COMSTAR UTS

Independent Auditors' Report

Financial Statements
Years ended December 31, 2005 and 2004

COMSTAR UTS AND SUBSIDIARIES

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Deloitte.

ZAO Deloitte & Touche CIS
Business Center "Mokhovaya"
4/7 Vozdvizhenka St., Bldg. 2
Moscow, 125009
Russia

Tel: +7 (495) 787 0600
Fax: +7 (495) 787 0601
www.deloitte.ru

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Comstar UTS:

We have audited the accompanying consolidated and combined balance sheets of JSC "COMSTAR – United TeleSystems" ("Comstar UTS") and its subsidiaries (together – "the Group") as of December 31, 2005 and 2004 and the related consolidated and combined statements of operations and comprehensive income, changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated and combined financial statements present fairly, in all material respects, the financial position of the Group as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche

April 11, 2006

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COMSTAR UTS AND SUBSIDIARIES

CONSOLIDATED AND COMBINED BALANCE SHEETS AS OF DECEMBER 31, 2005 AND 2004
(Amounts in thousands of U.S. dollars)

	December 31, 2005	December 31, 2004
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents (Note 5)	$ 74,639	$ 67,436
Short-term investments (Note 6)	116,134	105,313
Trade receivables, net (Note 7)	78,310	63,504
Other receivables and prepaid expenses (Note 8)	80,572	60,669
Inventories and spare parts (Note 9)	26,881	23,004
Assets held for resale (Note 2)	15,260	-
Deferred tax assets, current portion (Note 21)	13,432	15,693
Total current assets	405,228	335,619
Property, plant and equipment, net (Note 10)	1,144,149	1,031,757
Intangible assets, net (Note 11)	55,355	30,240
Long-term investments (Note 12)	30,510	11,290
Restricted cash	2,272	3,268
Deferred tax assets, long-term portion (Note 21)	3,847	6,274
TOTAL ASSETS	$ 1,641,361	$ 1,418,448
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 28,707	$ 17,699
Deferred connection fees, current portion	42,598	35,790
Subscriber prepayments	41,228	34,095
Accrued expenses and other current liabilities (Note 13)	43,409	23,620
Taxes payable	17,837	19,563
Debt, current portion (Note 14)	86,617	85,616
Capital lease obligations, current portion (Note 15)	14,050	6,782
Total current liabilities	274,446	223,165
LONG-TERM LIABILITIES:		
Deferred connection fees, net of current portion	110,514	104,087
Debt, net of current portion (Note 14)	102,184	104,482
Capital lease obligations, net of current portion (Note 15)	30,765	19,917
Post-retirement obligations (Note 16)	16,216	11,513
Property, plant and equipment contributions (Note 17)	102,746	103,822
Deferred tax liabilities, long-term portion (Note 21)	9,005	19,397
Total long-term liabilities	371,430	363,218
TOTAL LIABILITIES	645,876	586,383
COMMITMENTS AND CONTINGENCIES (Note 24)	-	-
MINORITY INTERESTS	516,114	450,624
SHAREHOLDERS' EQUITY:		
Share capital (Note 18)	18,982	72,133
Treasury stock	(3,929)	-
Additional paid-in capital	100,051	43,335
Retained earnings	352,647	250,756
Accumulated other comprehensive income	11,620	15,217
TOTAL SHAREHOLDERS' EQUITY	479,371	381,441
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 1,641,361	$ 1,418,448

See notes to consolidated and combined financial statements.

COMSTAR UTS AND SUBSIDIARIES

CONSOLIDATED AND COMBINED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004
(Amounts in thousands of U.S. dollars, except for per share amounts)

	Year ended December 31,	
	2005	**2004**
OPERATING REVENUES (Note 19)	$ 907,624	$ 695,133
OPERATING EXPENSES (Note 20)	(639,273)	(521,414)
OPERATING INCOME	268,351	173,719
OTHER INCOME/(EXPENSE):		
Interest income	7,696	7,941
Interest expense	(17,961)	(18,695)
Foreign currency transactions (loss)/gain	(2,219)	4,368
Gain/(loss) from disposal of an affiliate (Note 4)	1,989	(6,610)
INCOME BEFORE INCOME TAX AND MINORITY INTERESTS	257,856	160,723
Income tax expense (Note 21)	(59,329)	(41,076)
Income from affiliates	499	542
Minority interests	(93,141)	(44,400)
INCOME FROM CONTINUING OPERATIONS	105,885	75,789
Gain from discontinued operations, net of income tax charge of $1,430 (Note 3)	-	4,182
Loss from disposal of discontinued operations, net of income tax charge of $841 (Note 3)	-	(3,831)
NET INCOME	**$ 105,885**	**$ 76,140**
Other comprehensive (loss)/income:		
Translation adjustment, net of minority interest of $13,788 and $34,175, respectively	(3,597)	13,538
Comprehensive income	$ 102,288	$ 89,678
Weighted average number of common shares outstanding for the period from November 22, 2005 to December 31, 2005 (Note 2)	221,198,360	
Earnings per common share, basic and diluted for the period from November 22, 2005 to December 31, 2005 (Note 2)	$ 0.04	-

See notes to consolidated and combined financial statements.

COMSTAR UTS AND SUBSIDIARIES

CONSOLIDATED AND COMBINED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004
(Amounts in thousands of U.S. dollars)

	Year ended December 31, 2005	2004
OPERATING ACTIVITIES:		
Net income	$ 105,885	$ 76,140
Adjustments to reconcile net income to net cash provided by operations:		
Gain from discontinued operations	-	(4,182)
Loss from disposal of discontinued operations	-	3,831
Depreciation and amortization	90,437	76,138
Loss from disposal of fixed assets	6,581	4,312
Loss from disposal of an affiliate	-	6,610
Gain from disposal of long-term investments	(1,989)	-
Deferred taxes	(5,796)	1,453
Income from affiliates	(499)	(542)
Foreign currency transactions loss/(gain) on non-operating activities	2,102	(4,177)
Postretirement benefits	5,117	6,315
Minority interests	93,141	44,400
Provision for doubtful debts	4,503	1,307
Impairment of property, plant and equipment	1,513	-
Changes in operating assets and liabilities:		
Trade receivables	(15,741)	(7,815)
Other receivables and prepaid expenses	(23,640)	(19,013)
Inventories and spare parts	(3,736)	(3,083)
Accounts payable	10,630	(2,727)
Deferred connection fees	15,316	30,790
Subscriber prepayments	10,229	4,683
Taxes payable	(1,309)	5,028
Accrued expenses and other current liabilities	1,180	6,338
Net cash provided by operations	293,924	225,806
INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(194,953)	(150,481)
Proceeds from sale of property, plant and equipment	1,351	1,454
Proceeds from property insurance recovery	5,806	-
Purchases of intangible assets	(22,127)	(18,366)
Proceeds from disposal of subsidiaries, net of cash disposed	-	16,211
Acquisition of subsidiaries, net of cash acquired	(24,277)	-
Acquisition of minority interests	(8,529)	-
Purchases of long-term investments	(36,394)	-
Proceeds from sale of long-term investments	13,449	652
Purchases of short-term investments	(327,072)	(249,465)
Proceeds from sale of short-term investments	326,442	211,656
Decrease in restricted cash	961	467
Net cash used in investing activities	(265,343)	(187,872)

COMSTAR UTS AND SUBSIDIARIES

CONSOLIDATED AND COMBINED STATEMENTS OF CASH FLOWS (continued)
FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004
(Amounts in thousands of U.S. Dollars)

	Year ended December 31,	
	2005	**2004**
FINANCING ACTIVITIES:		
Contributions from the controlling shareholder	12,508	-
Proceeds from borrowings	125,126	101,329
Principal payments on borrowings	(128,147)	(99,969)
Principal payments on capital lease obligations	(12,439)	(10,641)
Dividends and other distributions to shareholders	(17,393)	(10,201)
Net cash used in financing activities	(20,345)	(19,482)
Effects of foreign currency translation on cash and cash equivalents	(1,033)	2,032
INCREASE IN CASH AND CASH EQUIVALENTS	7,203	20,484
CASH AND CASH EQUIVALENTS, beginning of the year	67,436	46,952
CASH AND CASH EQUIVALENTS, end of the year	$ 74,639	$ 67,436
SUPPLEMENTAL INFORMATION:		
Cash paid for interest, net of amounts capitalized	$ 16,201	$ 15,109
Income taxes paid	67,175	40,187
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Property, plant and equipment received free of charge	$ 6,281	$ 13,597
Equipment acquired through vendor financing	2,921	20,714
Equipment acquired under capital leases	28,779	25,966

In addition, non-cash investing activities during the years ended December 31, 2005 and 2004 included acquisitions and disposals of subsidiaries and affiliates, as described in Note 4.

See notes to consolidated and combined financial statements.

COMSTAR UTS AND SUBSIDIARIES

CONSOLIDATED AND COMBINED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004

(Amounts in thousands of U.S. dollars)

	Share capital	Treasury stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income	Total
Balances at January 1, 2004	**$ 72,133**	**$ -**	**$ 43,335**	**$ 176,947**	**$ 1,679**	**$ 294,094**
Dividends declared	-	-	-	(2,331)	-	(2,331)
Net income	-	-	-	76,140	-	76,140
Translation adjustment, net of minority interest of $34,175	-	-	-	-	13,538	13,538
Balances at December 31, 2004	**$ 72,133**	**$ -**	**$ 43,335**	**$ 250,756**	**$ 15,217**	**$ 381,441**
Contribution from the controlling shareholder	-	-	5,513	-	-	5,513
Acquisition of interest in a subsidiary from the controlling shareholder	-	-	(4,301)	-	-	(4,301)
Common stock issuance by subsidiaries	-	-	6,995	-	-	6,995
Dividends declared	-	-	-	(3,994)	-	(3,994)
Net income	-	-	-	105,885	-	105,885
Restructuring of the Group	(53,151)	(3,929)	48,509	-	-	(8,571)
Translation adjustment, net of minority interest of $13,788	-	-	-	-	(3,597)	(3,597)
Balances at December 31, 2005	**$ 18,982**	**$ (3,929)**	**$ 100,051**	**$ 352,647**	**$ 11,620**	**$ 479,371**

See notes to consolidated and combined financial statements.

