OAO ROSTELECOM

CONSOLIDATED FINANCIAL STATEMENTS
PREPARED IN ACCORDANCE WITH
INTERNATIONAL FINANCIAL REPORTING STANDARDS

FOR THE YEAR ENDED DECEMBER 31, 2005

INDEX

STATEMENT OF DIRECTORS' RESPONSIBILITIES

To the Shareholders of OAO Rostelecom

1. International convention requires that management prepare consolidated financial statements which present fairly, in all material respects, the state of affairs of the Group at the end of each financial period and of the results and cash flows for each period. Management are responsible for ensuring that all Group entities keep accounting records which disclose with reasonable accuracy the financial position of each entity and which enable them to ensure that the consolidated financial statements comply with International Financial Reporting Standards and that their statutory accounting reports comply with Russian laws and regulations. They also have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

2. Management considers that, in preparing the consolidated financial statements set out on pages 5 to 71, the Group has used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgments and estimates, and that appropriate International Financial Reporting Standards have been followed.

3. The consolidated financial statements, which are based on the statutory accounting reports adjusted to comply with International Financial Reporting Standards, are hereby approved on behalf of the Board of Directors.

For and on behalf of the Board of Directors:

D.E. Erokhin,
General Director

OAO Rostelecom
1st Tverskaya-Yamskaya, 14,
Moscow
Russian Federation

June 23, 2006

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of OAO Rostelecom

We have audited the consolidated balance sheets of OAO Rostelecom, an open joint stock company, and subsidiaries (hereinafter referred to as the "Group") as of December 31, 2005, 2004 and 2003, and the related consolidated statements of income, cash flows and changes in shareholders' equity for each of the three years in the period ended December 31, 2005. These financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Group's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Group as of December 31, 2005, 2004 and 2003, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2005 in conformity with International Financial Reporting Standards as published by the International Accounting Standards Board.

As discussed in Note 5 to the financial statements, upon application of the revised IAS No. 39 in 2005, the Group retrospectively changed its method of accounting for investments for all periods presented.

International Financial Reporting Standards vary in certain significant respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of such differences is presented in Note 35 to the consolidated financial statements.

As described in Note 35 to the consolidated financial statements, this Note was restated to adjust the Group's accounting for the impairment of property, plant and equipment under accounting principles generally accepted in the United States of America.

Moscow, Russia
June 23, 2006

(In millions of Russian Rubles, refer to Note 4)

	Notes	December 31, 2005	December 31, 2004 (as restated, see Note 5)	December 31, 2003 (as restated, see Note 5)
ASSETS				
Non-current assets				
Property, plant and equipment	7	40,628	45,987	49,585
Goodwill	7	-	9	17
Investments in associates	9	331	2,511	2,381
Long-term financial investments	10	3,343	264	126
Other non-current assets		13	17	26
Total non-current assets		**44,315**	**48,788**	**52,135**
Current assets				
Inventory		761	614	548
Accounts receivable	11	5,232	5,375	6,648
Prepaid income tax		373	238	433
Short-term investments	12	12,238	8,150	2,755
Cash and cash equivalents	13	2,398	1,255	2,529
Total current assets		**21,002**	**15,632**	**12,913**
Total assets		**65,317**	**64,420**	**65,048**
EQUITY AND LIABILITIES				
Equity attributable to equity holders of the parent				
Share capital	14	100	100	100
Retained earnings including other reserves		49,597	50,738	47,870
Total equity attributable to equity holders of the parent		**49,697**	**50,838**	**47,970**
Minority interest	16	-	-	191
Total equity		**49,697**	**50,838**	**48,161**
Non-current liabilities				
Interest bearing loans – net of current portion	18	3,232	777	1,641
Non-current portion of finance lease payable	16	369	-	-
Non-current accounts payable	15	378	340	487
Non-current portion of vendor financing payable	17	-	353	-
Deferred tax liability	19	4,171	5,954	7,482
Total non-current liabilities		**8,150**	**7,424**	**9,610**
Current liabilities				
Accounts payable, provisions and accrued expenses	15	4,056	3,191	3,567
Finance lease payable	16	52	-	-
Taxes payable		830	1,154	1,778
Vendor financing payable	17	1,677	706	-
Current portion of interest bearing loans	18	851	1,107	1,932
Short-term borrowings		4	-	-
Total current liabilities		**7,470**	**6,158**	**7,277**
Total liabilities		**15,620**	**13,582**	**16,887**
Total equity and liabilities		**65,317**	**64,420**	**65,048**

The notes on pages 9 to 71 are an integral part of these consolidated financial statements.

(In millions of Russian Rubles unless otherwise stated, refer to Note 4)

	Notes	2005	2004 (as restated, see Note 5)	2003 (as restated, see Note 5)
		Year ended December 31,		
Revenue				
Local operators		25,227	22,648	15,792
Subscribers		8,955	8,740	9,319
Foreign operators		4,706	4,560	4,483
Other		2,067	1,370	1,673
Total revenue	20	**40,955**	**37,318**	**31,267**
Operating expenses				
Wages, salaries, other benefits and payroll taxes		(6,242)	(5,109)	(3,946)
Depreciation	7	(7,136)	(7,498)	(8,252)
Impairment of property, plant and equipment and goodwill	7	(4,970)	-	-
Charges by network operators – international		(7,059)	(6,484)	(5,913)
Charges by network operators – national		(8,741)	(7,883)	(4,053)
Administration and other costs	22	(3,877)	(3,353)	(4,060)
Taxes other than on income		(492)	(587)	(507)
Repairs and maintenance		(822)	(813)	(800)
Bad debt recovery/(expense)	11	140	(369)	(337)
Loss on sale of property, plant and equipment		(1,356)	(217)	(1,214)
Total operating expenses		**(40,555)**	**(32,313)**	**(29,082)**
Operating profit		**400**	**5,005**	**2,185**
Income/(loss) from associates and joint ventures	9	169	(25)	115
Interest expense		(77)	(13)	(202)
Interest income		886	478	402
Income from sale of investments		408	-	25
Other non-operating income, net	24	55	72	1,150
Foreign exchange (loss)/gain, net		(168)	102	72
Profit before tax		**1,673**	**5,619**	**3,747**
Current tax charge		(2,829)	(2,892)	(2,002)
Deferred tax benefit		2,134	1,539	1,780
Income tax expense	25	**(695)**	**(1,353)**	**(222)**
Profit for the period from continuing operations		**978**	**4,266**	**3,525**
Net loss from discontinued operations, net of tax, including impairment of property, plant and equipment of 419	23	-	-	(2,459)
Profit for the period		**978**	**4,266**	**1,066**
Attributable to:				
Equity holders of the parent		978	4,266	346
Minority interest – continuing operations		-	-	70
Minority interest – discontinued operations		-	-	650
Minority interest - total		-	-	720
		Rubles	**Rubles**	**Rubles**
Earnings per share attributable to equity holders of the parent – basic and diluted	27	**1.01**	**4.39**	**1.10**
Earnings per share attributable to equity holders of the parent – continuing operations	27	**1.01**	**4.39**	**3.63**
Loss per share attributable to equity holders of the parent– discontinued operations	27	**-**	**-**	**(2.53)**

The notes on pages 9 to 71 are an integral part of these consolidated financial statements.

(In millions of Russian Rubles, refer to Note 4)

	Note	Year ended December 31, 2005	2004 (as restated, see Note 5)	2003 (as restated, see Note 5)
Cash flows from operating activities				
Profit before income tax		1,673	5,619	3,747
Adjustments to reconcile net income before tax and discontinued operations to cash generated from operating activities:				
Net loss from discontinued operations before tax	23	-	-	(2,116)
Depreciation	7	7,136	7,498	8,276
Impairment losses	7, 23	4,970	-	551
Bad debt (recovery) /expense	11	(140)	369	339
(Income) /loss from associates and joint ventures	9	(169)	25	(203)
Loss on sale of property, plant and equipment		1,356	217	1,214
(Income) /loss from sale of investments		(408)	-	98
Net interest and other non-operating income		(864)	(537)	(422)
Loss from discontinued operations	23	-	-	804
Other non-monetary expense /(income)		-	4	(42)
Foreign exchange loss /(gain), net		168	(102)	(13)
Changes in net working capital:				
(Increase) /decrease in accounts receivable		(421)	4,581	(2,540)
Increase in lease receivables		-	-	(3,685)
Decrease /(increase) in inventories		44	(81)	(46)
Increase /(decrease) in payables and accruals		49	(7,132)	(1,335)
Cash generated from operations		**13,394**	**10,461**	**4,627**
Interest paid		(193)	(94)	(956)
Interest received		766	202	577
Income tax paid		(3,024)	(2,815)	(2,173)
Net cash provided by operating activities		**10,943**	**7,754**	**2,075**
Cash flows from investing activities				
Purchase of property, plant and equipment		(7,788)	(4,502)	(3,328)
Proceeds from sale of property, plant and equipment		183	289	21
Purchase of subsidiaries, net of cash acquired		-	-	(642)
Purchase of available-for-sale investments, net		(59)	-	-
Purchase of financial assets, other than available-for-sale investments		(32,174)	(13,550)	(8,415)
Proceeds from sale of available-for-sale investments, net of direct costs		699	-	1,453
Proceeds from sale of investment other than available-for-sale, net of direct costs		28,824	12,156	7,687
Dividends received from associates		99	74	13
Repayment of lease obligations	23	(33)	(520)	(3,520)
Cash acquired as a result of obtaining control over GlobalTel		140	-	-
Cash (disposed of)/received on discontinuance of segments, net of cash disposed of		-	-	91
Net cash used in investing activities		**(10,109)**	**(6,053)**	**(6,640)**
Cash flows from financing activities				
Drawdown of interest bearing loans		3,082	343	9,939
Repayment of interest bearing loans		(1,137)	(1,951)	(6,471)
Proceeds from issuance of promissory notes		-	-	2,208
Redemption of promissory notes		-		(1,455)
Dividends paid		(1,637)	(1,359)	(706)
Dividends paid to minority shareholders of a subsidiary		-	-	(29)
Net cash provided by/(used in) financing activities		**308**	**(2,967)**	**3,486**
Effect of exchange rate changes on cash and cash equivalents		**1**	**(8)**	**(34)**
Net increase/(decrease) in cash and cash equivalents		**1,143**	**(1,274)**	**(1,113)**
Cash and cash equivalents at beginning of year		**1,255**	**2,529**	**3,642**
Cash and cash equivalents at the end of year		**2,398**	**1,255**	**2,529**
Non-monetary transactions:				
Non-cash additions to property, plant and equipment		412	-	316

The notes on pages 9 to 71 are an integral part of these consolidated financial statements.

((In millions of Russian Rubles unless otherwise stated, refer to Note 4)

		Attributable to equity holders of the parent				Minority interest	Total equity
	Note	Share capital	Unrealized gain on available-for-sale investments	Retained earnings	Total		
Balance at December 31, 2002		**100**	**311**	**47,867**	**48,278**	**2,825**	**51,103**
Available-for-sale investments							
Valuation gain on available-for-sale investments, net of tax		-	133	-	133	-	133
Transferred to profit on sale		-	(81)	-	(81)	-	(81)
Total income and expense for the period recognized directly in equity		**-**	**52**	**-**	**52**	**-**	**52**
Profit for the period (as restated)		-	-	346	346	720	1,066
Total income and expense		**-**	**52**	**346**	**398**	**720**	**1,118**
Minority interest in disposed subsidiaries		-	-	-	-	(3,322)	(3,322)
Purchase of minority interest			-	-	-	(3)	(3)
Dividends		-	-	(706)	(706)	(29)	(735)
Balance at December 31, 2003		**100**	**363**	**47,507**	**47,970**	**191**	**48,161**
Available-for-sale investments							
Valuation gain on available-for-sale investments, net of tax		-	32	-	32	-	32
Total income and expense for the period recognized directly in equity		**-**	**32**	**-**	**32**	**-**	**32**
Profit for the period (as restated)			-	4,266	4,266	-	4,266
Total income and expense			**32**	**4,266**	**4,298**	**-**	**4,298**
Minority interest in disposed subsidiaries			-	-	-	(191)	(191)
Dividends	14	-	-	(1,430)	(1,430)	-	(1,430)
Balance at December 31, 2004		**100**	**395**	**50,343**	**50,838**	**-**	**50,838**
						-	
Effect of obtaining control over GlobalTel	6	-	-	(826)	(826)	-	(826)
Available-for-sale investments							
Valuation gain on available-for-sale investments, net of tax		-	736	-	736	-	736
Transferred to profit on sale		-	(243)	-	(243)	-	(243)
Total income and expense for the period recognized directly in equity		**-**	**493**	**-**	**493**	**-**	**493**
Profit for the period		-	-	978	978	-	978
Total income and expense		**-**	**493**	**978**	**1,471**	**-**	**1,471**
Dividends	14	-	-	(1,786)	(1,786)	-	(1,786)
Balance at December 31, 2005		**100**	**888**	**48,709**	**49,697**	**-**	**49,697**

The notes on pages 9 to 71 are an integral part of these consolidated financial statements.

1. REPORTING ENTITY

These consolidated financial statements are presented by OAO “Rostelecom” (“Rostelecom” or the “Company”), and its subsidiaries (together the “Group”), which are incorporated in the Russian Federation (“Russia”). The principal activity of the Group is the provision of intercity and international telecommunications services to the Government, businesses and individuals of Russia. The Group operates the main intercity network and the international telecommunications gateways of the Russian Federation, carrying traffic that originates in other national and international operators’ networks to other national and international operators for termination.

The Company’s headquarters are located in Moscow at 1st Tverskaya-Yamskaya Street, 14.

These consolidated financial statements incorporate the results of operations of the Company and its subsidiaries, as detailed in Note 8.

Rostelecom was established as an open joint stock company on September 23, 1993 in accordance with the Directive of the State Committee on the Management of State Property of Russia No. 1507-r, dated August 27, 1993. As of December 31, 2005, the Government of the Russian Federation controlled indirectly 50.67% of the voting share capital of the Company, by virtue of its 75% less one share direct holding in OAO Svyazinvest (“Svyazinvest”), the parent company of Rostelecom.

2. BASIS OF PRESENTATION

These consolidated financial statements have been prepared in accordance with and comply with International Financial Reporting Standards (“IFRS”), as published by the International Accounting Standards Board (“IASB”).

The Group maintains its accounting records and prepares its statutory accounting reports in accordance with Russian accounting legislation and instructions in Russian Rubles (Rbl). These consolidated financial statements are based on the underlying accounting records, appropriately adjusted and reclassified for fair presentation in accordance with the standards and interpretations prescribed by the IASB.

The consolidated financial statements have been prepared using the historical cost convention, restated for the effects of inflation up to December 31, 2002 (refer to Note 4), and modified by the initial valuation of property, plant and equipment as further disclosed in Note 5 to these consolidated financial statements, and measurement of available-for-sale investments at fair value (refer to Note 5). The functional currency of the Group and the reporting currency for these consolidated financial statements is the Russian Ruble (Rbl).

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant estimates relate to the recoverability and depreciable lives of property, plant and equipment, fair values of assets and liabilities acquired in business combinations, post employment benefits, allowance for doubtful accounts, and deferred taxation. Actual results could differ from these estimates.

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

Impairment of Property, Plant and Equipment

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the assets' recoverable amount. An asset's recoverable amount is 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 group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. 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 assessment of the time value of money and the risks specific to the assets. In 2005, the Group recognized an impairment loss of 4,970 (refer to Note 7).

The determination of impairment of property, plant and equipment involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment is based on a large number of factors, such as changes in current competitive conditions, expectations of growth in the telecommunication industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate an impairment exists. The recoverable amount and the fair values are typically determined using a discounted cash flow method which incorporates reasonable market participant assumptions. The identification of impairment indicators, the estimation of future cash flows and the determination of fair values for assets (or group of assets) requires management to make significant judgments concerning the identification and validation of impairment indicators, expected cash flows, applicable discount rates, useful lives and residual values. Specifically, the estimation of cash flows underlying the value in use of the Group's property, plant and equipment considers the impact of the new rules and regulations of the regulatory reform and restructuring of the national telecommunication sector as discussed in detail in Note 30(d). As part of this reform, a new price-setting and settlements mechanism among the telecom operators was introduced. Some elements of this mechanism remain unclear and may be subject to additional clarification from the regulators. If this mechanism is changed, this may significantly affect the management's estimates of the future cash flows and operating results and, consequently, the amount of potential impairment of the Group's property, plant and equipment.

The determination of the recoverable amount of a cash-generating unit involves the use of estimates by management. Methods used to determine the value in use include discounted cash flow-based methods and methods that use quoted stock market prices as a basis. These estimates, including the methodologies used, can have a material impact on the fair value and ultimately the amount of any property, plant and equipment impairment.

Useful Lives of Items of Property, Plant and Equipment

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end and, if expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors".

Fair Values of Assets and Liabilities Acquired in Business Combinations

The Group is required to recognize separately, at the acquisition date, the identifiable assets, liabilities and contingent liabilities acquired or assumed in the business combination at their fair values, which involves estimates. Such estimates are based on valuation techniques, which require considerable judgment in forecasting future cash flows and developing other assumptions.

Site Restoration Provisions

The Group reviews site restoration provisions at each balance sheet date and adjusts them to reflect the current best estimate in accordance with IFRIC 1 "Changes in Existing Decommissioning, Restoration and Similar Liabilities". The amount recognized as a provision is the best estimate of the expenditure required to settle the present obligation at the balance sheet date. The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Considerable judgment is required in forecasting future site restoration costs. Future events that may affect the amount required to settle an obligation are reflected in the amount of a provision where there is sufficient objective evidence that they will occur.

