Open joint-stock company «Dalsvyaz»

Consolidated Financial Statements as of December 31, 2002

with Independent Auditors' Report

Open joint-stock company «Dalsvyaz»

Contents

Dalsvyaz

INDEPENDENT AUDITORS' REPORT

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To the Shareholders and Board of Directors of OAO «Dalsvyaz»

1. We have audited the accompanying consolidated balance sheet of OAO «Dalsvyaz» (a Russian open joint-stock company - hereinafter «the Company»), as of December 31, 2002, and the related statements of operations, cash flows and shareholders' equity for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

2. Except as discussed in paragraph 5, we conducted our audit in accordance with International Standards on Auditing issued by the International Federation of Accountants. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

3. The Company has not presented comparative amounts for the year ended December 31, 2001 as required by International Accounting Standard («IAS») 1, «Presentation of Financial Statements».

4. As described in note 21 «Pension Plans and Employee Benefits», the Company has not determined and presented its obligations existing under defined benefits plans in accordance with IAS 19, «Employee Benefits». We were not able to quantify the adjustments, if any, to the financial statements.

5. As described in note 8 «Property, Plant and Equipment», the Company's accounting records relating to fixed assets are not designed to support their presentation in accordance with IAS 16, «Property, Plant and Equipment», IAS 29, «Financial Reporting in Hyperinflationary Economies» and IAS 36, «Impairment of Assets». As such, certain estimates were made by management to present fixed assets in the accompanying financial statements. Owing to the nature of the Company's records, we were unable to satisfy ourselves as to the adjustments, if any, which might have been determined to be necessary had additional evidence been available to better analyze the assumptions and estimates made by management.

6. As a result of the matters described in paragraphs 4 and 5 above, adjustments, if any, could materially affect (i) property, plant and equipment, equipment contributions, assets and liabilities under defined benefits plans, deferred income tax liability, and retained earnings as of December 31, 2002, (ii) depreciation expense, other benefits expense, income tax expense and net income for the year ended December 31, 2002, and (iii) related disclosures.

7. In our opinion, except for the effects on the financial statements of such adjustments, if any, from the matters referred to in paragraphs 3, 4 and 5 above, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of OAO «Dalsvyaz» as of December 31, 2002, and the results of its operations and its cash flows for the year then ended in conformity with International Financial Reporting Standards.

8. As described in note 1 «Corporate Information», the Company was the subject of a reorganization that was approved by the shareholders on December 21, 2001. The Company has accounted for the merger based on the principles of uniting of interests as described in IAS 22 «Business Combinations». In applying this method, the Company has reflected amounts in the financial statements as if the entities had been combined from January 1, 2002, the earliest period presented.

August 11, 2003

Consolidated Balance Sheet as of December 31, 2002

(In thousands of rubles in terms of purchasing power of the ruble at December 31, 2002)

	Notes	2002
ASSETS		
Non-current assets		
Property, plant and equipment, net	8	7,369,264
Intangible assets, net	9	13,164
Investments in associates	11	129,018
Advances to suppliers of equipment		45,464
Available-for-sale financial assets	12	10,292
Total non-current assets		7,567,202
Current assets		
Inventories, net	13	240,001
Trade accounts receivable, net	14	317,770
Other current assets, net	15	349,653
Cash and cash equivalents	16	99,585
Total current assets		1,007,009
Total assets		8,574,211

SHAREHOLDERS' EQUITY AND LIABILITIES		
Shareholders' equity		
Preference shares	17	311,689
Ordinary shares	17	955,814
Inflation impact on share capital		1,830,700
Retained earnings and other reserves		2,872,421
Total shareholders' equity		5,970,624
Commitments and contingencies	**22**	**-**
Minority interest		**-**
Non-current liabilities		
Long-term borrowings	18	110,642
Equipment contributions		111,580
Obligations under finance leases	19	106,631
Deferred income tax liability	5	728,466
Other long-term liabilities		22,713
Total non-current liabilities		1,080,032
Current liabilities		
Accounts payable and accrued expenses	20	714,960
Amount owing to Rostelecom for interconnection fees		59,657
Taxes and social security payable	20	288,146
Dividends payable		10,993
Short-term borrowings	18	150,433
Short-term portion of long-term borrowings	18	227,649
Short-term portion of obligations under finance leases	19	71,717
Total current liabilities		1,523,555
Total liabilities and shareholders' equity		**8,574,211**

The accompanying notes form an integral part of these financial statements

Consolidated Statement of Operations for the year ended December 31, 2002

(In thousands of rubles in terms of purchasing power of the ruble at December 31, 2002)

	Notes	2002
Revenues	4	5,665,594
OPERATING EXPENSES		
Wages, salaries, other benefits and payroll taxes		(2,386,497)
Depreciation and amortization	8	(651,319)
Materials, repairs, maintenance and utilities		(702,820)
Taxes other than on income		(167,601)
Interconnection charges		(841,121)
Bad debt expense		(61,540)
Loss on disposal of property, plant and equipment		(24,653)
Other operating expenses	4	(429,806)
Total operating expenses		(5,265,357)
Income from operations		400,237
Income from associates		46,665
Interest expense and similar items, net	4	(83,275)
Other expenses, net		(48,150)
Foreign currency exchange loss, net		(67,767)
Net monetary gain		70,479
Income before taxation and minority interest		318,189
Income tax expense	5	(244,457)
Net income before minority interest		73,732
Minority interest		-
Net income		73,732
Preferred dividends		(25,475)
Net income attributable to ordinary shareholders		48,257
Basic and diluted earnings per share, rubles		0.50

The accompanying notes form an integral part of these financial statements

Consolidated Statement of Cash Flows for the year ended December 31, 2002

(In thousands of rubles in terms of purchasing power of the ruble at December 31, 2002)

	2002
Cash flows from operating activities	
Income before taxation and minority interest	318,189
Adjustments to reconcile net income before taxation and minority interest to cash provided by operating activities:	
Depreciation and amortization	651,319
Loss on fixed assets disposals	24,653
Interest expense, net	83,275
Bad debt expense	61,540
Income from associates	(46,665)
Foreign exchange loss	67,767
Inflation gain	(70,479)
Other non-cash items	(45,102)
	726,308
Increase in accounts receivable	(83,592)
Decrease in inventory	4,432
Increase in other current assets	(70,014)
Decrease in accounts payable and accrued liabilities	(60,230)
Increase in taxes and social security payables	114,182
Interest paid	(52,988)
Income tax paid	(175,555)
Interest received	417
Net cash provided by operating activities	721,149
Cash flows from investing activities	
Purchase of property, plant and equipment	(502,829)
Dividends received	1,515
Net cash used in investing activities	(501,314)
Cash flows from financing activities	
Proceeds from loans and borrowings	355,265
Repayments of loans and borrowings	(384,315)
Payments under lease agreements	(114,893)
Dividends paid	(46,866)
Net cash used in financing activities	(190,809)
Effect of exchange rate changes on cash and cash equivalents	-
Net increase in cash and cash equivalents	29,026
Monetary effects on cash and cash equivalents	(14,192)
Cash and cash equivalents at beginning of the year	84,751
Cash and cash equivalents at end of the year	99,585
Non-cash additions to property, plant and equipment	271,991