1. DESCRIPTION OF THE BUSINESS

Nature of the business - JSC "COMSTAR–United TeleSystems" ("Comstar UTS") and subsidiaries (together – "the Group") is a provider of fixed line communications services, including voice, Internet dial-up and broadband, pay TV and various value added services, to commercial and residential customers throughout the Moscow metropolitan area and in other select regions in Russia. The controlling shareholder of Comstar UTS is JSFC Sistema ("Sistema"). The entities of the Group are incorporated in the Russian Federation ("the RF").

The Group has two reportable segments: the Traditional fixed line communications segment, comprised of MGTS and the Alternative fixed line communications segment, comprised of all other entities of the Group.

The Group's restructuring and the initial public offering - The Group was formed in the fourth quarter of 2005 through the consolidation by Sistema of its fixed line communications businesses under Comstar UTS. In November 2005, Comstar UTS issued additional 255,919,860 common shares to acquire Sistema's stakes in MGTS, MTU-Inform, Telmos and MTU-Intel and MGTS' stakes in MTU-Inform, Telmos and MTU-Intel. In December 2005, Sistema Multimedia, a subsidiary of Sistema, was merged into MTU-Intel (Note 4).

In February 2006, Comstar UTS completed an initial public offering of 146,500,000 common shares, including 139,000,000 newly issued shares and 7,500,000 shares sold by the shareholders. The shares (in the form of global depositary receipts ("GDRs"), with one GDR representing one share) were admitted to trade on the London Stock Exchange. The Group's net proceeds from the offering amounted to approximately $976 million.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation - The accompanying financial statements have been prepared in conformity with the accounting principles generally accepted in the United States of America ("U.S. GAAP"). The Group's entities maintain accounting records and prepare their financial statements in Russian rubles in accordance with the requirements of accounting and tax legislation in Russia. The accompanying consolidated and combined financial statements differ from the financial statements prepared for statutory purposes in Russia in that they reflect certain adjustments, not recorded in the accounting books of the Group's entities, which are appropriate to present the financial position, results of operations and cash flows in accordance with U.S. GAAP.

Principles of consolidation and combination - The Group's restructuring in November 2005 (Note 1) has resulted in a change in the reporting entity. The consolidated financial statements presented for the periods subsequent to the restructuring include the financial statements of Comstar UTS and its subsidiaries.

The combined financial statements of the Group's entities are presented for the periods preceding the restructuring. The combined financial statements have been prepared as if the restructuring had occurred from the beginning of the earliest period presented.

The assets and liabilities of the entities transferred to the Group under the common control were recorded in these financial statements at the historical cost of their acquisition by the Group's controlling shareholder.

All significant intercompany transactions, balances and unrealized gains (losses) have been eliminated.

The ownership interest of Comstar UTS and proportion of its voting power (together with Sistema) in its major subsidiaries as of December 31, 2005 were as follows:

Operating entities	**December 31, 2005**	
	Ownership interest	**Proportion of voting power**
MGTS	46%	56%
MTU-Inform	99%	99%
Telmos	100%	100%
MTU-Intel	52%	100%
Golden Line	52%	100%
Tyumenneftegazsvyaz	75%	89%
TK Overta	100%	100%
Conversiya-Svyaz	100%	100%
CTK Contrast-Telecom	100%	100%
Unitel	100%	100%
AMT	46%	100%

The ownership interest of Comstar UTS in MGTS is determined by taking into account both the common and preferred (non-voting) shares of MGTS (Note 18).

Accounts of newly acquired subsidiaries have been consolidated or combined, as appropriate, in the Group's financial statements from the beginning of the year when control was acquired, with pre-acquisition earnings included in minority interests in the statements of operations.

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

Examples of significant estimates include the allowance for doubtful accounts, the recoverability of long-lived tangible and intangible assets, and valuation allowances on deferred tax assets.

Concentration of business risk - The Group's principal business activities are within the Russian Federation. Laws and regulations affecting businesses operating in the Russian Federation are subject to rapid changes and the Group's assets and operations could be at risk due to negative changes in the political and business environment.

Foreign currency translation - The Group follows a translation policy in accordance with Statement on Financial Accounting Standards ("SFAS") No. 52, "Foreign Currency Translation".

Management has determined that the functional currency of MGTS is the Russian ruble ("RUR"). Management believes that USD is still the appropriate functional currency of the other Group's entities, as the majority of their revenues, costs, capital expenditures and debt are either priced, incurred, payable or otherwise measured in USD.

The Group has selected the USD as its reporting currency and translates the financial statements of MGTS into USD. Assets and liabilities are translated at the exchange rates current at the balance sheet date, while income and expense items are translated at average rates of exchange prevailing during the year. The resulting translation loss of $3.6 million was recorded within other comprehensive income for the year ended December 31, 2005. For the year ended December 31, 2004, the Group recorded a translation gain of $13.5 million.

The official rate of exchange, as determined by the Central Bank of the RF, between the RUR and the USD at December 31, 2005 was 28.78 rubles to 1 U.S. dollar (December 31, 2004: 27.75).

The Russian ruble is not a fully convertible currency outside of the RF territory. The translation of ruble denominated assets and liabilities into U.S. dollars for the purpose of these financial statements does not indicate that the Group could realize or settle in U.S. dollars the reported values of the assets and liabilities. Likewise, it does not indicate that the Group could return or distribute the reported U.S. dollar values of capital and retained earnings to its shareholders.

Revenue recognition - The Group's revenues are principally derived from the provision of telecommunication services which consist of (i) monthly subscription fees, (ii) local traffic charges, (iii) connection fees, (iv) revenues from data transmission and internet services, (v) revenues from value-added and additional telecommunication services, (vi) revenues from services to other operators and (vii) revenues from payphones. The Group records revenues over the periods they are earned as follows:

(i) Monthly subscription fees are recognized in the month during which the telephone services are provided to customers;
(ii) Local traffic charges are recognized as the services are provided;
(iii) Upfront fees received for the connection of new subscribers are deferred and recognized over the expected subscriber relationship period. According to management estimates, the average subscriber relationship period for residential wireline voice phone subscribers of the Traditional fixed line communications segment is 15 years. For all other categories of subscribers, except for residential subscribers of the Group's broadband Internet services (see Note 2, Change in estimate), the subscriber relationship period is estimated at 3 to 5 years;
(iv) Revenues from the provision of data transmission and internet services are recognized when the services are provided to customers;
(v) Revenues derived from value-added and additional telecommunication services are recognized when the services are provided to customers;
(vi) Revenues from services to other operators are recognized when the services are provided to the operators; and
(vii) Revenues from payphones are recognized as the prepaid calling cards are used by the customers or expire.

Local telephone services provided by MGTS, totaling approximately 37% and 38% of the consolidated and combined revenues for the years ended December 31, 2005 and 2004, respectively, are regulated tariff services, and changes in rate structure are subject to the Federal Tariff's Service approval.

Management believes that the Group is not subject to the requirements of SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation" as the regulated rates for local telephone services provided by MGTS are not designed to recover the specific costs of providing the regulated services.

During the year ended December 31, 2004, MGTS was required to grant discounts ranging from 20% to 100% on installation and monthly fees to certain categories of residential subscribers, such as pensioners, military veterans and disabled individuals, and was entitled to reimbursement from the federal budget for these discounts. Due to the lack of certainty of reimbursement, MGTS accounted for such revenues upon collection. In the year ended December 31, 2004, the discounts provided by MGTS to its subscribers and not compensated by the federal budget amounted to $24.9 million. In accordance with the new legislation effective January 1, 2005, substantially all MGTS' subscribers are required to pay the full price for residential service, and those entitled to discounts are to receive reimbursement from the government rather than discounts from MGTS.

Change in estimate - Effective July 1, 2005, the Group has changed its estimates of average subscriber lives for residential subscribers of the broadband Internet services from 3 years to 1 year. The effect of this change in estimate in the year ended December 31, 2005 was an increase in net income of approximately $4.0 million, net of income tax.

Cash and cash equivalents - Cash and cash equivalents include cash on hand, amounts on deposit in banks and cash invested temporarily in various instruments with maturities of three months or less at the time of purchase.

Fair value of financial instruments - Financial instruments carried on the balance sheet include cash and bank balances, receivables, investments, accounts payable and debt. The particular recognition methods adopted are disclosed in the individual policy statements associated with each item.

Short-term financial instruments consist primarily of cash and bank balances, receivables, short-term investments, payables and short-term debt. The estimated fair value of such financial instruments as of December 31, 2005 approximated their carrying value.

Long-term financial instruments consist primarily of long-term investments and long-term debt.
It is not practicable for the Group to estimate the fair values of all of its long-term investments due to quoted market prices not being readily available and regular valuations are not being completed or obtained due to the excessive costs involved.

Fair values of corporate bonds issued by MGTS are disclosed in Note 14. As of December 31, 2005, the fair value of other fixed rate debt, including capital lease obligations and variable rate debt approximated carrying value.

Short-term investments - Short-term investments represent investments in promissory notes and time deposits, which have original maturities in excess of three months and mature within twelve months from the balance sheet date. These investments are being accounted for at amortized cost.
Management periodically assesses the recoverability of the carrying values of the investments and, if necessary, records impairment losses to write the investment down to fair value. For the years ended December 31, 2005 and 2004, no such impairments have occurred.

