	283,200

Accumulated other comprehensive loss – The following table represents components of accumulated other comprehensive loss balance, net of taxes, as of December 31, 2014 and 2013:

	2014	2013
Accumulated currency translation loss	$ (5,402,999)	$ (1,516,611)
Unrealized (loss)/gain on available-for-sale securities	(14,499)	37,600
Unrealized gain on derivatives	119,109	46,210
Unrecognized actuarial gain	9,553	9,381
Total accumulated other comprehensive loss	**$ (5,288,836)**	**$ (1,423,420)**
Less: amounts of accumulated other comprehensive loss attributable to noncontrolling interests	1,545,434	516,702
Total accumulated other comprehensive loss attributable to Sistema JSFC	**$ (3,743,402)**	**$ (906,718)**

25. SEGMENT INFORMATION

As a diversified holding company, the Company invests in a range of companies which meet its investment and return criteria. The Chief Operating Decision Maker is the Company's Management Board. Information reported to the Company's Management Board for the purpose of resource allocation and the assessment of segment performance is focused on each individual investment holding. The Group's reportable segments are MTS, SSTL, MTS Bank, RTI and Corporate. The Other category includes other operating segments including Targin, BPGC, LesInvest, Sistema Mass-media, Detsky mir, Intourist, Medsi, Binnopharm, Sitronics-N, Leader-Invest and SG-trans, none of which meets the quantitative thresholds for determining reportable segments.

See Note 1 for a description of the activities of each operating segment of the Group. The accounting policies of the reportable segments are the same as the Group's accounting policies described in appendix A1.to the notes to the financial statements. Segment profit represents the operating income/(loss).

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

Financial information by reportable segment is presented below:

For the year ended December 31, 2014	**MTS**	**RTI**	**MTS Bank**	**SSTL**	**Corporate**	**Total reportable segments**	**Other**	**Total**
Net sales to external customers[(a)]	10,837,126	1,528,287	698,182	220,717	49,967	13,334,279	3,250,678	16,584,957
Intersegment sales	28,521	316,820	17,263	-	25,391	387,995	37,242	425,237
Equity in results of affiliates[(b)]	(37,940)	-	-	-	-	(37,940)	(24,477)	(62,417)
Net interest revenue/(expense) [(c)]	-	-	(377,575)	-	-	(377,575)	-	(377,575)
Depreciation and amortization	1,934,339	85,796	17,735	60,374	14,274	2,112,518	179,600	2,292,118
Operating income/(loss)	2,765,484	172,070	(396,963)	(431,828)	(546,842)	1,561,921	286,744	1,848,665
Interest income	120,926	42,160	-	7,477	106,825	277,388	50,609	327,997
Interest expense	435,117	143,175	-	90,277	135,031	803,600	73,809	877,409
Income tax expense/(benefit)	533,856	33,831	(61,779)	-	(127,264)	378,644	74,773	453,417
Investments in affiliates	152,262	36	-	-	100,448	252,746	95,815	348,561
Segment assets	11,014,182	2,125,279	3,882,609	485,465	1,949,713	19,457,248	3,201,538	22,658,786
Indebtedness[(d)]	5,191,423	841,307	-	568,170	1,223,056	7,823,956	438,807	8,262,763
Capital expenditures [(e)]	2,314,951	105,052	27,592	43,296	28,099	2,518,990	383,592	2,902,582

For the year ended December 31, 2013	**MTS**	**RTI**	**MTS Bank**	**SSTL**	**Corporate**	**Total reportable segments**	**Other**	**Total**
Net sales to external customers[(a)]	12,488,877	1,685,546	878,832	209,432	46,237	15,308,924	3,193,061	18,501,985
Intersegment sales	21,884	509,963	24,301	-	36,742	592,890	18,115	611,005
Equity in results of affiliates[(b)]	77,615	(1,696)	-	-	-	75,919	(40,165)	35,754
Net interest revenue/(expense) [(c)]	-	-	40,678	-	-	40,678	-	40,678
Depreciation and amortization	2,244,014	96,374	19,152	63,666	14,378	2,437,584	195,964	2,633,548
Operating income/(loss)	3,662,740	(776,878)	18,954	(210,185)	834,945	3,529,576	84,721	3,614,297
Interest income	87,704	45,045	-	9,522	116,328	258,599	45,791	304,390
Interest expense	486,636	138,020	-	121,513	159,215	905,384	129,802	1,035,186
Income tax expense/(benefit)	720,893	(80,025)	(2,645)	-	140,376	778,599	63,508	842,107
Investments in affiliates	153,168	-	-	-	45,210	198,378	166,886	365,264
Segment assets	15,218,084	2,530,299	6,919,610	847,342	3,572,805	29,088,140	3,250,757	32,338,897
Indebtedness[(d)]	6,682,047	1,228,635	-	596,641	1,574,531	10,081,854	437,054	10,518,908
Capital expenditures [(e)]	2,561,310	95,009	21,379	45,765	73,224	2,796,687	197,706	2,994,393

(a) Interest income and expense of MTS Bank are presented as revenues from financial services and cost of financial services, correspondingly, in the Group's consolidated financial statements.

(b) Equity in results of affiliates of MTS segment for the year,2014 includes $135 million of its share of the earnings of MTS Bank and Stream, which is further eliminated on consolidation (2013: $5 million).

(c) Represents the net interest result of the Group's banking activities. In reviewing the performance of MTS Bank, the chief operating decision maker reviews the net interest result, rather than the gross interest amounts.

(d) Represents the sum of short-term and long-term debt.

(e) Represents purchases of property, plant and equipment and intangible assets.