The accompanying notes form an integral part of these financial statements

Consolidated Statement of Shareholders' Equity for the year ended December 31, 2002

(In thousands of rubles in terms of purchasing power of the ruble at December 31, 2002)

	Share capital (nominal)		Inflation impact on share capital	Retained earnings and other reserves	Total equity
	Preference shares	Ordinary shares			
At January 1, 2002	311,689	955,814	1,830,700	2,847,745	5,945,948
Net income for the year	-	-	-	73,732	73,732
Dividends	-	-	-	(49,056)	(49,056)
At December 31, 2002	311,689	955,814	1,830,700	2,872,421	5,970,624

The accompanying notes form an integral part of these financial statements

Notes to Consolidated Financial Statements Year ended December 31, 2002

(In thousand rubles in terms of purchasing power of the ruble at December 31, 2002)

1. CORPORATE INFORMATION

Authorization of Accounts

The consolidated financial statements of OAO "Dalsvyaz" and its subsidiary (the "Company") for the year ended December 31, 2002 were authorized for issue by its appointed General Director and Chief Accountant on August 11, 2003.

The Company

The Company completed its last charter registration on January 22, 2003. This amendment was due to the process of merging OAO "Dalsvyaz" with six other regional telecom enterprises located in the Far East region of Russia. The Company is an open joint stock company incorporated in Russia.

The Company was privatized in 1994 and its principal activity is providing local and long-distance and international telephone services, telegraph and data transfer services, including Internet. Other types of activity of the Company include production of telecommunication equipment and its technical support, motor transport repair and maintenance of recreational facilities and other social infrastructure. Associated companies provide cellular services in the Far East region of the Russian Federation.

Open joint-stock company Svyazinvest, a federal holding company majority-owned by the Russian Federation, owns 51% of the Company's ordinary shares. Domestic and international long-distance telecommunication services are provided by OAO "Rostelecom", a subsidiary of OAO "Svyazinvest".

The average number of employees in the Company in 2002 was approximately 20,073 persons (after giving retroactive effect of the reorganization described below).

The registered office of the Company is in the city of Vladivostok (Russian Federation), Svetlanskya st., 57

2002 Reorganization

In 2001 the Company's management started the Company's reorganization by obtaining shareholder approval to merge the following regional enterprises of OAO "Svyazinvest" wherein 62,062,396 ordinary and 19,995,626 preference shares of the Company were exchanged for 100% of the outstanding shares of the regional enterprises as follows:

Regional Enterprise	Ordinary Shares Issued by the Company	Preference Shares Issuedby the Company	Exchange Ratio
OAO Electrosvyaz of Khabarovsk region	18,534,423	6,178,141	6.10
OAO Sakhalinsvyaz	14,559,239	4,149,114	195.51
OAO Kamchatsvyazinform	12,188,544	4,062,848	75.06
OAO Amursvyaz	8,754,631	2,930,364	168.79
OAO Magadansvyazinform	5,933,493	1,977,831	1.53
OAO Telegraphno-telephonnaya Company	2,092,066	697,328	8.20
Total	62,062,396	19,995,626	

1. CORPORATE INFORMATION (CONTINUED)

The merger was completed and effective on September 30, 2002. In 2002 transaction costs related to the merger were 18,527 and expensed.

While International Financial Reporting Standards do not specify accounting principles to be applied to transactions among entities under common control, the Company has accounted for the merger based on the principles of uniting of interests as described in IAS 22 "Business Combinations". In applying this method, the Company has reflected amounts in the financial statements at their historical carrying amounts as if the entities had been combined from January 1, 2002, the earliest period presented. Unless otherwise described, all information presented in these financial statements gives retroactive effective to the reorganization.

Based on the requirements of IAS 22, the following table summarizes total assets, liabilities, revenues and pre-tax income (loss) of the regional operations for the year in which the reorganization has been completed.

	Total assets	Total liabilities	Revenue	Pre-tax Income(loss)
The Company	3,199,334	1,031,236	1,807,533	(307,942)
OAO Electrosvyaz of Khabarovsk region	1,940,517	566,390	1,281,417	236,441
OAO Sakhalinsvyaz	1,208,022	320,515	841,334	181,092
OAO Kamchatsvyazinform	979,692	311,999	660,729	44,041
OAO Amursvyaz	780,086	250,409	558,029	114,129
OAO Magadansvyazinform	368,303	86,851	403,617	18,478
OAO Telegraphno-telephonnaya Company	98,257	36,187	112,935	31,950
Total	8,574,211	2,603,587	5,665,594	318,189

Before the restructuring in October 2002, the businesses operated as separate subsidiaries of OAO Svyazinvest. Accordingly, the Company has a limited operating history as a combined business.

Russian Business Environment

The Russian economy while deemed to be of market status beginning in 2002, continues to display certain traits consistent with that of a market in transition. These characteristics have in the past included higher than normal historic inflation, lack of liquidity in the capital markets, and the existence of currency controls, which cause the national currency to be illiquid outside of Russia. The continued success and stability of the Russian economy will be significantly impacted by the government's continued actions with regard to supervisory, legal, and economic reforms.

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

Liquidity and Financial Resources

As of December 31, 2002, the Company's current liabilities exceeded its current assets by 516,546. As a result, significant uncertainties exist as to the Company's liquidity and future capital resources.

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

If needed, management believes that certain projects may be deferred or curtailed in order to fund the Company's current operating needs.

Through 2003, the Company anticipates funding from a) existing cash reserves, b) cash generated from operations, c) placement of ruble bonds in the Russian market, and d) other financing from domestic and international lending institutions.

Management also expects to continue to be able to delay payment for certain operating costs to manage its working capital requirements, if necessary.

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation

The Company maintains its accounting records and prepares its statutory accounting reports in Russian Rubles and in accordance with the Regulations on Accounting and Reporting in the Russian Federation. The accompanying financial statements presented in accordance with International Financial Reporting Standards (IFRS) are based upon the statutory accounting records that are maintained in accordance with the Russian accounting regulations under the historical cost convention. These statutory accounting reports have been adjusted to present the accompanying financial statements in accordance with IFRS. IFRS include standards and interpretations approved by the International Accounting Standards Board (IASB), and International Accounting Standards and Standing Interpretations Committee interpretations approved by the International Accounting Standards Committee Foundation (IASCF) that remain in effect. Significant differences exist between Russian Accounting Regulations and IFRS.

