

# **OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES**

## **Consolidated Financial Statements**

At December 31, 2004 and  
2003 and for the Years Ended  
December 31, 2004, 2003 and 2002

# OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

## TABLE OF CONTENTS

---

	<b>Page</b>
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM	1
CONSOLIDATED FINANCIAL STATEMENTS AT DECEMBER 31, 2004 AND 2003 AND FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002:	
Consolidated balance sheets at December 31, 2004 and 2003	2-3
Consolidated statements of operations for the years ended December 31, 2004, 2003 and 2002	4
Consolidated statements of changes in shareholders' equity for the years ended December 31, 2004, 2003 and 2002	5
Consolidated statements of cash flows for the years ended December 31, 2004, 2003 and 2002	6-7
Notes to consolidated financial statements	8-56

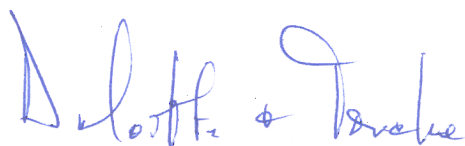
## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of OJSC Mobile TeleSystems:

We have audited the accompanying consolidated balance sheets of Mobile TeleSystems, a Russian Open Joint-Stock Company, and subsidiaries (the "Group") as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004. 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. The Group is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Group as of December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.



March 22, 2005, except for Note 23,  
as to which the date is May 24, 2005

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### CONSOLIDATED BALANCE SHEETS

AT DECEMBER 31, 2004 AND 2003

*(Amounts in thousands of U.S. dollars, except share and per share amounts)*

	December 31,	
	2004	2003
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents (Note 4)	\$ 274,150	\$ 90,376
Short-term investments, including related party amounts of \$73,100 and \$245,000 as of December 31, 2004 and 2003, respectively (Note 5)	73,360	245,000
Trade receivables, net (Note 6)	162,525	99,951
Accounts receivable, related parties (Note 17)	17,768	3,356
Inventory (Note 7)	89,518	67,291
Prepaid expenses	79,971	46,679
Deferred tax asset, current portion (Note 14)	49,850	44,423
VAT receivable	272,578	209,629
Other current assets	21,235	33,774
<b>Total current assets</b>	<b>1,040,955</b>	<b>840,479</b>
<b>PROPERTY, PLANT AND EQUIPMENT</b> , net of accumulated depreciation of \$901,416 and \$532,268, respectively (Note 8)	3,234,318	2,256,076
<b>LICENSES</b> , net of accumulated amortization of \$417,158 and \$257,024, respectively (Notes 3 and 20)	771,271	703,103
<b>GOODWILL</b> (Notes 3 and 22)	108,329	8,533
<b>OTHER INTANGIBLE ASSETS</b> , net of accumulated amortization of \$277,905 and \$148,052, respectively (Notes 3 and 9)	328,533	304,144
<b>DEBT ISSUANCE COSTS</b> , net of accumulated amortization of \$9,345 and \$4,586, respectively (Note 11)	16,546	9,431
<b>INVESTMENTS IN AND ADVANCES TO ASSOCIATES</b> (Note 19)	81,235	103,585
<b>Total assets</b>	<b>\$ 5,581,187</b>	<b>\$ 4,225,351</b>

The accompanying notes to consolidated financial statements are an integral part of these statements.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### CONSOLIDATED BALANCE SHEETS (CONTINUED)

AT DECEMBER 31, 2004 AND 2003

(Amounts in thousands of U.S. dollars, except share and per share amounts)

	December 31,	
	2004	2003
<b>CURRENT LIABILITIES:</b>		
Accounts payable, related parties (Note 17)	\$ 17,009	\$ 31,904
Trade accounts payable	242,495	168,039
Deferred connection fees, current portion (Note 10)	45,083	21,467
Subscriber prepayments and deposits	308,859	191,768
Debt, current portion (Note 11)	370,845	103,312
Notes payable, current portion (Note 11)	-	597,836
Capital lease obligations, current portion (Notes 12 and 17)	8,561	9,122
Income tax payable	22,567	11,128
Accrued liabilities (Note 13)	180,677	143,789
Other payables	33,872	19,604
<b>Total current liabilities</b>	<u>1,229,968</u>	<u>1,297,969</u>
<b>LONG-TERM LIABILITIES:</b>		
Notes payable, net of current portion (Note 11)	800,000	800,000
Debt, net of current portion (Note 11)	753,795	142,418
Capital lease obligations, net of current portion (Notes 12 and 17)	3,947	7,646
Deferred connection fees, net of current portion (Note 10)	47,665	25,177
Deferred taxes (Note 14)	160,390	180,628
<b>Total long-term liabilities</b>	<u>1,765,797</u>	<u>1,155,869</u>
<b>Total liabilities</b>	<u>2,995,765</u>	<u>2,453,838</u>
<b>COMMITMENTS AND CONTINGENCIES</b> (Note 21)	-	-
<b>MINORITY INTEREST</b>	62,099	47,603
<b>SHAREHOLDERS' EQUITY:</b>		
Common stock: (2,096,975,792 shares with a par value of 0.1 rubles authorized and 1,993,326,138 shares issued as of December 31, 2004 and 2003, 432,414,940 of which are in the form of ADS (Note 1))	50,558	50,558
Treasury stock (7,202,108 and 9,929,074 common shares at cost as of December 31, 2004 and 2003, respectively) (Note 16)	(7,396)	(10,197)
Additional paid-in capital	564,160	559,911
Unearned compensation (Note 16)	(1,780)	(869)
Shareholder receivable (Note 11)	(18,237)	(27,610)
Accumulated other comprehensive income (Note 2)	22,444	7,595
Retained earnings	1,913,574	1,144,522
<b>Total shareholders' equity</b>	<u>2,523,323</u>	<u>1,723,910</u>
<b>Total liabilities and shareholders' equity</b>	<u>\$ 5,581,187</u>	<u>\$ 4,225,351</u>

The accompanying notes to consolidated financial statements are an integral part of these statements.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars, except share and per share amounts)*

	Years ended December 31,		
	2004	2003	2002
<b>NET OPERATING REVENUE</b>			
Services revenue and connection fees	\$ 3,800,271	\$ 2,465,089	\$ 1,299,141
Sales of handsets and accessories	86,723	81,109	62,615
	<u>3,886,994</u>	<u>2,546,198</u>	<u>1,361,756</u>
Cost of services, excluding of depreciation and amortization shown separately below (including related party amounts of \$56,722, \$37,680 and \$31,607, respectively)	481,097	301,108	196,445
Cost of handsets and accessories	218,590	173,071	90,227
General and administrative expenses (including related party amounts of \$14,557, \$11,002 and 9,602, respectively) (Note 18)	575,296	355,230	215,942
Provision for doubtful accounts (Note 6)	26,459	32,633	7,047
Other operating expenses	29,777	18,859	6,067
Sales and Marketing expenses (including related party amounts of \$59,113, \$23,668 and \$12,140, respectively)	460,983	326,783	171,977
Depreciation and Amortization expenses	<u>675,729</u>	<u>415,916</u>	<u>209,680</u>
Net operating income	<u>1,419,063</u>	<u>922,598</u>	<u>464,371</u>
CURRENCY EXCHANGE AND TRANSACTION (GAINS)/LOSSES	(6,529)	(693)	3,474
OTHER EXPENSES (including related party amounts of \$5,303, \$6,161 and \$5,141, respectively):			
Interest income	(21,792)	(18,076)	(8,289)
Interest expense	107,956	106,551	44,389
Other (income) expenses, net	<u>(33,456)</u>	<u>3,420</u>	<u>(2,454)</u>
Total other expenses, net	<u>52,708</u>	<u>91,895</u>	<u>33,646</u>
Income before provision for income taxes and minority interest	<u>1,372,884</u>	<u>831,396</u>	<u>427,251</u>
PROVISION FOR INCOME TAXES (Note 14)	354,664	242,480	110,417
MINORITY INTEREST	<u>30,342</u>	<u>71,677</u>	<u>39,711</u>
NET INCOME	<u>\$ 987,878</u>	<u>\$ 517,239</u>	<u>\$ 277,123</u>
Weighted average number of common shares outstanding	1,984,497,348	1,983,374,949	1,983,359,507
Earnings per share, basic and diluted:			
Net income	\$ 0.50	\$ 0.26	\$ 0.14

The accompanying notes to consolidated financial statements are an integral part of these consolidated statements.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

(Amounts in thousands of U.S. dollars, except share amounts)

	Common Stock		Treasury Stock		Other comprehensive income	Additional Paid-in Capital	Unearned Compensation	Shareholder Receivable	Retained Earnings	Total
	Shares	Amount	Shares	Amount						
<b>BALANCES, December 31, 2001</b>	1,993,326,138	\$ 50,558	(9,966,631)	\$ (10,206)	\$ -	\$ 555,794	\$ -	\$ (38,958)	\$ 461,091	\$ 1,018,279
Receivable from Sistema (Note 11):	-	-	-	-	-	-	-	-	-	-
Increases for interest	-	-	-	-	-	2,073	-	(2,073)	-	-
Payments from Sistema	-	-	-	-	-	-	-	6,619	-	6,619
Issuance of stock options (Note 16)	-	-	-	-	-	235	(235)	-	-	-
Amortization of deferred compensation (Note 16)	-	-	-	-	-	-	23	-	-	23
Dividends declared	-	-	-	-	-	-	-	-	-	-
Translation adjustment	-	-	-	-	-	-	-	-	-	-
Net income	-	-	-	-	-	-	-	-	277,123	277,123
<b>BALANCES, December 31, 2002</b>	1,993,326,138	\$ 50,558	(9,966,631)	\$ (10,206)	-	\$ 558,102	\$ (212)	\$ (34,412)	\$ 738,214	\$ 1,302,044
Receivable from Sistema (Note 11):	-	-	-	-	-	-	-	-	-	-
Increases for interest	-	-	-	-	-	807	-	(807)	-	-
Payments from Sistema	-	-	-	-	-	-	-	7,609	-	7,609
Issuance of stock options (Note 16)	-	-	-	-	-	1,002	(1,002)	-	-	-
Stock options exercised (Note 16)	-	-	37,557	9	-	-	-	-	-	9
Amortization of deferred compensation (Note 16)	-	-	-	-	-	-	345	-	-	345
Dividends declared (Note 1)	-	-	-	-	-	-	-	-	(110,931)	(110,931)
Translation adjustment	-	-	-	-	7,595	-	-	-	-	7,595
Net income	-	-	-	-	-	-	-	-	517,239	517,239
<b>BALANCES, December 31, 2003</b>	1,993,326,138	\$ 50,558	(9,929,074)	\$ (10,197)	\$ 7,595	\$ 559,911	\$ (869)	\$ (27,610)	\$ 1,144,522	\$ 1,723,910
Receivable from Sistema (Note 11):	-	-	-	-	-	-	-	-	-	-
Increases for interest	-	-	-	-	-	1,190	-	(1,190)	-	-
Payments from Sistema	-	-	-	-	-	-	-	10,563	-	10,563
Issuance of stock options (Note 16)	-	-	-	-	-	1,811	(1,811)	-	-	-
Stock options exercised (Note 16)	-	-	2,726,966	2,801	-	1,248	-	-	-	4,049
Amortization of deferred compensation (Note 16)	-	-	-	-	-	-	900	-	-	900
Dividends declared (Note 1)	-	-	-	-	-	-	-	-	(218,826)	(218,826)
Translation adjustment	-	-	-	-	15,361	-	-	-	-	15,361
Change in fair value of interest rate swaps, net of taxes	-	-	-	-	(512)	-	-	-	-	(512)
Net income	-	-	-	-	-	-	-	-	987,878	987,878
<b>BALANCES, December 31, 2004</b>	1,993,326,138	\$ 50,558	(7,202,108)	\$ (7,396)	\$ 22,444	\$ 564,160	\$ (1,780)	\$ (18,237)	\$ 1,913,574	\$ 2,523,323

The accompanying notes to consolidated financial statements are an integral part of these statements.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002 (Amounts in thousands of U.S. dollars)

	Years ended December 31,		
	2004	2003	2002
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income	\$ 987,878	\$ 517,239	\$ 277,123
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>			
Minority interest	30,342	71,677	39,475
Depreciation and amortization	675,729	415,916	209,680
Amortization of deferred connection fees	(46,978)	(29,372)	(24,854)
Equity in net income of associates	(24,146)	(2,670)	-
Inventory obsolescence expense	4,610	3,307	5,614
Provision for doubtful accounts	26,459	32,633	7,047
Deferred taxes	(76,023)	(43,001)	(18,989)
Non-cash expenses associated with stock bonus and stock options	900	213	23
<b>Changes in operating assets and liabilities:</b>			
Increase in accounts receivable	(101,223)	(64,384)	(20,305)
Increase in inventory	(24,179)	(14,737)	(18,186)
Increase in prepaid expenses and other current assets	(18,571)	(19,151)	(10,056)
Increase in VAT receivable	(55,044)	(50,230)	(64,154)
Increase in trade accounts payable, accrued liabilities and other current liabilities	331,835	148,544	30,354
<b>Net cash provided by operating activities</b>	<b>1,711,589</b>	<b>965,984</b>	<b>412,772</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Acquisitions of subsidiaries, net of cash acquired	(355,744)	(667,206)	(143,396)
Purchases of property, plant and equipment	(1,204,400)	(839,165)	(502,054)
Purchases of intangible assets	(154,544)	(119,606)	(72,218)
Purchases of short-term investments	(114,440)	(215,000)	-
Proceeds from sale of short-term investments	286,340	-	55,304
Investments in and advances to associates	(413)	(69,110)	(35,557)
<b>Net cash used in investing activities</b>	<b>(1,543,201)</b>	<b>(1,910,087)</b>	<b>(697,921)</b>

The accompanying notes to consolidated financial statements are an integral part of these statements.



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002 (Amounts in thousands of U.S. dollars)

	Years ended December 31,		
	2004	2003	2002
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Proceeds from stock options exercised	4,049	-	-
Proceeds from issuance of notes	-	1,097,000	50,808
Repayment of notes	(600,000)	-	-
Notes and debt issuance cost	(12,039)	(9,556)	(649)
Capital lease obligation principal paid	(15,274)	(22,646)	(1,804)
Dividends paid including taxes	(232,662)	(110,864)	-
Proceeds from loans	1,177,556	712,716	52,851
Loan principal paid	(320,511)	(677,374)	(7,008)
Payments from Sistema	9,654	8,269	6,619
<b>Net cash provided by financing activities</b>	<b>10,773</b>	<b>997,545</b>	<b>100,817</b>
Effect of exchange rate changes on cash and cash equivalents	4,613	2,273	(636)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS:</b>	<b>183,774</b>	<b>55,715</b>	<b>(184,968)</b>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<b>90,376</b>	<b>34,661</b>	<b>219,629</b>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<b>\$ 274,150</b>	<b>\$ 90,376</b>	<b>\$ 34,661</b>
<b>SUPPLEMENTAL INFORMATION:</b>			
Income taxes paid	\$ 430,109	\$ 286,016	\$ 147,346
Interest paid	\$ 142,899	\$ 79,824	\$ 43,438
<b>Non-cash investing activities:</b>			
Additions to network equipment and software under capital lease	\$ 2,861	\$ 10,928	\$ 18,917
Payable related to business acquisition (Note 3)	\$ -	\$ 27,500	\$ -
Additions to network through Hermes financing	\$ 8,800	\$ -	\$ -

The accompanying notes to consolidated financial statements are an integral part of these statements.

# OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

### 1. DESCRIPTION OF BUSINESS

**Business of the Group** – OJSC Mobile TeleSystems and its subsidiaries (“MTS” or the “Group”) is the leading provider of wireless telecommunication services in the Russian Federation (“RF”), Ukraine and Uzbekistan in terms of the number of subscribers and revenues. The Group has operated primarily in the GSM standard since 1994.