Accounts receivable - Accounts receivable are stated at their net realizable value after deducting an allowance for doubtful accounts. Such provisions reflect either specific cases or estimates based on evidence of collectibility.

Concentrations of credit risk with respect to trade receivables are limited due to a highly diversified customer base, which includes a large number of individuals, private businesses and state-financed institutions.

Prepaid expenses - Prepaid expenses are primarily comprised of advance payments for inventories, spare parts and services to vendors.

Value-added taxes - Value-added taxes (“VAT”) related to sales are payable to the tax authorities upon provision of services and issuance of an invoice to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales.

Inventories and spare parts - Inventories and spare parts comprise equipment for resale, cables and spare parts and are stated at the lower of cost or market. Cost is computed on a weighted average basis. The entities of the Group periodically assess their inventories and spare parts for obsolete or slow moving stock and write down slow-moving inventories and spare parts to their market value.

Assets held for sale - Assets held for sale comprise the cost of a building constructed by the Group with intention to sell to a third party.

Property, plant & equipment - For the Group's entities acquired by Sistema through business combinations accounted for by the purchase method, property, plant and equipment ("PP&E") were assigned their fair values at the date of acquisition by Sistema. If fair values of the identifiable net assets of the acquired entities exceeded acquisition cost, the fair values of non-current assets held by the acquired entities at the acquisition date, including PP&E, were reduced by such excess. All subsequent purchases of PP&E have been recorded at cost.

Property, plant and equipment transferred to MGTS free of charge (Note 17) are capitalized at their fair value at the date of transfer and deferred revenue is recorded and amortized to the consolidated and combined statements of operations over the contributed asset's life.

Cost includes major expenditures for improvements and replacements which extend useful lives of the assets or increase their revenue generating capacity. Repairs and maintenance are charged to the statements of operations as incurred.

The Group accounts for leases based on the requirements of SFAS No. 13, "Accounting for Leases". Leases are classified as capital leases whenever terms of the lease transfer substantially all of the benefits and rewards incident to the ownership. All other leases are classified as operating leases. Capital leases are recorded at the fair market value of the asset or the present value of future minimum lease payments, whichever is lower. The discount rate used in determining the present value of the minimum lease payments is the Group's incremental borrowing rate, unless (1) it is practicable to learn the implicit rate computed by the lessor and (2) the implicit rate is less than the Group's incremental borrowing rate. If both of those conditions are met, the interest rate implicit in the lease is used.

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

Property, plant and equipment are depreciated on a straight-line method utilizing estimated useful lives of the assets as follows:

Buildings	20-47 years
Telecommunication equipment	10-17 years
Cables and transmission devices	10-31 years
Motor vehicles	4-5 years
Office equipment and other	3-25 years

Leasehold improvements are depreciated on a straight-line basis over the shorter of their useful life or lease term.

Property, plant and equipment held and used by the Group is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may have been impaired. Recoverability of assets to be held and used is measured by comparison of the carrying amount of the assets to the future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. An impairment loss of $1.5 million has been recorded relating to equipment that was identified as obsolete during the year ended December 31, 2005.

The Group incurs costs associated with operating and other equipment, which require installation and related works to commence revenue generating activities. All costs necessarily incurred which are directly attributable to the construction, preparation and installation of an item to commence revenue generating activities are capitalized.

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

Asset retirement obligations - In accordance with SFAS No. 143, "Accounting for Asset Retirement Obligations", the Group calculates an asset retirement obligation and an associated asset retirement cost when the Group has a legal obligation in connection with the retirement of tangible long-lived assets. The Group's obligations under SFAS No. 143 arise from certain of its leases and relate primarily to the cost of removing equipment from such lease sites. As of December 31, 2005, the estimated assets retirement obligations were not significant to the Group's consolidated financial position and results of operations.

Intangible assets - Intangible assets are stated at acquisition cost. License costs are amortized on a straight-line basis over the license period starting from the date such license area becomes commercially operational. Amortization of other finite-life intangible assets, comprised mostly of billing systems and other software, is computed on a straight-line basis over five years.

Investments - Investments in businesses in which the Group does not have control, but exercises significant influence over operating and financial policies ("affiliates"), are accounted for using the equity method.

Prior to December 2005, MGTS owned 51% of voting common shares of Mediatel, with the remaining shares owned by Concern SITRONICS, a subsidiary of Sistema. Mediatel, a company incorporated in the RF, provides support and maintenance services for telecommunication equipment and software, primarily to the Group. In January 2004, MGTS entered into an agreement with Concern SITRONICS in respect of corporate governance of Mediatel that provides that control over the operating and financial policies of Mediatel (including, but not limited to, the rights to establish its operating and capital decisions, including budgets, and the rights to select and set the compensation of management responsible for implementation of these decisions) was transferred to Concern SITRONICS. The Group's investment in Mediatel was accounted for using the equity method of accounting in 2005 and 2004. In December 2005, MGTS sold 51% stake in Mediatel to Concern SITRONICS for cash consideration of $1.9 million.

Investments in corporate shares where the Group owns more than 20% of share capital, but does not have the ability or intent to control or exercise significant influence over operating and financial policies, as well as investments in corporate shares where the Group owns less than 20% of share capital, are accounted for at cost of acquisition. Management periodically assesses realizability of the carrying values of such investments.

The promissory notes purchased by the Group are carried at cost and a discount against the nominal value is accrued over the period to maturity, if it exceeds one year. A provision is made, based on management's assessment, for notes that are considered uncollectible.

Income taxes - Income taxes have been computed in accordance with the laws of the RF. Income tax rate in the RF equals 24%. In July 2004, amendments to Russian income tax legislation were enacted

to increase the income tax rate on dividends paid within Russia to 9% (previously 6%) effective January 1, 2005.

Deferred income taxes are accounted for under the liability method and reflect the tax effect of all significant temporary differences between the tax basis of assets and liabilities and their reported amounts in the combined financial statements. A valuation allowance is provided for deferred tax assets if it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Retirement benefit and social security costs - In Russia, all social contributions, including contributions to the pension fund, are substituted with the unified social tax ("UST") calculated by the application of a regressive rate from 26% to 2% (from 35.6% to 2% before January 1, 2005) of the annual gross remuneration of each employee. UST is allocated to three social funds, including the pension fund, where the rate of contributions vary from 20% to 2% (from 28% to 2% before January 1, 2005), respectively, depending on the annual gross salary of each employee.
The contributions are expensed as incurred.

MGTS has historically offered its employees certain benefits upon and after retirement. The cost of such benefits is recognized during an employee's years of active service (Note 16). The Group accounts for pension plans following the requirements of FAS No. 87, "Employers' Accounting for Pensions" and FAS No. 132R, "Employers' Disclosure about Pensions and Other Postretirement Benefits, an amendment of FASB Statements No. 87, 88 and 106".

Borrowing costs - Borrowing costs were recognized as an expense in the period in which they were incurred. Borrowing costs for assets that require a period of time to get them ready for their intended use are capitalized and amortized over the related assets' estimated useful lives. The capitalized borrowing costs for the years ended December 31, 2005 and 2004 amounted to $0.5 million and $0.8 million, respectively.

Advertising costs - Advertising costs are expensed as incurred and are reflected as a component of operating expenses within selling and marketing in the statements of operations (Note 20).

Subscriber acquisition costs - Subscriber acquisition costs represent the direct costs incurred to connect each new subscriber including dealer's commissions. The Group expenses these costs as incurred.

Minority interests - In the consolidated financial statements of the Group minority interests represent shares in book value of net assets of subsidiaries proportional to equity interests in those entities owned by shareholders other than Comstar UTS. In the combined financial statements presented for the periods prior to the Group's restructuring, minority interests represented shares in book value of net assets of the combined entities proportional to equity interests in those entities owned, directly or indirectly, by shareholders other than Sistema.

Distributions to shareholders - Dividends are recognized at the date they are declared. Distributable retained earnings of the Group are based on amounts extracted from statutory accounts of individual entities and may differ from amounts calculated on the basis of U.S. GAAP.

Earnings-per-share - Earnings-per-share are computed using the two-class method based on earnings for the period subsequent to the Group's restructuring (from November 22, 2005 to December 31, 2005). Net income available to Comstar UTS's shareholders for that period is divided by the weighted average number of common shares outstanding during the period.
Such earnings-per-share amount may not be comparable to earnings-per-share amounts determined in future years and, further, such earnings-per-share amount may not fully reflect the expected relationship between earnings for the year ended December 31, 2005 and the amount of outstanding stock as of that date.
Comprehensive income - Comprehensive income is defined as net income plus all other changes in net assets from non-owner sources.

New accounting pronouncements - In December 2004, the FASB issued FAS No. 153, "Exchanges of Nonmonetary Assets", an amendment of APB Opinion No. 29, "Accounting for Nonmonetary Transactions". FAS No. 153 eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets set in the APB Opinion No. 29 and replaces it with a general exception for exchanges that do not have commercial substance. FAS No. 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. FAS No. 153 is effective prospectively for nonmonetary exchanges occurring after June 15, 2005. The adoption of FAS No. 153 did not have a material impact on the Group's financial position or results of operations.

In December 2004, the Financial Accounting Standards Board ("FASB") issued FAS No. 123R, "Share-Based Payment" ("FAS No. 123R"), a revision of FAS No. 123, "Accounting for Stock-Based Compensation". FAS No. 123R supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" and requires all entities to recognize compensation cost in an amount equal to the fair value of share-based payments grant-date to employees. That cost is recognized over the period during which an employee is required to provide service in exchange for an award of equity instruments. FAS No. 123R must be adopted by most public entities no later than the beginning of the first fiscal year commencing after June 15, 2005. The adoption of FAS No. 123R did not have a material impact on the Group's financial position or results of operations.