The consolidated financial statements have been prepared on an historical cost basis (adjusted for the effects of inflation in accordance with IAS 29), except for the measurement at fair value of available-for-sale financial assets.

Financial statement presentation herein is limited to the balance sheet at December 31, 2002 and the related statements of operations, cash flows and shareholders' equity for the year ended December 31, 2002. A comparative balance sheet at December 31, 2001, along with separate comparative statements of operations, cash flows and shareholders' equity for the year ended December 31, 2001, and the related note disclosures for such comparative financial statements, as required by International Accounting Standard ("IAS") 1, "Presentation of Financial Statements", have not been presented. Following the reorganization described in Note 1, the Company believes that presentation of comparative financial information is not practicable, including the determination of retained earnings as of January 1, 2002.

Management Estimates

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

Basis of Consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiary. As described elsewhere, the Company has accounted for the reorganization based on the principles of uniting of interests as described in IAS 22 "Business Combinations".

Subsidiaries are consolidated from the date on which control is transferred to OAO "Dalsvyaz" and cease to be consolidated from the date on which control is transferred from the Company.

Significant intercompany balances and transactions have been eliminated.

Investments in Associates

The Company's investments in its associates are accounted for under the equity method of accounting. This is an entity in which the Company has significant influence and which is neither a subsidiary nor a joint venture of the Company. The investment in associates are carried in the balance sheet at cost plus post-acquisition changes in the Company's share of net assets of the associates, less any impairment in value. The income statement reflects the Company's share of the results of operations of the associates.

Accounting for the Effects of Inflation

The accompanying consolidated financial statements are prepared in accordance with IFRS and under the historical cost convention and adjusted in accordance with IAS 29 "Financial Reporting in Hyperinflationary Economies" (IAS 29).

The adjustments and reclassifications made to the statutory records for the purpose of IFRS reporting include the restatement for changes in the general purchasing power of the ruble in accordance with IAS 29. IAS 29 requires that financial information prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. These adjustments were calculated using conversion factors derived from the Russian Federation Consumer Price Index ("CPI") published by the Russian State Committee on Statistics.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The indices used to adjust amounts in these consolidated financial statements with respect to 2002 prices (2002 = 1.0) for the years ended December 31, and the respective conversion factors, are:

Year	Index	Conversion factor
1992	7,541	362.4
1993	67,846	40.3
1994	211,612	12.9
1995	487,575	5.6
1996	594,110	4.6
1997	659,403	4.1
1998	1,216,401	2.2
1999	1,663,091	1.6
2000	1,997,843	1.4
2001	2,374,037	1.2
2002	2,733,087	1.0

The main guidelines followed in adjusting the consolidated financial statements to current purchasing power are:

• all amounts are stated in terms of the measuring unit current at December 31, 2002;

• monetary assets and liabilities at December 31, 2002 are not restated as they are already expressed in terms of the monetary unit current at December 31, 2002;

• non-monetary assets and liabilities which are not carried at amounts current at December 31, 2002 and shareholders' equity are restated by applying the relevant conversion factors;

• indexation adjustments to property, plant and equipment applicable to prior periods are credited to "Retained earnings and other reserves" in the accompanying balance sheet;

• all items in the consolidated statements of income and of cash flows are adjusted by applying appropriate conversion factors with the exception of depreciation, amortization and losses from disposal of fixed assets and other assets;

• the effect of inflation on the Company's net monetary position is included in the consolidated statement of operations as a gain or loss on net monetary position.

Effective from January 1, 2003, international accounting and financial reporting bodies have determined that the Russian Federation no longer meets the criteria of IAS 29 for hyperinflation. As a result, management has determined that it will cease to restate for changes in the general purchasing power of the ruble subsequent to December 31, 2002. The annual rate of inflation during 2002 was 15.1%.

Foreign Currency Translation

Foreign currency assets and liabilities are translated into rubles at official Central Bank of the Russian Federation (CBR) exchange rates at the yearend. Transactions denominated in foreign currencies are reported at the CBR rates of exchange at the date of the transaction. Any gains or losses on assets and liabilities denominated in foreign currencies arising from a change in official exchange rates after the date of transaction are recognized as currency translation gains or losses.

Transactions that are conducted in rubles when the related assets and liabilities are denominated in foreign

currencies (or conventional units) are recorded in the Company's financial statements on the same principles as transactions denominated in foreign currencies.

Property, Plant and Equipment

Property, plant and equipment are depreciated on the straight-line basis over the estimated economic useful lives of each class of assets as follows:

Buildings and constructions	45 years
Analogue switches	20 years
Digital switches	15 years
Cable and transmission devices:	
Duct	10 years
Radio and fixed link transmission equipment	10 years
Vehicles	5 years
Computers, office and other equipment	3 years

Construction in progress is recorded as the total of actual expenses incurred by the Company from the beginning of construction to the reporting date, adjusted for the effect of inflation from the date when such expenses occur to the reporting date in accordance with IAS 29. Construction in progress is depreciated once the property, plant and equipment are put into operation.

Borrowing costs that are directly attributable to the acquisition or construction of fixed assets are capitalized as part of the cost of the related asset when it is probable that they will result in future economic benefits to the Company and the costs can be measured reliably. Capitalization of borrowing costs commences when the activities to prepare the asset for intended use start and lasts until the assets are ready for their intended use. Other interest expenses and borrowing costs are recognized as expenses in the period in which they are incurred.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in the income statement.

The cost of maintenance, repairs and replacement of minor items of property is charged to maintenance expense. Renewals and betterments are capitalized. Upon sale or retirement of property, plant and equipment, the cost and related accumulated depreciation are eliminated from the accounts. Any resulting gains or losses are included in the determination of net income.

The period of validity of the Company's operating licenses is significantly shorter than the useful lives used for depreciation of the cost of property, plant and equipment. 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.

Property, Plant and Equipment Contributions

Property, plant and equipment transferred to the Company free of charge by its customers and other entities outside the privatization process is capitalized at market value at the date of transfer and a corresponding deferred income is recognized as a liability in the balance sheet and credited to the statement of operations on the same basis as the equipment is depreciated.

If contributions of property, plant and equipment do not generate revenues such contributions are not recorded.

Grants received from municipal authorities for the purchase of property, plant and equipment are reflected in the balance sheet as deferred income and recognized as income during the useful life of a respective asset in accordance with IAS 20 "Accounting for Government Grants and Disclosure of Government Aid Information".

