Open Joint Stock Company
Far East Telecommunications Company

Consolidated Financial Statements

For the year ended 31 December 2007
with Independent Auditors' Report

OJSC Far East Telecommunications Company

Consolidated Financial Statements

For the year ended 31 December 2007

Contents

ZAO KPMG
Naberezhnaya Tower Complex, Block C
18 Krasnopresnenskaya Naberezhnaya
Moscow 123317
Russia

Telephone +7 (495) 937 4477
Fax +7 (495) 937 4400/99
Internet www.kpmg.ru

Independent Auditors' Report

To the Board of Directors OJSC Far East Telecommunications Company

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of OJSC Far East Telecommunications Company (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as at 31 December 2007, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2007, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO KPMG

ZAO KPMG
25 June 2008

OJSC Far East Telecommunications Company

Consolidated Balance Sheet as at 31 December 2007

(in millions of Russian Roubles)

	Notes	31 December 2007	31 December 2006 (restated)
ASSETS			
Non-current assets			
Property, plant and equipment	**7**	12,992	10,203
Intangible assets and goodwill	**8**	2,882	1,031
Investments in associates	**10**	67	24
Financial investments	**11**	18	7
Long–term accounts receivable and other assets	**12**	12	17
Long–term advances given	**13**	234	2,554
Total non-current assets		**16,205**	**13,836**
Current assets			
Inventories	**14**	449	338
Trade and other accounts receivable	**15**	1,263	1,006
Income tax receivable		35	1
Financial investments	**11**	771	1
Other current assets	**16**	394	401
Cash and cash equivalents	**17**	342	184
Total current assets		**3,254**	**1,931**
TOTAL ASSETS		**19,459**	**15,767**
EQUITY AND LIABILITIES			
Shareholders' equity			
Share capital	**18**	4,366	4,366
Treasury shares		(1)	(6)
Retained earnings		2,672	1,552
Total equity attributable to equity holders of the parent		**7,037**	**5,912**
Minority interest		1,399	21
Total equity		**8,436**	**5,933**
Non-current liabilities			
Long–term borrowings	**19**	4,704	3,247
Long–term finance lease obligations	**20**	225	555
Pension liabilities	**23**	964	436
Long–term income tax payable		-	1
Long–term other taxes payable		-	1
Deferred income		115	122
Deferred income tax liability	**30**	741	385
Provisions	**24**	-	179
Total non-current liabilities		**6,749**	**4,926**
Current liabilities			
Accounts payable and accrued expenses	**21**	1,640	1,226
Income tax payable		3	29
Other taxes payable	**22**	183	106
Dividends payable		35	24
Short–term borrowings	**19**	803	2,022
Current portion of long–term borrowings	**19**	846	423
Current portion of long–term finance lease obligations	**20**	306	372
Provisions	**24**	458	706
Total current liabilities		**4,274**	**4,908**
Total liabilities		**11,023**	**9,834**
TOTAL EQUITY AND LIABILITIES		**19,459**	**15,767**

OJSC Far East Telecommunications Company

Consolidated Income Statement

for the year ended 31 December 2007

(in millions of Russian Roubles, except per share amounts)

	Notes	2007	2006 (restated)
Revenues	**25**	**15,001**	**10,899**
Wages, salaries, other benefits and payroll taxes		(4,734)	(3,891)
Depreciation and amortization	**7, 8**	(2,088)	(1,813)
Materials, repairs and maintenance, utilities		(1,411)	(941)
Taxes other than income tax		(257)	(186)
Interconnection charges – domestic operators		(1,681)	(954)
Allowance for of doubtful receivables		(58)	(40)
(Loss)/gain on disposal of property, plant and equipment		(132)	22
Other operating income	**26**	286	76
Other operating expenses	**27**	(2,407)	(2,082)
Operating profit		**2,519**	**1,090**
Share of result of associates	**10**	(2)	(2)
Interest expense, net	**28**	(550)	(542)
Other gains/(losses) from financial investments, net	**29**	44	(47)
Foreign exchange gain, net		3	19
Profit before income tax and minority interest		**2,014**	**518**
Income tax expense	**30**	(654)	(403)
Profit for the year		**1,360**	**115**
Attributable to:			
Shareholders of the Company		1,272	105
Minority interest		88	10
Profit for the year		**1,360**	**115**
Basic and diluted earnings per share (Russian Roubles)	**31**	10,034	826

OJSC Far East Telecommunications Company

Consolidated Statement of Cash Flows

for the year ended 31 December 2007

(in millions of Russian Roubles)

	Notes	2007	2006 (restated)
Cash flows from operating activities:			
Profit before income tax		2,014	518
Adjustments for:			
Other gain from investments, net		(44)	60
Depreciation and amortization	**7, 8**	2,088	1,813
Loss/(gain) on disposal of property, plant, and equipment		132	(22)
Foreign exchange gain, net		(3)	(19)
Share of result of associates	**10**	2	2
Interest expense, net	**28**	550	542
Allowance for doubtful receivables		58	40
Allowance for inventories obsolescence and doubtful other assets		-	37
Provisions		(427)	885
Operating cash flows before changes in working capital		4,370	3,856
Decrease/(increase) in accounts receivable		63	(348)
Decrease in other current assets		147	142
Decrease in inventories		14	42
Decrease in accounts payable, accrued expenses and advances received		(275)	(309)
Increase/(decrease) in taxes payable others than income tax		77	(276)
(Decrease)/increase in pension liabilities		(55)	60
Cash flows generated from operations before income taxes and interest paid		4,341	3,167
Interest paid		(231)	(410)
Income tax paid		(835)	(474)
Cash flows from operating activities		**3,275**	**2,283**
Cash flows from investing activities:			
Acquisition of property, plant and equipment		(2,188)	(2,262)
Proceeds from sales of property, plant and equipment		236	345
Acquisition of intangible assets		(328)	(321)
Acquisition of subsidiaries less cash proceeds received		61	(2,309)
Proceeds from sale of associates and other financial assets		11	-
Acquisition of financial assets		(764)	(34)
Interest received		30	78
Dividends received		1	1
Cash flows utilized in investing activities		**(2,941)**	**(4,502)**
Cash flows from financing activities:			
Proceeds from borrowings		4,019	5,921
Repayment of borrowings		(1,097)	(2,918)
Repayment of finance lease obligations		(366)	(430)
Repayment of vendor financing obligations		(164)	(174)
Repayment of promissory notes		(2,428)	-
Dividends paid		(140)	(154)
Cash flows from/(utilized in) financing activities		**(176)**	**2,245**
Net increase in cash and cash equivalents		**158**	**26**
Cash and cash equivalents at the beginning of the year		**184**	**158**
Cash and cash equivalents at the end of the year (see note 17)		**342**	**184**

OJSC Far East Telecommunications Company

Consolidated Statement of Changes in Equity

for the year ended 31 December 2007

(in millions of Russian Roubles)

	Share capital Preference shares	Share capital Ordinary shares	Treasury shares	Retained earnings	Total	Minority interest	Total equity
Balance at 31 December 2005 (as previously reported)	**1,081**	**3,285**	**-**	**2,479**	**6,845**	**12**	**6,857**
Effect of change in accounting policy and errors correction (Note 2)	-	-	-	(862)	(862)	-	(862)
Balance at 31 December 2005 (as restated)	**1,081**	**3,285**	-	**1,617**	**5,983**	**12**	**5,995**
Profit for the year				105	105	10	115
Total recognised income and expenses for the year					105	10	115
Dividends to shareholders	-	-	-	(170)	(170)	-	(170)
Treasury shares acquired	-	-	(6)	-	(6)	-	(6)
Acquisition of minority interest	-	-	-	-	-	(1)	(1)
Balance at 31 December 2006 (as restated)	**1,081**	**3,285**	**(6)**	**1,552**	**5,912**	**21**	**5,933**
Profit for the year				1,272	1,272	88	1,360
Total recognised income and expenses for the year					1,272	88	1,360
Dividends to shareholders	-	-	-	(152)	(152)	-	(152)
Treasury shares sold	-	-	5	-	5	-	5
Acquisition of subsidiaries	-	-	-	-	-	1,292	1,292
Acquisition of minority interest	-	-	-	-	-	(2)	(2)
Balance at 31 December 2007	**1,081**	**3,285**	**(1)**	**2,672**	**7,037**	**1,399**	**8,436**

1 General Information

The consolidated financial statements of OJSC Far East Telecommunication Company (hereinafter “the Company”) and its subsidiaries (“the Group”) for the year ended 31 December 2007, was authorized by the General Director and the Chief Accountant on 25 June 2008.

The Parent Company, OJSC Far East Telecommunication Company, was incorporated as an open joint stock company in the Russian Federation.

The Company’s official address: 690950, Russia, Primorskiy Kray, Vladivostok, Svetlanskaya str.57.

The Company provides telephone services (including local and intrazone telephone services), telegraph services, data transmission services, rents out communication and radio communication lines in the territory of the Far East Federal District of the Russian Federation.

Open joint-stock company Svyazinvest, controlled by the Russian Government, as a holding company, owned 51% of the Company’s ordinary voting stock as at 31 December 2007.

Information of the Company’s main subsidiaries is disclosed in Note 9. All subsidiaries are incorporated under the laws of the Russian Federation.

Liquidity and Financial Resources

The world economy is suffering the consequences of the global financial crisis in the mortgage lending market and the ensuing liquidity crisis. In the current unfavorable context, there are short-term risks related to both increase in interest rates on loans being raised and the availability of borrowing.

In 2007, the Company raised both short and long-term borrowings to finance its operations. Borrowings were primarily raised in the form of bank loans. In 2007, the Company repaid its liabilities in full and in due time.

As at 31 December 2007, the Company’s current liabilities exceeded its current assets by RUR 1,020 million (31 December 2006: RUR 2,977 million).

The key instrument used by the Company to maintain the adequate level of solvency is the availability of financing in the form of a revolving credit lines and overdrafts (as of January 1, 2008, available financing amounted to some RUR 1,012 million).

In 2008, the Company expects to finance almost all its operating and investing activities out of proceeds from principal operations. New borrowings may be needed to refinance part of the loans portfolio in order to meet early redemption of bonds due in June and December 2008.

In case of adverse changes in the financial market and increase in interest rates, the Company plans to take the following steps to maintain the adequate level of solvency:

- optimize expenses, including decrease in personnel costs (by optimizing the headcount, cutting the variable portion of salary/wages), optimize use of inventory and repair and maintenance expenses, control administrative and other expenses, optimize costs related to sales and customer service through bundling of services and outsourcing;
- revise the capital expenditure program to downsize the investment program or extend investment project timeframes. The current contracts with vendors permit the Company to carry out these measures;
- increase the efficiency of working capital utilization, *inter alia*, decrease the level and average age of accounts receivable, in particular by changing the existing contractual relations with customers, increase accounts payable to an optimal level.

Thus, the Company management does not expect the situation in the borrowings market to have a significant impact on the Company's ability to raise external financing in 2008.

The Company's Position in the Communication Services Market

Establishment of New Tariffs Based on Tariff Plans

In conformity with current Russian laws regulating activities of natural monopolies, the Company is included in the register of natural monopolies in the area of communications. As a result, tariffs for a number of communication services provided by the Company are established by the Federal Tariff Service (hereinafter, "the Russian FTS").

The Russian FTS sets tariffs for local telephone services using the economically justifiable costs method based on gross revenue required to cover the cost of services, part of other costs and standard profit. Yet, certain cross-subsidies remain with respect to local telephone services. In line with current legislation, cross-subsidies are partially provided via state-regulated tariffs for intrazone telephone calls and via compensatory markup on tariffs for local and zonal call initiation services for intrazone, long distance domestic and international telephone calls.

The Company provides interconnection services and traffic transmission services to operators. The Company is included in the register of operators that have a prominent position in the public telecommunication network. Tariffs charged by the Company for interconnection and traffic transmission services are subject to state regulation.

Ceiling tariffs have been established for the Company to charge for interconnection services, including ceiling tariffs for establishing and servicing interconnection points and traffic transmission services within the public telephone network. The Company has established tariffs for interconnection services, call initiation and termination services at the maximum level, except for the tariff for local call termination services at the Company's node.

A compensatory markup was established on tariffs for the Company's local and zonal call initiation services for long distance domestic and international telephone calls for the period through 1 January 2008.

Change in Tariff Calculation Rules

In line with changes introduced by the Russian FTS into the Procedure for Calculation of Tariffs and Tariff Plans for Local Telephone Services in Q3 2007, it was decided to substantially reduce tariffs for local telephone services for individual subscribers connected via dual-circuit lines effective 1 January 2008:

- the tariff for provision to a subscriber for permanent use of a subscriber line of any type was reduced by 25%,
- the tariff for provision of local telephone connection services (where the operator lacks technology to maintain time-based accounting for local telephone calls and uses combined and fixed payment schemes) was reduced by 50%.

Universal Telecommunication Services

Starting from 2005, Russian Federation government guarantees provision of universal telecommunication services that include local telephone connection services in the fixed-line telephone system using payphones, access to the information and inquiry service system and availability of free-of-charge 24-hour emergency services calls, as well as data transmission services and access to the Internet using multiple access points, in hard-to-reach and geographically remote areas of the Russian Federation.

The Company has tendered for the right to provide universal telecommunication services, specifically telephone services using payphones, in its licensed areas. In 2007, the Company won 7 tenders (2005-2006: 16) and entered into 7 agreements with the Federal Telecommunications Agency, which outline the terms and conditions of providing universal telephone services using payphones (2005-2006: 16). As of 31 December 2007, the Company had installed the total of 2,735 payphones pursuant to the above agreements.

Universal telecommunication services are subject to tariffs calculated by the Federal Telecommunications Agency and indicated in the agreements that outline the terms and conditions of providing universal telecommunication services. The established tariffs for universal telecommunication services do not cover the costs the Company incurs to provide these services. The excess of economically justified costs incurred to provide universal telecommunication services over revenue received based on the established tariffs constitutes losses from provision of universal telecommunication services which are reimbursable from the Universal Service Fund.

Contributions to the Universal Service Fund are taken to income of the federal budget under the established RF budget income classification code. The income and expense sections of a federal budget for the relevant year include operator contributions to the Fund and amounts to be expensed from the Fund in line with the budgetary classification of the Russian Federation. Thus, the Universal Service Fund constitutes one of the state budget funds.

Losses are reimbursed by the Federal Telecommunications Agency subject to the procedure set by Government of the Russian Federation and indicated in agreements that outline the terms and conditions of providing universal telecommunication services. In first half of 2007, pursuant to the agreement terms, the Company was reimbursed for losses on a semi-annual basis. Since Q3 2007, losses have been reimbursed on a quarterly basis. The Federal Telecommunications Agency takes the final decision on the amount of such reimbursement based on the annual results after the Company submits the opinion of an independent audit for confirming that:

- losses claimed for reimbursement have been calculated correctly;
- separate accounting has been performed correctly in compliance with industry legislation;
- the Company has made contributions to the universal service fund in full.

Information on the amount of reimbursed losses from universal telecommunication services is provided in Note 26.