Open Joint-Stock Company Mobile TeleSystems (“MTS OJSC” or the “Company”) was created on March 1, 2000, through the merger of Closed Joint-Stock Company Mobile TeleSystems (“MTS CJSC”) and RTC CJSC, a wholly-owned subsidiary. MTS CJSC was formed in 1993 to design, construct and operate a cellular telecommunications network in Moscow and the Moscow region. The development of the network was achieved through green-field build-out in the regions for which the company was granted 900 or 1800 MHz (“GSM-900” and “GSM-1800”) cellular licenses or through the acquisition of majority stakes in local GSM operators (see Note 20 Operating Licenses and Note 3 Businesses Acquired).

The Company’s shares are traded in the form of American Depositary Shares (“ADS”). Each ADS represents 20 shares of common stock of the Company. The Company issued a total of 17,262,204 ADS, representing 345,244,080 common shares.

**Ownership** – As of December 31, 2004 and December 31, 2003, MTS’ shareholders of record and their respective percentage direct interests were as follows:

	December 31,	
	2004	2003
Joint-Stock Financial Corporation “Sistema” (“Sistema”)	41.0%	41.0%
T-Mobile Worldwide Holding GmbH (“T-Mobile”)	10.1%	25.4%
VAST, Limited Liability Company (“VAST”)	3.1%	3.1%
Invest-Svyaz-Holding, Closed Joint-Stock Company	8.0%	8.0%
ADS Holders	21.7%	17.4%
GDR Holders and Others	16.1%	5.1%
	<u>100.0%</u>	<u>100.0%</u>

In March 2003, Sistema and T-Mobile (together, “the Shareholders”) entered into a call option agreement, pursuant to which T-Mobile granted Sistema the option to acquire from it 199,332,614 shares of MTS, representing 10.0% of outstanding common stock of MTS. On April 26, 2003, Sistema exercised its option with T-Mobile to purchase an additional 6.0% of the outstanding common stock of MTS and purchased T-Mobile’s 49.0% interest in Invest-Svyaz-Holding, bringing its interest in Invest-Svyaz-Holding to 100.0%. Concurrently with this transaction, T-Mobile sold its holding of 5.0% in MTS on the open market in the form of Global Depositary Receipts (“GDRs”) listed on the London Stock Exchange.

In December 2004 T-Mobile sold 15.09% stake in MTS on the open market in form of the GDR’s.

Sistema owns a 51.0% equity interest in VAST, a limited liability company incorporated under the laws of the Russian Federation; the remaining 49.0% interest is held by ASVT, a Russian open joint-stock company. Sistema’s effective ownership in MTS is 50.6% at December 31, 2004 and December 31, 2003.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

In April 2003, Sistema issued \$350.0 million 10.25% notes, due in 2008. These notes are collateralized by 193,473,900 shares of common stock of MTS OJSC.

On June 30, 2003, the Group approved cash dividends of \$1.12 per ADS (\$0.056 per share) for a total of \$111.0 million. As of December 31, 2004 dividends were fully paid.

On November 28, 2003, common shares of MTS OJSC were included by the Board of Moscow Interbank Currency Exchange ("MICEX") into the MICEX "B" Quotation List.

On June 24, 2004, MTS' shareholders approved cash dividends totaling \$220.0 million (\$2.2 per ADS), including \$ 1.1 million related to treasury stock, which were fully paid by December 31, 2004.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND NEW ACCOUNTING PRONOUNCEMENTS

**Accounting Principles** – MTS maintains its accounting books and records in Russian rubles for its subsidiaries located in the Russian Federation ("RF"), in Ukrainian hryvnias for Ukrainian Mobile Communications ("UMC"), and Uzbek som for Uzdurobita based on respective local accounting and tax legislations. The accompanying consolidated financial statements have been prepared in order to present MTS' financial position and its results of operations and cash flows in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") and expressed in terms of U.S. dollars.

The accompanying consolidated financial statements differ from the financial statements used for statutory purposes in that they reflect various adjustments, not recorded on the entities' books, which are appropriate to present the financial position, results of operations and cash flows in accordance with U.S. GAAP. The principal adjustments are related to revenue recognition, foreign currency translation, deferred taxation, consolidation, acquisition accounting and depreciation and valuation of property and equipment and intangible assets.

**Basis of Consolidation** – Wholly-owned subsidiaries and majority-owned subsidiaries where the Company has operating and financial control are consolidated. Those ventures where the Company exercises significant influence, but does not have operating and financial control are accounted for using the equity method. All significant intercompany accounts and transactions are eliminated upon consolidation. The Company's share in net income of unconsolidated affiliates is included in other income in the accompanying consolidated statements of operations and disclosed in Note 19. Results of operations of subsidiaries acquired are included in the consolidated statements of operations from the date of their acquisition.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

As of December 31, 2004 and 2003, MTS has investments in the following significant legal entities:

	Accounting Method	December 31,	
		2004	2003
ACC	Consolidated	100.0%	100.0%
Telecom XXI	Consolidated	100.0%	100.0%
Telecom-900	Consolidated	100.0%	100.0%
SCS-900	Consolidated	100.0%	88.5%
FECS-900	Consolidated	100.0%	60.0%
Uraltel	Consolidated	99.8%	99.8%
MTS Finance (1)	Consolidated	100.0%	100.0%
BM Telecom	Consolidated	100.0%	100.0%
Kuban-GSM	Consolidated	100.0%	100.0%
Dontelecom	Consolidated	100.0%	100.0%
MTS-Barnaul	Consolidated	100.0%	100.0%
BIT	Consolidated	100.0%	100.0%
MTS-Capital	Consolidated	100.0%	100.0%
UMC	Consolidated	100.0%	100.0%
Sibchallenge	Consolidated	100.0%	100.0%
TSS	Consolidated	100.0%	100.0%
Volgograd Mobile	Consolidated/Equity	100.0%	50.0%
Astrakhan Mobile	Consolidated/Equity	100.0%	50.0%
Mar Mobile GSM	Consolidated	100.0%	100.0%
Primtelefon	Consolidated/Equity	100.0%	50.0%
MSS	Consolidated	91.0%	83.5%
ReCom	Consolidated	53.9%	53.9%
TAIF Telcom	Consolidated	100.0%	52.7%
UDN-900	Consolidated	100.0%	51.0%
Novitel	Consolidated	100.0%	51.0%
MTS-Kostroma	Consolidated	100.0%	100.0%
MTS-NN	Consolidated	100.0%	65.0%
Uzdunrobita	Consolidated	74.0%	-
Sibintertelecom	Consolidated	93.5%	-
Gorizont-RT	Consolidated	76.0%	-
Telesot Alania	Consolidated	52.5%	-
MTS-Komi Republic	Equity	26.0%	26.0%
MTS Belarus	Equity	49.0%	49.0%
MTS Tver	Equity	26.0%	26.0%

(1) Represents beneficial ownership.

**Translation Methodology** – Management uses the U.S. dollar as the functional currency for MTS OJSC and the most of its subsidiaries because the majority of their revenues, costs, property, plant and equipment and intangible assets purchases, and debt are either priced, incurred, payable or otherwise measured in U.S. dollars. Each of the legal entities domiciled in Russia, Ukraine, Uzbekistan and Belarus maintains its records and prepares its financial statements in the local currency, either Russian ruble, Ukrainian hryvnia, Uzbek som or Belarusian ruble, in accordance with the requirements of local statutory accounting and tax legislation.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

Translation (re-measurement) of financial statements denominated in local currencies into U.S. dollars has been performed in accordance with the provisions of Statement of Financial Accounting Standard ("SFAS") No. 52 "Foreign currency translation":

- For subsidiaries of the Group, where functional currency is the U.S. dollar, monetary assets and liabilities have been translated at the period end exchange rates. Non-monetary assets and liabilities have been translated at historical rates. Revenues, expenses and cash flows have been translated at historical rates. Translation differences resulting from the use of these rates have been accounted for as foreign currency gains and losses in the accompanying consolidated statements of operations.
- For UMC and Kuban-GSM where functional currency is the local currency, Ukrainian hryvnia and Russian ruble, respectively, all year end balance sheet items have been translated into U.S. dollars at the period end exchange rate. Revenues and expenses have been translated at period average exchange rate. In addition, a "new cost basis" for all non-monetary assets of Kuban-GSM has been established as of January 1, 2003, when the Russian economy ceased to be considered hyperinflationary. Cumulative translation adjustment related to the translation of UMC and Kuban-GSM, in the amount of \$22.4 million, net of income taxes, was reported as accumulated other comprehensive income in the accompanying consolidated balance sheet at December 31, 2004.

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

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

**Cash and Cash Equivalents** – Cash represents cash on hand and in MTS' bank accounts and short-term investments having original maturities of less than three months.

**Short-term Investments** – Short-term investments represent investments in term deposits, which have original maturities in excess of three months but less than twelve months. These investments are being accounted for at cost.

**Allowance for Doubtful Accounts** – MTS provides an allowance for doubtful accounts based on management's periodic review for recoverability of accounts receivable from customers and other receivables.

**Prepaid Expenses** – Prepaid expenses are primarily comprised of advance payments made for inventory and services to vendors.

**Inventory** – Inventory, accounted for at cost, determined by the first-in, first-out, or FIFO method, consists of telephones and accessories held for sale and spare parts to be used for equipment maintenance within next twelve months and other inventory items.

Telephones and accessories held for sale are written down to their market values based on specific periodic reviews and are expensed as cost of equipment sold.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**Value-added Tax (“VAT”)** – Value-added tax related to sales is payable to the tax authorities on an accrual basis based upon invoices issued to the customer. VAT incurred for purchases may be reclaimed from the state, subject to certain restrictions, against VAT related to sales.

**Property, Plant and Equipment** – Property, plant and equipment, including improvements that extend useful lives, are stated at cost. Property, plant and equipment with a useful life of more than one year is capitalized at historical cost and depreciated on a straight-line basis over its expected useful life as follows:

Network and base station equipment	5 – 12 years
Leasehold improvements	shorter of 8 - 10 years or lease term
Office equipment and computers	5 years
Buildings	50 years
Vehicles	4 years

Construction in progress and equipment held for installation is not depreciated until the constructed or installed asset is ready for its intended use.

Maintenance and repair costs are expensed as incurred, while upgrades and improvements are capitalized.

As a result of recent financial statement restatements by numerous U.S. public companies and publication of a letter by the Chief Accountant of the SEC regarding the interpretation of longstanding lease accounting principles, MTS has corrected its accounting practices for the leasehold improvements in the fourth quarter of 2004. The primary effect of this accounting correction was to accelerate to earlier periods depreciation expenses with respect to certain components of previously capitalized leasehold improvements.

These corrections resulted in a cumulative, net charge to net income of \$34.9 million in the fourth quarter of 2004, of which \$21.5 million relates to the years 1998 through 2003. The net cumulative charge is comprised of a \$44.5 million increase in depreciation expense related primarily to depreciation of capitalized leasehold improvements expenses for base stations; a decrease of \$1.4 million in the equity net income from the MTS-Belarus also related to depreciation of capitalized leasehold improvements expenses for base stations positions; and increase of \$11.0 million related to additional deferred tax benefit due to the change in accounting base for property, plant and equipment.

All components of the net charge are non-cash and do not impact historical or future cash flows or the timing of payments under the related leases.

**Asset Retirement Obligations** - In accordance with Statement of Financial Accounting Standards, or SFAS, No. 143, “Accounting for Asset Retirement Obligations, the Group calculates an asset retirement obligation and an associated asset retirement cost when the Group has a legal obligation in connection with the retirement of tangible long-lived assets. The Group’s obligations under SFAS No. 143 arise from certain of its leases and relate primarily to the cost of removing equipment from such lease sites. As of December 31, 2004 the estimated assets retirement obligations were not significant to the Group’s consolidated financial position and results of operations.

**License Costs** – License costs are capitalized as a result of (a) purchase price allocated to licenses acquired in business combinations and (b) licenses purchased directly from government organizations, which require license payments.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

Current operating licenses of the Group do not provide for automatic renewal upon expiration. As the Group and the industry do not have sufficient experience with the renewal of licenses, license costs are being amortized during the initial license period without consideration of possible future renewals, subject to periodic review for impairment, on a straight-line basis over three to ten years starting from the date such license becomes commercially operational.

***Other Intangible Assets and Goodwill*** – Intangible assets represent various purchased software costs, telephone numbering capacity, acquired customer base and rights to use premises. A part of the rights to use premises was contributed by shareholders to the Group's charter capital. Telephone numbering capacity costs with finite contractual life are being amortized over five to ten years and the rights to use premises are being amortized over ten years. Amortization of numbering capacity costs starts immediately upon the purchase of numbering capacity. Telephone numbering capacity with unlimited contractual life is not amortized, but is reviewed, at least annually, for impairment in accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets." ("SFAS No. 142")

Software costs are amortized over four years. Acquired customer bases are amortized over their estimated average subscriber life from 20 to 76 months. Other intangible assets are being amortized over three to four years. All finite-life intangible assets are being amortized using the straight-line method.

Goodwill represents an excess of the cost of business acquired over the fair market value of identifiable net assets at the date of acquisition.

Goodwill is reviewed for impairment at least annually or whenever it is determined that one or more impairment indicators exist. The Group determines whether an impairment has occurred by assigning goodwill to the reporting unit identified in accordance with SFAS No. 142, and comparing the carrying amount of the reporting unit to the fair value of the reporting unit. If a goodwill impairment has occurred, the Group recognizes a loss for the difference between the carrying amount and the implied fair value of goodwill. To date, no impairment of goodwill has occurred.

***Leasing Arrangements*** – The Group accounts for leases based on the requirements of SFAS No. 13, "Accounting for Leases." Certain subsidiaries of the Group lease operating facilities, which include switches, base stations and other cellular network equipment, as well as billing systems. For capital leases, the present value of future minimum lease payments at the inception of the lease is reflected as an asset and a liability in the balance sheet. Amounts due within one year are classified as short-term liabilities and the remaining balance as long-term liabilities.

***Subscriber Acquisition Costs*** – Subscriber acquisition costs represent the direct costs paid for each new subscriber enrolled through MTS' independent dealers. MTS expenses these costs as incurred.

***Investments Impairment*** – Management periodically assesses the realizability of the carrying values of the investments and if necessary records impairment losses to write the investment down to fair value. For the three years in the period ended December 31, 2004, no such impairment has occurred.

***Debt Issuance Costs*** – Debt issuance costs are amortized using the effective interest method over the terms of the related debt.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

***Impairment of Long-Lived Assets*** – MTS periodically evaluates the recoverability of the carrying amount of its long-lived assets in accordance with SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets.” Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, MTS compares undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, MTS records impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets. No impairment of long-lived assets has occurred during the three years in the period ended December 31, 2004.

***Subscriber Prepayments*** – MTS requires the majority of its customers to pay in advance for telecommunication services. All amounts received in advance of service provided are recorded as a subscriber prepayment liability and are not recorded as revenues until the related services have been provided to the subscriber.

***Revenue Recognition*** – Revenues are recognized on an accrual basis, when services are actually provided or title to equipment passes to customer, regardless of when the resulting monetary or financial flow occurs.

MTS categorizes the revenue sources in the statements of operations as follows:

- Service revenue and connection fees: (a) subscription fees, (b) usage charge, (c) value added service fees, (d) roaming fees charged to other operators for guest roamers utilizing MTS’ network, (e) connection fees and (f) prepaid phone cards;
- Sales of handsets and accessories.

***Subscription Fees*** – MTS recognizes revenues related to the monthly network fees in the month that the wireless service is provided to the subscriber.

***Usage Charges and Value Added Services Fees*** – Usage charges consist of fees based on airtime used by subscriber, the destination of the call and the service utilized.

Value added service fees are based on usage of airtime or volume of data transmitted for value added services, such as short message services, internet usage and data services. MTS recognizes revenues related to usage charges and value added services in the period when services are rendered.

***Roaming Fees*** – MTS charges roaming per-minutes fees to other wireless operators for non-MTS subscribers utilizing MTS’ network. MTS recognizes such revenues when the services are provided.

