OAO CenterTelecom

Consolidated Financial Statements

Year ended December 31, 2004

With Report of Independent Auditors

OAO CenterTelecom

Consolidated Financial Statements

Year ended December 31, 2004

Contents

ERNST & YOUNG

CJSC Ernst & Young Vneshaudit
Sadovnicheskaya Nab., 77, bld. 1
Moscow, 115035, Russia
Tel.: 7 (095) 705-9700
7 (095) 755-9700
Fax: 7 (095) 755-9701
www.ey.com/russia

ЗАО "Эрнст энд Янг Внешаудит"
Россия, 115035, Москва
Садовническая наб., 77, стр. 1
Тел.: 7 (095) 705-9700
7 (095) 755-9700
Факс: 7 (095) 755-9701
ОКПО: 00139790

Independent Auditors' Report

To the Shareholders and Board of Directors of OAO CenterTelecom

1. We have audited the accompanying consolidated balance sheet of OAO CenterTelecom (a Russian open joint-stock company – hereinafter "the Company"), as at December 31, 2004 and the related consolidated statements of operations, cash flows and changes in shareholders' equity for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of OAO Russian Telecommunications Network (a Russian open joint-stock company – hereinafter "RTS"), a wholly-owned subsidiary, which statements reflect total consolidated assets of 968,843 thousand Roubles as at December 31, 2004, total consolidated revenues of 699,172 thousand Roubles and consolidated pre-tax income of 70,599 thousand Roubles for the year then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for RTS, is based solely on the report of other auditors.

2. Except as discussed in paragraph 3, we conducted our audit in accordance with International Standards on Auditing issued by the International Federation of Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

3. As described in Note 2 "Basis of Presentation of the Financial Statements" and Note 5 "Property, Plant and Equipment", the Company has transitioned to International Financial Reporting Standards (IFRS) at January 1, 2003 and applied an exemption in IFRS 1, First-time Adoption of International Financial Reporting Standards, which permits 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. However, we were not able to satisfy ourselves as to (i) whether the carrying amounts of property, plant and equipment as at January 1, 2003 are representative of fair value; (ii) resulting depreciation expense for the years presented and (iii) the respective deferred tax balances as at the reporting dates and deferred tax expense for the years presented.

4. As described in Note 2 "Basis of Presentation of the Financial Statements", the Company has not determined and presented its obligations existing under defined benefit plans in accordance with IAS 19, Employee Benefits. We were not able to quantify the respective adjustments to the financial statements for the years presented.

5. As described in Note 7 "Investments in Subsidiaries", the Company accounted for the purchase of subsidiaries based on historical cost of their net assets. The Company did not identify and estimate the fair value of the acquired assets and liabilities as required by IFRS 3, Business Combinations. We were not able to quantify the respective adjustments to the financial statements for the year ended December 31, 2004.

6. In our opinion, based on our audit and the report of other auditors, except for the effects on the financial statements of such adjustments, if any, which might have been determined to be necessary had we been able to satisfy ourselves to the matters referred to in paragraph 3 above, and except for the effects on the financial statements of the matters referred to in paragraphs 4 and 5 above, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of OAO CenterTelecom as at December 31, 2004 and the consolidated results of operations and its cash flows for the year then ended in conformity with International Financial Reporting Standards.

Ernst & Young Vneshaudit

September 19, 2005

OAO CenterTelecom

Consolidated Balance Sheet at December 31, 2004

(in thousands of Russian Roubles)

	Notes	December 31, 2004	December 31, 2003
ASSETS			
Non-current assets			
Property, plant and equipment	**5**	**30,000,961**	24,314,535
Intangible assets	**6**	**3,328,070**	1,045,017
Investments in associates and joint ventures	**8**	**15,927**	30,721
Available-for-sale financial assets		**13,662**	8,358
Other financial assets	**9**	**323,626**	209,311
Long-term advances given	**10**	**1,056,076**	659,308
		34,738,322	26,267,250
Current assets			
Inventories	**11**	**577,518**	543,198
Trade receivables	**12**	**1,936,643**	1,668,768
Other current assets	**13**	**2,369,709**	1,668,232
Cash and cash equivalents	**14**	**1,417,214**	1,052,589
		6,301,084	4,932,787
TOTAL ASSETS		**41,039,406**	31,200,037
SHAREHOLDERS' EQUITY AND LIABILITIES			
Shareholders' equity			
Preference shares	**15**	**304,840**	304,840
Ordinary shares	**15**	**914,526**	914,526
Net unrealized gains		**4,517**	2,624
Retained earnings		**11,340,893**	12,606,161
		12,564,776	13,828,151
Minority interest	**16**	**23,974**	358
Non-current liabilities			
Long-term borrowings	**17**	**12,972,648**	6,959,174
Finance lease obligations	**18**	**1,775,171**	1,167,947
Long term taxes payable		**24,346**	25,545
Deferred revenue		**617,789**	628,487
Deferred income tax liabilities	**26**	**122,849**	527,176
Other non-current liabilities		**13,254**	18,098
		15,526,057	9,326,427
Current liabilities			
Trade and other payables	**19**	**3,176,723**	1,747,874
Payables to Rostelecom	**31**	**191,544**	219,152
Taxes payable	**20**	**1,395,882**	1,024,537
Dividends payable		**15,241**	15,323
Short-term borrowings	**17**	**4,572,646**	3,419,649
Current portion of long-term borrowings	**17**	**2,900,072**	1,105,797
Current portion of finance lease obligations	**18**	**672,491**	512,769
		12,924,599	8,045,101
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		**41,039,406**	31,200,037

General Director R.A. Amarian Chief Accountant R.P. Konstantinova

ЦЕНТР ТЕЛЕКОМ

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

OAO CenterTelecom

Consolidated Statement of Operations

For the year ended December 31, 2004

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

	Notes	2004	2003
Revenues	**22**	**26,047,204**	21,316,738
Operating expenses			
Wages, salaries, other employee benefits and payroll taxes		**(9,413,121)**	(7,580,068)
Depreciation and amortization	**5, 6**	**(4,243,359)**	(3,665,988)
Gain (loss) on disposal of property, plant, and equipment		**1,150**	(94,706)
Materials, repairs and maintenance, utilities		**(2,499,688)**	(2,053,886)
Taxes other than income tax		**(627,418)**	(446,159)
Interconnection charges		**(4,048,930)**	(2,635,649)
Provision for impairment of receivables	**12**	**(831,322)**	(801,968)
Other operating expenses	**23**	**(3,471,798)**	(2,274,102)
Total operating expenses		**(25,134,486)**	(19,552,526)
Operating profit		**912,718**	1,764,212
Share in profit (loss) of associates and joint ventures		**2,282**	(750)
Finance cost, net	**24**	**(2,032,987)**	(1,279,714)
Gain (loss) from investments	**25**	**274,243**	(25,097)
Foreign exchange gain (loss), net		**59,845**	(89,082)
Profit (loss) before income tax and minority interest		**(783,899)**	369,569
Income tax expense	**26**	**(126,069)**	(133,150)
Profit (loss) before minority interest		**(909,968)**	236,419
Minority interest	**16**	**(8,003)**	17,212
Net profit (loss)		**(917,971)**	253,631
Basic and diluted earnings (loss) per share (Russian Roubles)	**27**	**(0.44)**	0.12

General Director

R.A. Amarian

Chief Accountant

R.P. Konstantinova

ЦЕНТР ТЕЛЕКОМ

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

OAO CenterTelecom

Consolidated Cash Flow Statement

For the year ended December 31, 2004

(in thousands of Russian Roubles)

	Notes	2004	2003
Cash flows from operating activities			
Profit (loss) before income tax and minority interest		(783,899)	369,569
Adjustments for:			
Depreciation and amortization	**5, 6**	4,243,359	3,665,988
(Gain) loss on disposal of property, plant and equipment		(1,150)	94,706
Provision for impairment of receivables	**12**	831,322	801,968
Share in profit (loss) of associates and joint ventures		(2,282)	750
(Gain) loss from investments	**25**	(274,243)	25,097
Finance cost, net	**24**	2,032,987	1,279,714
Foreign exchange (gain) loss, net		(59,845)	89,082
Recovery of provision for deferred income tax assets		(614)	-
Operating profit before working capital changes		**5,985,635**	**6,326,874**
Increase in trade receivables		(951,472)	(1,240,023)
Increase in other current assets		(676,413)	(381,491)
(Increase) decrease in inventories		(28,848)	8,069
Decrease in trade and other payables		(93,159)	(125,734)
Increase in taxes payable		169,205	226,688
Cash flows generated from operations		**4,404,948**	**4,814,383**
Interest paid		(1,949,908)	(1,170,969)
Income taxes paid		(313,866)	(809,924)
Net cash flows from operating activities		**2,141,174**	**2,833,490**
Cash flows from investing activities			
Purchase of property, plant and equipment		(6,996,281)	(5,488,709)
Purchase of intangible assets		(74,459)	(52,337)
Purchase of Oracle E-Business Suite software		(180,235)	(919,517)
Proceeds from disposal of property, plant and equipment		90,060	4,484
Acquisition of subsidiaries, net of cash acquired		(1,372,349)	-
Disposal of subsidiaries, net of cash disposed		116,731	-
Acquisition of associates		(2,815)	-
Proceeds from disposal of associates		125,717	-
Purchase and disposal of investments available-for- sale and other financial assets		(30,969)	(2,365)
Interest received		62,639	4,864
Dividends received from associates/available-for-sale investments		79	4,469
Net cash flows used in investing activities		**(8,261,882)**	**(6,449,111)**

OAO CenterTelecom

Consolidated Statement of Cash Flows

For the year ended December 31, 2004

(in thousands of Russian Roubles)

	Notes	2004	2003
Cash flows from financing activities			
Proceeds from promissory notes issued		2,389,405	535,906
Repayment of promissory notes		(1,041,512)	-
Proceeds from borrowings		7,441,833	8,954,077
Repayment of borrowings		(6,327,741)	(5,092,283)
Proceeds from bonds issued		6,818,478	2,000,000
Repayment of bonds		(1,284,820)	(600,000)
Repayment of finance lease obligations		(650,277)	(277,850)
Repayment of vendor financing obligations		(508,280)	(882,566)
Repayment of (proceeds from) other non-current liabilities		(3,984)	730
Dividends paid		(347,769)	(275,753)
Net cash flows from financing activities		**6,485,333**	**4,362,261**
Effects of exchange rate changes on cash and cash equivalents		-	(1,342)
Net increase in cash and cash equivalents		364,625	745,298
Cash and cash equivalents at 1 January		1,052,589	307,291
Cash and cash equivalents at 31 December		1,417,214	1,052,589
Non-monetary transactions:			
Property, plant and equipment acquired on credit terms		1,470,674	442,414
Property, plant and equipment acquired under finance lease agreements		1,413,383	1,169,376
Amdocs software acquired through vendor financing		884,920	-
Property, plant and equipment received free-of-charge		22,758	85,104

General Director
R.A. Amarian

Chief Accountant
R.P. Konstantinova

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

OAO CenterTelecom

Consolidated Statement of Changes in Shareholders' Equity

For the year ended December 31, 2004

(in thousands of Russian Roubles)

	Notes	Share Capital		Retained earnings	Net unrealized gain	Total
		Preference shares	Ordinary shares			
At December 31, 2002		304,840	914,526	12,612,530	-	13,831,896
Net profit		-	-	253,631	-	253,631
Change in the fair value of available-for-sale financial assets		-	-	-	2,624	2,624
Dividends	28	-	-	(260,000)	-	(260,000)
At December 31, 2003		304,840	914,526	12,606,161	2,624	13,828,151
Net loss		-	-	(917,971)	-	(917,971)
Change in the fair value of available -for -sale financial assets		-	-	-	1,893	1,893
Dividends	28	-	-	(347,297)	-	(347,297)
At December 31, 2004		**304,840**	**914,526**	**11,340,893**	**4,517**	**12,564,776**

General Director
R.A. Amarian

Chief Accountant
R.P. Konstantinova

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

1. General Information

Authorization of Accounts

The consolidated financial statements of OAO CenterTelecom and its subsidiaries – (hereinafter "the Company") for the year ended December 31, 2004 were authorized for issue by the General Director and Chief Accountant of the Company on September 19, 2005.

The Company

The Company's principal activity is providing telephone services (including local, long-distance and international calls), telegraph, data transfer services, rent of channels and wireless communication services on the territory of Central Federal District of the Russian Federation.

OAO Svyazinvest, a federal holding company controlled by the Russian Federation, owns 50.69% of the Company's ordinary shares as of December 31, 2004.

The number of employees in the Company as of December 31, 2004 was 67,432 persons (2003 – 71,289).

The parent Company is an open joint stock company incorporated in accordance with the laws of the Russian Federation. Information on the Company's main subsidiaries is disclosed in Note 7.

The registered office of the Company is Russia, Moscow region, city of Khimki, Proletarskaya st. 23.