The following table summarizes dividends to Corporate, declared in 2014 and 2013:

	2014	**2013**
Bashneft	$ 818,456	$ 1,162,041
MTS	744,460	635,369
Other	89,903	49,084

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

The reconciliation of segment operating income to the consolidated income from continuing operations before income tax expense and a reconciliation of segment assets to the consolidated assets are as follows:

	2014	2013
Operating income – reportable segments	$ 1,561,921	$ 3,529,576
Operating income – other	286,744	84,721
	1,848,665	**3,614,297**
Intersegment eliminations	(110,216)	(47,725)
Operating income	**$ 1,738,449**	**$ 3,566,572**
Interest income	212,774	182,447
Change in fair value of derivative financial instruments		30,199
Interest expense	(811,346)	(960,136)
Foreign currency transaction loss	(548,596)	(298,264)
Income from continuing operations before income tax	**$ 591,281**	**$ 2,520,818**

	2014	2013
Total assets – reportable segments	$ 19,457,248	$ 29,088,140
Total assets – Bashneft	-	12,674,507
Total assets – other	3,201,538	3,250,757
	22,658,786	**45,013,404**
Intersegment eliminations	(1,988,309)	(1,764,410)
Total assets	**$ 20,670,477**	**$ 43,248,994**

For the years ended December 31, 2014 and 2013, the Group did not have revenues from transactions with a single external customer amounting to 10% or more of the Group's consolidated revenues. For the years ended December 31, 2014 and 2013 the Group's revenues outside of the RF were as follows:

	2014	2013
Ukraine	$ 813,708	$ 1,282,410
India	272,863	253,196
Armenia	186,120	156,883
Central and Eastern Europe	107,372	40,997
Other	154,753	210,661
Total	**$ 1,534,816**	**$ 1,944,147**

As of December 31, 2014 and 2013, the Group's long-lived assets located outside of the RF were as follows:

	2014	2013
Ukraine	$ 332,987	$ 755,373
India	320,604	710,225
Armenia	288,308	354,840
Central and Eastern Europe	68,369	34,953
Other	87,870	111,887
Total	**$ 1,098,138**	**$ 1,967,278**

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

26. RELATED PARTY TRANSACTIONS

The Group sells goods and provides services to and purchases goods and services from its related parties on normal commercial terms. During the years ended December 31, 2014 and 2013, the Group entered into transactions with related parties as follows:

	2014	2013
Sales	$ 17,220	$ 14,921
Revenue from banking activities	34	51
Cost related to banking activities	(48,385)	(30,370)
Cost of sales	(45,595)	(1,188)
Selling, general and administrative expenses	(515)	(12,110)

As of December 31, 2014 and 2013, the related party balances were as follows:

	2014	2013
Assets:		
Short-term investments	$ 5,212	$ 9,840
Accounts receivable, net	5,469	1,362
Other current assets	27,083	4,907
Long-term investments	36,174	17,402
Liabilities:		
Accounts payable	$ (4,134)	$ (890)
Liabilities from banking activities	(541,556)	(526,056)
Accrued expenses and other current liabilities	(3,411)	(646)
Long-term debt	(37)	(64)

27. SHARE-BASED COMPENSATION

The Company and several of its subsidiaries operate share-based compensation plans in order to compensate their employees. This is done through either “equity” plans, in which employees may exercise their options for shares, or “phantom” plans, which generally allow employees to receive cash compensation which varies depending on the share price that the options are linked to.

All such plans, including those of MTS, are immaterial to the Group and consequently have not been disclosed here. A discussion has been included below of the plans operated at the Company level.

Sistema JSFC share-based long-term motivation program – In 2014 and 2013 the Company’s Board of Directors established two-year motivational programs for senior and mid-level management. Participants of the programs upon fulfillment of certain performance conditions and subject to continuing employment with the Group will be granted ordinary shares in the Company. As a result, the Group recognized an expense of $79.4 million and $54.2 million in the consolidated statement of operations and comprehensive income for the years ended December 31, 2014 and 2013, respectively. The fair value of awards granted was measured based on the fair value of the Company’s ordinary shares.

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

28. ASSET RETIREMENT OBLIGATIONS

As of December 31, 2014 and 2013, the estimated present value of the Group's asset retirement obligations and change in liabilities were as follows:

	2014	2013
Balance, beginning of the year	$ **83,809**	$ **90,986**
Liabilities incurred in the current period	1,900	9,257
Property dispositions	(1,067)	-
Accretion expense	6,559	2,963
Revisions in estimated cash flows	677	(13,840)
Currency translation adjustment	(38,163)	(5,557)
Balance, end of the year	**$ 53,715**	**$ 83,809**
Current portion	-	-
Long-term portion	53,715	83,809
Balance, end of the year	**$ 53,715**	**$ 83,809**

The Group's asset retirement obligations relate primarily to the cost of removing telecommunication equipment from sites. Revisions in estimated cash flows are attributable to changes in economic assumptions, such as inflation rates.

The Group recorded the long-term portion of asset retirement obligations as a separate line item in the consolidated statements of financial position, the current portion – as a component of accrued expenses and other current liabilities.

29. REDEEMABLE NONCONTROLLING INTERESTS

Redeemable noncontrolling interests as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
SSTL	$ 720,000	$ 688,000
K-Telecom, MTS subsidiary in Armenia	56,734	89,583
RTI (Note 5)	16,032	27,547
Total	**$ 792,766**	**$ 805,130**

The Group is a party to a put option agreement to acquire the RF's 17.14% interest in SSTL during one year beginning March 2016 at the higher of $777 million or its market value at that date determined by an independent appraiser. The Group accounted for the redeemable noncontrolling interests in SSTL at the redemption value and presented this as temporary equity in its consolidated statements of financial position.

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

30. COMMITMENTS AND CONTINGENCIES

Operating leases – The Group leases land, buildings and office space mainly from municipal organizations through contracts which expire in various years through 2068.

