Open Joint Stock Company
Southern Telecommunications Company

Consolidated Financial Statements

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

OJSC Southern Telecommunications Company
Consolidated Financial Statements
For the year ended 31 December 2007

Contents

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

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

Independent Auditors' Report

To the Board of Directors of OJSC Southern Telecommunications Company

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

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

ZAO KPMG, a company incorporated under the Laws of the Russian Federation and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative.

Basis for Qualified Opinion

As described in Note 2, the cost of property, plant and equipment at the date of adopting International Financial Reporting Standards ("IFRS"), 1 January 2003, was determined by reference to its fair value at that date. The fair value of property, plant and equipment was assumed by management to be equal to its carrying amount in the Group's previous GAAP financial statements. This assumption is not consistent with a measurement of fair value as envisaged by IFRS 1 *First-time Adoption of International Financial Reporting Standards.* The effects of this departure from International Financial Reporting Standards, if any, on the carrying amount of property, plant and equipment, depreciation, taxation, net profit and retained earnings as at and for the years ended 31 December 2007 and 31 December 2006 have not been determined.

Qualified Opinion

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

ZAO KPMG
10 June 2008

OJSC Southern Telecommunications Company
Consolidated Balance Sheet
As at 31 December 2007

(In millions of Russian Roubles)

	Notes	2007	2006
ASSETS			
Non-current assets			
Property, plant and equipment	**6**	32,857	32,095
Intangible assets	**7**	2,037	1,856
Investments in associates	**9**	615	530
Long-term investments	**10**	22	15
Other long-term assets	**11**	142	204
Long-term advances given	**12**	47	156
Deferred tax assets	**29**	4	7
Total non-current assets		**35,724**	**34,863**
Current assets			
Inventories	**13**	681	778
Accounts receivable	**14**	986	702
Current income tax receivable		241	283
Prepayments for current assets		86	113
Other current assets	**15**	808	732
Cash and cash equivalents	**16**	562	331
Assets classified as held for sale		-	39
Total current assets		**3,364**	**2,978**
TOTAL ASSETS		**39,088**	**37,841**
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Share capital	**18**	3,039	3,039
Retained earnings		7,960	7,020
Total equity attributable to equity holders of the parent		**10,999**	**10,059**
Minority interest		-	9
Total equity		**10,999**	**10,068**
Non-current liabilities			
Long-term borrowings	**19**	13,032	6,331
Long-term finance lease liabilities	**20**	472	1,229
Pension liabilities	**23**	1,458	1,283
Long-term provision		4	18
Deferred revenue		313	359
Deferred income tax liabilities	**29**	953	928
Total non-current liabilities		**16,232**	**10,148**
Current liabilities			
Accounts payable, accruals and advances received	**21**	3,722	3,343
Current income tax payable		31	5
Other taxes payable	**22**	348	386
Dividends payable		31	29
Short-term borrowings	**19**	2,181	1,181
Current portion of long-term borrowings	**19**	4,654	11,680
Current portion of long-term finance lease liabilities	**20**	758	812
Provisions	**24**	132	181
Liabilities classified as held for sale		-	8
Total current liabilities		**11,857**	**17,625**
Total liabilities		**28,089**	**27,773**
TOTAL EQUITY AND LIABILITIES		**39,088**	**37,841**

General Director
A.V. Andreev

Chief Accountant
T.V. Rusinova

The accompanying notes form an integral part of these consolidated financial statements

OJSC Southern Telecommunications Company
Consolidated Income Statement
For the year ended 31 December 2007
(In millions of Russian Roubles)

	Notes	2007	2006
Revenues	**25**	**20,231**	**17,959**
Wages, salaries, other benefits and payroll taxes		(5,793)	(6,105)
Depreciation and amortisation	**6,7**	(3,554)	(3,325)
Materials, repairs and maintenance, utilities		(2,610)	(2,274)
Taxes other than income tax		(781)	(775)
Interconnection charges		(1,834)	(1,061)
Reversal of impairment of receivables	**14**	24	401
Loss on disposal of property, plant and equipment		(41)	(4)
Write-off re. Oracle EBS and Amdocs		(342)	-
Other operating expenses	**26**	(1,915)	(1,900)
Operating profit		**3,385**	**2,916**
Share of profit of associates	**9**	189	95
Interest expense, net	**27**	(2,135)	(2,293)
Gain on sale of investments, net	**28**	40	13
Foreign exchange gain, net		312	59
Profit before income tax		**1,791**	**790**
Income tax expense	**29**	(595)	(429)
Profit for the year from continuing operations		**1,196**	**361**
Profit /(loss) after tax from discontinued operations		19	(14)
Profit for the year		**1,215**	**347**
Attributable to:			
Equity holders of the parent		1,215	350
Minority interests		-	(3)
		1,215	**347**
Earnings per share			
Basic and diluted earnings per share	**30**	0.31	0.09

The accompanying notes form an integral part of these consolidated financial statements

OJSC Southern Telecommunications Company
Consolidated Statement of Cash Flows
For the year ended 31 December 2007
(In millions of Russian Roubles)

	Notes	2007	2006
Cash flows from operating activities			
Profit before income tax from continuing operations		1,791	790
Profit / (loss) after tax from discontinued operations		19	(14)
Adjustments for:			
Depreciation and amortisation	**6,7**	3,554	3,334
Loss on disposal of property, plant and equipment		41	4
Write-off re. Oracle EBS and Amdocs		342	-
Foreign exchange gain, net		(312)	(59)
Share of profit of associates	**9**	(189)	(95)
Gain on sale of investments	**28**	(40)	(13)
Interest expense, net	**27**	2,135	2,293
Loss from goodwill impairment		-	6
Reversal of allowance for impairment of receivables	**14**	(24)	(401)
Write-down of inventory to net realisable value		35	10
Provision for tax fines and penalties and other claims		(14)	162
Movement in pension liabilities		175	415
Operating cash flows before working capital changes		**7,513**	**6,432**
(Increase)/decrease in accounts receivable		(224)	473
(Increase)/decrease in other current assets		(76)	507
Decrease in inventories		62	68
(Decrease)/increase in accounts payable		(638)	406
Decrease in taxes payable other than income tax		(38)	(196)
Cash flows generated from operations		**6,599**	**7,690**
Interest paid		(2,168)	(2,716)
Income tax paid		(499)	(372)
Net cash flows from operating activities		**3,932**	**4,602**
Cash flows from investing activities			
Purchase of property, plant and equipment		(3,477)	(2,379)
Purchase of intangible assets		(35)	(45)
Purchase of Oracle E-Business Suite software		(92)	(66)
Purchase of Amdocs Billing software		(146)	(156)
Proceeds from disposal of investments and other assets		57	10
Proceeds from disposal of property, plant and equipment		89	81
Proceeds from sale of subsidiaries		22	-
Interest received		13	7
Dividends received		120	97
Net cash used in investing activities		**(3,449)**	**(2,451)**
Cash flows from financing activities			
Proceeds from borrowings		3,619	8,560
Repayment of borrowings		(1,831)	(8,191)
Proceeds from debt securities issued		4,764	-
Repayment of debt securities		(5,610)	(2,000)
Repayment of finance lease liabilities		(811)	(1,011)
Repayment of vendor financing liabilities		(119)	(166)
Proceeds from promissory notes		2,410	2,141
Repayment of promissory notes		(2,420)	(1,863)
Dividends paid		(254)	(62)
Net cash used in financing activities		**(252)**	**(2,592)**
Net increase/(decrease) in cash and cash equivalents		**231**	**(441)**
Cash and cash equivalents at the beginning of the year		**331**	**772**
Cash and cash equivalents at the end of the year	**16**	**562**	**331**

The accompanying notes form an integral part of these consolidated financial statements

OJSC Southern Telecommunications Company
Consolidated Statement of Changes in Equity
For the year ended 31 December 2007
(In millions of Russian roubles)

		Attributable to equity holders of the parent						
		Share capital						
	Notes	**Preference shares**	**Ordinary shares**	**Unrealised gain on available-for-sale investments**	**Retained earnings**	**Total**	**Minority interests**	**Total equity**
Balance at 31 December 2005		751	2,288	5	6,731	9,775	12	9,787
Profit for the year		-	-	-	350	350	(3)	347
Change due to disposal of available-for-sale investments		-	-	(5)	-	(5)	-	(5)
Total recognised gains and losses						**345**	**(3)**	**342**
Dividends to equity holders of the parent		-	-	-	(61)	(61)	-	(61)
Balance at 31 December 2006		**751**	**2,288**	**-**	**7,020**	**10,059**	**9**	**10,068**
Profit for the year		-	-	-	1,215	1,215	-	1,215
Total recognised gains						**1,215**	**-**	**1,215**
Disposal of subsidiaries classified as held for sale		-	-	-	-	-	(9)	(9)
Dividends to equity holders of the parent	**31**	-	-	-	(275)	(275)	-	(275)
Balance at 31 December 2007		**751**	**2,288**	**-**	**7,960**	**10,999**	**-**	**10,999**

1. General Information

Authorization of Accounts

The consolidated financial statements of OJSC Southern Telecommunications Company and its subsidiaries - (hereinafter "the Company") for the year ended 31 December 2007 were authorized for issue by the General Director and the Chief Accountant of the Company on 17 June 2008.

The Company

The Company is an open joint stock company incorporated in accordance with the laws of the Russian Federation.

The registered office of the Company is in the city of Krasnodar (the Russian Federation), 66 Karasunskaya street.

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

OJSC Svyazinvest is the Company's parent company which owned 50.69% of the Company's ordinary voting stock as at 31 December 2007. OJSC Svyazinvest is controlled by the Federal Government of the Russian Federation.

Information of the Company's main subsidiaries is disclosed in note 8. All subsidiaries are incorporated under the laws of the Russian Federation.

Liquidity and Financial Resources

As of 31 December 2007, the Company's current liabilities exceeded its current assets by RUR 8,493 million (2006 – RUR 14,678 million). Consequently, there is an uncertainty about the Company's ability to maintain its liquidity and to pay its existing debts as they fall due.

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

In 2007, the Company raised both short and long-term borrowings to finance its operations. In 2007, the Company repaid its liabilities in full and in due time. The key instrument used by the Company to maintain the adequate level of solvency is the availability of financing in the form of a revolving credit lines and promissory notes.

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

- optimize expenses, including decrease in personnel costs (by optimizing the headcount, cutting the variable portion of salary/wages), optimize use of inventory and repair and maintenance expenses, control administrative and other expenses, optimize costs related to sales and customer service through outsourcing;

- revise the capital expenditure program to downsize the investment program or extend investment project timeframes. The current contracts with vendors permit the Company to carry out these measures;

- increase the efficiency of working capital utilization, *inter alia*, decrease the level and average age of accounts receivable, in particular by changing the existing contractual relations with customers, increase accounts payable to an optimal level.

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

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

Through 2008, the Company anticipates funding from cash generated from operations and financing from domestic and international lending institutions. Management believes that these sources will be sufficient to settle short-term liabilities. If needed, management believes that payment terms on certain current operations may be deferred in case of insufficiency of working capital.

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

The Company's Position in the Communication Services Market

Establishment of New Tariffs Based on Tariff Plans

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

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

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

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

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

Change in Tariff Calculation Rules

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

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

Universal Telecommunication Services

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

The Company has tendered for the right to provide universal telecommunication services, specifically telephone services using payphones, in its licensed areas. In 2007, the Company won 10 tenders (2005-2006 – 10) and entered into 10 agreements with the Federal Telecommunications Agency, which outline the terms and conditions of providing universal telephone services using payphones (2005-2006 – 38). As of 31 December 2007, the Company had installed the total of 7,581 payphones pursuant to the above agreements.

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

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

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

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

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

National Project Education

In 2006-2007, the Company was involved in the implementation of the national priority project Education. As part of this project, the Company's branches connected to the Internet 5,136 educational institutions in the territory of the Southern Federal District of the Russian Federation, including 2,889 educational institutions connected to the Internet in 2007. The Company's costs incurred in 2007 to connect educational institutions totaled RUR 489 million.