Tariff Setting

Under the Russian legislation, the Company is considered a monopolist for fixed line telecommunication services. As a result, tariffs charged by the Company are set by federal authorities. Tariffs charged to the Company by OAO Rostelecom (the primary provider of domestic long distance and international telecommunication services in the Russian Federation, which is controlled by OAO Svyazinvest) are also subject to state regulation, thus creating a cross-subsidization mechanism.

Liquidity and Going Concern

As of December 31, 2004, the Company's current liabilities exceeded its current assets by approximately 6,623,515 (2003 - 3,112,314). As a result, there may be some doubt about the Company's ability to attract further financing 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 lease.

Through 2005 the Company anticipates funding from a) cash generated from operations; b) financing from domestic lending institutions. Management also expects to continue to be able to delay payment for certain operating costs to manage its working capital requirements if necessary.

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

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

2. Basis of Presentation of the Financial Statements

Basis of Preparation

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

The Company has transitioned to IFRS at the beginning of the earliest period presented in these financial statements (January 1, 2003) using the provisions of IFRS 1, "First-time Adoption of International Financial Reporting Standards", which is effective for periods starting on or after January 1, 2004. IFRS 1 applies to first-time adopters of IFRS including companies that previously applied some, but not all IFRS, and disclosed this fact in its most recent financial statements. The Company's previous financial statements disclosed that management made certain estimates and assumptions to present the carrying value of fixed assets which did not comply with historical cost as defined by IAS 16, "Property, plant, and equipment".

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.

Management estimates that the carrying value of all of the Company's property, plant and equipment is 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.

The Company has also applied the exemption permitted by IFRS 1 which allows an entity to recognize all cumulative actuarial gains and losses at the date of transition even if the corridor approach is used for latter actuarial gains and losses.

Further the Company did not apply the provision of IAS 19 "Employee benefits" and as such did not account for defined benefit obligations. However the Company has engaged an actuary to assess the pension obligation and as a result, the defined benefit obligation will be recorded in subsequent periods.

Accounting for the Effect of Inflation

Prior to January 1, 2003 the characteristics of the economic environment of the Russian Federation indicated the existence of hyperinflation. Non-monetary assets and liabilities acquired prior to December 31, 2002, and share capital transactions occurring before December 31, 2002, have been restated in accordance with IAS 29 "Financial Reporting in Hyperinflationary Economies" by applying the relevant conversion factors to the historical cost through December 31, 2002.

Management Estimates

The preparation of financial statements requires management of the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates with regard to those financial statements relate to the valuation and useful lives of fixed assets, deferred taxation and accounts receivable provision, as discussed in Notes 5, 12 and 26.

(in thousands of Russian Roubles)

2. Basis of Presentation of Financial Statement (continued)

Reconciliation of Equity and Net Profit Reported under Previous GAAP and under IRFS

Shareholders' equity and net income are reconciled between previous Generally Accepted Accounting Principles (GAAP) and IFRS as follows:

	Shareholders' equity as at December 31, 2003	**Net profit (loss) for the year ended December 31, 2003**	**Shareholders' equity as at January 1, 2003**
Previous GAAP as reported:	**13,105,393**	**158,059**	**13,246,536**
Accrual of dividends to the holders of preference shares	41,826	-	-
Discounting of interest free loans, net of tax	59,559	(4,379)	63,938
Consolidation of ZAO Sotovaia Svyaz Chernozemia	(34,672)	(34,672)	-
Capitalization of interest expenses, net of tax	49,300	49,300	-
Accrual of expenses related to 2003, but recognized in 2004, net of tax	68,098	68,098	-
Accrual of expenses related to 2002, but recognized in 2003, net of tax	-	33,608	(33,608)
Recognition of fixed assets as a result of physical inspection in 2004, net of tax	414,988	(60,892)	475,880
Correction of error made under previous GAAP: settlements with Rostelecom, net of tax	111,931	37,989	73,942
Previous GAAP as restated:	**13,816,423**	**247,111**	**13,826,688**
Goodwill amortization	11,728	6,520	5,208
International Financial Reporting Standards	**13,828,151**	**253,631**	**13,831,896**

Certain inconsequential reclassifications have been made to the 2003 financial statements, for them to conform to the 2004 presentation.

3. Summary of Significant Accounting Policies

3.1 Basis of Consolidation

Subsidiaries, which are those entities in which the Company has an interest of more than one half of the voting rights, or otherwise has power to exercise control over its operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Company 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. Summary of Significant Accounting Policies (continued)

3.1 Basis of Consolidation (continued)

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

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

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 fair value of the identifiable assets and liabilities of the subsidiary at the acquisition date, and the minorities' portion of movements in equity since the date of the combination. Minority interest is presented separately from liabilities and shareholders' equity.

Losses allocated to minority interest do not exceed the minority interest in the equity of the subsidiary unless there is a binding obligation of the minority to fund the losses. All such losses are allocated to the Company.

IFRS 3 "Business Combinations" applies only to business combinations, such as the acquisition of a subsidiary, whereby the acquirer has obtained control over the business. However, the standard is silent on how later exchange transactions should be accounted for, such as the acquisition of some or all of the minority interest in a subsidiary. The Company does not remeasure the assets and liabilities of the subsidiary to reflect their fair values at the date of the transaction. The difference between the cost of the additional interest in the subsidiary and the minority interest's share of the assets and liabilities is recognized directly in retained earnings in the statement of changes in shareholders' equity at the date of the acquisition of the minority interest.

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 by the equity method of accounting and are initially recognised 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 recognised in the statement of operations and its share of movements in reserves is recognised 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 recognise further losses, unless the Company is obligated to make further payments to, or on behalf of, the associate.

Unrealised gains on transactions between the Company and its associated undertakings are eliminated to the extent of the Company's interest in the associated undertakings; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

3.3 Interest in joint venture

The Company recognises its interest in a jointly controlled entity using the equity method.

3. Summary of Significant Accounting Policies (continued)

3.4 Investments

The Company classified its investments into the following categories: held-to-maturity and available-for-sale. Investments with fixed maturity that the management has the intent and ability to hold to maturity are classified as held-to-maturity and are included in non-current assets. Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; these are included in non-current assets unless management has the express intention of holding the investment for less than 12 months from the balance sheet date or unless they will need to be sold to raise operating capital, in which case they are included in current assets. Management determines the appropriate classification of its investments at the time of the purchase and re-evaluates such designation on a regular basis.

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. All investments are initially recognised at cost, being the fair value of the consideration given and including transaction costs. Available-for-sale investments are subsequently carried at fair value, whilst held-to-maturity investments are carried at amortised cost using the effective yield method. Realised and unrealised gains and losses arising from changes in fair value of available-for-sale investments are recognised directly in equity until investments are sold, collected or otherwise disposed of, or until they are determined to be impaired. Upon disposal, cumulative gains or losses previously recognised as a component of equity, are included in the statement of operations.

For investments that are actively traded in organised financial markets, fair value is determined by reference to Stock Exchange quoted market bid prices at the close of business on the balance sheet date. For investments where there is no quoted market price, fair value is determined by reference to the current market value of another instrument which is substantially the same or is calculated based on the expected cash flows of the underlying net asset base of the investment.

3.5 Foreign Currency Translation

The 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 functional currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to the consolidated statement of operations. 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.

Assets and liabilities settled in Rubles 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.

3.6 Property, Plant and Equipment

Property, plant and equipment are stated at purchase or construction cost less accumulated depreciation and any impairment in value. For the property, plant and equipment acquired prior to January 1, 2003, fair values as at January 1, 2003 have been used as deemed cost (refer to Note 2) in accordance with the exemption provided in IFRS 1.

Depreciation is calculated on a straight-line basis. The depreciation periods, which approximate the estimated useful economic lives of the respective assets, are as follows:

3. Summary of Significant Accounting Policies (continued)

3.6 Property, Plant and Equipment (continued)

Buildings	50 years
Constructions	20 years
Analog switches	15 years
Digital switches	15 years
Other telecommunication equipment	15 years
Transportation equipment	5 years
Computers, office and other equipment	4-5 years
Land	not depreciated

For the purposes of disclosure, property, plant and equipment are aggregated into the following groups:

Land, buildings and constructions;
Switches and transmission devices;
Construction in progress and equipment for installation;
Other assets, in which computers, vehicles and other equipment are included.

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

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised and the assets replaced are retired. Gains and losses arising from the retirement of property, plant and equipment are included in the statement of operations as incurred.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year the item is derecognised.

Borrowing costs that are directly attributable to the acquisition, construction or production of qualifying property, plant and equipment items are capitalised as part of the cost of these items. All other borrowing costs are recognised as an expense when incurred.

IAS 36 "Impairment of Assets" requires that the recoverable amount of an asset, including property, plant and equipment, should be estimated whenever there is an indication that the assets may be impaired.

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

3. Summary of Significant Accounting Policies (continued)

3.7 Goodwill

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. 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. Goodwill is not amortized but is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that carrying amount may be impaired. As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units expected to benefit from the combination's synergies.

Impairment is determined by assessing the recoverable amount of the cash-generating unit, to which the goodwill relates. Where recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognized. Where goodwill forms part of a cash generating unit and part of the operation within that unit are 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 on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

3.8 Intangible Assets

Intangible assets acquired separately are capitalized at cost and from a business acquisition are capitalized at fair value as at the date of acquisition. Following initial recognition, the cost model is applied to the class of intangible assets. Intangible assets created within the business are not capitalized and expenditure is charged against profits in the year in which the expenditure is incurred.

Licenses and software are depreciated on a straight-line basis over the estimated useful life equal to the term of license or of the right to use the software. Useful life of other intangible assets is five years.

At each reporting date, the Company assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the carrying amount of any intangible asset, is assessed and, when impaired, the asset is written down immediately to its recoverable amount.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

3.9 Recoverable Amount of Non-current Assets

At each reporting date, the Company assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the Company makes a formal estimate of recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount. Recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets.

3. Summary of Significant Accounting Policies (continued)

3.10 Inventories

Inventories are valued at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale.

Cost of inventory is determined on the weighted average basis.

3.11 Trade and Other Receivables

Trade and other receivables are recognized and carried at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable.

Accounts that are individually significant are assessed for uncollectability and recognized individually. Upon which, uncollectability is measured and recognized on a portfolio basis for accounts of similar customers that are not individually identified as doubtfully recoverable.

The amount of the provision is recognised in the statement of operations.

3.12 Value-Added Tax

The tax authorities permit the settlement of sales and purchases value added tax (VAT) on a net basis.

Value added tax recoverable

VAT recoverable relates to purchases which have not been settled at the balance sheet date. VAT recoverable is reclaimable against sales VAT upon payment for the purchases.

Value added tax payable

Value added tax payable represents VAT related to sales which is payable to tax authorities upon collection of receivables from customers net of VAT on purchases which have been settled at the balance sheet date. In addition, VAT related to sales which have not been settled at the balance sheet date (VAT deferred) is also included in VAT payable. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT. The related VAT deferred liability is maintained until the debtor is written off for tax purposes.

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.

For the purpose of the consolidated cash-flow statement, cash and cash equivalents consist of cash and cash equivalents as described above.

3. Summary of Significant Accounting Policies (continued)

3.14 Borrowings

All loans and borrowings are initially recognized at cost, being the fair value of the consideration received net of issue costs associated with the borrowing.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Gains and losses are recognized in net profit or loss when the liabilities are derecognized or impaired, as well as through the amortization process

3.15 Leases

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

Capitalized leased assets are depreciated using the straight-line method over the estimated useful life of the asset like other fixed assets within the same class, with consideration of the contractual terms under which the assets can be used.

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

3.16 Pensions and Other Post-Employment Benefits

Unified social tax

Social contributions are made through a unified social tax (UST) calculated by the Company by the application of a regressive rate (from 35.6% to approximately 26%) to the annual gross remuneration of each employee. The Company allocates the UST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund vary from 28% to 14% 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.

Other pension plans and post-employment benefits

Under collective bargaining agreements and internal regulations on additional pension benefits, the Company also provides benefits for its employees by using post-employment 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.

Post-employment benefit plans include defined contribution plans and defined benefit plans.

3. Summary of Significant Accounting Policies (continued)

3.16 Pensions and Other Post-Employment Benefits (continued)

Defined contribution plan is a post-employment benefit plan under which the Company's obligation is limited solely to the amount of a contribution it agrees to pay into a fund. In this case all actuarial and investment risks will be borne by employees. The Company recognizes contributions under a defined contribution plan in the period to which they are attributable.

Under defined benefit plans, the Company's obligation is to provide the agreed benefits to current and former employees. In this case actuarial and investment risks fall on the Company.

3.17 Deferred Income Taxes

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or the initial recognition 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.

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.

Deferred income tax relating to items recognised directly in equity is recognised in equity and not in the income statement.