Post-Employment Benefits

The Group uses actuarial valuation method for measurement of the present value of defined post-employment benefit obligations and related current service cost (refer to Note 26). This involves the use of demographic assumptions about the future characteristics of current and former employees who are eligible for benefits (mortality, both during and after employment, rates of employee turnover, etc.) as well as financial assumptions (discount rate, future salary and benefit levels, etc.).

Allowances

The Group makes allowances for doubtful accounts receivable. Significant judgment is used to estimate doubtful accounts. In estimating doubtful accounts historical and anticipated customer performance are considered. Changes in the economy, industry, or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the consolidated financial statements. As of December 31, 2005, 2004 and 2003, allowances for doubtful accounts have been created in the amount of 1,371, 2,284 and 2,689, respectively (refer to Note 11).

3. OPERATING ENVIRONMENT OF THE GROUP

General

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. As a result, there are significant uncertainties that may affect future operations, the recoverability of the Group's assets, and the ability of the Group to maintain or pay its debts as they mature. These consolidated financial statements do not include any adjustments that may result from the future clarification of these uncertainties. Such adjustments, if any, will be reported in the Group's consolidated financial statements in the period when they become known and can be reasonably estimated.

Regulatory reform in telecommunications industry

In 2005 new regulations in the national telecommunication sector were put in force. The new regulations allowed telecommunication operators to apply for long-distance telecommunication licenses. As a result, effective January 1, 2006, the Group's status as a monopoly supplier of long distance and international communication services has been changed (refer to Note 30).

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Currency exchange and control

Foreign currencies, in particular the US Dollar, play a significant role in the underlying economics of many business transactions in Russia. Following the 1998 economic crisis, the Ruble's value fell significantly against the US Dollar, falling from a pre-crisis rate of approximately 6 Rubles to 1 US Dollar, to 27 Rubles to 1 US Dollar by the end of 1999. During 2000 - 2005, the Ruble's value fluctuated between 26.9 and 31.8 to 1 US Dollar. As of June 23, 2006, the exchange rate was 26.97 Rubles to 1 US Dollar.

The following table summarizes the exchange rate of the Ruble to 1 US Dollar as of December 31, 2005, 2004 and 2003.

As of December 31,	Exchange Rate
2005	28.78
2004	27.75
2003	29.45

Source: Central Bank of Russia

The Central Bank of Russia has established strict currency control regulations designed to promote the commercial utilization of the Ruble. Such regulations place restrictions on the conversion of Rubles into foreign currencies and establish requirements for partial conversion of foreign currency sales to Rubles.

Inflation

The Russian economy has been characterized by relatively high rates of inflation. The following table summarizes the annual rate of inflation for the past three years:

For the year ended December 31,	Annual inflation
2005	10.9%
2004	11.7%
2003	12.0%

Source: Federal Service of Public Statistics

Taxation

Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include value added tax, corporate income tax (profits tax) and payroll (social) taxes, together with others. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies. Therefore, the government's implementation of these regulations is often inconsistent or nonexistent. Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, who are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia substantially more significant than typically found in countries with more developed tax systems.

Refer to Note 30 for description of possible tax contingencies.

4. ACCOUNTING FOR THE EFFECTS OF INFLATION

Prior to December 31, 2002, the Russian Federation met the definition of a hyperinflationary economy as defined by International Accounting Standard ("IAS") No. 29, "Financial Reporting in Hyperinflationary Economies".

IAS No. 29 requires that financial statements prepared on a historical cost basis be adjusted to take into account the effects of inflation, for entities reporting in hyperinflationary economies. The Group has utilized the general price index reported by the Federal Service of Public Statistics in the application of IAS No. 29.

Effective January 1, 2003, the economy of the Russian Federation ceased to meet the criteria of hyperinflationary economy. Accordingly, beginning January 1, 2003, the Company ceased to apply IAS No. 29 on a prospective basis.

As a result of this change, the carrying amounts of non-monetary assets expressed in the Russian Rubles current at December 31, 2002 formed the carrying basis for the respective assets at January 1, 2003.

5. PRINCIPAL ACCOUNTING POLICIES

Set out below are the principal accounting policies used to prepare these consolidated financial statements:

Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial year except that the Group has adopted those new/revised standards mandatory for financial years beginning on or after 1 January 2005. The changes in accounting policies result from adoption of the following new or revised standards:

- IAS No. 1, "Presentation of Financial Statements",
- IAS No. 2, "Inventories",
- IAS No. 8, "Accounting Policies, Changes in Accounting Estimates and Errors",
- IAS No. 10, "Events after the Balance Sheet Date",
- IAS No. 16, "Property, Plant and Equipment",
- IAS No. 17, "Leases",
- IAS No. 21, "The Effects of Changes in Foreign Exchange Rates",
- IAS No. 24, "Related Party Disclosures",
- IAS No. 27, "Consolidated Financial Statements and Accounting for Investments in Subsidiaries",
- IAS No. 28, "Investments in Associates",
- IAS No. 31, "Interests in Joint Ventures",
- IAS No. 32, "Financial Instruments: Disclosure and Presentation (revised 2003)",
- IAS No. 39, "Financial Instruments: Recognition and Measurement",
- IAS No. 40, "Investment Property",
- IFRS No.2, "Share-based Payment",
- IFRS No.3 "Business Combinations",
- IFRS No.4 "Insurance Contracts".

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Except for the matters discussed below, the adoption of the above standards did not have a material impact on the Group's results of operations, financial position, cash flows, disclosures and overall presentation of financial statements.

Upon application of the revised IAS No.1 and IAS No.27, the Group changed the format of presentation of financial statements and related disclosures, where needed. Minority interests in net assets of the Group's subsidiaries are presented within equity, separately from parent shareholders' equity. Previously, minority interests were presented separately from liabilities and equity in the Group's consolidated balance sheets.

Upon application of the revised IAS No. 39, the Group reconsidered classification of its investments in bills of exchange in line with the provisions of this revised Standard. Accordingly, the Group re-represented bills of exchange as loans and receivables in the consolidated balance sheet as of December 31, 2004 and 2003. Reclassification of bills of exchange did not have a material impact on the Group's results of operations, financial position and cash flows for all periods presented.

Upon application of revised IAS No.39, the Group recognizes holding gains and loses resulting from changes in fair value of available-for-sale investments as a separate component of equity until the investment is derecognized or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the determination of net income. Previously, gains and losses resulting from changes in fair value of available-for-sale investments were included in determination of net income.

As required by transition provisions of IAS No.39, the Group applied this Standard retrospectively. The opening balance of retained earnings for the earliest prior period presented and all other comparative amounts were adjusted as if this Standard had always been in use.

The summarized effect of adoption of IAS No.1 and IAS No.39 on the corresponding figures is as follows:

	As previously reported	Effects of application of IAS No.1	Effects of retrospective application of IAS No.39	As restated
Consolidated statement of income for the year ended 31 December 2003				
Other non-operating income, net	1,219	-	(69)	1,150
Deferred tax benefit	1,763	-	17	1,780
Profit for the period from continuing operations	3,507	70	(52)	3,525
Net loss from discontinued operations, net of tax	(3,109)	650	-	(2,459)
Profit for the period	398	720	(52)	1,066
Earnings per share – basic and diluted	0.41	0.74	(0.05)	1.10
Earnings per share – continuing operations	3.61	0.07	(0.05)	3.63
Earnings per share – discontinued operations	(3.20)	0.67	-	(2.53)

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

	As previously reported	Effects of application of IAS No.1	Effects of retrospective application of IAS No.39	As restated
Consolidated statement of income for the year ended 31 December 2004				
Other non-operating income, net	115	-	(43)	72
Deferred tax benefit	1,528	-	11	1,539
Profit for the period from continuing operations	4,298	-	(32)	4,266
Profit for the period	4,298	-	(32)	4,266
Earnings per share – basic and diluted	4.42	-	(0.03)	4.39
Earnings per share – continuing operations	4.42	-	(0.03)	4.39
Consolidated statement of changes in shareholders' equity for the year ended 31 December 2003				
Profit for the period attributable to equity holders of the parent	398	-	(52)	346
Valuation gain on available-for-sale investments, net of tax	-	-	133	133
Transferred to profit on sale	-	-	(81)	(81)
Minority interest in disposed subsidiaries	-	(3,322)	-	(3,322)
Purchase of minority interest	-	(3)	-	(3)
Dividends	(706)	(29)	-	(735)
Consolidated statement of changes in shareholders' equity for the year ended 31 December 2004				
Profit for the period attributable to equity holders of the parent	4,298	-	(32)	4,266
Valuation gain on available-for-sale investments, net of tax – continuing operations	-	-	32	32
Minority interest in disposed subsidiaries	-	(191)	-	(191)

Principles of consolidation

The consolidated financial statements of the Group comprise the financial statements of the Company and its subsidiaries.

A subsidiary is an entity that is controlled by the Company, either through ownership, directly or indirectly, of more than 50% of the voting share capital of the entity, or by other means. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases.

All inter-company transactions, balances and unrealized gains on transactions between companies of the Group 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 adjusted to conform to the policies adopted by the Group.

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 extra losses are allocated to the Group.

Companies where the Group owns more than 50% of the voting share capital but the minority shareholder enjoys substantive participation rights and has effective veto rights that would prevent the Group from taking decisions that are significant in the ordinary course of business, i.e. the Group is unable to exercise control, are accounted for under the equity method.

The Group’s interest in joint venture which is jointly controlled entity is accounted for using the equity method of accounting until the date on which the Group ceases to have joint control over the joint venture. When the Group contributes or sells assets to the joint venture, any portion of gain or loss from the transaction is recognized based on the substance of the transaction. When the Group purchases assets from the joint venture, the Group does not recognize its share of the profit of the joint venture from the transaction until it resells the assets to an independent party.

Associates in which the Group has significant influence but not a controlling interest are accounted for using the equity method of accounting. Significant influence is usually demonstrated by the Group owning, directly or indirectly, between 20% and 50% of the voting ownership interest or by power to participate in the financial and operating policy decisions of associates. The Group’s share of the net income or losses of associates is included in the consolidated statement of income, the Group’s share of movement in reserves is recognized in equity and the Group's share of the net assets of associates is included in the consolidated balance sheet.

An assessment of investments in associates for possible impairment or reversal of impairment recognized previously is performed when there is an indication that the asset has been impaired or the impairment losses recognized in prior years no longer exist. When the Group’s share of losses exceeds the carrying amount of the investment, the investment is reported at nil value and recognition of losses is discontinued except to the extent of the Group’s commitment to fund future losses. Unrealized profits that arise from transactions between the Group and its associates are eliminated in the proportion to the Group’s share in such associates, and unrealized losses are excluded in the proportion to the Group’s share in such associates, if there is no evidence of indicators of impairment of an asset transferred.

Goodwill and excess of acquirer’s interest in the net fair value of acquiree’s identifiable assets, liabilities and contingent liabilities over cost

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

Goodwill is not amortized. Instead it is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired. As at the acquisition date any goodwill acquired in acquisitions is allocated to each of the cash-generating units or groups of cash-generating units expected to benefit from the combination's synergies, irrespective of whether other assets and liabilities of the Group are assigned to those units or group of units. Each unit or group of units to which goodwill is so allocated:

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

Impairment is determined by assessing the recoverable amount of the cash-generating unit, 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 operations 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.

In case of excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost of business combination the Group:

(a) reassesses the identification and measurement of the acquiree's identifiable assets, liabilities and contingent liabilities and the measurement of the cost of the combination:
(b) recognizes in profit or loss any excess remaining after that reassessment immediately.

Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value. The cost of the network comprises all expenditures up to and including the cabling and wiring to the local telephone operator's intercity exchange, and includes contractors' charges and payments on account, materials, direct labor, and interest costs on specific project financing up to the date of commissioning of the relevant assets.

Subsequent expenditures are capitalized if it can be clearly demonstrated that they extend the life of the asset or significantly increase its revenue generating capacity beyond its originally assessed standard of performance. Expenditure for continuing repairs and maintenance are charged to the statement of income as incurred. Social assets are expensed on acquisition.

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

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

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

	Number of years
Buildings and site services	10 – 50
Cable and transmission devices:	
• Channels	10 – 40
• Cable	30 – 40
• Radio and fixed link transmission equipment	15 – 20
• Telephone exchanges	15
Other	5-10

The useful life of an asset encompass the entire time they are available for use, regardless of whether during that time it is in use or is idle.

The useful lives and residual value of assets and methods are reviewed at each financial year-end and, if expectations differ from previous estimates, the changes are accounted for prospectively (refer to Note 7).

Depreciation of an asset ceases at the earlier of the date the asset is classified as held for sale and the date the asset is derecognized.

At each balance sheet date an assessment is made as to whether there is any indication that the Group's assets may be impaired. If any such indication exists, an assessment is made to establish whether the recoverable amount of the assets has declined below the carrying amount of those assets as disclosed in the financial statements. When such a decline has occurred, the carrying amount of the assets is reduced to the recoverable amount. The amount of any such reduction is recognized immediately as an expense in the statement of income. Any subsequent increase in the recoverable amount of the assets are reversed when the circumstances that led to the write-down or write-off cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future. Increase of the recoverable amount is limited to the lower of its recoverable amount and carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years.

The recoverable amount is determined as the higher of the assets' fair value less cost to sell, or value in use. The value in use of the asset is estimated based on forecast of future cash inflows and outflows to be derived from continued use of the asset and from the estimated net proceeds on disposal, discounted to present value using an appropriate discount rate.

For the purpose of determining the opening balances on the first application of IFRS at 1 January 1994, the Company performed a valuation of the property, plant and equipment, as reliable historical cost information and information regarding acquisition dates was not available. These values were used as deemed cost. A brief description of the methodology applied in performing this valuation is set out below for each major asset category:

- Buildings and site services - current replacement cost;
- Cable and transmission devices - current replacement cost;
- Telephone exchanges - modern equivalent asset;
- Assets in course of construction - indexed historical cost.

Construction in progress represents properties under construction and is stated at cost. This includes cost of construction, plant and equipment and other direct costs. Construction in progress is not depreciated until the constructed or installed asset is ready for its intended use.

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

Indefeasible Rights of Use (IRU)

Indefeasible Rights of Use (IRU) represent the right to use a portion of the capacity of a terrestrial or submarine transmission cable granted for a fixed period. IRUs are recognized as an asset when the Group has the specific indefeasible right to use an identified portion of the underlying asset, generally optical fibers or dedicated wavelength bandwidth, and the duration of the right is for the major part of the underlying asset's economic life. They are depreciated over the shorter of the expected period of use and the life of the contract.

Leases

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the commencement of lease term 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 on a straight-line basis over the shorter of the estimated useful life of the asset or the lease term unless there is a reasonable certainty that the Group will obtain ownership by the end of the lease term, in which case the assets are depreciated over their estimated useful lives.

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

Inventory

Inventory principally consists of fuel and spare parts for the network. Inventory is stated at the lower of cost incurred in bringing each item to its present location and its net realizable value. Cost is calculated on a first in first out basis. Items used in the construction of new plant and equipment are capitalized as part of the related asset. Inventory used in the maintenance of equipment is charged to operating costs as utilized and included in repair and maintenance and other costs in these consolidated statements of income.

Accounts receivable

Trade and other accounts receivable are stated in the balance sheet at original invoice amount less an allowance for any uncollectible amounts. The allowance is created based on the historical pattern of collections of accounts receivable and specific analysis of recoverability of significant accounts. Bad debts are written off in the period in which they are identified.

Financial instruments

Financial instruments carried on the balance sheet include cash and cash equivalents, investments (other than in consolidated subsidiaries and equity method investees), receivables, accounts payable and borrowings. The particular recognition methods adopted for financial instruments are disclosed in the individual policy statements associated with each item.

Financial assets are classified into the following categories: loans and receivables, held-to-maturity, at fair value through profit or loss and available-for-sale. The Group determines the classification of its investments after initial recognition. All purchases and sales are recognized on the settlement date, which is the date that the investment is delivered to or by the Group.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, not originated with the intent to be sold immediately. Such assets are carried at amortized cost using the effective interest method. Gains and losses are recognized in income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Financial assets at fair value through profit and loss are financial assets which are either classified as held for trading or are designated by the Group as at fair value through profit or loss upon initial recognition. Financial assets are classified as held for trading if they are acquired for the purposes of selling in the near term. Gains and losses on investments held for trading are recognized in income.

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

The Group had no securities classified as held-to-maturity or at fair value through profit or loss at December 31, 2005, 2004 and 2003. Loans and receivables, including bills of exchange, are stated at amortized cost determined on an individual basis.

Borrowings

Borrowings are initially recognized at cost, being the fair value of the consideration received, net of transaction costs incurred. In subsequent periods, borrowings are measured at amortized cost using the effective interest rate method; any difference between the fair value of the consideration received (net of transaction costs) and the redemption amount is recognized as interest expense over the period of the borrowings.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks, and highly liquid investments with original maturities of three months or less, with insignificant risks of diminution in value.

Deferred income taxes

Deferred income tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences:

- except where the deferred income tax liability arises from goodwill amortization 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; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in 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 assets are recognized for all deductible temporary differences, carry-forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carry-forward of unused tax credits and unused tax losses can be utilized:

- except where the deferred income tax asset relating to the deductible temporary difference arises from 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; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognized to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized.

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

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

Revenue and operating costs recognition

Revenue and operating costs for all services supplied and received are recognized at the time the services are rendered. Revenue is recognized when it is probable that the economic benefits associated with the transaction will flow to the enterprise and the amount of revenue can be reliably measured. Revenues and expenses are reported net of respective value added tax.