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

Plans to Digitalize the Company's Networks

At the end of 2007, 68.8% of local telephone networks were digitalized. Commissioning of new electronic telephone exchanges and replacement of quasi-electronic and analog telephone exchanges by the electronic ones help the Company to improve the quality of provided services, broaden their range and meet industry requirements. The Company is planning to digitalize its local telephone networks in accordance with the requirements by the year of 2012.

2. Basis of preparation of financial statements

Statement of compliance

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

Presentation of financial statements

The consolidated financial statements are prepared based on the standalone financial statements of the parent company, OJSC Southern Telecommunications Company, its subsidiaries and associates using unified accounting policies.

The functional and presentation currency of the Company is the Russian Rouble, which is the national currency of the Russian Federation.

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

Accounting principles

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

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

The Company transitioned to IFRS as of 1 January 2003 using the provisions of IFRS 1 *First-time Adoption of International Financial Reporting Standards.*

The Company has applied an exemption permitted by IFRS 1 which allows an entity to measure property, plant, and equipment at the date of transition to IFRS at fair value and use that fair value as deemed cost. The Company has also applied the exemption permitted by IFRS 1 which allows an entity to recognize all cumulative actuarial gains and losses on employees defined benefit plans at the date of transition even if the corridor approach is used for latter actuarial gains and losses.

Management estimates that the carrying value of all of the Company's property, plant and equipment as of the date of transition to IFRS was broadly comparable to their fair values.

However, management engaged an independent appraiser to support these fair values and as a result, the reported carrying amount of property, plant and equipment may be adjusted for the purposes of the consolidated financial statements of the Company for the year ending 31 December 2008.

Changes in Accounting Policies

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

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

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

The principal effects of these changes in policies are discussed below

IFRS 7 Financial Instruments: Disclosures

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

IAS 1 (amended in 2005) Presentation of Financial Statements - Capital Disclosures

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

IFRIC 8 Scope of IFRS 2

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

IFRIC 9 Reassessment of Embedded Derivatives

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

IFRIC 10 Interim Financial Reporting and Impairment

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

IFRSs and IFRIC Interpretations Approved but not yet Effective

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

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

IFRS 8 Operating Segments;

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

IAS 1 (amended in 2007) Presentation of Financial Statements

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

IAS 23 (amended in 2006) Borrowing Costs

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

IFRIC 11, IFRS 2 – Group and Treasury Share Transactions

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

IFRIC 12 Service Concessions Arrangements

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

IFRIC 13 Customer Loyalty Programs

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

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

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

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

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

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

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

IFRS 3 (amended in 2008) Business Combinations

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

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

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

The Company expects that the adoption of the standards and interpretations listed above will have no significant impact on the Company’s results of operation and financial positions in the period of initial application.

3. Summary of Significant Accounting Policies

3.1. Principles of Consolidation

The consolidated financial statements of the Company represent the financial statements of the group of companies, i.e. the parent and its subsidiaries, presented as if the Company operated as a single economic entity.

Subsidiaries

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases.

All intercompany transactions, balances and unrealized gains on transactions between group companies are eliminated.

Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Company.

3.2. Investments in Associates

Associates are entities in which the Company generally has between 20 % and 50% of the voting rights, or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognized at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Company’s share of net assets of the associate. The Company’s share of its associates’ profits or losses is recognized in the income statement, and its share of movements in reserves is recognized in equity. However, when the Company’s share of losses in an associate equals or exceeds its interest in the associate, the Company does not recognize further losses, unless the Company is obliged to make further payments to, or on behalf of, the associate.

3.3. Investments

The Company’s investments are classified as either loans and receivables or available-for-sale investments, as appropriate. When investments are recognised initially, they are measured at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Company determines the classification of its investments at their initial recognition. All purchases and sales of investments are recognised on the settlement date, which is the date that the investment is delivered to or by the Company. Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Company has the positive intention and ability to hold to maturity. During the period the Company did not hold any investments in this category. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

(a) those that the Company intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;
(b) those that the Company upon initial recognition designates as available for sale; or
(c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale.

Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in income when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale investments are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for-sale investments are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement. Reversals of impairment losses in respect of equity instruments are not recognised in the income statement. Impairment losses in respect of debt instruments are reversed through profit or loss if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the income statement.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis.

3.4. Accounting Policies, Changes in Accounting Estimates and Errors

Change in Accounting Policies

The Company accounts for a change in accounting policy resulting from the initial application of a Standard or an Interpretation in accordance with the specific transitional provisions, if any, in that Standard or Interpretation.

Changes in Accounting Estimates

The effect of a change in an accounting estimate is recognized prospectively by including it in profit or loss in the period of the change, if the change affects that period only or the period of the change and future periods, if the change affects both.

Prior Period Errors

Prior period error is corrected by retrospective restatement except to the extent that it is impracticable to determine either the period-specific effects or the cumulative effect of the error.

3.5. Foreign Currency Transactions

The measurement functional and presentation currency of the Company is the Russian Rouble, which is the national currency of the Russian Federation. Transactions in foreign currencies are initially recorded in the measurement functional currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the measurement functional currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to the consolidated income statement as foreign exchange gains (losses). Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction.

(In millions of Russian roubles)

Assets and liabilities settled in Roubles but denominated in foreign currencies are recorded in the Company's consolidated financial statements using the same principles as for assets and liabilities denominated in foreign currencies.

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

Currency	2007	2006
Russian Roubles per US dollar	24.5462	26.3311
Russian Roubles per Euro	35.9332	34.6965

3.6. Property, Plant and Equipment

3.6.1. Initial recognition

Property, plant and equipment are recorded at purchase or construction cost, excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value. For the property, plant and equipment acquired prior to 1 January 2003, fair values as at 1 January 2003 have been used as deemed cost (refer to note 1) in accordance with the exemption provided in IFRS 1.

Management assesses indications of impairment at each balance sheet date, and when events or changes in circumstances indicate that the carrying values may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of fair value less cost to sell and value in use. Impairment losses are recognized in the income statement. Impairment losses recognised in previous periods are reversed, if there has been a change in the estimates, used to determine the recoverable amount.

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

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

Interest costs on borrowings to finance the construction of property, plant and equipment are capitalized, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

3.6.2. Depreciation and Useful Life

Depreciation is calculated on property, plant and equipment on a straight-line basis from the time the assets are available for use, over their estimated useful lives as follows:

Buildings	20-50 years
Constructions	10-20 years
Analogue switches	5-15 years
Digital switches	2-15 years
Other telecommunication equipment	2-15 years
Transportation equipment	5 years
Computers, office and other equipment	3 years
Land	not depreciated

The asset's residual values, useful lives and depreciation methods are reviewed, and adjusted as appropriate, at each financial year-end.

Depreciation of an asset begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with IFRS 5 and the date that the asset is derecognised.

The depreciation charge for a period is usually recognized in the income statement, except where depreciation of property, plant and equipment is included in the cost of other assets, created using such property, plant and equipment.

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

3.6.3. Construction in Progress

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

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

3.6.4. Assets Received Free of Charge

Equipment related to main activity of the Company transferred to the Company free of charge outside the privatization process is capitalized at market value at the date of transfer. A corresponding income is fully recognized in the income statement, except where transfers of equipment relate to rendering of future services to the transferee, in which case the Company recognises deferred revenue in the amount of the fair value of the equipment received, and amortises it to the income statement on the same basis that the equipment is depreciated.

Equipment contributions that will not generate any future economic benefit for the Company are not recognized.

3.7. Intangible Assets

3.7.1. Goodwill

Goodwill represents the excess of the cost of an acquisition over the net fair value of the Company's share of the identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate at the date of acquisition. Goodwill on an acquisition of a subsidiary is included in intangible assets. Goodwill on an acquisition of an associate is included in the investments in associates. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Company are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated represents the lowest level within the Company at which the goodwill is monitored for internal management purposes.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

An impairment loss recognized for goodwill is not reversed in a subsequent period.

3.7.2. Licences

Cost of licences paid to the Government for permission to provide telecommunication services within an identifiable period of time is recognized as intangible assets.

3.7.3. Software and Other Intangible Assets

Software and other intangible assets acquired separately are measured on initial recognition at cost. The cost of other intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

3.7.4. Useful Life and Amortization of Intangible Assets

The Company assesses whether the useful life of an intangible asset is finite or indefinite and, if finite, the length of or number of production, or similar units constitutes that useful life. An intangible asset is regarded by the entity as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity.

Intangible assets with finite lives are amortized over the useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired.

Amortization periods and methods for intangible assets with finite useful lives are reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates.

The cost of licences and software is depreciated on a straight-line basis over the estimated useful life equal to the term of the licences or the right to use the software. The useful life of other intangible assets is approximately 10 years.

Intangible assets with indefinite useful lives are not amortized, but tested for impairment annually either individually or at the cash-generating unit level. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

3.8. Borrowing Costs

The borrowing costs are capitalized by the Company as part of the cost of the asset when it is probable that they will result in future economic benefits to the entity and the costs are directly attributable to the acquisition, construction or production of a qualifying asset including construction in progress.

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization on that asset is determined as the actual borrowing costs incurred on that borrowing during the period.

To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization is determined by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average of the borrowing costs applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs capitalized during a period shall not exceed the amount of borrowing costs incurred during that period.

3.9. Leases

Leases where all the risks and rewards of ownership of the asset are transferred from the lessor to the lessee are classified as finance leases.

Leases where the lessor retains substantially all the risks and rewards of ownership of the asset are classified as operating leases

3.9.1. Finance Leases

At the commencement of the lease term or the date from which the lessee is entitled to exercise its right to use the leased asset, the Company recognizes finance leases as assets and liabilities in their balance sheet at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. At the commencement of the lease term the asset and the liability for the future lease payments are recognized in the balance sheet at the same amounts except for any initial direct costs of the lessee that are added to the amount recognized as an asset.

Lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

The depreciation policy for depreciable leased assets is consistent with that for depreciable assets that are owned, and the depreciation recognized is calculated in accordance with the accounting policy of the Company applicable for depreciable and amortized assets. If there is no reasonable certainty that the Company will obtain ownership by the end of the lease term, the asset is fully depreciated over the shorter of the lease term and its useful life.

3.9.2. Operating Leases

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

3.10. Inventories

Inventories are recorded at the lower of cost and net realizable value. Cost of inventory is determined on the weighted average basis. The cost of finished goods and work in progress comprises cost of raw materials and other materials, direct labour and other direct costs, as well as the corresponding share of production indirect cost (calculated on the basis of norms of production capacities usage). Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

3.11. Advances Given

Advances given to acquire non-current assets are classified as non-current not dependant on the delivery terms of the asset and considered a non-monetary asset. Long-term advances given for operating activities are also classified as a non-current asset.

3.12. Financial Instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets comprise cash and cash equivalents; an equity instrument of another entity; a contractual right to receive cash or another financial asset from another entity, or to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the Company; or a contract that will or may be settled in the Company's own equity instruments and is a non-derivative for which the Company is or may be obliged to receive a variable number of the Company's own equity instruments, or a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments. For this purpose the Company's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the Company's own equity instruments.

Financial liabilities include contractual obligations to deliver cash or another financial asset to another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the Company; or a contract that will or may be settled in the Company's own equity instruments and is a non-derivative for which the Company is or may be obliged to deliver a variable number of the Company's own equity instruments or a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the Company's own equity instruments. For this purpose the Company's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.

The Company recognizes a financial asset or a financial liability on its balance sheet when, and only when, the Company becomes a party to the contractual provisions of the instrument.

When a financial asset or financial liability is recognized initially, the Company measures it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

The Company classifies its financial assets and financial liabilities as current or non-current based on the term of its maturity taking into account other factors that limit the Company's ability to realize assets within 12 months or the existence of call options in financial liabilities valid within 12 months after the balance sheet date.