Rental expense under operating leases amounting to $641.0 million and $678.5 million for the years ended December 31, 2014 and 2013, respectively, is included in selling, general and administrative expenses. Rental expense under operating leases amounting to $204.6 million and $238.1 million for the years ended December 31, 2014 and 2013 respectively, is included in cost of sales.

Future minimum rental payments under operating leases in effect as of December 31, 2014, are as follows:

Year ended December 31		
2015	$	282,393
2016		204,009
2017		202,489
2018		204,662
2019		199,758
Thereafter		303,487
Total	**$**	**1,396,798**

Capital commitments – As of December 31, 2014, the Group had executed purchase agreements of approximately $840.0 million to acquire property, plant and equipment and intangible assets.

Guarantees – As of December 31, 2014, MTS Bank and its subsidiaries guaranteed loans for several companies, including related parties, which totaled $217.2 million. These guarantees would require payment by the Group only in the event of default on payment by the respective debtor. As of December 31, 2014, no event of default has occurred under any of the guarantees issued by the Group.

Commitments on loans and unused credit lines – As of December 31, 2014, MTS Bank and its subsidiaries had $126.9 million of commitments on loans and unused credit lines available to its customers.

Taxation – Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include VAT, corporate income tax, a number of turnover-based taxes, and payroll (social) taxes. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies; therefore, the government's implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems.

Generally, according to Russian tax legislation, tax declarations remain open and subject to inspection for a period of three years following the tax year. As of December 31, 2014, tax declarations of certain companies of the Group in Russia for the preceding three fiscal years were open for further review.

The Group purchases supplemental software from foreign suppliers of telecommunications equipment in the ordinary course of business. The Group's management believes that customs duties are calculated in compliance with applicable legislation. However there is a risk that the customs authorities may take a different view and impose additional customs duties.

Pricing of revenue and expenses between each of the Group's subsidiaries and various discounts and bonuses to the Group's subscribers in the course of performing its marketing activities may be subject to transfer pricing rules. The Group's management believes that taxes payable are calculated in compliance with the applicable tax regulations relating to transfer pricing. However there is a risk that the tax authorities may take a different view and impose additional tax liabilities. As of December 31, 2014 and 2013, no provision was recorded in the consolidated financial statements in respect of such additional claims.

In November 2014, the Russian legislation was amended to introduce the concept of "controlled foreign companies" and the new tax regime for such entities. It is expected that the adoption of the new rules will generally lead to an increase in the administrative and, in certain cases, tax burden for the Russian entities that have subsidiary structures incorporated outside the Russian Federation. The management does not believe the law can materially impact the Group's tax obligations as of December 31, 2014.

Management believes that it has adequately provided for tax and customs liabilities in the accompanying consolidated financial statements. As of December 31, 2014 and 2013, the provision accrued amounted to $53.3 million and $69.6 million, respectively. In addition, the accrual for unrecognized income tax benefits, potential penalties and interest recorded in accordance with the authoritative guidance on income taxes totaled $6.1 million and $18.8 million as of December 31, 2014 and 2013, respectively. However, the risk remains that the relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant.

With regard to matters where practice concerning payment of taxes is unclear, management estimated possible tax exposure to be $21 million and $nil as of December 31, 2014 and 2013, respectively.

Operating environment – Starting from March 2014, sanctions have been imposed in several tranches by the U.S. and the E.U. on certain Russian officials, businessmen and companies. Following the decline in oil prices in 2014 and early 2015, Russia, which is the main market of the Group's operations, has experienced significant economic instability, characterized by the substantial depreciation of the Russian rouble, growth of interest rates caused by the decision of the Central Bank of the Russian Federation to significantly increase its key interest rate, a forecasted decline in gross domestic product and a significant decline in the value of shares traded on the Russian stock exchanges. International credit agencies downgraded Russia's long-term foreign currency sovereign rating with a negative outlook. Neither the Company, nor any of its subsidiaries are subject to the current sanctions, and the Group does not appear on the U.S. or E.U. lists of sanctioned parties. However, there is significant uncertainty regarding the extent or timing of any potential further economic or trade sanctions. Any continuing economic and political instability could have a negative impact on the Group's operating results.

Although the Group's reporting currency is the U.S. dollar, it generates most of its revenues in Russian roubles, which is also the functional currency of its principal operating subsidiaries. Therefore, the Group's reported results of operations are significantly impacted by the fluctuations in the exchange rate between the U.S. dollar and the Russian rouble, which depreciated against the U.S. dollar by 42% in 2014, and was on average 17% lower than the average value of the Russian rouble compared to the U.S. dollar during 2013. Also, given that most of the Group's revenues are generated in Russian roubles, the Group faces exchange rate risk relating to payments that the Group must make in currencies other than the Russian rouble.

During 2014, a deterioration in the political environment in Ukraine, the second largest market of the Group's operations, has led to general instability, economic deterioration and armed conflict in the eastern portion of Ukraine. The deterioration has further exacerbated the country's already weak macroeconomic trends, which have led to reduced credit ratings, significant depreciation of its national currency and increased inflation. In 2014, the Ukrainian Parliament adopted a law allowing for the imposition of sanctions against countries, persons and companies deemed by the Ukrainian government to threaten Ukrainian national interests, national security, sovereignty or the territorial integrity of Ukraine. The National Bank of Ukraine passed a decree prohibiting Ukrainian companies from paying dividends to foreign investors. These circumstances, combined with continued political and economic instability in Ukraine, could result in a negative impact on our business, including the Group's financial position and results of operations. For example, such risks apply to the Group's funds deposited in Ukrainian banks, the liquidity of which is negatively affected by the economic downturn. As of December 31, 2014, the Group held $376.9 million in current accounts and deposits in Ukrainian banks, including $90.2 million in Delta Bank (Note15) (fully provided as of December 31, 2014) and $25.1 million in Kyivska Rus Bank (Note 31).