In March 2005, FASB issued Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations - an interpretation of FASB Statement No. 143." This Interpretation clarifies that the term "conditional asset retirement obligation" as used in FASB Statement No. 143, "Accounting for Asset Retirement Obligations", refers to a legal obligation to perform an asset retirement activity, in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Uncertainty about the timing and (or) method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists to make a reasonable estimate of the fair value of the obligation. Interpretation 47 is effective for the Group beginning January 1, 2006.
The adoption of Interpretation 47 did not have a material impact on the Group's financial position or results of operations.

In March, 2005, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin ("SAB") No. 107, "Share Based Payment". SAB 107 summarizes the views of the SEC staff regarding the interaction between SFAS 123R and certain SEC rules and regulations, and provides the staff's views regarding the valuation of share−based payment arrangements for public companies. The Group adopted SAB 107 concurrently with the adoption of SFAS 123(R) with effect from January 1, 2006. The adoption of SAB 107 did not have a material impact on the Group's financial position or results of operations.

In May 2005, the FASB issued FAS No. 154, "Accounting Changes and Error Corrections", which replaces APB Opinion No. 20, "Accounting Changes" and FAS No. 3, "Reporting Accounting Changes in Interim Financial Statements". FAS No. 154 changes the requirements for the accounting and reporting of a change in accounting principle and is applicable to all voluntary changes and to changes required by an accounting pronouncement if such pronouncement does not specify transition provisions. FAS No. 154 requires retrospective application to the prior periods' financial statements of changes in accounting principle. In cases when it is impracticable to determine the period-specific or cumulative effects of an accounting change, the statement provides that the new accounting principle should be applied as of the earliest period for which retrospective application is practicable or, if impracticable to determine the effect of a change to all prior periods, prospectively from the earliest date practicable. This Statement is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

In June 2005, the EITF reached a consensus on EITF Issue No. 05-6, "Determining the Amortization Period for Leasehold Improvements." As part of a business combination, the acquiring entity will often assume existing lease agreements of the acquired entity and acquire the related leasehold improvements. The issues are whether the "lease term" should be reevaluated at consummation of a purchase business

combination and whether the amortization period for acquired leasehold improvements should be reevaluated by the acquiring entity in a business combination. The consensus reached by EITF No. 05-6 is effective for leasehold improvements that are purchased or acquired in reporting periods beginning after June 29, 2005.

In October 2005, the FASB issued FASB Staff Position ("FSP") FAS 13-1, "Accounting for Rental Costs Incurred during a Construction Period". Under the provisions of FSP FAS 13-1, lessees may not capitalize rental costs incurred on building or ground operating leases during a construction period. Instead, rental costs should be expensed on a straight-line basis starting at the beginning of the lease term, i.e., when the lessee takes possession of or is given control of the leased property. The provisions of FSP FAS 13-1 are effective starting with the first reporting period beginning after December 15, 2005. The adoption of FSP FAS 13-1 did not have a material effect on the Group's financial position or results of operations.

3. DISCONTINUED OPERATIONS

During 2003, Sistema made a decision to discontinue the operations of P-Com, a subsidiary of the Group. In August 2004, the Group sold its 83.25% of P-Com's voting common shares to Sky-Link, an affiliate of Sistema, for cash consideration of $16.0 million.

In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" the financial statements of the Group reflect P-Com's business as discontinued operations for the year ended December 31, 2004. Accordingly, assets, liabilities and income and expense items of P-Com have been excluded from the respective captions in the statement of operations and have been reported as gain or loss from discontinued operations, net of applicable taxes for the year ended December 31, 2004.

Revenues from discontinued operations and income from discontinued operations before income taxes and minority interest for the year ended December 31, 2004 (prior to the date of disposal) were $32.4 million and $8.4 million, respectively.

4. ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES AND AFFILIATES

Acquisition of minority interest in Telmos

In February 2005, Sistema acquired an additional 20% equity stake in Telmos from Rostelecom for a total cash consideration of $8.5 million, increasing its voting power in Telmos to 100%.
In September 2005, Comstar UTS purchased the 20% stake in Telmos from Sistema for a total cash consideration of $12.8 million. The excess of purchase price over the respective share in net assets of Telmos of $4.3 million was recorded as a decrease in the Group's additional paid-in capital.

Investment in Metrocom

In September 2005, Comstar UTS completed the purchase of a 45% stake in Metrocom, a leading alternative fixed line operator in St-Petersburg, for a total cash consideration of $12.2 million.
At December 31, 2005, Comstar UTS's investment exceeded its underlying equity in the net assets of Metrocom by $7.6 million.

Acquisitions of controlling interests in regional fixed line operators

In the fourth quarter of 2005, as a part of its program of regional expansion, the Group has acquired controlling interests in a number of alternative fixed-line operators in certain regions of Russia. The acquisitions were accounted for using the purchase method of accounting. The purchase price allocations have not been finalized as of the date of these financial statements.

In October 2005, Comstar UTS acquired 89.4% of the ordinary shares and 31.9% of the preferred shares of Tyumenneftegazsvyaz, a leading alternative fixed line telecommunications services provider operating in the Tyumen region, as well as in the autonomous districts of Khanty Mansi and Yamalo Nenets, for $9.1 million in cash. The preliminary purchase price allocation was as follows:

		(000's)
Current assets	$	3,642
Non-current assets		14,697
Current liabilities		(5,107)
Non-current liabilities		(1,688)
Minority interests		(2,465)
Purchase price	**$**	**9,079**

In December 2005, Comstar UTS acquired all of the shares of Conversiya Svyaz and Overta, two leading alternative fixed-line operators in the Saratov region, for $9.0 million in cash and $1.0 million in a deferred cash payment. The preliminary purchase price allocation was as follows:

		(000's)
Current assets	$	3,359
Non-current assets		9,053
Current liabilities		(652)
Non-current liabilities		(1,734)
Purchase price	**$**	**10,026**

In December 2005, Comstar UTS completed the purchase of 100% of shares of CTK Contrast Telecom, an alternative fixed-line operator in the Moscow region, for $5.6 million in cash. The preliminary purchase price allocation was as follows:

		(000's)
Current assets	$	2,065
Non-current assets		3,600
Current liabilities		(101)
Purchase price	**$**	**5,564**

In December 2005, Comstar UTS acquired all of the shares of Unitel, an alternative fixed-line operator in the Moscow region, for $4.5 million in cash. The preliminary purchase price allocation was as follows:

		(000's)
Current assets	$	466
Non-current assets		4,588
Current liabilities		(533)
Purchase price	**$**	**4,521**

Pro forma results of operations (unaudited)

The following pro forma financial data for the years ended December 31, 2005 and 2004 give effect to the acquisition of Tyumenneftegazsvyaz, Conversiya Svyaz, Overta, CTK Contrast Telecom and Unitel, as if they had occurred as of January 1, 2004:

	(000's)			
		2005		**2004**
Operating revenues	$	907,624	$	725,691
Operating income		268,351		176,966
Net income		108,839		77,886

The pro forma information is based on various assumptions and estimates. The pro forma information is not necessarily indicative of the operating results that would have occurred if the Group's acquisitions had been consummated at the beginning of the respective period, nor is it necessarily indicative of future operating results. The pro forma information does not give effect to any potential revenue enhancements or cost synergies or other operating efficiencies that could result from the acquisitions.

Other acquisitions and disposals of subsidiaries and affiliates

In June 2004, 100% of voting common shares of MTU-Inform Plus were sold to Sistema Mass Media, a subsidiary of Sistema, for $0.2 million. Subsequent to the sale, the name of the company was changed to Sistema Multimedia. The Group retained control over Sistema Multimedia operations. In December 2005, Sistema Multimedia was merged into MTU-Intel (Note 1).
As a result of the merger, Comstar UTS's ownership in MTU-Intel decreased from 100% to 52%. The remaining shares of the merged entity are held by Sistema Mass Media. The respective share of MTU-Intel's net assets in the amount of $8.5 million was recorded as minority interest and a concurrent decrease in the Group's additional paid-in capital.

In October 2004, MGTS sold shares of MCC to Sky-Link, an affiliate of Sistema, for $0.7 million in cash. As a result of this transaction, the Group recognized a loss from disposal of an affiliate of $6.6 million.

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of December 31, 2005 and 2004 consisted of the following:

	December 31, 2005	December 31, 2004
Cash	$ 45,699	$ 32,837
Cash equivalents:		
Promissory notes	20,798	30,535
Deposits	6,428	3,935
Other	1,714	129
	28,940	34,599
Total	**$ 74,639**	**$ 67,436**

Promissory notes with original maturities less than three months, included in cash equivalents as of December 31, 2005 are comprised of Ruble-denominated promissory notes of $12.7 million and USD-denominated promissory notes of $8.1 million. The weighted average interest rate on promissory notes, included in cash equivalents as of December 31, 2005 was 1.9%.

Cash and cash equivalents with the Moscow Bank of Reconstruction and Development ("MBRD"), a subsidiary of Sistema, as of December 31, 2005 and 2004 amounted to $45.1 million and $45.5 million, respectively.

6. SHORT-TERM INVESTMENTS

Short-term investments as of December 31, 2005 and 2004 consisted of the following:

	December 31, 2005	December 31, 2004
RUR-denominated time deposits in MBRD	$ 52,116	$ 19,821
USD-denominated time deposits in MBRD	4,600	4,600
Promissory notes from other subsidiaries and affiliates of the controlling shareholder:		
Sistema Telecom	37,036	34,828
Sky-Link	11,845	26,277
MBRD	5,603	12,081
P-Com	3,822	5,087
Other	1,112	1,188
	116,134	103,882
Promissory notes from third parties	-	1,431
Total	**$ 116,134**	**$ 105,313**

The interest rates of RUR-denominated time deposits in MBRD vary from 6.5% to 7.9%. USD-denominated time deposits in MBRD have the original term of nine months and bear interest of 7.0% per annum.