***Connection Fees*** – MTS defers initial connection fees on its prepaid and postpaid tariff plans from the moment of initial signing of the contract with subscribers over the estimated average subscriber life. Prior to December 31, 2003 the Group estimated that the average expected term of the subscriber relationship ranged from 39 to 47 months.

Based on management analysis of the subscriber base in the regions the Group operates, churn periods effective January 1, 2004, have been changed accordingly. Commencing January 1, 2004 the Group calculates an average expected term of the subscriber relationship for each region and amortizes regional connection fees accordingly. Average expected subscriber life ranges from 20 to 76 months. The effect of change in estimate in 2004 was approximately \$8.5 million, net of income tax or \$0.004 per share.



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

**Prepaid Phone Cards** – MTS sells prepaid phone cards to subscribers, separately from the handsets. These cards allow subscribers to make a predetermined allotment of wireless phone calls and/or take advantage of other services offered by the Group, such as short messages and sending or receiving faxes.

At the time that the prepaid phone card is purchased by a subscriber, MTS records the receipt of cash as a subscriber prepayment. The Group recognizes revenues from the sale of phone cards in the period when the subscriber uses airtime under the phone card. Unused airtime on sold phone cards is not recognized as revenues until the related services have been provided to the subscriber or the prepaid phone card expired.

Recently MTS introduced a new line of prepaid service tariff plans, whereby a customer may purchase a package that allows a connection to the MTS network and a predetermined allotment of wireless phone calls and/or other services offered by the Group. Revenues under these plans are allocated between connection fees and service fees based on their relative fair values.

**Sales of Handsets and Accessories** – MTS sells handsets and accessories to customers who are entering into contracts for service and also as separate distinct transactions. The Group recognizes revenues from the sale of handsets and accessories when a title for product passes to the customer. MTS records estimated returns as a direct reduction of sales at the time the related sales are recorded. The costs of handsets and accessories, whether sold to subscribers through the distribution channel or as part of the service contract, are expensed when title passes to the customer.

In Ukraine, MTS also from time to time sells handsets at prices below cost. MTS recognizes these subsidies in cost of equipment when the sale is recorded.

**Expense Recognition** – Expenses incurred by MTS in relation to the provision of wireless communication services mainly relate to interconnection and line rental costs, roaming expenses, costs of handsets and other accessories sold, depreciation and amortization and maintenance of the network.

Calls made by subscribers from areas outside of territories covered by the Group licenses are subject to roaming fees charged by the wireless provider in those territories. These fees are recorded as roaming expenses, as MTS acts as the principal in the transaction with subscriber and bears the risk of non-collection from the subscriber. Roaming fees are charged to MTS subscribers based on Group's existing tariffs and are recorded as service revenues.

Any fees paid to dealers as commissions are recorded as a component of sales and marketing expenses.

**Taxation** – Deferred tax assets and liabilities are recognized for the expected future tax consequences of existing differences between financial reporting and tax reporting bases of assets and liabilities, and for the loss or tax credit carry-forwards using enacted tax rates expected to be in effect at the time these differences are realized. Valuation allowances are recorded for deferred tax assets for which it is more likely that these assets will not be realized.

**Advertising Costs** – Advertising costs are expensed as incurred. Advertising costs for the years ended December 31, 2004, 2003 and 2002 were \$159,035, \$102,018 and \$48,624, respectively, and are reflected as a component of sales and marketing expenses in the accompanying consolidated statements of operations.

**Government Pension Fund** – Subsidiaries of the Group contribute to the local state pension fund and social fund, on behalf of all its employees.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

In Russia, starting from January 1, 2001 all social contributions, including contributions to the pension fund, were substituted with a unified social tax (“UST”) calculated by the application of a regressive rate from 35.6% to 2% of the annual gross remuneration of each employee. UST is allocated to three social funds, including the pension fund, where the rate of contributions to the pension fund vary from 28% to 2%, respectively, depending on the annual gross salary of each employee. The contributions are expensed as incurred.

In Ukraine, the subsidiary of the Group is required to contribute a specified percentage of each employee payroll up to a fixed limit to the Ukrainian pension fund, unemployment fund and social security fund.

The Group does not participate in any pension funds other than described above.

**Earnings per Share** – Basic earnings per share (“EPS”) have been determined using the weighted average number of shares outstanding during the year. Diluted EPS reflect the potential dilution of stock options, granted to employees. There are 3,530,970 stock options outstanding as at December 31, 2004.

The following is the reconciliation of the share component for basic and diluted EPS with respect to the Group’s net income:

	<b>December 31,</b>		
	<b>2004</b>	<b>2003</b>	<b>2002</b>
Weighted average number of common share outstanding	1,984,497,348	1,983,374,949	1,983,359,507
Dilutive effect of stock options, as if exercised	<u>1,168,573</u>	<u>1,727,131</u>	<u>405,946</u>
Weighted average number of common shares and potential shares outstanding	<u>1,985,665,921</u>	<u>1,985,102,080</u>	<u>1,983,765,453</u>

**Fair Value of Financial Instruments** – The fair market value of financial instruments, consisting of cash and cash equivalents, accounts receivable and accounts payable, which are included in current assets and liabilities, approximates the carrying value of these items due to the short term nature of these amounts. As of December 31, 2004 the \$400 million Notes due in 2008 have fair value of 105.5% or \$422 million and the \$400 million Notes due in 2010 have fair value of 102.4% or \$410 million. As of December 31, 2004, fair value of other fixed rate debt including capital lease obligation approximated its carrying value. The fair value of variable rate debt approximates carrying value.

**Derivative Financial Instruments and Hedging Activities** – From time to time, in its acquisitions the Group uses derivative instruments, consisting of put and call options on all or part of the minority stakes of acquired companies, to defer payment of the purchase price and provide optimal acquisition structuring. In addition, in December 2004, the Group entered into two variable-to-fixed interest rate swap agreements to manage its exposure to changes in fair value of future cash flows of its variable-rate long term debt, which is caused by interest rate fluctuations. The Group does not use derivatives for trading purposes.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The Group accounts for its derivative financial instruments following the provisions of SFAS No. 133 “Accounting for Derivative Instruments and Hedging Activities” and SFAS No. 149 “Amendment of Statement 133 on Derivative Instruments and Hedging Activities.” All derivatives are recorded as either assets or liabilities in the consolidated balance sheets and measured at their respective fair values. The Group’s interest rate swap agreements are designated as a cash flow hedge and the hedging relationship qualifies for hedge accounting. The effective portion of the change in fair value of interest rate swap agreements is, accordingly, recorded in other comprehensive income and reclassified to interest expense when the hedged debt affects the interest expense. Changes in fair value of other derivative instruments are recognized in net income as those instruments were not designated as hedges.

At the inception of the hedge and on a quarterly basis, the Group performs an analysis to assess whether changes in cash flows of its interest rate swap agreements are deemed highly effective in offsetting changes in cash flows of the hedged debt. If at any time the correlation assessment will indicate that the interest rate swap agreements are no longer effective as a hedge, the Group will discontinue hedge accounting and all subsequent changes in fair value will be recorded in net income.

**Comprehensive income** – Comprehensive income is defined as net income plus all other changes in net assets from non-owner sources. The following is the reconciliation of other comprehensive income, net of tax for the years ended December 31, 2004, 2003 and 2002:

	Year ended December 31,		
	2004	2003	2002
Net Income	\$ 987,878	\$ 517,239	\$ 277,123
Translation Adjustment	15,361	7,595	-
Change in fair value of interest rate swaps, net of tax of \$123	(512)	-	-
Total Comprehensive Income	<u>\$ 1,002,727</u>	<u>\$ 524,834</u>	<u>\$ 277,123</u>

**Comparative Information** – Certain prior year amounts have been reclassified to conform to the current period presentation.

**Stock-based Compensation** – MTS accounts for stock options issued to employees, non-employee directors and consultants following the requirements of SFAS No. 123, “Accounting for Stock-Based Compensation” and SFAS No. 148 “Accounting for Stock Based Compensation – Transition and Disclosure, an amendment to FASB Statement No. 123.” Under the requirements of these statements, the Company elected to use intrinsic value of options on the measurement date as a method for accounting for compensation to employees and non-employee directors. Compensation to consultants is measured based on the fair value of options on the measurement date as determined using a binomial option-pricing model.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

If the Group had elected to recognize compensation costs based on the fair values of options at the date of the grant, net income and earning per share amounts would have been as follows:

	December 31,		
	2004	2003	2002
Net income as reported	\$ 987,878	\$ 517,239	\$ 277,123
Pro-forma effect of the application of fair value method of accounting	(1,078)	(727)	(460)
Pro-forma net income	<u>\$ 986,800</u>	<u>\$ 516,512</u>	<u>\$ 276,663</u>
Earnings per share – basic and diluted			
As reported	\$ 0.50	\$ 0.26	\$ 0.14
Pro-forma	\$ 0.50	\$ 0.26	\$ 0.14

***New and Recently Adopted Accounting Pronouncements*** – In January 2003, the Financial Accounting Standards Board, or FASB, issued FASB Interpretation No. 46, “Consolidation of Variable Interest Entities – an interpretation of ARB No. 51” (“FIN 46”), to address perceived weaknesses in accounting for entities commonly known as special-purpose or off-balance-sheet. In addition to numerous FASB Staff Positions written to clarify and improve the application of FIN 46, the FASB announced a deferral for certain entities, and an amendment to FIN 46 entitled FASB Interpretation No. 46R, “Consolidation of Variable Interest Entities” (FIN 46R). FIN 46 establishes consolidation criteria for entities for which “control” is not easily discernable under Accounting Research Bulletin No. 51, “Consolidated Financial Statements,” which is based on the premise that holders of the equity of an entity control the entity by virtue of voting rights.

FIN 46 provides guidance for identifying the party with a controlling financial interest resulting from arrangements or financial interests rather than from voting interests. FIN 46 defines the term variable interest entity, or VIE, and is based on the premise that if a business enterprise absorbs a majority of the VIE’s expected losses and/or receives a majority of its expected residual returns (measures of risk and reward), that enterprise (the primary beneficiary) has a controlling financial interest in the VIE. Under FIN 46, the assets, liabilities, and results of the activities of the VIE should be included in the consolidated financial statements of the primary beneficiary. The Group was required to apply the provisions of FIN 46R in the first quarter 2004. As the Group did not have any VIEs during the year ended December 31, 2004, the adoption of this new method of accounting for VIEs did not affect its financial condition or results of operations as of December 31, 2004.

In September 2004, EITF issued a final consensus on EITF Issue No. 04-1, “Accounting for Preexisting Relationships between the Parties to a Business Combination”. In this issue the EITF reached a consensus that a business combination between two parties having a preexisting relationship is a multiple-element transaction with one element being the business combination and the other element being the settlement of the preexisting relationship. This Issue requires certain additional disclosures for business combinations between parties with a preexisting relationship. EITF Issue No. 04-1 is effective for reporting periods beginning after October 13, 2004. The Group does not anticipate that the adoption of EITF Issue No. 04-1 will have a material impact on its financial position or results of operations.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

At the September 2004 meeting of the Emerging Issues Task Force, the SEC staff issued an announcement D-108 "Use of the residual method to value acquired assets other than goodwill" stating that companies must use the direct value method to determine the fair value of their intangible assets acquired in business combinations completed after September 29, 2004.

The SEC staff also announced that companies that currently apply the residual value approach for valuing intangible assets with indefinite useful lives for purposes of impairment testing, must use the direct value method by no later than the beginning of their first fiscal year after December 15, 2004.

As of December 31, 2004, the Group performed the annual impairment test to measure the fair value of our 900 and 1800 megahertz or MHz, licenses in its national footprint using the residual value approach. Under this new accounting guidance, the Group performed an impairment test to measure the fair value of our 900 and 1800 MHz licenses as of January 1, 2005 using the direct value method. Based on the assessment no impairment charge as of December 31, 2004 is required.

In December 2004, Financial Accounting Standards Board ("FASB") issued SFAS No. 123R (revised 2004), "Share-Based Payment." The statement is a revision of FASB Statement No. 123, "Accounting for Stock Based Compensation", and supersedes Accounting Principles Board, or APB, Opinion No. 25, "Accounting for Stock Issued to Employees." The statement focuses primarily on accounting for transactions in which the Group obtains employee services in share-based payment transactions. This statement requires a public company to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. This standard is scheduled to become effective in the first interim reporting period beginning after June 15, 2005. Assuming that the effective date is not delayed, the Group will apply this new standard to its interim reporting period beginning July 1, 2005. The Group has not yet determined the amount of impact on the consolidated statements of operations following adoption and subsequent to 2005 or the transition method the Group will use. The Group does not believe that results of the adoption of SFAS No. 123R will be significant to the consolidated financial position or results of operations.

In March 2005, the U.S. Securities and Exchange Commission, or SEC, released Staff Accounting Bulletin 107, "Share-Based Payments", or SAB 107. The interpretations in SAB 107 express views of the SEC staff, or staff, regarding the interaction between SFAS No. 123R and certain SEC rules and regulations, and provide the staff's views regarding the valuation of share-based payment arrangements for public companies. In particular, SAB 107 provides guidance related to share-based payment transactions with nonemployees, the transition from nonpublic to public entity status, valuation methods (including assumptions such as expected volatility and expected term), the accounting for certain redeemable financial instruments issued under share-based payment arrangements, the classification of compensation expense, non-GAAP financial measures, first-time adoption of SFAS No. 123R in an interim period, capitalization of compensation cost related to share-based payment arrangements, the accounting for income tax effects of share-based payment arrangements upon adoption of SFAS No. 123R, the modification of employee share options prior to adoption of SFAS No. 123R.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

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

### 3. BUSINESSES ACQUIRED

**Gorizont - RT Acquisition** – In December 2004, MTS completed transaction to acquire a 76.0% stake in Gorizont-RT, a GSM mobile phone operator in the Republic of Sakha (Yakutia) in the Far East of Russia, for cash consideration of \$53.2 million. Gorizont-RT holds licenses to provide GSM-900/1800 services in the Republic of Sakha (Yakutia). Commencing from the date of acquisition, MTS consolidates financial results of Gorizont-RT. The Gorizont-RT's customer base as at the date of acquisition was approximately 100,000 subscribers.

The acquisition was accounted for using the purchase method. The purchase price allocation was as follows:

Current assets	\$	3,820
Non-current asset		17,501
License costs		26,362
Customer base cost		1,050
Trade mark		153
Goodwill		20,214
Current liabilities		(4,949)
Non-current liabilities		(529)
Deferred taxes		(6,814)
Minority interest		(3,604)
Purchase price	\$	<u>53,204</u>

Goodwill is mainly attributable to economic potential of the market assuming low regional penetration level as of the date of acquisition.

**Sibintertelecom Acquisition** – In November 2004, MTS acquired a 93.53% stake in Sibintertelecom, mobile phone operator in Chita region and Aginsk-Buryatsk District in the Far-East of Russia, for cash consideration of \$37.4 million. Sibintertelecom holds license to provide 900 MHz services in Chita region and Aginsk-Buryatsk District in the Far-East of Russia. Sibintertelecom is the sole mobile service provider in two regions with a total population of 1.23 million. Commencing from the date of acquisition, MTS consolidates financial results of Sibintertelecom. The company's customer base as at the date of acquisition was approximately 100,000 subscribers.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The acquisition was accounted for using the purchase method of accounting. The purchase price allocation was as follows:

Current assets	\$	5,939
Non-current asset		6,966
License costs		29,555
Customer base cost		1,488
Trademark		465
Goodwill		10,376
Current liabilities		(9,523)
Deferred taxes		(7,668)
Minority interest		(190)
Purchase price	\$	<u>37,408</u>

Goodwill is mainly attributable to economic potential of the market assuming low regional penetration level as of the date of acquisition.

**Telesot Alania Acquisition** – In December 2004, MTS purchased a 52.5% stake in Telesot Alania, a GSM mobile phone operator in the Republic of North Ossetia in the Southern part of Russia, for cash consideration of \$6.2 million. Telesot Alania holds license to provide 1800/900 MHz services in the Republic of North Ossetia in the Southern part of Russia. Commencing from the date of acquisition, MTS consolidates financial results of Telesot Alania. Telesot Alania's customer base as at the date of acquisition was approximately 54,000 subscribers.