The Company charges and pays to regional telephone operators and other telecommunication service providers in Russia either an agreed proportion of the amounts they bill to their subscribers or an agreed settlement rate based on traffic minutes (refer to Note 20). For outgoing telephone traffic originating in Moscow, subscribers are charged directly by the Company based on pre-set per minute tariffs.

The Company charges amounts to foreign network operators for incoming calls and other traffic that originate outside Russia. The Group is charged by foreign operators for completing international calls. These revenues and costs are shown gross in these consolidated financial statements.

Amounts payable to and receivable from the same operators are shown net in the balance sheet where a legal right of offset exists and there is intention either to settle on a net basis, or to realize the asset and settle the liability simultaneously.

Revenues from the sale of transmission capacity on terrestrial and submarine cables (indefeasible rights of use – IRU) are recognized on a straight-line basis over the life of the contract.

Employee benefits

Through December 31, 2003 the Company made certain payments to employees on retirement, or when they otherwise left the employment of the Company. These obligations, which were unfunded, represented obligations under a defined benefit pension scheme. For such plans, the pension accounting costs were assessed using the projected unit credit method. Under this method, the cost of providing pensions is charged to the statement of income so as to spread the regular cost over the average service lives of employees. Actuarial gains and losses were recognized in the statement of income immediately.

Where such post-employment employee benefits fell due more than 12 months after the balance sheet date, they were discounted using a discount rate determined by reference to market yields on Government bonds at the balance sheet date. This benefit plan was curtailed and settled on December 31, 2003.

The Company also operates a defined benefit pension scheme which requires one-off contributions, representing net present value of future monthly payments to employees, to be made by the Company to pension fund upon employees’ dismissal. A participating employee with fifteen or more years of service in telecommunication industry is eligible for the pension provided dismissal is accepted within six months after the statutory retirement age. The pension fund is liable for payments to the retired employees. Under the scheme benefits payable are indexed periodically. Actuarial gains and losses are recognized in the statement of income immediately.

The Company also participates in a defined contribution plan. Contributions made by the Company on defined contribution plans are charged to expenses when incurred. Effective January 1, 2004, maximum contribution is established at 100 Rubles per month per employee.

The Company also grants additional pensions to employees as an incentive to retire at statutory retirement age. Contributions are made to a separately administered fund. Based on a history of paying such postretirement benefits, the plan is accounted for as a defined benefit pension scheme (refer to Note 26).

The Company accrues for the employees’ compensated absences (vacations) as the additional amount that the Company expects to pay as a result of the unused vacation that has accumulated at the balance sheet date.

Under provision of the Russian legislation, social contributions are made through a unified social tax (“UST”) calculated by the Group by the application of a regressive rate (from 26% to 17%) 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 20% to 14% depending on the annual gross salary of each employee. The Company’s contributions relating to UST are expensed in the year to which they relate.

Advertising costs

Advertising costs are charged to the statement of income as incurred (refer to Note 22).

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Borrowing costs

Borrowing costs are expensed, except for those that would have been avoided if the expenditure to acquire the qualifying asset had not been made. To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization is determined by applying a capitalization rate to the expenditures on that asset. The capitalization rate is the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining the qualifying asset. Qualifying borrowing costs are capitalized with the relevant qualifying asset from the date the activities to prepare the asset are in progress and expenditures and borrowing costs are being incurred until the related asset is substantially ready for its intended use. Capitalized borrowing costs are subsequently charged to the statement of income in the period over which the asset is depreciated.

Foreign currency transactions

Transactions denominated in foreign currencies are translated into Rubles at the exchange rate as of the transaction date. Foreign currency monetary assets and liabilities are translated into Rubles at the exchange rate as of the balance sheet date.

Exchange differences arising on the settlement of monetary items, or on reporting the Group's monetary items at rates different from those at which they were initially recorded in the period, or reported in previous financial statements, are recorded as foreign currency exchange gains or losses in the period in which they arise.

As at December 31, 2005, 2004 and 2003, the rates of exchange used for translating foreign currency balances were (in Russian Rubles for one unit of foreign currency):

	2005	**2004**	**2003**
US Dollars	28.78	27.75	29.45
Japanese Yen	0.2453	0.2675	0.2754
Special Drawing Rights (SDR)	41.13	42.98	43.60
EURO	34.18	37.81	36.82

Source: the Central Bank of Russia

Dividends

Dividends are recognized when the shareholder's right to receive the payment is established. Dividends in respect of the period covered by the financial statements that are proposed or declared after the balance sheet date but before approval of the financial statements are not recognized as a liability at the balance sheet date in accordance with IAS No. 10, “Events After the Balance Sheet Date”. The amount of dividends proposed or declared after the balance sheet date but before the financial statements were authorized for issue is disclosed in Note 14.

Minority interest

Minority interest includes that part of the net results of operations and of net assets of subsidiaries attributable to interests which are not owned, directly or indirectly through subsidiaries, by the Company. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair values of identifiable assets and liabilities of the subsidiary at the acquisition date, and the minority's portion of movements in net assets since the date of the combination. The losses applicable to the minority interest holder in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary.

The excess, and any further losses applicable to the minority, are charged against the majority interest, except to the extent that the minority has a binding obligation to, and is able to, make good for the losses. If the subsidiary subsequently reports profits, the majority interest holder is allocated all such profits until the minority's interest holder share of losses previously absorbed by the majority has been recovered. If a subsidiary or an associate has outstanding cumulative preferred shares which are held outside the Group, the Company computes its share of profit or losses after adjusting for the preferred dividends, whether or not the dividends have been declared.

Minority interest in the acquiree is stated at the minority's interest holder proportion of the net fair values of the acquiree's identifiable assets, liabilities and contingent liabilities recognized as part of allocating the cost of the combination at the acquisition date.

Earnings per share

IAS No. 33, as revised, requires the application of the "two-class method" to determine earnings applicable to ordinary shareholders, the amount of which is used as a nominator to calculate earnings per ordinary share. The application of the "two-class method" requires that the profit or loss after deducting preferred dividends is allocated to ordinary shares and other participating equity instruments to the extent that each instrument shares in earnings as if all of the profit or loss for the period had been distributed. The total profit or loss allocated to each class of equity instrument is determined by adding together the amount allocated for dividends and the amount allocated for a participation feature.

Segment information

Operating segments are the primary segments of the Group. Through December 1, 2003, the Group identified the following operating segments:

- Telecommunications services
- Leasing services
- Banking and investing activities

Effective December 1, 2003, the Company discontinued two of its components represented by the leasing and banking and investing business segments (refer to Notes 21 and 23) and operates only in one segment being provision of telecommunication services.

Operating segments were identified based on the organizational structure of the Group and types of activities the Company and its subsidiaries are engaged in.

The accounting principles used to reflect transactions between reportable segments are the same as those used for transactions with external parties.

Discontinued operations

Assets or disposal groups that are expected to be sold and meet specific criteria are measured at the lower of carrying amount and fair value less costs to sell. Such assets are not depreciated and are presented separately in the balance sheet.

Operations forming a major line of business or area of geographical operations are classified as discontinued when the assets in the operations are classified as held for sale or when the entity has disposed of the operation. The results of discontinued operations are shown separately on the face of the income statement and respective amounts for prior periods presented in the financial statements are re-represented so that this presentation relate to all operations that have been classified as discontinued by the latest balance sheet date.

Reclassifications

Certain amounts reported in the prior period consolidated financial statements have been reclassified to conform with the current year presentation.

New accounting pronouncements

During 2004-2005, the IASB published several revised International Accounting Standards, issued several new International Financial Reporting Standards and gave notice of the withdrawal of one International Accounting Standard. Most of these revised and new standards will apply to accounting periods commencing on or after January 1, 2006. The new pronouncements are the following:

- IAS No. 19 (amended 2004), “Employee Benefits”,
- IAS No. 39 (amended 2005), “Financial Instruments: Recognition and Measurement ”,
- IFRS No.6 “Exploration for and Evaluation of Mineral Resources”,
- IFRS No.7 “Financial Instruments: Disclosures”,
- IFRIC No.4 “Determining whether an Arrangement contains a lease”,
- IFRIC No.5 “Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds”
- IFRIC No. 6 “Liabilities arising from Participating in a Specific Market-Waste Electrical and Electronic Equipment”,
- IFRIC 7 “Applying the Restatement Approach under IAS 29 *Financial Reporting in Hyperinflationary Economies”,*
- IFRIC 8 “Scope of IFRS 2”

The Group expects that the adoption of the pronouncements listed above will have no significant impact on the Group’s results of operations, financial position and cash flows in the period of initial application.

6. BUSINESS COMBINATIONS

The Group owns 51% of the ordinary shares of GlobalTel, a Russian closed joint stock company since inception of GlobalTel. GlobalTel was created in 1996 to provide access to a US-based global mobile satellite telephone network. Since the time of its launch, the global satellite network has experienced technical problems and low subscriber interest, as the result of which GlobalTel has only recently developed its operations beyond the development stage. The US owner of the satellite network also owns the remaining 49 per cent of GlobalTel. The charter of GlobalTel, its by-laws and the way GlobalTel historically conducted its operations provided for substantive participation of both shareholders in the economic activities of GlobalTel. The minority shareholder had effective veto rights that would prevent the Group from causing GlobalTel to take an action that is significant in the ordinary course of its business. Because effective control of GlobalTel did not rest with the Group, management accounted for the investment in GlobalTel under the equity method. The Group did not recognize its share in losses of GlobalTel as the accumulated share in losses of GlobalTel exceeded the investment of the Group in GlobalTel. Loans and other accounts receivable from GlobalTel were fully provided for as a loss from GlobalTel. Any receipts from GlobalTel in respect of the loans and receivable were recognized as gain from associates in the period they were received.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

On April 25, 2005 the shareholders' meeting of GlobalTel approved a new charter which abolished the other shareholder's veto and substantive participation rights. The Group assessed that these changes resulted in it obtaining control over GlobalTel, thus, converting it from jointly controlled entity to a subsidiary of the Group. Consequently, the results of operations and financial position of GlobalTel were consolidated in the financial statements of the Group in accordance with IAS No. 27, "Consolidated Financial Statements and Accounting for Investments in Subsidiaries", prospectively beginning from April 25, 2005.

The obtaining control over GlobalTel was accounted for using the purchase method, in accordance with provisions of IFRS 3, "Business combinations". Accordingly, the results of operations and financial position of GlobalTel were consolidated by the Group beginning from April 25, 2005. The following table summarizes the fair values of net assets acquired at the date of obtaining control:

	April 25, 2005
Property, plant and equipment	357
Inventories	191
Trade and other accounts receivable	37
Other current assets	161
Cash	138
Short-term debt (Loral)	(219)
Vendor financing (Globalstar)	(1,206)
Lease liabilities	(86)
Other current liabilities	(199)
Provisional fair value of net assets acquired	(826)
Share in accumulated deficit of GlobalTel	826
Total investment	-

From the date of acquisition, GlobalTel has contributed 37 to the reduction of the net profit of the Group. If the combination had taken place at the beginning of the year, the profit for the Group would have been 976 and revenue would have been 41,178.

In accordance with Russian legislation, joint stock companies must maintain a level of equity (net assets) that is greater than the charter capital. In the event that a company's net assets, as determined under Russian accounting legislation, fall below certain minimum levels, specifically below zero, the company can be forced to liquidate. GlobalTel has had, and continue to have, negative equity as reported in its Russian statutory financial statements. Management believes that the risk of the initiation of statutory liquidation procedures or other material adverse actions is remote.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

7. PROPERTY, PLANT AND EQUIPMENT

The net book value of property, plant and equipment as of December 31, 2005, 2004 and 2003 was as follows:

	Buildings and site services	Cable and transmission devices	Other	Construction in progress	Total
Cost					
At January 1, 2005	22,507	123,287	24,470	4,313	174,577
Additions	-	-	-	7,944	7,944
Additions with acquired subsidiaries	-	328	28	79	435
Disposals	(1,055)	(11,527)	(2,204)	(8)	(14,794)
Transfer	228	1,886	3,425	(5,539)	-
Reclassification	3,952	(2,423)	(1,529)	-	-
At December 31, 2005	25,632	111,551	24,190	6,789	168,162
Accumulated Depreciation and Impairment					
At January 1, 2005	(15,242)	(95,634)	(17,714)	-	(128,590)
Depreciation expense	(757)	(4,761)	(1,618)	-	(7,136)
Impairment losses	(1,112)	(2,687)	(1,026)	(136)	(4,961)
Disposals	679	10,460	2,014	-	13,153
Reclassification	(1,506)	228	1,278		-
At December 31, 2005	(17,938)	(92,394)	(17,066)	(136)	(127,534)
Net book value at December 31, 2005	**7,694**	**19,157**	**7,124**	**6,653**	**40,628**

	Buildings and site services	Cable and transmission devices	Other	Construction in progress	Total
Cost					
At January 1, 2004	23,386	122,290	23,266	5,345	174,287
Additions	-	-	-	4,773	4,773
Disposals	(950)	(2,068)	(958)	(14)	(3,990)
Disposal of subsidiaries	-	(241)	(131)	(121)	(493)
Transfer	71	3,306	2,293	(5,670)	-
At December 31, 2004	22,507	123,287	24,470	4,313	174,577
Accumulated Depreciation					
At January 1, 2004	(15,471)	(92,756)	(16,475)	-	(124,702)
Depreciation expense	(544)	(4,901)	(2,053)	-	(7,498)
Disposals	773	1,957	754	-	3,484
Disposal of subsidiaries	-	66	60	-	126
At December 31, 2004	(15,242)	(95,634)	(17,714)	-	(128,590)
Net book value at December 31, 2004	**7,265**	**27,653**	**6,756**	**4,313**	**45,987**

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

	Buildings and site services	Cable and transmission devices	Other	Construction in progress	Total
Cost					
At January 1, 2003	24,012	127,811	23,635	3,872	179,330
Additions	-	-	-	3,579	3,579
Additions with acquired subsidiaries	580	-	-	-	580
Disposals	(1,294)	(5,646)	(784)	(56)	(7,780)
Disposal of subsidiaries and write-down of property, plant and equipment	(580)	(551)	(291)	-	(1,422)
Transfer	668	676	706	(2,050)	-
At December 31, 2003	23,386	122,290	23,266	5,345	174,287
Accumulated Depreciation					
At January 1, 2003	(15,823)	(92,369)	(14,860)	-	(123,052)
Depreciation –continuing operations	(546)	(5,353)	(2,353)	-	(8,252)
Depreciation –discontinued operations	-	-	(24)	-	(24)
Disposals	898	4,966	659	-	6,523
Disposal of subsidiaries	-	-	103	-	103
At December 31, 2003	(15,471)	(92,756)	(16,475)	-	(124,702)
Net book value at December 31, 2003	**7,915**	**29,534**	**6,791**	**5,345**	**49,585**

Impairment of property, plant and equipment

As discussed in detail in Note 30, as part of the regulatory reform and restructuring of the national telecommunications sector aimed to facilitate competition and make the industry more attractive for investors, in 2005 the Ministry of Telecommunications issued a number of new rules and regulations that resulted in change of the Group's status as a monopoly supplier of long distance and international communications effective 1 January 2006.

The Group performed the assessment of the impact of the new rules and regulations on its business and results of operations that resulted in a 4,970 impairment loss recognized in the statement of income for the year ended 31 December 2005 related to write-down of certain property, plant and equipment of 4,961 and goodwill of 9 to their recoverable amount. The recoverable amount of property, plant and equipment was based on value in use and was determined at the cash-generating unit level. The cash-generating unit consists of the Company and its subsidiaries: Westelcom and MTs NTT. Impairment analysis was performed based on the value in use as fair value less cost to sell cannot be determined reliably. In determining value in use for the cash-generating unit, the cash flows were discounted at a rate of 16.65% on a pre-tax basis and cash flows beyond the 5-year period were extrapolated using a 5% growth rate.

Leased assets

Leased assets as of December 31, 2005, where the Group is a lessee of IRU under a finance lease, comprised of the following:

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

	2005
Cost – capitalized finance leases	412
Impairment loss and accumulated depreciation	(51)
Net book value	**361**

Refer to Note 16 for further details regarding finance leases.

Changes in estimate of useful lives

During 2002, the Group formalized a plan to discontinue leasing satellite channels beginning from February 2003. The Group has accordingly revised its estimate of the remaining period of use of the satellite channels. Depreciation expense of 210 was recognized in the consolidated statement of income for the year ended December 31, 2003, net book value of these assets amounted to nil as of December 31, 2005, 2004 and 2003. Amounts receivable from the lessor net of allowance for doubtful accounts receivable of 253, amounting to nil (2004: nil, 2003: 525) are included in other accounts receivable as of December 31, 2005, 2004 and 2003, respectively.

In March 2006 the Company formalized a plan to gradually discontinue using analog trunk lines and equipment beginning from January 2006 through the end of 2010. The Company has accordingly revised its estimate of the remaining period of use of the analog lines and equipment. The change in accounting estimates will be accounted for on a prospective basis effective January 1, 2006.

Site restoration provision

In connection with the above plan to discontinue using analog trunk lines and equipment the Group recognized a site restoration obligation of 25 in the consolidated balance sheet as of December 31, 2005 (refer to Note 15). The above costs the Group expects to incur in connection with abandonment and land restoration are included in additions to Cable and transmission devices for the year ended December 31, 2005.

Interest capitalization

Interest amounting to 118, 161 and 123 was capitalized in property, plant and equipment for the years ended December 31, 2005, 2004 and 2003. The capitalization rate used to determine the amount of borrowing costs eligible for capitalization is 5.4%, 6.1%, and 6.3%, respectively.