National Project "Education"

In 2006-2007, the Company was involved in the implementation of the national priority project "Education". As part of this project, the Company's branches connected to the Internet 1,677 educational institutions in the territory of the Far East Federal District of the Russian Federation, including 636 educational institutions connected to the Internet in 2007.

Under the agreement with OJSC RTComm.RU, the Company provided services that involved establishment of virtual communication channels from general education institutions to access hubs and provision of 24-hour use of the established communication channels.

The Company's costs incurred to connect educational institutions totaled RUR 284 million in 2007 (2006: RUR 84 million). The Company's income from services provided under the national project "Education" amounted to RUR 17 million in 2007 (2006: RUR 4 million).

Plans to Digitalize the Company's Networks

At the end of 2007, 70.02% of local telephone networks were digitalized. Commissioning of new electronic telephone exchanges and replacement of quasi-electronic and analog telephone exchanges by the electronic ones help the Company to improve the quality of provided services, broaden their range and meet industry requirements. The Company is planning to digitalize its local telephone networks in accordance with the requirements by the year of 2010.

2 Basis of Presentation of the Financial Statements

Statement of Compliance

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

Presentation of Financial Statements

Consolidated financial statements of the Company are prepared on the basis of standalone financial statements of the parent and its subsidiaries and associates prepared under unified accounting policies.

The consolidated financial statements of the Company are presented in millions of Russian Roubles with all values being rounded off to the nearest million, except when otherwise indicated.

Basis of Accounting

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

The consolidated financial statements have been prepared under the historical cost convention except property, plant and equipment recognized at fair value, which was used as an actual cost of the property, plant and equipment as of the date of transition to IFRS; available-for-sale investments were measured at fair value.

Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except that the Company has adopted those new/revised standards mandatory for financial years beginning on or after 1 January 2007. Adoption of new and revised standards did not have significant effect on the financial statements of the Company; they did however rise to additional disclosures.

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

- IFRS 7 "*Financial Instruments: Disclosures*";
- IAS 1 (amended 2005) "*Presentation of Financial Statements - Capital Disclosures*";
- IFRIC 8 "*Scope of IFRS 2*";
- IFRIC 9 "*Reassessment of Embedded Derivatives*";
- IFRIC 10 "*Interim Financial Reporting and Impairment*".

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

IFRS 7 Financial instruments: Disclosures

The Standard requires disclosures that enable users of the financial statements to evaluate the significance of the Company's financial instruments and the nature and extent of risks arising from those financial instruments. If necessary, the comparable information was reviewed in accordance with new requirements. The changes did not have a material effect on the result of operations or financial position of the Company.

IAS 1 (amended in 2005) Presentation of Financial Statement: Disclosures on Capital

The Standard Requires the Company to make new disclosures to enable users of the financial statements to evaluate the Company's objectives, policies and processes for managing capital. These new disclosures are shown in Note 36.

IFRIC 8 "Scope of IFRS 2"

IFRIC 8 "Scope of IFRS 2" requires applying IFRS 2 in all cases where the entity cannot identify some or all of the goods or services received, specifically, if the equity instruments are issued to cover the liability which appears to be less than the fair value of the equity instruments granted. This Interpretation did not have a material effect on the result of operations or financial position of the Company.

IFRIC 9 "Reassessment of Embedded Derivatives"

IFRIC 9 "Reassessment of Embedded Derivatives" establishes that the date to assess the existence of an embedded derivative is the date when the Company first becomes party to a contract, with reassessment made only if there is a change to the contract that significantly modifies the cash flows. This Interpretation did not have a material effect on the result of operations or financial position of the Company.

IFRIC 10 "Interim Financial Reporting and Impairment"

IFRIC 10 "Interim Financial Reporting and Impairment" requires the Company not to reverse an impairment loss recognized in a previous interim period in respect of goodwill or an investment in either an equity instrument or a financial asset carried at cost. This Interpretation did not have a material effect on the result of operations or financial position of the Company.

IFRSs and IFRIC Interpretations not yet effective

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

- IFRS 8 "*Operating Segments*";
- IAS 1 (amended 2007) "*Presentation of Financial Statements*";
- IAS 23 (amended 2006) "*Borrowing Costs*";
- IFRIC 11, "*IFRS 2 – Group and Treasury Share Transactions*";
- IFRIC 12 "*Service Concessions Arrangements*";
- IFRIC 13 "*Customer Loyalty Programmes*";
- IFRIC 14 "*IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*";
- Amendments to IAS 32 and IAS 1 "*Puttable Financial Instruments and Obligations Arising on Liquidation*";
- Amendments to IFRS 2 "*Share-based Payment - Vesting Conditions and Cancellations*";
- IFRS 3 (amended 2008) "*Business Combinations*";
- IAS 27 (amended 2008) "*Consolidated and Separate Financial Statements*".

IFRS 8 "Operating Segments"

IFRS 8 "Operating Segments" sets out requirements for disclosure of information about an entity's operating segments and also cancels the requirement to disclose the information about the entity's primary (products and services) and secondary (geographical areas in which it operates) segments. The Standard changes the procedure of assessment of segment financial information, requires an entity to use the financial data of the operating segments that was included in assessment made to provide financial information to the chief operating decision makers to decide how to allocate operational resources and in assessing performance. Requires to disclose the factors which were used to determine the operating segments. This Interpretation must be applied for annual reporting periods that commence on or after 1 January 2009.

IAS 1 (amended 2007) "Presentation of Financial Statements"

IAS 1 (amended 2007) "Presentation of Financial Statements" requires disclosure of changes in shareholders' equity separately from other changes in equity. It also requires disclosure, on the face of the statement of changes in equity related to transactions with equity holders only whereas all other changes in equity (i.e. income and expenses for the period recognized directly in equity), will be shown separately. Introduces the new statement of comprehensive income: it presents all items of income and expense recognized in the income statement, together with all other items recognized directly in equity. Changes in income and expenses recognized in equity may be reflected either in the statement of comprehensive income in two separate statements: income statement or statement of comprehensive income. This Interpretation must be applied for annual reporting periods that commence on or after 1 January 2009.

IAS 23 (amended 2006) "Borrowing Costs"

IAS 23 (amended 2006) "Borrowing Costs" eliminates the possibility to immediately recognize as borrowing costs interest expenses which relate to assets that necessarily take a substantial period of time to get ready for their intended use or sale. The standard must be applied for annual reporting periods that commence on or after 1 January 2009.

IFRIC 11 "IFRS 2 – Group and Treasury Share Transactions"

IFRIC 11, "IFRS 2 – Group and Treasury Share Transactions" determines whether certain transactions should be accounted for as equity-settled or as cash-settled under the requirements of IFRS 2, and relates to the accounting treatment of share-based payment arrangements that involve two or more entities within the same group. This interpretation must be applied for reporting periods that commence on or after 1 March 2007.

IFRIC 12 "Service Concessions Arrangements"

IFRIC 12 "Service Concessions Arrangements" sets out general recognition principles for the obligations and related rights in service concession arrangements. This Interpretation must be applied for reporting periods that commence on or after 1 January 2008.

IFRIC 13 "Customer Loyalty Programs"

IFRIC 13 "Customer Loyalty Programs" requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted. Therefore part of the fair value of the consideration received is allocated to the award credits and deferred over the period that the award credits are executed. This Interpretation must be applied for reporting periods that commence on or after 1 July 2008.

IFRIC 14 "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction"

IFRIC 14 "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" provides guidance on how to assess the limit on the amount of surplus in a defined benefit scheme that can be recognized as an asset under IAS 19 "Employee Benefits". This Interpretation must be applied for reporting periods that commence on or after 1 January 2008.

Amendments to IAS 32 and IAS 1 "Puttable Financial Instruments and Obligations Arising on Liquidation"

Amendments to IAS 32 and IAS 1 "Puttable Financial Instruments and Obligations Arising on Liquidation" require some financial instruments and liabilities arising from the liquidation under certain conditions be classified as equity. It also sets out which information related to puttable financial instruments to be classified as equity is subject to disclosure. These amendments must be applied for reporting periods that commence on or after 1 January 2009.

Amendments to IFRS 2 "Share-based Payment - Vesting Conditions and Cancellations"

Amendments to IFRS 2 "Share-based Payment - Vesting Conditions and Cancellations" define the term "vesting condition" as either an explicit or implicit service requirement. Other conditions comprise "non-vesting conditions" which must be considered in assessing fair value of the equity instruments granted. If the rights related to the equity instrument were not vested due to the failure to meet the requirement which was a vesting condition to be fulfilled and its fulfillment was controlled by the entity or its counterparty, the equity instrument is recognized as cancelled. These amendments must be applied for reporting periods that commence on or after 1 January 2009.

IFRS 3 (amended 2008) "Business Combinations"

IFRS 3 (amended 2008) "Business Combinations" introduces some changes in accounting for business combinations which will affect the amounts of goodwill to be recognized and the financial results to be recognized in the period of acquisition and subsequent periods. This Standard must be applied for annual reporting periods that commence on or after 1 July 2009.

IAS 27 (amended 2008) "Consolidated and Separate Financial Statements"

IAS 27 (amended 2008) "Consolidated and Separate Financial Statements" requires accounting for the movements in the parent's portion of a subsidiary's equity as an equity transaction. Changes the requirements for accounting for losses incurred by the subsidiary as well as the requirements for accounting for the cease of control over the subsidiary. This Standard must be applied for annual reporting periods that commence on or after 1 July 2009.

The Company believes that adoption of the standards listed above will have no significant impact on the financial statements, operating results and financial position of the Company.

Revision of the Historical Financial Information

In the course of the preparation of the financial statements for 2007, the Company identified some errors which related to the historical financial information. The errors related to 2006 and previous years were corrected through the revision of the comparable information for 2006 and adjustments of the balances of assets, liabilities and retained earnings as of 31 December 2005, respectively.

Fair Value of the Property, Plant and Equipment

During 2007 an independent appraiser completed a valuation of the Company's property, plant and equipment which existed as at 1 January 2003, the date of transition to IFRS. Fair values of property, plant and equipment as at 1 January 2003 have been used as deemed cost as of that date.

As a result, net book values of property, plant and equipment, balances of deferred revenue related to property, plant and equipment received free of charge, and balances of deferred tax liabilities as at 31

(in millions of Russian Roubles)

December 2005 and 2006, as well as amount of depreciation and loss on disposal of property, plant and equipment, revenue related to amortization of respective deferred revenue, and related amounts of deferred tax charge (credit) for the year ended 31 December 2006 have been restated in these financial statements as shown below.

	As previously reported	**Restatement**	**Restated**		**Description of adjustments**
Consolidated balance sheet as at 31 December 2006					
Property, plant and equipment	11,786	(1,583)	10,203	1	Result of changes in the value of property, plant and equipment as at 31 December 2006
Deferred revenue	(101)	(21)	(122)	2	Result of change of deferred revenue as at 31 December 2006
Deferred income tax liabilities	(903)	518	(385)	3	Result of change of deferred income tax liability as at 31 December 2006
Retained earnings	(2,638)	1,086	(1,552)	4	Result of p.1,2,3 on retained earnings as at 31 December 2006
Consolidated income statement for the year ended 31 December 2006					
Revenues	(10,885)	(14)	(10,899)	5	Result of change of due to change in deferred revenue as at 31 December 2006
Depreciation and amortisation	1,298	515	1,813	6	Result of change of depreciation and amortization as at 31 December 2006
Gain on disposal of property, plant and equipment	(30)	8	(22)	7	Result of change of loss on disposal of property, plant and equipment as at 31 December 2006
Other operating expenses	2,247	(165)	2,082	8	Result of change in write off of social assets
Income tax expense	523	(120)	403	9	Result of change of income tax as at 31 December 2006
Profit for the year	(339)	224	(115)	10	Result of 5-9above on net profit for 2006
Retained earnings as at 31 December 2005	(2,479)	862	(1,617)	11	Result of restatement on retained earnings as at 31 December 2005

As a result of the adjustments, net profit of the Company in 2006 decreased by RUR 224 million, retained earnings for the prior years decreased by RUR 862 million.

After the errors were corrected, earnings per share decreased by 1,766 Rouble/share.

3 Summary of Significant Accounting Policies

3.1. Principles of Consolidation

The consolidated financial statements of the Company represent the financial statements of OJSC Far East Telecommunication Company and its subsidiaries as of 31 December of each year. The financial statements of subsidiaries are prepared for the same reporting period as the financial statements of the parent Company based on unified accounting policies.

All inter-group balances, transactions, income and expenses resulting from operations within the Company and recognized in the assets are entirely eliminated.

Subsidiaries are fully consolidated as of the date of acquisition, being the date when the Company acquired control over the subsidiary, and continue to be consolidated until the date when such control ceases.

Minority interest represents the portion of profit or loss and net assets not held by the Company and are presented in the income statement and within equity in the consolidated balance sheet separately from parent shareholders' equity.

Acquisition of Subsidiaries

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

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

Increases in Ownership Interests in Subsidiaries

The differences between the carrying values of net assets attributable to interests in subsidiaries acquired and the consideration given for such increases are recognized in equity as of the transaction date as the purchase of the minority interests and are charged or credited to retained earnings and reserves.

3.2. Property, Plant and Equipment

3.2.1. Cost of Property, Plant and Equipment

Property, plant and equipment are recorded at purchase or construction cost less accumulated depreciation and accumulated impairment in value. Such cost includes the cost of replacing part of the property, plant and equipment when that cost is incurred, if the recognition criteria are met. When each major inspection is performed, its cost is recognized as a component in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied. Major renewals and improvements are capitalized, and the assets replaced are retired. Gains and losses arising from the retirement of property, plant and equipment are included in the income statement as incurred. All other repairs and maintenance are charged to the statement of income when the expenditure is incurred.

(in millions of Russian Roubles)

Interest on loans and borrowings received to finance capital expenditures is capitalized to fixed assets during the period of their construction and implementation stage. Other interest expenses are charged to profit and loss statement.

At each reporting date management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount, and the difference is recognized as an expense (impairment loss) in the income statement. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

3.2.2. Depreciation and Useful Life

Depreciation of property, plant and equipment is calculated on a straight-line basis. The depreciation of the property, plant and equipment which requires state or technical registration commences from the put into operation.

The property, plant and equipment's residual values, useful lives and methods are reviewed and adjusted as appropriate at each reporting date.

As of 1 January 2007 the Company's management reassessed the remaining useful lives of items of property, plant and equipment which resulted in the revision of the remaining useful lives of the certain items of property, plant and equipment.

The Company applies the following useful lives:

	2007	**2006**
Buildings	10 -50	50
Transmission devices (radio and communication lines)	10-15	20
Other constructions (exclusive communication lines)	7-50	20
Analogue switches	2-10	15
Other telecommunication equipment	2 – 15	15
Transportation equipment	4-10	5
Computers, office and other equipment	2 – 7	4-5
Other property, plant and equipment	1-10	5
Land	Not depreciated	Not depreciated

Reassessment of the remaining useful lives was caused by the rapid replacement of telecommunication equipment and technologies, including new industry requirements to communication network digitalization. The Company actively introduces new services and technologies related to the broadband access to the Internet, engages in the upgrades of its fixed line network infrastructure and implements packet switching. The acceleration of the physical obsolescence of the computers and office equipment was due to the technological change in the telecommunication.