Intangible Assets

Intangible assets acquired separately from a business are capitalized at cost. Intangible assets acquired as part of an acquisition of a business are capitalized separately from goodwill if the fair value can be measured reliably on initial recognition, subject to the constraint that, unless the asset has a readily ascertainable market value, the fair value is limited to an amount that does not create or increase any negative goodwill arising on the acquisition. Intangible assets, excluding development costs, created within the business are not capitalized and expenditure is charged against profits in the year in which it is incurred.

The carrying values of intangible assets are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Research and Development Costs

Research and development costs are expensed as incurred.

Investments

All investments are initially recognized at cost. After initial recognition, investments which are classified as held for trading and available-for-sale are measured at fair value, if determinable. Gains or losses on investments held for trading are recognized in income. Gains or losses on available-for-sale investments are recognized as a separate component of equity until the investment is sold, collected or otherwise disposed of, or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in income.

Other long-term investments that are intended to be held-to-maturity, such as bonds, are subsequently measured at amortized cost using the effective interest rate method.

The majority of the Company's investments are in securities that are not actively traded on organized financial markets.

Inventories

Inventories are priced at the lower of cost or net realizable value. When inventories are expensed to production, cost is determined on the basis of weighted average.

Accounts Receivable

Accounts receivable are stated at face value, less an allowance for doubtful accounts. An estimate of doubtful debts is made when collection of the full amount is no longer probable.

Cash and Cash Equivalents

Cash and cash equivalents represent cash on hand and in the Company's bank accounts, as well as cash deposits and short-term investments with original maturity dates of 3 months or less as of December 31, 2002.

Interest-Bearing Loans and Borrowings

All loans and borrowings are initially recognized at cost. After initial recognition, interest-bearing loans and borrowings, are subsequently measured at amortized cost using the effective interest rate method.

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an interest expense.

Pensions and Other Post-employment Benefits

Social contributions (including contributions to the state pension fund) are made through a unified social tax ("UST") calculated by the Company by the application of a regressive rate from 35.6% to 2% to the annual gross remuneration of each employee. The Company allocates the UST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund vary from 28% to 2% depending on the annual gross salary of each employee.

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

Under collective bargaining agreements, the Company also provides post-employment retirement benefits. The majority of the Company's employees are eligible to participate under such defined benefit plans based upon a number of factors, including years of service, age and compensation. The amount of payment depends on the employee' service period.

The Company has not complied with IAS 19 "Employee Benefits". Specifically, the Company has not made an actuarial determination of the present value of its benefit obligation under these arrangements to allow it to record its obligation and make the required disclosures under IAS 19 as of December 31, 2002.

In order to fund a portion of the Company's obligation, the Company also participates in plans under which the Company has committed to contribute agreed amounts (negotiated annually) to certain non-government pension plans. Contributions made by the Company to these plans are charged to expense when incurred.

Leases

Finance leases of equipment that transfer substantially all the risks and rewards incident to ownership of the leased item to the Company are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so far as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to interest expense.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as an expense in the income statement on a straight-line basis over the lease term.

Revenue

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.

The Company categorizes its revenue sources in eleven major categories:

1. Monthly subscription fees for local services;
2. Long distance services;
3. Network services;
4. Installation fees;
5. Internet services;
6. Radio and TV broadcasting;
7. Rent of assets;
8. Telegraph services;
9. Wireless services;
10. Other telecommunication services;
11. Other revenue.

Monthly subscription fees

The Company recognizes revenues related to the monthly network fees for local services in the month that the service is provided to the subscriber.

Long distance services

Revenues from long distance services are based on time used by the caller, the destination of the call and the services utilized. The Company charges long distance fees on a per-minute basis. The Company recognizes revenues related to the long distance services in the period when the services are rendered.

Network services

The Company provides other telecommunication operators with assess to its network. The Company recognizes revenues related to rent of channels in the period when the services were rendered.

Installation fees

The Company recognizes installation fees for indefinite contracts with its subscribers as revenues when the installation is complete.

Internet services

The Company recognizes revenues related to the Internet services in the period when the services are rendered.

Radio and TV broadcasting

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

Rent of assets

The Company leases its premises to other businesses under annual contracts. Renewal options are available on the majority of leases. These contracts are accounted for as operating leases and related rental revenues are recognized over the lease term.

Telegraph services

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

Wireless services

The Company recognizes the revenues related to wireless services in the period when the services were rendered.

Other telecommunication services

Other telecommunication services mainly include revenues from payphones network, rent of channels, and sales of handsets and accessories.

Other revenue

Revenues other than telecommunication revenues primarily consist of revenue from production of telecommunication equipment and its technical support, transportation services, maintenance of recreational facilities and other social infrastructure and sale of goods and services provided by non-core units.

Income Tax

Deferred tax assets and liabilities are calculated in respect of temporary differences in accordance with IAS 12 “Income Taxes”.

IAS 12 requires the use of a balance sheet liability method for financial reporting and accounting for deferred income taxes. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. The Company’s principal temporary differences arise in respect of property, plant and equipment. 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.

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 settled based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax liabilities relating to undistributed earnings of associated companies are recognized when it is probable that such earnings will be remitted to the Company in the foreseeable future.

Value-added Tax

Value-added taxes related to sales are payable to the tax authorities on an accrual basis based upon invoices issued to the subscriber. VAT incurred for purchases and paid to suppliers may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that are not currently reclaimable as of the balance sheet date are recognized in the balance sheet on a gross basis.

3. SEGMENT INFORMATION

The Company provides telecommunication (wireline and wireless) services and other services. Management considers that the Company operates in one geographical segment. Certain services provided between the wireline and wireless segments are not invoiced, and accordingly not recognized, between the branches of the Company performing such services. During 2002 information about business segments was as follows:

	Wireline communications services	Wireless communications services	Other operations	Eliminations	Consolidated
REVENUE					
External sales	5,362,331	182,808	120,455	-	5,665,594
Inter-segment sales	-	-	-	-	-
Total revenue	5,362,331	182,808	120,455	-	5,665,594
RESULT					
Segment result	506,400	17,264	11,375	-	535,039
Unallocated corporate expenses	-	-	-	-	(134,802)
Operating profit	-	-	-	-	**400,237**
Income from associates	-	-	-	-	46,665
Interest expense and similar items	-	-	-	-	(83,275)
Other expenses, net	-	-	-	-	(48,150)
Foreign currency exchange loss, net	-	-	-	-	(67,767)
Net monetary gain	-	-	-	-	70,479
Income tax expense	-	-	-	-	(244,457)
Minority interest in subsidiary	-	-	-	-	-
Net income	-	-	-	-	73,732
OTHER INFORMATION					
Segment assets	6,974,808	237,779	156,677	-	7,369,264
Unallocated corporate assets	-	-	-	-	1,204,947
Consolidated total assets	-	-	-	-	8,574,211
Segment liabilities	(162,980)	(6,972)	-	-	(169,952)
Unallocated corporate liabilities	-	-	-	-	(2,433,635)
Consolidated total liabilities	-	-	-	-	(2,603,587)
Capital expenditure	732,835	24,983	16,462	-	774,280
Depreciation and amortization	(616,456)	(21,016)	(13,847)	-	(651,319)

4. REVENUES AND EXPENSES

Revenues

	2002
Domestic long distance services	2,019,824
Monthly subscription fees for local services	1,368,883
International long distance services	448,679
Installation fees	450,359
Telegraph services	151,942
Network services	215,033
Data transmission services	29,606
Radio and TV broadcasting	135,849
Wireless services	182,808
Internet services	219,666
Other telecommunication services	322,490
Other revenues	120,455
Total	**5,665,594**

Wireless revenues mainly include usage charges, subscription fees, value added services, and roaming fees charged to other operators for guest roamers utilizing the Company's network.