3.18 Provisions

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, and 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, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

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

3. Summary of Significant Accounting Policies (continued)

3.19 Shareholders' Equity

Share capital

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

Dividends

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

3.20 Revenue

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

The Company categorizes the revenue sources in thirteen major categories:

1. Long distance telephone services - domestic;
2. Long distance telephone services - international;
3. Local telephone services;
4. Installation and connecting fees;
5. Documentary services;
6. Mobile telecommunication services;
7. Radio and TV broadcasting;
8. Data transfer and telematic services;
9. "New services";
10. Rent of telecommunication channels;
11. Services for national telephone operators;
12. Other telecommunication services;
13. Other revenue.

Long distance telephone services (domestic and international)

Revenues from long distance telephone services depend on time of call, duration of call, destination of call, type of service used, subscriber category and the applied tariff plan. The Company charges long distance fees on a per-minute basis. The Company recognizes revenues related to the long distance services in the period when the services are rendered.

Local telephone services

Revenue from the local telephone services depends on the duration of the telephone connections and subscription fee, while time driven billing scheme is applied. If fixed payment scheme is applied then revenue depends on the subscription fee only. The Company recognizes revenues related to the monthly network fees for local services in the period the service is provided to the subscriber.

3. Summary of Significant Accounting Policies (continued)

3.20 Revenue (continued)

Installation and connecting fees

Installation and connection fees for indefinite period contracts are paid by a combination of a fixed cash amount and by the contribution of fixed assets consist of cable and duct, commonly referred to as the "last mile". Revenue received in the form of cash is recognized when the installation and connection are complete. For installation and connection fees paid in the form of fixed assets, revenue is deferred and recognized into income on the same basis that the fixed assets are depreciated.

Documentary services

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

Mobile telecommunication services

Major revenues from cellular services arise from airtime services including local, intercity long distance and international long distance calls, subscription fees, value added services, outbound and inbound roaming. The Company recognizes revenues related to mobile telecommunications services in the period when the services are rendered.

Radio and TV broadcasting

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

Data transfer and telematic services

The Company recognizes revenues related to data transfer and telematic services in the period when the services are rendered.

"New services"

Major revenues from "new services" include internet services, ISDN, IP-telephony, intelligent network services. The Company recognizes revenues related to "new services" in the period when the services are rendered.

Rent of telephone channels

Major revenues are recognized from the following services: rent of digital and analogue intercity, local and telegraph channels. The Company recognizes revenues from the rent of channels in the period when the services are rendered.

Services for national operators

Revenue from national service providers includes two different groups.

3. Summary of Significant Accounting Policies (continued)

3.20 Revenue (continued)

First group of revenues represents services rendered to OAO Rostelecom for termination of long-distance traffic of its operator-partners in the network of the Company.

In 2003 Ministry of Russian Federation for antimonopoly policy and entrepreneurial support (MAP) has conducted reform of the settlements system of OAO Svyazinvest companies with OAO Rostelecom for transit of intercity long-distance traffic. Before August 1, 2003 revenue calculation has been based on the integral settlement rate (ISR), multiplied by the total number of minute-distances (transfer of 1 minute of traffic over the 50 kilometer interval of OAO Rostelecom's network) during the period.

ISR has been calculated as a sum of linear settlement rates between zones and a difference between inbound and outbound termination settlement rates of the regional companies. The rate has been calculated and agreed by the MAP once per year according to traffic statistics of previous year, thus it has not reflected real economical benefits and costs related to changes of the incoming and outgoing structure of the traffic in the current settlement period.

In August 2003 new and more transparent inter-operators settlement system for intercity traffic has been introduced. New system separates payments of regional operators for the transfer of intercity traffic over the OAO Rostelecom network and termination of the traffic in the zone, where outgoing intercity call of own subscriber reaches its destination, and payments for the termination of the incoming intercity traffic from other operators in the own network of the Company.

Calculation of the costs for the transit of intercity traffic is based on the new settlement rate, that is equal to a sum of linear settlement rate multiplied by the number of 50 kilometer intervals between zonal termination settlement rate for the zone where the call is terminated. Revenue calculation for the transit of intercity traffic from OAO Rostelecom to the customers of OAO Svyazinvest regional companies is based on the termination settlement rates. New rates have been defined by the order of the MAP dated July 4, 2003.

Second group of revenues from national operators represents services rendered to interconnected telecom operators that transfer local, intercity and international traffic of their customers via the Company's network.

Major revenues are recognized from the services for transit of local, intercity and international traffic. Further, the Company generates revenue from interconnection to the network (one time fees), rent of channels, rent of equipment, data transfer and Internet services.

The Company recognizes revenues from national operators in the period when the services are rendered.

Other telecommunication services

Other telecommunication services primarily consist of revenues received by public switched telephone network (PSTN) stations from the rent of direct lines and local junctions, as well as subscription fees for wired-radio outlets. The Company recognizes revenues related to other telecommunication services in the period when the services are rendered.

Other revenue

Other revenues primarily consist of revenues received from manufacturing of the telecommunication equipment and its technical support, transportation services, recreation services and sale of products and services provided by auxiliary units.

3.21 Commitments

A commitment is a binding agreement for the exchange of a specified quantity of resources at a specified price on a specified future date or dates.

Significant commitments are disclosed.

Assets to be acquired and liabilities to be incurred as a result of the Company's commitment to purchase or sell goods or services are not recognized until at least one of the parties has performed under the agreement such that it either is entitled to receive an asset or is obligated to disburse an asset.

3.22 Contingencies

Contingent liabilities are not recognised in the financial statements as it is not probable that a liability will need to be settled or the outcome is dependant on a future event. They are disclosed in the accompanying notes unless the possibility of an outflow of resources embodying economic benefit is remote.

Contingent assets are not recognised in the financial statement but disclosed when an inflow of economic benefits is probable.

3.23 IFRS 3 "Business Combinations", IAS 36 "Impairment of Assets" and IAS 38 "Intangible Assets"

The company has chosen an early adoption of IFRS 3, IAS 36 and IAS 38 with provisions of these standards to be applied to business combinations for which the agreement date was on or after January 1, 2003.

4. Segment Information

The Company operates in one industry, mainly the provision of wireline telecommunication services, on the territory of Central Federal District 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.

(in thousands of Russian Roubles)

5. Property, Plant and Equipment

	Land, buildings and constructions	Switches and transmission devices	Construction in progress and equipment for installation	Vehicles and other	Total
Cost					
At December 31, 2003	10,230,722	11,927,712	2,006,371	3,235,442	27,400,247
Additions	-	-	9,692,238	-	9,692,238
Acquisition of subsidiaries	-	820,559	13,107	103,710	937,376
Disposals	(59,614)	(204,803)	(6,395)	(76,628)	(347,440)
Disposal of subsidiaries	(50,378)	(26,487)	(2,558)	(10,380)	(89,803)
Transfers	3,370,500	3,982,101	(8,228,329)	875,728	-
At December 31, 2004	**13,491,230**	**16,499,082**	**3,474,434**	**4,127,872**	**37,592,618**
Accumulated depreciation					
At December 31, 2003	(953,770)	(1,939,059)	-	(192,883)	(3,085,712)
Charge for the year	(1,208,835)	(2,556,092)	-	(446,869)	(4,211,796)
Acquisition of subsidiaries	-	(582,178)	-	(64,191)	(646,369)
Disposals	49,099	158,021	-	60,963	268,083
Disposal of subsidiaries	48,683	26,335	-	9,119	84,137
At December 31, 2004	**(2,064,823)**	**(4,892,973)**	**-**	**(633,861)**	**(7,591,657)**
Net book value as at December 31, 2004	**11,426,407**	**11,606,109**	**3,474,434**	**3,494,011**	**30,000,961**

	Land, buildings and constructions	Switches and transmission devices	Construction in progress and equipment for installation	Vehicles and other	Total
Cost					
At December 31, 2002	8,883,960	7,866,706	1,851,373	2,579,779	21,181,818
Additions	-	-	6,852,333	-	6,852,333
Disposals	(161,789)	(350,698)	(3,319)	(118,098)	(633,904)
Transfers	1,508,551	4,411,704	(6,694,016)	773,761	-
At December 31, 2003	**10,230,722**	**11,927,712**	**2,006,371**	**3,235,442**	**27,400,247**
Accumulated depreciation					
At December 31, 2002	-	-	-	-	-
Charge for the year	(1,094,047)	(2,234,402)	-	(306,177)	(3,634,626)
Disposals	140,277	295,343	-	113,294	548,914
At December 31, 2003	**(953,770)**	**(1,939,059)**	**-**	**(192,883)**	**(3,085,712)**
Net book value as at December 31, 2003	**9,276,952**	**9,988,653**	**2,006,371**	**3,042,559**	**24,314,535**

The Company has applied an 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. Management estimates that the carrying value of all of the Company's property, plant and equipment is broadly comparable to their fair values. However, management has 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.

(in thousands of Russian Roubles)

5. Property, Plant and Equipment (continued)

The carrying value of plant and equipment held under finance leases at December 31, 2004 is 3,387,850 (2003 – 2,013,181). Leased assets are pledged as security for the related finance lease obligations (see Note 18).

The carrying value of property, plant and equipment which were received through vendor financing in 2004, amounted to 213,319 (2003 – 442,414).

In 2004 the Company increased construction in progress by the amount of capitalized interest totaling 364,281 (2003 – 186,368). Capitalization rate in 2004 was 12.55% (2003 – 12.49%).

At December 31, 2004 bank borrowings are secured by properties to the value of 6,553,289 (2003 – 4,667,431) (see Note 17).

6. Intangible Assets

	Goodwill	**Licenses**	**Software**	**Total**
Cost				
At December 31, 2003	29,319	14,224	1,041,078	1,084,621
Additions	-	2,778	1,136,690	1,139,468
Acquisition of subsidiaries	1,177,744	-	454	1,178,198
At December 31, 2004	**1,207,063**	**17,002**	**2,178,222**	**3,402,287**
Accumulated amortization				
At December 31, 2003	-	(2,347)	(37,257)	(39,604)
Charge for the year	-	(3,123)	(31,278)	(34,401)
Acquisition of subsidiaries	-	-	(212)	(212)
At December 31, 2004	**-**	**(5,470)**	**(68,747)**	**(74,217)**
Net book value at December 31, 2004	**1,207,063**	**11,532**	**2,109,475**	**3,328,070**

	Goodwill	**Licenses**	**Software**	**Total**
Cost				
At December 31, 2002	**29,319**	**3,816**	**80,617**	**113,752**
Additions	-	10,408	961,517	971,925
Disposals	-	-	(1,056)	(1,056)
At December 31, 2003	**29,319**	**14,224**	**1,041,078**	**1,084,621**
Accumulated amortization				
At December 31, 2002	**-**	(291)	(12,777)	(13,068)
Charge for the year	-	(2,056)	(25,464)	(27,520)
Disposals	-	-	984	984
At December 31, 2003	**-**	**(2,347)**	**(37,257)**	**(39,604)**
Net book value at December 31, 2003	**29,319**	**11,877**	**1,003,821**	**1,045,017**

Goodwill arose on the acquisition of OAO RTS and OAO Aerocom (see Note 7).

(in thousands of Russian Roubles)

6. Intangible Assets (continued)

As of December 31, 2004 software includes Oracle E-business Suite software with a net book value of 1,099,752 (2003 – 919,517), including 180,235 of expenses for implementation (2003 – nil). In accordance with the supply contract, the Company has been provided with non-exclusive licenses for 18,049 users of E-business Suite 2003 Professional among other license applications.

The Company shall amortize the value of this software starting from the date of its implementation, proportionally to the quantity of licenses used, over useful life of the licenses. Until then the Company shall annually test this software for impairment. Full implementation of Oracle E-Business Suite software is expected by 2005 - 2008.

As of December 31, 2004 software also includes payments for Amdocs Billing Suite software with a net book value of 884,920 (2003 – nil). This software was purchased for the purpose of implementation of unified automated settlements system.

Amdocs Billing Suite software was supplied in December 2004 by OOO IBM Eastern Europe/Asia in exchange for 18 promissory notes issued by the Company in the amount of 1,093,751. Repayment of promissory notes issued is expected to be exercised by June 1, 2006 (see Note 17).

The Company shall start amortizing this asset starting from the date of software implementation proportionally to the cost of implemented modules. Until then the Company shall annually test this software for impairment. Full implementation of the unified automated settlements system is expected by 2009-2010.

Based on the results of the annual impairment test, the Company's management believes that the carrying values of intangible assets are recoverable as of December 31, 2004 and 2003.