Financial asset is derecognised when the rights to receive cash flows from the asset expired or the Company transferred its rights to receive cash flows from the asset.

Financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

3.13. Cash and Cash Equivalents

Cash and cash equivalents represent cash on hand and in the Company's bank accounts, as well as cash deposits and short-term investments with original maturities of three months or less.

3.14. Accounts Receivable and Allowance for Bad Debt

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

Allowance for impairment is created based on the historical pattern of collections of accounts receivable and a specific analysis of the recoverability of significant accounts.

Allowance for impairment is also created for other accounts receivable based on the assessment of the Company's ability to collect the debts.

Allowance for impairment is recognized in the income statement.

The carrying amount of current trade receivables is a reasonable approximation of their fair value.

The fair value of non-current trade receivables is calculated using the effective interest method.

3.15. Non-current Assets Held for Sale and Discontinued Operations

A discontinued operation is a component of the Company that either has been disposed of, or is classified as held for sale, and represents a separate major line of business or geographical area of operations, is part of a single co-coordinated plan to dispose of a separate major line of business or geographical area of operations or is a subsidiary acquired exclusively with a view to resale.

The Company classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.

The Company measures a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

Immediately before the initial classification of the asset (or disposal group) as held for sale, the carrying amounts of the asset (or all the assets and liabilities in the group) are be measured in accordance with applicable IFRSs and IFRICs.

The Company presents and discloses information that enables users of the financial statements to evaluate the financial effects of discontinued operations and disposals of non-current assets (or disposal groups).

3.16. Loans Given

Loans given are recognized at the amortized cost, using the effective interest method less allowance for impairment or uncollectibility. Loans given are recorded as the non-current assets unless the repayment is expected within 12 months after the balance sheet date.

3.17. Loans and Borrowings Received

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

3.18. Employee Benefits

3.18.1. Unified Social Tax

Under provisions of the Russian legislation, social contributions are made through a unified social tax ("UST") calculated by the Company by the application of a regressive rate to the annual gross remuneration of each employee. The Company allocates the UST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund varies depending on the annual gross salary of each employee.

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

3.18.2. Current Employment Benefits

Wages and salaries paid to employees are recognized as expense in the current period.

3.18.3. Other Pension Plans and Post-Employment Benefits

Under collective bargaining agreements and internal regulations on additional pension benefits, the Company also provides additional benefits for its active and retired employees by using post-employment defined benefit plans. The majority of the Company's employees are eligible to participate under such post-employment benefit plans based upon a number of factors, including years of service, age, and compensation.

The Company determines the present value of the defined benefit obligation and the fair value of any plan assets on each reporting date separately for each plan. The obligations are valued by professionally qualified independent actuaries hired by the Company using the projected unit credit method. The assets of the defined benefit plans are valued by professionally qualified actuaries or independent appraisers.

Actuarial gains and losses are recognised as income or expense when the net cumulative unrecognised actuarial gains and losses for each individual plan at the end of the previous reporting year exceeded 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognised over the expected average remaining working lives of the employees participating in the plans.

Upon introduction of a new plan or improvement of an existing plan past service cost is recognized on a straight-line basis over the average period until the amended benefits become vested. To the extent that the benefits vest immediately past service costs are immediately expensed.

Gains or losses on the curtailment or settlement of pension benefit obligations are recognized when the curtailment or settlement occurs.

3.19. Income Taxes

Tax expense (tax income) is the aggregate amount included in the determination of profit or loss for the period in respect of current tax and deferred tax.

Current tax is the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable).

Current tax liabilities (assets) for the current and prior periods are measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

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

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the entity expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

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

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

Deferred tax assets and liabilities are not discounted.

3.20. Shareholders’ Equity

3.20.1. Share Capital

Ordinary shares and non-redeemable preference shares with discretionary dividends are both classified as equity.

3.20.2. Dividends declared

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

3.21. Minority Interest

Minority interest is the interest in subsidiaries not held by the Company. Minority interest at the balance sheet date represents the minority shareholders’ portion of the fair values of identifiable assets and liabilities of the subsidiary at the acquisition date, and the minorities’ portion of movements in net assets since the date of the combination. Minority interest is presented within equity, separately from the parent shareholders’ equity.

3.22. Revenue Recognition

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

Revenue is recognized in the amount of cash or cash equivalents received in the form of cash or receivable. However, when the inflow of cash or cash equivalents is deferred, the fair value of the consideration may be less than the nominal amount of cash received or receivable. When the arrangement effectively constitutes a financing transaction, the fair value of the consideration is determined by discounting all future receipts using an effective interest rate.

Revenue from service contracts is accounted for when the services are provided. Revenue from timed calls and data transfer services is measured primarily by the volume of traffic processed in the period.

Revenue arising from separable installation and connection activities is recognised when it is earned, upon activation.

Interest income is recognized on accrual basis.

Dividend income is recognized on the date that the Company's right to receive payment is established.

Net gain/loss on disposal of property, plant and equipment is recognized when all risks and rewards are transferred to the buyer or its agent.

Revenues from lease and other services are recognized in period when such services were rendered.

3.23. Barter Transactions

When goods or services are exchanged for goods or services which are of a similar nature and value, the exchange is not regarded as a transaction which generates revenue. When goods are sold or services are rendered in exchange for dissimilar goods or services, the exchange is regarded as a transaction which generates revenue. The revenue is measured at the fair value of the goods or services received, adjusted by the amount of any cash or cash equivalents transferred. When the fair value of the goods or services received cannot be measured reliably, the revenue is measured at the fair value of the goods or services given up, adjusted by the amount of any cash or cash equivalents transferred.

3.24. Earnings per Share

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

The Company's preference shares are considered participating equity instruments for the purpose of earnings per share calculations (see note 30).

3.25. Provisions

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

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

3.26. Contractual Commitments

Contractual commitments comprise legally binding trading or purchase agreements with stated amount, price and date or dates in the future.

The Company discloses significant contractual commitments in the Notes to the financial statements.

The asset or liability under contractual commitments are not recognized in the financial statement until any of the parties performs in accordance with the contract and until any of the party became legally liable to pay or entitled to receive the payment under the terms of the contract.

3.27. Contingent Assets and Contingent Liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company or a present obligation that arises from past events but is not recognized because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation or the amount of the obligation cannot be measured with sufficient reliability. The Company does not recognize a contingent liability. A contingent liability is disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company. The Company does not recognize a contingent asset. A contingent asset is disclosed where an inflow of economic benefits is probable.

3.28. Events after the Balance Sheet Date

The Company adjusts the amounts recognized in its financial statements to reflect adjusting events after the balance sheet date. Events require an entity to adjust the amounts recognized in its financial statements are caused by favourable and unfavourable outcomes of conditions that existed at the balance sheet date and change in management estimates subject to uncertainties which was used for accounting of a number of business activities.

If non-adjusting events after the balance sheet date are material, nondisclosure could influence the economic decisions of users taken on the basis of the financial statements. Accordingly, the Company discloses the nature of the event and an estimate of its financial effect, or a statement that such an estimate cannot be made the following for each material category of non-adjusting event after the balance sheet date.

4. Significant accounting judgments and estimates

4.1. Judgments

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

Revenue recognition (principal / agent)

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

- Although the Company collects the revenue from the final customer, all credit risk is borne by the supplier of services;

- The Company cannot vary the selling prices set by the supplier by more than 1%.

Lease classification

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership, otherwise it is classified as operational lease. Determining whether an arrangement is, or contains, a lease shall be based on the substance of the arrangement, but not its legal form. Unless the opposite can be reasonably argued, where the lease term exceeds 75% of the asset's useful life, or where the discounted value of minimal lease payments at the commencement of the lease term amounts to at least 90% of the fair value of the leased asset, such lease is classified as a finance lease.

4.2. Estimation Uncertainty

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

Useful life of property, plant and equipment

The Company estimates remaining useful lives of its property, plant and equipment at least once a year at the financial year end. If the estimation differs from the previous estimations, the changes are accounted for in accordance with IAS 8 *Accounting Policies, Changes in* Accounting Estimates and Errors. These estimates may have a significant impact on the carrying value of property, plant and equipment and depreciation, charged to the income statement.

Fair value of unquoted investments available-for-sale

Fair value of investments actively traded in regulated financial markets is determined on the basis of market ask prices at the end of trade on the reporting date. Fair value of investments which are not actively traded is determined using valuation techniques, including those based on reference to recent arm's length market transactions between knowledgeable, willing parties, based on reference to the current fair value of another instrument that is substantially the same, or based on discounted cash flow analysis and option pricing models.

These valuation techniques are based on assumptions that are not supported by existing market prices and rates. Management believes that the fair value determined using valuation techniques and recorded in the balance sheet, and the corresponding changes in the fair value recorded in the statement of changes in equity, are reasonable and most accurate as at the balance sheet date.

Allowance for impairment of receivables (bad and doubtful debt reserve)

Management records a provision for bad and doubtful debts to account for estimated losses resulting from the customers' inability to settle the liabilities. To estimate if the provision is sufficient, management evaluates ageing of the debts, the experience of bad debt write-off, customers' creditworthiness and changes in payment terms. If the customers' financial position continues to deteriorate, the actual amount of bad debt write-off may exceed the estimation.

Pension liabilities

Pension liabilities are usually provided for by plans which are classified and accounted for as defined benefit pension plans. The discounted value of the pension plan liabilities and the related current service costs are determined on the basis of actuary valuations which use demographic and financial assumptions, including mortality rates for the service period and thereafter, staff turnover rates, discount rates, future salary and pension levels, and to a lesser extent the expected income on the pension plan's assets. If adjustments to the key assumptions are required, it will have a significant impact on the future expenses in respect of pension obligations. Refer to note 23 for further details.

(In millions of Russian roubles)

5. Segment Information

The Company provides the wireline telecommunication services, on the territory of the Southern Federal District regions of the Russian Federation. The Company's structure is based on territorial units which service the corresponding parts of the Company's network. The Company's management considers that the Company operates in one geographical and business segment and evaluates performance and makes investment and strategic decisions based upon a review of profitability for the Company as a whole.

6. Property, Plant and Equipment

	Land, buildings and structures	Switches and transmission devices	Construction in progress and equipment for installation	Vehicles and other assets	Total
Cost					
As of 31 December 2005	**18,515**	**15,638**	**2,438**	**3,016**	**39,607**
Additions	-	-	2,362	-	2,362
Reclassification to disposal group	-	-	(2)	-	(2)
Disposals	(64)	(286)	(27)	(77)	(454)
Transfers	937	1,375	(2,648)	336	-
As of 31 December 2006	**19,388**	**16,727**	**2,123**	**3,275**	**41,513**
Additions	-	-	4,259	-	4,259
Disposals	(72)	(144)	(42)	(98)	(356)
Transfers	1,071	2,521	(4,450)	858	**-**
As of 31 December 2007	**20,387**	**19,104**	**1,890**	**4,035**	**45,416**
Accumulated Depreciation					
As of 31 December 2005	**(1,702)**	**(4,067)**	**-**	**(757)**	**(6,526)**
Charge for the year	(848)	(2,066)	-	(338)	(3,252)
Disposals	55	244	-	61	360
As of 31 December 2006	**(2,495)**	**(5,889)**	**-**	**(1,034)**	**(9,418)**
Charge for the year	(785)	(2,278)	-	(354)	(3,417)
Disposals	66	117	-	93	276
As of 31 December 2007	**(3,214)**	**(8,050)**	**-**	**(1,295)**	**(12,559)**
Net book value as of 31 December 2005	**16,813**	**11,571**	**2,438**	**2,259**	**33,081**
Net book value as of 31 December 2006	**16,893**	**10,838**	**2,123**	**2,241**	**32,095**
Net book value as of 31 December 2007	**17,173**	**11,054**	**1,890**	**2,740**	**32,857**

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

	2007	2006
Switches and transmission devices	3,319	3,683
Construction in progress and equipment for installation	178	331
Vehicles and other	21	33
Total net book value of property, plant and equipment held under finance leases	**3,518**	**4,047**

(In millions of Russian roubles)

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

In 2007 the Company capitalised in the cost of construction in progress the interest amounted to RUR 89 million (2006: RUR 305 million). The capitalisation rate in 2007 was 10.07 % (2006: 11.08 %).