Pledged property, plant and equipment

Property, plant and equipment with a carrying value of 3,837, 2,066 and 2,158 was pledged in relation to loan agreements entered into by the Group as of December 31, 2005, 2004 and 2003, respectively (refer to Note 18). In addition, as of December 31, 2005 the Satellite Gateway equipment with a carrying value of 206 was pledged in connection with vendor financing received from Globalstar L.P. (minority shareholder of GlobalTel). Currently, GlobalTel is in default on this vendor financing (see also Note 17).

Discontinued operations

Included in the roll-forward of fixed assets movements for the year ended December 31, 2003 in the line "Disposal of subsidiaries and write-down of property, plant and equipment" is the amount of (551) representing partial impairment of property, plant and equipment as a result of discontinuing the leasing and banking and investing segments (refer to Note 23).

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Reclassification

Certain items of property, plant and equipment were reclassified during 2005 as a result of property, plant and equipment register verification. These reclassifications did not have significant impact on the amount of depreciation expense for all period presented.

8. SUBSIDIARIES

These consolidated financial statements include the assets, liabilities and results of operations of Rostelecom and the following of its subsidiaries, all registered in the Russian Federation:

Subsidiary	Main activity	Effective share of the Group as of December 31, 2005	Effective share of the Group as of December 31, 2004	Effective share of the Group as of December 31, 2003
ZAO GlobalTel (“GlobalTel”) (see Note 6)	Satellite telecommunications	51%	51%	51%
ZAO MTs NTT (“MTs NTT”)	Fixed line telecommunication services	100%	100%	100%
ZAO Westelcom (“Westelcom”)	Leasing of telecommunication equipment	100%	100%	100%

In April 2005, according to the changed charter of GlobalTel, the Group obtained control over GlobalTel and consolidated the latter in these financial statements as of December 31, 2005 (refer to Note 6). In the consolidated balance sheets of the Group as of December 31, 2004 and 2003 GlobalTel was accounted for under the equity method as a jointly controlled entity and included in investments in associates due to minority veto rights.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

9. INVESTMENTS IN ASSOCIATES AND JOINT VENTURES

Movements in investments in associates and joint ventures during the years ended December 31, 2005, 2004 and 2003 were as follows:

	2005	2004	2003
Beginning of year	2,511	2,381	2,635
Additions	22	110	-
Dividends received	(96)	(74)	(13)
Share in income included in continuing operations	316	170	36
Share in income included in discontinued operations	-	-	91
Removed investments on consolidation	(21)	-	-
Reclassification to long-term investments	-	(26)	-
Reclassification of investment in Golden Telecom	(2,197)	-	-
Disposal of associates	(204)	-	(368)
Reclassification of investments in ZAO Telecom-center (refer to Note 12)	-	(50)	-
End of year	**331**	**2,511**	**2,381**

Total income from associates and joint ventures presented in the consolidated statements of income is composed of the following:

	2005	2004	2003
Share in income/ (loss) of associates included in movements in investments in associates	316	170	36
(Loss) /income from GlobalTel (joint venture)	(147)	(195)	79
Total gain/(loss) from associates	**169**	**(25)**	**115**

Investments in associates and joint ventures as of December 31, 2005, 2004 and 2003 were as follows:

Associate	Main activity	Voting share capital, %	2005 Carrying amount	2004 Carrying amount	2003 Carrying amount
OAO RTComm.RU	Internet services	31	222	156	-
OAO MMTS-9	Telecommunication services	49	73	60	47
Golden Telecom, Inc., USA (“Golden Telecom”)	Telecommunication services	11.04 (2004: 11.08, 2003: 11.19)	-	2,067	2,066
GlobalTel (refer to Note 6 and Note 8)	Satellite telecommunications	51	-	-	-
ZAO Telmos	Telecommunication services	20	-	197	177
ZAO Telecom – center (refer to Note 12)	Telecommunication services	45	-	-	46
Other	Various		36	31	45
Total investments in associates			**331**	**2,511**	**2,,381**

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Summarized financial information as of December 31, 2005, 2004 and 2003 and for the years then ended of the associates disclosed above is presented below:

Aggregate amounts	2005	2004	2003
Assets	1,353	24,755	22,718
Liabilities	449	5,476	4,434
Revenue	3,401	20,051	12,044
Net income	226	2,151	1,667

All associates except for specifically otherwise mentioned are registered in the Russian Federation.

The main activity of RTComm.RU is provision of Internet access services to enterprises and individuals. As of December 31, 2005, 2004 and 2003, Rostelecom owned 31.09% of voting shares of RTComm.RU.

In September 2002, as a result of a sale of its 50% interest in EDN Sovintel to Golden Telecom, Inc. the Company acquired 4,024,067 ordinary shares of Golden Telecom. The excess of purchase price paid for shares of Golden Telecom over the fair value of identifiable net assets acquired in amount of 762 was determined to be amortized over the period of 8 years. Amortization charge of 95 reduced gain from associates (before tax) for both years ended December 31, 2004, and 2003. The unamortized part of 540 and 635 was included in carrying amount of investment in Golden Telecom as of December 31, 2004 and 2003, respectively.

During 2003 and 2004, as a result of a number of transactions initiated by the shareholders of Golden Telecom, the Company's share in the voting stock of Golden Telecom was diluted by 3.82%, from 14.9% as of December 31, 2002 to 11.08% as of December 31, 2004 (2003: 11.19%). The dilution of interest was accounted for as sale of interest in the associate. Loss of 15 and gain of 2 resulting from the dilution of interest were included in gain from associates in these consolidated statements of income for the years ended December 31, 2004 and 2003, respectively.

Management performed the analysis of the changes in the shareholders' structure of Golden Telecom during 2002, 2003 and 2004, and concluded that Rostelecom continued to exercise significant influence over the financial and operating policies of Golden Telecom through representation on its Board of Directors since in accordance with the Shareholders' Agreement Rostelecom had the right to appoint 2 out of 10 members to the Board of Directors of Golden Telecom. Accordingly, investment into Golden Telecom was accounted for using the equity method in the consolidated financial statements.

In December 2005, provisions in the Shareholders' Agreement that gave to the Company the right to appoint two directors to the Board of Golden Telecom lapsed and effective December 1, 2005, the Company's remaining rights are limited to maintaining membership of less than two directors in the Board of Golden Telecom, depending on the current effective voting power in the latter.

Management believes that the above change brought to cessation the Group's significant influence over Golden Telecom effective December 1, 2005. Consequently, in accordance with IAS No. 28, "Investments in associates", effective December 1, 2005, the Group discontinued applying equity method of accounting for its investment in Golden Telecom and reclassified this investment as an available-for-sale financial asset, as described in IAS No. 39, "Financial instruments: recognition and measurement", with initial cost equal to carrying value of equity investment in Golden Telecom at the date of the reclassification. As of December 31, 2005 investment in Golden Telecom is measured at its fair value determined based on NASDAQ closing bid price at the last trading day. (Refer to Note 9).

In April 2005, according to the changed charter of GlobalTel, the Group obtained control over GlobalTel and consolidated the latter in these financial statements as of December 31, 2005 (refer to Note 6 and Note 8).

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

In March 2005, the Group sold its 20% interest in ZAO Telmos to AFK "Systema" for a cash payment of 235.

The carrying amount of investments in associates in these consolidated financial statements is equal to the Group's share of underlying equity in the net assets of investee companies, including goodwill, if any. All associates have a December 31 year-end.

Accounting policies of associates may not comply with accounting policies used by the Group in preparation of these consolidated financial statements. In the opinion of management, differences in accounting policies of associates do not materially affect the Group's share in income (loss) of associates.

10. LONG-TERM FINANCIAL INVESTMENTS

Long-term financial investments are Ruble denominated and as of December 31, 2005, 2004 and 2003 comprised the following:

	2005	2004	2003
Notes receivable	-	94	29
Investment in Golden Telecom	3,017	-	-
Investment in OAO Sberbank of Russia	298	107	60
Other long-term financial investments	28	63	37
Total long-term financial investments	**3,343**	**264**	**126**

Investments in OAO Sberbank of Russia are classified as available-for-sale financial assets and stated at fair value (see also Note 5).

Following from cessation of Rostelecom's significant influence over Golden Telecom investment in the latter was reclassified into available-for-sale financial asset (refer to Note 9) and included in the long-term investments as of December 31, 2005 at fair value. The revaluation gain for the period from the date the Group lost significant influence over Golden Telecom through December 31, 2005 of 475 net of deferred income tax effect of 345 is recognized directly in equity for the year ended December 31, 2005.

In February 2005, the Group sold its 5% interest in MTT with a carrying value of 180 to AFK "Systema" for a cash payment of 180. As of December 31, 2004 and 2003 investment in MTT was included in other long-term financial investments.

In October 2005, the Group sold its 44% interest in ZAO "Teleport-TP" with a carrying value of 0.001 to OOO "Orbita-Telecom" for a cash payment of 13. As of December 31, 2004 and 2003 investment in ZAO "Teleport-TP" was included in other long-term financial investments.

In March 2005, the Group sold its 99% interest in OOO "Informtek" and its 30% interest in ODO "Teleradiocompany Yalta" to OOO "Kredo Esperto Yure" for a cash payment of 19 and 8, respectively. The carrying value of these investments amounted to nil.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

11. ACCOUNTS RECEIVABLE

Accounts receivable as of December 31, 2005, 2004 and 2003 comprised the following:

	2005	2004	2003
Trade accounts receivable	4,224	5,303	6,474
Less: allowance for doubtful trade accounts receivable	(898)	(1,774)	(2,406)
Trade accounts receivable, net	3,326	3,529	4,068
Prepayments	379	396	425
Prepaid taxes other than on income	1,210	1,265	1,507
Other accounts receivable	790	695	931
Less: allowance for doubtful other accounts receivable	(473)	(510)	(283)
Other accounts receivable, net	1,906	1,846	2,580
Total accounts receivable	**5,232**	**5,375**	**6,648**

Trade accounts receivable, net of allowances for doubtful accounts, include amounts totaling 459 (2004: 450, 2003: 761) due from foreign telecommunications operators which are denominated in foreign currencies, principally represented by Special Drawing Rights ("SDR") and US dollars, and amounts totaling 1,626 (2004: 1,511, 2003: 1,739) due from local telephone operators denominated in Russian Rubles. As of December 31, 2005, 2004 and 2003, the carrying value of trade accounts receivable approximated their fair value.

The following table summarizes the changes in the allowance for doubtful accounts receivable for the years ended December 31, 2005, 2004 and 2003:

	2005	2004	2003
Balance, beginning of year	2,284	2,689	2,443
(Recovery)/Provision for doubtful accounts receivable – continuing operations	(140)	369	337
Provision for doubtful accounts receivable – discontinued operations	-	-	2
Accounts receivable written-off	(773)	(774)	(93)
Balance, end of year	**1,371**	**2,284**	**2,689**

12. SHORT-TERM INVESTMENTS

Short-term investments include investments available-for-sale, which are stated at fair value, and loans and receivables which are stated at amortized cost using the effective interest rate method. Short-term investments comprised the following as of December 31, 2005, 2004 and 2003:

	2005	2004	2003
VEB bonds (USD denominated)	-	195	199
Bills of exchange	5,312	5,247	1,855
Short-term deposits and deposit certificates	6,878	2,658	700
Investments in ZAO Telecom-center	-	50	-
Other	48	-	1
Total short-term investments	**12,238**	**8,150**	**2,755**

Bills of exchange and short-term deposits and deposit certificates are classified as loans and receivables.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Fair value of investments, which are traded on active markets, is based on the market quotes for such investments. Fair value of investments, which are not traded on active market, is based on estimated discounted future cash flows. The discount rate is identified individually for each company and is based on the weighted average cost of capital.

Transactions with financial instruments are recognized using settlement date accounting. Assets are recognized on the day they are transferred to the Group and derecognized on the day that they are transferred by the Group.

Vnesheconombank (VEB) bonds, bearer securities guaranteed by the Ministry of Finance of Russia, had maturity date May, 14, 2008, and were stated in the consolidated balance sheets as of December 31, 2004 and at market value based on quotations obtained from the over the counter market. In June 2005 the Group sold Vnesheconombank (VEB) bonds for consideration of 202.

The Group invests temporarily available funds in bills of exchange issued by various Russian companies maturing within 12 months after the balance sheet date or with no fixed maturity, which the Group plans to sell during the next year. The bills of exchange bear interest in the range from 7.26% to 13.92% and are denominated in Rubles, as well as in foreign currencies. As of December 31, 2005, approximately 33% (2004: 40%, 2003: 26%) of the Group's total bills of exchange are denominated in foreign currencies, represented by US dollars. The Group uses bills of exchange as a financial instrument primarily for the purpose of receiving financial income.

Bills of exchange include promissory notes issued by OAO Svyazbank, which is related party (refer to Note 29), of 4,346 (2004: 590, 2003: 7) and Russian Industrial Bank (related party and subsidiary of RTC-Leasing, refer to Notes 23 and 29) of nil (2004: 795, 2003: nil). Short-term deposits include deposits in ZAO Promsvyazbank of 3,274 (2004: 500, 2003: 700), deposits in OAO Svyazbank of nil (2004: 900, 2003: nil) and deposits in Russian Industrial Bank of 1,817 (2004: 242, 2003: nil). Refer to Note 13 for cash held in these banks. Management of the Group is constantly monitoring financial position and performance of these banks and believes that amounts invested in promissory notes, cash and short-term deposits are fully recoverable.

In March 2005, the Group sold its 45% interest in ZAO Telecom-Center with a carrying value of 50 to OOO "Orbita", which is unrelated party, for a cash payment of 68.

13. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of December 31, 2005, 2004 and 2003 included cash on hand and at bank accounts as follows:

	2005	2004	2003
Cash on hand	2	1	2
Cash at bank – Rubles	2,165	379	1,736
Cash at bank – Foreign currencies	58	53	236
Short term deposits – Rubles	170	752	405
Short-term deposits – Foreign currencies	-	66	147
Other	3	4	3
Total cash and cash equivalents	**2,398**	**1,255**	**2,529**

As of December 31, 2005, cash at bank in foreign currencies held in escrow accounts on behalf of providers of loans to the Company amounted to nil (2004: 32, 2003: 105).

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Cash at bank denominated in Rubles include cash held in Russian Industrial bank of 22 (2004: 7, 2003: 561) and cash held in OAO Svyazbank of 539 (2004: 8, 2003: nil). Cash at bank denominated in foreign currencies include cash held in Russian Industrial Bank of 3 (2004: 1, 2003: 37). Short-term deposits denominated in Rubles include cash held in Russian Industrial Bank of nil (2004: 300, 2003: 147).

14. SHAREHOLDERS' EQUITY

Share capital

The authorized share capital of the Company as of December 31, 2005, 2004 and 2003 comprised 1,634,026,541 ordinary shares and 242,832,000 non-redeemable preferred shares. The par value of both ordinary and preferred shares amounted to Rbl 0.0025 per share.

As of December 31, 2005, 2004 and 2003, the issued and outstanding share capital was as follows:

	Number of shares	Nominal value	Carrying amount
Ordinary Shares, Rbl 0.0025 par value	728,696,320	1.822	75
Preferred Shares, Rbl 0.0025 par value	242,831,469	0.607	25
Total	**971,527,789**	**2.429**	**100**

There were no transactions with own shares during 2005, 2004 and 2003.

The Board of Directors of Rostelecom is authorized under its Charter to issue additional ordinary shares up to the total of the authorized share capital without further approval of shareholders.

The nominal share capital of the Company recorded on its incorporation has been indexed, to account for the effects of inflation from that date through December 31, 2002. The share capital in the Russian statutory accounts at December 31, 2005, 2004 and 2003 amounted to 2,428,819 nominal (uninflated) Rubles.

Ordinary shares carry voting rights with no guarantee of dividends.

Preferred shares have priority over ordinary shares in the event of liquidation but carry no voting rights except on resolutions regarding liquidation or reorganization of the Company, changes to dividend levels of preferred shares, or the issuance of additional preferred stock. Such resolutions require two-thirds approval of preferred shareholders. The preferred shares have no rights of redemption or conversion.

Preferred shares carry dividends amounting to the higher of 10% of the net income after taxation of the Company as reported in the Russian statutory accounts divided by the number of preferred shares and the dividends paid on one ordinary share. If the holders of preferred shares receive dividends of less than 10% of the net income after taxation as reported in the Russian statutory accounts, no dividends to the holders of ordinary shares are declared. Owners of preferred shares have the right to participate in and vote on all issues within the competence of general meetings following the annual general meeting at which a decision not to pay (or to pay partly) dividends on preferred shares has been taken.

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

Accordingly, the Company's preferred shares are considered participating equity instruments for the purpose of earnings per share calculations (refer to Note 27).

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Distributable earnings of all entities included in the Group are limited to their respective retained earnings, as mandated by statutory accounting rules. Statutory retained earnings of the Company as of December 31, 2005, 2004 and 2003 amounted to 28,972, 20,670 and 14,452, respectively.

Reserve capital

In accordance with the Company's Charter, Rostelecom has to maintain a reserve fund through a mandatory annual transfer of at least 5% of its statutory net profits up to the maximum amount of 15% of its statutory share capital. As of December 31, 2005, 2004 and 2003 the statutory reserve fund amounted to 364,323 nominal (uninflated) Rubles.