7. Investments in Subsidiaries

The consolidated financial statements include the assets, liabilities and financial results of OAO CenterTelecom and its subsidiaries listed below:

Subsidiary	**Main Activity**	**Ownership, %**		**Voting Shares, %**	
		2004	**2003**	**2004**	**2003**
ZAO VladimirTeleservice	Communication services	100%	50%	100%	50%
OOO Mobilcom	Communication services	100%	100%	100%	100%
OOO Teleport Ivanovo	Communication services	100%	100%	100%	100%
OOO Telecom Terminal	Repair and maintenance services	100%	100%	100%	100%
OOO Telecom stroy	Construction services	100%	100%	100%	100%
OAO RTS	Communication services	100%	-	100%	-
RTN (UK) Limited[1], UK	Communication services	100%	-	100%	-
RTN-Leasing[1], Gibraltar	Communication services	100%	-	100%	-
Alarini Enterprises Limited[1],	Communication	100%	-	100%	-

[1] Owned by OAO RTS which was acquired by the Company in March 2004.

(in thousands of Russian Roubles)

Subsidiary	Main Activity	Ownership, %		Voting Shares, %	
		2004	2003	2004	2003
Cyprus	services				
Real Plus Construction[1], Cayman Islands	Communication services	100%	-	100%	-
OOO Ortes[1]	Communication services	100%	-	100%	-
ZAO Restel[1]	Communication services	100%	-	100%	-
OOO Rosnet Neva[1]	Communication services	100%	-	100%	-
ZAO Rosnet International[1]	Communication services	99%	-	99%	-
OAO Aerocom	Communication services	99.6%	-	99.6%	-
OOO Tver Telecom	Communication services	85%	26%	85%	26%
ZAO CenterTelecomService of Moscow Region	Communication services	76%	51%	76%	51%
OOO VladPage	Communication services	75%	75%	75%	75%
ZAO CenterTelecomService	Communication services	74.9%	74.9%	74.9%	74.9%
OOO Svyaz-Service-Irga	Repair and maintenance services	70%	70%	70%	70%
OOO Vladimirskiy Taxophone	Communication services	51%	51%	51%	51%
ZAO Telecom of Ryazan Region	Communication services	50.9%	50.9%	50.9%	50.9%
ZAO TeleRossVoronezh[2]	Communication services	50%	50%	50%	50%
ZAO Sotovaia Svyaz Chernozemia	Communication services	-	45%	-	60%

All subsidiaries, except for specifically mentioned otherwise, are Russian legal entities registered in accordance with Russian legislation. All subsidiaries have the same financial year as the Company.

Acquisition of OAO Rossiyskaya Telecommunicationnaya Set (RTS)

In March 2004 the Company acquired 100% of ordinary voting shares of OAO RTS. The main business activity of OAO RTS represents data transfer services on the territory of Russian Federation.

The purchase price amounted to 845,122. Costs directly attributable to the acquisition amounted to 15,509. The fair value of identifiable assets, liabilities and contingent liabilities of OAO RTS approximated the book values.

[2] Control obtained due to the majority in the Board of Directors.

(in thousands of Russian Roubles)

7. Investments in Subsidiaries (Continued)

The financial results of OAO RTS were included in the consolidated financial statements since April 1, 2004. The fair value of identifiable assets and liabilities of OAO RTS as at the date of acquisition are as follows:

Cash paid	845,122
Costs directly attributable to the acquisition	15,509
Total consideration	**860,631**
Fair value of identifiable assets and liabilities:	
Property, plant and equipment	249,282
Long-term investments	8,319
Accounts receivable	82,921
Cash and cash equivalents	10,975
Other current assets	40,268
Current liabilities	(205,652)
Deferred tax liability	(3,149)
Other long-term liabilities	(289)
Total net assets	**182,675**
Share in acquired net assets	100%
Value of share in net identifiable assets	182,675
Goodwill	**677,956**

The cash outflow on the acquisition of OAO RTS is as follows:

Net cash acquired with the acquisition	10,975
Total consideration	(860,631)
Net cash outflow	**(849,656)**

As the result of the acquisition of OAO RTS the Company acquired additional 25% of shares held by OAO RTS in the Company's subsidiary ZAO CenterTelecomService of Moscow Region. The Company's ownership in ZAO CenterTelecomService of Moscow Region increased from 51% to 76% of ordinary voting shares. This transaction represents the purchase of minority interest from minority shareholders for the total amount of 8,312.

(in thousands of Russian Roubles)

7. Investments in Subsidiaries (Continued)

Acquisition of OAO Aerocom

In March 2004 the Company acquired 99.62% of ordinary voting shares of OAO Aerocom. OAO Aerocom operates as a provider of communications services on the territory of Russian Federation.

The purchase price amounted to 484,220. Costs directly attributable to the acquisition amounted to 7,927. The fair value of identifiable assets, liabilities and contingent liabilities of OAO Aerocom approximated the book values.

The financial results of OAO Aerocom are included in the consolidated financial statements since April 1, 2004. The fair value of identifiable assets and liabilities of OAO Aerocom as at the date of acquisition are as follows:

Cash paid	484,220
Costs directly attributable to the acquisition	7,927
Total consideration	**492,147**
Fair value of identifiable assets and liabilities:	
Property, plant and equipment	22,473
Intangible assets	267
Accounts receivable	44,502
Cash and cash equivalents	395
Other current assets	4,975
Current liabilities	(80,282)
Total net liabilities	**(7,670)**
Share in acquired net liabilities	99.62%
Value of share in net identifiable liabilities	(7,641)
Goodwill	**499,788**

The cash outflow on the acquisition of OAO Aerocom is as follows:

Net cash acquired with the acquisition	395
Total consideration	(492,147)
Net cash outflow	**(491,752)**

(in thousands of Russian Roubles)

7. Investments in Subsidiaries (Continued)

Acquisition of OOO Tver Telecom

In October 2004 the Company obtained control over OOO Tver Telecom by increasing its share of ownership from 26% to 85%. The fair value of identifiable assets, liabilities and contingent liabilities of OOO Tver Telecom approximated the book values.

The purchase price amounted to 17,182. Costs directly attributable to the acquisition amounted to 15.

The financial results of OOO Tver Telecom are included in the consolidated financial statements since October 1, 2004. The fair value of identifiable assets and liabilities of OOO Tver Telecom as at the date of acquisition are as follows:

Cash paid	17,182
Costs directly attributable to the acquisition	15
Total consideration	**17,197**
Fair value of identifiable assets and liabilities	
Property, plant and equipment	20,581
Long-term investments	3,118
Accounts receivable	16,913
Cash and cash equivalents	604
Other current assets	2,295
Current liabilities	(22,606)
Total net assets	**20,905**
Share in acquired net assets	59%
Value of share in net identifiable assets	12,334
Goodwill	**4,863**

The cash outflow on the acquisition of OOO Tver Telecom is as follows:

Net cash acquired with the acquisition	604
Total consideration	(17,197)
Net cash outflow	**(16,593)**

As a result of the acquisition of 59% additional interest in OOO Tver Telecom the Company reclassified its investments in OOO Tver Telecom from investments in associates to investments in subsidiaries as of December 31, 2004.

Other acquisitions and disposals of subsidiaries

In 2004 the Company increased its ownership in ZAO Vladimir Teleservice from 50% to 100% by acquiring additional 50% of its ordinary voting shares. This transaction represents the purchase of minority interest from minority shareholders for the total amount of 2,112.

In 2004 investments in ZAO SvyazProekt (53% ownership) were written-off due to its bankruptcy. There was no resulting loss on this write-off in 2004 because in 2003 corresponding impairment provision was created for the total amount of the investment of 21,701.

(in thousands of Russian Roubles)

7. Investments in Subsidiaries (Continued)

During 2004 the following disposals of shares of Subsidiaries occurred:

Subsidiary	Main Activity	Carrying value of net assets disposed	Proceeds from sale, net of transaction expenses	Gain on disposal of subsidiaries	Disposal of share in equity on the date of transaction, %
ZAO Sotovaia Svyaz Chernozemia	Communication services (NMT-450)	(34 634)	116 731	151 365	45
Total		**(34 634)**	**116 731**	**151 365**	

8. Investments in Associates and Joint Ventures

Investments in associates and joint ventures at December 31, 2004 and 2003 include:

Associate	Main activity	2004 Voting shares	2004 Carrying value	2003 Voting shares	2003 Carrying value
Joint activity	Cellular services	30%	14,579	30%	14,579
ZAO SK Kostars	Insurance services	28%	2,815	-	-
OAO Telecommunication company Rinfotels	Communication services	26%	1,348	26%	1,291
OOO Tver Telecom (see Note 7)	Communication services	-	-	26%	6,556
OAO Gazenergobank	Banking services	-	-	25%	8,264
ZAO Radiopaging	Communication services	-	-	30%	4,848
OAO Trunksvyaz	Communication services	-	-	25%	31
ZAO Smolenskaya Sotovaya Svyaz	Cellular services	40%	-	40%	-
ZAO Belgorodskaya Sotovaya Svyaz	Cellular services	30%	-	30%	-
ZAO Bryanskie Sotovye Seti	Cellular services	-	-	34%	-
ZAO Ryazanskaya Sotovaya Svyaz	Cellular services	-	-	40%	-
ZAO Kaluzhskaya Sotovaya Svyaz	Cellular services	-	-	42%	-
ZAO Tverskaya Sotovaya Svyaz	Cellular services	-	-	40%	-
OAO Rating	Communication services	-	-	25%	-
Impairment provision		-	(2,815)	-	(4,848)
Total			**15,927**		**30,721**

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

In 2004 the Company did not recognize its share in net loss of ZAO Smolenskaya Sotovaya Svyaz and ZAO Belgorodskaya Sotovaya Svyaz in the amount of 16,958 and 20,536, respectively. As of December 31, 2004 the Company's share in accumulated loss of associated ZAO Smolenskaya Sotovaya Svyaz and ZAO Belgorodskaya Sotovaya Svyaz amounted to 59,581 (2003 – 24,819). In accordance with IAS 28 "Accounting for Investments in Associates" the Company reduced the carrying value of the associates to zero in cases when the Company's share in accumulated loss exceeded the cost of the respective investment.

(in thousands of Russian Roubles)

8. Investments in Associates and Joint Ventures (continued)

Joint activity

The Company has a 30% interest in a joint venture with OOO Topsnabinvest and OOO Bowling-Center, which is involved in the creation, development and commercial service of CDMA standard radiotelephony in Ivanovo. The joint venture agreement concluded on November 29, 2002, is valid for 8 years.

The Company's share of the assets, liabilities, revenue and expenses of the joint venture, which are included in the consolidated financial statements under equity method, are as follows at December 31, 2004 and 2003 and for the years then ended:

	2004	2003
Non-current assets	**41,911**	45,466
Current assets	**17,039**	20,700
Current liabilities	**(10,354)**	(17,570)
Total net assets	**48,596**	**48,596**
Company's share in net assets	**14,579**	**14,579**
Revenue	**19,209**	22,067
Operating expenses	**(10,616)**	(8,503)
Other income	**36**	-
Net profit	**8,629**	**13,564**
Company's share in net income	**2,589**	**4,070**

Acquisition of interest in ZAO SK Kostars

On December 30, 2004 the Company acquired a 28% interest in ZAO SK Kostars, an insurance company, and obtained significant influence over it. Accordingly, the share of the Company in its results of operations and financial position has been recorded since December 31, 2004.

The purchase price amounted to 2,800. Costs directly attributable to the acquisition amounted to 15. The investment was initially recorded at cost for the total amount of consideration given 2,815. However, due to the fact that Federal Agency of Insurance Supervision had filed a cassation concerning invalidation of decree "On withdrawal of an insurance license" in a part of withdrawal of ZAO SK Kostars's insurance license, the decision was made to create an impairment reserve for the total amount of investment in ZAO SK Kostars.

(in thousands of Russian Roubles)

8. Investments in Associates and Joint Ventures (continued)

Disposals of associates

During 2004 the following disposals of shares in associates occurred:

Name	Main activity	Carrying value of investment	Proceeds from sale, net of transaction expenses	Gain/(loss) on disposal of associate	Disposal of share in equity on the date of transaction, %
ZAO Bryanskie Sotovye Seti	Cellular services	-	42,913	42,913	34%
ZAO Ryazanskaya Sotovaya Svyaz	Cellular services	-	40,665	40,665	40%
ZAO Kaluzhskaya Sotovaya Svyaz	Cellular services	-	28,369	28,369	42%
ZAO Tverskaya Sotovaya Svyaz	Cellular services	-	15,040	15,040	40%
OAO Gazenergobank	Banking services	8,992	7,687	(1,305)	25%
OAO Rating	Communication services	-	36	36	29%
Total		**8,992**	**134,710**	**125,718**	

Gains and losses arising on disposal of associates are included into "Gain (loss) from investments" in Consolidated Statement of Operations (see Note 25).

On April 30, 2004 investments in ZAO Radiopaging (30% ownership) were written-off due to its bankruptcy. There was no resulting loss on this write-off in 2004 because in 2003 corresponding impairment provision was created for the total amount of the investment of 4,848.