As of December 31, 2007 the bank borrowings are secured by property, plant and equipment with a carrying value of approximately RUR 6,071 million (2006: RUR 6,324 million) (see note 19).

Management estimates that the carrying value of all of the Company's property, plant and equipment as of the date of transition to IFRS was broadly comparable to their fair values. However, management intends to engage an independent appraiser to support these fair values and as a result, the reported carrying amount of property, plant and equipment may be adjusted. It is expected that the appraisal will be completed in the near future.

7. Intangible Assets

	Goodwill	Licences	Software	Other	Total
Cost					
As of 31 December 2005	**15**	**60**	**1,616**	**2**	**1,693**
Additions	-	27	314	-	341
Reclassification to disposal group	(15)	(53)	-	-	(68)
As of 31 December 2006	**-**	**34**	**1,930**	**2**	**1,966**
Additions	-	-	660	-	660
As of 31 December 2007	**-**	**34**	**2,590**	**2**	**2,626**
Accumulated amortization and impairment					
As of 31 December 2005	-	**(23)**	**(31)**	**(1)**	**(55)**
Charge for the year	-	(1)	(72)	-	(73)
Charge for disposal group	-	(11)	-	-	(11)
Impairment loss	(6)	-	-	-	(6)
Reclassification to disposal group	6	29	-	-	35
As of 31 December 2006	-	**(6)**	**(103)**	**(1)**	**(110)**
Charge for the year	-	(1)	(136)	-	**(137)**
Impairment loss	-	-	(342)	-	**(342)**
As of 31 December 2007	-	**(7)**	**(581)**	**(1)**	**(589)**
Net book value as of 31 December 2005	**15**	**37**	**1,585**	**1**	**1,638**
Net book value as of 31 December 2006	**-**	**28**	**1,827**	**1**	**1,856**
Net book value as of 31 December 2007	**-**	**27**	**2,009**	**1**	**2,037**

Oracle E-Business Suite (OEBS)

As of 31 December 2007 software includes OEBS software with a net book value of RUR 965 million (2006: RUR 1,045 million), including capitalised interest of RUR 8 million (2006: RUR 70 million).

	2007	2006
Net book value as of 1 January	**1,045**	**910**
Implementation costs	265	169
Amortization charge	(110)	(34)
Write-off re. licenses	(205)	-
Write-off of respective capitalized interest	(30)	-
Net book value as of 31 December	**965**	**1,045**

(In millions of Russian roubles)

In accordance with the supply contract, the Company acquired non-exclusive licences for 10,745 users of E-business Suite 2004 Professional.

In September 2006 the Company started to use this software in relation to the modules for accounting for non-current assets and payroll. The Company commenced amortizing the cost of mentioned software accordingly over its useful life of 10 years.

During 2007, the Company has written-off 5,372 licenses due to a reduction of personnel, in the amount of RUR 235 million, including capitalized interest of RUR 30 million.

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

Amdocs Billing Suite

As of 31 December 2007 software also includes Amdocs Billing Suite software with a net book value of RUR 762 million (2006: RUR 690 million), This software was purchased for the purpose of the implementation of unified automated billing system. The project of implementation of the unified automated billing system is expected to last 4-5 years.

Amdocs Billing Suite software was supplied in December 2005 by LLC IBM Eastern Europe/Asia, in exchange for 18 zero coupon promissory notes for the total amount of RUR 649 million. As at 31 December 2007, the promissory notes have been repaid.

The Company will commence amortizing this asset from the date of software implementation. Up to this moment the Company intends to perform the annual impairment test of the asset. During 2007, the Company recognised a write-off in the amount of RUR 107 million that was due to a partial deferral of implementation.

Licences

As of 31 December 2007 licences mainly included licences for providing the following types of services:

- local and intrazone telecommunication services;
- data transmission services with the exception of data transmission services for voice information transmission;
- telematic services;
- telegraph services;
- radio communication;
- local telecommunication services by payphones.

8. Consolidated subsidiaries

		Ownership,%		Voting Shares, %	
Subsidiary	**Activity**	**2007**	**2006**	**2007**	**2006**
OJSC Stavtelecom	Fixed line operator	100	100	100	100
OJSC Orbita Recreational House	Recreation services	100	100	100	100
OJSC Intmashservice	Repairs of communication facilities	100	100	100	100
CJSC Armavirskiy Zavod Svyazi	Cable production	100	100	100	100
CJSC Yugsvyazstroy	Construction services	100	100	100	100
LLC Factorial-99	Information agency	100	100	100	100
LLC YuTC-Finance	Financial services	100	100	100	100
CJSC TRC Photon	TV and radio broadcasting	-	51	-	51
LLC TO Accent	TV and radio broadcasting	-	51	-	51

(In millions of Russian roubles)

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

Discontinued operations

In April 2007 the Company sold its 51% interests in CJSC TRC Photon and LLC TO Accent for RUR 25 million and RUR 11 million respectively, to local authorities.

Total profit from discontinued operations after tax for 2007 is RUR 19 million (2006: loss of RUR 14 million).

9. Investments in associates

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

		2007		2006	
Associate	**Activity**	**Voting shares, %**	**Carrying value**	**Voting shares, %**	**Carrying value**
CJSC Volgograd GSM	Cellular services (GSM)	50	615	50	506
CJSC TeleRoss Kubanelektrosvyaz	Telecommunication services	-	-	50	20
CJSC TeleRoss-Volgograd	Telecommunication services	-	-	50	4
Total			**615**		**530**

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

The Company has investments in the following associates whose net assets were negative as of 31 December 2007 and 2006:

			Net assets as of 31 December	
Associate	**Activity**	**Voting share, %**	**2007**	**2006**
LLC Yug-Giprosvyaz	Project engineering	24	(9)	(5)
CJSC IR Telekinocompaniya	Commercial TV	24	(1)	(1)

The carrying value of investments in associates shown in these consolidated financial statements equals to the Company's share in net assets of the associated companies, except for investments in LLC Yug-Giprosvyaz and CJSC IR Telekinocompaniya. The carrying amount of investments in the latter associates was reduced to nil as these associates have accumulated losses exceeding the cost of the respective investments.

Gain on disposal of investments accounted for using the equity method is disclosed in note 28.

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

	2007	2006
Investments in associates as of 1 January, net	**530**	**564**
Share of income net of income tax	189	105
Dividends received	(87)	(129)
Impairment loss	-	(10)
Disposal of associates	(17)	-
Investments in associates as of 31 December, net	**615**	**530**

(In millions of Russian roubles)

The following table illustrates summarised financial information of the most significant associates:

Associate	Voting shares, %	Assets	Liabilities	Revenues	Net profit/(loss)
2007					
CJSC Volgograd GSM	50	2,029	(799)	1,796	376
2006					
CJSC Volgograd GSM	50	1,991	(979)	1,336	202
CJSC TeleRoss Kubanelektrosvyaz	50	43	(3)	52	16
CJSC TeleRoss-Volgograd	50	7	(1)	2	(1)

10. Long-term investments

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

	2007	2006
Long-term investments held-to-maturity	7	-
Long-term investments available-for-sale	15	15
Total long-term investments	**22**	**15**

As of 31 December 2007 and 2006 investments available-for-sale comprised the following:

	2007		2006	
Company	Ownership interest, %	Carrying value	Ownership interest, %	Carrying value
OJSC Svyazintech	11.00	13	11.00	13
CJSC RusleasingSvyaz	3.65	1	3.65	1
OJSC BETO	0.15	1	0.15	1
Total investments available-for-sale		**15**		**15**

Management believes that the carrying amount of these investments approximates their fair values.

11. Other long-term assets

As of 31 December 2007 and 2006 other long-term assets comprised the following:

	2007	2006
Long-term VAT receivable	120	170
Long-term loans given	3	8
Other	19	26
Total	**142**	**204**

12. Long-term advances given

(In millions of Russian roubles)

As of 31 December 2007 and 2006 long-term advances given to suppliers of equipment comprised the following:

	2007	2006
Advances given for capital construction	47	48
Acquisition and implementation of Oracle E-Business Suite software (note 7)	-	108
Total	**47**	**156**

13. Inventories

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

	2007	2006
Cable, materials and spare parts for telecommunications equipment	279	300
Construction materials, fuels and instruments	69	79
Finished goods and goods for resale	24	67
Instruments, special cloths, inventory	65	84
Other inventories	269	265
Provision for inventory obsolescence	(25)	(17)
Total	**681**	**778**

14. Accounts receivable

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

	Gross as at 31 December 2007	Allowance for impairment of receivables	Net as at 31 December 2007
Residential customers	432	(70)	362
Corporate customers	149	(22)	127
Interconnected operators	363	(35)	328
Governmental customers	82	(4)	78
Tariff compensation from the state budget	41	(27)	14
Other receivables	101	(24)	77
Total	**1,168**	**(182)**	**986**

	Gross as at 31 December 2006	Allowance for impairment of receivables	Net as at 31 December 2006
Residential customers	347	(98)	249
Corporate customers	158	(23)	135
Interconnected operators	190	(40)	150
Governmental customers	84	(7)	77
Tariff compensation from the state budget	122	(122)	-
Other receivables	93	(2)	91

(In millions of Russian roubles)

Total	**994**	**(292)**	**702**

The Company invoices its governmental and corporate customers on a monthly basis. The Company sends monthly payment requests to its residential customers and substantially relies upon these customers' timely payments based on the payment requests. All customer payments are based upon tariffs, denominated in roubles, in effect at the time the calls are made. In certain cases the Company received penalty fees for delayed payments and enforced payments through court decisions.

The following table summarises the changes in the allowance for impairment of accounts receivable:

	2007	**2006**
Balance as of 1 January	**292**	**744**
Trade receivables write-off	(86)	(51)
Reversal of impairment for the year	(24)	(401)
Balance as of 31 December	**182**	**292**

15. Other current assets

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

	2007	**2006**
VAT receivable	507	441
Deferred expenses	114	116
Other prepaid taxes	14	12
Settlements with personnel	7	8
Other receivables and current assets	193	155
Allowance for impairment of other current assets	(27)	-
Total	**808**	**732**

16. Cash and cash equivalents

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

	2007	**2006**
Cash in hand and in bank	562	331
Total	**562**	**331**

The Company uses an identical policy to define the composition and valuation of cash and cash equivalents for the balance sheet and for the cash flow statement.

17. Significant non-cash transactions

Included in revenues are non-cash transactions amounting to RUR 469 million (2006: RUR 3,501 million). These transactions represent mainly mutual offset of the balances with the same customer or supplier incurred in the course of normal operating activities.

Non-cash transactions above have been excluded from the consolidated statement of cash flows.

(In millions of Russian roubles)

18. Share Capital

The number of outstanding shares is as follows:

	Number of shares authorised (millions)	Par value	Carrying value
As of 31 December 2005	**3,933**	**1,298**	**3,039**
Ordinary	2,961	977	2,288
Preference	972	321	751
As of 31 December 2006	**3,933**	**1,298**	**3,039**
Ordinary	2,961	977	2,288
Preference	**972**	**321**	**751**
As of 31 December 2007	**3,933**	**1,298**	**3,039**

The ordinary and preference shares have a par value of RUR 0.33 per share. All authorised shares have been issued and fully paid.

The difference between the total par value and the total carrying value of share capital represents the effects of inflation accumulated until 1 January 2003.

The ordinary shareholders are entitled to one vote per share.