Sistema Telecom's promissory notes include $16.8 million of RUR-denominated notes and $20.2 million of USD-denominated notes. Interest rates vary from 0.7% to 4.0%.

Sky-Link's promissory notes include a RUR-denominated note of $6.8 million and a USD-denominated note of $5.1 million. USD-denominated promissory note is interest free, RUR-denominated note bears interest-rate of 11.0%.

MBRD's USD-denominated promissory notes bear interest rates from 4.5% to 6.0%. P-Com's RUR-denominated promissory note is interest-free.

As of December 31, 2004, Telmos held three RUR-denominated, substantially interest free, unsecured promissory notes of a party, controlled by Sistema. Two notes with a face value equivalent to $2.3 million and $2.2 million were repayable on demand but not earlier than March and June 2012, respectively. Another note with a face value equivalent to $1.0 million was repayable on demand but not earlier than November 2006. As repayment of those notes was considered doubtful, the Group recognized impairment loss equal to the carrying value of the promissory notes. In September 2005, the notes were disposed to a subsidiary of Sistema for a cash consideration of $5.5 million. The gain from disposal was recorded in additional paid-in capital.

7. TRADE RECEIVABLES, NET

Trade receivables, net of provision for doubtful debts, as of December 31, 2005 and 2004 consisted of the following:

		December 31, 2005		December 31, 2004
Trade receivables	$	87,697	$	69,563
Provision for doubtful receivables		(9,387)		(6,059)
Total	$	**78,310**	$	**63,504**

Trade receivables as of December 31, 2005 and 2004 include receivables from subsidiaries and affiliates of Sistema of $16.6 million and $13.5 million, respectively, of which receivables from Sky-Link's subsidiaries (P-Com and MCC) amounted to $14.1 million and $11.0 million, respectively.

8. OTHER RECEIVABLES AND PREPAID EXPENSES

Other receivables and prepaid expenses as of December 31, 2005 and 2004 consisted of the following:

		December 31, 2005		December 31, 2004
VAT recoverable	$	42,485	$	34,718
Other taxes receivable		4,688		4,555
Prepayments for services		9,657		8,670
Other receivables		23,742		12,726
Total	$	**80,572**	$	**60,669**

9. INVENTORIES AND SPARE PARTS

Inventories and spare parts as of December 31, 2005 and 2004 consisted of the following:

	December 31, 2005	December 31, 2004
Equipment for resale	$ 8,816	$ 5,888
Spare parts and other materials	18,065	17,116
Total	**$ 26,881**	**$ 23,004**

10. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment, net of accumulated depreciation, as of December 31, 2005 and 2004 consisted of the following:

	December 31, 2005	December 31, 2004
Buildings and site improvements	$ 222,627	$ 206,577
Switches and transmission devices	964,141	815,698
Other fixed assets	175,863	170,256
Construction in progress and equipment for installation	143,425	135,661
Property, plant and equipment, cost	1,506,056	1,328,192
Less: accumulated depreciation	(361,907)	(296,435)
Total	**$ 1,144,149**	**$ 1,031,757**

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

The depreciation charge for the years ended December 31, 2005 and 2004 amounted to $85.9 million and $74.8 million, respectively.

11. INTANGIBLE ASSETS, NET

Intangible assets, net of accumulated amortization, as of December 31, 2005 and 2004 consisted of the following:

	December 31, 2005			December 31, 2004		
	Gross carrying value	Accu-mulated amorti-zation	Net carrying value	Gross carrying value	Accu-mulated amorti-zation	Net carrying value
Licenses	$ 9,135	$ (1,458)	$ 7,677	$ 4,130	$ (401)	$ 3,729
Customer base	8,822	-	8,822	-	-	-
Billing systems and other software	64,332	(28,945)	35,387	44,897	(22,532)	22,365
Other	5,359	(1,890)	3,469	4,542	(396)	4,146
Total intangible assets, net	**$ 87,648**	**$ (32,293)**	**$ 55,355**	**$ 53,569**	**$ (23,329)**	**$ 30,240**

Amortization expense recorded on intangible assets for the years ended December 31, 2005 and 2004 amounted to $8.1 million and $4.5 million, respectively. Based on the intangible assets existing at December 31, 2005, the estimated amortization expense for each of the five succeeding years and thereafter is as follows:

Year ended December 31,	$
2006	16,453
2007	12,950
2008	10,672
2009	8,580
2010	4,843
Thereafter	1,857
Total	**$ 55,355**

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

12. LONG-TERM INVESTMENTS

Long-term investments as of December 31, 2005 and 2004 consisted of the following:

	December 31, 2005			**December 31, 2004**		
	Ownership, %		**Investment**	**Ownership, %**		**Investment**
Metrocom	45%	$	12,773	-		-
MBRD	6%		5,514	6%	$	5,720
Other investees, at cost	various		1,332	various		1,451
MBRD RUR-denominated deposits			10,640			-
P-Com RUR-denominated promissory notes			-			3,964
Interest free loans to investees			251			155
Total		**$**	**30,510**		**$**	**11,290**

MBRD RUR-denominated deposits mature in 2007-2008 and bear interest rate at 9.3% per annum.

13. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities as of December 31, 2005 and 2004 consisted of the following:

		December 31, 2005		**December 31, 2004**
Accrued payroll and applicable taxes	$	14,604	$	13,300
Accrued interest		2,046		3,664
Dividends payable		384		344
Other current liabilities		26,375		6,312
Total	**$**	**43,409**	**$**	**23,620**

14. DEBT OBLIGATIONS

The Group's debt obligations as of December 31, 2005 and 2004 consisted of the following:

	Currency	Annual interest rate (Actual at December 31, 2005)	December 31, 2005	December 31, 2004
MGTS Bonds 5th issue	RUR	8.3%	$ 52,115	-
MGTS Bonds 4th issue	RUR	10.0%	52,115	$ 54,057
MGTS Bonds 3rd issue	RUR	-	-	36,038
Total corporate bonds			104,230	90,095
ABN Amro	USD	LIBOR+3.0% (7.5%)	20,000	-
Citibank	USD	LIBOR+1.6% (6.3%)	21,227	15,144
MBRD	USD	11.0%	2,996	5,000
Vneshtorgbank	Euro	highest of 7.5% or EURIBOR+5.4% (8.6%)	13,107	9,908
Vneshtorgbank	USD	LIBOR+4.9% (9.6%)	2,920	7,073
Commerzbank	Euro	4.0%	2,708	-
Alfa Bank	USD	12.5%	-	1,517
Sberbank	RUR	-	-	12,613
Sistema Mass Media	RUR	-	-	6,994
Raiffeisenbank	USD	-	-	3,750
Vnesheconombank	USD	-	-	2,216
Long-term portion of vendor financing	various	various	5,190	14,996
Short-term portion of vendor financing	various	various	11,070	18,570
Other	various	various	5,353	2,222
Total debt			188,801	190,098
Less: amounts maturing within one year			(86,617)	(85,616)
Debt, net of current portion			**$ 102,184**	**$ 104,482**

Corporate bonds - In May 2005, MGTS issued 5-year RUR-denominated bonds (fifth issue) with a face value of RUR 1,500 million (equivalent to $52.1 million as of December 31, 2005). The bonds carry a coupon of 8.3% per annum. MGTS made an unconditional offer to repurchase the bonds at par value in May 2010.

In April 2004, MGTS issued 5-year RUR-denominated bonds (fourth issue) with the face value of RUR 1,500 million (equivalent to $52.1 million as of December 31, 2005). The bonds carried a coupon of 10.0% per annum. MGTS made an unconditional offer to repurchase the bonds at par value in April 2006.

In February 2003, MGTS issued 2-year RUR-denominated bonds (third issue) with a face value of RUR 1,000 million (equivalent to $34.7 million as of December 31, 2005) due in 2005. The bonds carry coupon of 12.3% during the first year of trading and 17.0% during the second year. MGTS fully repaid the bonds in February 2005.

As of December 31, 2005, the fair value of the bonds was approximately $103.8 million and ranged from 99.1% to 100.2% of the principal amount.

ABN Amro - In September 2005, Comstar UTS entered into a credit line with ABN Amro Bank limited to $20.0 million. The credit line bears interest of LIBOR+2.95% per annum and is repayable in seven equal consecutive quarterly installments with the last payment in September 2007. The credit line was opened to finance acquisitions. The credit line is fully and unconditionally guaranteed by MTU-Inform. As of December 31, 2005, the amount outstanding under the credit line was $20.0 million.

The credit line is subject to certain restrictive covenants including, but not limited to, limitations on the amount of dividends paid, loans issued to parties other than Sistema Telecom and acquisitions and investments made at terms different from the market. In addition, the Interest Cover Ratio of the Group should not be less than 3:1 and the Total Debt to EBITDA rate should not exceed 3:1.

Citibank - During three years ended December 31, 2005 MGTS entered into four credit facilities with Citibank for a total amount of $25.1 million. All facilities bear interest of LIBOR+1.6% and are repayable in 8 semi-annual installments with the last payments in 2008 – 2010. These credit facilities were opened to finance acquisitions of equipment from STROM Telecom, a subsidiary of Sistema. The facilities are collateralized by equipment with approximate carrying amount of $16.9 million as of December 31, 2005, a deposit of $2.3 million in Citibank and are guaranteed by Export Guarantee and Insurance Corporation of the Czech Republic. As of December 31, 2005, the amount outstanding under these facilities was $21.2 million.