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

3.2.3. Assets Received from Free of Charge

Equipment transferred to the Company free of charge by its customers and other entities outside the privatization process is capitalized at fair value at the date of transfer. Transfers of equipment mainly relate to the rendering of future services to the transferee the equipment. In this case, the Company recognizes the deferred income in the amount of fair value of the received property, plant and equipment and recognizes income in the income statement on the same basis that the equipment is depreciated.

3.2.4. Leases

Definition of the arrangement that contains lease is based on the terms of the arrangement, i.e. whether execution of the contract depends on the utilization of asset and/or assets or the arrangement stipulates the right on the use of such asset.

Finance leases in terms of which the Group assumes substantially all the risks and rewards of ownership are recognized as assets and liabilities in the balance sheet at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payment, each determined at the inception of the lease. Minimum lease payments are apportioned between the finance charge and the reduction of outstanding liability. Finance charges are recognized in the income statement.

If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset is fully depreciated over the shorter of the lease term and its useful life.

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

3.2.5. Construction in Progress

Construction in progress is an asset, which is under construction or requires any other activities to bring it to the location and condition necessary for it to be capable of operating in the manner intended by management.

Construction in progress is recorded as the total of actual expenditures incurred less any impairment losses. Construction in progress is not depreciated.

3.2.6. Subsequent Expenditure

Expenditure for continuing repairs and maintenance is charged to the income statement as incurred. Major renewals and improvements are capitalized, and the assets replaced are written off. Profit or loss from the assets write off is charged to the income statement as incurred.

Major inspections expenses are capitalized to the balance cost if the recognition requirements are met.

3.3. Intangible Assets and Goodwill

3.3.1. Goodwill

Goodwill on an acquisition of a subsidiary is included in intangible assets. Goodwill on an acquisition of an associate is included in the investments in associates. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Company are assigned to those units or groups of units. Each unit or group of units to which the goodwill is allocated:

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

Impairment is determined by assessing the recoverable amount of the cash-generating unit (groups of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognized. Impairment loss can not be reversed in future periods.

Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

3.3.2. Other Intangible Assets

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

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

The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortized over the useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates.

Useful lives of the intangible assets are described in Note 8.

3.4. Borrowing Costs

The borrowing costs are capitalized by the Company as part of the cost of the asset when the costs are directly attributable to the acquisition, construction of a qualifying asset including construction in progress. Other borrowing costs are expensed as incurred.

3.5. Associates

Associates are entities in which the Company generally has between 20% and 50% of the voting rights, or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method.

3.6. Investments and Other Financial Assets

The Company's investments are classified as either financial assets at fair value revalued through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets.

When financial assets are recognized initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset.

The Company determines the classification of its financial assets at initial recognition. At each financial year-end, the Company reviews the classification of financial assets when appropriate and is allowed by standards.

Purchases and sales of financial assets are recognized on the settlement date, which is the date that the investment is delivered to or by the Company.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortized cost using the effective interest rate less any allowance for impairment. Gains and losses are recognized in income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected losses that have not been incurred yet) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount is reduced by using the allowance. Loss is recognized in profit and loss statement.

Firstly the Company assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Company determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

Provision for doubtful accounts receivable is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Company will not be able to collect all of the amounts due under the original terms of the invoice. Impaired debts are derecognized when they are assessed as uncollectible.

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit and loss. Investments are classified as held for trading if they are acquired for the purpose of selling in the near term.

Non-derivative financial assets with fixed or determinable payments and fixed maturity that the Company has the positive intention and ability to hold to maturity are classified as held-to-maturity. All other investments, which were not classified to any of the three preceding categories, are available-for-sale investments. After initial recognition available-for-sale investments are measured at fair value with gains or losses being recognized as a separate component of equity until the investment is derecognized or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement.

3.7. Inventories

The cost of inventories comprises all costs of purchase and other costs incurred in bringing the inventories to their present conditions.

The cost of inventories is determined on the weighted average basis.

3.8. Cash and Cash Equivalents

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

3.9. Accounts Receivable

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

Allowance for impairment is created based on the historical pattern of collections of accounts receivable and a specific analysis of the recoverability of significant accounts. Allowance for impairment is also created for other accounts receivable based on the assessment of the Company's ability to collect the debts.

Allowance for impairment is recognized in the income statement. The carrying amount of current trade receivables is a reasonable approximation of their fair value. The fair value of non-current trade receivables is calculated using the effective interest method.

3.10. Shareholders' Equity

Share Capital

Ordinary shares and non-cumulative non-redeemable preference shares are both classified as equity.

Treasury Shares

When share capital recognized as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognized as a deduction from equity. Repurchased share are classified as treasury shares and are presented as a deduction from total equity until their subsequent sale or additional issue. The gain or loss on purchase, sale or cancellation of treasury shares is not recognized in the income statement. The consideration received from subsequent sale or additional issue of shares is included into share capital.

Minority Interest

Minority interest represents the interest in subsidiaries not held by the Company. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair value of the identifiable assets and liabilities of the subsidiaries at the date of the combination or the date when the subsidiary was established and the minorities' portion of movements in equity since the date of the combination or establishment.

Dividends

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

3.11. Financial Liabilities

3.11.1. Borrowings Received

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

3.11.2. Financial Guarantees

Financial guarantees issued by the Company arise from a contract that requires a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument.

Financial guarantee contracts are recognized initially at fair value adjusted for costs which directly relate to the issuance of the guarantees. Subsequently, financial guarantee obligations are estimated as the higher of best estimate of the expenditure required to settle the present obligation at the balance sheet date or the amount initially recognized less, when appropriate, cumulative amortization recognized in accordance with IAS 18 “Revenue”.

3.12. Employee Benefits

3.12.1. Current Employment Benefits

Wages and salaries paid to employees are recognized as expenses in the current period. The Company also accrues expenses for future vacation payments.

3.12.2. Unified Social Tax

Under provisions of the Russian legislation, social contributions are made through a unified social tax (“UST”) calculated by the Company by the application of a regressive rate (from 17% to 26%) to the annual gross remuneration of each employee.

3.12.3. Pensions and Other Post-Employment Benefit Plans

The Company provides defined benefit pension plan to its employees which requires contributions to be made to a separately administered fund. The Company also provides certain additional post-employment benefits and other long-service employees benefits of a defined nature such as lump-sum payments upon retirement and death and financial support to the Company’s old age and disabled pensioners.

The cost of providing benefits under the defined benefit plan is determined separately for each plan using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses for each individual plan at the end of the previous reporting period exceed 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plans.

The past service cost arises when the Company introduces a defined benefit plan or changes the benefits payable under an existing defined benefit plan. The past service cost is recognized as an expense on a straight line basis over the average period until the benefits become vested. If the benefits are already vested immediately following the introduction of, or changes to, a pension plan, past service cost is recognized immediately.

The defined benefit asset or liability comprises the present value of the defined benefit obligation less past service cost not yet recognized and less the fair value of plan assets out of which the obligations are to be settled directly. The value of any asset is restricted to the sum of any past service cost not yet recognized and the present value of any economic benefits available in the form of refunds from the plan or reductions in the future contributions to the plan.

3.13. Provisions

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

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

3.14. Deferred Income Taxes

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method.

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

Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

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

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

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

3.15. Revenue Recognition

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

Revenues from services are recognized in the period when services are rendered. Revenue from time-based telephony calls and data transmission services depends on the volume of traffic processed for the period.

3.15.1. Local Telephony Calls, including Universal Telecommunication Services

If the fixed payment scheme is applied then revenue is represented by the subscription fee only. If the time-driven billing scheme is applied, the revenue depends on the duration of the telephone connections. If the combined billing scheme is applied, the revenue depends on the fixed payment and the duration of the telephone connections for the excess of the subscriber's calls over the monthly limit. Customers of the Company use the service via installed fixed telephones; the service could be also accessed by means of payphones. The Company recognizes revenues from local calls in the period when the service is rendered.

3.15.2. Intrazone Telephony Services

The Company recognizes revenue from intrazone telephone services in the period when the services are rendered.

3.15.3. Mobile Radiotelephony (Cellular) Services

Revenues from cellular services arise primarily from airtime, subscription fees, value added services, outbound and inbound roaming. The Company recognizes revenues related to mobile telecommunications services in the period when the services are rendered.

3.15.4. Data Transfer and Telematics Services (Internet)

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

3.15.5. Installation and Connection Fees

Installation and connection fees for local telephone services are paid in cash and by the contribution of fixed assets consisting of cable and duct, commonly referred to as the "last mile". Connection fees for fixed-line services received in cash are recognized when the installation and connection are complete. Installation and connection fees for data transfer services, telematics services, mobile radiotelephone (cellular) services are recognized over the average contract period with the subscriber. These revenues are recognized under the respective type of telecommunication services. For installation and connection fees contributed in the form of fixed assets, revenue is deferred and recognized as income on the same basis that respective fixed assets are depreciated.

3.15.6. Interconnection and Traffic Transmission Services

Services to operators include interconnection revenues from Russian operators and charges for interconnection points, revenues received from the local and inter-zone calls initiation from the Company's network/termination in the Company's network and in the networks of interconnected operators. The Company recognizes revenues from operators in the period when the services are rendered.

3.15.7. Fees on Assistance and Agency Services

Fees on assistance services include fees for services provided to long-distance operators under the assistance agreements. These services comprise subscribers billing and invoicing for long-distance calls, delivery of bills, collection of respective receivables and some other services. The Company recognizes revenues related to assistance services in the period when the services are rendered.

3.15.8. Other Revenue from Non-Telecommunication Services

Other revenues primarily consist of revenues received from transportation and construction services, recreation services and sale of products and services provided by auxiliary units.

Reimbursement of losses from universal telecommunication services is recognized in the period to which it relates but not when those losses were reimbursed. The reimbursement is recorded in "Other operating income" line of the income statement.

Dividend income is reflected when the dividends are due to the Company.

3.16. Earnings per Share

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

3.17. Foreign Currency Transactions

The consolidated financial statements are presented in millions of Russian Rubles (Roubles), which is the Company's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to the income statement as foreign exchange gains (losses). Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as of the date of initial transaction. Non monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The exchange rates as of December 31, 2007 and 2006 were as follows:

Exchange rates at 31 December	2007	2006
US Dollar	24.5462	26.3311
EURO	35.9332	34.6965

4 Significant Accounting Judgments and Estimates

4.1. Judgments

In applying the accounting policies, management has made the following judgments, estimates and assumptions besides the accounting estimates, which most significantly affect the amounts reported in the financial statements:

Lease Classification

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership, otherwise it is classified as operational lease. Determining whether an arrangement is, or contains, a lease shall be based on the substance of the arrangement, but not its legal form.

Revenue Recognition

Agency fees relates to the sale of services where the Company acts as an agent in the transaction rather than as the principal. In the absence of specific guidance in IFRSs on distinguishing between an agent and a principal, management considered the following factors:

- Although the Company collects the revenue from the final customer, all credit risk is borne by the supplier of the goods.
- The Company cannot vary the selling prices set by the supplier.

4.2. Estimation Uncertainty

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

Useful Life of Property, Plant and Equipment

The Company estimates remaining useful lives of its property, plant and equipment at least once a year at the financial year end. If the estimation differs from the previous estimations, the changes are accounted for in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. These estimates may have a significant impact on the carrying value of property, plant and equipment and depreciation, charged to the income statement. Net book value of property, plant and equipment as at 31 December 2007 is RUR 12,992 million (as at 31 December 2006: RUR 10,203 million). Please, refer for detailed information to Note 7.

Impairment of Property, Plant and Equipment

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

Fair value of assets and liabilities acquired in Business Combinations

The Company recognizes separately, at the acquisition date, the identifiable assets, liabilities and contingent liabilities acquired or assumed in the business combination at their fair values, which involves estimates.

Such estimates are based on valuation techniques, which require considerable judgment in forecasting future cash flows and developing other assumptions. More details are provided in Note 6.

Impairment of Goodwill

In order to determine whether the goodwill is impaired, it is necessary to estimate the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Company to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows, and hence such estimates are subject to uncertainty. As of 31 December 2007, the carrying amount of the goodwill amounted to RUR 966 million (2006: Nil). More details are provided in Note 8.

Fair Values of Unlisted Available-for-Sale Investments

For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis or other valuation models. These valuation techniques are based on assumptions that are not supported by observable market prices or rates. Management believes the estimated fair values resulting from the valuation technique which are recorded in the balance sheet and the related changes in the fair values recorded in the statement of changes in equity are reasonable and the most appropriate at the balance sheet date. As of 31 December 2007, the fair values of unlisted available-for-sale investments amounted to RUR 18 million (2006: RUR 7 million). More details are provided in Note 11.

Allowance for Impairment of Accounts Receivable

Provision for impairment is based on the historical data related to collectability of accounts receivable and solvency analysis of the most significant debtors. If the financial condition of customers were to deteriorate, actual write-offs might be higher than expected. As of 31 December, 2007, allowances for impairment of accounts receivable have been created in the amount of RUR 296 million (2006: RUR 257 million). More details are provided in Notes 15 and 16.

Pension Obligations

The present value of defined post-employment benefit obligations and related current service cost are determined in accordance with actuarial valuation which rely on demographic and financial assumptions including mortality, both during and after employment, rates of employee turnover, discount rate, future salary and benefit levels and, to a limited extent, expected return on plan assets. In the event that further changes in the key assumptions are required, the future amounts of the pension benefit costs may be affected materially. As of 31 December 2007, net defined benefit obligations amounted to RUR 964 million (2006: RUR 436 million). More details are provided in Note 23.

Litigation and Claims

The Company exercises considerable judgment in measuring and recognizing provisions and the exposure to contingent liabilities related to pending litigations or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgment is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the final settlement. Because of the inherent uncertainties in this evaluation process, actual losses may be different from the originally estimated provision. These estimates are subject to change as new information becomes available, primarily with the support of internal specialists, if available, or with the support of outside consultants, such as actuaries or legal counsel. Revisions to the estimates may significantly affect future operating results. As of 31 December 2007, the best estimation of the litigation provision amounts to RUR 412 million (2006: RUR 813 million). More details are provided in Note 24.