LTE license – In July 2012, the Federal Service for Supervision in the Area of Communications, Information Technologies and Mass Media allocated MTS the necessary license and frequencies to provide LTE telecommunication services in Russia. Under the terms and conditions of the LTE license, the Group is obligated to fully deploy LTE networks within seven years, commencing from January 1, 2013 and deliver LTE services in each population center with over 50,000 inhabitants in Russia by 2019. Also, the Group is obligated to invest at least 15 billion rubles ($266.6 million using December 31, 2014 exchange rate) annually toward the LTE roll-out until the network is fully deployed. Management believes that as of December 31, 2014 the Group is in compliance with these conditions.

Bitel – In June 2013, an agreement was reached between Altimo, Altimo Holdings, MTS and its subsidiary MTS Finance, Nomihold and other associated parties to settle all disputes that have arisen from the Group's investment in Bitel made in 2005. The agreement covered matters involving a number of parties and legal proceedings, including those in the Isle of Man, London, Luxembourg and other jurisdictions. Pursuant to the agreement, all proceedings between the parties and their associated parties were discontinued and waived, and MTS received a total payment of $150 million. All parties made the necessary submissions to the respective courts and tribunals to document the settlement, which, among other actions, fully discharged any and all outstanding obligations under the award previously rendered by the London Court of International Arbitration (LCIA) against MTS Finance in 2011, as well as settled the tripartite LCIA arbitration between MTS, MTS Finance and Nomihold and a tort action filed by Nomihold against MTS in the English Courts.

Upon concluding the settlement agreement, the Group released a provision of $221 million, comprising $170 million set by the LCIA plus $51 million in damages, interest and other costs, that had been previously provided for in relation to the dispute with Nomihold. The Group also recognized a gain of $150 million with respect to the settlement payment in the consolidated statement of operations and comprehensive income for the year ended December 31, 2013.

Restriction on transactions with the shares of BPGC and Ufaorgsintez – In 2014, in the course of a litigation, which the Group is not a party to, the court imposed restrictions on transactions with the shares of BPGC and Ufaorgsintez, owned by the Group. The restrictions do not limit the Group's voting rights, rights to receive dividends or any other shareholders rights.

Investigations into former operations in Uzbekistan – In March 2014, the Group received requests for the provision of information from the United States Securities and Exchange Commission and the United States Department of Justice relating to an investigation of the Group's former subsidiary in Uzbekistan. The Group cannot predict the outcome of the investigations, including any fines or penalties that may be imposed, and such fines or penalties could be significant.

Other – In the ordinary course of business, the Group is a party to various legal proceedings, and subject to claims, certain of which relate to the developing markets and evolving fiscal and regulatory environments in which the Group operates. In the opinion of management, the Group's liability, if any, in all pending litigation, other legal proceedings or other matters will not have a material effect upon the financial condition, results of operations or liquidity of the Group. Management estimates the range of reasonably possible losses, if any, in all pending litigations or other legal proceedings being up to $28.0 million.

31. SUBSEQUENT EVENTS

For the purpose of the accompanying consolidated financial statements, subsequent events have been evaluated through April 2, 2015.

Acquisition of 3G license in Ukraine – In February 2015, MTS-Ukraine won a tender to acquire a nationwide license for the provision of 3G telecommunications services. The license with the cost of UAH 2,715 million ($156.9 million at the acquisition date) has been granted for 15 years. In accordance with the terms of the license MTS-Ukraine is required to launch provision of 3G services in all of the regional centers across Ukraine within 18 months upon allocation of the license.

Bond placement – In February 2015, the Company completed the placement of Series BO-01 unconvertible interest-bearing RUB-denominated bonds for the total amount of RUB 10 billion ($160.3 million at the date of the placement) at the coupon rate of 17% per annum.

Insolvency of Kyivska Rus Bank – In March 2015, the National Bank of Ukraine adopted a resolution declaring Kyivska Rus Bank (Ukraine) to be insolvent. As of December 31, 2014, the Group held $25.1 million in deposits in the bank. Management determined that insolvency of the bank did not provide evidence related to conditions existing as of December 31, 2014, and therefore considered to be a nonrecognized subsequent event.

A1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation – The consolidated financial statements include the accounts of the Company, as well as entities where the Company has operating and financial control, most often through the direct or indirect ownership of a majority voting interest. Those ventures where the Group exercises significant influence but does not have operating and financial control are accounted for using the equity method. Investments in which the Group does not have the ability to exercise significant influence over operating and financial policies are accounted for under the cost method and included in long-term investments in the consolidated statements of financial position. The consolidated financial statements also include accounts of variable interest entities ("VIEs") in which the Group is deemed to be the primary beneficiary. An entity is generally a VIE if it meets any of the following criteria: (i) the entity has insufficient equity to finance its activities without additional subordinated financial support from other parties, (ii) the equity investors cannot make significant decisions about the entity's operations or (iii) the voting rights of some investors are not proportional to their obligations to absorb the expected losses of the entity or receive the expected returns of the entity and substantially all of the entity's activities involve or are conducted on behalf of the investor with disproportionately few voting rights.
All significant intercompany transactions, balances and unrealized gains and losses on transactions have been eliminated.

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

Significant estimates for the Group include the allowances for doubtful accounts, customer loans and deferred tax assets, the valuation of goodwill and other long-lived assets, asset retirement obligations, unrecognized income tax benefits, redeemable noncontrolling interests, derivative instruments, share-based compensation, assets acquired and liabilities assumed in business combinations, the recoverability of investments, and the estimates of oil and gas reserves.

Concentration of business risk – The Group's principal business activities are in the RF, Ukraine and India. Laws and regulations affecting businesses operating in these countries are subject to rapid changes, which could impact the Group's assets and operations.