Based on restrictive covenants of the Citibank loan agreements, the Debt to Equity ratio and Debt Service to Earnings before Interest and Taxes (“EBIT”) ratio of MGTS should not exceed 3:1 and its aggregate debt may not exceed $250.0 million. The written approval of Citibank is required for MGTS to obtain borrowings individually exceeding $30.0 million (apart from the Sberbank loan, Raiffeisenbank loan and MGTS bonds) or alienate more than 10% of its assets.

MBRD - In March and July 2005, Sistema Multimedia entered into two credit facilities with MBRD for a total of $13.7 million. The balance under the facilities as of December 31, 2005 was $3.0 million. Both facilities are guaranteed by Sistema, bear interest of 11.0% per annum and mature in stages from 2008 to 2011.

Vneshtorgbank - In March 2005, MGTS entered into a credit agreement with Vneshtorgbank for an amount of Euro 5.3 million (equivalent of $6.2 million as of December 31, 2005) to finance acquisition of equipment. The loan matures in September 2010 and bears interest at Euribor+5.0% per annum. Equipment with approximate carrying value of $5.7 million is pledged to collateralize the outstanding balance under the agreement. As of December 31, 2005, the amount outstanding under the agreement was $6.2 million.

In July 2004, MGTS entered into two credit agreements for a total amount of Euro 7.3 million (equivalent of $8.6 million as of December 31, 2005) to finance the acquisition of equipment. The loans mature in January 2010 and bear interest at the highest of Euribor+5.4% or 7.5%. Equipment with approximate carrying value of $7.6 million is pledged to collateralize the outstanding balance under these agreements. As of December 31, 2005, the amount outstanding under these credit agreements was $6.9 million.

During the year ended December 31, 2002, the Group received a number of loans from Vneshtorgbank maturing in 2005-2006 to finance working capital. As of December 31, 2005, $2.9 million was outstanding under these loans. The loans are collateralized by equipment with an approximate carrying value of $3.3 million. The weighted average interest rate on the loans outstanding as of December 31, 2005 was 9.6% per annum.

Commerzbank **-** In December 2004, Sistema Multimedia entered into a credit line agreement with Commerzbank for Euro 5.5 million (equivalent of $6.5 million as of December 31, 2005). The loan bears interest of 4.0% per annum and matures in 2010. As of December 31, 2005, $2.7 million was outstanding under this credit line.

Alfa Bank **-** In December 2002, Golden Line obtained a USD-denominated credit facility from Alfa Bank bearing annual interest at the rate of 12.5%. The facility limit was $4.0 million. MTU-Inform guaranteed this credit facility and pledged equipment with the fair value of $4.7 million. The facility was fully repaid in November 2005.

Sberbank credit facilities **-** In September 2004, MGTS entered into a credit line with Sberbank for 600 million RUR ($20.8 million as of December 31, 2005) for general corporate purposes. The loan matures in 2007. The interest rate of the credit line depends on the gross cash flow on MGTS account opened in Sberbank, and was 11% per annum as of December 31, 2005. The loan was fully repaid in June 2005.

In December 2000, MGTS signed a credit facility with Sberbank for a total amount equivalent to $90.0 million to refinance its obligations under Eurobond borrowings. The loan was received in three tranches during the first quarter of 2001. In September 2002, MGTS prolonged repayment of the outstanding balance to the first quarter of 2005. The interest rate on the prolonged loan was 18% during the first six months and 12% during the second six months of the year. The loan was fully repaid in February 2005.

Vendor financing **-** Foreign suppliers of telecommunications equipment provide uncollateralized commercial credit to the Group denominated in various currencies on short-term and long-term bases, mostly interest free. The present value of the obligations under vendor financing agreements was determined using the Group's incremental borrowing rate at the date of transaction.

The loan repayments over future periods are as follows:

Year ended December 31,		
2006	$	86,617
2007		27,327
2008		9,177
2009		6,621
2010		59,059
Total	**$**	**188,801**

As of December 31, 2005, the Group is in compliance with all existing restrictive provisions of its debt obligations.

15. CAPITAL LEASE OBLIGATIONS

Capital lease obligations as of December 31, 2005 and 2004 consisted of the following:

		December 31, 2005		December 31, 2004
Total capital lease obligations	$	44,815	$	26,699
Less: current portion		(14,050)		(6,782)
Capital lease obligations, net of current portion	**$**	**30,765**	**$**	**19,917**

MGTS and Telmos enter into contracts for the lease of telecommunication equipment with Raiffeisen Leasing, MMB-Leasing and InvestSvyazHolding, a subsidiary of Sistema.
The agreements expire in 2006-2009 and assume transfer of ownership for equipment to the Group after the last lease payment is effected.

In February 2005, Sistema Multimedia entered into a contract for the lease of equipment with BSGV Leasing. After the legal merger with MTU-Intel in December 2005, the rights and obligations under the agreement were transferred to MTU-Intel. The agreement expires in 2009 and assumes transfer of ownership of this equipment to the Group after the last lease payment is effected.

The net book value of leased assets comprised $69.0 million and $42.7 million as of December 31, 2005 and 2004, respectively. Interest expense accrued on capital lease obligations for the years ended December 31, 2005 and 2004, and amounted to $2.9 million and $2.5 million, respectively.

The following table presents future minimum lease payments under finance leases together with the present value of the net minimum lease payments as of December 31, 2005:

Year ended December 31,		
2006	$	17,836
2007		15,897
2008		12,391
2009		6,158
Total minimum lease payments (undiscounted)		52,282
Less: amount representing interest		(7,467)
Total present value of net minimum lease payments	**$**	**44,815**

16. RETIREMENT AND POST-RETIREMENT BENEFITS

MGTS has historically provided certain benefits to employees upon their retirement and afterwards. Currently the main features under the defined benefit pension program include the following:

Monthly regular pension - Employees retiring with at least fifteen years of service receive lifetime payments varying from RUR 3,600 (equivalent of USD 125 as of December 31, 2005) to RUR 50,400 (equivalent of USD 1,751 as of December 31, 2005) per year depending on the employee’s actual years of service and qualification;

Death-in-service - Lump-sum payment of RUR 15,000 (equivalent of USD 521 as of December 31, 2005), payable upon death of an employee, irrespective of past service;

Lump-sum upon retirement - Lump-sum payment upon retirement of employees with at least five years of service varying from RUR 3,700 (equivalent of USD 129 as of December 31, 2005) to RUR 22,200 (equivalent of USD 771 as of December 31, 2005) depending on an employee’s actual years of service;

Monthly telephone subsidy - Qualifying pensioners (those who served more than 30 years at MGTS) receive a 50% subsidy (approximately USD 3.5 per month as of December 31, 2005) for their monthly telephone bills from MGTS; and

Death-while-pensioner - MGTS pays lump-sum benefits to the relatives of deceased pensioners of up to RUR 10,000 (equivalent of USD 347 as of December 31, 2005).

MGTS' pension obligations are measured as of December 31. The following are the key assumptions used in determining the projected benefit obligation and net periodic pension expense:

Discount rate	9.2%
Future salary increases	9.2%
Future pension increases	0.0%
Average life expectancy of members from date of retirement	17 years

The change in the projected benefit obligation and the change in plan assets are presented in the following table:

	Year ended December 31,	
	2005	**2004**
Projected benefit obligation, beginning of the year	$ 13,550	$ 6,034
Service cost	2,914	1,601
Interest cost	1,441	634
Plan amendments	-	4,488
Actuarial losses	2,118	855
Benefit payments	(668)	(433)
Foreign currency translation effect	(487)	371
Projected benefit obligation, end of the year	18,868	13,550
Less: fair value of plan assets	(2,652)	(2,037)
Unfunded status of the plan, end of the year	**$ 16,216**	**$ 11,513**

The increase in projected benefit obligation due to plan amendment in the year ended December 31, 2004 relates to the increase in the base rate used to determine the monthly payments to the retired employees. The changes in the projected benefit obligation due to actuarial losses for the years ended December 31, 2005 and 2004 relate primarily to the changes in the discount rate and employees turnover assumptions.

The accumulated benefit obligation as of December 31, 2005 and 2004 was $16.2 million and $11.5 million, respectively.

The components of the net periodic benefit costs for the years ended December 31, 2005 and 2004 are as follows:

	Year ended December 31,	
	2005	**2004**
Service cost	$ 2,914	$ 1,601
Interest cost	1,441	634
Net periodic benefit cost	**$ 4,355**	**$ 2,235**

The Group's management expects contributions to the plan during the year ended December 31, 2006 to amount to $0.9 million.

The future benefit payments to retirees under the defined benefit plan are expected as follows:

Year ended December 31,		
2006	$	4,499
2007		1,436
2008		1,370
2009		1,310
2010		1,257
2011-2015		4,365
Thereafter		1,979
Total	**$**	**16,216**

The plans assets for lifetime payments to employees retiring after January 1, 2004, are managed by Sistema Pension Fund, a subsidiary of Sistema.

17. PROPERTY, PLANT AND EQUIPMENT CONTRIBUTIONS

In the course of its business the Group receives telecommunication infrastructure which is intended to operate as an integral part of the Moscow city wire line network from the real estate constructors free of charge as provided by the regulations of the city government. Property, plant and equipment contributions received by the Group during the years ended December 31, 2005 and 2004 were as follows:

	Year ended December 31,	
	2005	**2004**
Property, plant and equipment, beginning of the year	$ 103,822	$ 88,388
Contributions received during the year	6,268	13,597
Foreign currency translation effect	(3,729)	4,993
Deferred revenue amortized	(3,615)	(3,156)
Property, plant and equipment, end of the year	**$ 102,746**	**$ 103,822**

18. SHARE CAPITAL

As of December 31, 2005, Comstar UTS' share capital comprised of 278,940,860 shares with par value of 1 Ruble, and amounted to $18,982. As a result of the Group's reorganization, MGTS owns 57,742,500 shares of Comstar UTS that are accounted for in these consolidated financial statements as treasury stock and are recorded at par value.