Dividends

Dividends declared to holders of preferred and ordinary shares in respect of the years ending December 31, 2004, 2003 and 2002 were as follows:

	2004	**2003**	**2002**
Dividend – preferred shares	722	790	310
Dividend – ordinary shares	1,064	640	396
	1,786	**1,430**	**706**
	Rbl	**Rbl**	**Rbl**
Dividend per preferred share	2.97	3.25	1.27
Dividend per ordinary share	1.46	0.88	0.54

15. ACCOUNTS PAYABLE, PROVISIONS AND ACCRUED EXPENSES

Accounts payable, provisions and accrued expenses consisted of the following as of December 31, 2005, 2004 and 2003:

	2005	**2004**	**2003**
Trade accounts payable	3,064	2,226	2,916
Short-term portion of pension obligations (refer to Note 26)	49	76	85
Short-term portion of site restoration provisions	8	-	-
Compensation related accruals	540	444	361
Other accrued expenses	339	325	156
Dividends payable	56	120	49
Current accounts payable, provisions and accrued expenses	4,056	3,191	3,567
Long-term portion of pension obligations (refer to Note 26)	123	108	121
Long-term portion of site restoration provisions	17	-	-
Long-term advances received	87	112	129
Other long-term accounts payable	151	120	237
Non-current accounts payable, provisions and accrued expenses	378	340	487
Total accounts payable, provisions and accrued expenses	**4,434**	**3,531**	**4,054**

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

As of December 31, 2005, trade accounts payable included amounts totaling 1,595, which are denominated in foreign currencies, principally represented by Special Drawing Rights and US Dollars (2004: 1,404, 2003: 1,326).

Trade accounts payable as of December 31, 2003 included accounts payable to RTC-Leasing of 520, which were repaid in 2004 (refer to Note 23).

Site restoration provisions represent present value of the expenditures the Company expects to incur in connection with phasing out of analog trunk lines during 2006-2010 in accordance with the formalized plan of the Company (refer also to Note 7). The discount rate of 16.65% was used based on the weighted average cost of capital. Total amount of site restoration provisions equals to 25, of which 8 are included in accounts payable and accrued expenses and 17 are included in non-current accounts payable in these consolidated balance sheet as of December 31, 2005.

16. FINANCE LEASE LIABILITIES

In April 2005, the Group entered into an IRU finance lease agreement for use a portion of the network capacity of a terrestrial optical fiber cables. The lease agreement is non-cancellable for the period of 15 years, which approximates the remaining useful life of the above optical fibers. Effective interest rate of the lease is 7.21% p.a. Lease payments are denominated in US Dollars. Future minimum lease payments together with the present value of the net minimum lease payments as of December 31, 2005 are as follows:

	2005
Finance lease liabilities – minimum lease payments	
Current portion of finance lease liability	53
Between one to two years	44
Between two to three years	44
Between three to four years	44
Between four to five years	44
Over five years	438
Total minimum lease payments	**667**
Less: interest	(246)
Present value of minimum lease payments	**421**

Present value of minimum lease payments	
Not later than 1 year	52
Later than 1 year and not later than 5 years	144
Later than 5 years	225
Total non-current lease payable	369
Total lease payable	**421**

Depreciation of property, plant and equipment under the finance lease contracts for 2005 amounted to 10 (refer Note 5). Finance charges for the year ended December 31, 2005 amounted to 14 and are included in interest expense in the consolidated statement of income.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

17. VENDOR FINANCING PAYABLE

Vendor financing payable include the following as of December 31, 2005, 2004 and 2003:

	2005	2004	2003
Globalstar L.P.	1,289	-	-
IBM Corporation	388	706	-
Vendor financing payable – current portion	1,677	706	-
IBM Corporation	-	353	-
Vendor financing payable – non-current portion	-	353	-
Total vendor financing	**1,677**	**1,059**	**-**

As of December 31, 2005, the Group had the following outstanding vendor financing payable:

- 1,289 (US$ 46 million) payable by GlobalTel to Globalstar L.P., which is the minority shareholder of GlobalTel, for the purchase of three gateways and associated equipment and services (refer Note 7). Globalstar L.P. has a lien over this equipment until the liability is fully paid. The initial vendor financing repayment schedule (denominated in US$) was as follows:

Payable in 2004	462
Payable in 2005	201
Payable in 2006	201
Payable in 2007	201
Payable in 2008	117
Total	**1,182**

  GlobalTel is in default in respect of payments in 2004 and 2005 and has not obtained a waiver from Globalstar L.P. As a result, the whole balance of 1,182 (US$ 41,078) is classified as current in these consolidated balance sheet as of December 31, 2005. Penalty interest in amount of 107, accrued for each day of delay at the rate of 10% p.a., is included in vendor financing payable in this balance sheet. As of December 31, 2005, Globalstar L.P. or its legitimate successors have not demanded immediate repayment of the defaulted vendor financing and loans. Management believes that if such immediate repayment is demanded, it would not have a material adverse effect on the Group's results of operations, financial position and operating plans.

- Promissory notes were issued to IBM Corporation in connection with implementation of the new billing system. The promissory notes bear interest at the rate of 6% p.a.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

18. INTEREST BEARING LOANS

The interest bearing loans as of December 31, 2005, 2004 and 2003 were as follows:

Maturity	**2005**	**2004**	**2003**
Current portion of interest bearing loans	851	1,107	1,932
Between one to two years	621	570	1,088
Between two to three years	587	109	518
Between three to four years	544	72	35
Between four to five years	520	26	-
Over five years	960	-	-
Non-current portion of interest bearing loans	3,232	777	1,641
Total interest bearing loans	**4,083**	**1,884**	**3,573**

As of December 31, 2005, 2004 and 2003, interest bearing loans, which are mostly denominated in foreign currencies, were as follows:

	Note	**2005**	**2004**	**2003**
US Dollars (US$)	(a)	3,812	1,457	2,639
Japanese Yen (JPY)	(b)	103	188	245
EURO	(c)	168	239	34
Foreign currency denominated loans		**4,083**	**1,884**	**2,918**
Russian Ruble denominated loans		**-**	**-**	**655**
Total interest bearing loans		**4,083**	**1,884**	**3,573**

As of December 31, 2005, the Group had the following loans outstanding:

a) US dollar denominated loans include the following amounts:

- US$ 15.24 million (439) on promissory notes issued to Alfa-bank in 2003. In June 2003, according to the Government decision #221 dated April 16, 2003, Rostelecom's overdue debt (with a principal of 11,601 million Japanese Yen (2,976 at the exchange rate as of June 30, 2003) and accrued interest of 20) payable to Vnesheconombank, acting as an agent of the Ministry of Finance of Russian Federation, was restructured by converting it into promissory notes issued to Alfa-Bank. Upon conversion, the carrying amount of debt amounted to US$ 98.6 (2,991 at the exchange rate as of June 30, 2003). As a result of conversion, Rostelecom's principal debt to the Ministry of Finance and interest accrued thereon were extinguished in full. Upon extinguishment of debt to the Ministry of Finance, the Company ceased to be in technical default in respect of this debt. According to the Ministry of Finance's resolution dated September 16, 2003, fines and penalties of 2,837 million Japanese Yen (749 at the exchange rate as of date of transaction) due from Rostelecom were forgiven and written off. In connection with this transaction a gain of 752 was recognized and included in other non-operating income in the consolidated statement of income for the year ended December 31, 2003 (refer to Note 24). The promissory notes to Alfa-Bank are repayable within 36 months in six semi-annual installments, beginning from December 2003, and bear interest of 5.94% per annum. The whole amount of promissory notes is included in the current portion of interest bearing loans.

- US$ 1.99 million (57) within a credit agreement between Rostelecom and Japanese Bank for International Cooperation entered into in March 2004 to finance the purchase of equipment for the reconstruction of the Tyumen-Surgut microwave line. Maximum amount of the credit line is US$ 2.66 million, of which US$ 1.60 million (Tranche A) is provided by JBIC and US$ 1.06 million (Tranche B) is provided by Sumitomo Mitsui Banking Corporation, a Japanese commercial bank. Tranche A and Tranche B bear interest of 4.67% and LIBOR plus 0.55%, respectively. The loan is repayable in semi-annual installments up to October, 2008. 19 relates to the current portion.

- US$ 6.96 million (201) on a credit agreement between Rostelecom and Japanese Bank for International Cooperation (JBIC) entered into in July 2005 to finance capital construction projects. Maximum amount of the loan is US$ 7.85 million, of which US$ 4.71 (Tranche A) is provided by JBIC and US$ 3.14 million (Tranche B) is provided by Sumitomo Mitsui Banking Corporation, a Japanese commercial bank. Tranche A and Tranche B bear interest of 6.29% and 6 months LIBOR plus 0.5%, respectively. The loan is repayable in semi-annual installments up to November, 2010. 40 relates to the current portion.

- US$ 100.00 million (2,878) on a credit agreement between Rostelecom and Vnesheconombank (VEB) and Credit Swiss First Boston (CSFB) entered into in December 2005 to finance running expenses with interest rate of 6-months LIBOR plus 3.25%. The total loan amount was provided by VEB and CSFB of US$ 99 million and US$ 1 million, respectively. To secure the debt, the Company pledged its telecommunication equipment with carrying value of 3,437. The loan is repayable annually up to the end of 2012. The total amount is included in non-current portion.

- US$ 7.00 million (201) on a credit agreement between GlobalTel and Loral Space and Communications Corporation (“Loral”). GlobalTel is in default in respect of these loans. Penalty amounted to 36 is included in the outstanding balance. As no waiver has been obtained from Loral, these loans are classified as current in the consolidated balance sheet as of December 31, 2005. The loan does not provide for any collateral.

b) Japanese Yen denominated loans include the following amounts:

- JPY 377.18 million (92) within a credit line provided by Vneshtorgbank with maximum amount of JPY 880.13 million open through February 25, 2005. The facility bears annual interest rate of 5.75%. To secure the debt, the Company pledged its telecommunication equipment with carrying value of 358. The final payment date on this credit line is to be not later than February 26, 2007. 61 relates to the current portion.

- JPY 44.99 million (11) within a credit line provided by Vneshtorgbank with maximum amount of JPY 105 million open through February 25, 2005. The facility bears annual interest rate of 5.75%. To secure the debt, the Company pledged its telecommunication equipment with carrying value of 42. The final payment date on this credit line is to be not later than February 26, 2007. 7 relates to the current portion.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

c) EURO denominated loans include the following:

- EURO 4.92 million (168) on a credit agreement between Rostelecom and ING BHF-BANK entered into in April 2004. Total amount of the credit line is EURO 7 million, payable up to 2009 in equal semi-annual installments and bearing interest of EURIBOR plus 0.875% per annum. The loan was taken for the purchase of equipment to be used in re-construction of fiber optic cable line Novosibirsk – Khabarovsk. 48 relates to the current portion.

During 2005 the Group fully repaid the loan payable to Sumitomo Corporation on a credit agreement entered into in March 1997.

As of December 31, 2005, 2004 and 2003, the weighted average interest rates of loans were 5.4%, 6.1% and 6.3%, respectively. Under IAS No. 39, "Financial Instruments: Recognition and Measurement", loans should be reflected in the financial statements at amortized cost, i.e. the amount at which they were measured at initial recognition less principal repayments, plus or minus the cumulative amortization of any difference between that initial amount and the maturity amount. The carrying amount of interest bearing loans equals their amortized cost.

The Group does not utilize financial instruments to hedge against its exposure to fluctuations in interest and foreign exchange rates.

Under the existing credit agreement with Vnesheconombank and CSFB the Group is required to meet various financial covenants applied to the statutory financial statements of the Company, including maintaining certain level of debt to equity and debt to income ratios. Management believes that as of December 31, 2005, the Group was in compliance with the above covenants.

19. INCOME TAXES

The components of net deferred tax assets and liabilities at December 31, 2005, 2004 and 2003, and the respective movements during 2005, 2004 and 2003, were as follows:

		Movement during 2005 recognized in		
	December 31, 2004	Equity	Profit for the period	December 31, 2005
Tax effects of future tax deductible items				
Investment valuation difference	34	(34)	-	-
Accounts receivable	474	-	(303)	171
Other	9	-	18	27
Gross deferred tax asset	**517**	**(34)**	**(285)**	**198**
Tax effects of future taxable items:				
Investments valuation difference	-	317	132	449
Property, plant and equipment	6,203	-	(2,485)	3,718
Accounts payable, provisions and accrued expenses	268	-	(66)	202
Gross deferred tax liability	**6,471**	**317**	**(2,419)**	**4,369**
Net deferred tax liability	**5,954**	**351**	**(2,134)**	**4,171**

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

	December 31, 2003	Movement during 2004 recognized in Equity	Movement during 2004 recognized in Profit for the period	December 31, 2004
Tax effects of future tax deductible items:				
Investment valuation difference	44	(11)	1	34
Accounts payable, provisions and accrued expenses	187	-	(187)	-
Accounts receivable	369	-	105	474
Other	3	-	6	9
Gross deferred tax asset	**603**	**(11)**	**(75)**	**517**
Tax effects of future taxable items:				
Property, plant and equipment	7,690	-	(1,487)	6,203
Accounts payable, provisions and accrued expenses	-	-	268	268
Leasing arrangements	395	-	(395)	-
Gross deferred tax liability	**8,085**	**-**	**(1,614)**	**6,471**
Net deferred tax liability	**7,482**	**11**	**(1,539)**	**5,954**

	December 31, 2002	Movement during 2003 recognized in Equity	Movement during 2003 recognized in Profit for the period	Movement during 2003 recognized in Acquisition /disposal of subsidiaries	December 31, 2003
Tax effects of future tax deductible items:					
Investment valuation difference	-	-	61	(17)	44
Accounts payable, provisions and accrued expenses	224	-	111	(148)	187
Accounts receivable	-	-	27	342	369
Other	-	-	-	3	3
Gross deferred tax asset	**224**	**-**	**199**	**180**	**603**
Tax effects of future taxable items:					
Property, plant and equipment	8,704	-	(880)	(134)	7,690
Accounts payable, provisions and accrued expenses		-			
Accounts receivable	10	-	(10)	-	-
Investment valuation difference	449	16	(71)	(394)	-
Leasing arrangements	1,015	-	(620)	-	395
Other	167	-	-	(167)	-
Gross deferred tax liability	**10,345**	**16**	**(1,608)**	**(695)**	**8,085**
Net deferred tax liability	**10,121**	**16**	**(1,780)**	**875**	**7,482**

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Differences between IFRS and statutory taxation and reporting regulations give rise to temporary differences between the carrying value of certain assets and liabilities for financial reporting and profits tax purposes. The tax effect of these temporary differences is recorded at the rate of 24% (investment valuation – at 9% to 15%).

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and the deferred income tax assets and deferred income tax liabilities relate to the income taxes levied by the same fiscal authority on the same taxable entity.

20. REVENUE

Revenue comprised the following for the years ending December 31, 2005, 2004 and 2003:

	2005	2004	2003
Revenue from local operators			
Telephone - international	6,772	6,160	5,171
Telephone - national	14,358	13,411	8,669
Other income from local operators	4,097	3,077	1,952
	25,227	**22,648**	**15,792**
Revenue from subscribers			
Telephone - international	2,633	2,900	3,027
Telephone - national	3,768	3,886	3,678
Internet access	44	-	1,060
Rent of telecommunication channels to subscribers	1,388	1,352	853
Television and radio transmission	574	602	584
Satellite services	548	-	-
Cellular services	-	-	117
	8,955	**8,740**	**9,319**
Revenue from foreign operators			
Telephone	4,098	4,041	3,871
Telex, telegraph and other	257	327	431
Rent of telecommunication channels	351	192	181
	4,706	**4,560**	**4,483**
Other revenue	2,067	1,370	1,673
Total revenue	**40,955**	**37,318**	**31,267**

Effective August 1, 2003, the Anti-Monopoly Ministry abolished the use of the Integral Settlement Rate (“ISR”) for settlements between Rostelecom and other domestic operators. Under the new settlements system, Rostelecom began to bill other operators originating domestic long-distance (“DLD”) calls using the Linear Settlement Rate (“LSR”) regulated by the Anti-Monopoly Ministry of the Russian Federation and to pay to other operators terminating the calls the termination fee calculated using the Termination Settlement Rate (“TSR”) also regulated by the Anti-Monopoly Ministry.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Prior to August 1, 2003, revenues and expenses related to DLD calls were recognized on the basis of ISR, i.e. on the net basis. The introduction of the new settlements system represents a change in business practice resulting in new accounting for changed practice. The pro-forma information calculated on the basis of the new settlement system as if it was applied effective January 1, 2003 is as follows:

	As reported above	**Pro-forma (unaudited)**
Revenue from local operators: telephone - national	8,669	12,396
Charges by network operators - national	(4,331)	(8,058)

21. SEGMENT INFORMATION

In most part of 2003 the Group operated in three industry segments: Telecommunications, Leasing and Banking and investing. As a result of divestiture of business of RTC-Leasing and discontinuance of the leasing, banking and investing segments (refer to Note 23), effective December 1, 2003, the Group operates in one industry segment, being the provision of domestic and international long distance telecommunication services in the Russian Federation. The results of this segment and assets and liabilities as of December 31, 2003, 2004 and 2005 are presented in the consolidated statements of income and the consolidated balances sheet, respectively.

The aggregate leasing, banking and investing segments' results, assets and liabilities as of December 1, 2003 are presented in Note 23.

An analysis of revenue by service type is disclosed in Note 20. A geographical analysis of revenue by the country or region of the customer for the years ending December 31, 2005, 2004 and 2003 is as follows:

	Russia	**CIS**	**USA**	**Western Europe**	**Eastern Europe**	**Others**	**Total**
2005	36,249	2,626	233	1,049	194	604	40,955
2004	32,758	2,670	256	966	191	477	37,318
2003	26,784	2,926	220	862	252	223	31,267

Leasing and banking and investing segments' revenue was principally earned in Russian Federation. Substantially all of the Group assets are located within the territory of the Russian Federation.