Foreign currency – Management has determined that the functional currencies of most of the Group's operating subsidiaries are the currencies of the countries of their domicile.

In preparing the financial statements of the entities within the Group, transactions in currencies other than the entities' functional currency are recognized at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not restated.

The Group has selected USD as its reporting currency. The Group's assets and liabilities are translated into USD at exchange rates prevailing on the reporting period end date. Revenues, expenses, gains and losses are translated into USD at average exchange rates prevailing during the reporting period. Equity is translated at the applicable historical rates. The resulting translation gain or loss is recorded as a separate component of other comprehensive income.

On the disposal of a subsidiary whose financial statements are prepared in a currency other than the reporting currency of the Group, all of the accumulated currency translation adjustments in respect of that operation attributable to the Group are reclassified to profit or loss.

As of December 31, 2014, the official exchange rate of the Russian Ruble, the functional currency of most of the Group's subsidiaries, determined by the Central Bank of the RF was RUB 56.26 for 1 USD (RUB 32.73 for 1 USD as of December 31, 2013).

Revenue recognition – Generally, revenues are recognized when all of the following conditions have been met: (i) there is persuasive evidence of an arrangement; (ii) delivery has occurred; (iii) the fee is fixed and determinable; and (iv) collectability of the fee is reasonably assured. Revenue amounts are presented net of value-added taxes.

Revenues under arrangements specific to the respective reportable segments of the Group are recognized as follows:

<u>MTS</u>

Revenues derived from wireless, local telephone, long distance, data and video services are recognized when services are provided. This is based upon either usage (minutes of traffic processed, volume of data transmitted) or period of time (monthly subscription fees).

Content revenue is presented net of related costs when MTS acts as an agent of the content providers while the gross revenue and related costs are recorded when MTS is a primary obligor in the arrangement.

Upfront fees received for connection of new subscribers, installation and activation of wireless, wireline and data transmission services (“connection fees”) are deferred and recognized over the estimated average subscriber life, as follows:

Mobile subscribers	1 -12.5 years
Residential wireline voice phone subscribers	15 years
Residential subscribers of broadband internet service	1 year
Other fixed line subscribers	3-5 years

MTS calculates an average life of mobile subscribers for each region in which it operates and amortizes connection fees based on the average life specific to that region.

Incentives provided to customers are usually offered on signing a new contract or as part of a promotional offering. Incentives representing the reduction of the selling price of the service (free minutes and discounts) are recorded in the period to which they relate, when the respective revenue is recognized, as a reduction to both accounts receivable and revenue. However, if the sales incentive is a free product or service delivered at the time of sale, the cost of the free product or service is classified as an expense. In particular, the Group sells handsets at prices below cost to contract subscribers. Such subsidies are recognized in the cost of sales.

<u>RTI</u>

Revenues from the long-term contracts are recognised using the percentage-of-completion method of accounting, measured by the percent of contract costs incurred to-date to estimated total contract costs. The completed-contract method is used for a single contract or a group of contracts for which reasonably dependable estimates cannot be made or for which inherent hazards make estimates doubtful. Provisions for estimated losses on construction contracts in progress are made in their entirety in the period in which such losses are determined. A total expected loss on a contract is recognised immediately in profit or loss.

Contract expenses are recognised as incurred unless they create an asset related to future contract activity.

The sales of software products and system integration services are generally multiple-element arrangements, involving the provision of related services, including customization, implementation and integration services, as well as ongoing support and maintenance provided to customers.

A multiple-element arrangement is separated into more than one unit of accounting if all of the following criteria are met: (a) the delivered items have value to the customer on a standalone basis; and (b) the arrangement includes a general right of return relative to the delivered items, delivery or performance of the undelivered items is considered probable and substantially in the control of the Group.

If evidence of the fair value of the undelivered elements of the arrangement does not exist, all revenue from the arrangement is deferred until such time that evidence of fair value does exist, or until all elements of the arrangement are delivered. Fees allocated to post-contract support are recognized as revenue on a pro rata basis over the support period. Fees allocated to other services are recognized as revenue as services are performed.

In cases where extended payment terms exist, license and related customization fees are recognized when payments are due, unless a history of collection, without providing concessions, has been established under comparable arrangements.

When sale agreements provide price protection to the dealer, the revenue is deferred until the dealer sells the merchandise to a third party due to the frequent sales price reductions and rapid technology obsolescence.

Where certain products of this segment are sold with a product return right, a reserve is established. In addition other post-contract support obligations are accrued at the time of sale.

MTS Bank

Revenues from interest bearing assets are recognized on an accrual basis using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Regulated services – Regulated tariff services provided by the Group primarily consist of local fixed-line telephone services and services rendered to other operators, such as traffic charges, connection fees and line rental services, provided by MTS in certain regions of RF, and energy transmission services provided by BPGC. Changes in the rate structure for such services are subject to the Federal Tariff Service approval. Revenues from regulated tariff services represented approximately 5.5% and 6.0% of the consolidated revenues for the years ended December 31, 2014 and 2013, respectively.

Cash and cash equivalents – Cash equivalents include demand deposits and other highly liquid investments with an original maturity of three months or less. Within the cash and cash equivalents balance are cash equivalents of $777.2 million and $1,211.8 million as of December 31, 2014 and 2013, respectively, which primarily comprise term deposits with banks and bank promissory notes with original maturities of three months or less.

Restricted cash – Restricted cash includes cash and cash equivalents restricted by agreements with third parties for special purposes.

Financial instruments – The Group's financial instruments include cash and cash equivalents, short-term investments, accounts receivable, derivative financial instruments, financial assets and liabilities from banking activities, accounts payable and short-term and long-term debt.