(in millions of Russian Roubles)

5 Segment Information

	2007				
	Fixed line	**Mobile**	**Other**	**Intercompany eliminations**	**Total for the Group**
REVENUE					
Sales to third parties	12,963	1,186	852		**15,001**
Inter–segment sales	71	22	46	(139)	
Total revenue	**13,034**	**1,208**	**898**	**(139)**	**15,001**
GROSS PROFIT					
Segment result	2,289	855	433		3,577
Unallocated corporate expenses					(1,058)
Operating profit					**2,519**
Share of result of associates					(2)
Interest income/(expense), net					(550)
(Losses)/gains from financial investments					44
Foreign exchange loss, net					3
Income tax expense					(654)
Profit for the year					**1,360**
ASSETS AND LIABILITIES					
Segment assets	16,920	859	324		18,103
Investments in associates					67
Unallocated corporate assets					1,289
Consolidated total assets					19,459
Segment liabilities	(9,837)	(96)	(86)		(10,019)
Unallocated corporate liabilities					(1,004)
Consolidated total liabilities					(11,023)
OTHER SEGMENT INFORMATION					
Capital expenditure					
Fixed assets	(1,498)	(42)	(14)	-	(1,554)
Depreciation and amortization	(1,969)	(93)	(26)		(2,088)
Bad debt (expense)/ recovery	42	16	-	-	58

(in millions of Russian Roubles)

	2006 (restated)				
	Fixed line	**Mobile**	**Other**	**Intercompany eliminations**	**Total for the Group**
REVENUE					
Sales to third parties	9,495	1,024	380	-	**10,899**
Inter–segment sales	58	-	40	(98)	**-**
Total revenue	**9,553**	**1,024**	**420**	(98)	**10,899**
GROSS PROFIT					
Segment result	635	689	(133)	-	1,191
Unallocated corporate expenses					(101)
Operating profit					**1,090**
Share of result of associates					**(2)**
Interest income (expense), net					**97**
Gain/(loss) from financial investments, net					**(639)**
Other income/(expense), net					**(47)**
Foreign exchange loss, net					**19**
Income tax expense					**(403)**
Profit for the year					**115**
ASSETS AND LIABILITIES					
Segment assets	13,674	1,619	199	-	**15,492**
Investments in associates					**24**
Unallocated corporate assets					**251**
Consolidated total assets					**15,767**
Segment liabilities	(9,081)	(99)	(89)	-	**(9,269)**
Unallocated corporate liabilities					**(565)**
Consolidated total liabilities					**(9,834)**
OTHER SEGMENT INFORMATION					
Capital expenditure					
Fixed assets	1,829	241	-	-	**2,070**
Intangible assets	335	33	-	-	**368**
Depreciation and amortization	(1,383)	(235)	(195)	-	**(1,813)**
Other non–cash expenses (provision for doubtful receivables)	(40)		-	-	**(40)**

The Company provides fixed line and mobile telecommunication services, as well as other services. Management believes that the Company operates in one geographical segment.

Transfer prices on segment operations are established in the same way as prices on operations with third parties are established. Income, expenses and financial results of segments allow transfer operations among segments eliminated while being consolidated.

Unallocated expenses, assets and liabilities are expenses, assets and liabilities that arise at the entity level and relate to the entity as a whole.

Segment assets consist primarily of property, plant and equipment, intangible assets, inventories, receivables, and operating cash and exclude financial investments, income tax assets and other assets that relate to the entity as a whole.

Segment liabilities primarily comprise operating liabilities, loans and leasing liabilities and exclude items such as deferred tax liabilities and other liabilities pertaining to the Company as a whole.

Capital expenditure comprises additions to property, plant, equipment and intangible assets. Loss of value and provisions relate only to those charges made against allocated assets.

(in millions of Russian Roubles)

6 Business Combinations

Acquisition of OJSC "Sakhatelecom"

In accordance to the results of the open bid took place in December 2006 the Company acquired 764,769 ordinary shares (51%) for RUR 2,295 million. Total amount paid is RUR 2,303 million including transaction costs of RUR 8 million.

Principal activity of OJSC "Sakhatelecom" is provision local telephony services in Republic of Sakha (Yakutiya).

The acquisition of OJSC Sakhatelecom was accounted for using the purchase method in accordance with provisions of IFRS 3 "Business Combinations". Accordingly, the results of operations and financial positions of OJSC Sakhatelecom were consolidated by the Company beginning from 1 January 2007. The information on the acquisition cost, fair value of identifiable assets, liabilities and contingencies of OJSC Sakhatelecom and goodwill as of the date of acquisition is disclosed below:

	2007
Acquisition price	2,295
Transaction costs	8
Total paid	**2,303**
Fair value of net identifiable assets and liabilities	
Property, plant and equipment	2,897
Intangible assets	707
Long-term investments	20
Trade and other receivables	471
Cash and cash equivalents	121
Other current assets	138
Short-term liabilities	(659)
Long-term liabilities	(1,061)
NET ASSETS	**2,634**
Company's share in acquired assets, %	51%
Assigned value of acquired share in identifiable net assets	1,343
Amount of goodwill arising on acquisition	**960**

The disclosure of carrying value of assets, liabilities and contingencies of OJSC Sakhatelecom in accordance with IFRS, immediately before the business combination, is impracticable as OJSC Sakhatelecom had not been IFRS reporter.

Based on the fair value of identifiable assets, liabilities and contingencies determined in accordance with IFRS 3, the acquisition cost exceeded the fair value of the share acquired in the net assets of OJSC Sakhatelecom by RUR 960 million. In accordance with IFRS 3, the amount was reported in the balance sheet in the line "Intangible assets". Management believes that the goodwill related to the expected synergies and other benefits expected from combining the assets and activities of OJSC Sakhatelecom with those of the Company.

The transaction price was fully paid in cash. The table below summarises net cash costs incurred in the acquisition:

	2007
Cash paid	2,303
Less: cash received in the acquisition of subsidiary	(121)
Net cash expenses	**2,182**

Profits of OJSC Sakhatelecom for 2007 included in the calculation of consolidated profit for the reporting period totalled to RUR 200 million.

(in millions of Russian Roubles)

Acquisition of Share Capital in LLC "Interdaltelecom"

The Company purchased 58% of share capital of LLC "Interdaltelecom" increasing its share from 39% to 97%. The amount of transaction is RUR 22 million.

Share is acquired for the further long-term investments with notification on acquisition made as at 29 December 2007.

Principal activity of LLC "Interdaltelecom" is providing local calls services in Primor'ye region of Far East.

Management believes that book value of assets, liabilities and contingent liabilities of LLC "Interdaltelecom" at the date of acquisition is in line with their fair value.

Management has assigned the acquisition price for 58% of LLC "Interdal'telecom" as follows:

	2007
Acquisition price	22
Total paid	**22**
Fair value of net identifiable assets and liabilities	
Property, plant and equipment	10
Long-term investments	50
Trade and other receivables	2
Cash and cash equivalents	-
Short-term liabilities	(7)
Long-term liabilities	(12)
Total net assets	**43**
Company's share in acquired assets, %	97%
Assigned value of acquired share in identifiable net assets	42
Amount of negative goodwill arising on acquisition	**20**

Acquisition of Additional Shares in ZAO AKOS

In 2007 the Company acquired additional 0.69% of shares in ZAO AKOS for RUR 8 million. This transaction resulted in goodwill of RUR 6 million which was recognised in "Intangible Assets".

Aggregated information on acquisitions for the year ended 31 December 2007 is listed below:

	2007
Aggregated acquisition price	2,325
Aggregated transaction costs	8
Total paid	**2,333**
Aggregated fair value of net identifiable assets and liabilities	
Property, plant and equipment	2,907
Intangible assets	707
Long-term investments	70
Trade and other receivables	473
Cash and cash equivalents	121
Other current assets	140
Short-term liabilities	(666)
Long-term Liabilities	(1,073)

(in millions of Russian Roubles)

7 Property, Plant and Equipment

	Land, buildings and constructions	Switches and transmission devices	Construction in progress and equipment for installation	Vehicles and other	Total
Cost					
At 31 December 2005	6,912	5,112	808	1,194	14,026
Additions	-	1	2,181	-	2,182
Additions due to acquisition of subsidiaries	28	49	-	3	80
Disposals	(166)	(51)	(230)	(38)	(485)
Transfers	673	1,044	(2,110)	393	-
At 31 December 2006	**7,447**	**6,155**	**649**	**1,552**	**15,803**
Additions	-	-	2,177	11	2,188
Additions due to acquisition of subsidiaries	1,994	666	132	115	2,907
Disposals	(483)	(178)	(162)	(57)	(880)
Transfers	477	1,225	(1,894)	192	-
At 31 December 2007	**9,435**	**7,868**	**902**	**1,813**	**20,018**
Accumulated Depreciation					
At 31 December 2005	(2,721)	(956)	-	(344)	(4,021)
Charge for the year	(896)	(565)	-	(280)	(1,741)
Disposals	97	38	-	27	162
Transfers	25	22	-	(47)	-
At 31 December 2006	**(3,495)**	**(1,461)**	**-**	**(644)**	**(5,600)**
Charge for the year	(640)	(937)	-	(361)	(1,938)
Disposals	350	119	-	43	512
At 31 December 2007	**(3,785)**	**(2,279)**	**-**	**(962)**	**(7,026)**
Net book value					
At 31 December 2005	**4,191**	**4,156**	**808**	**850**	**10,005**
At 31 December 2006	**3,952**	**4,694**	**649**	**908**	**10,203**
At 31 December 2007	**5,650**	**5,589**	**902**	**851**	**12,992**

(in millions of Russian Roubles)

Determination of Deemed Cost

The Company transitioned to IFRS as of 1 January 2003 using the provisions of IFRS 1, "*First Time Adoption of International Financial Reporting Standards"*. The Company has applied an exemption permitted by IFRS 1 which allows an entity to measure property, plant and equipment at the date of transition to IFRS at fair value and use that fair values as deemed cost. Management estimates that the carrying values of all of the Company's property, plant and equipment are broadly comparable to their fair values.

However, management engaged an independent appraiser, ZAO NEO Centre, to independently appraise property, plant and equipment as of 1 January 2003.

The majority of the Group's property, plant and equipment is specialised in nature and is rarely sold on the open market other than as part of a continuing business. While land and buildings were appraised on the basis of recent market transactions, the market for similar plant and equipment is not active in the Russian Federation and does not provide a sufficient number of sales of comparable items for using a market-based approach for determining fair value.

Consequently the fair value of property, plant and equipment was primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

The depreciated replacement cost was estimated based on internal sources and analysis of the Russian and international markets for similar property, plant and equipment. Various market data were collected from published information, catalogues, statistical data etc, and industry experts and suppliers of property, plant and equipment were contacted both in the Russian Federation and abroad.

In addition to the determination of the depreciated replacement cost, cash flow testing and review of alternative use were conducted in order to assess the reasonableness of those values. The results of this testing is set out below for the most significant consolidated entities:

At 1 January 2003	**Depreciated replacement cost**	**Discounted cash flows**	**Determined deemed cost**
Amur branch	989	1,084	989
Kamchatka branch	1,065	1,333	1,065
Magadan branch	650	858	650
Primorie branch	2,818	3,925	2,818
Sakhalin branch	1,167	1,528	1,167
Khabarovsk branch	2,039	2,417	2,039
Total	**8,728**	**11,145**	**8,728**

Below is a summary of key assumptions used to develop cash flow projections:

- The Company determined each branch as a separate cash generating unit;
- Operating income and expenses were determined at the actual level for the last 12 months before the date of valuation, 1 January 2003;
- The growth rate of 5% were used for operating income and expenses, this reflects average inflation rate for the remaining useful life of assets;
- The discount rate of 19% was used.

(in millions of Russian Roubles)

Reassessment of the Useful Lives

The property, plant and equipment useful lives and depreciation methods are reviewed annually at each reporting date and adjusted as appropriate. The Company reassessed useful lives as at 1 January 2007 and applied the revised remaining useful lives for certain property, plant and equipment objects going forward.

Under the remaining useful lives as of 1 January 2007 prior to reassessment, the depreciation charge for 2007 would have been RUR 369 million lower as compared with depreciation charge in income statement for 2007.

Depreciation of the Property, Plant and Equipment

The depreciation charge of the property, plant and equipment for 2007 in the amount of RUR 1,937 million was recognised in Depreciation and amortisation line in consolidated income statement (2006: RUR 1,741 million).

The net book value of fully depreciated fixed assets is RUR 2,856 million as at 31 December 2007 (RUR 2,827 million as at 31 December 2006).

Finance Lease

The net book value of plant and equipment held under finance leases at 31 December 2007 and 2006 amounted to:

	2007	2006
Buildings and constructions	-	2
Switches and transmission devices	1,206	1,622
Construction in progress and equipment for installation	4	11
Vehicles and other fixed assets	53	45
Total net book value of plant and equipment	**1,263**	**1,680**

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

Capitalized Interest

The Company increased construction in progress value by the amount of capitalized interest expense of RUR 52 million for the year ended 31 December 2007 (2006: RUR 67 million). Capitalization rate for the year ended 31 December 2007 – 8.6% (for the year ended 31 December 2006: 8.7%)

(in millions of Russian Roubles)

8 Intangible Assets and Goodwill

	Goodwill	Licenses	Software	Customer base	Trademark	Other	Total
At 31 December 2005	**77**	**179**	**647**	**15**	**-**	**12**	**930**
Additions	-	1	310	-	-	11	322
Additions due to acquisition of subsidiaries	14	-	-	-	-	-	14
Disposals	-	-	(14)	-	-	-	(14)
At 31 December 2006	**91**	**180**	**943**	**15**	**-**	**23**	**1,252**
Additions	-	6	346	-	-	-	352
Additions due to acquisition of subsidiaries	966	9	1	640	57	-	1,673
Disposals	-	(2)	(42)	-	-	(1)	(45)
At 31 December 2007	**1,057**	**193**	**1,248**	**655**	**57**	**22**	**3,232**
Accumulated amortization and impairment							
At 31 December 2005	**(77)**	**(16)**	**(14)**	**(8)**	**-**	**(3)**	**(118)**
Amortization charge for the year	-	(27)	(58)	(7)	-	(10)	(102)
Charge on disposal	-	1	12	-	-	-	13
Impairment charge	(14)	-	-	-	-	-	(14)
At 31 December 2006	**(91)**	**(42)**	**(60)**	**(15)**	**-**	**(13)**	**(221)**
Amortization charge for the year	-	(29)	(86)	(21)	(14)	-	(150)
Charge on disposal	-	2	18	-	-	1	21
Impairment charge	-	-	-	-	-	-	-
At 31 December 2007	**(91)**	**(69)**	**(128)**	**(36)**	**(14)**	**(12)**	**(350)**
Net book value at 31 December 2005	-	163	633	7	-	9	812
Net book value at 31 December 2006	-	138	883	-	-	10	1,031
Net book value at 31 December 2007	966	124	1,120	619	43	10	2,882

Oracle E-Business Suite (OEBS)

As at 31 December 2007 software includes OEBS software with a net book value of RUR 360 million (2006: RUR 326 million), including interest capitalized RUR 13 million (2006: RUR 4 million). The rate of the capitalization was 8.33% (2006: 9.00%).

The Company commenced the commercial operation of OEBS in relation to the modules for accounting for non-current assets and human resources. Amortization charge has begun from the moment of implementation (March 2006) proportionally to the quantity of licenses used during useful life limit (10 years).

Full implementation of Oracle E-Business Suite software is expected to be completed before 2009.

Licenses

The useful life of licenses is determined individually for each license based on the terms and conditions of the license agreement. The useful lives have been determined to be 1-5 years.

Trade Mark

The trade mark was acquired by the Company through a business combination with OJSC Sakhatelecom. The Company determined useful life of this intangible asset as four years.

Customer Base

The customer list was acquired through a business combination with OJSC Sakhatelecom. The Company determined the useful life as 30 years.

Amdocs Billing System Software

As at 31 December 2007 software also includes Amdocs Billing Suite software with a gross book value of RUR 293 million (2006 – RUR 315 millions).

This software was purchased for the purpose of the implementation of unified automated system. The project of implementation of the unified automated settlements system is expected to last 4-5 years.