The acquisition was accounted for using the purchase method of accounting. The purchase price allocation was as follows:

Current assets	\$	2,229
Non-current asset		5,085
License costs		3,606
Customer base cost		90
Current liabilities		(767)
Deferred taxes		(887)
Minority interest		(3,110)
Purchase price	\$	<u>6,246</u>

License costs are amortized over the remaining contractual terms of the licenses of approximately 2 years and customer base is amortized over the average subscriber's life of approximately 60 months.

**Uzdunrobita Acquisition** – In July 2004, MTS entered into an agreement to acquire 74.0% of Uzbekistan mobile operator JV Uzdunrobita ("Uzdunrobita") for a cash consideration of \$126.4 million, including transaction costs of \$5.4 million. Acquisition was completed on August 1, 2004 and starting from this date Uzdunrobita's financial results are consolidated. Uzdunrobita holds licenses to provide GSM-1800 mobile communication services in the whole territory of Uzbekistan, which has a population of approximately 25.2 million. Uzdunrobita's customer base as of the date of acquisition was approximately 230,000 subscribers.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The acquisition was accounted for using the purchase method. The purchase price allocation for the acquisition was as follows:

Current assets	\$	5,950
Non-current assets		67,293
License costs		40,861
Customer base cost		958
Trademark		3,622
Goodwill		46,470
Current liabilities		(14,705)
Non-current liabilities		(1,356)
Deferred taxes		(6,384)
Minority interest		(16,308)
Purchase price	\$	<u>126,401</u>

Goodwill is mainly attributable to economic potential of the market assuming low penetration level as of the date of acquisition. License costs are amortized over the remaining contractual terms of the licenses of approximately 12 years and customer base is amortized over the average remaining subscriber's life of approximately 39 months.

MTS also entered into call and put option agreements with the existing shareholders of Uzdurobita to acquire the remaining 26.0% of common shares of the company. The exercise period for the call and put option is 36 months from the acquisition date. The call and put option agreements stipulate a minimum purchase price of \$37.7 million plus 5% per annum commencing from the acquisition date. Fair value of the option was \$4.0 million at December 31, 2004 and included in other current assets on the consolidated balance sheet.

***Primtelefon Acquisition*** – In June 2004, MTS purchased 50.0% of Far-Eastern operator CJSC Primtelefon (“Primtelefon”) for cash consideration of \$31.0 million, increasing its effective ownership to 100%, as 50% of Primtelefon's shares were controlled through Vostok Mobile, a wholly-owned subsidiary of MTS. Commencing from the date of acquisition of the second stake, MTS consolidates financial results of Primtelefon. Primtelefon holds licenses to provide GSM 900/1800 mobile cellular communications in the Far-East region of Russia. The company's customer base as of the date of acquisition of the controlling stake was approximately 216,000 subscribers.

The acquisition was accounted for using the purchase method. The purchase price allocation was as follows:

Current assets	\$	11,041
Non-current assets		16,809
License costs		21,891
Current liabilities		(7,488)
Non-current liabilities		(5,671)
Deferred taxes		(5,582)
Purchase price	\$	<u>31,000</u>

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 7 years and customer base is amortized over the average remaining subscriber's life of approximately 41 months.



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**Telecom-900 Acquisition** – In August 2001, MTS acquired 81% of the outstanding common stock of Telecom-900, a Russian closed joint-stock company, for a cash consideration of \$26.8 million from Sistema. Telecom-900 is the holding company for three regional mobile phone operators, Siberia Cellular System 900 CJSC (“SCS-900”), Uraltel CJSC (“Uraltel”), and Far East Cellular Systems 900 CJSC (“FECS-900”).

At the date of acquisition these companies had approximately 96,000 subscribers and licenses to provide GSM 900/1800 mobile services in the Novosibirsk region, Altai Republic, Sverdlovsk region and Khabarovsk region.

Telecom-900 acquisition was accounted for using the purchase method of accounting. The purchase price was allocated as follows:

Current assets	\$	12,136
Non-current assets		29,297
License costs		31,542
Current liabilities		(21,883)
Non-current liabilities		(10,626)
Deferred taxes		(7,754)
Minority interest		(5,900)
Purchase price	\$	<u>26,812</u>

In November 2002, MTS acquired the remaining 19% of Telecom-900 from Invest-Svyaz-Holding, a shareholder of the Group and a wholly-owned subsidiary of Sistema, for a cash consideration of \$6.9 million. The acquisition was accounted for using the purchase method of accounting. The allocation of the purchase price increased recorded license costs by \$2.7 million.

On August 13, 2003, Telecom-900, completed the purchase of the 43.7% and 2.95% stakes in Uraltel for a cash consideration of \$35.7 million. The transaction increased Telecom-900’s ownership in Uraltel to 99.85%. The acquisition was accounted using purchase method of accounting. The allocation of purchase price increased recorded license cost by \$24.5 million.

In November 2003, the Group completed the purchase of the 30.0% stake in SCS-900 from Sibirtelecom for cash consideration of \$28.6 million. The Group’s acquisition of this stake increased its ownership in SCS-900 to 81.0%. On December 29, 2003, the Group acquired for cash consideration of \$9.3 million a 100% stake in ILIT LLC, a company which owns a 7.5% stake in SCS-900, increasing its ownership in SCS-900 to 88.5%. The acquisition was accounted using purchase method of accounting. The allocation of purchase price increased recorded license cost by \$25.7 million.

In March 2004, the Group acquired 11.0% stake in SCS-900 from CJSC Sibirskie Zvezdy for cash consideration of \$8.5 million, increasing its ownership in SCS-900 to 99.5%. The acquisition was accounted for using a purchase method of accounting. The allocation of purchase price increased recorded license cost by \$2.6 million.

In April 2004, the Group acquired 40.0% stake in FECS-900 from OJSC Dalnevostochnaya Kompaniya Electrosvyazi for cash consideration of \$8.3 million, increasing its ownership in FECS-900 to 100.0%. The acquisition was accounted for using a purchase method of accounting. The allocation of purchase price increased recorded license cost by \$4.1 million.

License costs are amortized over the remaining contractual terms of the respective license, ranging from 6 to 10 years at the date of the first acquisition. Customer base is amortized over the average remaining subscribers life ranging from 32 to 40 months.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**Tomsk Cellular Communications Acquisition** – In September 2003, MTS purchased 100.0% of Siberian operator Tomsk Cellular Communications (“TSS”) for cash consideration of \$47.0 million. TSS holds licenses to provide GSM 900/1800 mobile cellular communications in the Tomsk region. The company’s customer base as of the date of acquisition was approximately 183,000 subscribers.

The acquisition was accounted for using the purchase method. The purchase price allocation was as follows:

Current assets	\$	3,299
Non-current assets		11,412
License costs		49,282
Current liabilities		(4,543)
Non-current liabilities		(105)
Deferred taxes		(12,345)
Purchase price	\$	<u>47,000</u>

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 8 years and customer base is amortized over the average remaining subscribers life of approximately 76 months.

**Sibchallenge Acquisition** – On August 22, 2003, MTS completed the purchase of 100.0% of Sibchallenge, a cellular operator in the Krasnoyarsk region, for cash consideration of \$45.5 million, paid a finder’s fee of \$2.0 million and assumed net debt of approximately \$6.6 million. Sibchallenge holds licenses to provide GSM 900/1800 and DAMPS mobile services in the Krasnoyarsk region of Siberia, the Republic of Khakasiya, and in the Taimyr Autonomous region, all of which are located in the Siberian part of Russia. At the date of acquisition, Sibchallenge had approximately 132,000 subscribers.

The purchase price allocation was as follows:

Current assets	\$	4,078
Non-current assets		16,678
License costs		52,625
Current liabilities		(6,405)
Non-current liabilities		(6,628)
Deferred taxes		(12,894)
Purchase price	\$	<u>47,454</u>

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 8 years and customer base is amortized over the average remaining subscribers life of approximately 36 months.

**Kuban-GSM Acquisition** – In March 2002, MTS acquired 51% of Kuban-GSM, a Russian closed joint-stock company, for cash consideration of \$71.4 million. At the date of acquisition, Kuban-GSM had approximately 500,000 subscribers and it operates in thirteen major cities throughout the south of the European part of the Russian Federation, including Sochi, Krasnodar and Novorossiisk. The Kuban-GSM acquisition was accounted for using the purchase method of accounting.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The purchase price was allocated as follows:

Current assets	\$ 11,751
Non-current assets	80,848
License costs	62,549
Customer base cost	3,561
Current liabilities	(31,289)
Non-current liabilities	(19,827)
Deferred taxes	(15,866)
Minority interest	(20,327)
Purchase price	<u>\$ 71,400</u>

In October 2002, MTS exercised its option to acquire additional 353 shares for \$5.0 million payable in cash, increasing its ownership in Kuban-GSM to 52.7%. The acquisition of the additional interest was accounted for using the purchase method of accounting. The allocation of the purchase price increased recorded license costs by \$4.4 million, increased customer base cost by \$0.2 million, and decreased minority interest by \$0.5 million.

In September 2003, the Group acquired 100.0% of Kubtelesot for cash consideration of \$107.0 million. Kubtelesot owned 47.3% of Kuban-GSM, and the Group's purchase of this stake increased its ownership in Kuban-GSM to 100.0%. Kubtelesot was a holding company with no operational activities. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price increased recorded license cost by \$57.5 million, increased customer base cost by \$8.4 million, and decreased minority interest by \$59.0 million.

In May 2004, Kubtelesot was liquidated and all its shares in Kuban-GSM were transferred to OJSC MTS as the only shareholder.

License costs are amortized over the remaining contractual term of the license of approximately 5 years at the date of the acquisition. Acquired customer base is amortized over the average remaining subscribers life of approximately 48 months.

**UMC Acquisition** – On March 4, 2003, MTS acquired 57.7% of the outstanding voting interest of UMC, a provider of mobile services in Ukraine, for cash consideration of \$199.0 million, including the acquisition of 16.3% of the outstanding voting interest from Deutsche Telekom AG, a related party, for \$55.0 million. Acquisition costs relating to the transaction of \$1.4 million were capitalized. In connection with the acquisition, MTS also assumed debt of UMC with face value of approximately \$65.0 million, with the fair value of approximately \$62.0 million. At the date of acquisition, UMC had approximately 1.8 million subscribers and was one of the two leading mobile operators in Ukraine, operating under nationwide GSM 900/1800 and NMT 450 licenses.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The acquisition was accounted for using the purchase method. For convenience, MTS consolidated UMC from March 1, 2003. Purchase price allocation is as follows:

Current assets	\$	82,293
Non-current assets		272,721
License costs		82,200
Customer base cost		30,927
Current liabilities		(63,551)
Non-current liabilities		(78,580)
Deferred taxes		(27,425)
Minority interest		(99,581)
Purchase price	\$	<u>199,004</u>

MTS paid \$171.5 million of the purchase price in cash and agreed to pay the balance of the purchase price of \$27.5 million to Cetel B.V., a wholly-owned subsidiary of Deutsche Telekom AG, within one year. The amount payable accrued interest of 9% per annum. In March 2004, MTS cash settled the balance payable to Cetel B.V.

MTS also had an option agreement with Ukrtelecom to purchase its remaining 26.0% stake in UMC, exercisable from February 5, 2003 to November 5, 2005, with an exercise price of \$87.6 million. On June 4, 2003, MTS exercised its call option. As a result of the transaction, MTS' ownership in UMC increased from 57.7% to 83.7%. The acquisition was accounted for using purchase method of accounting. The allocation of purchase price increased recorded license cost by \$10.2 million, increased customer base cost by \$13.9 million, and decreased minority interest by \$66.4 million.

In addition, MTS entered into a put and call option agreement with TDC Mobile International A/S ("TDC") for the purchase of its 16.3% stake in UMC. The exercise period of the call option was from May 5, 2003 to November 5, 2004, and the put option was exercisable from August 5, 2003 to November 5, 2004. The call option price was \$85.0 million plus interest accrued from November 5, 2002 to the date of the exercise at 11% per annum; the price of the put option was calculated based on reported earnings of UMC prior to the exercise and was subject to a minimum amount of \$55.0 million. On June 25, 2003, MTS notified TDC of its intent to exercise its rights under the put and call option agreement. The purchase was completed during July 2003. MTS paid cash consideration of approximately \$91.7 million to purchase the remaining 16.3% stake in UMC. The acquisition was accounted for using purchase method of accounting. The allocation of purchase price increased recorded license cost by \$52.7 million, increased customer base cost by \$8.7 million, and decreased minority interest by \$43.8 million.

The UMC license costs are amortized over the remaining contractual terms of the licenses of approximately 9 to 13 years at the date of the acquisition, acquired customer base is amortized over the average remaining subscriber's life of approximately 32 months. Other acquired intangible assets, represented mostly by software, are amortized over their respective useful lives of 3 to 10 years.

In accordance with SFAS No. 141 "Business Combinations," the Group recognized \$8.0 million of goodwill relating to workforce-in-place.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**TAIF Telcom Acquisition** – In April 2003, MTS acquired 51.0% of the common shares of TAIF Telcom, a Russian open joint-stock company, for cash consideration of \$51.0 million and 50.0% of the preferred shares of TAIF Telcom for cash consideration of \$10.0 million. In May 2003, MTS acquired an additional 1.7% of the common shares of TAIF Telcom for cash consideration of \$2.3 million. In connection with the acquisitions, MTS also assumed indebtedness of approximately \$16.6 million that was collateralized by telecom equipment.

MTS also entered into call and put option agreements with the existing shareholders of TAIF Telcom to acquire the remaining 47.3% of common shares and 50.0% of preferred shares of TAIF Telcom.

The exercise period for the call option on common shares is 48 months from the acquisition date and for the put option on common shares is 36 months following an 18 months period after the acquisition date. The call and put option agreements for the common shares stipulate a minimum purchase price of \$49.0 million plus 8% per annum commencing from the acquisition date. The exercise period for the call option on preferred shares is 48 months following a 24 months period after the acquisition date and for the put option on preferred shares it is a 24 months period after the acquisition date. The call and put option agreements for the preferred shares stipulate a minimum purchase price of \$10.0 million plus 8% per annum commencing from the acquisition date. Fair value of the option was \$3.5 million at December 31, 2003.

The purchase price allocation for initial stake acquired was as follows:

Current assets	\$	3,870
Non-current assets		48,391
License costs		68,407
Current liabilities		(26,099)
Non-current liabilities		(5,550)
Deferred taxes		(16,814)
Minority interest		(8,965)
Purchase price	\$	<u>63,240</u>

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 4 years and customer base is amortized over the average remaining subscribers' life of approximately 38 months.

TAIF Telcom provides mobile services in the GSM-900/1800 standard in the Republic of Tatarstan and in the Volga region of Russia. At the date of acquisition, TAIF Telcom had approximately 240,000 subscribers.

In September 2004, MTS exercised its option to acquire the remaining 47.3% of common shares and 50.0% of preferred shares in TAIF Telcom for cash consideration of \$63.0 million, increasing its ownership to 100.0%. The Group received title to the acquired shares in October 2004. The purchase price allocation increased recorded license cost by \$35.8 million, increased acquired customer base by \$4.2 million; goodwill was recorded in the amount of \$21.2 million. Goodwill is mainly attributable to economic potential of the market.

**Dontelecom Acquisition** – On September 26, 2002, MTS completed its acquisition of 66.7% of the outstanding common stock of Dontelecom, a closed joint-stock company, for cash consideration of \$15.0 million (including 33.3% acquired from Sistema for \$7.5 million). At the date of acquisition, Dontelecom had approximately 39,000 subscribers. Dontelecom holds a GSM-900/1800 license to operate in the Rostov region. This acquisition was accounted for using the purchase method.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The purchase price was allocated as follows:

Current assets	\$	3,422
Non-current assets		8,401
License costs		14,739
Current liabilities		(5,849)
Non-current liabilities		(357)
Deferred taxes		(3,675)
Minority interest		(1,681)
Purchase price	\$	<u>15,000</u>

In October 2002, the Group completed the acquisition of the remaining 33.3% of the outstanding common stock of Dontelecom for \$7.5 million. The acquisition was accounted for using the purchase method of accounting. The purchase increased the recorded license costs by \$7.3 million.