Share capital as of December 31, 2004 was comprised of the share capitals of the combined entities as follows:

	Number of shares, authorised, issued and outstanding	Par value, Rubles		Amount
MGTS:				
Preferred stock	15,965,850	40	$	22,538
Common stock	79,829,200	40		112,462
Comstar UTS	23,021,000	1		10,088
MTU-Inform	1,000	10		1
Telmos	15,370	2,000		11,335
MTU-Intel	21,457	5		5
Sistema Multimedia	-	-		-
Less: cross holdings and minority interests				(84,296)
Total			**$**	**72,133**

MGTS' preferred shares carry guaranteed dividend rights amounting to the higher of (a) 10% of MGTS' net profit as determined under Russian accounting regulations and (b) the dividends paid on common shares. No dividends may be declared on common shares before dividends on preferred shares are declared. If the preferred dividend is not paid in full in any year the preferred shares also obtain voting rights, which will lapse after the first payment of the dividend in full. Otherwise, preferred shares carry no voting rights except on resolutions regarding liquidation or reorganization of MGTS and changes/amendments to MGTS' charter restricting the rights of holders of preferred shares. Such resolutions require the approval of 75% of the preferred shareholders. In the event of liquidation, dividends to preferred shareholders that have been declared but not paid have priority over ordinary shareholders.

19. OPERATING REVENUES

Operating revenues for the years ended December 31, 2005 and 2004 consisted of the following:

	Year ended December 31,	
	2005	**2004**
Alternative fixed line communications		
Moscow metropolitan area		
Corporates		
Voice	$ 72,155	$ 73,396
Data and internet	67,785	50,820
Value-added services	6,208	4,884
Other	2,798	2,404
Residential		
Voice	1,678	942
Data and internet: broadband	42,323	9,682
dial-up	20,034	25,097
Other	4,889	1,566
Operators	105,913	102,731
Other	13,950	10,151
Other regions of the RF	31,395	-
	369,128	**281,673**
Traditional fixed line communications		
Residential		
Voice	226,840	156,094
Payphones	2,383	8,008
Additional telecommunication services	9,230	5,268
Other	2,502	2,061
Corporates		
Voice	129,153	125,403
Access node / Trunks rental	33,678	19,215
Additional telecommunication services	12,428	9,907
Other	13,776	7,179
Operators	108,506	80,325
	538,496	**413,460**
Total	**$ 907,624**	**$ 695,133**

20. OPERATING EXPENSES

Operating expenses for the years ended December 31, 2005 and 2004 consisted of the following:

	Year ended December 31,	
	2005	2004
Employee costs	$ 237,147	$ 198,190
Depreciation and amortization	90,437	76,138
Repairs and maintenance	69,746	67,145
Network traffic	50,592	31,002
Taxes other than income taxes	33,839	29,528
Utilities and energy	17,659	16,443
Rent	18,200	16,006
Selling and marketing	27,836	19,452
Bank charges	10,567	9,109
Insurance	10,749	7,684
Transportation	9,181	3,343
Allowance for doubtful accounts	4,503	(243)
Impairment of property, plant and equipment	1,513	-
Insurance coverage	(5,806)	-
Cost of equipment sold	10,502	5,394
Other	52,608	42,223
Total	**$ 639,273**	**$ 521,414**

In February 2003, a fire occurred in one of MGTS' switching stations, significantly damaging Telmos' and MGTS' equipment. As a result of the fire, 40,000 telephone lines were damaged. The net book value of the damaged equipment and equipment that became obsolete as a result of replacement of the damaged equipment amounted to $9.7 million, including the net book value of leased equipment of $1.4 million. The damaged equipment of Telmos was insured by Rosno, a subsidiary of Sistema, and Rossia Insurance Co ("Rossia"). Telmos received insurance coverage of $1.7 million from Rosno and entered in coverage litigation with Rossia seeking compensation of damages in amount of $5.8 million. Additionally, MGTS has filed a claim against a third party seeking compensation of damages caused by a fire in the amount of approximately $8.7 million. Moscow arbitration court and, subsequently, courts of appeal ruled in favour of the Group in its litigation with Rossia regarding the insurance coverage for the equipment damaged as a result of the fire. During the third quarter of 2005, the Group has collected insurance recovery in amount of $5.8 million and recognized a gain in the same amount.

21. INCOME TAX EXPENSE

The Group's provision for income taxes for the years ended December 31, 2005 and 2004 was as follows:

	Year ended December 31,	
	2005	2004
Current taxes	$ 65,125	$ 39,623
Deferred taxes	(5,796)	1,453
Total	**$ 59,329**	**$ 41,076**

The provision for income taxes is different from that which would be obtained by applying the statutory income tax rate to net income before income tax and minority interests. The items causing this difference are as follows:

	Year ended December 31,	
	2005	2004
Income tax charge computed on income before taxes at standard rate applicable to the Group of 24%	$ 61,885	$ 38,574
Change in valuation allowance	(4,868)	(3,645)
Foreign currency transactions differences	(1,290)	1,007
Non-deductible expenses	3,602	5,140
Total	**$ 59,329**	**$ 41,076**

Temporary differences between the tax and accounting bases of assets and liabilities give rise to the following deferred tax assets and liabilities at December 31, 2005 and 2004:

	December 31, 2005	December 31, 2004
Deferred tax assets		
Deferred connection fees	$ 39,020	$ 36,220
Property, plant and equipment contributions	24,659	24,917
Valuation of property, plant and equipment	35,613	36,681
Allowance for doubtful accounts	654	3,758
Accrued operating expenses	5,188	3,164
Post-retirement benefits	3,892	2,763
Tax losses carryforward	1,324	1,607
Other	353	2,272
Less: valuation allowance	(30,144)	(35,012)
Total	**80,559**	**76,370**
Deferred tax liabilities		
Depreciation of property, plant and equipment	$ (71,156)	$ (70,210)
Other	(1,129)	(3,590)
Total	**$ (72,285)**	**$ (73,800)**
Net deferred tax assets, current portion	$ 13,432	$ 15,693
Net deferred tax assets, long-term portion	3,847	6,274
Net deferred tax liabilities, long-term portion	(9,005)	(19,397)

Deferred tax assets relating to tax losses carried forward in amount of $1.3 million as of December 31, 2005 expire in 2012 and are attributable to MTU-Inform.

22. SEGMENT INFORMATION

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", established standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Group's management evaluates performance of the segments based on operating income.

An analysis and reconciliation of the Group's business segment information to the respective information in the financial statements for the years ended December 31, 2005 and 2004 is as follows:

	Year ended December 31, 2005		
	Alternative fixed line communication services	**Traditional fixed line communication services**	**Total**
Net sales to external customers	$ 369,128	$ 538,496	$ 907,624
Intersegment sales	3,706	101,157	104,863
Depreciation and amortization	(30,030)	(60,407)	(90,437)
Operating income	64,721	206,357	271,078
Interest income	3,923	3,773	7,696
Interest expense	(2,926)	(15,035)	(17,961)
Income tax expense	(17,962)	(41,367)	(59,329)
Segment assets	457,502	1,232,862	1,690,364
Cash and cash equivalents	47,157	27,482	74,639
Indebtedness [(a)]	(39,862)	(193,754)	(233,616)
Capital expenditures	52,355	202,706	255,061

	Year ended December 31, 2004		
	Alternative fixed line communication services	**Traditional fixed line communication services**	**Total**
Net sales to external customers	$ 281,673	$ 413,460	$ 695,133
Intersegment sales	716	67,387	68,103
Depreciation and amortization	(22,216)	(53,922)	(76,138)
Operating income	62,387	113,129	175,516
Interest income	4,511	3,430	7,941
Interest expense	(1,562)	(17,133)	(18,695)
Income tax expense	(16,421)	(24,655)	(41,076)
Segment assets	374,739	1,065,473	1,440,212
Cash and cash equivalents	38,688	28,748	67,436
Indebtedness [(a)]	(27,237)	(189,560)	(216,797)
Capital expenditures	36,728	192,396	229,124

[(a)] – Represents the sum of short-term and long-term debt and capital lease obligations

The reconciliation of segment operating income to the income before income tax and minority interests and reconciliation of segment assets to the consolidated (combined) segment assets are as follows:

	Year ended December 31,	
	2005	**2004**
Total segment operating income	$ 271,078	$ 175,516
Intersegment eliminations	(2,727)	(1,797)
Operating income	268,351	173,719
Interest income	7,696	7,941
Interest expense	(17,961)	(18,695)
Foreign currency transactions (loss)/gain	(2,219)	4,368
Gain/(loss) from disposal of an affiliate	1,989	(6,610)
Income before income tax and minority interests	**$ 257,856**	**$ 160,723**
Total segment assets	$ 1,690,364	$ 1,440,212
Intersegment eliminations	(49,003)	(21,764)
Total assets	**$ 1,641,361**	**$ 1,418,448**

For the years ended December 31, 2005 and 2004, the Group did not have revenues from transactions with a single external customer amounting to 10% or more of the Group's revenues.

23. RELATED PARTY TRANSACTIONS

During the year ended December 31, 2005 and 2004, major transactions involving related parties (subsidiaries and affiliates of JSFC Sistema) were as follows:

Mobile Telesystems (MTS)

The Group has interconnection arrangements and line rental agreements with MTS, a subsidiary of Sistema. MTS also rents buildings for administrative, sales and marketing offices from the Group as well as premises for its switching and base station equipment. Amounts received by the Group under these agreements during the year ended December 31, 2005 and 2004 were approximately $35.7 million and $36.3 million, respectively. During the years ended December 31, 2005 and 2004, MTS purchased telephone numbering capacity from the Group for the amounts of $nil and $4.2 million, respectively.