The Group had no individual customers, other than the Government of the Russian Federation and its related parties (see Note 29), that accounted for greater than 10% of its revenue during the years ended December 31, 2005, 2004 and 2003.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

22. ADMINISTRATION AND OTHER COSTS

Administration and other costs consisted of the following for the years ended December 31, 2005, 2004 and 2003:

	2005	**2004**	**2003**
Administration costs	965	686	1,002
Advertising and similar costs	231	162	132
Office maintenance	1,287	1,264	1,160
Utilities and similar services	613	533	490
Consulting and similar services	220	208	261
Insurance	354	377	338
Extinguishment of liabilities	-	(428)	-
Other	207	551	677
Total administration and other costs	**3,877**	**3,353**	**4,060**

Extinguishment of liabilities represents a previously recorded liability for which there is no longer a legal obligation. The effect of the extinguishment has been recorded in administration and other costs as this is where it originally has been recorded.

23. DISCONTINUED OPERATIONS

As part of management's efforts to concentrate on the Company's core business segment and as part of the Company's drive to decrease total debt, effective December 1, 2003, the Company discontinued two of its components represented by the leasing and banking and investing business segments. The operations in these business segments were conducted through RTC-Leasing and its subsidiaries.

The results of operations and loss on discontinuance of the above mentioned business segments of 3,109, net of income tax expense of 343, was included in the accompanying consolidated statement of income for the year ended December 31, 2003 and reported in discontinued operations.

In February 2002, RTC-Leasing performed an additional issuance of ordinary shares which was made in accordance with trilateral agreement (the "Shareholders' Agreement") between Rostelecom and non-state pension fund Rostelecom-Garantiya (the initial shareholders in RTC-Leasing), RTC-Leasing and a consortium of new shareholders in RTC-Leasing (the "Consortium"). After this additional issuance of shares, Rostelecom, Rostelecom-Garantiya and the Consortium owned 32.27%, 3.60% and 64.13%, respectively, of outstanding ordinary voting shares of RTC-Leasing.

Under the Shareholders' Agreement, the control over RTC-Leasing was to pass to the Consortium after the latter performs certain actions intended to increase capitalization and investing attractiveness of RTC-Leasing. The Shareholders' Agreement defined in general the obligations of the Consortium. The Consortium was to expand customer base of RTC-Leasing, to develop new lease contracts for the amount of US$330 million, to facilitate financing and increase effectiveness of the business of RTC-Leasing.

To define specific obligations of the Consortium, the parties re-negotiated the terms of the Shareholders' Agreement and signed in May 2003 an additional agreement (the "Additional Agreement") which stipulated that the Consortium is obliged to perform certain actions which should have resulted in the following within timeframe specified:

- Decreasing Rostelecom's future lease payments to RTC-Leasing by the amount not less than 1,800, including 300 of VAT, within 6 months;
- Selling shares of RTC-Leasing owned by Rostelecom and non-state pension fund Rostelecom-Garantiya for total amount of proceeds not to be less than 750 within 6 months;
- Cancellation of all guarantees and pledges provided by Rostelecom in respect of loans payable by RTC-Leasing within 12 months.

Rostelecom continued to maintain control over RTC-Leasing through its right to appoint the majority of the board of directors of RTC-Leasing until the Consortium fulfills its obligations under the Additional Agreement. In addition, Rostelecom and Rostelecom-Garantiya had the right to purchase from the Consortium at par value all the shares in RTC-Leasing issued to the Consortium if the Consortium did not fulfill its obligations on decreasing future lease payments and selling of shares by November 30, 2003.

The discontinuance of the leasing and banking and investing business segments was executed in a series of transactions that constituted an exchange, involving cash consideration, by the Company of its controlling interest in RTC-Leasing to an additional interest in certain items of telecommunications equipment previously owned by RTC-Leasing. To execute this the following actions were undertaken.

On October 24 and 27, 2003, Rostelecom sold all of its shares in RTC-Leasing to the third party for 740.

On October 2, 2003 and on December 26, 2003, Rostelecom and RTC-Leasing signed agreements restructuring the future lease payments of Rostelecom to RTC-Leasing of 6,018, including VAT of 918. Before the restructuring, the liabilities were payable through 2012. As a result of the restructurings, 3,705 became due on January 28, 2004, and 2,313 became due on January 30, 2034.

Before December 31, 2003, Rostelecom effectively paid to RTC-Leasing the amount of 3,520 by purchasing promissory notes issued by RTC-Leasing. The amount due under the promissory notes was offset against the restructured lease obligation due on January 28, 2004.

On January 29, 2004, Rostelecom and RTC-Leasing signed an agreement replacing the restructured lease obligation of 2,313 due in 2034 with a loan payable by Rostelecom to RTC-Leasing in 2038 bearing interest at a rate of 0.1% per annum. Upon execution of this step, the title to the equipment passed from RTC-Leasing to Rostelecom.

On February 12, 2004, Westelcom and RTC-Leasing executed a loan assignment agreement under which Westelcom purchased from RTC-Leasing all rights to the loan for 368, including VAT of 57.

Managements of Rostelecom and RTC-Leasing finalized negotiating the above series of transactions by December 1, 2003. On December 1, 2003, the Company accepted the performance by the Consortium of its obligations under the Additional Agreement. The settlements continued through April 2004 due to the timing requirements for formal approvals of certain transactions.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

The results of operations and cash flows of RTC-Leasing were included in the accompanying consolidated financial statements through December 1, 2003. Net income of the discontinued business segments for the period starting from late October 2003, the date the Company transferred legal ownership of its voting shares of RTC-Leasing, through December 1, 2003 was allocated to minority interest in full. Amounts payable by the Company to RTC-Leasing were recorded in the accompanying consolidated balance sheet as of December 31, 2003 at fair value determined as actual amounts paid by Rostelecom and Westelcom to RTC-Leasing in January-April 2004.

The accompanying statement of income for the year ended December 31, 2003 include as discontinued operations the post-tax results of operations of the discontinued business segments, which comprised the following:

	2003
Revenue	837
Operating expenses	(577)
Other losses, net of gains	(1,021)
Loss before tax and minority interest	**(761)**
Income tax expense	(300)
Minority interest in the results of discontinued operations	(650)
Loss recognized on disposal	(804)
Income tax expense recognized on disposal	(175)
Impairment of carrying amount of additional interest in fixed assets acquired to fair value	(551)
Income tax benefit recognized on impairment	132
Net loss from the discontinued operations	**(3,109)**

The impairment of property, plant and equipment in the amount of 551 represents the difference between the carrying amount of the telecommunication equipment, as restated for hyperinflation, and its respective fair value determined by the reference to the replacement cost of this equipment.

The net cash flows for the year ended December 31, 2003 pertaining to the discontinued business segments as reported in the accompanying consolidated statements of cash flows, were as follows:

	2003
Net cash used in operating activities	(7,362)
Net cash used in investing activities	(2,380)
Net cash provided by financing activities	7,011

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

24. OTHER NON-OPERATING INCOME, NET

Other non-operating income consisted of the following for the years ended December 31, 2005, 2004 and 2003:

	2005	2004	2003
Fair value of contributions received	-	-	316
Gain on extinguishment of loans payable (refer to Note 18)	-	-	752
Dividend income	24	-	-
Reversal of previously recognized impairment	10	53	-
Other non-operating gain, net	21	19	82
Total other non-operating income, net	**55**	**72**	**1,150**

25. INCOME TAX EXPENSE

The components of income tax expense for the years ended December 31, 2005, 2004 and 2003 were as follows:

	2005	2004	2003
Current tax charge	2,829	2,892	2,002
Deferred tax benefit (Note 19)	(2,134)	(1,539)	(1,780)
Income tax expense	**695**	**1,353**	**222**

The reconciliation of the theoretical amount that would arise using the Russian statutory rate of 24% to the total actual income tax was as follows for the years ending December 31, 2005, 2004 and 2003:

	2005	2004	2003
Income tax expense at statutory rate	401	1,349	899
Effect of lease arrangements between Rostelecom and RTC-Leasing	-	-	(620)
Change in assessment for current tax of prior periods	28	62	16
Effect of share in income taxes of associates	(156)	(143)	(92)
Non-deductible expenses	422	85	267
Other non-temporary differences	-		(248)
Income tax expense	**695**	**1,353**	**222**

Non-deductible expenses comprise various costs that are non-deductible for Russian profits tax purposes, including depreciation of certain property, plant and equipment, certain employee costs, promotional and sponsorship expenditures, travel expenditures in excess of certain statutory allowances and other expenses.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

26. EMPLOYEES

The numbers of employees of the Group was equal to 23,634 as at December 31, 2005 (2004: 25,285, 2003: 26,742).

The Group makes payments to the Government pension fund for its employees. Such contributions are included in the unified social tax ("UST") calculated by the Group using regressive scale and are charged to expense when incurred during the employee's service period. Total contributions for UST amounted to 520 during the year ended December 31, 2005 (2004: 567, 2003: 439).

The Company participates in the non-state Joint Participation Program, which is a pension plan with defined contributions. To participate in the program, individuals should be full-time employees of the Company and should enter into non-state pension insurance agreement with NPF "Telecom-Soyuz", which is the successor of NPF "Rostelecom-Garantiya". Total expenses of the Group under this program amounted to 14 during the year ended December 31, 2005 (2004: 13, 2003: 18) and are included in wages, salaries, other benefits and payroll taxes in these consolidated statements of income.

The Company also operates a defined benefit pension scheme covering a large number of its employees, which requires contributions to be made to NPF "Telecom-Soyuz". Under the scheme certain annuity is acquired by the Company as of the termination date of an employee if the latter satisfies certain criteria, such as seniority of 15 years in telecommunication sector, including seniority of 10 years in the Company, and retirement on pension during 6 months after the date an employee is entitled to pension in accordance with Russian legislation.

The following table summarizes the components of net benefit expense recognized in the consolidated statement of income and the funded status and amounts recognized in the consolidated balance sheet for the above plan (refer to Note 15):

	2005	**2004**	**2003**
Opening defined benefit obligation	184	206	178
Net benefit expense (recognized in wages, salaries, other benefits and payroll taxes)			
Interest cost on benefit obligation	13	16	14
Current service cost	17	15	17
Amortization of past service cost	40	31	29
Actuarial losses on obligation	(23)	(34)	13
Total net benefit expense	47	28	73
Benefits paid	(59)	(50)	(45)
Closing defined benefit obligation	**172**	**184**	**206**

The principal assumptions used in determining pension benefit obligation for the Group's plan are shown below:

	2005	**2004**	**2003**
Discount rate	7.7%	8.7%	9.2%
Employee turnover rate	8.4%	10.5%	10.5%
Expected average annual salary increases	6%	7%	7%
Future pension benefits increases	5.5%	5.5%	5.5%

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

27. EARNINGS PER SHARE

The calculation of basic and diluted earnings per preferred and ordinary share is presented below (earnings per share data is stated in Rubles):

	2005		2004		2003	
Net income from continuing operations	978		4,266		3,525	
Net loss from discontinued operations	-		-		(2,459)	
Total net income attributable to equity holders of the parent	**978**		**4,266**		**1,066**	
	Preferred shares	**Ordinary shares**	**Preferred shares**	**Ordinary shares**	**Preferred shares**	**Ordinary shares**
Weighted average number of shares outstanding	**242,831,469**	**728,696,320**	**242,831,469**	**728,696,320**	**242,831,469**	**728,696,320**
Earnings per share – continuing operations	**1.01**	**1.01**	**4.39**	**4.39**	**3.63**	**3.63**
Losses per share – discontinued operations	**-**	**-**	**-**	**-**	**(2.53)**	**(2.53)**
Total earnings per share	**1.01**	**1.01**	**4.39**	**4.39**	**1.10**	**1.10**

The calculation of earnings per share is based on net profit for the period divided by the weighted average number of preferred and ordinary shares outstanding during the year. Dividends are fully allocated to continuing operations.

There are no potentially dilutive instruments, therefore, diluted earnings per share equal basic earnings per share.

28. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price.

For monetary assets and liabilities, the carrying amounts approximate their fair value and balance sheet items denominated in foreign currencies have been translated at appropriate period end exchange rates.

The carrying amounts of cash and cash equivalents approximate their respective fair values due to their short-term nature and negligible credit losses.

29. RELATED PARTY TRANSACTIONS

(a) The Government and OAO Svyazinvest as a shareholder

As indicated in Note 1, the immediate parent company of the Company is OAO Svyazinvest, which holds 50.67% of the voting capital of the Company, and its representatives comprise a majority of the Board of Directors. The Government of the Russian Federation, in turn, holds 75% less one share of the voting capital of OAO Svyazinvest and, therefore, ultimately controls the Company. It is a matter of Government policy to retain a controlling stake in sectors of the economy, such as telecommunications, that it views as strategic.

(b) Interest of the Government in the telecommunications sector in the Russian Federation and the protection of that interest

Effective telecommunications and data transmission are of great importance to Russia for various reasons, including economic, social, strategic and national security considerations. The Government has exercised and may be expected to exercise significant influence over the operations of the telecommunications sector and consequently, the Group. The Government, acting through the Federal Tariff Agency, has the general authority to regulate domestic tariffs, and does regulate tariffs. The Ministry of Information Technologies and Telecommunications of the Russian Federation has control over the licensing of providers of telecommunications services.

As discussed in detail in Note 30(d), as part of the regulatory reform and restructuring of the national telecommunications sector aimed to facilitate competition and make the industry more attractive for investors, in 2005 the Ministry of Telecommunications issued a number of new rules and regulations that resulted in change of the Group's status as a monopoly supplier of long distance and international communications effective January 1, 2006.

(c) Transactions with the Svyazinvest Group

The Svyazinvest Group uses the Group's network to carry traffic between its regional and other operators and to and from these regional operators, and to and from international operators.

The Group uses the regional networks of the Svyazinvest Group to complete calls and other traffic, including that originating from its direct subscribers in the city of Moscow.

Tariffs for services between the Company and the Svyazinvest Group are materially affected with governmental regulation as disclosed in paragraph (b) of this note.

The Group also consumes design services from certain companies of the Svyazinvest Group which are included in 2005 in additions of property, plant and equipment in amount of 47 (2004: 19, 2003: 37).

The Group makes certain contributions to non-for-profit organizations which are companies of the Svyazinvest Group.

The Group makes contributions to the non-state pension fund which provides the Company's employees with a number of post-employment benefits (refer to Note 26). OAO Svyazinvest executes significant influence over the operations of the fund.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

The amounts of revenue and expenses relating to the transactions with the Svyazinvest Group were as follows:

	2005	**2004**	**2003**
Revenue	17,475	16,987	11,944
Lease revenue (included in loss from discontinued operations)	-	-	472
Charges by network operators - national	(6,757)	(6,362)	(2,930)
Administration and other costs	(72)	(16)	-
Contributions to non-for-profit organizations (included in administration and other costs)	(125)	(244)	(54)
Contributions in pension fund included in wages, salaries, other benefit and payroll taxes	(167)	(77)	(148)

In addition, OAO Svyazinvest participates in the dividends declared by the Company, commensurate with its shareholding.

The amounts of receivables and payables due from and to the Svyazinvest Group were as follows:

	2005	**2004**	**2003**
Short-term investments	2	5	16
Accounts receivable, net	1,017	1,218	1,124
Accounts payable	(82)	(301)	(192)
Payable to non-for-profit organizations	(117)	-	-
Payable to pension fund (included in compensation related accruals)	(172)	(184)	(206)

(d) Transactions with the Government

Other state bodies ("Budget Organizations"), such as the Ministry of Defense and entities affiliated to the Government, mainly use the Group's network to carry communications traffic and to broadcast across the country.

The amounts of revenue and expenses relating to the transactions with the Government were as follows:

	2005	**2004**	**2003**
Revenue	2,148	2,180	1,409
Administration and other costs	(47)	(37)	(28)
Contributions to Fund of Telecommunication History (included in administration and other costs)	(23)	(24)	(30)
Contributions to State Research and Development Fund (included in administration and other costs)	-	-	(65)

The amounts of receivables and payables due from and to such organizations were as follows:

	2005	**2004**	**2003**
Accounts receivable, net	261	346	651
Accounts payable	(88)	(24)	(22)

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

The Company purchases electricity from OAO Energy and Electrification Unified Energy System (RAO UES), a monopoly of electricity provision in which Government of the Russian Federation controlled 53%. Total purchases amounted to 195, 216 and 197 in the year ended December 31, 2005, 2004 and 2003, respectively. Accounts payable to RAO UES were nil as of December 31, 2005, 2004 and 2003.

The Company deposits available cash with OAO Sberbank of Russia in which Government of the Russian Federation controls 64%. As of December 31, 2005, 2004 and 2003 short-term deposits held in OAO of Russia amounted to 1,000, nil and nil, respectively. As of December 31, 2005, 2004 and 2003 cash held in OAO Sberbank of Russia amounted to 1,364, 291 and 549, respectively.

Transactions with other Government controlled organizations were not significant and occurred in the normal course of business.