Hedging activities – The Group uses derivative instruments, including swap, forward and option contracts to manage foreign currency and interest rate risk exposures.

The Group designates derivatives as either fair value hedges or cash flow hedges in case the required criteria are met. Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the consolidated statement of operations and comprehensive income together with any changes in the fair value of the hedged asset or liability that is attributed to the hedged risk.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognized in accumulated other comprehensive loss. Gains and losses associated with the related hedged items are recognized in the consolidated statements of operations and comprehensive income, depending on their nature. The gain or loss relating to the ineffective portion is recognized immediately in the consolidated statement of operations and comprehensive income. For derivatives that do not meet the conditions for hedge accounting, gains and losses from changes in the fair value are included in the consolidated statement of operations and comprehensive income (Note 22).

Assets and liabilities related to multiple derivative contracts with one counterparty are not offset by the Group.

The Group does not use financial instruments for trading or speculative purposes.

Fair value of financial instruments – The fair value of certain financial instruments approximates their carrying value due to the short-term nature of these amounts, namely cash and cash equivalents, short-term investments, accounts receivable and accounts payable, short-term debt and assets and liabilities from banking activities which are included in current assets and liabilities.

Fair value measurements – The Group reviews its fair value hierarchy classifications quarterly. Changes in significant observable valuation inputs identified during these reviews may trigger reclassification of fair value hierarchy levels of financial assets and liabilities. During the years ended December 31, 2014 and 2013 no reclassifications occurred.

A three-level valuation hierarchy has been established under U.S. GAAP for disclosure of fair value measurements. The valuation hierarchy is based on the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument;
- Level 3 – one or more inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Accounts receivable – Accounts receivable are stated at their net realizable value after deducting a provision for doubtful accounts. Such provision reflects either specific cases of delinquencies or defaults or estimates based on evidence of collectability.

Assets from banking activities – Assets from banking activities comprise assets (cash and cash equivalents, loans, investments and other) involved in operations of MTS Bank. Impairment losses on loans to customers and banks are included in the allowance for loan losses. The allowance for loan losses represents management's best estimate of probable credit losses inherent in the lending portfolios as of the reporting period end. Loans that are not individually reviewed are evaluated as a group using reserve factor percentages based on historic loss experience and qualitative factors. Loans deemed to be uncollectible are charged against the allowance for loan losses. Correspondingly, recoveries of amounts previously charged as uncollectible are credited to the allowance for loan losses. A provision for loan losses is charged to the consolidated statement of operations and comprehensive income based on management's evaluation of the estimated losses, after giving consideration to the net chargeoffs which have been incurred in the Group's loan portfolio.

The Group performs detailed reviews of its lending portfolios on a periodic and systematic basis to identify inherent risks and to assess the overall collectability of those portfolios. The allowance on certain homogeneous loan portfolios, which generally consist of consumer and mortgage loans, is based on an evaluation of aggregated portfolios of homogeneous loans, generally by loan type.

Loss forecast models are utilized for portfolios of homogeneous loans which consider a variety of factors including, but not limited to, historical loss experience, anticipated defaults or foreclosures based on portfolio trends, delinquencies and credit scores, and estimated loss factors by loan type. The remaining loan portfolios are reviewed on an individual loan basis.

Loans subject to individual reviews are analyzed and segregated by risk according to the Group's internal risk rating scale. These risk classifications, in conjunction with an analysis of historical loss experience, current economic conditions and performance trends within specific portfolio segments, and any other pertinent information result in the estimation allowances for loan losses. An allowance for loan losses is established for individually impaired loans. A loan is considered impaired when, based on current information and events, it is probable that the Group will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the agreement. Individually impaired loans are measured based on the present value of payments expected to be received, or for loans that are solely dependent on the collateral for repayment, the estimated fair value of the collateral. If the recorded investment in impaired loans exceeds the measure of estimated fair value, an allowance is established as a component of the allowance for loan losses.

Inventories and spare parts – Inventories comprise raw materials, work-in-progress, finished goods and goods for resale. Inventory and spare parts are stated at the lower of cost or market value. Inventory is accounted for using either first-in, first-out or the weighted-average cost method.

The cost of raw materials includes the cost of purchase, customs duties, transportation and handling costs. Work-in-progress and finished goods are stated at production cost which includes direct production expenses and manufacturing overheads. Costs and estimated earnings in excess of billings on uncompleted contracts include the accumulated costs of projects contracted with third parties, net of related progress billings. The Group periodically assesses its inventories and spare parts for obsolete or slow-moving stock.

Value-added taxes – Value-added taxes ("VAT") related to sales are payable to the tax authorities on an accrual basis based on invoices issued to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that will be reclaimed against future sales are recorded as VAT receivable in the accompanying financial statements.

Property, plant and equipment – Property, plant and equipment are stated at historical cost. Cost includes major expenditures for improvements and replacements, which extend useful lives of the assets or increase their revenue generating capacity. Repairs and maintenance, including preventative maintenance, are charged to the consolidated statement of operations and comprehensive income as incurred.

The cost of major overhauls and replacements, which extend useful lives of the assets or increase their revenue generating capacity, are capitalized to the cost of the assets.

Depreciation for property, plant and equipment is computed under the straight-line method utilizing estimated useful lives of the assets as follows:

Buildings	20-50 years
Leasehold improvements	Lesser of the estimated useful life or the term of the lease
Switches and transmission devices	7-31 years
Network and base station equipment	4-12 years
Power and utilities	3-47 years
Other plant, machinery and equipment	3-25 years

Whilst there are certain assets within the Group that have useful lives longer than those presented above, these assets are quantitatively insignificant in comparison to the overall Group balance for each category. As such, the Group has taken the approach of reporting the useful economic lives which most faithfully represent the majority of assets, in order to provide a more reasonable range that more closely relates to the Group norm.