Other telecommunication services mainly include other GTS revenues, revenues from payphones exploitation, other revenues from domestic long-distance and international timed calls (conferences, maintenance services and other), and sales of handsets and accessories.

Revenues other than telecommunication revenues primarily consist of revenue from production of telecommunication equipment and its technical support, transportation services, maintenance of recreational facilities and other social infrastructure and goods.

For the year ended December 31, 2002, the Company identified revenue by these major customer groups:

	2002
Residential customers	3,151,303
Corporate customers	1,814,751
Government customers	699,540
Total	5,665,594

Other Operating Expenses

	2002
Rent (excluding channel rent)	(27,962)
Advertising	(9,609)
General and administrative	(185,334)
Audit and consulting expenses	(21,481)
Reorganization expenses	(18,527)
Other operating expenses	(166,893)
Total	**(429,806)**

General and Administrative Expenses

	2002
Transportation	(16,153)
Post	(7,687)
Education	(4,150)
Representative and business trip expenses	(22,247)
Fire and other security expenses	(46,708)
Payments to Gossvyaznadzor	(23,107)
Other general and administrative expenses	(65,282)
Total	(185,334)

Interest Income and Expenses

	2002
Interest income	416
Interest expense	(41,415)
Leasing interest expense	(47,041)
Less: Capitalized interest	4,765
Total	(83,275)

5. INCOME TAX

Income Tax Expense

	2002
Current tax charge	191,339
Deferred tax charge	53,118
Income tax charge	244,457

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

	2002
Profit from operating activities before income tax	318,189
At statutory tax rate of 24%	76,365
Effect of:	
Expenses not deductible for tax purpose	107,601
Permanent elements of monetary gain	163,640
Inflation effect on deferred tax balance at beginning of year	(21,294)
Other reconciling items	(81,855)
At effective tax rate of 77%	244,457

Deferred Income Tax

	Balance Sheet 2002
Deferred income tax liabilities:	
Property, plant and equipment	(829,329)
Investments in associates	(25,872)
Gross deferred income tax liabilities	(855,201)
Deferred income tax assets	
Accounts receivable	36,262
Accounts payable	68,277
Contributions of equipment	15,761
Other	6,435
Gross deferred income tax assets	126,735
Net deferred income tax liability	(728,466)

6. EARNINGS PER SHARE

Basic and diluted earnings per share are calculated by dividing the net profit for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year. Ordinary shares issued as part of the reorganization, that has been accounted for similar to a uniting of interests, are included in the calculation of the weighted average number of shares from January 1, 2002 as the financial statements of the Company are prepared as if the combined entity had existed as from that date. Therefore, the number of ordinary shares is the aggregate of the weighted average number of shares of the combining entities, adjusted to equivalent shares of the Company outstanding after the reorganization.

	2002
Net income attributable to ordinary shareholders for basic and diluted earnings per share	48,257
Weighted average number of ordinary shares for basic and diluted earnings per share	95,581,421
Earnings per ordinary share, rubles (basic and diluted)	0.50

The Company has no potential dilutive shares outstanding.

There have been no other transactions involving ordinary shares or potential ordinary shares since the reporting date and before the completion of these financial statements.

7. DIVIDENDS PROPOSED AND PAID

Declared in 2002 (for the year 2001):

Dividends on ordinary shares	23,581
Dividends on preference shares	25,475
Total	49,056

7. DIVIDENDS PROPOSED AND PAID (CONTINUED)

Approved by the annual shareholder meeting for the year ending 2002 (see Note 25 “Subsequent Events”)

Dividends on ordinary shares	29,630
Dividends on preference shares	18,078
Total	47,708

Dividends paid to shareholders are proposed by the directors and legally declared and approved at the annual shareholders' meeting. Earnings available for dividends are limited to profits determined in accordance with Russian statutory accounting regulations.

8. PROPERTY, PLANT AND EQUIPMENT

	Buildings and constructions	Switches and transmission equipment	Assets under construction and equipment for installation	Machines and other	Total
Cost					
As of January 1, 2002	10,057,456	8,139,549	404,315	1,169,792	19,771,112
Additions	-	-	774,280	-	774,280
Transfers	151,332	565,400	(834,159)	117,427	-
Disposals	(81,828)	(191,059)	-	(36,753)	(309,640)
As of December 31, 2002	10,126,960	8,513,890	344,436	1,250,466	20,235,752
Impairment					
As of January 1, 2002	(925,250)	(953,736)	(107,766)	(100,726)	(2,087,478)
Charge for the year	-	-	(48,785)	-	(48,785)
Recoveries / reversals	7,104	16,696	-	3,649	27,449
As of December 31, 2002	(918,146)	(937,040)	(156,551)	(97,077)	(2,108,814)
Accumulated Depreciation					
As of January 1, 2002	(5,644,372)	(3,953,716)	-	(791,073)	(10,389,161)
Charge for the year	(189,564)	(370,859)	-	(88,347)	(648,770)
Depreciation on disposals	74,725	174,362	-	31,170	280,257
As of December 31, 2002	(5,759,211)	(4,150,213)	-	(848,250)	(10,757,674)
Net book value as of December 31, 2002	3,449,603	3,426,637	187,885	305,139	7,369,264

The carrying value of switches and transmission equipment held under finance leases at December 31, 2002 is 178,348. Leased assets are pledged as security for the related finance lease liabilities (see Note 19 "Obligations under Finance Leases").

The total interest costs capitalized during 2002 amounted to 4,765.

Buildings and equipment with a book value of 208,602 as of December 31, 2002 secure bank loans. As of December 31, 2002 vendor financing from Siemens is secured by equipment amounting to 74,330 until the last installment is paid (see Note 18 "Loans and Borrowings").