(e) Transactions with investees

The Group is also involved in various telecommunication services with entities in which it has investments, including associates over which it exerts significant influence. A summary of these transactions is as follows:

	2005	**2004**	**2003**
Revenue	1,347	1,404	796
Charges by network operators – national	(162)	(262)	(126)

Amounts included in the consolidated balance sheets relating to the operations with these entities were as follows:

	2005	**2004**	**2003**
Accounts receivable, net	475	235	143
Accounts payable and accrued expenses	(23)	(29)	(44)

(f) Key management personnel's remuneration

During the year the Board of Directors consisted of the following members:

Until June 25, 2005	**Until December 31, 2005**
Yashin V.N.	Yashin V.N.
Avdiyants S.P.	Avdiyants S.P.
Belov V.Y.	Degtyarev V.V.
Degtyarev V.V.	Erokhin D.E.
Erokhin D.E.	Kiselev A.N.
Panchenko S.N.	Kuznetsov S.I.
Polischuk V.A.	Ragozina I.M.
Ragozina I.M.	Slipenchuk M.V.
Slipenchuk M.V.	Slizen V.A.
Finger G.M.	Terentieva N.A.
Yurchenko E.V.	Chechelnitsky E.A.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

During the year Management Board consisted of the following members:

Until June 25, 2005	Until December 31, 2005
Akopov S.L.	Akopov S.L.
Gaiduk A.A.	Belyaev K.V.
Gurevich D.M.	Gaiduk A.A.
Erokhin D.E.	Gurevich D.M.
Izotov V.Yu.	Erokhin D.E.
Kalugin I.A.	Isaev A.I.
Lutsky A.A.	Kalugin I.A.
Mironov V.K.	Lutsky A.A.
Romsky G.A.	Mironov V.K.
Rysakova G.V.	Rysakova G.V.
Sigalov D.V.	Sigalov D.V.
Terekhov V.V.	Terekhov V.V.
Khasyanova G.Sh.	Shlyapnikov A.A.

In 2005, the total remuneration of the directors and management board members, represented by short-term benefits, amounted to 131 (2004: 88, 2003: 100).

(g) Other related party transactions

In 2005, 2004 and 2003 the Group acquired promissory notes of OAO Svyazbank for 5,500, 1,333 and 7, respectively, and settled partially the promissory notes for 2,607, 750 and nil, respectively. Net income from sale of promissory notes of OAO Svyazbank amounted to 58 (2004: 12, 2003: nil) and was included in interest income in these consolidated statement of income. Also refer to Notes 12 and 13. Certain directors and managers of the Group and OAO Svyazinvest are directors of OAO Svyazbank.

During 4 months of 2005 and years ended December 31, 2004 and 2003 the Group acquired promissory notes of OAO Russian Industrial bank (OAO RIB) for 1,271, 795 and nil, respectively, and settled partially the promissory notes for 1,370, nil and nil, respectively. Gain from sale of promissory notes of OAO RIB amounted to 6 (2004: nil, 2003: nil) and was included in interest income in these consolidated statement of income. Also refer to Note 12. Certain managers of the Group were directors of OAO RIB till April 29, 2005.

In 2005, 2004 and 2003 the Group purchased software from ZAO Peter-Service. During 2005, 2004 and 2003 the Group incurred expenses in relation to this software in amount of 29, 58 and 290, respectively, the main part of which was capitalized and included in property, plant and equipment in these balance sheets as at December 31, 2005, 2004 and 2003, respectively. Prepayments made to ZAO Peter-Service included in the balance sheet amounted to 4, 11 and 27 as of December 31, 2005, 2004 and 2003, respectively. As of December 31, 2005 certain directors of the Group were directors of the company that controls ZAO Peter-Service.

The amounts of revenue and expenses relating to the transactions with other related parties were as follows:

	2005	**2004**	**2003**
Revenue	150	35	32
Administration and other costs	(31)	(13)	(32)

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

The amounts of receivables and payables due from and to such companies were as follows:

	2005	2004	2003
Accounts receivable, net	106	11	39
Accounts payable and accrued expenses	(5)	(2)	-

30. COMMITMENTS AND CONTINGENCIES

a) Legal proceedings

The Group is subject to a number of proceedings arising in the course of the normal conduct of its business. Management believes that the ultimate resolution of these matters will not have a material adverse effect on the results of operations or the financial position of the Company or the Group.

b) Taxation

Russian tax, currency and customs legislation is subject to varying interpretations and changes occurring frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Group's entities may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As of December 31, 2005 management believes that its interpretation of the relevant legislation is appropriate and the Group has adequately provided for tax liabilities in the consolidated balance sheet as of December 31, 2005. However, the general risk remains that relevant authorities could take different position with regard to interpretative issues and the effect could be significant.

As a result of the comprehensive tax inspection covering the period of 2003, the Federal Tax Service of the Russian Federation assessed 3,474 of additional taxes, including fines and penalties payable by the Company. The above assessment is based on the vague interpretation of tax legislation, relating in particular to accounting for revenue from traffic rendered and certain VAT deductions. The Group had similar transactions in 2004 and 2005, therefore, it is possible that in case of comprehensive tax inspection for these years, the Federal Tax Service of Russian Federation would assess additional taxes, including fines and penalties, with respect to the above issues. Currently, management is not able to determine reliably the amount of this exposure, if any. Management believes that the tax positions taken by the Group with respect to the above issues are appropriate and the Group has sufficient arguments to successfully defend its tax positions and prevail in the Court. At the date of approval of these financial statements the probability of Court examination can not be determined reliably in view of absence of existing court practice regarding above tax issues. No amounts related to this issue were accrued by the Group as of December 31, 2005.

c) 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 2006 to 2013. 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 Group.

d) Restructuring

In 2005 a set of new rules and regulations in the national telecommunication sector were enacted by the Ministry of Telecommunications as part of the regulatory reform and restructuring of the national telecommunications sector aimed to facilitate competition and make the industry more attractive for investors. New rules and regulations resulted in change of the Group's status as a monopoly supplier of long distance and international communication services effective January 1, 2006. The new regulations allowed telecommunication operators to apply for long-distance telecommunication licenses, 3 alternative operators received the respective licenses in 2005 and plan to start providing long distance and international communication services during 2006.

Effective January 1, 2006, in accordance with a new Russian telecommunications legislation, the Company switched to the new system of interaction with Russian operators and subscribers ("end users") for the provision of domestic long-distance (DLD) and international long-distance (ILD) services ("long-distance services").

The principles governing the interaction of operators in the provision of long-distance services to end users changed as follows:

- operators of DLD and ILD telephone networks ("long-distance operators") are to provide long-distance services to subscribers of local network operators;
- operators of intra-regional telephone networks are to provide long-distance operators with intra-regional origination and termination of calls; and
- local telephone network operators are to provide intra-regional network operators with local origination and termination of calls.

Settlements between operators are to be conducted in the order of the services rendered. Subscriber billing and collection activities, as well as other customer services, are to be performed by the long-distance operator or its agent.

Before January 1, 2006 the Company had a natural monopoly status and provided long-distance traffic transit services to Svyazinvest inter-regional telecommunications companies ("IRCs") and to other Russian operators. In every region of the Russian Federation, Svyazinvest IRCs and other operators independently billed for long-distance services provided to their local network subscribers (except for subscribers in Moscow) through their own subscriber billing systems. The operators settled with the Company for long-distance call transit and termination services, and the Company, in turn, paid the respective operator for call termination services. In Moscow, the Company billed subscribers for long-distance services directly, using its own subscriber billing system.

Before January 1, 2006 the Company was not required to bill and collect from end users for long-distance services or to provide them with other customer services throughout Russia directly. Thus, currently, the Company does not have at its disposal sufficient staff and other resources to process, prepare and analyze source documents, maintain information systems, issue bills, and collect payments to the full extent necessary.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

In order to perform the activities and ensure the corresponding infrastructure necessary to conform to the new regulatory requirements, effective January 1, 2006, the Company entered into service contracts with Svyazinvest IRCs and other operators of local and intra-regional networks to act as the Company's regional agents. Contracted services include customer services to end users, invoicing, and collection of payments for long-distance services provided by the Company. While relying on resources and data supplied by the regional agents in calculating charges for long-distance services, the Company bears responsibility for calculating charges in compliance with applicable regulations.

Management believes that the Company faces the following risks as a result of change in the scheme of settlements for the international and domestic long-distance traffic taken place from January 1, 2006:

- Risks associated with the functional capabilities of information and billing systems of Svyazinvest inter-regional telecommunications companies and other intra-regional and local operators
- Risks associated with the servicing of end users by the Company
- Risks associated with the transfer of information on subscribers
- Risks associated with rate policy

As referred to above in Note 7 the Group recognized an impairment loss of its property, plant and equipment upon assessing the impact of the new rules and regulations on its business and results of operations. The Group is currently evaluating if these changes have any other impact on its results of operations, financial position and cash flows. Effects of the introduction of the new settlement scheme will be reflected in the Group’s financial statement for the period in which the new system came into force.

e) Capital Commitments

As of December 31, 2005, contractual commitments of the Group for the acquisition of property, plant and equipment amounted to 6,220.

In connection with the finance lease agreement referred to above in Note 16, the Group also entered into non-cancelable operating lease agreements for the rent of its network capacity of a terrestrial optical fiber cables for the period of 13 years starting at various dates between 2006 and 2008.

Future minimum rentals receivable, denominated in US Dollars, under non-cancellable operating leases as of December 31, 2005 are as follows

	2005
Current portion	36
Between one to two years	61
Between two to three years	79
Between three to four years	76
Between four to five years	83
Over five years	571
Total minimum rental receivables	**906**

31. CREDIT RISK MANAGEMENT

A portion of the Group's accounts receivable is from the State and other public organizations. Collection of these receivables is influenced by political and economic factors. Management believes there were no significant unprovided losses relating to these or other receivables at December 31, 2005.

Financial instruments that could expose the Group to concentrations of credit risk are mainly trade and other receivables. The credit risk associated with these assets is limited due to the Group's large customer base and ongoing procedures to monitor the credit worthiness of customers and other debtors.

The Group deposits available cash with several Russian banks. Deposit insurance is not offered to banks operating in Russia. To manage the credit risk, the Group allocates its available cash to a variety of Russian banks and management periodically reviews the credit worthiness of the banks in which such deposits are held.

32. INTEREST RATE RISK MANAGEMENT

Trade and other receivables and payables are non-interest bearing financial assets and liabilities. Interest rates payable on the Group's loans and other borrowings are disclosed in Notes 17 and 18.

33. FOREIGN EXCHANGE RISK

In 2005, approximately 12% of the Group's revenues and 17% of the Group's expenses were denominated in currencies other than the Russian ruble. Revenues generated in foreign currency represent income received from foreign operators, and foreign currency denominated expenses consist primarily of payments to foreign operators for international long-distance traffic termination. Accounts receivable from foreign operators and accounts payable to foreign operators which are denominated in foreign currencies amounted to approximately 9% of the Group's total accounts receivable and 36% of the Group's total accounts payable as of December 31, 2005. All borrowings received by the Group during 2005 and outstanding as of December 31, 2005 are denominated in foreign currencies. Thus the Group is exposed to foreign exchange risk.

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

34. SUBSEQUENT EVENTS

In April 2006, the Group acquired 94.9% shares of ZAO Globus-Telecom, of which 60% was acquired from ZAO Alsean-N for a cash payment of 666, 15% was acquired from OAO RTC-Leasing for a cash payment of 155 and 20% was acquired through purchase of 100% share in OOO Telecomcenter. The latter was acquired from OOO Avteks for a cash payment of 281. The main activity of ZAO Globus-Telecom is provision of local telecommunication services.

The Group will account for the acquisition of Globus-Telecom applying the purchase method, in accordance with provisions of IFRS 3, "Business combinations". The results of operations and financial position of Globus Telecom shall be consolidated in the financial statements of the Group in accordance with IAS 27, "Consolidated Financial Statements and Accounting for Investments in Subsidiaries", effective April 3, 2006.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

The following table summarizes on a provisional basis the fair values of identifiable net assets of Globus-Telecom acquired as at the acquisition date:

	April 3, 2006
Property, plant and equipment	119
Intangible assets	
Number capacity	304
Contract-based intangible assets	201
Computer software	21
Employment contracts	12
Inventories	4
Trade and other accounts receivable	111
Cash	7
Other current assets	21
Short-term debt	(44)
Accounts payable and accrued liabilities	(137)
Other current liabilities	(14)
Provisional fair value of net assets acquired	**605**
Less: minority interest (5.1%)	(31)
Group's share of the fair value of net assets	574
Consideration paid	1,102
Goodwill	528

As of the date of these financial statements, the Group has not finalized the purchase price allocation for acquisition of Globus-Telecom.

In February 2006, the Group sold its 10% interest in ZAO "Telecross" to ZAO "Krosna-Invest" for a cash payment of 2. This consideration exceeds the carrying value as of December 31, 2005.

In February 2006, the Group sold its 90% interest in OOO "RTC-Sibir" to OOO"Tele-Mir" for a cash payment of 1. This consideration exceeds the carrying value as of December 31, 2005.

In March 2006, the Group sold its 17% interest in OOO "Artelecom-Service" to OOO "Artelecom-Service" for a cash payment of 9. This consideration exceeds the carrying value as of December 31, 2005.

In May 2006, the Group sold its 77% interest in OAO "A-Svyaz" to OAO "Dalsvyaz", a related party of the Group, for a cash payment of 10. This consideration exceeds the carrying value as of December 31, 2005.

In June 2006, the Group acquired 99.99% shares of ZAO Zebra Telecom from Starford Investments Company Ltd. for 365 in cash. As of the date of these consolidated financial statements the Group is in the process of determining fair value of assets acquired and liabilities assumed for the purposes of purchase price allocation.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

35. DIFFERENCES BETWEEN INTERNATIONAL FINANCIAL REPORTING STANDARDS AND ACCOUNTING PRINCIPLES GENERALLY ACCEPTED IN THE UNITED STATES

The Group's consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") which differ in certain respects from accounting principles generally accepted in the United States of America ("US GAAP").

The principal differences between IFRS and US GAAP are presented below together with explanations of certain adjustments that affect total shareholders' equity as of December 31, 2005, 2004 and 2003 and net income (loss) for the years ended December 31, 2005, 2004 and 2003.

Reconciliation of net income (loss)

	2005	**2004 (as restated, see Note 5)**	**2003 (as restated, see Note 5)**
Profit for the period reported under IFRS	**978**	**4,266**	**1,066**
Minority interest (a)	-	-	(720)
Impairment loss (b)	4,970	-	-
Depreciation on reversed impairment charge, as restated (c)	(628)	(697)	(609)
Unrealized gains on available-for-sale investments (d)			
Pension expense (e)	-	-	(30)
Impact of difference in accounting for investments acquired for resale (f)	-	-	59
Impact of goodwill amortization (g)	-	135	92
Reversal of impairment on investment in equity method investee (h)	-	-	55
Impact of difference in accounting for GlobalTel acquisition (i)	(826)	-	-
Deferred tax effects of US GAAP adjustments	(1,042)	167	107
Total	2,474	(395)	(1,046)
Net income/ (loss) under US GAAP	**3,452**	**3,871**	**20**

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Earnings per share

	2005		2004 (as restated, see Note 5)		2003 (as restated, see Note 5)	
Net income from continuing operations	3,452		3,871		3,106	
Net loss from discontinued operations	-		-		(3,086)	
Total net income/ (loss)	**3,452**		**3,871**		**20**	
	Preferred shares	**Ordinary shares**	**Preferred shares**	**Ordinary shares**	**Preferred shares**	**Ordinary shares**
Weighted average number of shares outstanding	**242,831,469**	**728,696,320**	**242,831,469**	**728,696,320**	**242,831,469**	**728,696,320**
Earnings per share – continuing operations	**3.55**	**3.55**	**3.98**	**3.98**	**3.20**	**3.20**
Losses per share – discontinued operations	**-**	**-**	**-**	**-**	**(3.18)**	**(3.18)**
Total earnings /(losses) per share	**3.55**	**3.55**	**3.98**	**3.98**	**0.02**	**0.02**

Basic and diluted earnings per share are the same for all periods presented, as there are no potentially dilutive instruments.

Reconciliation of shareholders' equity

	2005	2004 (as restated, see Note 5)	2003 (as restated, see Note 5)
Total shareholders' equity under IFRS	**49,697**	**50,838**	**48,161**
US GAAP adjustments:			
Minority interest (a)	-	-	(191)
Impairment of property, plant and equipment (b)	4,970	-	
Reversal of impairment of property, plant and equipment, as restated (c)	808	1,436	2,133
Impact of goodwill amortization (d)	262	262	127
Partial gain recognition, net of tax (g)	(3)	(3)	(3)
Deferred tax effects of US GAAP adjustments	(1,386)	(344)	(511)
Total	4,651	1,351	1,555
Total shareholders' equity under US GAAP	**54,348**	**52,189**	**49,716**

(a) Minority interest

In accordance with revised IAS No.1 "Presentation of Financial Statements", effective for financial statements issued for annual periods beginning on or after January 1, 2005, minority interest is included in total net income.

Under US GAAP, minority interest is deducted from net income and net income represents profit or loss attributable to equity holders.

(b) Impairment on property, plant and equipment

As discussed in detail in Note 30(d), as a result of the regulatory reform and restructuring of the national telecommunications sector, the Group lost its status as a monopoly supplier of long distance and international communications effective 1 January 2006. Management believes that adoption of new regulations in telecommunication sector and change in competitive environment these new regulations would trigger represent an indication that the Group's assets may be impaired constituted such an indication. IAS No. 36 requires an assessment of the recoverable amount of an asset whenever there is an indication that the Group's assets may be impaired.

Therefore, in accordance with provisions of IAS No.36 "Impairment of Assets" that require an assessment of the recoverable amount of assets whenever there is an indicator that they may be impaired, in December 2005, the Group performed the assessment of impact of the new rules and regulations on its business and results of operations and recognized an impairment loss of 4,970 on property, plant and equipment, other then construction in progress (see Note 7).

Under US GAAP, SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", requires an initial assessment of impairment based on undiscounted cash flows whenever there is an indication that impairment may exist. Due to the fact the sum of undiscounted expected future cash flows was in excess of the carrying amount of the Group's property, plant and equipment as of December 31, 2005, an impairment loss was not recognized for US GAAP reporting purposes. Management considers that all of the Group's property, plant and equipment, with the exception of construction in progress and property, plant and equipment pertaining to GlobalTel's operations, represent the lowest level for which there are largely independent and identifiable cash flows

Since no impairment loss was recognized under US GAAP in 2005, a different asset base will be used to compute US GAAP depreciation expense, loss on disposal of property, plant and equipment and the related deferred tax liability commencing 2006.