The Company took the decision on temporarily project suspension to implement Integrated Automatic Computation System on the basis of Amdocs Billing Suite and review the date of implementation.

Results of initial phase of Amdocs implementation process are used by the Company to balance settlements with subscribers and Automatic Computation System "Start" introduction. Considering this fact the expenses incurred by the Company in the amount of RUR 16 million.

Software development in object code format is inapplicable for the further usage development expenses in the amount RUR 22 million are recognized as Other expenses.

The Company will commence amortizing this asset from the date of software implementation. Until then the Company annually tests this software for impairment.

Amortisation

Amortisation charge for 2007 in the amount of RUR 150 million (2006: RUR 102 million) was recorded in line "Depreciation and amortization" of Consolidated Income Statement.

Goodwill and Intangible Assets Recognised in Business Combinations

The intangible assets recognised separately as a result of acquisition of OJSC SakhaTelecom (note 6) represent resources from which future economic benefits are expected to flow to the Company and include the following:

- Customer base;
- Software;
- Other intangible assets.

(in millions of Russian Roubles)

The customer base is an intangible asset that represents contractual relations with subscribers and has the useful life of 30 years.

Impairment Testing of Intangible Assets not yet Available for use

The Company performed impairment testing of intangibles not implemented. As at 31 December 2007 intangibles includes Amdocs Billing Suite and Oracle E-Business Suite. No impairment was revealed as the result of the test as at 31 December 2007.

Impairment Testing of Goodwill

In 2006 the Company recognised goodwill resulted from acquisition of OAO A-Svyaz that was subsequently restructured through the transfer of all operating assets and activities to Amur branch. As of 31 December 2006 the Company recognised an impairment of goodwill related to the acquisition of OAO A-Svyaz in the amount of RUR 14 million.

In 2007 the Company recognised goodwill of RUR 960 million resulted from acquisition of OJSC Sakhatelecom. The recoverable amount of goodwill was determined based on its value in use calculation using cash flow projections based on financial budgets approved by management covering a five years period. The discount rate applied to the cash flow projection is 15.5% and cash flows beyond this period were extrapolated based on average industry-wide profitability indices and using 4% growth rate.

In 2007 the Company recognised goodwill of RUR 6 million resulted from acquisition of additional 0.69% in ZAO AKOS, Company's subsidiary (note 6).

As a result of the test performed no impairment of goodwill was identified.

9 Consolidated Subsidiaries

The consolidated financial statements include the assets, liabilities and financial results of OJSC Far East Telecommunication Company and its subsidiaries, which main activity is provision of cellular and other telecommunication services. The subsidiaries controlled by the Company are listed below:

Subsidiary	Main Activity	Ownership,%		Voting Shares, %	
		31 December 2007	31 December 2006	31 December 2007	31 December 2006
OJSC "A-Svyaz"	Fixed line telecom services	91.80%	84.20%	91.80%	84.20%
LLC"Besprovodnie informatsionnie technologii"	Mobile services	100.00%	100.00%	100.00%	100.00%
CJSC "Integrator.ru"	Investing activity	100.00%	100.00%	100.00%	100.00%
LLC "Interdaltelecom"	Mobile services	97.00%	39.00%	97.00%	39.00%
CJSC "Sakhalinugol Telecom"	Fixed line telecom services	100.00%	100.00%	100.00%	100.00%
OJSC "Sakhatelecom"	Fixed line telecom services	51.00%	0.00%	51.00%	0.00%
CJSC "AKOS" (owned by CJSC "Integrator.ru")	Mobile services	94.26%	93.58%	94.26%	93.58%

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

(in millions of Russian Roubles)

10 Investments in Associates

The following table illustrates summarized financial information of the Company's associates:

Associate	Voting shares	Assets	Liabilities	Revenues	Net loss
2007					
LLC "Kamalyaskom"	50%	3	2	3	-
LLC "Magalyaskom"	50%	33	-	6	(2)
LLC "Vostoktelecom"	25%	227	(25)	246	21
2006					
LLC "Kamalyaskom"	50%	3	(2)	4	-
LLC "Magalyaskom"	50%	36	-	7	(1)
CJSC "Teleross-Vladivostok"	50%	12	-	3	(2)

Investments in associates at 31 December 2007 and 2006 comprised the following:

Associate	Activity	Voting shares	Carrying value
2007			
LLC "Kamalyaskom"	Mobile services	50%	1
LLC "Magalyaskom"	Mobile services	50%	16
LLC "Vostoktelecom"	Telecommunication services	25%	50
Total			**67**
2006			
LLC "Kamalyaskom"	Mobile services	50%	1
LLC "Magalyaskom"	Mobile services	50%	18
CJSC "Teleross-Vladivostok"	Telecommunication services	50%	5
LLC "Interdaltelecom"	Telecommunication services	39%	-
			24

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

As the result of the acquisition of additional share in LLC "Interdaltelecom" the Company reclassified financial investments in LLC "Interdaltelecom" as investments in subsidiary.

Sale of CJSC "Teleross-Vladivistok" shares

In accordance with the Board of Directors decision (minutes # 15 dated 15 March 2007) the Company and LLC "Sovintel" signed sales purchases agreement of shares owned by the Company. Total amount received is RUR 11 million, quantity of shares sold is 291,200.

Profit from Sale and other disposal of Company's share is disclosed in Note 29.

Movement in investments in associates for the years ended 31 December 2007 and 2006 is presented below:

	2007	2006
Investments in associates at 1 January	**24**	**26**
Acquisition of associates	50	-
Share of loss, net of income tax and dividends received	(2)	(2)
Disposal of associates	(5)	-
Investments in associates at 31 December	**67**	**24**

The carrying value of investments in associates shown in these consolidated financial statements is equivalent to the Company's share in the net assets of the associated companies.

(in millions of Russian Roubles)

11 Financial Investments

As at 31 December 2007 and 2006 the Company's investments comprised the following:

	2007	2006
Long term financial investments available-for-sale	18	7
Total long term financial investments	**18**	**7**
Financial investments held to maturity	770	-
Financial investments held for sale	1	1
Total short-term financial investments	**771**	**1**
Total financial investments	**789**	**8**

As at 31 December 2007 financial investments held for clearing consisted from promissory notes of "Russkiy Industrialny Bank" and "Svyaz-Bank" in the amount of RUR 470 million and RUR 300 million, respectively. At 31 December 2007 the promissory notes are recognised at initial value.

Financial investments as at 31 December 2007 are listed below:

	2007		2006	
Company	**Ownership interest**	**Carrying value**	**Ownership interest**	**Carrying value**
Long–term investments				
JSCB "Sberbank"	-	11		
OJSC "Svyazintech"	4.00%	5	4.00%	5
OJSC "SEZ Nakhodka"	8.47%	1	8.47%	1
OJSC "JSCB Svyazbank"	0.03%	1	0.03%	1
Short–term investments				
OJSC "Russian Industrial Bank"	Promissory notes	470		-
OJSC "JSCB Svyazbank"	Promissory notes	300		-
OJSC "Far East Commercial Bank Dalcombank"	1.40%	-		1
Others	-	1	-	-
Total investments		**789**		**8**

12 Long-term Accounts Receivable and Other Assets

As at 31 December 2007 and 2006 long-term accounts receivable and other assets comprised the following:

	2007	2006
Long-term accounts receivable	1	1
Long-term loans given	11	16
Total	**12**	**17**

As at 31 December 2007 and 2006 long-term loans given to employees are accounted at amortized cost using the effective interest rate of 18% (2006 - 16%).

13 Long-Term Advances Given

As at 31 December 2007 and 2006 long-term advances given comprised the following:

	2007	2006
Long term advances given for capital construction	234	259
Long term advances given for investing activities	-	2,295
Total	**234**	**2,554**

(in millions of Russian Roubles)

14 Inventories

Inventories as at 31 December 2007 and 2006 comprised the following:

	2007	2006
Cable, materials, fuel and spare parts for telecommunications equipment	194	160
Instruments and other inventories	250	170
Finished goods and goods for resale	5	8
Total	**449**	**338**

In 2007 the Company established the allowance for obsolete inventories in the amount of RUR 1 million (2006: RUR 2 million) and related expenses were recognized in line "Other operating expenses".

As at 31 December 2007 no inventories have been pledged as security for borrowings.

15 Trade and Other Accounts Receivable

Accounts receivable as at 31 December 2007 and 2006 comprised the following:

	Accounts receivable as at 31 December 2007	Allowance for impairment as at 31 December 2007	Accounts receivable, net as at 31 December 2007
Receivables from commercial organizations	243	(47)	196
Receivables from individuals	778	(154)	624
Receivables from budget organizations	68	(5)	63
Receivables from interconnect operators	280	(20)	260
Receivables from social funds for welfare recipients	34	(34)	-
Other receivables	132	(12)	120
Total	**1,535**	**(272)**	**1,263**

	Accounts receivable as at 31 December 2006	Allowance for impairment as at 31 December 2006	Accounts receivable, net as at 31 December 2006
Receivables from commercial organizations	140	(33)	107
Receivables from individuals	485	(65)	420
Receivables from budget organizations	56	(5)	51
Receivables from interconnect operators	404	(57)	347
Receivables from social funds for welfare recipients	91	(46)	45
Other receivables	52	(16)	36
Total	**1,228**	**(222)**	**1,006**

The Company invoices its customers on a monthly basis. The Company sends monthly payment requests and substantially relies upon these customers to remit payments based on the received payment requests. All customer payments are based upon tariffs, denominated in Roubles, in effect at the time the calls are made. In some cases the Company received penalty fees for the delayed payments and obtain repayments by court decisions.

As at 31 December 2007 the receivable for tariff compensation from the state budget related to granting discounts to certain categories of privileged subscribers amounted to 2,3% of total accounts receivable from customers (2006 – 7.7%). These receivables originated prior to January 2005, when Article 47 of the Federal Law No. 126-FZ On Communications dated 7 July 2003 came into force changing the procedure of providing telecommunication service benefits to individual customers. Prior to January 2005, those end-users (eligible for such a privilege) paid only 50% of the service fees and the remaining 50% were subject to compensation from the state budget.

(in millions of Russian Roubles)

In 2007 the Company legally enforced settlement from the federal budget of such outstanding receivables in the amount of RUR 54 million (2006: RUR 41 million).

The following table summarizes the changes in the allowance for doubtful receivables:

	2007	2006
Balance at January, 1	222	248
Allowance/(recovery of) for the year	58	40
Trade receivables write-off	(8)	(66)
Balance at 31 December	**272**	**222**

The amount of the allowance for doubtful receivables accrued during 2007 of RUR 58 million (2006: RUR 40 million) and was reflected as "Allowance for doubtful receivables" in the consolidated income statement.

16 Other Current Assets

As at 31 December 2007 and 2006 other current assets comprised the following:

	Other current assets as at 31 December 2007	Allowance for impairment as at 31 December 2007	Other current assets as at 31 December 2007
Advances given	121	(3)	118
Receivables from staff	18	-	18
Short-term loans given	53	-	53
VAT receivable	79	-	79
Other prepaid taxes	19	-	19
Deferred expenses	34	-	34
Other current assets	94	(21)	73
Total	**418**	**(24)**	**394**

	Other current assets as at 31 December 2006	Allowance for impairment as at 31 December 2006	Other current assets as at 31 December 2006
Advances given	116	-	116
Receivables from staff	4	-	4
Short-term loans given	17	-	17
VAT receivable	128	-	128
Other prepaid taxes	12	-	12
Deferred expenses	49	-	49
Other current assets	110	(35)	75
Total	**436**	**(35)**	**401**

17 Cash and Cash Equivalents

As at 31 December 2007 and 2006 cash and cash equivalents comprised the following:

	2007	2006
Cash on hand and at bank	342	184
Total	**342**	**184**

(in millions of Russian Roubles)

18 Share Capital

As at 31 December 2007 the par value and carrying value of the issued and fully paid ordinary and preference shares were as follows:

	Number of shares outstanding (thousands)	Treasury shares (thousands)	Number of shares on issue (thousands)	Total par value	Carrying value
As at 31 December 2006	**126,701**	**49**	**126,750**	**2,535**	**4,366**
Preference	31,143	26	31,169	623	1,081
Ordinary	95,558	23	95,581	1,912	3,285
As at 31 December 2007	**126,744**	**6**	**126,750**	**2,535**	**4,366**
Preference	31,166	3	31,169	623	1,081
Ordinary	95,578	3	95,581	1,912	3,285

All shares have a par value of RUR 20. The difference between the total par value and the total carrying value of share capital represents the effects of inflation accumulated through 1 January 2003. All authorised shares have been issued and fully paid.

The Company's shareholding structure as at 31 December 2007 was as follows:

	Share capital	Ordinary shares		Preference shares	
	%	Number (thousands)	%	Number (thousands)	%
OJSC "Svyazinvest"	38.13	48,331	50.56	-	-
CJSC "Depozitarno-Klringovaya Kompaniya"	19.20	16,250	17.00	8,090	25.95
CJSC "UBS Nominies"	9.87	5,831	6.10	6,674	21.41
Non-commercial partnership ''National deposiary centre"	14.50	12,285	12.85	6,096	19.56
Other legal entities	8.30	7,958	8.34	2,558	8.21
Individuals	10.00	4,926	5.15	7,751	24.87
Total	**100.00**	**95,581**	**100.00**	**31,169**	**100.00**

The ordinary shareholders are entitled to one vote per share.

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

At the balance sheet date the Company held 3,301 of preference shares and 3,022 of ordinary shares (2006: 26,375 of preference shares and 23,062 of ordinary shares).

(in millions of Russian Roubles)

In a case of liquidation, the property remaining after settlement with creditors, payment of preferred dividends and redemption of the par value of preferred shares is distributed among preferred and ordinary shareholders proportionately to the number of owned shares.

Distributable earnings of the parent company are limited to its respective retained earnings, as mandated by the statutory accounting rules. Statutory retained earnings of the Company as at 31 December 2007 and 2006 amounted to RUR 3,266 million and RUR 2,524 million, respectively.

In accordance with the Russian legislation, dividends may only be declared to the shareholders of the Company from net income as shown in the Company's Russian statutory financial statements. The Company reported net income of RUR 874 million and RUR 761 million in its statutory financial statements in 2007 and 2006, respectively.

According to the Order of the Federal Service on the Financial Markets of the Russian Federation No. 03 - 17/PS dated 01 April 2003 the Company was authorized to circulate 40% of its ordinary shares (38,232,568 shares) in the form of ADR outside the Russian Federation. According to the depositary agreement 1 ADR is equal to 30 ordinary shares.

As at the end of 2007 29,124 ADRs represented 873,720 deposited ordinary shares, which constituted 0.91% of total ordinary shares issued.