Movement in investments

Movement in investments in associates and Joint Ventures for the years ended December 31, 2004 and 2003 is presented below:

	2004	**2003**
Investments in associates and joint ventures at January 1	**30,721**	**36,107**
Acquisition of ZAO SK Kostars	2,815	-
Share of loss net of income tax and dividends received	(367)	(5,015)
Additional purchase of shares of OOO Tver Telecom	(5,435)	-
Disposal of associates	(8,992)	(9)
Impairment provision	(2,815)	(362)
Investments in associates and joint ventures at December 31	**15,927**	**30,721**

(in thousands of Russian Roubles)

9. Other Financial Assets

As of December 31, 2004 and 2003, other financial assets included:

	2004	2003
Long-term VAT receivable	**299,130**	172,368
Long-term investments held-to-maturity	**163**	163
Long-term accounts receivable	**22**	3,603
Long-term loans given	**24,311**	33,177
Total	**323,626**	209,311

As of December 31, 2004 and 2003 long-term loans given are composed of interest-free loans given to the employees of the Company.

10. Long-Term Advances Given

As of December 31, 2004 and 2003 advances to suppliers of equipment comprised the following:

	2004	2003
Advances for purchase of property and equipment	**1,056,076**	659,308
Total	**1,056,076**	659,308

11. Inventories

Inventories at December 31, 2004 and 2003 included the following:

	2004	2003
Cable, materials and spare parts for telecommunications equipment	**551,029**	512,523
Finished goods and goods for resale	**21,692**	21,358
Other inventories	**4,797**	9,317
Total	**577,518**	543,198

12. Trade Receivables

Trade receivables as of December 31, 2004 and 2003 comprised the following:

	2004	2003
Trade receivables – telecommunication services	**3,777,524**	2,858,918
Trade receivables – other	**152,865**	57,395
Provision for impairment of receivables	**(1,993,746)**	(1,247,545)
Total	**1,936,643**	1,668,768

The Company identified accounts receivable by the following major customer groups:

	2004	2003
Corporate customers	**733,442**	502,918
Residential customers	**1,090,091**	1,047,794
Governmental customers	**2,106,856**	1,365,601
Total	**3,930,389**	2,916,313

(in thousands of Russian Roubles)

12. Trade Receivables (continued)

The Company invoices its governmental and corporate customers on a monthly basis. For residential customers, the Company sends monthly payment requests and substantially relies upon these customers to remit payments based on the received payment requests. All customer payments are based upon tariffs, denominated in rubles, in effect at the time the calls are made. In certain cases the Company managed to collect penalties for payment delays and to enforce reimbursement in arbitration court.

Article 47 of the Federal Law "On Telecommunications" No. 126-FZ dated July 7, 2003 will be effective starting from 2005, which changes rules on granting privileges to residential customers for services rendered by telecommunication companies. Starting from January 2005 telecommunication customers with the right to privileges are obliged to pay for telecommunication services in full with the subsequent compensation of their expenses by budget funds of respective levels. However, in 2005 state budget does not provide for financing of the remaining debt of social security organizations to compensate expenses related to granting privileges to certain category of subscribers in the previous periods.

As of December 31, 2004 debt of social security organizations with regard to compensation of expenses related to granting privileges to certain category of subscribers amounted to 52.4% of total accounts receivable (2003 – 43.5%).

In 2004 the Company enforced by legal action from federal budget to cover stated accounts receivable of 53,627. In December 2004 based on assessment of probability of judicial recovery of accounts receivable related to compensation due from social security organizations, the Company has accrued provision for impairment of receivables of 1,712,281 (2003 - 1,008,709) representing 88% (2003 – 86%) of total receivables from social security organizations as of December 31, 2004.

The following summarizes the changes in the provision for impairment of trade receivables:

	2004	2003
Balance at January 1	**(1,247,545)**	(558,887)
Increase in provision for the year	**(831,322)**	(801,968)
Acquisition of subsidiaries	**(11,961)**	-
Trade receivables written-off	**97,082**	113,310
Balance at December 31	**(1,993,746)**	(1,247,545)

13. Other Current Assets

As of December 31, 2004 and 2003 other current assets comprised the following:

	2004	2003
VAT receivable	**1,269,407**	880,863
Prepaid income tax	**220,824**	238,349
Prepayments and advance payments	**206,130**	195,521
Deferred expenses	**202,625**	206,023
Deposit for the purchase of long-term investments	**143,939**	-
Receivables from sales of property, plant and equipment	**11,965**	4,544
Other prepaid taxes	**28,941**	21,389
Short-term loans given	**28,924**	-
Settlements with personnel	**10,783**	11,084
Other receivables and current assets	**246,171**	110,459
Total	**2,369,709**	1,668,232

(in thousands of Russian Roubles)

13. Other Current Assets (continued)

Subsequent to December 31, 2004 the deposit made for the purchase of long-term investments was returned to the Company.

14. Cash and Cash Equivalents

As of December 31, 2004 and 2003 cash and cash equivalents comprised the following:

	2004	2003
Cash at bank and on hand	**1,416,586**	1,028,494
Short-term deposits with original maturities of three months or less	**628**	23,940
Other cash equivalents	-	155
Total	**1,417,214**	1,052,589

As of December 31, 2003 the loan from ZAO KB Guta-bank was guaranteed by the restricted cash balance in ZAO KB Guta-bank in the amount of 225,000. This loan was fully repaid in 2004.

15. Share Capital

As at December 31, 2004 and 2003 the authorised number of ordinary and preference shares are 1,578,006,833 and 525,992,822 respectively. All authorised shares have been issued and fully paid.

Type of shares	Number of outstanding shares (thousands)	Par value per one share (Roubles)	Total par value	Carrying value
Ordinary	1,578,007	0.3	473,402	304,840
Preferred	525,993	0.3	157,798	914,526
Total	**2,104,000**		**631,200**	**1,219,366**

The ordinary shareholders, which represent 75% of the share capital, are entitled to one vote per share. Class A preference shares, which represent 25% of the share capital, give the holders the right to participate in general shareholders' meetings without voting rights except in instances where decisions are made in relation to re-organisation and liquidation of the Company, and where changes and amendments to the Company's charter, which restrict the rights of preference shareholders, are proposed. The preference shares have no rights of redemption or conversion but carry non-cumulative dividends per share of 10% of Russian statutory accounting net income for the year.

Annual amount of dividends on class A preference shares may not be less than dividends on ordinary shares. As such, the preference shareholders share in earnings along with ordinary shareholders and thus the preference shares are considered participating shares for the purpose of the calculation of earnings per share. If the Company fails to pay dividends, or has no profits in any year, the preferred shareholders have the right to vote in the general shareholders' meeting. Shareholders of class A preference shares have a preference right to recover the par value of preference shares in liquidation.

In 2001 the Company signed a deposit agreement with JP Morgan Chase Bank regarding placement of Level 1 American Depositary Receipts (ADR). In accordance with the deposit agreement, each ADR represents 100 ordinary shares of the Company. As of December 31, 2004, ADRs represented 223,192,800 deposited ordinary shares, which constituted 1.4698% of total ordinary shares issued.

15. Share Capital (continued)

The Company's shareholding structure as of December 31, 2004 (in thousands of shares) was as follows:

	Ordinary shares		Preference shares	
		%		%
OAO Svyazinvest	799,868	51%	-	-
Other legal entities	667,102	42%	432,677	82%
Individuals	111,037	7%	93,316	18%
Total	**1,578,007**	**100%**	**525,993**	**100%**

16. Minority Interest

Movement of minority interest for the years ended December 31, 2004 and 2003 is as follows:

	2004	2003
Minority interest as of January 1	358	17,570
Purchase of minority interest in existing subsidiaries (see Note 7)	(10,424)	-
Minority interest in net assets of acquired subsidiaries	3,312	-
Minority interest in net assets of disposed subsidiaries	23,115	-
Minority interest in net income of subsidiaries	8,003	(17,212)
Dividends paid to minority shareholders of subsidiaries	(390)	-
Minority interest as of December 31	23,974	358

(in thousands of Russian Roubles)

17. Borrowings

As of December 31, 2004 and 2003 borrowings comprised the following:

	Effective interest rate	Maturity	2004	2003
Short-term borrowings				
Bank loans				
Bank loans (Roubles)	13.6%	2005	**1,717,165**	1,980,470
Bank loans (US Dollars)	7.2%	2005	**3,352**	97,784
Bank loans (Euro)	6.9%	overdue 2005	**370,284**	623,756
			2,090,801	2,702,010
Bonds				
Bonds (Roubles)	13.6%	2005	**373,475**	78,699
Vendor financing				
Vendor financing (Roubles)	18.3%	2005	**44,534**	32,084
Vendor financing (US Dollars)	3.2%	2005	**693,161**	44,419
Vendor financing (Euro)	7.3%	2005	**2,478**	26,531
			740,173	103,034
Promissory notes				
Promissory notes (Roubles)	12.8%	2005	**1,368,197**	535,906
Total short-term borrowings			**4,572,646**	3,419,649

(in thousands of Russian Roubles)

17. Borrowings (continued)

Long-term borrowings	**Effective interest rate**	**Maturity**	**2004**	**2003**
Bank loans				
		overdue		
Bank loans (Roubles)	14.2%	2005-2009	**5,516,386**	3,465,443
Bank loans (US Dollars)	7.4%	2005-2007	**338,092**	710,900
Bank loans (Euro)	7.4%	2005-2007	**485,599**	653,373
Bank loans (Japanese Yens)	4.8%	2005	**5,830**	16,302
			6,345,907	4,846,018
Bonds				
Bonds (Roubles)	13.6%	2005-2009	**8,092,787**	2,559,028
Vendor financing				
Vendor financing:				
Vendor financing (Roubles)	5.6%	2005-2010	**13,607**	4,905
		overdue	**405,249**	157,949
Vendor financing (US Dollars)	5.8%	2005-2010		
		overdue	**233,860**	385,828
Vendor financing (Euro)	8.3%	2005-2007		
			652,716	548,682
Promissory notes				
Promissory notes (Roubles)	12.9%	2006	**669,928**	-
Borrowings from related parties (OAO Svyazinvest, see Note 31)	16%	2005	**29,000**	33,015
Restructured connection fees from customers (Roubles)			**82,382**	78,228
Total long-term borrowings			**15,872,720**	8,064,971
Less: Current portion of long-term borrowings			**(2,900,072)**	(1,105,797)
Total long-term borrowings less current portion			**12,972,648**	6,959,174

As of December 31, 2004 short-term borrowings include interest payable in the amount of 486,605 (2003 – 419,333).

As of December 31, 2004 bank loans are guaranteed by collateral of property, plant and equipment amounting to 8,032,258 (2003 – 6,984,820).

(in thousands of Russian Roubles)

17. Borrowings (continued)

As of December 31, 2004, long-term borrowings had the following maturity schedule:

Maturity date	Bank loans	Bonds	Vendor financing	Promissory notes	Other	Total
Overdue	74,537	-	19,371	-	18	93,926
2005	2,007,506	600,000	159,008	-	29,000	2,795,514
2006	473,613	1,974,206	364,873	669,928	-	3,482,620
2007	387,216	-	84,304	-	2,554	474,074
2008	2,150,832	-	-	-	17,004	2,167,836
2009 and after	1,252,203	5,518,581	25,160	-	62,806	6,858,750
Total	**6,345,907**	**8,092,787**	**652,716**	**669,928**	**111,382**	**15,872,720**

As of December 31, 2003, long-term borrowings had the following maturity schedule:

Maturity date	Bank loans	Bonds	Vendor financing	Other	Total
Overdue	45,929	-	-	-	45,929
2004	768,433	-	333,349	4,015	1,105,797
2005	2,088,202	600,000	46,943	29,528	2,764,673
2006	512,054	1,959,028	41,541	3,018	2,515,641
2007	103,494	-	126,849	17,120	247,463
2008 and thereafter	1,327,906	-	-	57,562	1,385,468
Total	**4,846,018**	**2,559,028**	**548,682**	**111,243**	**8,064,971**

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

Currency	2004	2003
Russian Roubles	17,907,461	8,767,778
US dollars	1,439,854	1,011,052
Euros	1,092,221	1,689,488
Japanese yens	5,830	16,302
Total	**20,445,366**	**11,484,620**

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

The most significant borrowings are presented below:

Short-term Loans

Bank Loans

Most of short-term borrowings denominated in Rubles represent bank loans received to finance working capital. Major part of loans is collateralized with telecommunications equipment.

17. Borrowings (continued)

Sberbank

In 2004 the Company entered into short-term loan agreements with Sberbank. The loans mature in 2005. As of December 31, 2004 the outstanding liability under these agreements amounted to 409,777. Interest is accrued at 11-14% per annum. The loans are secured by property and equipment with collateral value of 468,194.

Alfa-Bank

In 2004 the Company entered into short-term loan agreements with Alfa-Bank. The loans mature in 2005. As of December 31, 2004 the outstanding liability under these agreements amounted to 572,823. Interest is accrued at 15% per annum. The loans are secured by property and equipment with collateral value of 426,715.