The Company's accounting records relating to fixed assets are not designed to support their presentation in accordance with IAS 16 "Property, Plant and Equipment", IAS 29 "Financial Reporting in Hyperinflationary Economies" and IAS 36 "Impairment of Assets". As such certain estimates were made by management to present fixed assets in the accompanying financial statements.

In the future, the Company expects to hire an independent appraiser to assist in reconstruction of the historical cost of the Property, Plant and Equipment, in order to make the necessary adjustments, if any, to the Company's books and records, in order to comply with IFRS.

9. INTANGIBLE ASSETS

	Licenses	Software	Total
Cost			
At January 1, 2002		9,951	9,951
Additions	1,998	8,873	10,871
Disposals		(688)	(688)
At December 31, 2002	1,998	18,136	20,134
Accumulated amortization			
At January 1, 2002		(5,109)	(5,109)
Charge for the year	(182)	(2,367)	(2,549)
Disposals		688	688
At December 31, 2002	(182)	(6,788)	(6,970)
Net book value at December 31, 2002	1,816	11,348	13,164

Intangible assets are amortized on a straight-line basis over the estimated useful economic lives of the assets, which is 5 years.

10. INVESTMENT IN SUBSIDIARY

The consolidated financial statements include the financial statements of OAO “Dalsvyaz” and its 60% owed subsidiary ZAO “Sotovye Sety Birobidgana”, whose main activity is providing cellular services. This subsidiary is a Russian legal entity registered in accordance with Russian regulations. As of the end of 2002, the subsidiary has a retained loss.

11. INVESTMENTS IN ASSOCIATES

Investments in associates as of December 31, 2002 comprised the following:

		As of December 31, 2002	
Associate	**Main activity**	**Carrying value**	**Voting shares**
ZAO Primtelephone	Cellular services	90,140	50.0%
OOO Magalyascom	Cellular services	15,987	50.0%
ZAO Dalnevostochnaya sotovaya svyaz –900 (DSS-900)	Cellular services	13,980	40.0%
ZAO TeleRoss Vladivostok	Communications services	8,345	50.0%
OOO Kamalyascom	Cellular services	566	50.0%
ZAO Khabarovskiy sotovyi telephone	Cellular services		30.0%
Total		129,018	

12. AVAILABLE-FOR-SALE FINANCIAL ASSETS

Available-for-sale financial assets as of December 31, 2002 comprised the following:

		As of December 31, 2002	
Company	**Main activity**	**Carrying value**	**Voting shares**
OAO DalTelecomInternational	Cellular services	2,624	6.4%
AKB Primorie	Bank services	2,152	8.2%
OAO SEZ Nakhodka	Communications services	1,101	8.47%
AKB Dalcombank	Bank services	858	1.4%
AKB (ZAO) Svyaz bank, Moscow	Bank services	680	0.4%
SAO Dalstar	Insurance services	500	5.0%
OAO Imperial	Investment trust	240	19.6%
Other		2,137	
Total		10,292	

Available-for-sale financial assets do not have a quoted market price in an active market. Accordingly, management has reflected such assets at cost.

13. INVENTORIES

Inventories as of December 31, 2002 comprised the following:

	2002
Cable, materials and spare parts for telecommunication equipment	222,042
Finished goods and goods for sale	18,649
Other inventory	225
Provision for obsolescence	(915)
Total	240,001

14. TRADE ACCOUNTS RECEIVABLE

As of December 31, 2002, the Company identified trade receivables by the following major customer groups:

	2002
Government customers	284,020
Residential customers	149,061
Corporate customers	134,889
Less allowance for doubtful accounts	(250,200)
Total	317,770

The Company invoices its governmental and corporate customers on a monthly basis. For residential customers, the Company sends monthly payment requests and substantially relies upon these customers to remit payments based on the received payment requests. All customer payments are based upon tariffs, denominated in rubles, in effect at the time of calls made. In limited circumstances, the Company has billed and collected penalties associated with delays in payment and has been able to obtain certain payments through the Arbitrage Court. In order to further reduce a portion of the risk associated with customer nonpayments, the Company has in certain circumstances negotiated arrangements wherein the Company has accepted payment in goods and services, which are utilized in carrying out its non-core business.

15. OTHER CURRENT ASSETS

Other current assets as of December 31, 2002 comprised the following:

	2002
Prepayments and advances	90,205
Settlements with personnel	16,749
VAT	127,835
Taxes prepaid	27,889
Other receivables	101,314
Less allowance for doubtful accounts	(14,339)
Total	349,653

16. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of December 31, 2002 comprised the following:

	2002
Cash at bank and in hand	89,552
Short-term bank deposits	10,033
Total	99,585

The fair value of cash and cash equivalents equals its book value.

17. SHARE CAPITAL

Share capital:	2002
Preference shares , 10 rubles par value	
31,168,901 shares authorized -	
31,168,901 shares issued and	
outstanding as of December 31, 2002	311,689
Ordinary shares, 10 rubles par value	
95,581,421 shares authorized -	
95,581,421 shares issued and	
outstanding as of December 31, 2002	955,814
Total share capital	1,267,503

The state registration of the charter documents was completed on January 22, 2003. In accordance with IAS 10 “Events After the Balance Sheet Date” such changes of the charter capital were recognized as of December 31, 2002 in the accompanying financial statements.

The share capital account represents the authorized capital of the Company as stated in the charter documents. The Company had 95,581,421 ordinary shares and 31,168,901 preference shares type A issued as of December 31, 2002. All shares have a par value of 10 rubles. All shares are fully paid.

Dalsvyaz

Of the capital shares issued as of December 31, 2002, 75.4% was attributable to ordinary shares and 24.6% attributable to preference shares, type A. The ordinary

shareholders are allowed one vote per share. Preference shares type A are non-voting. All ordinary shares and preference shares type A are eligible for distribution of earnings available in accordance with Russian statutory accounting regulations. Preference shares type A are entitled to a minimum annual dividend in the amount equal to 9.8% of statutory net income available for dividends. Dividends on preference shares type A may not be less than the dividends on ordinary shares. Shareholders of preference shares type A have a preferred right to recover the par value of preference shares in liquidation.

In August 2001, the Company concluded a Depositary Agreement with JP Morgan Chase Bank in respect of American Depositary Receipts (ADRs), Level 1. The issue was registered on August 22, 2001. The depositary agreement between the Company and JP Morgan Chase Bank was revised on August 16, 2002 in accordance with the reorganization (see Note 1 "Corporate Information"). In accordance with the depositary agreement each ADR is equal to 30 ordinary shares of the Company. As at December 31, 2002 no ADRs were deposited.