The following table represents ADR registration for 2005-2007:

	ADR (quantity)	**Ordinary Shares Equivalent (quantity)**	**Ordinary Shares %**	**Charter Capital %**
31 December 2005	**51,603**	**1,548,090**	**1.62%**	**1.22%**
Withdrawal 2006	(26,466)	(793,980)	(0.83%)	(0.63%)
31 December 2006	**25,137**	**754,110**	**0.79%**	**0.59%**
Additions 2007	3,987	119,610	0.12%	0.09%
31 December 2007	**29,124**	**873,720**	**0.91%**	**0.68%**

(in millions of Russian Roubles)

19 Borrowings

As at 31 December 2007 and 2006 borrowings comprised the following:

	Interest rate	Maturity date	2007	2006
Short–term borrowings				
Bank loans (Roubles)	7%	2008	772	-
Bonds (Roubles)			-	-
Promissory notes (Roubles)	8.60%	2008	-	1,950
Accrued interest		2008	31	70
Other short term borrowings (Roubles)	7-8.85%	2007	-	2
Total short–term borrowings			**803**	**2,022**
Long–term borrowings				
Bank loans (Roubles)	8.75- 14%	2008-2012	2,237	55
Bonds (Roubles)	8.6%	2008-2012	3,176	3,486
Bank loans (Roubles)	Mosprime plus 2.3%	2009	110	-
Vendor financing (Roubles)	-	2008	7	27
Vendor financing (US Dollars)	5.4-10%	2008	20	82
Vendor financing (Euro)	8%	2008	-	20
Less: Current portion of long–term borrowings			(846)	(423)
Total long–term borrowings			**4,704**	**3,247**

In 2007, the Company entered into 7 bank loan agreements to receipt of current and non-current assets and financing of current operations with the carrying value of RUR 3,975 million (2006: RUR 452 million). The interest rates of the loans vary from 7.4% to 12.8% per annum. Bank loans are secured by property, plant and equipment with the carrying value of approximately RUR 1,294 million (2006: RUR 134 million).

As at 31 December 2007 and 2006 the Company's borrowings are denominated in the following currencies:

	2007	2006
Russian roubles	6,333	5,590
US Dollars	20	82
Euro	-	20
Total	**6,353**	**5,692**

(in millions of Russian Roubles)

As at 31 December 2007 the short-term and long-term borrowings had the following maturity schedule:

Maturity date	Bank loans	Bonds	Vendor financing	Total
2008	902	720	27	1,649
2009	765	756	-	1,521
2010	668	600	-	1,268
2011	651	700	-	1,351
2012	164	400	-	564
Total	**3,150**	**3,176**	**27**	**6,353**

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

Short-term Borrowings

Loans and borrowings

Short term loans and borrowings as at 31 December 2007 is represented by loans and borrowings received for financing of the current assets. The majority of the loans and borrowings are pledged by the telecommunication equipment.

Sberbank

In June 2007 the Company signed two loan agreements for RUR 770 million with Sberbank to finance the operating activities. The interest rate is 7.4% p.a. These loans are secured by the property, plant and equipment; the carrying value of the pledged property, plant and equipment is RUR 1,046 million.

Promissory notes

In December 2006, the Company entered into 2 promissory note loans with Svyazbank in the total amount RUR 1,950 million. The loan bears interest of 8.6%.

In May 2007 the Company entered into promissory note loans with Russian Industrial Bank for RUR 250 million. Interest rate is 7.5% p.a.

During 2007 the Company fully repaid all promissory notes.

Long-term Borrowings

Loans and borrowings

Sberbank

In January 2007 the Company obtained the credit line for RUR 1,955 million from Sberbank to finance the acquisition of 51% of shares of OJSC Sakhatelecom. The loan should be repaid by 29 January 2012. Interest rate is 8.75% p.a.

The loan is secured by the property, plant and equipment with a carrying value of RUR 130 million and 51% of shares of OJSC Sakhatelecom with a pledge value of RUR 2,295 million. At 31 December 2007 the outstanding balance was RUR 1,955 million.

Svyazbank

In December 2007 the Company signed the revolving loan agreement with Svyazbank with limit of RUR 450 million to finance operating, investing and financing activities. The interest rate is 9.4% p.a. The outstanding balance as at 31 December 2007 is RUR 128 million. This loan is unsecured.

Bank Societe Generale Vostok (BSGV)

In December 2007 the Company signed a loan agreement with BSGV for non-revolving credit line of RUR 500 million to finance operating and financing activities. The credit line was provided for 18 months, the interest rate is Mosprime plus 2.3% variable rate.

Svyaz Bank

In February 2007 ZAO AKOS entered into the loan agreement with SvyazBank for the total amount of RUR 95 million. The loan is repayable until 13 February 2009. The interest rate is 12.75% per annum. The outstanding balance as at 31 December 2007 is RUR 55 million. The loan is unsecured.

Promsvyazbank

In November 2005 ZAO AKOS received a bank loan of RUR 50 million. The interest rates are as follows: until 14 November 2008 is 14% p.a.; after 15 November 2008 – 28% p.a. The outstanding balance as at 31 December 2007 is RUR 27 million. The loan is unsecured.

Dalnevostochny Bank

In October 2006 ZAO AKOS received bank loan of RUR 55 million. The interest rate is 11.25%. The outstanding balance as at 31 December 2007 is RUR 71 million. The loan is secured by the property, plant and equipment with the carrying value of RUR 47 million.

Alfa Bank

In 2007 OJSC SakhaTelecom entered into revolving loan facility agreement with Alfa Bank for RUR 300 million. The interest rate is 9%. The Company does not have any outstanding balance as at 31 December 2007. The loan is secured by the property, plant and equipment with the carrying value of RUR 294 million.

Bonds

In June 2006 the Company registered two interest rate bonds issues consisting of 2,000,000 bonds and 1,500,000 bonds with a nominal value of RUR 1,000 each. Bond issues have 12 and 6 coupon payments, respectively. Payments on the 1st coupon was made on 182nd day after placement (in December 2006), payment on other coupons will be made after each 182 days. Interest rate on coupons was determined as 8.85% and 8.6%, respectively. Bonds are payable in the proportion determined in percentage of nominal value starting from December 2007 (for RUR 1,500,000 thousand bond issue) and starting from December 2009 (for RUR 2,000,000 thousand bond issue). The full repayment of bonds payable should be in July 2009 and May 2012, respectively.

Issued bonds provide the right for the advance repayment for bonds holders on appropriate dates. The nearest date of such offer is 4 June 2008. Therefore the outstanding balance of RUR 750 million was classified as a short-term bonds payable as at 31 December 2007.

In June and December 2007 the Company discharged its interest obligations on the second and third coupons payments in the amount of RUR 304 million. The amounts of each coupon payment were RUR 64 million (for RUR 1,500 million bond issue) and RUR 88 million (for RUR 2,000 million bond issue). The amount of coupone income for each bond issues were as follows: RUR 42.88 (for RUR 1,500 million bond issue) and RUR 44.13 (for RUR 2,000 bond issue). The interest obligation was discharged in time.

In December 2007 the Company partially repaid bonds of RUR 300 million.

At 31 December 2007 the outstanding balance was RUR 3,176 million and interest payable was RUR 28 million.

(in millions of Russian Roubles)

Vendor financing

BETO-Huawei

In 2003-2005, the Company entered into several agreements with BETO-Huawei denominated in US Dollars, under which it delivered telecommunication equipment to the Company. The amount outstanding as at 31 December 2007 was RUR 20 million. Equipment received under these agreements is pledged to the supplier until the final payment is made.

C- Boss

In May 2006 the Company entered into agreement with C-Boss for software delivery, the contract is denominated in Russian Roubles. The outstanding amount as at 31 December 2007 was RUR 7 million.

20 Finance Lease Obligations

The Company has financial lease contracts for telecommunication equipment. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments as at 31 December 2007 and 2006 are as follows:

	2006		2005	
	Minimum lease payments	**Present value of payments**	**Minimum lease payments**	**Present value of payments**
Current portion	386	306	531	372
2 to 5 years	257	225	670	555
Over 5 years	-	-	-	-
Total minimum lease payments	**643**	**531**	**1,201**	**927**
Less amounts representing finance charges	(112)	-	(274)	
Present value of minimum lease payments	**531**	**531**	**927**	**927**
Less current portion of long term financial lease obligations	-	(306)	-	(372)
Long-term financial lease obligations	-	**225**	**-**	**555**

In 2006 and 2005, the Company's primary lessors were OJSC "RTC-Leasing" and LLC "Promsvyazleasing". In 2007, the effective interest rate on lease liabilities ranged from 21% to 34% per annum (2006: 19% to 38% per annum).

OJSC "RTC-Leasing" purchases telecommunication equipment from domestic and foreign suppliers and provides such equipment to the Company under finance lease agreements. The Company's obligations under finance leases to OJSC "RTC-Leasing" as at 31 December 2007 amounted to RUR 530 million (2006: RUR 883 million).

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

21 Accounts Payable and Accrued Expenses

As at 31 December 2007 and 2006, the Company's accounts payable and accrued expenses comprised the following:

	2007	2006
Accounts payable for the suppliers of fixed assets	215	102
Accounts payable for the suppliers of intangible assets	19	-
Accounts payable for the interconnect operators	335	144
Trade accounts payable	200	145
Advances received from subscribers	333	355
Salaries and wages	478	403
Other accounts payable	60	77
Total	**1,640**	**1,226**

(in millions of Russian Roubles)

Other accounts payable include outstanding settlements with insurance providers and payments to NP CIPRT.

22 Other Taxes Payable

Short-term Taxes Payable

As at 31 December 2007 and 2006 taxes payable comprised the following:

	2007	2006
Value-added tax	89	16
Property tax	52	43
Individual income tax	8	13
Unified social tax	31	30
Other taxes	3	4
Total	**183**	**106**

Included in value added tax payable is the amount of RUR 4 million (2006: RUR 16 million), which represents deferred value added tax, that is only payable to the tax authorities when the underlying receivables are recovered or written off.

Long-term Taxes Payable

Long-term taxes payable comprise various taxes payable to the Russian Government which were previously past due and which have been restructured to be repaid over a period of up to 10 years following the application of Government Resolution No. 1002 dated 3 September 1999.

Long-term taxes payable is accounted for at fair value at restructuring date and at amortized cost in subsequent period. Fair value is present value of future cash flows discounted by rate of 12%.

23 Pensions and Other Post-Employment Benefits

In addition to statutory pension benefits the Company also provides for non-government pension using the post-employment benefit plans.

Defined Benefit Pension Plans

The majority of the employees are eligible for defined benefit schemes. The defined benefit pension plans cover most of employees and provide old age retirement pension and disability pension. The plans provide for payment of retirement benefits starting from statutory retirement age, which is currently 55 for women and 60 for men. The amount of payment is calculated using the formulae determined for each regional branch of the Company. According to such formulae the amount of benefit depends on a number of parameters, including an employee's salary at the retirement date and number of years with the Company.

Non-government pension fund Telecom-Soyuz, which is related to the Company (see note 35), maintains the defined benefit pension plan. Non-government pension fund Erel also maintains the defined benefit pension plan for OJSC Sakhatelecom.

According to the plan terms the pensions are defined monetary values for each regional branches of the Company and depend on participants' positions, past service in the Company and wage at retirement. The benefits do not vest until and are subject to the employee retiring from the Company on or after the above-mentioned ages.

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

Additionally the Company provides death-in-pension payments and financial support of a defined benefit nature to its old age and disabled pensioners.

(in millions of Russian Roubles)

There were 15,348 active employees participating to the defined benefit pension plan of the Company and no pensioners eligible to the post-employment and post-retirement benefits, as at 31 December 2007 (as at 31 December 2006 – 13,806 and 0 respectively).

As at 31 December 2007 and 2006 the net liabilities of defined benefit pension and other post-employment benefit plans comprised the following:

	2007	2006
Present value of defined benefit obligation	1,317	699
Fair value of plan assets	(221)	(27)
Present value of unfunded obligations	1,096	672
Unrecognized past service cost	(291)	116
Unrecognized actuarial losses	159	(352)
Net pension liability in the balance sheet	**964**	**436**

As at 31 December 2007 management estimated employees' average remaining working life at 8 years (2006: 8 years).

The amount of net expense for the defined benefit pension and other post-employment benefit plans recognized in 2007 and 2006 is as follows:

	2007	2006
Service cost	75	43
Interest cost	92	66
Expected return on plan assets	(14)	(7)
Net actuarial losses/(gains) recognised in year	(6)	-
Past service cost recognized in current year	(9)	-
Amortization of past service cost – non–guaranteed portion	41	43
Curtailment or final settlement effect	(84)	(33)
Net expense for the defined benefit pension plans	**95**	**112**

The amount of net expense for the defined benefit pension and other post-employment benefit plans is included in the consolidated statement of operations line "Wages, salaries, other benefits and payroll taxes".

The movements in the net liability for defined benefit pension and other post-employment benefit plans in 2007 and 2006 are as follows:

	2007	2006
Net liability at 1 January	436	377
Acquisitions	583	
Net expense for the year	95	112
Contributions	(150)	(53)
Net liability at 31 December	**964**	**436**

Changes in the present value of the defined benefit obligation are as follows:

	2007	2006
Present value of defined benefit obligation at 1 January	699	999
Acquisitions	739	
Service cost	75	42
Interest cost	92	66
Actuarial (gain)/losses	(517)	(186)
Past service cost/(asset)	439	(16)
Benefits paid	(87)	(13)
Settlement and curtailment (gain)/loss	(123)	(193)
Present value of defined benefit obligations at 31 December	**1,317**	**699**

(in millions of Russian Roubles)

Movements in the net assets of defined benefit pension and other post-employment benefit plans during 2007 and 2006 are characterized by the following factors:

	2007	2006
Fair value of plan assets at 1 January	27	173
Acquisitions	156	-
Actual return on plan assets	14	7
Employer contributions	150	53
Benefits paid	(87)	(13)
Curtailment or final settlement effect	(39)	(193)
Fair value of plan assets at 31 December	**221**	**27**

As at 31 December 2007 the pension plan assets did not include the Company's financial instruments.

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

	2007	2006
Equities of Svyazinvest Group companies	-	1.57%
Other Russian equities	14.42%	7.59%
Russian municipal bonds	27.66%	30.81%
Bank deposits	5.82%	0.73%
Russian corporate bonds	47.62%	34.18%
Russian corporate promissory notes	3.44%	24.86%
Other assets	1.04%	0.26%

As at 31 December 2007 and 2006 the principle actuarial assumptions of defined benefit pension and other post-employment benefit plans were as follows:

	2007	2006
Discount rate	6.50%	6.50%
Expected return on plan assets	7.47%	7.29%
Future salary increases	9.20%	9.20%
Rate used for calculation of annuity value	6.00%	6.00%
Increase in financial support benefits	5.00%	0.00%
Staff turnover	7.00%	7.00%
Mortality tables (source of information)	USSR 1985/86	USSR 1985/86

Historical information:

	2007	2006	2005	2004	2003
Defined benefit obligation	1,317	699	999	696	606
Plan assets	(221)	(27)	(173)	(160)	(102)
(Deficit)/surplus	1,096	672	826	536	504
Experience adjustments on plan liabilities	60	255	57	(9)	(26)
Experience adjustments on plan assets	(7)	1	6	2	3

(in millions of Russian Roubles)

24 Provisions

	Personnel dismissal	Provisions for legal claims	Tax provisions	Total
Balance at 31 December 2005	**-**	**-**	**-**	**-**
Accrued	72	1	812	**885**
Provision amortized	-	-	-	**-**
Unused amounts reversed	-	-	-	**-**
Balance at 31 December 2006	**72**	**1**	**812**	**885**
Accrued	46	412	-	**458**
Provision amortized	-	-	-	**-**
Used during the year	72	1	(633)	**(706)**
Unused amounts reversed	-	-	(179)	**(179)**
Balance at 31 December 2007	**46**	**412**	**-**	**458**
Non-current	-	-	-	**-**
Current	46	412	-	**458**
	46	**412**	**-**	**458**

Personnel Dismissal Plans

In December 2007 the Company made a provision for termination payments to the employees who as of 31 December 2007 had been notified of their forthcoming termination (in accordance with the procedure set forth in article 180 of the Russian Labour Code). The provision amounted RUR 46 million as at 31 December 2007 (2006: RUR 72 million).