Trustbank

In 2004 the Company entered into short-term loan agreement with Trustbank. The loan matures in 2005. As of December 31, 2004 the outstanding liability under this agreement amounted to 502,103. Interest is accrued at 14-16% per annum. The loan is not secured.

Vnesheconombank

In 1995-1997 the Ministry of Finance (hereafter "the Ministry") granted the Company long-term financing for purchases of telecommunication equipment from various foreign vendors. Vnesheconombank has been acting as an agent of the Ministry on collection of payments from the company. The liability was initially denominated in Deutsche Marks (DM), and later in Euro after introduction of the Euro.

Following the crisis of 1998 and the significant increase of the exchange rate of DM to Ruble, repayments on these agreements were ceased. As a result, as of December 31, 2004 approximately 335,898 of payable (2003 - 373,133), including interest payable of 55,706 (2003 - 59,720) due to Vnesheconombank were overdue.

As of December 31, 2004 the outstanding short-term liability, including overdue amounts, under these agreements amounted to 369,242 (2003 – 439,170). Interest is accrued at Plafond C+2%. In 2004 the interest rate applied varied in the range of 6-7% per annum. The loan is not secured.

Rossiyskiy Bank Razvitiya (RBR)

In 2004 the Company entered into short-term loan agreement with RBR. The loan matures in 2005. As of December 31, 2004 the outstanding liability under this agreement amounted to 138,989. Interest is accrued at 12% per annum. The loan is not secured.

Promsvyazbank

In 2003-2004 the Company entered into short-term loan agreements with Promsvyazbank. The loans mature in 2005. As of December 31, 2004 the outstanding liability under these agreements amounted to 60,701. Interest is accrued at 12% per annum. The loans are secured by property and equipment with collateral value of 110,479.

17. Borrowings (continued)

Vendor Financing

ZAO Sokol-ATS

In April 2003 the Company entered into agreement with ZAO Sokol-ATS, under which Sokol-ATS delivered telecommunication equipment to the Company. The agreement matures in 2005. As of December 31, 2004 the outstanding liability under these agreements amounted to 44,533. Interest is accrued at a weighted average interest rate on the Company interest bearing borrowings obtained in appropriate period.

OOO IBM East Europe/Asia

In 2004 the Company entered into software delivery agreement with OOO IBM East Europe/Asia. Under the agreement conditions the Company issued promissory notes and transferred it to OOO IBM East Europe/Asia as a payment guarantee. Part of the liability on promissory notes, which mature in 2005 and as of December 31, 2004 amounting to 692,699 is classified as short-term vendor financing liability. The outstanding amount under this agreement is denominated in US dollars. Interest is accrued at 5% per annum. The liability is not collateralized.

Promissory Notes

In 2004 the Company issued promissory notes at par value of 1,410,000 with the discount of 181,489 applied upon issue. The notes were purchased by ZAO RTC-Invest and OOO Brokerskaya kontora Severo-Zapadnyi Investicionnyi Center. Interest on the notes is accrued at 12.9 %. The liability on the promissory notes as of December 31, 2004 amounted to 1,349,299. The notes mature in 2005.

In 2003 the Company issued promissory notes at par value of 606,082. A discount of 76,569 was applied to the notes upon issue. The notes were purchased by OAO Vneshtorgbank and ZAO RTC-Invest. Interest on the notes was accrued at 14%. The notes matured in 2004.

17. Borrowings (continued)

Long-term borrowings

Bank loans

Sberbank

In 2003-2004 the Company entered into long-term loan agreements with Sberbank. The loans mature in 2005-2009. As of December 31, 2004 the outstanding liability under these agreements amounted to 4,939,546, including liabilities maturing in 2005 amounted to 1,474,556. Interest is accrued at 12-15% per annum. The loans are secured by property and equipment with collateral value of 5,049,048.

Vnesheconombank

In 1995-1997 the Ministry provided long-term financing to the Company to purchase telecommunications equipment from various foreign vendors. Vnesheconombank acted as the Company's lending agent on behalf of the Ministry. Initially the agreement was denominated in DM. After transition to Euro, the loan was converted to Euro. As of December 31, 2004 the outstanding liability under these agreements amounted 260,161, including liabilities maturing in 2005 amounted to 167,841. The interest under this agreement is accrued at floating rate Plafond C+2%, which in 2004 approximated 6-7%. The loan is not collateralized.

Vneshtorgbank

In 2002-2004 the Company entered into long-term loan agreements with Vneshtorgbank. The loans mature in 2005-2007. As of December 31, 2004 the outstanding liability under these agreements amounted to 526,617, including liabilities maturing in 2005 amounted to 325,608. Interest is accrued at 6-13% per annum. The loans are secured by property and equipment with collateral value of 793,227.

Promsvyazbank

In 2004 the Company entered into long-term loan agreements with Promsvyazbank. The loans mature in 2005-2009. As of December 31, 2004 the outstanding liability under these agreements amounted to 409,288, including liabilities maturing in 2005 amounted to 9,288. Interest is accrued at 12-15% per annum. The loans are secured by property and equipment with collateral value of 740,427.

Guta-Bank

In 2001-2004 the Company entered into long-term loan agreements with Guta-Bank. The loans mature in 2005-2007. The amounts payable under the agreements are denominated in Russian roubles and US dollars. Interest for loans denominated in Russian roubles is accrued at 14-15% per annum, for loans, denominated in dollars – LIBOR + 7%. As of December 31, 2004 the outstanding liability under these agreements amounted to 60,077 for loans, denominated in Russian rubles and 133,698 for loans, denominated in US dollars. The loans are secured by property and equipment with collateral value of 150,758.

Vendor Financing

OOO IBM East Europe/Asia

As described earlier in this Note, in 2004 the Company entered into software delivery agreement with OOO IBM East Europe/Asia, under which the Company issued promissory notes and transferred it to OOO IBM East Europe/Asia as a payment guarantee. Part of the liability on promissory notes, which mature in 2006, amounting to 346,403 is classified as long-term vendor financing liability and as of December 31, 2004.

17. Borrowings (continued)

Mashpriborkom

In 1997 the Company entered into a number of agreements with Mashpriborkom. The agreements mature in 2005-2007. The outstanding amount under these agreements is denominated in Euro. Interest is accrued at 9% per annum. As of December 31, 2004 the outstanding long-term liability under these agreements amounted to 98,761, including liability maturing in 2005 of 37,372. The loans are secured by property and equipment with collateral value of 157,394.

Iskratel

In 2002-2004 the Company entered into a number of agreements with Iskratel. Under the agreements Iskratel undertook to deliver telecommunications equipment. The agreements mature in 2005-2007. The outstanding amount under these agreements is denominated in US Dollars and Euro. Interest is accrued at 9% per annum. As of December 31, 2004 the outstanding long-term liability under these agreements amounted to 89,111 including liability maturing in 2005 amounted to 57,615. The liability is not collateralized.

Siemens AG

In 1994-1998 the Company entered into a number of agreements with Siemens AG, under which Siemens AG undertook to deliver telecommunications equipment. The agreements mature in 2005-2007. The outstanding amount under these agreements is denominated in Euro. Interest is accrued at 7% per annum. As of December 31, 2004 the outstanding long-term liability under these agreements amounted to 32,342, including liability maturing in 2005 amounted to 29,442. The liability is not collateralized.

Promissory Notes

In 2004 the Company issued promissory notes at par value of 763,175 with the discount of 133,175 applied upon issue. The notes were purchased by Vneshtorgbank. Interest on the notes is accrued at 11.7 %. The liability on the promissory notes as of December 31, 2004 amounted to 669,928. The notes mature in 2006.

Bonds

In June 2002 the Company registered the issue of interest-bearing bonds 02 series with a par value of 1,000 Roubles each for the total amount of 600,000. Bonds have 6 coupons. Payments against the first coupon are made on the 91-st day from the date of issue; interest per other coupons are payable on the 273, 456, 638, 821 and 1,003-rd day. Coupon interest rate on the first and second coupons is determined at 20% per annum; coupon interest rate on the third and forth coupons is determined at 18% per annum; coupon interest rate on the fifth and sixth coupons is determined at 16% per annum. Effective coupon interest rate is set at 16.62% per annum. The bonds mature in 1,003 days from the date of issue in April 2005. The outstanding amount of liability was classified as a current portion of long-term borrowings and amounted to 600,000. Part of the sixth coupon interest payable in April 2005 was accrued as short-term liability in the amount of 18,672. Subsequent to December 31, 2004, the Company fully redeemed these bonds (see Note 34).

In September 2003 the Company registered the issue of interest-bearing bonds 03 series with a par value of 1,000 Roubles each for the total amount of 2,000,000. Bonds have 6 coupons. Payments against the first coupon are made on the 183-rd day from the date of issue; interest per other coupons are payable every subsequent 183-rd day. Coupon interest rate is determined at 12.35 % per annum. The bonds mature in 1,095 days from the date of issue in September 2006. Part of the third coupon interest payable in March 2005 was accrued as short-term liability in the amount of 71,740.

(in thousands of Russian Roubles)

17. Borrowings (continued)

In September 2003 the Company offered to buy back its 03 series bonds at 101.5% of par value in September – October 2004. Bonds for the total amount of 1,284,820 were repurchased and issued back in September – October 2004 for the same amount.

In September 2004 the Company also published an irrevocable offer to buy back 03 series bonds on September 19, 2005. Subsequent to the year end bond offer expired and none were submitted for repurchase. These bonds were classified as long-term liability.

In June 2004 the Company registered and issued interest-bearing bonds 04 series with a par value of 1,000 Rubles each for the total amount of 5,622,595. The bonds mature in 1,830 days from the date of issue. Bonds have 10 coupons. Payments against the first coupon are made on the 183-rd day from the date of issue; interest per other coupons are payable every subsequent 183-rd day. Coupon interest rate is determined at 13.8% per annum.

In June 2004 the Company announced an irrevocable offer to repurchase 04 series bonds in September 2006. The outstanding liability of 5,622,595 was classified as long-term and part of the first coupon interest payable in February 2005 was accrued as short-term liability in the amount of 289,114.

18. Finance Lease Obligations

The Company has finance lease contracts for telecommunication equipment. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments as of December 31, 2004 and 2003 are as follows:

	2004		**2003**	
	Minimum lease payments	**Present value of payments**	**Minimum lease payments**	**Present value of payments**
Within one year	1,132,393	672,491	877,871	512,769
After one year but no more than five years	2,427,529	1,775,171	1,700,217	1,167,947
Total minimum lease payments	3,559,922		2,578,088	
Less amounts representing finance charges	(1,112,260)		(897,372)	
Present value of minimum lease payments	2,447,662	2,447,662	1,680,716	1,680,716

In 2004 and 2003 the Company's primary lessors were OAO RTC-Leasing and OOO Promsvyazleasing. In 2004 effective interest rate on leasing liabilities denominated in Russian rubles was 27% per annum (2003 - 34%).

OAO RTC-Leasing purchases telecommunication equipment from domestic and foreign suppliers and leases that equipment. The Company’s obligations under capital leases to OAO RTC-Leasing as of December 31, 2004 comprised 2,275,991 (2003 - 1,362,038).

Pursuant to agreements concluded with OAO RTC-Leasing, the lessor is entitled to adjust the lease payment schedule in the event of change in certain changes in economic environment, in particular, change in the refinancing rate of the Central Bank of the Russian Federation.

As of December 31, 2004 finance lease obligations denominated in foreign currency, mainly US Dollars, amounted 152,588 (2003 - 284,728).

(in thousands of Russian Roubles)

19. Trade and Other Payables

As of December 31, 2004 and 2003, the Company's accounts payable and other current liabilities comprised the following:

	2004	2003
Trade accounts payable	**568,162**	500,359
Advances received from subscribers	**425,230**	406,424
Accounts payable for capital investments	**1,633,963**	399,929
Salaries and wages	**305,842**	178,409
Other accounts payable	**243,526**	262,753
Total	**3,176,723**	1,747,874

117,527 and 34,774 of trade payables are denominated in foreign currency, mainly US dollars and Euro, as of December 31, 2004 and 2003, respectively. 54,745 and 20,443 of other payables are denominated in foreign currency, mainly US dollars and Euro, as of December 31, 2004 and 2003, respectively.

20. Taxes Payable

As of December 31, 2004 and 2003, the Company had the following current taxes payable:

	2004	2003
VAT	**845,639**	623,884
Income tax	**323,614**	121,474
Property tax	**149,203**	92,561
Sales tax	**-**	41,401
Tax penalties and fines	**22,788**	23,938
Unified social tax	**14,216**	78,369
Individual income tax	**968**	35,077
Other taxes	**39,454**	7,833
Total	**1,395,882**	1,024,537

Included in value added tax payable is the amount of 580,528 (2003 - 412,513), which represents deferred value added tax that is only payable to the tax authorities when the underlying receivable is recovered or written off.