License costs are amortized over the remaining contractual term of the license of approximately 3 years at the date of the acquisition. Customer base is amortized over the average remaining subscribers life of approximately 20 months.

***BM Telecom Acquisition*** – In May 2002, MTS completed its acquisition of 100% of the outstanding common stock of Ufa-based BM Telecom, a closed joint-stock company, for \$41.0 million in cash. At the date of acquisition, BM Telecom had approximately 100,000 subscribers and it holds a GSM-900/1800 license to operate in Bashkortostan Republic of Russia. This acquisition was accounted for using the purchase method. The purchase price was allocated as follows:

Current assets	\$	3,312
Non-current assets		14,736
License costs		48,932
Current liabilities		(3,603)
Non-current liabilities		(10,227)
Deferred taxes		(12,150)
Purchase price	\$	<u>41,000</u>

License costs associated with the acquisition of BM Telecom are amortized over the remaining term of the license of approximately 5 years. Customer base is amortized over the average remaining subscribers life of approximately 30 months.

***Acquisitions of Various Regional Companies*** – In August 2003, the Group reached an agreement to acquire, in a series of related transactions, equity interests in five Russian regional mobile phone operators from MCT Corporation for a total of \$71.0 million. The Group agreed to purchase a 43.7% stake in Uraltel (described above) and 100.0% of Vostok Mobile BV, which holds a 50.0% stake in Primtelefon.

The Group also agreed to purchase Vostok Mobile South, which holds 50.0% stakes in Astrakhan Mobile and Volgograd Mobile, as well as an 80.0% stake in Mar Mobile GSM. The Group also entered into agreements to acquire the remaining 20.0% of Mar Mobile GSM and another 2.95% stake in Uraltel from existing shareholders unrelated to MCT Corporation for approximately \$1.0 million.

On August 26, 2003, the Group completed the acquisition of Vostok Mobile and recorded a 50.0% stake investment in Primtelefon using the equity method of accounting.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

On October 14, 2003, the Group completed the purchase of Vostok Mobile South and thus acquired a 50.0% stake in Volgograd Mobile and Astrakhan Mobile and an 80.0% stake in Mar Mobile GSM. Also, in a separate transaction the Group completed the acquisition of the remaining 20.0% stake in Mar Mobile GSM from existing shareholders unrelated to MCT Corporation, thus consolidating a 100.0% ownership in the company.

In August 2004, MTS acquired from UTK the remaining 50.0% stakes in Astrakhan Mobile and Volgograd Mobile, increasing its ownership to 100.0%. An acquisition price was paid in cash and amounted to \$1.1 million and \$2.9 million, respectively. Commencing from the date of acquisition financial results of both companies are consolidated into MTS financial statements. Astrakhan Mobile holds a 800/1800 MHz licenses covering Astrakhan region (population of approximately 1 million) and Volgograd Mobile holds a 800/1800 MHz licenses covering Volgograd region (population of approximately 2.7 million). As of July 31, 2004, two companies provided AMPS/DAMPS services to around 10 thousand subscribers. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price for the first and second stakes in both companies resulted in an increase in license cost by \$16.5 million.

In April 2004, MTS acquired from OJSC Sibirtelecom additional 7.5% stake in MSS, a company, which operates in the Omsk region, for \$2.2 million in cash. This acquisition increased MTS's ownership in MSS to 91%. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price increased recorded license cost by \$1.1 million.

In April and May of 2004, MTS acquired the remaining stakes in the following subsidiaries:

- 35% of MTS-NN (a service provider in Nizhny Novgorod) for \$0.5 million, and
- 49% of Novitel (handsets dealer in Moscow) for \$1.3 million.

Both acquisitions increased MTS's share in the respective companies to 100%. The acquisitions were accounted for using the purchase method of accounting. The allocation of purchase price increased recorded goodwill by \$1.8 million.

In August 2004, MTS acquired from OJSC Volgatelecom remaining 49% stake in UDN-900 for \$6.4 million in cash. This acquisition increased MTS's ownership in UDN to 100%. The allocation of purchase price increased recorded license cost by \$0.3 million. UDN-900 provides GSM 900 services under the MTS brand in Udmurtia Republic (population 1.6 million). UDN's subscriber base as of July 31, 2004 was 219,760.

***Pro Forma Results of Operations (unaudited)*** – The following unaudited pro forma financial data for the years ended December 31, 2004 and 2003, give effect to the acquisitions of Uzdurobita, Primatelefon and other various regional companies as if they had occurred at January 1, 2003.

	December 31,	
	2004	2003
Pro forma:		
Net revenues	\$ 3,986,932	\$ 2,636,072
Net operating income	1,440,480	936,174
Net income	972,362	495,411
Earnings per share, basic and diluted	\$ 0.49	\$ 0.25

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The pro forma information is based on various assumptions and estimates. The pro forma information is not necessarily indicative of the operating results that would have occurred if the Group acquisitions had been consummated as of January 1, 2003, nor is it necessarily indicative of future operating results. The pro forma information does not give effect to any potential revenue enhancements or cost synergies or other operating efficiencies that could result from the acquisitions. The actual results of operations of these companies are included in the consolidated financial statements of the Group only from the respective dates of acquisition.

#### 4. CASH AND CASH EQUIVALENTS

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

	December 31,	
	2004	2003
U.S. dollar current accounts	\$ 107,172	\$ 20,130
U.S. dollar term deposits	45,295	886
Ruble current accounts	90,527	40,597
Ruble deposits	2,596	20,201
Hryvnia current accounts	10,190	1,371
Uzbek som deposit accounts	15,106	-
Uzbek som current accounts	715	-
Other	2,549	7,191
Total cash and cash equivalents	<u>\$ 274,150</u>	<u>\$ 90,376</u>

#### 5. SHORT-TERM INVESTMENTS

Short-term investments, denominated in U.S. dollars, as of December 31, 2004 comprised of the following:

	Annual interest rate	Maturity date	December 31, 2004
OJSC Moscow Bank of Reconstruction and Development	8.4%	December 9, 2005	\$ 30,000
East-West United Bank S.A.	2.0%	April 04, 2005	23,100
OJSC Moscow Bank of Reconstruction and Development	8.4%	October 10, 2005	10,000
OJSC Moscow Bank of Reconstruction and Development	8.4%	December 14, 2005	10,000
Other			260
Total short-term investments			<u>\$ 73,360</u>



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

Short-term investments, denominated in U.S. dollars, as of December 31, 2003 comprised of the following:

	<u>Annual interest rate</u>	<u>Maturity date</u>	<u>December 31, 2003</u>
OJSC Moscow Bank of Reconstruction and Development	4.8%	February 2, 2004	\$ 200,000
OJSC Moscow Bank of Reconstruction and Development	8.4%	October 21, 2004	19,100
OJSC Moscow Bank of Reconstruction and Development	8.0%	October 4, 2004	10,000
OJSC Moscow Bank of Reconstruction and Development	8.4%	November 23, 2004	5,000
OJSC Moscow Bank of Reconstruction and Development	8.4%	December 5, 2004	5,900
OJSC Moscow Bank of Reconstruction and Development	8.4%	December 20, 2004	5,000
Total short-term investments			<u>\$ 245,000</u>

OJSC Moscow Bank of Reconstruction and Development is a related party (see also Note 17).

#### 6. TRADE RECEIVABLES, NET

Trade receivables as of December 31, 2004 and 2003 were as follows:

	<u>December 31,</u>	
	<u>2004</u>	<u>2003</u>
Accounts receivable, subscribers	\$ 154,453	\$ 87,149
Accounts receivable, roaming	24,731	26,500
Allowance for doubtful accounts	(16,659)	(13,698)
Trade receivables, net	<u>\$ 162,525</u>	<u>\$ 99,951</u>

The following table summarizes the changes in the allowance for doubtful accounts for the years ended December 31, 2004, 2003 and 2002:

	<u>December 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Balance, beginning of the year	\$ 13,698	\$ 6,270	\$ 5,187
Provision for doubtful accounts	26,459	32,633	7,047
Accounts receivable written off	(23,498)	(25,205)	(5,964)
Balance, end of the year	<u>\$ 16,659</u>	<u>\$ 13,698</u>	<u>\$ 6,270</u>

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 7. INVENTORY

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

	December 31,	
	2004	2003
Spare parts for base stations	\$ 14,775	\$ 26,635
Handsets and accessories	30,574	23,499
Other inventory	44,169	17,157
Total Inventory	<u>\$ 89,518</u>	<u>\$ 67,291</u>

Obsolescence expense for the years ended December 31, 2004, 2003 and 2002 amounted to \$4,610, \$3,307 and \$5,614, respectively, and was included in General and administrative expenses in the accompanying consolidated statements of operations. Spare parts for base stations included in inventory are expected to be utilized within 12 months period.

#### 8. PROPERTY, PLANT AND EQUIPMENT

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

	December 31,	
	2004	2003
Network and base station equipment (including leased network and base station equipment of \$67,905 and \$66,311, respectively) and related leasehold improvements	\$ 2,538,240	\$ 1,775,180
Office equipment, computers, software and other (including leased office equipment, computers and software of \$1,613 and \$1,923, respectively)	249,458	147,395
Buildings and related leasehold improvements	202,095	151,262
Vehicles	15,658	11,611
Property, plant and equipment, at cost	<u>3,005,451</u>	<u>2,085,448</u>
Accumulated depreciation (including accumulated depreciation on leased equipment of \$30,304 and \$23,343)	(901,416)	(532,268)
Equipment for installation	275,010	334,264
Construction in-progress	855,273	368,632
Property, plant and equipment, net	<u>\$ 3,234,318</u>	<u>\$ 2,256,076</u>

Depreciation expenses during the years ended December 31, 2004, 2003 and 2002 amounted to \$385.7, \$233.1 and \$116.0 million, respectively, including depreciation expenses for leased property, plant and equipment in the amount of \$5.4, \$7.6 and \$3.4 million, respectively.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 9. OTHER INTANGIBLE ASSETS

Intangible assets at December 31, 2004 and 2003 comprised of the following:

	Useful lives	December 31, 2004			December 31, 2003		
		Gross carrying value	Accumulated amortization	Net carrying value	Gross carrying value	Accumulated amortization	Net carrying value
<b>Amortized intangible assets</b>							
	20 to						
Acquired customer base	76 months	\$ 94,632	\$ (50,276)	\$ 44,356	\$ 81,289	\$ (18,307)	\$ 62,982
Rights to use premises	10 years	19,638	(12,393)	7,245	19,638	(10,476)	9,162
Numbering capacity with finite contractual life, software and other	3 to 10 years	474,921	(215,236)	259,685	338,222	(119,269)	218,953
		<u>589,191</u>	<u>(277,905)</u>	<u>311,286</u>	<u>439,149</u>	<u>(148,052)</u>	<u>291,097</u>
<b>Unamortized intangible assets:</b>							
Numbering capacity with indefinite contractual life		17,247	-	17,247	13,047	-	13,047
Total other intangible assets		<u>\$ 606,438</u>	<u>\$(277,905)</u>	<u>\$ 328,533</u>	<u>\$ 452,196</u>	<u>\$(148,052)</u>	<u>\$ 304,144</u>

As a result of a limited availability of local telephone numbering capacity in Moscow and the Moscow region, MTS has been required to enter into agreements for the use of telephone numbering capacity with several telecommunication operators in Moscow. Costs of acquiring numbering capacity with finite contractual life are amortized over period of five to ten years in accordance with the terms of the contract entered into to acquire such capacity. Numbering capacity with indefinite contractual life is not amortized.

The significant component of MTS' right to use premises was obtained in the form of contributions to its charter capital in 1993. These premises included MTS' administrative offices and facilities utilized for mobile switching centers. In addition and simultaneously with acquisition of UMC in 2003 the Group obtained some additional property rights.

Amortization expense for the years ended December 31, 2004, 2003 and 2002 amounted to \$129.9, \$69.2 and \$30.0 million, respectively. Based on the amortizable intangible assets existing at December 31, 2004, the estimated amortization expense is \$130.5 million during 2005, \$82.6 million during 2006, \$54.3 million during 2007, \$37.6 million during 2008, \$2.8 million during 2009 and \$3.5 million thereafter. Actual amortization expense to be reported in future periods could differ from these estimates as a result of new intangible assets acquisitions, changes in useful lives and other relevant factors.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 10. DEFERRED CONNECTION FEES

Deferred connection fees for the years ended December 31, 2004 and 2003 were as follows:

	December 31,	
	2004	2003
Balance at beginning of the year	\$ 46,644	\$ 41,904
Payments received and deferred during the year	93,082	34,112
Amounts amortized and recognized as revenue during the year	(46,978)	(29,372)
Balance at end of the year	92,748	46,644
Less current portion	45,083	21,467
Non-current portion	\$ 47,665	\$ 25,177

MTS defers initial connection fees paid by subscribers for the first time activation of network service as well as one time activation fees received for connection to various value added services. These fees are recognized as revenue over the estimated average subscriber life (see Note 2).

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 11. DEBT

At December 31, 2004 and 2003 debt comprised of the following:

	<u>Currency</u>	<u>Annual interest rate (Actual rate at December 31, 2004)</u>	<u>December 31, 2004</u>	<u>December 31, 2003</u>
9.75% Notes due 2008	USD	9.75%	\$ 400,000	\$ 400,000
8.38% Notes due 2010	USD	8.38%	400,000	400,000
10.95% Notes due 2004	USD	10.95%	-	299,640
Floating Rate Notes due 2004	USD	-	-	298,196
<b>Total notes</b>			<b>\$ 800,000</b>	<b>\$ 1,397,836</b>
<b>Less current portion</b>			<b>-</b>	<b>597,836</b>
<b>Total long-term notes</b>			<b>\$ 800,000</b>	<b>\$ 800,000</b>
Syndicated loan	USD	LIBOR+2.50% (5.28%)	\$ 600,000	\$ -
EBRD	USD	LIBOR+3.10% (5.88%)	150,000	-
CSFB	USD	LIBOR+2.20% (4.76%)	140,000	-
HSBC Bank plc & ING-BHF-Bank	USD	LIBOR+0.44% (3.21%)	77,003	-
Hermes Credit Facility	EUR	EURIBOR+0.65% (2.86%) LIBOR+2.25%-4.15%	63,851	55,550
ING Bank (Eurasia)	USD	(4.81%-6.71%)	46,667	60,000
HSBC	USD	LIBOR+2.75% (5.24%)	17,500	25,000
Ericsson	USD	LIBOR+4.00% (6.56%)	14,850	23,400
Deutsche Telekom AG and TDC Mobile International A/S	USD	-	-	14,819
Nordea Bank Sweden	USD	LIBOR+0.40% (3.18%)	6,499	-
West LB	EUR	EURIBOR+2.00% (4.22%)	4,000	5,092
KFW	EUR	EURIBOR+0.95% (3.16%)	1,478	4,313
Citibank	USD	LIBOR+1.15% (3.71%)	868	10,000
Dresdner	USD	-	-	15,400
AVAL bank	UAH	-	-	10,890
International Moscow Bank	RUR	-	-	10,864
MBRD	RUR	-	-	1,220
Ruble denominated debt	RUR	4.30%-16.50%	1,924	5,860
Other debt	USD	-	-	3,322
<b>Total debt</b>			<b>\$ 1,124,640</b>	<b>\$ 245,730</b>
<b>Less current portion</b>			<b>370,845</b>	<b>103,312</b>
<b>Total long-term debt</b>			<b>\$ 753,795</b>	<b>\$ 142,418</b>

**The Notes** – On December 21, 2001, MTS Finance S.A. (“MTS Finance”), a 100% beneficially owned subsidiary of MTS, registered under the laws of Luxembourg, issued \$250.0 million 10.95% (effective interest rate of 11.25%) notes at the price of 99.254%. Proceeds received from the notes, net of underwriting discount, were \$248.1 million. Related debt issuance costs in the amount of \$3.9 million were capitalized. On March 20, 2002, MTS Finance issued additional \$50.0 million 10.95% (effective interest rate of 10.25%) notes at a price of 101.616%. Proceeds received from these notes, including the offering premium, were \$50.8 million. Related debt issuance costs in the amount of \$0.6 million were capitalized. All the notes are fully and unconditionally guaranteed by MTS OJSC. MTS Finance made interest payments on the notes semi-annually in arrears on June 21 and December 21 of each year, commencing on June 21, 2002. The notes were listed on the Luxemburg Stock Exchange. In May 2002, these notes were registered with the SEC under the Securities Act of 1933. In December 2004, the Group redeemed all outstanding notes, mentioned above, in the principal amount plus accrued interest thereon to the date of redemption.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

On January 30, 2003, MTS Finance issued \$400.0 million 9.75% notes at par. These notes are fully and unconditionally guaranteed by MTS OJSC and mature on January 30, 2008. MTS Finance is required to make interest payments on the notes semi-annually in arrears on January 30 and July 30, commencing on July 30, 2003. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes were \$400.0 million and related debt issuance costs of \$3.9 million were capitalized.