Preference shares give the holders the right to participate in general shareholders' meetings without voting rights except in instances where decisions are made in relation to the reorganization and liquidation of the Company, and in relation to changes and amendments to the Company's charter which restrict the rights of preference shareholders. The preference shares have no rights of redemption or conversion but carry non-cumulative dividends per share of 10% of the Russian accounting net income for the year. If the Company fails to pay the above mentioned dividends, or has no profits in any year, the preferred shareholders have the right to vote in the general shareholders' meeting. Owners of the preferred shares have the right to participate in and vote on all issues within the competence of general meetings following the annual general meeting in which a decision not to pay (or to pay partially) dividends on preferred shares has been taken. Annual amount of dividends on preference shares may not be less than dividends on ordinary shares. The preference shareholders participate in earnings along with ordinary shareholders. Accordingly, the Company's preferred shares are considered participating equity instruments for the purpose of earnings per share calculations (refer to note 30).

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

Distributable earnings of the parent company are limited to its retained earnings, as mandated by statutory accounting rules. Statutory retained earnings of the Company as of 31 December 2007 and 2006 amounted to RUR 8,375 million and RUR 6,788 million respectively.

In accordance with the Company's Dividend policy, dividends may only be declared to the shareholders of the Company from net income as shown in the Company's Russian statutory financial statements. The Company reported net income of RUR 1,827 million and RUR 1,184 million in its statutory financial statements in 2007 and 2006, respectively.

Dividends were declared in 2007 in respect of 2006 to holders of ordinary shares and preference shares of Rouble 0.053031 per ordinary share (2006: Rouble 0.01031 per ordinary share) and Rouble 0.121838 per preference share (2006: Rouble 0.031395 per preference share). Refer to note 31.

(In millions of Russian roubles)

In February 1998, the Company placed Level 1 American Depositary Receipts (ADRs). Each depository receipt is equal to 50 ordinary shares of the Company.

The following table represents ADR registration for 2006-2007:

Date	ADR (quantity)	Ordinary Shares Equivalent (quantity)	Ordinary Shares %	Charte Capit %
31 December 2005	**2,826,679**	**141,333,950**	**4.77**	**3.**
Additions 2006	830,938	41,546,900	1.40	1.
31 December 2006	**3,657,617**	**182,880,850**	**6.18**	**4.**
Disposals 2007	(218,349)	(10,917,450)	(0.37)	(0.2
31 December 2007	**3,439,268**	**171,963,400**	**5.81**	**4.**

Currently the ADR's are traded on the following stock markets:

Stock market	CUSIP(WKN)	ADR ticker	ISIN
Over-the-counter (OTC) market (USA)	843899105	STJSY	S1843899105
Frankfurt Stock Exchange (FSE)	912640	KUE.FRA	US8438991056
Berlin Stock Exchange (BerSE)	912640	KUE	US8438991056
NEWEX (Vienna, Austria)	912640	KUE	US8438991056

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

	Ordinary shares		Preference shares		
	Number (thousands)	**%**	**Number (thousands)**	**%**	**Total**
OJSC Svyazinvest	1,500,671	50.69	-	-	1,500,671
Other legal entities	1,219,955	41.21	773,876	79.60	1,993,831
Individuals	239,887	8.10	198,276	20.40	438,163
Total	**2,960,513**	**100.00**	**972,152**	**100.00**	**3,932,665**

19. Loans and borrowings

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

	Interest rate	Maturity date	2007	2006
Short-term borrowings				
Bank loans (Russian Roubles)	6.8%	2008	1,612	267
Promissory notes (Russian Roubles)	9.75%	2008	200	600
Interest accrued	-	-	369	314
Total short-term borrowings			**2,181**	**1,181**
Long-term borrowings				
Bank loans				
Bank loans (Russian Roubles)	9-10%	2008-2011	3,115	2,696

(In millions of Russian roubles)

	Interest rate	Maturity date	2007	2006
Bank loans (US dollars)	LIBOR+(4.4%-5.6%)	2009-2013	4,296	4,608
Total bank loans			**7,411**	**7,304**
Bonds (Russian Roubles)	7.77%-10.45%	2008-2010	**8,688**	**9,573**
Vendor financing (Euro)			-	80
Promissory notes (Russian Roubles)	8%-9.77%	2008	1,539	1,005
Other borrowings (Russian Roubles)			48	49
Less: Current portion of long-term borrowings			(4,654)	(11,680)
Total long-term borrowings			**13,032**	**6,331**

As of 31 December 2007 bank borrowings are secured by property, plant and equipment with the carrying value of approximately RUR 6,071 million (2006: RUR 6,324 million) (see note 6).

As of 31 December 2007 loans and borrowings had the following maturity schedule:

Maturit date	Bank loans	Bonds	Promissory notes	Other	Total
2008	4,078	854	1,894	9	**6,8**
2009	1,262	5,929	-	3	**7,1**
2010	1,386	1,996	-	2	**3,3**
2011	886	-	-	27	**9**
2012	767	-	-	2	**7**
After 2012	767	-	-	5	**7**
Total	**9,146**	**8,779**	**1,894**	**48**	**19,8**

The Company's borrowings are denominated in the following currencies:

Currency	2007	2006
Russian Roubles	14,973	13,827
US dollars	4,419	4,744
Euro	475	621
Total	**19,867**	**19,192**

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

Short-Term Borrowings

Bank Loans

OJSC Sberbank

Short-term borrowing from OJSC Sberbank represents a Rouble denominated loan received in 2007. The loan accrues annual interest of 6.8%. The principle amount outstanding as of 31 December 2007 was RUR 1,600 million. The loan is not secured.

Promissory notes

In 2007 the Company issued promissory notes to OJSC Vneshtorgbank. The promissory notes mature in 2008. Amount of promissory notes outstanding as of 31 December 2007 was equal to RUR 200 million.

Long-Term Borrowings

Below is a summary of individually significant long-term loans and borrowings.

Bank Loans

OJSC Sberbank

In 2003-2006 the Company raised a number of long-term loans denominated in Roubles amounting to RUR 1,760 million. The loans bear annual interest at 9.5%. The loans mature in 2008. As of 31 December 2007, the amounts outstanding were equal to RUR 1,760 million and presented in long-term borrowings. The loans are secured with property, plant and equipment valued at RUR 2,087 million.

OJSC Megregionalny Kommerchesky Bank Razvitiya Svyazi i Informatiki

Long-term borrowing from OJSC Megregionalny Kommerchesky Bank Razvitiya Svyazi I Informatiki represents a Rouble denominated loan of RUR 1,000 million received in 2007. The loan matures in 2010. The loan accrues annual interest of 9%. As of 31 December 2007, the principal amount outstanding was RUR 1,000 million. The loan is not secured.

Ministry of Finance of Russian Federation

In 1995-1996, the Ministry of Finance of the Russian Federation provided long-term financing to the Company to purchase telecommunications equipment from various foreign vendors. Vnesheconombank acted as the agent on behalf of the Government of Russian Federation. The loans are denominated in Euro. In July 2005 the Company received a claim from the Ministry of Finance of the Russian Federation for immediate repayment of outstanding amount overdue of RUR 974 million (Euro 28 million) to the bank.

In December 2006 at the stage of legal proceedings the Company signed an amicable agreement with Ministry of Finance. On 5 March 2007 terms of the amicable agreement were approved by Arbitrary Court of Krasnodar region. The amicable agreement came into force on 27 December 2006 and stipulates a restructuring of the Company’s liability: penalty interest accrued for untimely payments in the amount of RUR 330 million (Euro 9,5 million) is forgiven and the principal amount will be paid in equal annual instalments during a period from 27 December 2006 to 1 January 2012. Interest on restructured debt is payable at 2% per annum.

As at 31 December 2007 the outstanding amount of the debt to the Ministry of Finance was accounted for at amortised cost using effective interest rate of 10.06% and amounted to RUR 475 million, including short term part in the amount of RUR 119 million. The liability is secured by property, plant and equipment valued at RUR 1,260 million

Credit Suisse International

In 2006 the Company entered into two loan agreements with Credit Suisse International. Financing agreement in the amount of 50 million US dollars was signed in August 2006 and Guaranteed financing agreement in amount of 125 million US dollars was signed in September 2006. Credit period for the first loan is 37 months, including grace period of 24 months. The loan bears interest at a rate which is an aggregate of Margin (5.60%) and LIBOR. The loan was obtained in order to refinance the Company's debt. The loan is secured by equipment valued at RUR 1,673 million under pledge agreement. Credit period for the second loan is 7 years, including grace period of 4 years. The loan bears interest at a rate which is an aggregate of Margin (4.40%) and LIBOR. The loan was obtained in order to refinance the Company's debt. The loan is secured by bank guarantee under the agreement concluded between the Company and JSC Vneshtorgbank. In accordance with this agreement Company pays commission in the amount of 0.3% of the guaranteed amount on a quarterly basis. Bank guarantee is secured by equipment valued at RUR 3,360 million (125 million US dollars). Amount outstanding under these loans as of 31 December 2007 was RUR 4,296 million.

The loan agreements concluded between the Company and Credit Suisse International provide for certain covenants to be complied with by the Company at the end of each interim quarterly period. The covenants are defined on the basis of financial statements prepared under the Russian statutory accounting regulations.

- The Company's ratio of "net debt" (an aggregate of long-term and short term borrowings less amount of cash) to "adjusted income" (aggregate amount of operating income, other operating income, amortisation less the amount of other operating costs) for the three months period before the date of ratio calculation ("adjusted income" for previous quarter of the same financial year is not included to calculation) should not exceed 20:1; - The Company's ratio of "net debt" to equity should not exceed 2.5 to 1;

- As of 31 March, 30 June, 30 September and 31 December, the Company's ratio "adjusted income" to interest payable for the 3 month period preceding the relevant calculation date (but not including "adjusted income" and interest payable for the quarter preceding such period of the same financial year) shall be at least 2.5 to 1.

During 2007 and as of 31 December 2007, the Company was in line with the above covenants.

Bonds

Bonds (Series 02)

On 11 February 2004 the Company issued 1,500 thousand non-convertible interest-bearing bonds, Series 02, par value of 1,000 Roubles each. The bonds mature in 3 years from the date of issue and have 6 semiannual coupons. The interest rate under the first and second coupons was set at 9.25% per annum, on the third and fourth coupons - 12% per annum, on the fifth and sixth coupons – 10.5% per annum. These bonds had two options of early redemption at par – in February 2005 and February 2006. In February 2005 and February 2006 bondholders exercised the right of early redemption in the amount of RUR 1,093 million and RUR 218 million, respectively, and these bonds were placed at the secondary market at par for the same amount. These bonds were fully redeemed in February 2007.

Bonds (Series 03)

On 6 October 2004 the Company issued 3,500 thousand non-convertible interest-bearing bonds, Series 03, par value of 1,000 Roubles each. Bonds mature in five years from the date of issue and have 10 semiannual coupons. The interest rate under first three coupons is 12.3 % per annum, interest rate for fourth, fifth and sixth coupons set at 10.9% per annum, interest rates under next coupons will be set 10 days prior to payment of the coupon. The bond issue has two options of early redemption at par value in April 2006 and in October 2007. In April 2006 bondholders did not exercise their right of early redemption. In October 2007 bondholders exercised the rights of early redemption in the amount of RUR 2,860 million, and these bonds were placed at the secondary market at par for the same amount. As there is no right of early redemption of bonds in 2008, the outstanding liability was classified as long-term borrowings as at 31 December 2007.

(In millions of Russian roubles)

Bonds (Series 04)

In December 2005 the Company issued 5,000 thousand non-convertible interest-bearing bonds Series 04, par value of 1,000 Roubles each. Bonds mature in four years from the date of issue and have 16 quarterly coupons. The interest rate under first four coupons is set at 10.5%, and 10% per annum for the rest of the coupons. In accordance with the terms of the offering, in December 2006 the Company redeemed RUR 500 million of these bonds. In June and December 2007 the Company redeemed second and third portions of the issue in amount of RUR 1,250 million. The rest of the obligation is to be settled in several installments during the period from 2008 to 2009. Respectively, the bonds in amount RUR 750 million are included in to current portion of long-term borrowings and the remaining part of these bonds obligations is included into long-term borrowings as of 31 December 2007.