21. Pension Obligations

In addition to statutory pension benefits, the Company also contributes to post-employment benefit plans, which covers most of its employees. The Company participates in both defined contribution and defined benefit plans. In respect of the later, the Company applied the exemption permitted by IFRS 1 which allows an entity to recognize all cumulative actuarial gains and losses at the date of transition, even if the corridor approach is used for later actuarial gains and losses.

Defined contribution pension plans

For employees of certain branches, the Company provides post-employment benefits, which are classified as defined contribution pension plans. Non-government pension fund Telecom-Soyuz, which is related to the Company, maintains the plan.

During 2004 the Company made 62,858 of contributions under all of its pension plans (2003 – 132,244) that were expensed.

(in thousands of Russian Roubles)

21. Pension Obligations (continued)

Defined benefit pension plans

Most employees are covered by defined benefit pension plan. The defined benefit pension plan provides old age retirement pension and disability pension. The plans provide for payment of retirement benefits starting from statutory retirement age, which are 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 the relative pay of participants and their past service in the Company at retirement. The benefits do not vest until and are subject to the employee retiring from the Company on or after the above-mentioned ages.

Non-government pension fund Telecom-Soyuz, which is related to the Company, maintains the defined benefit pension plan. The Company makes contributions to the pension fund in the amount set forth in the agreement with the pension fund.

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

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

22. Revenues

By revenue types	2004	2003
Long distance telephone services - national	**9,165,242**	7,767,105
Long distance telephone services - international	**1,782,194**	1,504,012
Local telephone services	**7,906,535**	6,318,677
Installation and connecting fees	**2,037,886**	1,788,734
Documentary services	**89,383**	58,784
Mobile telecommunication services	**322,012**	412,292
Radio and TV broadcasting	**678,310**	533,293
Data transfer and telematic services	**388,046**	322,698
New services	**918,873**	576,686
Rent of telecommunication channels	**187,603**	146,438
Services for national telephone operators	**730,920**	687,919
Other telecommunication services	**813,837**	734,472
Other revenue	**1,026,363**	465,628
Total	**26,047,204**	21,316,738

The Company identifies revenue by the following major customer groups:

Customer groups	2004	2003
Residential customers	**13,704,967**	11,530,598
Corporate customers	**9,015,268**	7,104,023
Government customers	**1,804,773**	1,451,824
Tariff compensation from the state budget	**1,522,196**	1,230,293
Total	**26,047,204**	21,316,738

(in thousands of Russian Roubles)

23. Other Operating expenses

	2004	2003
Cost of goods sold	**(276,438)**	(78,431)
Rent of premises	**(370,544)**	(257,344)
Bank charges	**(269,858)**	(176,843)
Audit and consulting fees	**(144,439)**	(147,219)
Advertising expenses	**(134,669)**	(60,774)
Non-Commercial Partnership related expenses	**(296,677)**	(72,144)
Insurance	**(273,045)**	(231,278)
Mobilization activity	**(27,299)**	(17,433)
Fire and other security services	**(388,577)**	(314,337)
Transportation services	**(174,640)**	(110,405)
Education expenses	**(72,204)**	(67,078)
Payments to Gossvyaznadzor	**(71,718)**	(63,667)
Business travel expenses and representation costs	**(50,590)**	(44,887)
Post services	**(15,312)**	(21,433)
Network explotation, monitoring and maintenance	**(65,959)**	(49,699)
Upkeep of buildings and constructions	**(93,710)**	(48,597)
Agency commission	**(21,783)**	-
Charitable contributions	**(115,758)**	(117,120)
Fines and penalties	**(21,893)**	(26,365)
Other expenses	**(586,685)**	(369,048)
Total	**(3,471,798)**	**(2,274,102)**

24. Finance Cost, net

	2004	2003
Interest income	**62,639**	4,864
Interest expense	**(1,680,810)**	(932,162)
Finance charges payable under finance lease	**(414,816)**	(352,416)
Total	**(2,032,987)**	(1,279,714)

25. Gain (Loss) From Investments, net

	2004	2003
Gain (loss) on sale of share in the following associates (see Note 8):		
ZAO Bryanskiye Sotoviye Seti	42,913	-
ZAO Ryazanskaya Sotovaya Svyaz	40,665	-
ZAO Kalujskaya Sotovaya Svyaz	28,369	-
ZAO Tverskaya Sotovaya Svyaz	15,040	-
OOO Rating	36	-
OAO Gazenergobank	(1,305)	-
ZAO Sotovaya Svyaz Chernozemya (see Note 7)	151,365	-
Gain (loss) on sale of other financial assets	73	(3,313)
Loss on write-off of investments	(118)	-
Impairment provision (see Note 8)	(2,815)	(21,987)
Dividend income	20	203
Total	**274,243**	(25,097)

(in thousands of Russian Roubles)

26. Income Tax

The income tax charge for the years ended December 31, 2004 and 2003 comprised the following:

	2004	**2003**
Current income tax expense	(533,530)	(682,423)
Deferred income tax benefit	407,461	549,273
Total income tax expense	**(126,069)**	(133,150)

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

	2004	**2003**
Profit (loss) before income tax and minority interest	**(783,899)**	369,569
Statutory income tax rate	24%	24%
Theoretical income tax at statutory income tax rate	**188,136**	(88,697)
Expenditures allowable for income tax purpose	**(344,149)**	(275,473)
Carry-forward of tax losses and unused tax credits resulting in the decrease of current income tax expense	**-**	3,115
Other	**29,945**	227,905
Total income tax charge for the year at the effective rate of 16% (2003 - 36%)	**(126,069)**	(133,150)

The composition of deferred income tax assets and liabilities as of December 31, 2004 and 2003 was as follows:

	December 31, 2004	**December 31, 2003**
Deferred income tax assets		
Accounts payable and accrued expenses	77,767	159,151
Accounts receivable	130,970	50,452
Effect of investments valuation	72,124	7,459
Other	42,774	65,600
Gross deferred income tax assets	**323,635**	**282,662**
Deferred tax liabilities		
Property, plant and equipment	(411,025)	(779,786)
Leasing	(35,459)	(30,052)
Gross deferred income tax liabilities	**(446,484)**	**(809,838)**
Net deferred income tax liability	**(122,849)**	**(527,176)**

(in thousands of Russian Roubles)

26. Income Tax (continued)

The movement in net deferred income tax liability for the years ended December 31, 2004 and 2003 is presented below:

	2004	2003
Net deferred income tax liability at January 1	(527,176)	(1,075,621)
Deferred income tax benefit	407,461	549,273
Deferred income tax liability of acquired subsidiaries	(3,149)	-
Recovery of provision for deferred income tax asset	614	-
Deferred income tax related to unrealized gain on available-for-sale financial assets	(599)	(828)
Net deferred income tax liability at December 31	**(122,849)**	**(527,176)**

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 where there is a net consolidated tax loss. Therefore, deferred tax asset of one company is not offset against deferred tax liability of another company.

27. Earnings (Loss) per Share

Earnings per share is calculated by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the period (see Note 3).

The Company has no financial instruments convertible into ordinary shares; therefore, the diluted earnings per share equal basic earnings per share.

	2004	2003
Weighted average number of preference shares outstanding (thousands)	**1,578,007**	1,578,007
Weighted average number of ordinary shares outstanding (thousands)	**525,993**	525,993
Weighted average number of ordinary and preference shares outstanding (thousands)	**2,104,000**	2,104,000
Net profit (loss)	**(917,971)**	253,631
Earnings (loss) per share, (basic and diluted)	**(0.44)**	0.12

28. Dividends Declared and Proposed for Distribution

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 determined in accordance with Russian statutory accounting regulations. Dividends are accrued in the year they are declared and approved.

In accordance with Russian legislation, dividends may only be declared to the shareholders of the Company from net income as shown in the Company's Russian statutory unconsolidated financial statements. The Company had 397,711 net income for the year ended December 31, 2004 (2003 – 1,482,149).

(in thousands of Russian Roubles)

28. Dividends Declared and Proposed for Distribution (continued)

Dividends declared and approved during the year:

	2004	2003
Dividends on ordinary shares - 0.124867 Roubles per share (2003 – 0.096 Rubles per share)	**197,041**	151,570
Dividends on preference shares - 0.285662 Roubles per share (2003 – 0.206 Roubles per share)	**150,256**	108,430
Total	**347,297**	260,000

Dividends for 2004 approved by the annual shareholders' meeting in (see Note 34):

Dividends on ordinary shares, 0.063008 Roubles per share	99,427
Dividends on preference shares, 0.075611 Roubles per share	39,771
Total	139,198

29. Contingencies and Operating Risks

Operating Environment of the Company

The Russian economy while deemed to be of market status continues to display certain characteristics consistent with that of a market in transition. These characteristics include, but are not limited to, relatively high inflation and the existence of currency controls which cause the national currency to be illiquid outside of Russia. The stability of the Russian economy will be significantly impacted by the government's policies and actions with regards to supervisory, legal, and economic reforms.

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

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. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As of December 31, 2004 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. The Company intends to defend its position on these issues. As at December 31, 2004 the financial statements do not contain adjustments which may become necessary because of these uncertainties and positions assumed by the Company.

29. Contingencies and Operating Risks (continued)

In February 2005 tax authorities raised significant claim against one of the companies of Svyazinvest Group, as a result of tax examination of the company's operations for the years 2002-2003.

The Company does not expect similar claims since Dalsvyaz disagreed with the claim raised by tax authorities, brought the case before the court to contest tax authorities' claim, and estimated the probability of winning the claim as high. Additionally, the tax authorities carried out examination in other companies of the Svyazinvest Group for the same periods, and claims raised against them were insignificant.

Insurance Coverage

During 2004 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 Proceeding

The Russian legal system is characterized by (1) inconsistencies between and among laws, Presidential decrees, and Russian governmental, ministerial and local orders, decisions, and resolutions and other acts; (2) conflicting local, regional and federal rules and regulations; (3) the lack of judicial and administrative guidance on interpreting legislation; (4) the relative inexperience in legislation interpretation; and (5) a high degree of discretion on the part of governmental authorities. Management is unable to estimate what developments may occur in respect of the Russian legal system or the resulting effect of any such developments on the Company's financial condition or future results of operations. In the foreseeable future economic instability in the country may affect the Company's operations. The financial statements do not include any adjustment that may result from these uncertainties.

In July 2005 the Ministry of Finance of the Russian Federation filed a claim against the Company demanding immediate repayment of debts outstanding to Vnesheconombank as of July 12, 2005 in the amount of 457,428 (13,259 thousand euro).

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 or other claims outstanding, which could have a material effect on the result of operations or financial position of the Company and which have not been accrued or disclosed in these consolidated financial statements.

Licenses

Substantially all of the Company's revenues are derived from operations conducted pursuant to licenses granted by the Russian Government. These licenses expire in various years ranging from 2005 to 2012. The Company has renewed these licenses on a regular basis in the past, and believes that it will be able to renew licenses without additional cost in the normal course of business. Suspension or termination of the Company's main licenses or any failure to renew any or all of these main licenses could have a material adverse effect on the financial position and operations of the Company.

It is also known that the government of the Russian Federation plans to strengthen competition in telecommunication, for the reason of which it may issue additional licenses for local and international services to other operators. At the present time it is impossible to predict consequences, if any, of such changes on the Company's financial and economic activity.

(in thousands of Russian Roubles)

29. Contingencies and Operating Risks (continued)

Guarantees

As of December 31, 2004 the Company has guaranteed credit line facilities provided by Sberbank to OAO RTC-Leasing, a lessor of telecommunication equipment. The guarantees amounted to 2,809,960 (2003 – 1,491,181).

Asset retirement obligations

The Company may incur cost related to retirement of telecommunication lines and other assets and restoration of environment. Such costs may arise in connection with registration of title by landlords based on the Land Code of the Russian Federation, which came into force effective 2001. The management believes that occurrence of such events is unlikely. In addition, the timing and amount of such costs may not be identified and measured reliably. The liability would be initially recognized in the period in which sufficient information exists to estimate a range of potential settlement dates that is needed to employ a present value technique to estimate fair value.

30. Commitments

Finance leases

The Company entered into several finance leases with OAO RTC-Leasing. The equipment under these leases will be delivered in 2005. Cost of equipment acquired through these leases, inclusive of installation and other capitalized services approximated 532,688, exclusive of VAT.

Operating leases

The Company has entered into commercial leases of premises where it is not in the best interest of the Company to purchase these assets. These leases have an average life of between 5 and 10 years with renewal terms included in the contracts.

Future minimum rentals payable under non-cancellable operating leases as at December, 31 are as follows:

	2004	**2003**
Within one year	**160,579**	111,704
After one year but not more than five year	**65,869**	34,340
More than five years	**85,986**	29,019
Total	**312,434**	**175,063**

Capital commitments

As of December 31, 2004 the Company has commitments of 1,968,490 for capital investments into modernization and expansion of its network and for the purchases of intangible assets (Oracle, Amdocs).