On August 5, 2003, MTS Finance issued \$300.0 million notes bearing interest at floating rate 3 months LIBOR + 4.00% at the price of 99%. These notes were fully and unconditionally guaranteed by MTS OJSC and matured on August 7, 2004. MTS Finance was required to make interest payments on the notes quarterly, commencing on November 5, 2003. The notes were listed on the Luxembourg Stock Exchange. Proceeds received from the notes, net of underwriting discount, were \$297.0 million and related debt issuance costs of \$1.8 million were capitalized. On May 5, 2004, the Group redeemed all outstanding floating rate notes, mentioned above, in the principal amount plus accrued interest thereon to the date of redemption.

On October 14, 2003, MTS Finance issued \$400.0 million notes bearing interest at 8.38% at par. The cash proceeds, net of issuance costs of approximately \$4.6 million, amounted to \$395.4 million. These notes are fully and unconditionally guaranteed by MTS OJSC and will mature on October 14, 2010. MTS Finance is required to make interest payments on the notes semi-annually in arrears on April 14 and October 14 of each year, commencing on April 14, 2004. The notes are listed on the Luxembourg Stock Exchange.

Subject to certain exceptions and qualifications, the indentures governing the notes contain covenants limiting the Group's ability to:

- incur debt;
- create liens;
- lease properties sold or transferred by the Group;
- enter into loan transactions with affiliates;
- merge or consolidate with another person or convey its properties and assets to another person; and
- sell or transfer any of its GSM licenses for the Moscow, St. Petersburg, Krasnodar and Ukraine license areas.

In addition, if the Group experiences certain types of mergers, consolidations or other changes in control, noteholders will have the right to require the Group to redeem the notes at 101% of their principal amount, plus accrued interest. The Group is also required to take all commercially reasonable steps necessary to maintain a rating of the notes from Moody's or Standard & Poor's. The notes also have cross default provisions with publicly traded debt issued by Sistema, the shareholder of the Group.

If the Group fails to meet these covenants, after certain notice and cure periods, the noteholders can accelerate the debt to be immediately due and payable.

Management believes that the Group is in compliance with all restrictive debt covenants provisions during the three year period ended as of December 31, 2004.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**Syndicated Loan** – In July 2004, MTS OJSC entered into a \$500.0 million syndicated loan agreement (“Syndicated Loan”) with international financial institutions: ING Bank N.V., ABN AMRO Bank N.V., HSBC Bank PLC, Raiffeisen Zentralbank Oesterreich AG ZAO, Bank Austria Creditanstalt AG, Commerzbank Aktiengesellschaft and other. The credit facility bears interest of LIBOR +2.50% per annum and matures in 3 years. The proceeds were used by OJSC MTS for corporate purposes, including refinancing of its existing indebtedness. In September 2004, MTS extended the total amount available under the Syndicated Loan for an additional \$100.0 million to a total amount of \$600.0 million. Commitment fee for the Syndicated Loan amounted to \$0.5 million. The debt issuance costs in the amount of \$10.2 million has been capitalized. At December 31, 2004, \$600.0 million was outstanding under this credit facility. The Syndicated Loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios. As of December 31, 2004, the Group is in compliance with all existing covenants.

**EBRD Loan** – In December 2004, MTS OJSC entered into a credit facility with European Bank for Reconstruction and Development (“EBRD”) for the total amount of \$150.0 million. The facility bears interest at LIBOR +3.10%. Commitment fee of 0.50% per annum should be paid in accordance with the credit agreement. The final maturity of this agreement is December 15, 2011. As of December 31, 2004, the balance outstanding under the loan was \$150.0 million. The loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios. As of December 31, 2004 the Group is in compliance with all existing covenants.

**CSFB Loans** – In April 2004, MTS OJSC entered into a short-term bridge loan facility with Credit Swiss First Boston for the total amount of \$200.0 million. The proceeds were used to repay the floating rate notes originally due in August 2004. Amounts outstanding under the loan agreement bear interest at LIBOR+2.25%. The MTS OJSC repaid \$110.0 million and \$90.0 million due under the loan in June 2004 and July 2004, respectively.

In October 2004, MTS Finance entered into a short-term loan facility with CSFB for the total amount of \$140.0 million. Amounts outstanding under the loan agreement bear interest at LIBOR+2.20%. The final maturity of this short-term loan facility was April 29, 2005. As of December 31, 2004 the balance outstanding under the loan was \$140.0 million. The loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios. As of December 31, 2004, the Group is in compliance with all existing covenants.

**HSBC Bank plc and ING BHF-BANK AG** – In October 2004, MTS OJSC entered into two credit facility agreements with HSBC Bank plc and ING BHF-BANK AG for the total amount \$122.3 million. The funds were used to purchase telecommunication equipment and software from Siemens AG and Alcatel SEL AG for the technical upgrade and expansion of network. Euler Hermes Kreditversicherungs-AG, the German credit export agency, is providing export credit cover in respect to both facilities. The facility bears interest at LIBOR + 0.44%. A commitment fee of 0.20% per annum and an arrangement fee of 0.25% should be paid in accordance with the loan agreement. The principal and interest amounts are to be repaid in seventeen equal half year installments, starting July 2005 for the first agreement and September 2005 for the second one. As of December 31, 2004, the outstanding balance under these agreements was \$77.0 million. The final maturity of these agreements is in July and September 2013. The loan facility is subject to certain restrictive covenants. As of December 31, 2004, the Group is in compliance with all existing covenants.

**Hermes Credit Facility (“HECF”)** – On December 30, 2003, UMC entered into Hermes Credit Facility with ING BHF Bank and Commerzbank Aktiengesellschaft to finance the acquisition of GSM equipment from Siemens AG. The aggregate amount available under this credit facility is EUR 47.4 million (\$64.5 million at December 31, 2004). In 2004, the agreement was amended to increase the amount available under the facility by EUR 9.2 million (\$12.5 million as of

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

December 31, 2004). The loan is guaranteed by MTS OJSC and bears interest at EURIBOR+0.65%. The amount outstanding is redeemable in 10 equal semi-annual installments starting on July 31, 2004. As of December 31, 2004 and 2003, the amounts outstanding under the loan were \$63.9 million and \$55.6 million, respectively. The available credit facility as at December 31, 2004 and 2003 was \$0.6 million and \$3.7 million, respectively.

**ING Bank (“Eurasia”)** – In September 2003, UMC entered into a \$60.0 million syndicated credit facility with ING Bank (“Eurasia”) ZAO, ZAO Standard Bank and Commerzbank Aktiengesellschaft with an interest rate of LIBOR + 2.25% – 4.15%. The loan is guaranteed by MTS OJSC. The proceeds were used by UMC to refinance its existing indebtedness. The loan is payable in 8 equal quarterly installments starting from September 2004. As of December 31, 2004 and 2003, \$46.7 million and \$60.0 million were outstanding, respectively, under this credit facility.

**HSBC Bank LLC** – In October 2003, TAIF Telcom entered into a \$25.0 million credit facility with HSBC Bank LLC, which is guaranteed by MTS OJSC. The facility bears interest at LIBOR + 2.75% and is redeemable in ten equal quarterly installments commencing on June 2004. The funds were used to purchase telecommunication equipment and general corporate purposes. The loan is subject to certain restrictive covenants including, but not limited to, restriction on the amount of dividends paid by TAIF Telcom until MTS owns 100% of TAIF Telcom’s outstanding common stock. As of December 31, 2004 and 2003 the outstanding balances under the credit facility were \$17.5 million and \$25.0 million, respectively.

**Ericsson Debt Restructuring** – In December 1996, Rosico, a wholly-owned subsidiary merged into MTS OJSC in June 2003, entered into a credit agreement with Ericsson Project Finance AB (“Ericsson”) that provided for a credit facility with an aggregate principal amount of \$60.0 million and had a maximum term of five years (the “Ericsson Loan”). The loan was repayable in ten equal consecutive quarterly payments of \$6.0 million commencing in 1999. On July 24, 2001, MTS, Rosico and Ericsson signed an amendment to the credit agreement rescheduling Rosico principal payments in nineteen consecutive quarterly installments. The amounts advanced under the agreement bear interest of LIBOR + 4.00%. If Rosico fails to pay any amount under this facility, the overdue interest would bear interest at a rate of an additional 6.00% per annum. The credit agreement contains covenants restricting Rosico’s ability to encumber its present and future assets and revenues without lender’s express consent.

Concurrent with the Group’s acquisition of Rosico, Sistema agreed to fund the full and timely repayment of the Ericsson Loan and to indemnify Rosico and MTS for any costs incurred by either Rosico or MTS in connection with the repayment of the Ericsson Loan. During 2000, Sistema and MTS agreed on a method that would allow Sistema to fund its obligation in a manner that minimizes the total costs of meeting this obligation (including related tax costs). Under this method, MTS enters into a long-term, ruble-denominated promissory notes with 0% interest and maturities from 2049 to 2052 to repay a portion of the funding from Sistema. The carrying value of these notes is insignificant at December 31, 2004 and 2003. The Group records interest expense on these notes over the term, such that the full amount of the obligation will be reflected as a liability at the date of repayment. Through December 31, 2004, Sistema has made payments under this obligation in the amount of \$60.0 million, \$45.1 million of which are repayable in the form of long-term, ruble denominated promissory notes with 0% interest. Amounts receivable from Sistema under this indemnification are recorded as shareholder receivable in the accompanying consolidated balance sheets.



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

On February 25, 2003, Ericsson assigned all of its rights and obligations under the Ericsson Loan to Salomon Brothers Holding Company, Inc.

At December 31, 2004 and 2003, \$14.9 million and \$23.4 million were outstanding, respectively, under the Ericsson Loan.

***Deutsche Telekom AG and TDC Mobile International A/C*** – The credit facilities with Deutsche Telekom AG and TDC Mobile International A/C bear interest at LIBOR + 5.00%-7.00% and were redeemable in five equal quarterly installments commencing April 2003. At December 31, 2003 the unpaid balance under these loans was \$14.8 million. The debt was fully repaid in April 2004.

***Nordea Bank Sweden loan*** – In September 2003, Primtelefon entered into a long-term loan facility with Nordea Bank Sweden for the total amount of \$9.8 million. Amounts outstanding under the loan agreement bear interest at LIBOR+0.40% and mature in October 2006. The loan is guaranteed by MTS OJSC. As of December 31, 2004 and 2003, the amounts outstanding under the loan were \$6.5 million and nil, respectively.

***WestLB International loan*** – In July 2002, MTS-P entered into a credit facility agreement with WestLB International S.A. Amounts outstanding under this agreement bear interest of EURIBOR + 2.00% per annum for the first two years for each advance and 4.00% per annum for the remaining interest periods for each advance until maturity. The final maturity of this agreement is December 28, 2006. The loan is guaranteed by MTS OJSC. As of December 31, 2004 and 2003, the balances outstanding under the loan were \$4.0 million and \$5.1 million, respectively.

***KFW*** – On December 21, 1998, UMC entered into two loan agreements with KWF, a German bank, for EUR 1.9 million and EUR 10.9 million. These loans bear interest at EURIBOR + 0.95% per annum and mature on March 31, 2004 and February 28, 2005, respectively. As of December 31, 2004 and 2003 the outstanding balances under these loans were \$1.5 million and \$4.3 million, respectively.

***Citibank credit facility*** – In November 2002, Telecom XXI entered into a credit facility with Citibank. Amounts borrowed under the credit facility bear interest of LIBOR + 3.50% per annum. Overdue amounts bear an additional 3.00% per annum. The \$10.0 million outstanding under this facility as of December 31, 2003, was fully repaid in July 2004.

The balance outstanding as at December 31, 2004, in the amount of \$0.9 million is comprised of the amounts borrowed by Primtelefon and Astrakhan Mobile, which bear interest at LIBOR + 1.15% and are payable in 2006.

***Dresdner Bank Credit Facilities*** – In December 2001 and April 2002, UDN-900 entered into credit agreements with Dresdner Bank (“Dresdner”), maturing in April 2004. As of December 31, 2003 the amount outstanding under these agreements was \$5.4 million. These borrowings bear interest at LIBOR + 3.20% per annum and are guaranteed by MTS OJSC. In April 2004, the loans were fully repaid.

In October 2002, MSS entered into a credit agreement with Dresdner to borrow up to \$10.0 million. As of December 31, 2004 and 2003, \$nil and \$10.0 million, respectively, were outstanding under this agreement. Borrowings under this agreement bear interest of LIBOR + 3.20%-3.35% per annum. The loan was guaranteed by MTS OJSC.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**AVAL Bank** – On December 31, 2003, UMC had the balance of \$10.9 million of overdraft with AVAL bank. The short-term overdraft facility was limited to 110.0 million hryvnias (\$20.6 million at December 31, 2003), bore interest at 10.00-16.00% per annum and matured on June 30, 2004. The balance of overdraft was fully repaid in January 2004.

**International Moscow Bank** – On June 9, 2003, Kuban-GSM entered into a 350.0 million ruble (\$12.6 million at December 31, 2004) credit facility with International Moscow Bank. Amounts borrowed under this facility mature in June 2005, bear an interest rate of 13.4% per annum and are collateralized by equipment with a book value of 458.1 million rubles (approximately \$16.5 million at December 31, 2004). As of December 31, 2003, approximately \$10.9 million was outstanding under this facility. The loan was fully repaid in March 2004. As of December 31, 2004, the available credit facility was \$12.6 million.

**ABN AMRO loan** - In November 2004, MTS signed a loan agreement with ABN AMRO Bank N.V. (Stockholm branch) for \$ 56.6 million and EUR 8.4 million. These funds will be used to purchase telecommunication equipment from Ericsson AB for expansion of the network. The loan is repayable on a biannual basis in equal installments over 9 years and bears an interest rate of USD LIBOR/EURIBOR+0.35% per annum. As of December 31, 2004, \$nil was outstanding under the facility.

**MBRD** – In August 2004, Novitel entered into ruble-denominated credit facility with Moscow Bank for Reconstruction and Development (“MBRD”), a related party. The facility allows borrowings of up to 60.0 million ruble (\$2.2 million at December 31, 2004). The loan bears interest at 15.00% per annum and is collateralized by equipment with a book value of 63.0 million rubles (approximately \$2.3 million at December 31, 2004). The facility was fully repaid by December 2004.

In 2003, Dontelecom entered into a ruble-denominated loan agreement with MBRD. The amounts borrowed bore interest at 18.5% and were payable in June 2004. As of December 31, 2003, \$1.2 million were outstanding under the facility. The loan was fully repaid in June 2004.

During the year 2003, MTS OJSC signed several short-term loan agreements with MBRD. Amounts borrowed were payable during the period of one to two months. During 2003, interest expense on these loans was approximately \$0.3 million.