Assets held under capital leases are initially recognized as assets of the Group at their fair value at the inception of a lease or, if lower, at the present value of minimum lease payments. The discount rate used in determining the present value of the minimum lease payments is the Group's incremental borrowing rate, unless (1) it is practicable to determine the implicit rate computed by the lessor; and (2) the implicit rate is less than the Group's incremental borrowing rate. If both of those conditions are met, the interest rate implicit in the lease is used.

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

Construction in progress and equipment for installation are not depreciated until an asset is placed into service.

Asset retirement obligations – The Group calculates asset retirement obligations and an associated asset retirement cost when the Group has a legal or constructive obligation in connection with the retirement of tangible long-lived assets.

Business combinations – Acquisitions of businesses from third parties are accounted for using the acquisition method, with assets and liabilities of an acquired entities being measured at their fair values as at the date of acquisition. Noncontrolling interests are measured at fair value.

Goodwill – Goodwill is determined as the excess of the consideration transferred plus the fair value of any noncontrolling interests in the acquiree at the acquisition date over the fair values of the identifiable net assets acquired. The excess of the fair values of the identifiable net assets acquired over the cost of the business combination plus the fair value of any noncontrolling interests in the acquiree at the acquisition date is credited to income ("negative goodwill").

Goodwill is not amortized to operations, but instead is reviewed for impairment at least annually. At first step, the Group asseses qualitative factors to determine whether it is more likely than not that goodwill is impaired as a basis for determining whether it is necessary to perform the quantitative impairment test. Goodwill is than reviewed for impairment by comparing the carrying value of each reporting unit's net assets (including allocated goodwill) to the fair value of the reporting unit. If the reporting unit's carrying amount is greater than its fair value, the next step is performed whereby the implied fair value that relates to the reporting unit's goodwill is compared to the carrying value of the reporting unit's goodwill. The Group recognizes a goodwill impairment charge for the amount by which the carrying value of goodwill exceeds the fair value.

Other intangible assets – Other intangible assets include billing and telecommunication software and other software, operating licenses, acquired customer bases and customer relationships, radio frequencies, trademarks and telephone numbering capacity.

All finite-life intangible assets are amortized using the straight-line method utilizing estimated useful lives of the assets as follows:

Billing and telecommunication software	1-20 years
Operating licenses	3-20 years
Acquired customer base	1-8 years
Acquired radio frequencies	2-15 years
Software and other	1-10 years

Trademarks and numbering capacity with indefinite contractual life are not amortized, but are reviewed, at least annually, for impairment.

If the fair value of the intangible asset is less than its carrying value, an impairment loss is recognized in an amount equal to the difference. The Group also evaluates the remaining useful life of its intangible assets that are not subject to amortization on an annual basis to determine whether events and circumstances continue to support an indefinite useful life. If an intangible asset that is not being amortized is subsequently determined to have a finite useful life, that asset is tested for impairment.

Investments – The Group's share in the net assets and net income of certain entities, where the Group has the ability to exercise significant influence over their operating and financial policies ("affiliates") is included in the consolidated financial statements using the equity method of accounting. The Group's share in the net income of affiliates is included within operating income, given that the Group has day-to-day involvement in the business activities and they are considered to be integral to the Group's business. Other-than-temporary decreases in the value of investments in affiliates are recognized in net income.

All other equity investments, which consist of investments for which the Group does not have the ability to exercise significant influence, are accounted for under the cost method or at fair value. Investments in private companies are carried at cost, less provisions for other-than-temporary impairment in value. For public companies that have readily determinable fair values, the Group classifies its equity investments as available-for-sale or trading. For available-for-sale securities, the Group records these investments at their fair values with unrealized holding gains and losses included in the consolidated statement of operations and comprehensive income/(loss), net of any related tax effect. For trading securities, the Group records the investment at fair value. Unrealized holding gains and losses for trading securities are included in earnings.

The Group purchases promissory notes for investing purposes. These notes are carried at cost and the discount against the nominal value is accrued over the period to maturity. A provision is made, based on management assessment, for notes that are considered uncollectible. The notes are classified as held-to-maturity.

Investments which are expected to be realized within twelve months after the statement of financial position date are classified as short-term investments. Other investments are classified as long-term investments.

Debt issuance costs – Debt issuance costs are recorded as an asset and amortized using the effective interest method over the terms of the related loans.

Impairment of long-lived assets other than goodwill and indefinite lived intangible assets – The Group periodically evaluates the recoverability of the carrying amount of its long-lived assets. Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, the Group compares the undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, the Group records impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets (Note 15).

Liabilities from banking activities – Liabilities from banking activities include deposits from banks and customers, promissory notes issued and other liabilities that arise out of operations of MTS Bank.

Property, plant and equipment contributions – Telecommunication equipment and transmission devices, installed at newly constructed properties in Moscow, have been historically transferred to OJSC Moscow City Telephone Network (hereinafter, "MGTS"), a fixed line operator and subsidiary of the Group, by the Moscow City Government free of charge. These assets are capitalized by the Group at their market value at the date of transfer. Simultaneously, deferred revenue is recorded in the same amount and is amortized as a reduction of the depreciation charge in the consolidated statement of operations and comprehensive income over the contributed assets' life.

Income taxes – Income taxes of the Group's Russian entities have been computed in accordance with RF laws. The corporate income tax rate in the RF is 20%. The income tax rate on dividends paid within Russia is 9% or 0% subject to meeting certain conditions. The foreign subsidiaries of the Group are paying income taxes in their respective jurisdictions.

Deferred tax assets and liabilities are recognized for differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the tax bases of assets and liabilities that will result in future taxable or deductible amounts. The deferred tax assets and liabilities are measured using the enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. In making such determination, the Group considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations.