31. Balances and Transactions with Related Parties

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

(in thousands of Russian Roubles)

31. Balances and Transactions with Related Parties (continued)

During 2004 and 2003 the Company entered into the following transactions with related parties:

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the related party relationships for those related parties with whom the Company entered into significant transactions or had significant balances outstanding at December 31, 2004 and 2003 are detailed below.

Related party		Sales to related parties	Purchases from related parties	Amounts owed by related parties	Amounts owed to related parties
OAO Svyazinvest	**2004**	-	**7,731**	-	**29,622**
	2003	-	24,909	-	30,362
OAO Rostelecom	**2004**	**1,196,280**	**3,188,927**	**-**	**191,544**
	2003	534,666	2,258,166	-	219,152
Center for Research of the Problems in Development of Telecommunications	**2004**	**-**	**322,917**	**52,608**	**-**
	2003	-	68,199	6,000	-
NPF Telecom-Soyuz	**2004**	**-**	**96,318**	**-**	**33,460**
	2003	-	128,303	-	-
Associates	**2004**	**22,217**	**3,102**	**3,281**	**-**
	2003	6,616	1,797	1,342	58
Other companies of Svyazinvest Group	**2004**	**16,842**	**238,384**	**96,534**	**44,417**
	2003	9,937	100,895	27,755	37,803
OAO RTComm.RU	**2004**	**315**	**70,081**	**-**	**2,241**
	2003	110	45,396	-	1,259
TOTAL	**2004**	**1,235,654**	**3,927,460**	**152,423**	**301,284**
	2003	551,329	2,627,665	35,097	288,634

OAO Svyazinves

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

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

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

31. Balances and Transactions with Related Parties (continued)

OAO Rostelecom

OAO Rostelecom, a majority owned subsidiary of OAO Svyazinvest, is the primary provider of domestic long distance and international telecommunications services in the Russian Federation. The annual expense associated with traffic carried by OAO Rostelecom and terminated outside of the Company's network is stated as interconnection charges. Further, OAO Rostelecom uses the Company's network to provide incoming long-distance and international traffic to its subscribers and partner operators.

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. Certain entities financed by the Government budget are users of the Company's network. These entities are generally charged lower tariffs as approved by the Ministry of Antimonopoly Policies and Entrepreneurship Support than those charged to other customers. In addition, the Government may by law require the Company to provide certain services to the Government in connection with national security and the detection of crime.

Government subscribers accounted for approximately 4.64% of trade accounts receivable as of December 31, 2004 (2003 - 6.92%). Amounts outstanding from government subscribers as of December 31, 2004, amounted to 72,985 (2003 – 58,535).

Associates

During 2004 and 2003 the Company also provided telecommunication and other services to the associates, including connection to public network, and rent of space for equipment and offices. The total effect of these transactions on the Company's financial position is insignificant.

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

Non-commercial partnership Center for Research of the Problems in Development of Telecommunications (hereinafter "the Partnership") is a subsidiary of OAO Svyazinvest. The Company has an agreement with the Partnership, under which it provides financing for mutually beneficial projects undertaken by the Partnership on behalf of the Company and other subsidiaries and associates of OAO Svyazinvest. Payments to the Partnership included in other operating expenses in the accompanying consolidated statement of operations for the year ended December 31, 2004 amounted to 296,677 (2003 – 72,144).

NPF Telecom-Soyuz

The Company has a number of pension agreements with NPF "Telecom-Soyuz" which is a party related to OAO Svyazinvest, which holds the majority in the Board of Directors of NPF "Telecom-Soyuz" ("the Fund"), because Svyazinvest Group is the main contributor of this Fund. Payments to this pension fund in 2004 amounted to 62,858 (2003 - 132,244). For 2005 the amount of payments to the Fund is set at 283,920 (see Note 21).

ZAO RTC-Invest

In 2004 the Company issued Promissory Notes to ZAO RTC-Invest, an associate of OAO Svyazinvest, for amount of 1,175,000 (2003 – 270,000). The Promissory Notes are with a discount. The discount amounted to 148,804 (2003 – 35,487).

31. Balances and Transactions with Related Parties (continued)

Compensation to key management personnel

Key management personnel comprise members of Management Board and Board of Directors of the Company, totaling 22 persons as at December, 31 2004 an 2003. Total compensation to key management personnel included in the statement of operations line "Wages, salaries, other benefits and payroll taxes" amounted to 51,244 and 38,532 for the years ended December, 31 2004 and 2003, respectively.

Compensation to key management personnel consists of contractual salary, performance bonus depending on operating results and payments for non-government pension benefits.

32. Financial risk management objectives and policies

Fair value

Fair value of a financial instrument is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction (except for forced sale or liquidation) Market prices are considered to be the best evidence of faire value.

Carrying value of monetary assets and liabilities approximate their fair value. Balance sheet items denominated in foreign currencies have been translated into Rubles using the exchange rate, prevailing at the reporting date.

Carrying value of cash and cash equivalents approximate their respective fair value due to their short-term nature and negligible credit losses.

Credit risk

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

Financial assets, which potentially subject Company entities 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 significance of the client base and regular monitoring procedures over customers' and other debtors' ability to pay debts. Part of accounts receivable is represented by state and other non-commercial organizations. Recovery of this debt is influenced by political and economic factors, however, management believes that as of December 31, 2004 there is no significant risk of loss to the Company beyond the provision already recorded.

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

Foreign exchange risk

Foreign exchange risk is the risk that fluctuations in exchange rates will adversely affect items in the Company's statement of operations, balance sheet and/or cash flows. Foreign currency denominated liabilities (see Notes 17, 18 and 19) give rise to foreign exchange exposure.

(in thousands of Russian Roubles)

32. Financial risk management objectives and policies (continued)

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

For the period from January 1, 2004 to December 31, 2004 exchange rate of the Russian Rouble to US Dollar increased by approximately 13% and exchange rate of the Russian Ruble to Euro decreased by approximately 14%. Taking into account instability of economic situation in Russia, there is a probability of significant fall in exchange rate of the Russian Rouble in the future. Possible fall in the exchange rate of the Russian Rouble will lead to increase in the amount of the Company's borrowings, as well as will cause difficulties in attraction of funds including for refinancing of existing debt.

Interest rate risk

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

33. Financial Instruments

The following table presents as of December 31, 2004 and 2003 the carrying amount by maturity of the Company's financial instruments that are exposed to interest rate risk:

As of December 31, 2003:	**Within 1 year**	**1-5 years**	**More than 5 years**	**Total**
Fixed rate				
Short-term borrowings	3,314,101	-	-	3,314,101
Long-term borrowings	1,016,226	6,616,884	65,047	7,698,157
Finance lease obligations	512,769	1,167,947	-	1,680,716
Floating rate				
Short-term borrowings	105,548	-	-	105,548
Long-term borrowings	135,500	231,314	-	366,814

As of December 31, 2004:	**Within 1 year**	**1-5 years**	**More than 5 years**	**Total**
Fixed rate				
Short-term borrowings	4,489,131	-	-	4,489,131
Long-term borrowings	2,780,880	12,773,970	101,130	15,655,980
Finance lease obligations	672,491	1,775,171	-	2,447,662
Floating rate				
Short-term borrowings	83,515	-	-	83,515
Long-term borrowings	119,192	97,548	-	216,740

Interest on financial instruments classified as floating rate is revised at intervals less than one year.

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

The Company has no significant interest-bearing assets.

34. Events After The Balance Sheet Date

Purchase of additional share in ZAO CenterTelecomService of Moscow Region

The Company acquired 24% share (24,000 ordinary shares) in ZAO CenterTelecomService of Moscow Region for 7,961. Records in shareholder registers attesting to the transfer of title to these securities were made in January-February 2005. As a result of this transaction the Company increased its share to 100% of share capital.

Purchase of share in OAO Svyazintek

The Company acquired 18% share (2,700 ordinary shares) in OAO Svyazintek for 27. Records in shareholder registers attesting to the transfer of title to these securities were made on April 14, 2005.

Purchase of additional share in OAO Aerocom

The Company acquired 0.38% share (8,000 ordinary shares) in OAO Aerocom, for 991. Records in shareholder registers attesting to the transfer of title to these securities were made in May 2005. As a result of this transaction the Company increased its share to 100% of share capital.

Consolidation of OAO Aerocom and ZAO CenterTelecomService of Moscow Region into OAO RTS

In June 2005 the Company's Board of Directors approved the reorganization of OAO Aerocom and ZAO CenterTelecomService of Moscow Region and of OAO RTS adhesion contract with OAO Aerocom and ZAO CenterTelecomService of Moscow Region with OAO RTS.

Loan agreements

In January 2005 the Company entered into loan agreements with OAO Vneshtorgbank for the total amount of 7,784 thousand US dollars. The loans mature in January 2008. The Company pays interest on the loans to the bank at the rate of 13% per annum.

In February 2005 the Company entered into loan agreement with ZAO AKB Promsvyazbank for 600,000. The loan matures in February 2010. The Company pays interest on the loan to the bank at the rate of 14.5% per annum. The loan is guaranteed by collateral of telecommunications equipment amounted to 1,038,119.

In March 2005 the Company entered into an overdraft agreement with ZAO AKB Promsvyazbank for 150,000. The overdraft will be redeemed in September 2005. The Company pays interest on the overdraft to the bank at the rate of 12.5% per annum.

In March 2005 the Company entered into a loan agreement with OAO Sberbank for 1,020,980. The loan matures in September 2006. The Company pays interest on the loan to the bank at the rate of 12% per annum. The loan is guaranteed by collateral of telecommunications equipment amounted to 592,955.

In April 2005 the Company entered into a loan agreement with OAO Alfa-Bank for 682,303. The loan matures in April 2008. The Company pays interest on the loan to the bank at the rate of 15.5% per annum. The loan is guaranteed by collateral of telecommunications equipment amounted to 1,165,637.

34. Events After The Balance Sheet Date (continued)

In February-May 2005 the Company issued Promissory notes to OOO Brokerskaya Kontora Severo-Zapadniy Investitsionny Center for the total amount of 1,653,000. The notes mature in 2006.

In May 2005 the Company entered into loan agreement with OAO National bank Trust for the total amount of 1,500,000. The loan matures in May 2006. The Company pays interest on the loan to the bank at the rate of 14% per annum.

In June 2005 the Company entered into loan agreement with OAO Sberbank for 660,000. The loan matures in December 2006. The Company pays interest on the loan to the bank at the rate 12% per annum. The loan is guaranteed by collateral of telecommunications equipment amounted to 538,061.

Retirement of bonds 02 series

In April 2005 the Company repaid its bonds of 02 series in the amount of 600,000.

Agreement with Non-commercial partnership

In June 2005 the Company's Board of Directors has approves membership's fees to Non-Commercial Partnership Center for Research of the Problems in Development of Telecommunications in the amount of 214,801.

Change in share capital

On January 14, 2005 the Company increased the par value of its preferred and ordinary shares from 0.3 Roubles to 3 Roubles per share.

Dividends

On June 30, 2005, the general meeting of the Company's shareholders approved dividends for 2004 in the amount of 0.076 Roubles per preference share and 0.063 Roubles per ordinary share. Total dividends declared amounted to 39,771 and 99,427 for preference and ordinary shares, respectively. Dividends for the year ended December 31, 2004 are payable during 2005 and shall be carried in the financial statements for the year ended December 31, 2005 (see also Note 28 "Dividends Declared and Proposed for Distribution").

Telecommunication reform

In 2005 within the framework of government efforts to restructure the telecommunication industry (liberalization of the telecommunication market) the Company will be providing domestic and international long-distance communication services on the basis of restructured relations with OAO Rostelecom. These relations will be regulated by an agreement to assist in provision of domestic and international long-distance communication services and an agreement on interconnection to telecommunications lines.

Under the assistance agreement, the Company will provide on a compensatory basis an access to domestic and international long-distance communication services of OAO Rostelecom, keep records and rating of provided services and receive payments for them, and also claim accounts receivable. The Company's revenue under the assistance agreement will be formed by fees paid by OAO Rostelecom.

Under the interconnection agreement, the Company will provide to OAO Rostelecom traffic transmission services (call initiation and completion, traffic transit to/from interconnected operator networks).

34. Events After The Balance Sheet Date (continued)

The Company expects that the modified interaction framework will result in a decrease in both revenue and expenses, but the profit will remain at the previous level.

Unified social tax

The Federal Law No. 70-FZ dated July 20, 2004 amended article 24 of the Tax Code of the Russian Federation. It stipulates reduction of unified social tax rate effective January 1, 2005.

Reduction of the unified social tax rate from 35.6% to 26% will lead to decrease in the amount of unified social tax, decrease in operating expenses, and increase in net profit of the Company.

The Company's management is not able to estimate the effect of the change in the unified social tax rate effective January 1, 2005 on its net profit for 2005.