The following table presents aggregate scheduled maturities of debt principal outstanding as of December 31, 2004:

Payments due in the year ended December 31,	
2005	\$ 370,845
2006	365,749
2007	227,195
2008	447,240
2009	40,100
Thereafter	473,511
	<u>\$ 1,924,640</u>

In December 2004, the Group entered into two variable-to-fixed interest rate swap agreements with ABN AMRO Bank N.V and with HSBC Bank PLC to hedge MTS' exposure to variability of future cash flows caused by the change in LIBOR related to the syndicated loan. MTS agreed with

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

ABN AMRO to pay a fixed rate of 3.27% and receive a variable interest of LIBOR on \$100.0 million for the period from October 7, 2004 up to July 27, 2007. MTS agreed with HSBC Bank PLC to pay a fixed rate of 3.25% and receive a variable interest of LIBOR on \$150.0 million for the period from October 7, 2004 up to July 27, 2007. These instruments qualify as cash flow hedges under the requirements of SFAS No. 133 as amended by SFAS No. 149. As of December 31, 2004, the Group recorded a liability of \$0.6 million in relation to these contracts in the accompanying consolidated balance sheet and a loss of \$0.5 million, net of tax of \$0.1 million, as other comprehensive income in the accompanying consolidated statement of changes in shareholders equity in relation to the change in fair value of these agreements. In 2004, there were no amounts reclassified from other comprehensive income to income due to hedge ineffectiveness.

## 12. CAPITAL LEASE OBLIGATIONS

The following table presents future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of December 31, 2004:

Payments due in the year ended December 31,		
2005	\$	10,547
2006		3,233
2007		826
2008		171
2009		169
Thereafter		451
Total minimum lease payments (undiscounted)		15,397
Less amount representing interest		(2,889)
Present value of net minimum lease payments		12,508
Less current portion of lease payable		(8,561)
Non-current portion of lease payable	\$	3,947

For a schedule by years of future minimum lease payments under capital leases to Invest-Svyaz-Holding, a related party, together with the present value of the net minimum lease payments as of December 31, 2004, see Note 17.

## 13. ACCRUED LIABILITIES

Accrued liabilities at December 31, 2004 and 2003 were comprised of the following:

	December 31,	
	2004	2003
Accrued payroll and vacation	\$ 44,673	\$ 6,595
VAT	32,174	33,545
Interest payable	31,177	32,911
Taxes other than income	23,706	31,139
Other accruals	48,947	39,599
Total accrued liabilities	\$ 180,677	\$ 143,789

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 14. INCOME TAX

MTS' provision for income taxes was as follows for the years ended December 31, 2004, 2003 and 2002:

	<b>December 31,</b>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Current provision for income taxes	\$ 430,687	\$ 285,481	\$ 129,406
Deferred income tax benefit	(76,023)	(43,001)	(18,989)
Total provision for income taxes	<u>\$ 354,664</u>	<u>\$ 242,480</u>	<u>\$ 110,417</u>

Effective January 1, 2002, the statutory income tax rate in Russia was set at 24%. From January 1, 2004, UMC statutory income tax rate changes from 30% to 25% as a result of changes in Ukrainian tax legislation.

The statutory income tax rate reconciled to MTS' effective income tax rate is as follows for the years ended December 31, 2004, 2003 and 2002:

	<b>December 31,</b>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Statutory income tax rate for year	24.0%	24.0%	24.0%
Adjustments:			
Expenses not deductible for tax purposes	1.0	2.3	2.1
Effect of higher tax rate of UMC	0.2	0.9	-
Currency exchange and transaction gains	1.2	1.6	-
Other	(0.6)	0.4	(0.3)
Effective income tax rate	<u>25.8%</u>	<u>29.2%</u>	<u>25.8%</u>

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

Temporary differences between the tax and accounting bases of assets and liabilities give rise to the following deferred tax assets and liabilities at December 31, 2004 and December 31, 2003:

	December 31,	
	2004	2003
Assets (liabilities) arising from tax effect of:		
<b>Deferred tax assets</b>		
Depreciation of property, plant and equipment	\$ 48,829	\$ 19,171
Deferred connection fees	22,598	8,805
Subscriber prepayments	18,151	12,030
Accrued expenses	18,934	7,316
Allowance for doubtful accounts	5,220	14,157
Inventory obsolescence	2,759	3,906
Amortization of intangible assets	9,148	5,444
Loss carryforward (Rosico and MSS)	7,171	7,113
Other	4,328	5,683
	<u>137,138</u>	<u>83,625</u>
Valuation allowance	(7,171)	(7,113)
Total deferred tax assets	<u>129,967</u>	<u>76,512</u>
<b>Deferred tax liabilities</b>		
Licenses acquired	\$ (179,935)	\$ (168,889)
Depreciation of property, plant and equipment	(31,429)	(14,084)
Customer base	(10,746)	(15,506)
Other intangible assets	(9,797)	(11,980)
Other	(8,600)	(2,258)
Total deferred tax liabilities	<u>(240,507)</u>	<u>(212,717)</u>
Net deferred tax liability	<u>(110,540)</u>	<u>(136,205)</u>
Net deferred tax assets, current	\$ 49,850	\$ 44,423
Net deferred tax liability, long term	\$ (160,390)	\$ (180,628)

As of December 31, 2004, the Group had a tax loss carryforward in the amount of \$29,879 related to operations of Rosico. As of December 31, 2003, the Group had taxable losses carryforwards in the amount of \$29,638 related to operations of Rosico and MSS. These loss carryforwards resulted in deferred tax assets at December 31, 2004 and December 31, 2003 in the amounts of \$7,171 and \$7,113, respectively. As Russian companies are required to file tax declarations on a standalone basis, MTS is not able to utilize these losses to offset its taxable income. While Rosico was merged into MTS OJSC in June 2003, the Group has still recorded a valuation allowance for the entire amount of the available tax loss carryforward related to Rosico as MTS has not yet performed all procedures necessary to determine what amounts will be available for deductions in the future.

The Group does not record a deferred tax liability related to undistributed earnings of UMC, as it intends to permanently reinvest these earnings. The undistributed earnings of UMC amounted to \$559.5 and \$327.8 million as of December 31, 2004 and 2003, respectively.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 15. SHAREHOLDERS' EQUITY

In accordance with Russian laws, earnings available for dividends are limited to profits determined in accordance with Russian statutory accounting regulations, denominated in rubles, after certain deductions. Net income of MTS OJSC for the years ended December 31, 2004, 2003 and 2002 that is distributable under Russian legislation totaled 15,209 million rubles (\$527.9 million), 13,423 million rubles (\$437.4 million) and 10,759 million rubles (\$343.3 million), respectively.

In December 2004, the shareholder of the Group T-Mobile Worldwide Holding GMBH sold 15.09% stake in MTS on the open market in the form of GDRs.

#### 16. STOCK BONUS AND STOCK OPTION PLANS

In 2000, MTS established a stock bonus plan and stock option plan (the "Option Plan") for selected officers, key employees and key advisors. During its initial public offering in 2000 (see Note 1) MTS allotted 9,966,631 shares of its common stock to fund the Option Plan.

During 2004, 2003 and 2002, MTS made several grants pursuant to its stock option plan to employees and directors of the Group. These options generally vest over a two year period from the date of the grant, contingent on continued employment of the grantee with the Company.

A summary of the status of the Group's Option Plan is presented below:

	Shares	Weighted average exercise price, U.S. dollar
Outstanding at January 1, 2002	1,829,221	1.31
Granted	2,846,681	1.49
Forfeited	(27,481)	1.31
Outstanding at December 31, 2002	<u>4,648,421</u>	<u>1.42</u>
Granted	1,952,632	2.43
Exercised	(37,557)	1.31
Exchanged for cash award	(1,746,310)	1.31
Forfeited	(19,776)	1.31
Outstanding at December 31, 2003	<u>4,797,410</u>	<u>1.87</u>
Granted	1,665,256	5.95
Exercised	(2,726,966)	1.49
Forfeited	(204,730)	1.92
Outstanding at December 31, 2004	<u>3,530,970</u>	<u>4.09</u>

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

As of December 31, 2004, the Group had the following stock options outstanding:

<u>Exercise prices</u>	<u>Number of shares</u>	<u>Remaining weighted average life (years)</u>
2.43	1,868,214	0.54
5.95	1,662,756	1.54
	<u>3,530,970</u>	

None of the options outstanding at December 31, 2004 and 2003 were exercisable.

According to the terms of the Option Plan, the exercise price of the options equals the average market share price during the hundred day period preceding the grant date. The difference in the exercise price of the option and the market price at the date of grant is shown as unearned compensation in the consolidated statements of changes in shareholders' equity and is amortized to expense over the vesting period of 2 years. This amount historically had been insignificant to the consolidated financial statements.

The Group's Option Plan does not routinely allow a grantee to receive cash in lieu of shares, however due to the lack of liquidity for the Group's stock in the Russian market, 1,746,310 options were cancelled by MTS in 2003 and exchanged for a cash award of \$2.9 million.

The fair value of options granted during the three years in the period ended December 31, 2004 were estimated using the binomial option pricing model based on the following assumptions:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Risk free rate	4.5%	5.2%	6.1%
Expected dividend yield	3%	3%	3%
Expected volatility	48.8%	40.0%	50.0%
Expected life (years)	2	2	2
Fair value of options (per share)	\$2.36	\$1.02	\$0.50

In accordance with the Russian legislation, MTS Board members and key employees may be considered insiders with respect to the Group and thus may be restricted from selling their shares.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 17. RELATED PARTIES

Related party balances as of December 31, 2004 and 2003, comprised of the following:

	December 31,	
	2004	2003
Accounts receivable:		
Rosno for insurance	\$ 9,065	\$ -
Kvazar-Micro for information systems consulting	2,161	-
MTT for interconnection	1,497	822
T-Mobile for roaming	1,198	853
Maxima for advertising	884	83
STROM telecom for software	-	1,074
Receivables from investee companies	2,963	524
Total accounts receivable, related parties	<u>\$ 17,768</u>	<u>\$ 3,356</u>
Accounts payable:		
Strom Telecom for software	\$ 7,070	\$ -
MTT for interconnection	2,964	-
T-Mobile for roaming	1,580	-
MTU-Inform for interconnection	2,398	2,398
MGTS for interconnection	607	704
Cetel B.V. for UMC shares	-	27,500
Other	2,390	1,302
Total accounts payable, related parties	<u>\$ 17,009</u>	<u>\$ 31,904</u>

Transactions with major related parties are described below.

***Moscow Bank of Reconstruction and Development (“MBRD”)*** – Starting August 2000, MTS has been keeping certain bank and deposit accounts with MBRD, whose major shareholder is Sistema. As of December 31, 2004, MTS’ cash position at MBRD amounted to \$72.0 million in current accounts. As of December 31, 2003, MTS’ cash position at MBRD amounted to \$279.7 million, including \$265.2 million in time deposits and \$14.5 million in current accounts. The related interest accrued and collected on the deposits for the years ended December 31, 2004 and 2003 amounted to \$6.8 million and \$9.9 million, respectively, and was included as a component of interest income in the accompanying consolidated statements of operations.

Borrowing transactions with MBRD are described in Note 11.

***Rosno OJSC*** – MTS arranged medical insurance for its employees and property with Rosno OJSC, whose significant shareholder is Sistema. Insurance premium paid to Rosno OJSC for the years ended December 31, 2004, 2003 and 2002 amounted to \$7.6 million, \$16.9 million and \$4.9 million, respectively. Management believes that all of the insurance contracts with Rosno OJSC have been entered at market terms.

***Kvazar-Micro Corporation (“Kvazar”)*** – Kvazar, a Ukrainian based company providing solutions, services, and business consulting in the field of information and communication technologies. Since July 2004, Sistema is a controlling shareholder of Kvazar. In 2004, MTS signed agreements for software implementation services with Kvazar. Related fees for the year 2004 amounted to approximately \$9.7 million. Management believes that these agreements are at market terms.



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

**Maxima Advertising Agency (“Maxima”)** – In 2004, 2003 and 2002, MTS had agreements for advertising services with Maxima, a subsidiary of Sistema. Advertising costs related to Maxima for the years ended December 31, 2004, 2003 and 2002 amounted to \$48.9 million, \$23.7 million and \$12.1 million, respectively. Management believes that these agreements are at market terms.

**Telmos** – In 2004, 2003 and 2002, MTS had interconnection and line rental arrangements with, and received domestic and international long-distance services from Telmos, a subsidiary of Sistema. Interconnection and line rental expenses for the years 2004, 2003 and 2002 comprise \$1.6 million, \$1.6 million and \$1.8 million, respectively. Management believes that these arrangements are at market terms.

**Moscow City Telephone Network (“MGTS”)** – In 2004, 2003 and 2002, MTS had line rental agreements with MGTS and rented cable plant from MGTS for installation of optic-fiber cable. MTS also rented buildings for administrative office, sales and marketing offices as well as premises for switching and base station equipment. Rental expenses for the years 2004, 2003 and 2002 amounted to \$5.9 million, \$4.5 million and \$3.4 million, respectively. Management believes that all these transactions were made at market terms. Sistema is the majority shareholder of MGTS.

**MTU-Inform** – In 2004, 2003 and 2002, MTS had interconnection and line rental agreements with MTU-Inform, a subsidiary at Sistema. Interconnection and rental expenses for the years 2004, 2003 and 2002, were \$25.7 million, \$23.3 million and \$24.3 million, respectively. In 2003 and 2002, MTS also purchased telephone numbering capacity from MTU-Inform for \$2.0 million and \$2.6 million, respectively. Management believes that these agreements are at market terms.

**Comstar** – In 2004, 2003 and 2002, MTS had interconnection and line rental agreements with Comstar, a subsidiary of Sistema. Cost of interconnecton and line rental services rendered by Comstar for the years 2004, 2003 and 2002 amounted to \$3.1 million, \$3.6 million and \$3.5 million, respectively. In 2004, MTS also purchased telephone numbering capacity from Comstar for \$ 4.2 million. Management believes that these agreements are at market terms.

**T-Mobile** – In 2004, 2003 and 2002, the Group had non-exclusive roaming agreements with T-Mobile, a shareholder of the Group. Roaming expenses for the years ended December 31, 2004, 2003 and 2002 amounted to \$ 6.1 million, \$1.7 million and \$1.1 million, respectively. Management believes that these agreements are at market terms.

**Invest-Svyaz-Holding** – In 2004 and 2003, MTS entered into agreements with Invest-Svyaz-Holding, a shareholder of MTS and a wholly-owned subsidiary of Sistema, for leasing of network equipment and billing system. These leases were recorded as capital leases in compliance with requirements of SFAS No. 13, “Accounting for Leases.” The present value of future lease payments due within one year are classified as current liabilities, and the remaining balance as long-term liabilities. The interest rate implicit in these leases varies from 14% to 44%, which management believes are market terms.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The following table summarizes the future minimum lease payments under capital leases to Invest-Svyaz-Holding together with the present value of the net minimum lease payments as of December 31, 2004:

Payments due in the year ended December 31,	
2005	\$ 8,174
2006	3,058
2007	653
Total minimum lease payments (undiscounted)	11,885
Less amount representing interest	(2,436)
Present value of net minimum lease payments	9,449
Less current portion of lease obligations	(6,103)
Non-current portion of lease obligations	<u>\$ 3,346</u>

In addition to the above lease transactions, the Group guarantees debt of Invest-Svyaz-Holding in the amount of \$21.6 million to a third party, which is used by Invest-Svyaz-Holding primarily to finance its leases to the Group.

For the year ended December 31, 2004, principal and interest paid to Invest-Svyaz-Holding were \$6.4 and \$4.1, respectively. Principal and interest paid to Invest-Svyaz-Holding for the year ended December 31, 2003, were \$5.4 million and \$3.3 million, respectively. Principal and interest paid for the year ended December 31, 2002, were \$2.9 million and \$1.4 million, respectively. Management believes that these agreements are at market terms.