Bonds (Series 05)

In May 2007 the Company issued 2,000 thousand non-convertible interest-bearing bonds, Series 05, par value 1,000 Roubles each. Bonds mature in five years from the date of issue and have semiannual coupons. The interest rate under first six coupons is set at 7.55% per annum. The interest rates under next seven to ten coupons will be set 10 days prior to payment of the coupon. The outstanding liability was classified as long-term borrowings as at 31 December 2007.

The bonds do not provide any put options.

Promissory notes

In 2006 the Company issued non-interest bearing promissory notes to OJSC Vneshtorgbank. These promissory notes mature in 2008. Amount outstanding as at 31 December 2007 is RUR 825 million and is classified as current portion of long-term borrowings. Effective interest rate is 9.23-9.77% per annum.

In 2007 the Company issued promissory notes to OJSC Megregionalny Kommerchesky Bank Razvitiya Svyazi I Informatiki. These promissory notes mature in 2008. Amount outstanding as at 31 December 2007 is RUR 714 million and is classified as short-term borrowings. Effective interest rate is 8.0-9.33% per annum.

20. Finance Lease Liabilities

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

	2007		**2006**	
	Minimum lease payments	**Present value of payments**	**Minimum lease payments**	**Present value of payments**
Current portion	970	758	1,199	
From 1 to 5 years	553	472	1,522	1,
Total minimum lease payments	**1,523**	**1,230**	**2,721**	**2,**

(In millions of Russian roubles)

Less amounts representing finance charges	(293)	-	(680)	
Present value of minimum lease payments	**1,230**	**1,230**	**2,041**	**2,**

In 2007 and 2006 the Company's primary lessor was OJSC RTC-Leasing. In 2007 and 2006 the effective interest rate on lease liabilities ranged from 20 % to 25 % per annum.

OJSC RTC-Leasing purchases telecommunication equipment from domestic and foreign suppliers and provides such equipment to the Company under finance lease agreements. OJSC RTC-Leasing is entitled to adjust the lease payment schedule in the event of a change in certain economic conditions, in particular, a change in the refinancing rate of the Central Bank of the Russian Federation.

Guarantees issued in favour of OJSC RTC-Leasing are described in note 33.

21. Accounts Payable, Accruals and Advances Received

As of 31 December 2007 and 2006 accounts payable and other current liabilities comprised the following:

	2007	**2006**
Accounts payable for capital investments	1,361	836
Accounts payable to interconnected operators	200	163
Trade accounts payable – other	814	885
Salaries and wages	636	690
Advances received from subscribers	390	363
Payables to OJSC Rostelecom	154	145
Advances received on disposal of assets	63	53
Other accounts payable	104	208
Total	**3,722**	**3,343**

22. Other taxes payable

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

	2007	**2006**
Value-added tax	16	72
Property tax	183	178
Unified social tax	93	89
Employees' income tax	46	40
Other taxes	10	7
Total	**348**	**386**

23. Pensions and Other Post-Employment Benefit Plans

(In millions of Russian roubles)

In addition to statutory pension benefits, the Company also contributes to post-employment benefit plans, which cover most of its employees.

The defined benefit pension plan provides an old age retirement pension and disability pension. The plans provide for payment of retirement benefits starting from the statutory retirement age, which is currently 55 for women and 60 for men. The benefits are based on a formula specific to each branch of the Company. According to the formula the benefits depend on a number of parameters, including an employee's salary at the retirement date and number of years with the Company. The benefits do not vest until and are subject to the employee retiring from the Company on the above-mentioned ages, with the exception of employees made redundant in less than two years up to being eligible for state pension.

The non-government pension funds Telecom-Soyuz, which is related to the Company (note 35), maintains the defined benefit pension plan. The Company makes contributions to the pension funds in the amount set forth in the agreement with the pension fund.

The Company further provides other long-term employee benefits of a defined benefit nature, such as lump-sum payments on occasion of death, disability, retirement; as well as jubilee payments to its employees and pensioners.

Additionally the Company provides financial support of a defined benefit nature to its old age and disabled pensioners.

As of 31 December 2007 there were 28,572 working employees participating in the defined benefit pension plans of the Company and 8,830 pensioners eligible to other post-employment benefit plans provided by the Company (as of 31 December 2006 – 31,017 and 9,080 respectively).

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

	2007	2006
Present value of defined benefit obligation	2,052	1,908
Fair value of plan assets	-	-
Present value of unfunded obligations	**2,052**	**1,908**
Unrecognized past service cost	(208)	(43)
Unrecognized actuarial losses	(386)	(582)
Net pension liabilities	**1,458**	**1,283**

As of 31 December 2007 management estimated the employees' average remaining working life at 9 years (2006 - 9 years).

The amount of net expense for the defined benefit pension plans recognized in 2007 and 2006 was as follows:

	2007	2006
Interest cost	136	137
Service cost	93	93
Expected return on plan assets	-	(2)
Actuarial losses	15	52
Amortization of past service cost	33	66
Past service cost recognized in current year	11	196
Curtailment or final settlement effect	16	59
Net expense for the defined benefit pension plans	**304**	**601**

(In millions of Russian roubles)

Expenses in respect of the defined benefit pension plans were included in the line “Wages, salaries, other benefits and payroll taxes” of the consolidated income statement.

Changes in the present value of the defined benefit obligation in 2007 and 2006 were as follows:

	2007	2006
Defined benefit obligation at January 1	**1,908**	**1,983**
Interest cost on benefit obligation	136	137
Current service cost	93	93
Past service cost	209	(98)
Benefits paid	(45)	(52)
Liabilities extinguished on settlements	(84)	(181)
Actuarial (gains)/losses on obligation	(165)	26
Defined benefit obligation at December 31	**2,052**	**1,908**

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

	2007	2006
Net liability as of 1 January	1,283	868
Net expense for the year	304	601
Contributions	(129)	(186)
Net liability as of 31 December	**1,458**	**1,283**

Movements in the assets of defined benefit pension and other post-employment benefit plans during 2007 and 2006 were as follows:

	2007	2006
Fair value of plan assets as of 1 January	**-**	**47**
Actual return on plan assets	-	-
Employer contributions	129	186
Settlements	(84)	(181)
Benefits paid	(45)	(52)
Fair value of plan assets as of 31 December	**-**	**-**

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

	2007 per annum	2006 per annum
Discount rate	6.60%	7.00%
Expected return on plan assets	n/a	n/a
Future salary increases, nominal	9.20%	9.20%
Relative pay increase (career progression)	1.00%	1.00%
Rate used for calculation of annuity value	6.00%	6.00%
Increase in financial support benefits	5.00%	5.00%
Staff turnover	7.00%	7.00%
Mortality tables (source of information)	USSR 1985/86	USSR 1985/86

Amounts for the current and previous four periods are as follows:

(In millions of Russian roubles)

	2007	2006	2005	2004	2003
Present value of defined benefit obligation	2,052	1,908	1,982	1,597	1,168
Plan assets	-	-	(47)	(205)	(146)
Deficit	2,052	1,908	1,935	1,392	1,022
Experience adjustments on plan liabilities	229	67	113	(419)	10
Experience adjustments on plan assets	-	-	(18)	(1)	6

The amount of experience adjustments is included into actuarial gains and losses and represents effects of differences between the previous actuarial assumptions and what has actually occurred. Experience adjustments on plan liabilities in the year 2007 and prior periods were caused primarily by non-recurring considerable excess of actual number of dismissed employees, as well as of the change in the amount of benefits set out in the terms of the plan, over initially projected changes in respective parameters in the long-term perspective.

24. Provisions

	Tax provisions (Note 33)	Provision for claim from CJSC Westelcom	Guarantees	Total
Balance at 31 December 2005	**-**	**-**	**20**	**20**
Accrual of provision	118	44	-	162
Reclassification from long-term part	-	-	19	19
Amortisation of provision	-	-	(20)	(20)
Balance at 31 December 2006	**118**	**44**	**19**	**181**
Accrual of provision	-		-	-
Reclassification from long-term part	-	-	14	14
Amortisation of provision	-	-	(19)	(19)
Utilisation of provision		(44)		(44)
На 31 декабря 2007 г.	**118**	**-**	**14**	**132**

The Company guaranteed the credit line facilities provided by OJSC Sberbank to OJSC RTC-Leasing, a lessor of telecommunication equipment. The total amount of loans guaranteed as of 31 December 2007 is RUR 674 million (2006: RUR 1,407 million). As of 31 December 2007 the carrying amount of such guarantees issued amounted to RUR 18 million (2006: RUR 37 million).

During 2007, movements in long-term provisions were as follows:

	Guarantees (Note 33)
Balance at 31 December 2005	**37**
Provision reclassified to current part	(19)
Balance at 31 December 2006	**18**
Provision reclassified to current part	(14)
Balance at 31 December 2007	**4**

25. Revenues

Revenues for the years ended 31 December 2007 and 2006 comprised the following:

By revenue type	2007	2006
Local telephone services	9,008	8,443

(In millions of Russian roubles)

Intra-zone connection	3,769	3,101
Interconnection services	2,901	2,915
Data transmission, telematic services (Internet), telegraph services	2,878	1,849
Fees on assistance services	557	721
Radio and TV broadcasting	315	275
Other telecommunications services	136	65
Other revenues	667	590
Total	**20,231**	**17,959**

Local telephone services and intra-zone connection include revenue for rent of a subscriber line in the amount of RUR 491 million (2006: RUR 428 million).

Revenue from installation is included in revenue on local telephone services in the amount of RUR 437 million (2006: RUR 480 million).

The Company identifies revenue by the following major customer groups:

Customer groups	**2007**	**2006**
Residential customers	10,337	9,024
Corporate customers and interconnected operators	8,117	7,428
Governmental customers	1,777	1,507
Tariff compensation from the state budget	-	-
Total	**20,231**	**17,959**

26. Other Operating Expenses

Other operating expenses, net for the years ended 31 December 2007 and 2006 comprised the following:

(In millions of Russian roubles)

	2007	2006
Advertising expenses	52	59
Lease of premises	218	204
Fire and other security services	253	248
Universal service fund payments	193	167
Non-commercial partnership expenses (note 35)	184	113
Business travel expenses and representation costs	51	57
Insurance of property	21	40
Charitable contributions	46	35
Audit and consulting fees	53	49
Cost of goods sold	94	74
Tax provision	-	118
Agency fee	223	122
Post services	11	10
Education expenses	22	22
Provision for Westelcom claim	-	44
Transportation charges	36	47
Reimbursement of losses from provision of universal telecommunication services	(98)	-
Other expenses	556	491
Total	**1,915**	**1,900**

In 2007 the Company made payments to the Universal service fund. These payments are prescribed by the Federal Law on Communications and Government Decree # 243 of 21 April 2005. Payments are calculated as 1.2 % of the revenues from the telecommunication services less revenues from interconnection services.

Other expenses include expenses related to third party services and managerial costs; credit organisations charges, inventory impairment charges and non-core activity expenses.