The following represents the Company's shareholders as of December 31, 2002 (in thousands of shares):

	Ordinary shares		**Preference shares**		**Total**
		%		%	
OAO "Svyazinvest"	48,331	51	-		48,331
Other legal entities	40,245	42	19,864	64	60,109
Individuals	7,005	7	11,305	36	18,310
Total	95,581	100	31,169	100	126,750

18. LOANS AND BORROWINGS

Loans and borrowings as of December 31, 2002 comprised the following:

	Effective interest rate	**Maturity**	**2002**
Short-term borrowings			
Sberbank	19-22%	2003	109,719
Dalcombank	17%	2003	18,000
Kamchatprombank	21%	2003	1,650
Other	0-22%	2003	21,064
Total short-term borrowings			150,433
Long-term borrowings			
Vnesheconombank	7.5%	up to 2007	196,261
Siemens	10 – 11%	up to 2005	87,889
Italtel	7.5%	up to 2003	26,499
Sumitomo	5%	up to 2004	8,421
Other	0–13%	up to 2005	19,221
Total long-term borrowings			338,291
Less: current portion of long-term borrowings			(227,649)
Total			110,642

Dalsvyaz

Short-term borrowings

Short-term ruble borrowings mainly represent bank loans received for working capital financing purposes.

Long-term borrowings

Vnesheconombank

During 1996-1997 the Ministry of Finance of the Russian Federation (hereinafter "the Ministry") granted the Company long-term financing for purchases of telecommunication equipment from various foreign vendors. Vnesheconombank has been acting as an agent of the Ministry on collection of payments from the Company. The liability was initially denominated in Deutsche Mark (DM), and later in Euro after introduction of the Euro. Interest is accrued at 7.5%. The loan is not secured.

Following the crisis of 1998 and the significant increase of the exchange rate of DM to ruble, repayments on these agreements were ceased. As a result, approximately 52,664 of loans due to Vnesheconombank, which were included in current portion of long-term borrowings in the consolidated balance sheet as of December 31, 2002, were overdue.

Siemens

In 1995-2000 the Company concluded vendor financing agreements with Siemens. Under these contracts, Siemens delivered and installed telecommunication equipment to the Company. The amounts payable under these agreements are denominated in Euro and are repayable in equal installments during 2003 – 2005. Interest is accrued from 10% to 11% per annum. The loans are secured by equipment amounting to 74,330 until the last installment is paid.

Italtel

In 1996 the Company entered into an agreement with Italtel, under which Italtel delivered telecommunication equipment to the Company. The amounts payable under this agreement are denominated in USD and are repayable during 2003. Interest is accrued at 7.5% per annum. The loan is not secured.

Sumitomo

In 1998 the Company entered into an agreement with Sumitomo, under which Sumitomo delivered telecommunication equipment to the Company. The amounts payable under this agreement are denominated in Japanese yen (JPY) and are repayable during 2003- 2004. Interest is accrued at 5% per annum. The loan is not secured.

19. OBLIGATIONS UNDER FINANCE LEASES

The Company has finance lease contracts for telecommunication equipment. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments as of December 31, 2002 are as follows:

	Minimum payments	**Present value of payments**
Within one year	128,403	71,717
After one year but not more than five years	142,197	104,750
More than 5 years	3,480	1,881
Total minimum lease payments	274,080	
Less amounts representing finance charges	(95,732)	
Present value of minimum lease payments	178,348	178,348

In 2002 the Company's major lessors were Promsvyazleasing and RTC-Leasing (see also Note 23 "Related Parties Disclosures").

In accordance with the agreements with RTC-Leasing, the lessor has a right to adjust schedules of future lease payments subject to certain changes in economic environment, in particular, change in the refinancing rate of the Central Bank of the Russian Federation.

20. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses as of December 31, 2002 comprised the following:

	2002
Accounts payable	236,691
Salary and wages payables	268,969
Subscriber prepayments	169,952
Other trade payables	39,348
Total	714,960

As of December 31, 2002, the Company identified the following major taxes payable:

	2002
Value added tax	192,673
Profit tax	15,854
Property tax	15,724
Personal income tax	15,512
Sales tax	17,936
Unified social tax	29,584
Other taxes	863
Total	288,146

21. PENSION PLANS AND EMPLOYEE BENEFITS

In 2002 the Company made various payments to employees in addition to salary. These payments generally represent financial aid to the Company's employees with limited abilities and bonuses to employees, which had made no breaches of internal policies during the last fiscal year. Such benefits were included in salary, benefits, salary taxes and other social expenditures in the accompanying consolidated statements of operations for the year ended December 31, 2002 and approximated 29,694.

In addition to statutory pension benefits, the Company also contributes to defined benefit plans, which cover most of its employees. Non-government pension fund "Telecom-Soyuz" which is not related to the Company, maintain the plans. The plans provide for payments of retirement benefits starting from statutory retirement age, which is currently 55 for women and 60 for men. The benefits are based on a formula recognizing minimal statutory pension level, length of service, both in the Company and in the telecommunications industry as well as final average earnings and position in the Company. The benefits are not vesting and are subject to the employee retiring from the Company on or after the above-mentioned respective ages. The Company makes contributions to the pension funds in the amounts representing fixed percentage of participating employees' salaries or in amounts fixed in the agreements with pension funds, depending on the nature of each particular agreement.

As described in Note 2 "Summary of Significant Accounting Policies" the Company has not made an actuarial determination of the present value of its benefit obligation under these arrangements to allow it to record its obligation and make the required disclosures under IAS 19 "Employee Benefits" as of December 31, 2002.

22. COMMITMENTS AND CONTINGENCIES

Insurance Coverage

The Russian insurance industry is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. During 2002, the Company did not maintain insurance coverage on a significant part of their property, plant and equipment asset bases, business interruption, or third party liability in respect of property or environmental damage arising from accidents on the Company's property or relating to the Company's operations. Until the Company obtains adequate insurance coverage, there is a risk that the loss of destruction of certain assets could have a material adverse effect on the Company's operation and financial position.

Litigation, Claims and Assessments

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

Management is unable to estimate what developments may occur in respect of the Russian legal system or the resulting effect of any such developments on the Company's financial condition or future results of operations. The financial statements do not include any adjustment that may result from these uncertainties.

Capital Investment Commitments

As of December 31, 2002 the total contractual commitments of the Company for capital investments in modernization and expansion of its network were 333,148 including 317,597 commitments with RTC-leasing.