Provision for Legal Claims

The provision for legal claims recognized in the balance sheet represents the total amount of provision with respect to appropriate actions at law instigated against the Company. Management believes that the amount of the provision as at 31 December 2007 will be fully utilized in the second half of 2008. Management estimates that amount of final payment will not exceed the amount of the provision as at 31 December 2007.

The Company established the provision for the following major cases:

- claims from ZAO Primtelefon and OAO Novaya Telephonnaya Kompaniya for the application of the consequences of invalid transactions (interconnection agreements) for the network capacity increase; the total amount of claims is RUR 356 million. The management assesses the risk as probable;
- claim from OAO Novaya Telephonnaya Kompaniya for data transmission services for 2006 and January – June 2007 for the total amount of RUR 24 million. In January 2008 the Company concluded the amicable agreement. According to the latter the Company will pay the full amount of the claim during the first half of 2008;
- claims from OJSC Sakhatelecom's employees for overnight compensations of RUR 29 million. The management assesses the risk as probable.

Tax Provisions

The Company filed a court claim to the Moscow Arbitrary Court for the Decision of the Intraregional Tax Inspectorate for Major Taxpayers No. 7 (ITIMT) on the results of 2003 – 2005 audit, the total amount of the additional taxes, fines and penalties is RUR 200 million. On 26 October 2007 the Moscow Arbitrary Court made a decision to nullify the Decision of ITIMT. As of the date of the approval of these consolidated financial statements the Company is not aware of any actions of ITIMT representatives. As of 31 December 2006 the Company accrued RUR 179 million as a tax provision.

The Company made a compliant on the decision of ITIMT for the results of 2001 – 2002 audit, the total amount of the additional taxes, fines and penalties is RUR 633 million, this amount was included into the tax provisions as of 31 December 2006. The Company fully repaid the claim in 2007.

(in millions of Russian Roubles)

On 19 February 2008 the Presidium of the Supreme Arbitrary Court recognised the additional taxes, fines and penalties related to the interconnection settlements with OJSC Rostelecom as partially unjustified. The amount of additional taxes, penalties and fines related to this case and fully paid by the Company to the budget is RUR 74 million. This amount was included into accounts receivable balance as at 31 December 2007.

25 Revenues

By revenue types	**2007**	**2006 (as restated)**
Local telephone calls	5,712	4,025
Revenues from interconnected operators	2,066	1,780
Long distance and intrazonal telephone services	2,544	1,715
New services (Internet, ISDN, ADSL, IP-telephony)	2,395	1,443
Cellular services	1,186	1,003
Installation and connection fees	385	356
Radio and TV broadcasting	245	229
Other telecommunications services	92	19
Other revenues	376	329
Total	**15,001**	**10,899**

In line "Other revenues" the Company included the rent income in the amount of RUR 293 million (2006: RUR 147 million).

The Company identifies revenue by the following major customer groups:

Customer groups	**2007**	**2006**
Individuals	8,056	5,855
Commercial organizations	5,533	4,083
Budget organizations	1,412	961
Total	**15,001**	**10,899**

(in millions of Russian Roubles)

In 2007 part of company's revenue from service rendering and goods sold was received on contract with non-cash discharge of obligations:

	2007	2006
Total number of counterparties with non-cash payments	97	494
OJSC "Rostelecom"	-	1,496
LLC "Vostoktelecom TC"	-	69
OJSC "Mejregionalniy tranzit telecom"	24	57
FGUP Pochta Rossii	17	-
OJSC "Novaya telefonnaya kompaniya"	-	34
LLC "Dalsvyaz-Kurier"	-	24
CJSC "Rostelegraph"	-	22
LLC "Ekvant"	-	8
JSCB Sberbank	2	-
LLC Edelveis Trans-Telecom	1	-
Others	3	109
Total	**47**	**1,819**

26 Other Operating Income

	2007	2006
Reimbursement of losses from universal telecommunication services	129	-
Reimbursement of losses	29	6
Income as a result of stockcounts	13	3
Written off accounts payable	8	5
Fines, late payment interest, penalty for breach of contract	2	4
Other income	105	58
Total	**286**	**76**

27 Other Operating Expenses

	2007	2006 (as restated)
Accrual of provisions for contingent liabilities	371	811
Other services related to the administration	237	124
Agency fee	206	108
Fire and other security services	194	183
Lease of premises	194	171
Audit and consulting fees	186	135
Advertising expenses	144	125
Universal service fund payments	137	72
Tax fines and penalties	118	2
Non-commercial partnership expenses	112	69
Business travel expenses and representation costs	72	50
Additional tax payments	67	-
Transportation services	48	20
Banks service fees	45	25
Member fees, charity contribution, payments to labor unions	41	29
Insurance	37	50
Expenses on the fixed assets transfer	14	7
Education expenses	11	12
Losses from fixed and other assets write off	11	2
Postal services	10	8
Other expenses	152	79
Total	**2,407**	**2,082**

(in millions of Russian Roubles)

28 Interest Expense, Net

	2007	2006
Interest income	(76)	(97)
Interest expense	465	400
Interest expense accrued on finance leases	161	239
Total	**550**	**542**

29 Other gains/(losses) From Financial Investments, net

	2007	2006
Loss from the impairment of investments	(11)	(47)
Gain / (loss) from the sale of investments	32	(1)
The excess of the net assets purchased over the cost of investment	20	-
The increase of the fair value of the investments	1	-
Dividend income	2	1
Total	**44**	**(47)**

30 Income Tax

Income tax charge for the years ended 31 December 2007 and 2006 comprised the following:

	2007	2006
Current income tax expense	773	461
Deferred tax expense	(119)	(58)
Total income tax for the year	**654**	**403**

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

	2007	2006
Profit before income tax and minority interest	2,014	518
Statutory income tax rate	24%	24%
Theoretical tax charge at statutory income tax rate	483	124
Increase resulting from the effect of:		
Non-taxable income	(71)	(16)
Non-deductible expenses	242	295
Total income tax of effective tax rate 32.47% (2006 – 77.8%)	**654**	**403**

Deferred income tax assets and liabilities as at 31 December 2006 and 2005, and their movements in 2006 were as follows:

	31 December 2005, as restated	**Origination and reversal of temporary differences**	**Sale of subsidiaries**	**31 December 2006, as restated**	**Origination and reversal of temporary differences**	**Subsidiaries acquisition**	**31 December 2007**
Property, plant and equipment	(458)	46	(1)	(413)	(64)	(276)	(753)
Intangible assets	(54)	(18)	-	(72)	(10)	(170)	(252)
Financial investments	(3)	-	-	(3)	(2)	(7)	(12)
Inventories	-	2	-	2	1	-	3
Trade and other accounts receivable	14	(9)	-	5	(5)	-	-
Loans and borrowings	(2)	7	-	5	(5)	-	-
Finance lease liabilities	(142)	44	-	(98)	94	-	(4)
Pension liabilities	73	3	-	76	14	-	90
Deferred income	20	(1)	-	19	(3)		16
Accounts payable and accrued expenses	31	26	-	57	(29)	-	28
Provisions	79	(42)	-	37	128	(22)	143
Total deferred income tax liability, net	**(442)**	**58**	**(1)**	**(385)**	**119**	**(475)**	**(741)**

A temporary difference relating to investments in subsidiaries of RUR 732 million has not been recognised as the Group is able to control the timing of reversal of the difference, and reversal is not expected in the foreseeable future.

31 Earnings per Share

The Company has not financial instruments which may be converted into ordinary shares, therefore, the diluted earnings per share equal to basic earning per share.

Earnings per share is calculated by dividing the profit attributable to ordinary and to preference shareholders (see note 18) by the weighted average number of ordinary and preference shares outstanding respectively during the year. The Company has no dilutive potential ordinary shares.

The following is a reconciliation of the profit attributable to ordinary and preference shareholders:

	2007	**2006**
Net profit for the year attributable to the shareholders of the Company	1,272	105
Less: attributable to preference shareholders	(313)	(26)
Attributable to ordinary shareholders	959	79

The following is a reconciliation of the weighted average number of ordinary shares:

In thousands of shares	**2007**	**2006**
Issued shares at 1 January	95,581	95,581
Effect of own shares held	(13)	(12)
Weighted average number of shares for the year ended 31 December	95,568	95,569

(in millions of Russian Roubles)

32 Dividends Declared and Proposed for Distribution

Dividends Declared and Approved Subsequent in 2007

Dividends declared to shareholders are determined by the Board of Directors and will be officially recommended at the annual shareholders' meeting:

Dividends on ordinary share – RUR 0.91 per share	88
Dividends on preferred share – RUR 2.76 per share	86
Total	**174**

The number of shares using for calculation the dividends amount is equal to the number of shares on issue at the reporting date.

Dividends paid to shareholders are determined by the Board of Directors and officially approved at the annual shareholders' meeting. In accordance with Russian legislation, earnings available for dividends are limited to the Company's profits based on financial statements prepared in accordance with Russian accounting and reporting regulations. In 2007 and 2006 the Company's net profit in accordance with Russian accounting totalled to RUR 874 million and RUR 761 million, respectively.

33 Contingencies and Operating Risks

Operating Environment of the Company

The Russian Federation has been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in this environment. Consequently, operations in the Russian Federation involve risks that typically do not exist in other markets. The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

Taxation

The taxation system in the Russian Federation is relatively new and is characterized by frequent changes in legislation, official pronouncement in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

As at 31 December 2007 the management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Company's tax, currency and customs positions will be sustained.

On 28 January 2008 OJSC Sakhatelecom received the decision of the Interregional Tax Inspectorate for Major Taxpayers No. 7 (ITIMT No. 7) of the Federal Tax Service of the Russian Federation on the results of the tax audit for 2004 – 2006. Total amount of additional taxes, fines and penalties is RUR 140 million, including fines and penalties of RUR 40 million. The additional amounts relate to the settlement with operators on interconnection, network cooperation and data transmission. The Company does not agree with the result of the tax audit and made a compliant to the Federal Tax Service of the Russian Federation. As of the date of the signing of this consolidated financial statement company's compliant was not reviewed. In May 2008 the Company claimed the suit against ITIMT No. 7 to the Moscow Arbitrary Court.

Insurance

The Insurance Business in Russia is on the development stage and many insurance services are not distributed in the Russian Federation yet, which available in other countries. During 2007 the Company did not maintain insurance coverage on a significant part of its property, plant and equipment, business interruption losses, or third party liability in respect of property or environmental damage arising from accidents relating to the Company's property or the Company's operations. Until the Company obtains adequate insurance coverage, there is a risk that losses resulting from destruction of certain assets could have a material adverse effect on the Company's operations and financial position.

Legal Proceedings

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

Licenses

Substantially all of the Company's revenues are derived from operations conducted pursuant to licenses granted by the Russian Government. These licenses expire in various years ranging from 2008 to 2012. The Company has renewed these licenses on a regular basis in the past, and believes that it will be able to renew the licenses without additional cost in the normal course of business. Suspension or termination of the Company's main licenses or any failure to renew any or all of these main licenses could have a material adverse effect on the financial position and operations of the Company.

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

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

The management believes there are no reasons licenses would not be prolonged or some of them would be suspended or cancelled.

Guarantees Issued

The Company has provided financial guarantees for third parties for the total amount of RUR 529 million (2006: RUR 900 million). Management believes that the Company did not have any contractual commitments to extend financial guarantees, credit or other assistance.

34 Commitments

As at 31 December 2007 the Company has commitments for capital investments into the modernization and expansion of its network in the amount of RUR 590 million (2006: RUR 619 million).

As at 31 December 2007 the Company has commitments for purchasing of new fixed assets in the amount of RUR 49 million.

As at 31 December 2007 the Company has commitments for purchasing of new intangible assets in the amount of RUR 33 million.

(in millions of Russian Roubles)

35 Balances and Transactions with Related Parties

The nature of the significant Company's related party transactions in 2007 and 2006 is presented below:

	OJSC "Svyazinvest"	Subsidiaries of OJSC "Svyazinvest"	Associates	State-controlled companies	Other
2006					
Provision of telecommunication services, interconnection and traffic transmission services	-	1,416	23	2,484	23
Other income	-	1	1	154	2
Purchase of telecommunication services, interconnection and traffic transmission services	-	120	4	-	257
Purchase of other services	-	-	-	847	101
Interest income	-	-	-	-	72
Interest expenses	-	-	-	-	27
Dividends payable	43	-	-	-	-
2007					
Provision of telecommunication services, interconnection and traffic transmission services	-	1,289	-	883	4
Rendering of assistance and agency services	-	-	-	88	-
Rent income	-	-	-	3	-
Other income	-	2	1	32	-
Purchase of telecommunication services, interconnection and traffic transmission services	-	240	3	89	8
Purchase of other services	-	2	-	445	327
Interest expense	-	-	-	7	-
Dividend payable	39	-	1	-	-

The nature of the significant Company's related party transactions balances outstanding as of 31 December 2007 and 2006 is detailed below:

	OJSC "Svyazinvest"	Subsidiaries of OJSC "Svyazinvest"	Associates	State-controlled companies	Other
At December 31, 2006					
Trade and other receivables	-	198	21	220	137
Accounts payable	-	8	6	147	23
At December 31, 2007					
Trade and other receivables	-	125	2	65	10
Accounts payable	-	157	6	71	23
Guaranties issued	-	-	-	5	-

(in millions of Russian Roubles)

Other related parties comprise the following categories: key management personnel; parties exercising significant influence over the Company; non-state pension funds; other parties recognised as related parties but not included in separate categories.

Outstanding balances as of the year-end are unsecured, interest free and the settlements occur in cash (or mutual offset of the balances with the same customer or supplier). There have been no guarantees provided or received with regard to any related party receivables or payables. For the year ended 31 December 2007 the Company has not recorded impairment of related parties' receivables. This assessment is undertaken each reporting year through examining the financial position of the related party and the market in which the related party operates.

OJSC SvyazInvest

The parent entity of the Company is OJSC SvyazInvest, a wholly owned by the Russian Government until July 1997 when the Russian Government sold 25% plus one share to the private investors.

Effectively operating telecommunication and data transmission networks are essential for Russia due to various reasons including economic, strategic and national security considerations. Consequently, the Government has and may be expected to continue to exercise significant influence over the operations of OJSC Svyazinvest and its subsidiaries.

The Russian Federation Ministry of Communications and Information Technologies has control over the licensing of providers of telecommunication services.

OJSC Rostelecom

OJSC Rostelecom, a majority-owned subsidiary of Svyazinvest, is the primary provider of domestic long-distance and international telecommunication services in the Russian Federation.