(In millions of Russian roubles)

27. Interest expense, net

Interest expense, net for the years ended 31 December 2007 and 2006 comprised the following:

	2007	2006
Interest income	(17)	(7)
Interest expense on bank and other borrowings	1,734	1,778
Interest expense accrued on finance leases	368	543
Other finance charges	50	(21)
Total	**2,135**	**2,293**

28. Gain on sale of investments

Gain from sale of associates and other investments for the year ended 31 December 2007 and 2006 comprised the following:

	2007	2006
Gain on disposal of shares of CJSC TeleRoss Kubanelektrosvyaz	24	-
Gain on disposal of shares of CJSC TeleRoss-Volgograd	1	-
Other gain on investments	15	13
Total	**40**	**13**

29. Income Tax

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

	2007	2006
Current income tax expense	(567)	(222)
Deferred income tax charge	(28)	(207)
Total income tax for the year	**(595)**	**(429)**

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

	2007	2006
Profit before income tax	**1,791**	**790**
Statutory income tax rate	24%	24%
Income tax at applicable income tax rate of 24%	(430)	(190)
Increase/(decrease) resulting from the effect of:		
Non-taxable income	114	79
Non-deductible expenses and other permanent differences	(279)	(318)
Total income tax charge for the year	**(595)**	**(429)**
Effective income tax rate	**33%**	**54%**

(In millions of Russian roubles)

The composition of deferred income tax assets and liabilities as of 31 December 2007 and 2006 was as follows:

	2007	2006
Deferred tax assets		
Accounts payable and accrued expenses	12	95
Accounts receivable	8	43
Deferred revenue	75	86
Pension liabilities	165	165
Total deferred tax assets	**260**	**389**
Deferred tax liabilities		
Property, Plant and Equipment	(768)	(742)
Intangible assets	(164)	(183)
Investments	(55)	(52)
Finance lease	(154)	(211)
Loans and borrowings	(43)	(87)
Other	(25)	(35)
Total deferred tax liabilities	**(1,209)**	**(1,310)**
Deferred tax liabilities, net	**(949)**	**(921)**

The Company has not recognised a deferred tax liability in respect of investments in subsidiaries in the amount of RUR 88 million (2006 – RUR 89 million), as management believes that the Company is able to control the timing of reversal of respective temporary differences, and reversal is not expected in the foreseeable future.

The movement in net deferred tax liabilities for the years ended 31 December 2007 and 2006 is presented below:

	2007	2006
Deferred tax liability, net as of 1 January	**(921)**	**(719)**
Deferred income tax charge	(28)	(207)
Transfer to disposal group	-	5
Deferred tax liability, net as of 31 December	**(949)**	**(921)**

In the context of the Company's current structure, tax losses and current tax assets of the different companies may not be set off against current tax liabilities and taxable profits of other companies and, accordingly, taxes may accrue even if there is a net consolidated tax loss. Therefore, a deferred tax asset of one company is not offset against a deferred tax liability of another company.

30. Earnings per Share

The Company has no financial instruments which may be converted into ordinary shares; therefore, the diluted earnings per share equal to basic earnings per share.

	2007	2006
Profit for the year attributable to equity holders of the Parent	1,215	350
Less: attributable to preference shareholders	(300)	(86)
Attributable to ordinary shareholders	915	264
Weighted average number of ordinary shares outstanding (thousands), note 18	2,960,513	2,960,513
Basic and diluted earnings per share, attributable to ordinary equity holders of the Parent, Russian	**0.31**	**0.09**

(In millions of Russian roubles)

Roubles

31. Dividends Declared for Distribution

Dividends declared in 2007 based on 2006 results:

Dividends on ordinary shares - 0.053031 Roubles per share	157
Dividends on preference shares – 0.121838 Roubles per share	118
Total	**275**

Dividends paid to shareholders are determined by the Board of Directors and declared and officially approved at the annual shareholders' meeting. Earnings available for dividends are limited to profits of OJSC Southern Telecommunications Company determined in accordance with the Russian statutory accounting regulations. Dividends are accrued in the year they are declared and approved.

32. Operating Lease

As of 31 December 2007 and 2006 minimum lease payments under non-cancelable operating leases where the Company is a lessee were allocated by years as follows:

	2007 Minimum lease payments	**2006** Minimum lease payments
Current portion (less than 1 year)	55	32
From 1 to 5 years	84	66
Over 5 years	524	489
Total minimum lease payments	**663**	**587**

In 2007 operating lease expenses of the Company recorded in "Other operating expenses" line of the consolidated income statement amounted to RUR 65 million (2006 - RUR 56 million).

33. Contingencies and Operating Risks

Operating Environment of the Company

The Russian Federation has been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in this environment. Whilst there have been improvements in the Russian economic situation, such as an increase in gross domestic product and a reduced rate of inflation, Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. Consequently, operations in the Russian Federation involve risks that typically do not exist in other markets. The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

Taxation

Russian tax, currency and customs legislation is subject to varying interpretations and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Company may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. It is not practical to determine the amount of unasserted claims that may manifest, if any, or the likelihood of any unfavourable outcome.

Based on the results of the tax audits for 2002-2003, the tax authorities issued to the Company tax claims in the amount of RUR 678 million and fines and penalties of RUR 376 million in respect of settlements with other operators under interconnection agreements. The Company is disputing this decision of Federal Tax Service at court. At present the litigation is under consideration by the Arbitrary Court of Moscow. According to decision of the Arbitrary Court of Moscow dated 27 May 2008, court hearings are postponed. Based on similar court practice in 2006, the management believes that it is probable that a number of episodes of these disputes will be decided in favour of tax authorities. Accordingly, during 2006 the Company created a provision for negative outcome of this litigation in the amount of RUR 118 million (note 24).

Based on the results of the tax audits for 2004-2006, the tax authorities issued to the Compay tax claims in the amount of RUR 295 million, including fines and penalties of RUR 77 million. These tax claims relate primarily to settlements with interconnected operators.

However, management considers that with high level of probability claims of tax authorities will be declared invalid based on the results of similar tax audits and corresponding results of court hearings with participation of other subsidiaries of OAO Svyzinvest Group. As of 31 December 2007, the Company`s financial statements does not contain any other adjustments than the above stated, in which necessity can arise, if decision of tax authorities based on tax audits for 2002-2003 and 2004-2006 periods will be declared valid by a court.

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

Insurance

Insurance services are still developing in Russia and many services, available in other countries, are not yet widespread in the Russian Federation. During 2007 and 2006 the Company did not maintain insurance coverage on a significant part of its property, plant and equipment, business interruption losses or third party liability in respect of property or environmental damage arising from accidents relating to the Company’s property or the Company’s operations. Until the Company obtains adequate insurance coverage, there is a risk that losses resulting from destruction of certain assets could have a material adverse effect on the Company’s operations and financial position.

Legal claims and litigation

Management is unable to estimate what developments may occur in respect of the Russian legal system or the resulting effect of any such developments on the Company’s financial position or future results of operations. In the nearest future the Company’s activity could be subject to judicial reform factors. No adjustments related to these uncertainties were recognized in the consolidated statements.

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

(In millions of Russian roubles)

Licences

Substantially main part of the Company's revenues is derived from operations conducted pursuant to licences granted by the Russian Government. These licences expire in various years ranging from 2008 to 2012. Suspension or termination of the Company's main licences or any failure to renew any or all of these main licences could have a material adverse effect on the financial position and operations of the Company.

The Government of the Russian Federation is in process of liberalization of telecommunications market for which additional licences for rendering telecommunication services have been granted to a number of alternative operators. It is possible that the Company's future results of operations and cash flows could be materially affected by the increased competition in a particular period but the effect can not be currently determined.

Guarantees issued

The Company mainly guaranteed credit line facilities provided by OJSC Sberbank of Russia to OJSC RTC-Leasing, a lessor of telecommunication equipment (note 20). As of 31 December 2007 the total guarantees amounted to RUR 674 million (2006 - RUR 1,407 million). Management believes that the likelihood of significant payments being required under these agreements is remote. As at 31 December 2007, the Company did not have any contractual commitments to extend financial guarantees, credit or other assistance.

34. Contractual Commitments

Capital Investments

As of 31 December 2007 the Company has commitments for capital investments into modernization and expansion of its network in the amount of RUR 312 million (2006 – RUR 493 million).

35. Balances and Transactions with Related Parties

The nature of the related party relationships for those related parties with whom the Company entered into significant transactions during 2007 or had significant balances at 31 December 2007 are detailed below.

Nature of transaction	Subsidiaris of OJSC Svyazinvest	Associate companies	Government organizations	Other
2006				
Rendering Services				
Telecommunicatio services	2,694	74	325	-
Rent of premises	-	6	1	-
Other services an goods	-	4	23	-
Purchases				
Telecommunicatio services	416	14	24	1
Software development and IT consulting	110	-	-	-
Other services	-	8	485	-

(In millions of Russian roubles)

Nature of transaction	Subsidiaris of OJSC Svyazinvest	Associate companies	Government organizations	Other
Donations	113	-	-	-
Pensions	-	-	-	181
Dividends	-	129	-	-
Interest on loans	-	-	486	-

Nature of transaction	Subsidiaris of OJSC Svyazinvest	Associate companies	Government organizations	Other
2007				
Rendering Services				
Telecommunication services	2,278	56	425	-
Rent of premises	-	5	6	-
Other services and goods	-	14	16	-
Purchases				
Telecommunication services	395	31	454	-
Software development and IT consulting	292	4	-	-
Other services	-	-	798	-
Donations	184	-	-	-
Pensions	-	-	-	84
Dividends	-	87	-	-
Interest on loans	-	-	231	-

As of 31 December 2007 and 2006 significant outstanding balances with related parties were as follows:

Nature of balance	Subsidiaris of OJSC Svyazinvest	Associate companies	Government organizations	Other
As at 31 December 2006				
Accounts receivable	125	77	36	-
Accounts payable	302	166	17	-
Loans received (inc. interest)	-	-	3,145	-
As at 31 December 2007				
Accounts receivable	58	5	68	-
Accounts payable	357	3	31	13
Loans received (inc. interest)	-	-	4,158	-

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

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

(In millions of Russian roubles)

OJSC Svyazinvest

The Company's parent entity OJSC Svyazinvest was wholly owned by the Russian Government until July 1997 when the Government sold 25% plus one share of the Charter Capital of OJSC Svyazinvest to a private investor.

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

The Government's influence is not confined to its shareholdings in OJSC Svyazinvest. It has general authority to regulate tariffs and has control over the licensing of providers of telecommunications services.

OJSC Rostelecom

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

The revenues associated with OJSC "Rostelecom" are formed in the proceeds from zonal initiation/ termination of call from/ to the Company's networks and from/ to the networks of connected operators and revenues under the assistance agreement.

Expenses associated with OJSC "Rostelecom" include payments for services of call termination to the networks of the other telecommunication operators and, if the call is initiated from mobile radiotelephone network, expenses for interconnection, as well as expenses for long-distance domestic and international telecommunication services provided by the Company.

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

	2007	**2006**
Revenues from services provided for OJSC Rostelecom	2,149	2,610
Expenses on OJSC Rostelecom services	123	68
Accounts payable to OJSC Rostelecom as of 31 December	154	145
Accounts receivable from OJSC Rostelecom as of 31 December	32	6

Transactions with Government Organizations

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

In the context of its operating activities the Company renders services to the entities directly or indirectly controlled by the Government on market conditions.

The Company can not disconnect certain companies which are strategic entities for the Government. The tariffs for such companies are also regulated by the Government, but at the same level as for the commercial organisations.

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

Non-commercial partnership Centre for Research of the Problems in Development of Telecommunications (hereinafter "the Partnership") is an entity OJSC Svyazinvest controls through its subsidiaries. The Company has an agreement with the Partnership, under which it provides funding for industry research and common administrative activities on behalf of the Company and other subsidiary and associates of OJSC Svyazinvest. Payments to the Partnership included in other operating expenses in the accompanying consolidated income statement for the year ended 31 December 2007 amounted to RUR 184 million (2006 - RUR 113 million).

OJSC Svyazintech

OJSC Svyazintech was established by OJSC Svyazinvest subsidiaries which own among them 100% of its share capital, for implementation and further support of information systems, and coordination, management and realization of centralized industry programs related to information technologies in the companies of the Svyazinvest Group. In 2007 OJSC Svyazintech provided the Company with the services related to implementation and further support of information systems, in particular, software Oracle E-Business Suite and Amdocs Billing Suite. In 2007 the Company incurred expenses on services provided by OJSC Svyazintech in the amount of RUR 200 million (2006 - RUR 110 million). These expenses were capitalized as part of the carrying value of respective intangible assets.

NPF Telecom-Soyuz

In 2005 the Company signed centralised pension agreements with NPF Telecom-Soyuz (see note 23). OJSC Svyazinvest holds the majority in the Board of Directors of NPF Telecom-Soyuz (hereafter "the Fund"). Payments from the Company to the Fund in 2007 amounted to RUR 84 million (2006 - RUR 181 million).