23. RELATED PARTY DISCLOSURES

(1) Settlements with associates

The Company's consolidated financial statements include the following amounts as of December 31, 2002:

Accounts receivable from associates:

Name of related party	2002
ZAO DSS-900	2,006
ZAO Primtelephone	952
ZAO TeleRoss-Vladivostok	1,078
ZAO Khabarovskyi sotovyi telephone	2,017
OOO Magalyascom	770
OOO Kamalyascom	125
Total	6,948

Accounts payable to associates:

Name of related party	2002
ZAO DSS-900	(219)
ZAO Primtelephone	(5,292)
ZAO TeleRoss-Vladivostok	(1,681)
ZAO Khabarovskyi sotovyi telephone	(256)
Total	(7,448)

The consolidated statement of operations for 2002 include the following transactions:

Sales to associates:

Name of related party	2002
ZAO DSS-900	8,382
ZAO Primtelephone	10,358
ZAO TeleRoss-Vladivostok	4,944
ZAO Khabarovskyi sotovyi telephone	5,803
OOO Magalyascom	1,430
OOO Kamalyascom	127
Total	31,044

Purchases from associates:

Name of related party	2002
ZAO DSS-900	(432)
ZAO Primtelephone	(2,819)
ZAO TeleRoss-Vladivostok	(3,715)
ZAO Khabarovskyi sotovyi telephone	(697)
Total	(7,663)

All operations with associates were performed under market prices.

(2) Svyazinvest

The Company regards Svyazinvest as its parent entity. Svyazinvest was wholly owned by the Russian Government until July 1997 when the Government sold 25% plus one share of the charter capital of Svyazinvest to the private sector.

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

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

Dalsvyaz

(3) Rostelecom

Rostelecom, a majority owned subsidiary of Svyazinvest, is the primary provider of domestic long distance and international telecommunications services in the Russian Federation. The Company has negotiated interconnection agreements with Rostelecom. The annual expense associated with traffic carried by Rostelecom and terminated outside of the Company's network is stated as interconnection charges. In 2002 interconnection charges related to Rostelecom amounted to 569,871.

(4) RTC-Leasing

RTC-Leasing is a subsidiary of Rostelecom. RTC-Leasing purchases telecommunication equipment from domestic and foreign suppliers and leases the equipment. The Company's obligations under capital leases to RTC-Leasing included in the accompanying consolidated balance sheet as at December 31, 2002 may be summarized as follows:

	Minimum payments	**Present value of payments**
Within one year	24,750	11,801
After one year but not more than five years	60,217	33,849
More than 5 years	666	640
Total minimum lease payments	85,633	
Less amounts representing finance charges	(39,344)	
Present value of minimum lease payments	46,289	46,289

(5) Transactions with State Organizations

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

Government subscribers accounted for approximately 50 % of trade accounts receivable as of December 31, 2002. Amounts outstanding from Government subscribers as of December 31, 2002 amounted to 284,020, including 215,000 for privilege category of invividuals.

(6) Non-Commercial Partnership

Non-commercial partnership "Center for Research of the Problems in Development of Telecommunications" (hereinafter "the Partnership") is an entity related to Svyazinvest. The Company has an agreement with the Partnership, under which it provides financing for mutually beneficial projects undertaken by the Partnership on behalf of the Company, and other subsidiaries and associates of Svyazinvest. Payments to the Partnership included in other operating expenses in the accompanying consolidated income statement for the year ended December 31, 2002 amounted to 46,652.

24. FINANCIAL INSTRUMENTS

Fair Values

Management believes that carrying values of the financial instruments included in the accompanying consolidated balance sheet as at December 31, 2002 approximates their fair values.

Interest Rate Risk

The following table sets out, by maturity, the Company's financial instruments that are exposed to interest rate risk as of December 31, 2002.

	<1 year	1-5 years	>5 years	Total
Fixed rate				
Short-term borrowings	(150,433)	-	-	(150,433)
Long-term borrowings	(227,649)	(110,642)	-	(338,291)
Obligations under financial leases	(71,717)	(104,750)	(1,881)	(178,348)

Interest on financial instruments classified as fixed rate is fixed until maturity of the investment.

25. SUBSEQUENT EVENTS

(1) Dividends

On June 11, 2003, the annual meeting of shareholder of the Company approved the dividends for the year 2002 in the amount of 0.58 rubles per one preference share and 0.31 rubles per one ordinary share. Total dividend announced amounted to 47,708. Dividends for the year ending December 31, 2002 are payable during 2003 and will be recognized in the financial statements as of and for the year ending December 31, 2003.

(2) Tariffs for Telecom Services

Effective July 1, 2003, tariffs for certain type of local and long-distance calls and installation fees were increased by approximately 13%.

(3) Decision of Bonds Issue

On May 29, 2003, the Board of Directors approved the issue of 1,000,000 documentary bearer non-convertible bonds with 1,000 roubles face value each. Bonds have 6 coupons. Interest payments per each coupon are scheduled for every 182nd day from the first day of the placement. Interest rate is to be set on tender held on the date of issue. The debentures mature 1,092 days after the placement. As at August 11, 2003, no placement was performed.

(4) Sberbank Loan

On May 29, 2003 the Board of Directors of OAO "Dalsvyaz" approved a loan with Sberbank in the amount of 96,000 at an interest rate of 17% for a period of 18 months. The loan is secured by equipment in the total amount of 173,186.

(5) Purchases of Telecommunications Equipment

In July 2003, the Company concluded several agreements with Beta Hawaii for the total amount of USD 1,254 thousand (approximately 38,121). Under these agreements Beta Hawaii is to deliver and install various telecommunications equipment.

(6) Leasing Contracts

In 2003 the Company concluded a number of capital lease agreements with RTC-Leasing, a subsidiary of Rostelecom, and Promsvyazleasing, undiscounted future lease payments amounted to 1,014,210 and 387,141, respectively.

(7) Implementation of Oracle

On May 29, 2003 the Board of Directors approved an agreement with ZAO "Open Technologies 98" to purchase Oracle E-Business Suite for the amount of USD 9,654 thousand (approximately 306,847).

(8) Telecommunications Reforms

A new law "On Telecommunications" will come into effect on January 1, 2004.

Subsequent to December 31, 2002, Rostelecom commenced reforms of the system of settlements with regional operators for domestic long-distance traffic. Under the existing method, settlements between Rostelecom and regional operators are based on one minute of domestic transit traffic sent through 50 km of Rostelecom networks. The integral settlement rate (ISR) contains two components – a linear component and a termination charge, which is calculated based on the weighted average of incoming and outgoing traffic. The ISR was set once a year based on the traffic data for the preceding year and distorted the economic benefits and costs of providing and terminating transit traffic in the year applied.

Under the planned changes, full consideration is expected to be given to the cost of Rostelecom carrying and benefits to the Company in terminating domestic long-distance traffic. Such system will allow the Company to receive revenues for terminating domestic long-distance traffic based on actual volumes of traffic in the current period, which will increase the transparency and timeliness of settlements.

As of August 11, 2003 the Company did not sign the new interconnection agreements with Rostelecom.

Management cannot currently predict the outcome of these changes on the Company's future operations.