The annual revenue from OJSC Rostelecom relates to traffic transmission services provided by the Company to OJSC Rostelecom under the interconnection agreement and to the fees received under the assistance agreement which is a combination of agent agreement and service agreement.

The annual expense associated with OJSC Rostelecom relates to payments for call termination to the networks of other telecommunication operators, if the call is initiated from a mobile radiotelephony network, as well as interconnection expenses and expenses related to long-distance domestic and international telecommunication services provided to the Company.

The respective amounts included in the consolidated financial statements as of 31 December 2007 and 2006 and for the years then ended were as follows:

	2007	2006
Expenses on OJSC "Rostelecom" services	162	120
Revenues from services provided for OJSC "Rostelecom"	1,051	1,416
Revenues under assistance agreements with OJSC "Rostelecom"	2	-
Accounts payable to OJSC "Rostelecom" as of December 31	8	147
Accounts receivable from OJSC "Rostelecom" as of December 31	198	101

Transactions with State-controlled Companies

State-controlled organisations are a significant element in the Company's customer base, purchasing services both directly through numerous authorities and indirectly through their affiliates.

Certain entities financed by the Government are users of the Company's network. These entities typically lease communication channels at lower rates that those fixed by the Federal Service on Tariffs for other customers. In addition the Government may by law require the Company to provide certain services to the Government in the interest of national security and the detection of crime.

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

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

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

Non-Commercial Partnership Centre for Research of Problems in Development of Telecommunications (hereinafter the Partnership) is an entity controlled by OJSC Svyazinvest through its subsidiaries.

The Company has an agreement with the Partnership, under which it provides financing for the latter to implement mutually beneficial project on behalf of the Company and other subsidiaries and associates of OJSC Svyazinvest. Contributions to the Partnership included in the line "Other operating expenses" in the accompanying consolidated income statement for 2007 amounted to RUR 112 million (2006: RUR 69 million).

In addition, the Partnership acted as agent for the Company with respect to Oracle E-Business Suite development and implementation services. In 2007 the Company's expenses related to the reimbursement of the Partnership for the costs it incurred under the agreements with contractors totalled RUR 91 million (2006: RUR 27 million).

The Company had outstanding liability to the Partnership as of 31 December 2007 in the amount of RUR 20 million (31 December 2006: RUR 20 million and the account receivable in the amount of RUR 106 million).

OJSC Svyazintek

OJSC Svyazintek was established by OJSC Svyazinvest subsidiaries which own among them 100% of its share capital. OJSC Svyazintek provides to the Company services related to implementation and post-implementation support of information systems, in particular, Oracle E-Business Suite and Amdocs Billing Suite softwares.

In 2007 the Company incurred expenses on services provided by OJSC Svyazintek in the amount of 104 (2006: 102). This amount is included in the deferred expenses related to the software.

Non-government Pension Fund Telecom Soyuz

The Company signed a pension insurance agreement with Non-government pension fund Telecom-Soyuz (note 23).

Compensation to Key Management Personnel

Key management personnel comprise members of Management Board and Board of Directors of the Company, totalling 19 as of 31 December 2007 and 19 as of 31 December 2006.

Compensation to members of Management Board and Board of Directors for 2007 consists of contractual salary, performance bonus depending on operating results and other compensations and totals RUR 64 million (2006: RUR 53 million).

36 Financial Instruments

The Company's principal financial instruments comprise bank loans, bonds and promissory notes, finance leases and cash and cash equivalents. The main purpose of these instruments is to raise finance for the Company's operations. Short term deposits are also actively used as a financial instrument to place available funds. The Company has other financial assets and liabilities such as trade receivable and trade payables, which arise directly from its operations.

The main risks arising from the Company's financial instruments are foreign exchange risk, interest rate risk, credit risk and liquidity risk.

(in millions of Russian Roubles)

Capital Management Policy

The Company's capital management policy is primarily focused on increasing credit ratings, improving financial independence and liquidity ratios, improving the structure of payables, and reducing the cost of capital.

The main methods of capital management are profit maximisation, investment program management, sale of assets to reduce debt burden, debt capital management, debt portfolio restructuring, use of different classes of borrowed funds.

The Company's policy is to maintain certain ratios within acceptable limits, including the financial independence ratio, the net debt/shareholders' equity ratio, and the net debt/EBITDA ratio.

Current year international rating agency Fitch upgraded long term credit risk of the Company from "B" to "B+" and affirmed short term credit risk at "B", the outlook is "Stable". Standard and Poor's upgraded the Corporate Governance Score based on national scale from CGS 5.3 to CGS 5.4.

Capital management is conducted at the level of separate significant legal entities of the Company. The ratios of financial independence, net debt/shareholders' equity and net debt/EBITDA are calculated using the statutory accounting data. The financial independence ration is calculated as shareholders' equity to the balance sheet total at the end of the period. Net debt/shareholders' equity is calculated as net debt to shareholders' equity at the end of the period. Net debt/EBITDA is calculated as net debt at the year end to EBITDA for the previous period.

The Company's capital management policy was not changed in 2007 compared to 2006.

Foreign Exchange Risk

Foreign exchange risk is the risk that fluctuations in exchange rates will adversely affect the Company's cash flows. Liabilities denominated in foreign currencies (notes 19 and 21) give rise to foreign exchange exposure.

The Company is generally exposed to foreign exchange risk with respect to liabilities denominated in foreign currencies. As of 31 December 2007 the Company had currency-denominated liabilities of RUR 20 million (2006: RUR 102 million), including liabilities denominated in US Dollars of RUR 20 million (2006: RUR 82 million) and EURO – denominated liabilities of Nil (2006: RUR 20 million).

Over the period from 1 January 2007 through 31 December 2007 the Rouble increased by approximately 7.27% in relation to the US Dollar which resulted in a decrease in the Rouble equivalent of the borrowings of approximate 3.

The sensitivity analysis of profit and equity to the foreign exchange risk is shown in the table below:

	USD		**EUR**	
	Changes in exchange rate, %	**Effect on income before income tax**	**Changes in exchange rate, %**	**Effect on income before income tax**
2007	+10	(2)	+5	-
	-10	2	-5	-
2006	+10	(8)	+5	(1)
	-10	8	-5	1

The Company uses forward contracts as a tool to manage foreign exchange risks.

Hedging

In the year 2007 and 2006 the Company did not hedge its foreign exchange risks or interest rate change risks.

Liquidity Risk

The Company monitors its risk of a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial investments and financial assets (e.g. accounts receivables, other financial assets) and projected cash flows from operations. The Company's objective is to maintain a balance between continuity of funding and flexibility through the use of bank overdrafts, bank loans, bonds, finance leases.

(in millions of Russian Roubles)

As of 31 December 2007 long-term borrowings and other liabilities had the following maturities:

Maturity date	Trade and other accounts payable	Loans and borrowings	Bonds	Vendor financing	Total
within 2008	1,640	1,168	1,030	27	3,865
within 2009	-	961	927	-	1,888
within 2010	-	798	750	-	1,548
within 2011	-	723	797	-	1,520
after 2001	-	177	435	-	612
Total	**1,640**	**3,827**	**3,939**	**27**	**9,433**

Distribution of borrowing by maturity is based on contractual undiscounted cash flows. These flows include the repayment of principal amount as well as interest payments and other additional payments to be made during respective period. In case when the interest rate included floating part the rate, this part for projection was set as equal to the interest rate as at 31 December 2007.

Interest Rate Risk

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

The following table presents the Company's financial instruments that are exposed to interest rate risk as of 31 December 2007 and 2006:

	< 1 year	1 - 5 years	> 5 years	Total
As of 31 December 2007				
Fixed rate				
Financial investments	770	-	-	770
Short-term loans and borrowings	803	-	-	803
Long-term loans and borrowings	846	4,704	-	5,550
Finance lease liabilities	306	225	-	531
Floating rate				
Long term loans and borrowings	-	110	-	110

	< 1 year	1 - 5 years	> 5 years	Total
As of 31 December 2006				
Fixed rate				
Short-term loans and borrowings	2,022	-	-	2,022
Long-term loans and borrowings	423	3,247	-	3,670
Finance lease liabilities	372	555	-	927

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

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Company's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgement to decide whether it believes that a fixed or variable rate would be more favourable to the Company over the expected period until maturity.

Prior to 2007 the Company primarily borrowed at fixed rate. In December 2007 the Company received a new variable rate facility.

(in millions of Russian Roubles)

Credit Risk

Credit risk is the risk that counter-party will fail to discharge an obligation and cause the Company to incur a financial loss. Financial assets, which potentially expose the Company to credit risk, consist primarily of trade receivables. The carrying amount of accounts receivable, net of provision for impairment of receivables, represents the maximum amount exposed to credit risk.

The Company has no significant concentrations of credit risk due to the significance of the customer base and regular monitoring procedures over customers' and other debtors' ability to pay debts. Part of accounts receivable is represented by state and other non-commercial organizations. Recovery of this debt is influenced by political and economic factors. Management believes that as 31 December 2007 there is no significant risk of loss to the Company beyond the provision already recorded.

The Company places spare cash on deposits with a number of Russian commercial financial institutions and in short-term promissory notes issued by Russian commercial bank. To manage credit risk the Company places spare cash in different financial institutions, and the Company's management analyses the risk of default of these financial institutions on a regular basis.

The analysis of trade and other receivables aged but not impaired is provided below:

As of 31 December 2007	Post due (days)						
	Total	<30	31-90	61-90	91-180	181-360	>361
Corporate customers	70	-	53	17	-	-	-
Residential customers	35	4	25	6	-	-	-
Governmental customers	12	-	10	2	-	-	-
Interconnected operators	14	-	12	2	-	-	-
Tariff compensation from the State budget	-	-	-	-	-	-	-
Other receivables	84	70	9	5	-	-	-
Total	**215**	**74**	**109**	**32**	**-**	**-**	**-**

As of 31 December 2006	Post due (days)						
	Total	<30	31-90	61-90	91-180	181-360	>361
Corporate customers	55	-	34	21	-	-	-
Residential customers	7	-	7	-	-	-	-
Governmental customers	14	-	9	5	-	-	-
Interconnected operators	56	-	27	29	-	-	-
Tariff compensation from the State budget	45	-	-	-	-	-	45
Other receivables	18	-	12	6	-	-	-
Total	**195**	**-**	**89**	**61**	**-**	**-**	**45**

Fair Value of Financial Instruments

The Company estimates the fair value of its financial assets and liabilities to not be materially different from their carrying amounts except in the following instances:

	2007		**2006**	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Long term bonds	2,426	2,466	3,486	3,507
Short term bonds	750	755	-	-

The fair values for disclosure purposes were determined based on the quoted market prices of respective bonds at each balance sheet date.

37 Subsequent Events

Dividends

Annual dividend per share was approved at the Company's General Shareholders' Meeting on 11 June 2008. The General Shareholders' Meeting approved dividend for 2007 of 0.92 Roubles per ordinary share and 2.76 Roubles per preference share, which amounted to 173. Following the approval annual dividend payable to shareholders will be recognized in the 2008 financial statements (see also note 32).

Tariff Regulations

Pursuant the Order No. 365 – s/10 of the Federal Service on Tariffs dated 23 November 2007 the changes in tariffs for local telephony services effective 1 February 2008 were introduced in the Far East region.

Local Telephony Calls

Individual subscribers:

- The maximum tariffs for local telephony services per minute are rounded off to even numbers under time-based billing scheme;
- Since 1 February 2008 the maximum tariffs for local telephony connections under fixed payment scheme are reduced by 25.7% from 267.23 Roubles to 198.43 Roubles.

Corporate subscribers:

- The basic volume of local calls under the combined payments scheme has been established at the same level as the basic volume of local calls for individual subscribers under the combined payments scheme;
- The maximum tariffs for local telephony services per minute are rounded off to even numbers under time-based billing scheme.

Interconnection and Traffic Transmission Services

Pursuant to the Russian Government Decree No. 627 dated 19 October 2005, the compensation markup on local and intrazone initiation services was canceled starting 1 January 2008.

The Decree No. 666 of the Russian Government, dated 12 October 2007 "Concerning amendments to certain acts of the Russian Government related to telecommunication issues", since 1 March 2008 services related to maintenance of communication facilities representing interconnection points have been excluded from the scope of interconnection services. Given that, in 2008 the Company anticipates a decrease in revenue from interconnection services provided to telecom operators to the extent related to interconnection point maintenance and a decrease in expenses related to the same services provided to the Company by other operators.

Russian Government Decree No. 776 dated 14 November 2007 "Concerning amendments to the Russian Government Decree No. 627 dated 19 October 2005" establishes that since 1 March 2008 an operator is entitled to determine a threshold for traffic transmission services (not to exceed 1,000 minutes/month per interconnection point supporting one connection at a time) subject to guaranteed payment by the buyer of traffic transmission services, if the amount of services provided in the billing period is below the established threshold.

Acquisition of interest in ZAO Systemy Gibridnoi Pechati

In February 2008 the Company's Board of Directors agreed to purchase 1,326,000 ordinary shares in ZAO Systemy Gibridnoi Pechati for 133.

The shares will be purchased to establish efficient printing and delivery of bills, receipts, and subscriber notification forms.

Acquisition of interest in OOO Interdaltelecom

In January 2008 the Company acquired additional 3% in OOO Interdaltelecom for 1 and increased its participation from 97% to 100%.

Acquisition of interest in OOO Set Stolica

In May 2008 the Company entered into transaction on acquisition of 100% interest in OOO Set Stolica, the operator in Yakutsk serving 3,000 subscribers. The Company expects to complete this transaction in October 2008. The Federal Antimonopoly Service gave proper authorization for the deal.

Merger of ZAO AKOS and OOO Integrator.RU

According to the decision of the Company's Board of Directors made in November 2007 and the decision of the shareholders' meeting of ZAO AKOS made in January 2008 OOO Integrator.RU was merged with ZAO AKOS. On 4 March 2008 appropriate record was made in the State Registrar of the legal entities.

Liquidation of OAO A-Svyaz and ZAO SakhalinUgolTelecom

On 15 April 2008 the liquidation of ZAO SakhalinUgolTelecom was completed in accordance with the Company's Board of Directors decision made in June 2007.

On 23 April 2008 the liquidation of OAO A-Svyaz was completed in accordance with shareholders' meeting decision made in September 2007.

Legal proceedings with the Tax authorities

On 19 February 2008 the Presidium of the Supreme Arbitrary Court recognised the additional taxes, fines and penalties related to the interconnection settlements with OJSC Rostelecom during 2001 - 2002 as unjustified. The amount of additional taxes, penalties and fines related to this case and fully paid by the Company to the budget is RUR 74 million. The claims of the tax inspectorate were based on the fact that the method on revenue distribution between the Company and OAO Rostelecom did not cover the related expenses incurred by the Company. Hence the Company rendered services to OAO Rostelecom free-of-charge. However the Presidium of the Supreme Arbitrary Court made a decision that such settlements were in accordance with the legislation effective at that time.

Dividends of OJSC Sakhatelecom

At the annual shareholders meeting held on 4 June 2008 the shareholders of OJSC Sakhatelecom made a decision to distribute RUR 55 million as dividends for 2007.

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