Related parties pricing policy

The Company's pricing policy in respect of related party transactions is based on market terms, or, if applicable, on regulated tariffs.

Compensation to Key Management Personnel

Key management personnel of the Company comprise members of the Management Board and the Board of Directors of the Company totalling 25 persons as of 31 December 2007 (2006: 19).

In 2007 compensation to members of the Board of Directors, Management Board and the Audit Committee of OJSC Southern Telecommunications Company included salary, bonuses and compensation for involvement in management bodies of OJSC Southern Telecommunications Company and amounts to RUR 57 million (2006: RUR 69 million).

36. Financial Instruments

The Company's principal financial instruments comprise bank loans, bond loans and promissory notes debt, finance leases, cash and cash equivalents. The main purpose of these instruments is to raise finance for the Company's operations. The Company has other financial assets and liabilities such as trade receivables and trade payables, which arise directly from its operations.

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

(In millions of Russian roubles)

Capital Management Policy

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

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

The Company's policy is to maintain financial independence ratio within a range of 0.33-0.36, net debt/shareholder's equity within a range of 1.40-1.29, and net debt/EBITDA within a range of 3.01-2.64.

Current year international rating agency Standard&Poor's revised long term credit risk of the Company from "B-" to "B", at the same time revised projection from "Stable" to "Positive", and increased corporate credit rating based on national scale from "ruBBB" to "ruA".

Capital management is conducted at the level of separate significant legal entities of the Company. The financial independence ratios, net debt/shareholder's equity, net debt/EBITDA are calculated using the statutory accounting data. The Group's capital management policy was not changed in 2007 compared to 2006.

As the OJSC Southern Telecommunications Company is a key legal entity of the Company, the indicators used to manage capital are based on its statutory accounting data. The financial independence ratio is calculated as shareholder's equity to the balance sheet total at the end of the period. Net debt/shareholder's equity is calculated as net debt to shareholder's equity at the end of the period. Net debt/EBITDA is calculated as net debt at the year-end to EBITDA for the previous period.

Foreign Exchange Risk

Foreign exchange risk is the risk that fluctuations in exchange rates will adversely affect the Company's cash flows. As a result, these fluctuations in exchange rates will be reflected in respective items of the Company's income statement, balance sheet and/or statement of cash flows. Foreign currency denominated liabilities (Notes 19, 20, 21) give rise to foreign exchange risk exposure.

As of 31 December 2007 the Company's liabilities in foreign currencies were RUR 4,894 million (2006 – RUR 5,324 million), including liabilities denominated in US dollars: RUR 4,419 million (2006 – RUR 4,744 million) and denominated in Euro: RUR 475 million (2006 – RUR 621 million).

For the period from 1 January 2007 to 31 December 2007 exchange rate of the Russian Rouble to US Dollar increased by approximately 6.78% and exchange rate of the Russian Rouble to Euro decreased by 3.56%.

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

	USD		**EUR**	
	Changes in exchange rate, %	**Effect on income before income tax**	**Changes in exchange rate, %**	**Effect on income before income tax**
2007	+10	(442)	+5	(24)
	-10	442	-5	24

(In millions of Russian roubles)

2006	+10	(474)	+5	(31)
	-10	474	-5	31

The Company does not have formal arrangements to mitigate foreign exchange risks of the Company's operations.

According to current risk management policy the Company performs the integral evaluation of risks, taking into account the following:

- The level of risks impact on the financial ratios;
- The probability of risk.

Moreover, the Company used qualitative criteria – the level of risk controllability - to make decisions over the risk response strategy.

Taking into account the structure of currency portfolio of the Company and the exchange rates of USD and Euro during 2007, the Company evaluated foreign exchange risk as not significant.

Interest Rate Risk

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

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

	< 1 year	**1-5 years**	**> 5 years**	**Total**
As of 31 December 2007:				
Fixed rate				
Short-term obligations	1,829	-	-	**1,829**
Long-term obligations	3,416	1,411	14	**4,841**
Finance lease obligations	758	472	-	**1,230**
Floating rate				
Long-term obligations	1,590	8,539	3,068	**13,197**

	< 1 year	**1-5 years**	**> 5 years**	**Total**
As of 31 December 2006:				
Fixed rate				
Short-term obligations	2,431	-	-	**2,431**
Long-term obligations	540	6,314	17	**6,871**
Finance lease obligations	812	1,229	-	**2,041**
Floating rate				
Long-term obligations	9,890	**-**	**-**	**9,890**

Cash flow sensitivity analysis for variable rate instruments is shown below:

	Change in interest rate	**Cash flow sensitivity**
2007	+100 basis points	(132)
	-100 basis points	132
2006	+100 basis points	(99)
	-100 basis points	99

Liquidity Risk

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

(In millions of Russian roubles)

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements:

2007

Maturity date	Loans and borrowings	Bonds	Promissory notes	Other	Total
within 2008	4,666	1,495	1,975	10	8,146
within 2009	1,769	6,627	-	4	8,400
within 2010	1,764	2,075	-	4	3,843
within 2011	1,188	-	-	24	1,212
within 2012	957	-	-	4	961
after 2012	862	-	-	10	872
Total	**11,206**	**10,197**	**1,975**	**56**	**23,434**

2006

Maturity date	Loans and borrowings	Bonds	Promissory notes	Other	Total
within 2007	7,480	6,942	1,001	118	15,541
within 2008	2,627	1,037	948	10	4,622
within 2009	140	2,867	-	3	3,010
within 2010	130	-	-	3	133
within 2011	120	-	-	24	144
after 2011	-	-	-	1	1
Total	**10,497**	**10,846**	**1,949**	**159**	**23,451**

Distribution of borrowings by maturity is based on contractual undiscounted cash flows. These flows include the repayment of principal amount as well as interest payments and other additional payments to be made during respective periods.

In case when the liabilities were nominated in foreign currency the exchange rate for the projected periods was taken equal to the rates as at 31 December 2007. In case when the interest rate included floating part the rate of this part for projection was set as equal to the interest rate as at 31 December 2007.

Calculations are made with the use of nominal interest rate. Effective interest rates used in determination of carrying values of liabilities are not used when calculating the projected interest.

Total undiscounted cash flows differ from the amount included in the balance sheet because the balance sheet amounts are based on discounted cash flows.

Credit Risk

Credit risk is the risk that counterparty will fail to discharge an obligation and cause the Company to incur a financial loss.

Financial assets, which are potentially subject to credit risk, consist principally of trade receivables. The carrying amount of accounts receivable, net of provision for impairment of receivables, represents the maximum amount exposed to credit risk.

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

(In millions of Russian roubles)

The Company places cash on bank accounts in a number of Russian commercial financial institutions. Insurance of bank accounts is not provided by financial institutions operating in Russia. To manage the credit risk the Company places cash in different financial institutions and the Company's management analyzes the risk of default of these financial institutions on a regular basis.

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

As of 31 December 2007	**Post-due (days)**						
	TOTAL	**<30**	**31-61**	**61-90**	**91-180**	**181-360**	**>361**
Corporate customers	21	9	5	2	-	5	-
Residential customers	71	42	12	5	2	10	-
Governmental customers	13	8	3	1	-	1	-
Interconnected operators	17	-	8	2	1	6	-
Tariff compensation from the state budget	9	-	9	-	-	-	-
Other receivables	13	2	2	1	1	1	6
Total	**144**	**61**	**39**	**11**	**4**	**23**	**6**

As of 31 December 2006	**Post-due (days)**						
	TOTAL	**<30**	**31-61**	**61-90**	**91-180**	**181-360**	**>361**
Corporate customers	1	1					-
Residential customers	58	34	11	3	2	8	-
Governmental customers	16	11	3	1	-	1	-
Interconnected operators	43	23	11	3	1	5	-
Tariff compensation from the state budget	-	-	-	-	-	-	-
Other receivables	10	4	3	3	-	-	-
Total	**128**	**73**	**28**	**10**	**3**	**14**	**-**

Hedging

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

Fair Value

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

	2007		**2006**	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Long-term bonds	7,925	7,922	3,273	3,437
Short-term portion of long-term bonds	763	777	6,300	6,616

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

(In millions of Russian roubles)

37. Subsequent Events

Dividends

The Board of Directors of the Company proposed the following distribution of profits to the Annual Shareholders' meeting to be held on 17 June 2008:

Dividends for 2007 proposed for approval

Dividends on ordinary shares – 0.082069 Roubles per share	243
Dividends on preference shares - 0.187915 Roubles per share	183
Total	**426**

Dividends payable for 2007 will be recognised in financial statements for the year 2008.

Tariffs

Following Order # 360-c/5 of the Federal Tariff Service of Russia, dated 23 November 2007, OJSC Southern Telecommunications Company changed tariffs for local telecommunication services effective 1 February 2008.

Tariffs for Local Telephone Communication Services

For subscribers – residential customers:

- the amount of fixed monthly subscribers' fee for tariff with unlimited number of local calls had decreased for filials of autonomy level by 40% and for filials of territory and region level by 46 % to RUR 160 and RUR 190 respectively starting from 1 February 2008 (2007 – RUR 270 and RUR 350 respectively);

For subscribers – legal entities:

- the ultimate level of tariff for basic volume of local telephone connections using the combined payment scheme is fixed at RUR 65 for filials of autonomy level and at RUR 95 for filials of territory and region level except for Astrakhan region filial, for which it is RUR 85;

- the ultimate tariffs per minute of local calls over basic volume using the combined payment scheme is fixed at the level of the respective tariffs in the amount of RUR 0.14 for filials of autonomy level and RUR 0.18 for filials of territory and region level;

- the ultimate tariffs for local telephone connections using the fixed payment scheme is fixed at RUR 270 for filials of autonomy level and RUR 350 for filials of territory and region level for unlimited number of telephone connections.

Tariffs for Access to the Local Telecommunication Network

Tariffs for individual subscribers in rural areas of Kabardino-Balkariya, Rostov region, Astrakhan region and Krasnodar Territory were reduced by 29%, 25%, 17% and 25% respectively and from 1 February 2008 amount to RUR 5,000; RUR 6,000; RUR 5,000 and RUR 6,000 respectively (2007 – RUR 7,000; RUR 8,000; RUR 6,000 and RUR 8,000). Tariffs for legal entities were unchanged.

Tariffs for Interconnection and Traffic Transmission Services

Following Order # 360-c/5 of the Federal Tariff Service, dated 23 November 2007, the compensatory markup on local and zone initiation services was canceled. Russian Government's Decree dated 19 October 2005 # 627 introduced compensatory markup for the period up to 1 January 2008.

According to the Decree #. 666 of the Russian Government *On amendments to certain acts of the Russian Government related to telecommunication matters*, dated 12 October 2007, services related to maintenance of communication facilities representing interconnection points were excluded from the scope of interconnection services effective as of 1 March 2008.

Acquiring of share in CJSC Systemy Gibridnoy Pechati

In accordance with the Minutes #14 dated 7 February 2008, the Company's Board of Directors made a decision to acquire 3,952,000 ordinary voting shares of CJSC Systemy Gibridnoy Pechati with par value of 100 roubles each. The purpose of investment is development of hybrid printing system.

Transfer of rights in respect of these shares will be shown in shareholders register in the year 2008.

The share was acquired for RUR 395 million and represents 5.08% of share capital of CJSC Systemy Gibridnoy Pechati.

CLN issue

On 29 May 2008 the Company placed in full its 5-year credit linked notes (CLNs) worth RUR 3.5 billion at 98.154% of nominal value. The yield rate to the 12-month put option equaled 11% per annum. The coupon rate was set at 9% per annum. The issue provides for a buyback option three years after the placement date and the Borrower's right to revise the interest rate. 50% of the CLN issue is to be repaid in 4.5 years. Renaissance Capital is the CLN arranger, MDM Bank is the co-arranger.

The Company plans to use the money accumulated from the CLN floatation to refinance its short-term borrowings and to turn some short-term liabilities into long-term.