Uncertain tax positions are recognized in the consolidated financial statements for positions which are not considered more likely than not of being sustained based on the technical merits upon examination by the tax authorities. The measurement of the tax benefit recognized in the consolidated financial statements is based upon the largest amount of tax benefit that, in management’s judgment, is greater than 50% likely of being realized based on a cumulative probability assessment of the possible outcomes.

The Group recognizes interest and penalties relating to unrecognized tax benefits within income taxes.

Treasury stock – If the Group reacquires the Company’s own equity instruments, those instruments (“treasury shares”) are recognized as a deduction of equity at cost, being the consideration paid to reacquire the shares. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company’s own equity instruments. Such treasury shares may be acquired and held by the Company or by other subsidiaries of the Group.

Share-based compensation – The Group calculates and records the fair value of equity instruments, such as stock options or restricted stock, awarded to employees for services received and recognizes such amounts in the consolidated statement of operations and comprehensive income. The fair value of the equity instruments is measured on the date they are granted and is recognized over the period during which the employees are required to provide services in exchange for the equity instruments (Note 27). Share-based compensation expense includes the estimated effects of forfeitures. Such estimates are adjusted over the requisite service period to the extent actual forfeitures differ, or are expected to differ from such estimates. Changes in estimated forfeitures are recognized in the period of change and also impact the amount of expense to be recognized in future periods.

For share-based compensation that include a component that will be settled in cash, and a component that is settled in equity, the Group accounts for the awards separately, based on their substance. For the component that is settled in cash, the awards generally are accounted for as liabilities with compensation cost recognized over the service (vesting) period of the award based on the fair value of the award remeasured at each reporting period. For the component that is settled in equity, compensation cost is measured based on the fair value of the award on the date of grant and the compensation cost is recognized over the service (vesting) period of the award.

Retirement and postretirement benefits – Subsidiaries of the Group contribute to local state pension funds and social funds, on behalf of their employees.

In Russia all social contributions paid during the year ended December 31, 2014 are represented by payments to governmental social funds, including the Pension Fund of the Russian Federation, the Social Security Fund of the Russian Federation and the Medical Insurance Fund of the Russian Federation.

In the Ukraine, subsidiaries of the Group are required to contribute a specified percentage of each employee’s payroll up to a fixed limit into a pension fund, an unemployment fund and a social security fund. The contributions are expensed as incurred.

In addition to the above, MGTS have defined benefit plans to provide their employees certain benefits upon and after retirement. The net period cost of the Group's defined benefit plans is measured on an actuarial basis using the projected unit credit method and several actuarial assumptions. The recognition of expense for defined benefit plans is significantly impacted by estimates made by management such as discount rates used to value certain liabilities, expected return on assets, mortality rates, future rates of compensation increase and other related assumptions. Gains and losses occur when actual experience differs from actuarial assumptions. If such gains or losses exceed ten percent of the greater of plan assets or plan liabilities the Company amortizes those gains or losses over the average remaining service period of the employees.

The Group records in the statement of financial position the funded status of its pension plans based on the projected benefit obligation.

Borrowing costs – Borrowing costs are recognized as an expense in the period in which they are incurred. Borrowing costs for assets that require a period of time to get them ready for their intended use are capitalized and amortized over the related assets' estimated useful lives.

Advertising costs – Advertising costs are expensed as incurred. Advertising costs for the year ended December 31, 2014 and 2013 were $266.0 million and $328.7 million, respectively, and were reflected as a component of selling, general and administrative expenses in the accompanying consolidated statements of operations and comprehensive income.

Redeemable noncontrolling interests – From time to time, in order to optimize the structure of business acquisitions and to defer payment of the purchase price the Group enters into put and call option agreements to acquire noncontrolling interests in the existing subsidiaries. As these put and call option agreements are not freestanding, the underlying shares of such put and call option agreements are classified as redeemable securities and are accounted for at either redemption value or the fair value of redeemable noncontrolling interests as of the reporting date. The fair value of redeemable noncontrolling interests is assessed based on discounted future cash flows of the acquired entity ("Level 3" significant unobservable inputs of the hierarchy established by U.S. GAAP guidance). Any changes in redemption value of redeemable noncontrolling interests are accounted for in the Group's retained earnings. Redeemable noncontrolling interests are presented as temporary equity in the consolidated statement of financial position.

Earnings per share – Basic earnings per share ("EPS") is based on net income attributable to the Group divided by the weighted average number of shares outstanding during the year.

Diluted EPS is based on net income attributable to the Group adjusted in certain circumstances, divided by the weighted average number of shares outstanding during the year, adjusted for the dilutive effect of all potential shares that were outstanding during the year. Such potentially dilutive shares are excluded when the effect would be to increase diluted earnings per share or reduce the diluted loss per share.

Distributions to shareholders – Distributable retained earnings of the Group are based on amounts extracted from the standalone statutory accounts of the Company (based on the Russian accounting standards) and may significantly differ from consolidated amounts calculated on the basis of U.S. GAAP.

Reclassifications and revisions – Certain comparative information presented in the consolidated financial statements for the year ended December 31, 2013 has been revised in order to achieve comparability with the presentation used in the consolidated financial statements for the year ended December 31, 2014. Such reclassifications and revisions were not significant to the Group financial statements, except for presentation of the loss on deconsolidation of Bashneft (Note 2).

Recently adopted accounting pronouncements – Effective January 1, 2014, the Group adopted Accounting Standards Update ("ASU") 2013-05, Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity, ASU 2013-07, Liquidation Basis of Accounting and ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The adoption of these amendments did not have a material impact on the Group's consolidated balance sheet or results of operations.

Transition to International Financial Reporting Standards –To conform with the Russian legislation, the Group will prepare its consolidated financial statements for the year ended December 31, 2015 in accordance with International Financial Reporting Standards ("IFRS").