Deferred tax effect was computed using tax rate of 24%.

(c) Reversal of impairment on property, plant and equipment, including restatement of previously issued financial information

In 1998, the Group recognized an impairment loss of 8,699 on its property, plant and equipment other than construction in progress. The impairment loss was calculated based on the present value of estimated future cash flows from the continued use of the assets using a real-terms (inflation adjusted) discount rate of 20%.

Under US GAAP, the sum of undiscounted expected future cash flows was in excess of the carrying amount of the Group's property, plant and equipment as of December 31, 1998, and an impairment loss was not recognized for US GAAP reporting purposes. Thus, a different asset base was used to compute US GAAP depreciation expense, loss on disposal of property, plant and equipment and the related deferred tax liability commencing 1999.

Deferred tax effect was computed using tax rate of 24% for 2005, 2004 and 2003. Deferred tax benefit recognized on reversal of impairment on property, plant and equipment in 2005, 2004 and 2003 represents the effects of reversal of the temporary differences associated with disposals and additional depreciation.

In 2005, the Group determined that property, plant and equipment carrying balances related to non-productive social assets should have been impaired based on the impairment review performed in 1998 under US GAAP. Respective impairment charge was made in the Group's 1998 financial statements prepared under IFRS.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Social assets are primarily comprised of kindergartens, recreation areas, living apartments for Group employees, schools and other objects of social infrastructure.

As a result, management revised its accounting for property, plant and equipment carrying balances, related depreciation expense, loss on disposal of property, plant and equipment and the related deferred tax liability as of December 31, 2004 and the two years then ended as follows:

Reconciliation of net income (loss)

	2004	2003
Net income /(loss) under US GAAP, as previously reported	**3,679**	**(171)**
Depreciation on reversed impairment charge, as reported	889	800
Depreciation on reversed impairment charge, as restated	(697)	(609)
Impact of restatement	192	191
Net income under US GAAP, as restated	**3,871**	**20**

The above correction of property, plant and equipment carrying balances, related depreciation expense and loss on disposal of property, plant and equipment did not have deferred tax effects as social assets are not deductible for statutory purposes and, therefore, represent permanent difference under both IFRS and US GAAP.

Reconciliation of shareholders' equity

	2004	2003
Total shareholders' equity under US GAAP, as previously reported	**55,081**	**52,800**
Impairment of property, plant and equipment	(3,084)	(3,275)
Depreciation expense	192	191
Total shareholders' equity under US GAAP, as restated	**52,189**	**49,716**

The reconciliation of earnings per share, as restated, and earnings per share previously reported for the years ended December 31, 2004 and 2003 under US GAAP is as follows:

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Earnings per share

	2004	**2003**
Net income from continuing operations, as reported	3,679	2,915
Net loss from discontinued operations	-	(3,086)
Total net income/ (loss), as reported	**3,679**	**(171)**
Reversal of depreciation charge related to impairment, net of tax	192	191
Net income from continuing operations, as restated	3,871	3,106
Net loss from discontinued operations	-	(3,086)
Total net income, as restated	**3,871**	**20**

	Preferred shares	**Ordinary shares**	**Preferred shares**	**Ordinary shares**
Weighted average number of shares outstanding	**242,831,469**	**728,696,320**	**242,831,469**	**728,696,320**
Earnings per share – continuing operations, as reported	**3.79**	**3.79**	**3.00**	**3.00**
Losses per share – discontinued operations	**-**	**-**	**(3.18)**	**(3.18)**
Total earnings /(losses) per share, as reported	**3.79**	**3.79**	**(0.18)**	**(0.18)**
Earnings per share – continuing operations, as restated	**3.98**	**3.98**	**3.20**	**3.20**
Losses per share – discontinued operations	**-**	**-**	**(3.18)**	**(3.18)**
Total earnings per share, as restated	**3.98**	**3.98**	**0.02**	**0.02**

(d) Unrealized gains on available-for-sale investments

In accordance with the previous version of IAS No. 39, “Financial Instruments: Recognition and Measurement” that was effective for the years ended December 31, 2004 and 2003, the Group included unrealized gains and losses from change in the fair value of securities classified as available-for-sale investments in the determination of net income.

As referred to above in Note 5, upon application of revised IAS No. 39, the Group reconsidered classification of its investments in bills of exchange and re-represented them as loans and receivables in the consolidated balance sheets as of December 31, 2004 and 2003. In accordance with revised IAS No. 39 loans are receivables are carried at amortized cost using the effective interest method. Gains and losses are recognized in income through amortization process. Therefore, the reclassification of bills of exchange did not have a material impact on the Group’s results of operations for all periods presented.

Also upon application of revised IAS No.39, the Group recognizes holding gains and loses resulting from changes in fair value of available-for-sale investments, net of tax, as a separate component of equity.

As required by transition provisions of IAS No.39, the Group applied this Standard retrospectively. The opening balance of retained earnings for the earliest prior period presented and all other comparative amounts were adjusted as if this Standard had always been in use. The effects of adoption of revised IAS No.39 on the corresponding figures are summarized above in Note 5.

Under US GAAP, SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", provides that such available-for-sale securities are reported at fair value with unrealized gains and losses, net of tax, to be excluded from earnings and reported as a separate component of comprehensive income. Unrealized gains and losses represent the net change in fair value of investments classified as available-for-sale. Declines in value of available-for-sale securities judged to be other than temporary are recognized in the statement of operations. Dividend and interest income, including amortization of the premium and discount arising at acquisition, for all three categories of investments in securities shall continue to be included in earnings.

Upon retrospective application of IAS 39, previously reported reconciling differences between IFRS and US GAAP with respect to accounting for available-for-sale investments have been reversed and no longer exist.

(e) Pension expense and obligations

The Company made certain payments to employees on retirement. These obligations were substantially similar to those typically existing under a defined benefit pension scheme.

IAS No. 19, "Employee Benefits", was issued by the International Accounting Standards Board to revise existing standards relating to retirement benefits cost, and became effective for the financial statements beginning on or after January 1, 1999. In accordance with US GAAP, similar issues are covered by SFAS No. 87, "Employer's Accounting For Pensions". Under both standards, pension expense is based upon a specified methodology that includes a designated actuarial approach and reflects the concept of accrual accounting. Pension expense is reflected in the consolidated statement of income systematically over the working lives of employees covered by the plan. Plan amendments (including initiation of a plan) often include provisions that grant increased benefits based on services rendered in prior periods. Because plan amendments are granted with the expectation that the employer would realize economic benefits in future periods, SFAS No. 87 does not require the cost of providing such retroactive benefits (that is, prior service cost) to be included in net periodic pension cost entirely in the year of the amendment. SFAS No. 87 provides for recognition of prior service cost during the future service periods of employees who are expected to receive benefits under the plan.

In accordance with IAS 19, prior service cost is recognized as an expense on a straight-line basis over the average period until the benefits become vested (i.e. become no longer conditional on future employment). To the extent that the benefits are already vested immediately following the introduction of, or changes to, a defined benefit plan, an enterprise should recognize prior service cost immediately.

Prior service cost under a defined benefit plan related to certain payments to employees on retirement had been fully recognized in IFRS accounts. In US GAAP accounts, unrecognized transition amounts related to this plan were amortized over 10 years. Since as of December 31, 2003, the above plan was curtailed and settled in full, the Group recognized a loss of 30 in US GAAP accounts with respect to unamortized portion of past service cost as of that date.

(f) Accounting for investments in associates

Before IFRS No.5 was adopted, the Group accounted for an investment in associate that was acquired and held exclusively with a view to its disposal in the near future as an available-for-sale financial asset in accordance with IAS 39, "Financial Instruments: Recognition and Measurement".

In 2002 the Group acquired and in 2003 sold certain investments which in the normal course of business would qualify for equity method accounting. In IFRS accounts these investments were classified and accounted for as available-for-sale.

Effective January 1, 2002, SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets", eliminated the exception to application of the equity method for an investment in associates where significant influence is likely to be temporary. Accordingly, in US GAAP accounts, the investments in these associates were accounted for using equity method of accounting.

As investments were sold in 2003, the amount of 59 reported in the reconciliation of net income and shareholders' equity for 2003 above represents reversal of differences in accounting for these investments under IFRS and US GAAP, reported in prior periods.

Before IFRS No. 3 "Business combinations" was adopted, the Group amortized goodwill acquired in business combinations. As described in Note 9, during 2002, the Group acquired 15% of voting stock of Golden Telecom, Inc. In the opinion of management, the Group exercised significant influence over financial and operating policies of Golden Telecom. Therefore, in accordance with IAS No.28, "Accounting for Investments in Associates" effective for the years ended 31 December 2004 and 2003, the Group amortized the equity method goodwill related to its investment in Golden Telecom over its estimated useful life of 8 years. During 2004 and 2003 the equity method goodwill related to investment in Golden Telecom recognized in IFRS accounts amounted to 135 and 95, respectively.

Effective January 1, 2005, IFRS No.3 "Business combinations" prohibited amortization of goodwill and required to test it for impairment annually.

In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets", goodwill is not amortized and is subject to annual impairment tests in accordance with SFAS No. 142. The Group performed the annual impairment test in respect to recoverability of the carrying amount of goodwill at December 31, 2005, 2004 and 2003 by comparing the fair value to the carrying amount for both IFRS and US GAAP purposes. The fair value exceeded the carrying amount.

(g) Partial gain recognition

During 2002 the Group completed a sale of its 50% interest in EDN Sovintel to Golden Telecom in exchange for a cash payment of US$10 million, no-interest bearing US$46 million promissory note and 15% of then outstanding ordinary shares of Golden Telecom.

In connection with this transaction, in its IFRS accounts, the Group recognized a gain of 1,733, which represented a difference between fair value of the total consideration received and the carrying amount of the investment in EDN Sovintel as of the date of sale, net of direct costs associated with the transaction. Before the sale to Golden Telecom, the Group accounted for its investment in EDN Sovintel using equity method.

In its US GAAP accounts, in accordance with requirements of Emerging Issues Task Force Issue No. 01-02, "Interpretations of APB 29", the Group recognized a gain of 1,730. The difference of 3 between the amount of gain recognized under IFRS and US GAAP pertains to a portion of the gain represented by the economic interest retained by the Group.

(h) Reversal of impairment on investment in equity method investee

During 2002 due to certain changes in management's estimates and in accordance with provisions of IAS No. 36, "Impairment of Assets", in its IFRS accounts the Group recorded a partial reversal of impairment loss of 55 recognized in 2001 in connection with its investment in MCC, which is accounted for using equity method.

US GAAP prohibits reversals of previously recognized impairment losses.

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

In 2003 the investment in MCC was sold. Accordingly, all differences in accounting for this investment under IFRS and US GAAP reported in prior periods reversed in 2003.

(i) Accounting for acquisition of GlobalTel

As described in Note 6, in 2005 the Group obtained control over GlobalTel. The obtaining control over GlobalTel was accounted for using the purchase method, in accordance with provisions of IFRS No. 3 "Business combinations". The Group recognized its share in accumulated deficit of GlobalTel of 826 directly in equity.

For US GAAP purposes prior to obtaining control over GlobalTel on April 25, 2005, the Group accounted for its investments in GlobalTel under equity method. Since GlobalTel incurred substantial losses from inception and had negative equity, the Group reduced its investment in GlobalTel to 0 and suspended recognition of further equity method losses. Upon obtaining control over GlobalTel, in accordance with transition provisions of EITF 96-16 "Investor's Accounting for an Investee when the Investor has a Majority of the Voting Interest but the Minority has Certain Approval or Veto Rights" the Group consolidated GlobalTel on April 25, 2005. Upon consolidation, assets and liabilities of GlobalTel were recorded at their carrying values as of that date and the Group recorded a charge of 826 for the cumulative losses previously not recorded. The following table summarizes the effect of consolidation of GlobalTel on April 25, 2005 on the consolidated financial statements of the Group:

	April 25, 2005
Property, plant and equipment	357
Inventories	191
Trade and other accounts receivable	37
Other current assets	161
Cash	138
Short-term debt (Loral)	(219)
Vendor financing (Globalstar)	(1,206)
Lease liabilities	(86)
Other current liabilities	(199)
Cumulative effect adjustment	826
	-

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

Investments in associates

Summarized financial information for 2005, 2004 and 2003 of the Group's significant equity method investee, Golden Telecom, Inc, was as follows (translated into Rubles using exchange rate as of December 31, 2005, 2004 and 2003, respectively):

	2005	2004	2003
Income statement information			
Revenues	19,209	16,205	10,619
Operating income	3,337	2,651	2,054
Net income	2,190	1,798	1,633
Financial position information			
Current assets	6,072	5,558	5,542
Non-current assets	19,320	16,801	15,937
Current liabilities	3,796	3,234	2,944
Non-current liabilities	1,598	1,418	1,365
Net assets	19,431	17,381	17,090

New US GAAP standards adopted in 2005

The Group adopted the provisions of the reached consensus on Issue No. 03-1 "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" (EITF 03-1). The issue is to determine the meaning of other-than-temporary impairment and its application to debt and equity securities within the scope of FASB Statement No. 115 "Accounting for Certain Investments in Debt and Equity Securities." The impairment methodology for investments accounted for under the equity method is predicated on the notion of other-than-temporary. The taskforce reached a consensus that the application guidance in EITF 03-1 should be used in determining when an investment is considered impaired, whether that impairment is other-than-temporary and the measurement of the impairment.

The Group adopted the provisions of the reached consensus on EITF Issue 03-16 ("EITF 03-16"), "Accounting for Investments in Limited Liability Companies." EITF 03-16 provides guidance about when to account for an investment in a limited liability company that maintains a specific ownership account for each investor using the cost method or the equity method of accounting.

The Group adopted the provisions of the reached consensus on EITF Issue 02-14 ("EITF 02-14"), "Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock." EITF 02-14 requires an investor to apply the equity method of accounting to investments in common stock of a corporation or in-substance common stock of a corporation, when the investor has the ability to exercise significant influence over the operating and financial policies of the investee. For investments in corporations that are not common stock or in-substance common stock that were previously accounted for under the equity method, EITF 02-14 requires that the investor discontinue the equity method unless required by other applicable guidance.

Effective January 1, 2005, the Group early adopted provisions of SFAS No. 153, Exchanges of Non-monetary Assets—an amendment of APB Opinion No. 29, the FASB issued in December 2004. SFAS No. 153 eliminates the exception from fair value measurement for non-monetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No. 29, Accounting for Non-monetary Transactions, and replaces it with an exception for exchanges that do not have commercial substance. SFAS No. 153 specifies that a non-monetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange.

The adoption of the above standards, interpretations or revisions did not have a material impact on the Group's results of operations, financial position or cash flows.

New accounting pronouncements

During 2005-2006, several new standards, interpretations or revisions to existing standards were issued.

The Group is currently evaluating the impact of the following new or revised standards and interpretations on its results of operations, financial position and cash flows and is in process of developing an implementation strategy:

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections - a replacement of APB Opinion No. 20 and FASB Statement No. 30. SFAS No. 154 replaces APB Opinion No. 20, Accounting Changes, and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements, and applies to all voluntary changes in accounting principle and changes the requirements for the accounting for, and reporting of, a change in accounting principle. SFAS No. 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principle unless it is impracticable. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. Earlier application is permitted for accounting changes and corrections of errors made occurring in fiscal years beginning after June 1, 2005. The Group expects to adopt SFAS No. 154 beginning January 1, 2006. The impact adopting SFAS No. 154 cannot be accurately estimated at this time as no such accounting changes are currently contemplated.

Consolidated statements of changes in shareholders' equity and comprehensive income under US GAAP for the years ended December 31, 2005, 2004 and 2003 are as follows:

(In millions of Russian Rubles unless otherwise stated, refer to Note 5)

	Common shares Number of shares	Common shares Share capital	Preferred shares Number of shares	Preferred shares Share capital	Retained earnings	Accumulated other comprehensive income	Total shareholders' equity
Balance as of January 1, 2003	**728,696,320**	**75**	**242,831,469**	**25**	**49,939**	**312**	**50,351**
Comprehensive income							
Net income	-	-	-	-	20	-	**20**
Net change in unrealized gain on available-for-sale investments	-	-	-	-	-	51	**51**
Total comprehensive income	-	-	-	-	20	51	**71**
Dividends for 2002	-	-	-	-	(706)	-	**(706)**
Balance as of December 31, 2003	**728,696,320**	**75**	**242,831,469**	**25**	**49,253**	**363**	**49,716**
Comprehensive income							
Net income	-	-	-	-	3,871	-	**3,871**
Net change in unrealized gain on available-for-sale investments	-	-	-	-	-	32	**32**
Total comprehensive income	-	-	-	-	3,871	32	**3,903**
Dividends for 2003	-	-	-	-	(1,430)	-	**(1,430)**
Balance as of December 31, 2004	**728,696,320**	**75**	**242,831,469**	**25**	**51,694**	**395**	**52,189**
Comprehensive income							
Net income	-	-	-	-	3,452	**-**	**3,452**
Net change in unrealized gain on available-for-sale investments	-	-	-	-	262	231	**493**
Total comprehensive income	-	-	-	-	3,714	231	**3,945**
Dividends for 2004	-	-	-	-	(1,786)	-	**(1,786)**
Balance as of December 31, 2005	**728,696,320**	**75**	**242,831,469**	**25**	**53,622**	**626**	**54,348**