Rosno

The Group purchases insurance services from Rosno. The insurance premium paid to Rosno during the year ended December 31, 2005 and 2004 amounted to $8.5 million and $7.4 million, respectively. Insurance recovery received from Rosno for the same periods amounted to $nil and $0.2 million, respectively.

STROM telecom and Mediatel

The Group purchases telecommunication equipment and software from STROM telecom and Mediatel. The cost of equipment and software purchased from these entities during the year ended December 31, 2005 and 2004 was $22.7 million and $13.2 million, respectively. Related accounts payable as of December 31, 2005 and December 31, 2004 amounted to $6.9 million and $12.1 million, respectively.

MBRD

During the years ended December 31, 2005 and 2004, the Group has received interest income on MBRD's promissory notes of $3.0 million and $3.1 million, respectively.

Sistema Telecom, Sky-Link

Interest income received by the Group on promissory notes of Sistema Telecom and Sky-Link for the years ended December 31, 2005 and 2004 amounted to $2.2 million and $1.0 million, respectively.

RA Maxima

During the year ended December 31, 2005, the Group purchased advertising from advertising agency RA Maxima, a subsidiary of Sistema. The amount of advertising purchased from RA Maxima during the year ended December 31, 2005 was $5.6 million.

Invest-Svyaz-Holding

The Group enters into agreements with Invest-Svyaz-Holding, a subsidiary of Sistema, for leasing of network equipment and billing system. These leases were recorded as capital leases based on the requirements of SFAS No. 13, "Accounting for Leases". The net book value of assets leased under such agreements as of December 31, 2005 and 2004 was $53.5 million and $28.5 million, respectively. The interest rate implicit in the leases varied from 14.0% to 23.9%.

The following table summarizes the future minimum lease payments under capital leases to Invest Svyaz-Holding together with the present value of the net minimum lease payments as of December 31, 2005:

Year ended December 31,		
2006	$	16,482
2007		14,893
2008		11,545
2009		5,595
Total minimum lease payments (undiscounted)		48,515
Less: amount representing interest		(6,884)
Present value of net minimum lease payments		41,631
Less: current portion of lease obligations		(12,966)
Non-current portion of lease obligations	**$**	**28,665**

24. COMMITMENTS AND CONTINGENCIES

Operating leases - The Group leases land, buildings and office space from municipal organizations through contracts, which expire in various years through 2049. Rental expenses for the years ended December 31, 2005 and 2004 amounted to $18.2 million and $16.0 million, respectively.

Future minimum rental payments under operating leases in effect as of December 31, 2005 are as follows:

Year ended December 31,		
2006	$	17,688
2007		11,970
2008		5,501
2009		5,116
2010		4,544
Thereafter		26,867
Total	**$**	**71,686**

Capital commitments - In December 2003, MGTS announced its long-term investment program for the period from 2004 to 2012 providing for extensive capital expenditures including expansion and full digitalization of the Moscow telephone network. The program was approved by the resolution of Moscow City Government of December 16, 2003. At the inception of the investment program, capital expenditures were estimated to be approximately $1,600.0 million and included reconstruction of 350 local telephone stations and installation of 4.3 million of new phone numbers.

In the course of completion of the investment program, MGTS entered into a series of agreements with Sistema Hals, a subsidiary of Sistema, on project development and reconstruction of buildings of automatic telephone exchanges. The main part of work under the contracts is to be performed in 2006-2008.

In December 2005, MGTS entered into an agreement to acquire telecommunications equipment and related services from ECI Telecom (Israel). The vendor financing amounting to $2.3 million will bear interest of LIBOR+4% and be repayable in 9 equal quarterly installments starting October 2006

As of December 31, 2005, the Group has commitments to spend $2.1 million on network development and acquisition of new telecommunication equipment.

Licenses - Substantially all of the Group's revenues are derived from operations conducted pursuant to licenses granted by the Russian Government. These licenses expire in various years ranging from 2006 to 2013. The Group has no reason to believe that the licenses will not be renewed or that any license will be suspended or terminated.

Issued guarantees - In December 2004, MGTS became a guarantor under the credit facility between Sistema-Hals and WestLB Vostok Bank. The loan of $10.4 million matures in December 2006. The guarantee amounted to $10.4 million as of December 31, 2005.

MGTS is a guarantor under several credit facilities between Commerzbank (Eurasia) and Invest-Svyaz-Holding. The credit facilities mature in 2006-2008. The guarantees amounted to $20.1 million as of December 31, 2005.

Under these guarantees the Group could be potentially liable for a maximum amount of $30.5 million in case of borrower's default under the obligations. As of December 31, 2005, no event of default has occurred under any of the guarantees issued by the Group.

Pledges - As of December 31, 2005, 13,411,300 MGTS' ordinary shares were pledged under MTS' debt to Salomon Brothers Holding Company, Inc. The balance of the debt as of December 31, 2005 amounted to $3.2 million.

Russian environment and current economic situation - Over the past decade Russia has undergone substantial political and social changes. As an emerging market, Russia does not possess a fully developed business and regulatory infrastructure that would generally exist in a more mature market economy. The current government is attempting to address these issues; however it has not yet fully implemented the reforms necessary to create banking and judicial systems that usually exist in more

developed markets. As a result, operations in Russia involve risks that typically do not exist in more developed markets.

Interest of the Moscow city government in the telecommunications sector in the Moscow metropolitan area - The operations of the telecommunications network in Moscow are of considerable interest to the city government. The city government has exercised and may be expected to continue to exercise influence over the Group's operations. In particular, the city government may influence setting of tariffs charged to customers to protect low income groups, such as pensioners.

Regulations on telecommunications - On January 1, 2004, a new Communications Law came into effect in Russia. The law sets the legal basis for the telecommunications business in Russia and defines the status that state bodies have in the telecommunications sector.

The Communications Law introduced Universal Service Reserve Fund (the "USRF") which resulted in higher costs for all operators, including the Group. Under the Communications Law, all telecommunications operators must contribute to the USRF. The USRF is designed to fund socially important but economically unviable projects. In April 2005, the Russian government approved several provisions clarifying how the USRF will be collected and administered. Starting July 1, 2005, the amount of the universal service charge is 1.2% of the total revenues received from the usage of public telecommunication network less connection fees and revenues received from interconnection services provided to other operators. For the year ended December 31, 2005, the related expense of $5.2 million was recorded in other operating expenses.

The Russian government has also issued several implementing acts under the Law on Telecommunications, such as Resolution No. 87, dated February 18, 2005, approving the list of the types of licensed telecommunication activities, and Resolution No. 68, dated February 11, 2005, regarding the rules applicable to the state registration of telecommunication infrastructure such as real property. However, it is presently not yet clear how these regulations would be implemented. Thus, the uncertainty related to the Law on Telecommunications continues.

Taxation environment - Russian tax legislation is subject to varying interpretations with changes occurring frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group may not coincide with that of management. As a result, transactions may be challenged by tax authorities and the Group may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three years.

Contingencies - In the normal course of business, the Group is subjected to proceedings, lawsuits, and other claims. While such matters are subject to many uncertainties, and outcomes are not predictable with assurance, management of the Group believes that any financial impact arising from these matters would not be material to its financial position or annual operating results.

During the first half of 2005, MGTS filed seven claims in the Moscow Arbitration Court against the Ministry of Labor and Social Development of the Russian Federation for the recovery of losses it incurred in connection with the provision of communications services in 2003 to 2004 to Russian veterans at a reduced rate. Pursuant to the Federal Law on Veterans, MGTS is seeking full reimbursement from federal funds totaling approximately $15.8 million. In the second half of 2005, the Arbitration Court ruled in favor of MGTS for the full amount. Although writs of execution have been obtained with respect to four of the seven claims, MGTS has not yet received any payments.

25. SUBSEQUENT EVENTS

In January 2006, Comstar UTS entered into a $140.0 million credit facility with ING Bank. It was fully repaid in March 2006.

In February 2006, Comstar UTS has acquired the remaining 1% minority stake in MTU-Inform for the total amount of 2.6 million USD. Comstar UTS has thereby increased its interest in MTU-Inform to 100%.

In February 2006, Comstar UTS announced the results of its public share purchase offer to MGTS common stock shareholders. For the first two months of 2006, Comstar UTS acquired 3,363,332 MGTS' ordinary shares, representing 4.21% of the Company's outstanding ordinary share capital, during the offer period for a total cash consideration of RUR 1,600 million (equivalent of $58.4 million as of December 31, 2005). In March 2006, Comstar UTS further purchased 3.82% of MGTS' common stock from minority shareholders for $71.5 million. As a result, Comstar UTS' voting power and ownership interest in MGTS increased to 63.65% and 53.04%, respectively.

In February 2006, Comstar UTS completed an initial public offering of 146,500,000 common shares (see Note 1 for details).

In March 2006, Comstar UTS announced the terms of its second public share purchase offer to MGTS shareholders. The offer price was set at RUR 490 (equivalent of $17.1 as of December 31, 2005) per one common share of MGTS. Shareholders of MGTS could accept this offer within 30 days of the receipt of official notification.

In March 2006, Comstar UTS fully repaid $20.0 million under ABN Amro Bank credit line.

In March 2006, Russian telecommunication authorities included Comstar UTS into the register of operators occupying a "substantial position" in the market. Connection and traffic transmission tariffs that such operators may charge other operators are regulated by the government. Tariffs are set at the economically justified levels based on actual costs for interconnection provided by operators.

In April 2006, Comstar UTS purchased promissory notes from Sistema for the total amount of $118.2 million, including $45.0 million of USD-denominated notes maturing on October 9, 2006, $55.0 million of USD-denominated notes maturing on June 29, 2006 and $18.2 million of RUR-denominated notes maturing on June 29, 2006. Interest rates vary from 5.9% to 6.0%.