**STROM telecom** – During 2004 and 2003, the Group entered into a number of agreements with STROM telecom, a subsidiary of Sistema, for a total amount up to \$116.5 and \$32.3 million, respectively. Pursuant to these contracts, the Group purchased in 2004 and 2003 billing systems and communication software support systems for approximately \$9.1 and \$23.7 million, respectively. Advances paid under these agreements and outstanding as of December 31, 2004 and 2003, amount to \$51.0 million and \$1.1 million, respectively.

**MTT** – In 2004, MTS had interconnection and line rental agreements with MTT, a subsidiary at Sistema. Interconnection expenses for the year 2004 amounted to \$16.1 million. Management believes that these agreements are at market terms.

See Note 3 for other related parties transactions.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

#### 18. GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses for the years ended December 31, 2004, 2003 and 2002 consisted of the following:

	December 31,		
	2004	2003	2002
Salaries and social contributions	\$ 256,989	\$ 156,808	\$ 84,706
Repair and maintenance	81,538	39,406	20,361
General and administrative	72,586	42,530	26,549
Rent	54,054	31,968	15,578
Billing and data processing	28,238	22,067	9,549
Taxes other than income	50,033	40,432	39,119
Consulting expenses	19,694	11,361	7,692
Insurance	7,554	7,351	6,774
Inventory obsolescence expense	4,610	3,307	5,614
General and administrative expenses	<u>\$ 575,296</u>	<u>\$ 355,230</u>	<u>\$ 215,942</u>

#### 19. INVESTMENTS IN AND ADVANCES TO ASSOCIATES

At December 31, 2004 and 2003, the Group's investments in and advances to associates included, respectively, the following:

	December 31,	
	2004	2003
MTS Belarus – loans receivable	\$ 51,894	\$ 51,481
MTS Belarus – equity investment	27,699	5,884
Primtelefon – equity investment	-	31,174
Astrakhan Mobile and Volgograd Mobile – equity investment	-	5,806
Astrakhan Mobile and Volgograd Mobile – loans receivable	-	6,850
Volgograd Mobile – loans receivable	-	204
MSS – note receivable	-	827
Receivables from other investee companies	1,642	1,359
Total investments in and advances to associates	<u>\$ 81,235</u>	<u>\$ 103,585</u>

**MTS Belarus** – As of December 31, 2004 and 2003, the Group provided MTS Belarus with a total of \$51.9 million and \$51.5 million in loans, respectively. These loans bear interest at 3.00% to 11.00% per annum. In addition, the Group guarantees the debt of MTS Belarus in the amount of \$25.0 million to several banks.

**Primtelefon, Astrakhan Mobile and Volgograd Mobile** – As described in Note 3, in August 2003 the Group purchased equity interests in various Russian regional mobile operators, including stakes in Primtelefon, Astrakhan Mobile and Volgograd Mobile, as a part of its strategic business plans.

Following the acquisition in 2004 of the additional stakes in Primtelefon, Astrakhan Mobile and Volgograd Mobile, those companies have been consolidated starting June 30, 2004 for Primtelefon and September 1, 2004 for both Astrakhan Mobile and Volgograd Mobile.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The Group's share in net income of unconsolidated affiliates is included in other income in the accompanying consolidated statements of operations. For the years ended December 31, 2004, 2003 and 2002, this share amounted \$24.2 million, \$2.7 million and nil net income, respectively.

#### 20. OPERATING LICENSES

In connection with providing telecommunication services, the Group has been issued various operating licenses by the Russian Ministry of Information Technologies and Communications. In addition to the licenses received directly from the Russian Ministry of Information Technologies and Communications, the Group was granted access to various telecommunication licenses through acquisitions. At December 31, 2004 and 2003, the recorded values of the Group's telecommunication licenses were as follows:

	December 31,	
	2004	2003
Moscow license area (MTS OJSC)	\$ 255,812	\$ 255,812
Ukraine (UMC)	171,815	151,857
Krasnodar and Adigeya regions (Kuban-GSM)	124,396	124,396
Five regions of Asian Russia (Telecom-900)	91,202	84,395
North-Western region (Telecom XXI)	74,639	74,639
Tatarstan Republic (TAIF Telcom)	104,159	68,407
Krasnoyarsk region, Taimyr region and Khakassia Republic (Sibchallenge)	52,625	52,625
Tomsk region (TSS)	49,282	49,282
Bashkortostan Republic (BM Telecom)	48,932	48,932
Far East (Primtelefon)	48,107	-
Uzbekistan (Uzdunrobita)	40,861	-
Rostov region (Dontelecom)	22,067	22,067
Seven regions of European Russia	19,503	19,503
Other	85,029	8,212
Licenses, at cost	1,188,429	960,127
Accumulated amortization	(417,158)	(257,024)
Licenses, net	\$ 771,271	\$ 703,103

Amortization expense for the years ended December 31, 2004, 2003 and 2002, amounted to \$160.1 million, \$113.6 million and \$63.7 million, respectively.

Based on the amortizable intangible assets existing at December 31, 2004, the estimated future amortization expenses are \$222.9 million during 2005, \$168.5 million during 2006, \$125.6 million during 2007, \$75.8 million during 2008, \$37.3 million during 2009 and \$140.8 million thereafter. Actual amortization expense to be reported in future periods could differ from these estimates as a result of new intangible assets acquisitions, changes in useful lives and other relevant factors.

Each of the Group's licenses, except the licenses covering the Moscow license area and Uzbekistan, contains a requirement for service to be commenced and for subscriber number and territorial coverage targets to be achieved by a specified date. The Group has met these targets or received extensions to these dates in those regional license areas in which the Group has not commenced operations. Management believes that the Group is in compliance with all material terms of its licenses.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

The Group's operating licenses do not provide for automatic renewal. The Group has limited experience with the renewal of its existing licenses. However, management believes that licenses required for the Group's operations will be renewed upon expiration.

#### 21. COMMITMENTS AND CONTINGENCIES

**Capital Commitments** – As of December 31, 2004, the Group had executed non-binding purchase agreements in the amount of approximately \$164.7 million to subsequently acquire property, plant and equipment.

**Operating Leases** – The Group has entered into lease agreements of space for telecommunication equipment and offices, which expire in various years up to 2053. Rental expenses under these operating leases of \$54.0 million, \$32.0 million and \$15.6 million for the years ended December 31, 2004, 2003 and 2002, respectively, are included in general and administrative expenses in the accompanying statements of operations. Future minimum lease payments due under non-cancelable leases at December 31, 2004 are as follows:

Payments due in the years ended December 31,		
2005	\$	33,459
2006		17,787
2007		14,021
2008		10,670
2009		7,261
Thereafter		35,475
Total	\$	<u>118,673</u>

**Operating Licenses** – Since the commencement of MTS' operations in 1994, a number of telecommunication licenses for the Russian Federation were issued to MTS and its now consolidated subsidiaries. These license agreements stipulate that certain fixed "contributions" are to be made to a fund for the development of telecommunication networks in the Russian Federation. Most of MTS' current licenses provide for the payment of such fees, which in the aggregate could total approximately \$103.0 million, as at December 31, 2004. According to the terms of licenses, such contributions are to be made during the license period upon the decision and as defined by the Board of Directors of the Association of GSM-900 Operators (the "Association"). The Association is a non-governmental, not-for-profit association, and its Board of Directors comprises of representatives of the major cellular communications companies, including MTS.

The Association has not adopted any procedures enforcing such payments and no such procedures have been established by the Russian legislation. To date, MTS has not made any such payments pursuant to any of the current operating licenses issued to MTS and its consolidated subsidiaries. Further, the management of MTS believes that MTS will not be required to make any such payments in the future. In relation to these uncertainties, MTS has not recorded a contingent liability in the accompanying consolidated financial statements.

**Provision for Doubtful Accounts** – In 2003, MTS incurred a loss of \$16.7 million due to dealers and subscriber fraud. In 2003, the Group's management took measures to prevent further fraud of that nature. No significant losses from the dealers' fraud were incurred during year ended December 31, 2004.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

**Issued Guarantees** – As of December 31, 2004, the Group has issued guarantees to third party banks for the loans taken by Invest-Svyaz-Holding, a shareholder of the Group for a total amount of \$21.6 millions (see also Note 17). The guarantees expire by May 2006. The Group issued additional guarantees on behalf of MTS-Belarus, an equity investee, for the total amount of \$25.0 million. Under these guarantees, the Group could be potentially liable for a maximum amount of \$46.6 in case of the borrower's default under the obligations. The guarantees expire by April 2007.

As of December 31, 2004, no event of default has occurred under any of the guarantees issued by the Group.

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

On January 1, 2004, a new Law on telecommunications came into effect in Russia. The law sets the legal basis for the telecommunications business in Russia and defines the status that state bodies have in the telecommunications sector. The Group cannot predict with any certainty how the new law will affect MTS. The new law creates a new interconnect pricing regime in 2004 that should be more transparent and unified and it creates a universal service charge calculated as a percentage of revenue, which will be introduced from 2005. The new law may increase the regulation of the MTS operations and until the time when appropriate regulations consistent with the new law are promulgated, there will be a period of confusion and ambiguity as regulators interpret the legislation.

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 ("VAT"), corporate income tax (profits tax), a number of turnover-based taxes, and payroll (social) taxes and 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. Accordingly, few precedents with regard to tax rulings have been established. 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, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems.

In recent years, the Russian government has initiated revisions of the Russian tax system. Effective January 1, 1999, the first part of the Tax Code was enacted. Effective January 1, 2001, the second part of the Tax Code was enacted and effective January 1, 2002, new regulations, relating to federal income tax were enacted. The new tax system is generally intended to reduce the number of taxes, the overall tax burden on businesses, and to simplify the tax laws.

Generally, tax declarations remain open and subject to inspection for a period of three years following the tax year. As of December 31, 2004, tax declarations of the Group for the preceding three fiscal years were open to further review.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

---

In the ordinary course of business, MTS may be party to various legal and tax proceedings, and subject to claims, certain of which relate to the developing markets and evolving fiscal and regulatory environments in which MTS operates. In the opinion of management, the MTS's liability, if any, in all pending litigation, other legal proceeding or other matters will not have a material effect upon the financial condition, results of operations or liquidity of MTS.

Management believes that it has adequately provided for tax liabilities in the accompanying consolidated financial statements; however, the risk remains that relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant.

**UMC** – On June 7, 2004, the General Prosecutor of Ukraine filed a claim against MTS and others in the Kiev Commercial Court seeking to unwind the sale by Ukrtelecom of its 51% stake in UMC to MTS. The complaint also seeks an order that would prohibit MTS from alienating 51% of its stake in UMC until the claim is resolved.

On August 12, 2004, the Kiev Commercial Court rejected a claim of General Prosecutor of Ukraine against MTS. No appeal was filed to the Court by the office of General Prosecutor of Ukraine within an established period. As of the date of these statements an office of General Prosecutor of Ukraine filed a request to the Constitutional Court of Ukraine to clear out terms of the State Privatization Plan for 2000-2002 and respond whether Ukrtelecom had a right to sell 51% stake in UMC.

MTS believes that it acquired a stake in UMC in full compliance with the Ukrainian law and, if required, intends to vigorously defend its acquisition of UMC.

## 22. SEGMENT INFORMATION

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", established standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the chief operating decision maker or group in deciding how to allocate resources and in assessing performance. The Group's business is organized based on geographical operations. Management of the Group regularly reviews certain operational and statistical information by license area, however currently no discrete financial information is available on this basis, therefore the performance is measured and decisions about resource allocation are made by management based on operating income by legal entities as an aggregate of the license area information.

Intercompany eliminations presented below consist primarily of the following items: intercompany sales transactions, elimination of gross margin in inventory and other intercompany transactions conducted under the normal course of operations.

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

*(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)*

At December 31, 2004, the Group has several operating segments, of which four are reportable segments – MTS OJSC, UMC, Telecom XXI and Kuban-GSM.

	Year ended December 31,		
	2004	2003	2002
Revenue:			
MTS OJSC	\$ 2,129,544	\$ 1,471,198	\$ 1,044,877
UMC(1)	832,313	394,038	-
Telecom XXI	297,194	210,460	79,166
Kuban-GSM	225,350	168,401	79,317
Other	796,256	432,770	211,826
Intercompany eliminations	(393,663)	(130,669)	(53,430)
Total revenue	<u>\$ 3,886,994</u>	<u>\$ 2,546,198</u>	<u>\$ 1,361,756</u>
Depreciation and amortization:			
MTS OJSC	\$ 253,485	\$ 199,946	\$ 144,004
UMC	124,935	66,392	-
Telecom XXI	57,265	36,782	17,343
Kuban-GSM	68,140	32,299	21,224
Other	175,221	82,185	27,109
Intercompany eliminations	(3,317)	(1,688)	-
Total depreciation and amortization	<u>\$ 675,729</u>	<u>\$ 415,916</u>	<u>\$ 209,680</u>
Operating income:			
MTS OJSC	\$ 728,101	\$ 527,837	\$ 365,698
UMC	317,860	131,704	-
Telecom XXI	104,936	80,632	2,331
Kuban-GSM	74,622	74,599	27,725
Other	198,390	123,577	72,806
Intercompany eliminations	(4,846)	(15,751)	(4,189)
Total operating income	<u>\$ 1,419,063</u>	<u>\$ 922,598</u>	<u>\$ 464,371</u>
Total operating income	\$ 1,419,063	\$ 922,598	\$ 464,371
Currency exchange and transaction losses (gains)	(6,529)	(693)	3,474
Interest income	(21,792)	(18,076)	(8,289)
Interest expense	107,956	106,551	44,389
Other (income)/expenses	(33,456)	3,420	(2,454)
Income before provision for income taxes and minority interest	<u>\$ 1,372,884</u>	<u>\$ 831,396</u>	<u>\$ 427,251</u>
Additions to long-lived assets:			
MTS OJSC	\$ 679,023	\$ 389,446	\$ 360,598
UMC (1)	303,761	900,465	-
Telecom XXI	62,333	174,128	175,361
Kuban-GSM	69,689	172,949	199,225
Other	714,344	393,526	169,378
Total additions to long-lived assets	<u>\$ 1,829,150</u>	<u>\$ 2,030,514</u>	<u>\$ 904,562</u>

(1) Acquired in March 2003.



## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)

	December 31,	
	2004	2003
Long-lived assets:		
MTS OJSC	\$ 1,891,869	\$ 1,454,570
UMC, including goodwill in the amount of \$8,000 as of December 31, 2004 and 2003	838,020	648,812
Telecom XXI	295,505	288,256
Kuban-GSM	279,883	276,883
Other, including goodwill in amounts of \$100,329 and \$533 as of December 31, 2004 and 2003, respectively	1,174,582	623,037
Intercompany eliminations.	(37,408)	(19,702)
Total long-lived assets	<u>\$ 4,442,451</u>	<u>\$ 3,271,856</u>
Total assets:		
MTS OJSC	\$ 2,717,814	\$ 2,328,426
UMC	993,997	772,792
Telecom XXI	363,888	345,784
Kuban-GSM	393,656	319,546
Other	1,573,239	727,600
Intercompany eliminations	(461,407)	(268,797)
Total assets	<u>\$ 5,581,187</u>	<u>\$ 4,225,351</u>

### 23. SUBSEQUENT EVENTS

**The Notes** – On January 27, 2005, MTS Finance issued \$400.0 million 8.00% unsecured notes at 99.736%. These notes are fully and unconditionally guaranteed by MTS OJSC and mature on January 28, 2012. MTS Finance is required to make interest payments on the notes semi-annually in arrears on January 28 and July 28, commencing on July 28, 2005. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes were \$398.9 million.

**ADS Ratio Change** – In December 2004, the Group announced that it will be changing its current ADS ratio effective January 3, 2005, the first trading day in 2005. The ratio has changed from 1 ADS per 20 ordinary shares to 1 ADS per 5 ordinary shares.

**Acquisition of Subsidiary** – In February 2005, MTS signed an agreement to acquire a 74.9% stake in Sweet-Com LLC, a holder of 3.5GHz radio frequency allocation for Moscow region, for a cash consideration of \$2.0 million. The Company is providing wide-range radio access services for the “last mile” based on the Radio-Ethernet technology.

The purchase price allocation for this acquisition has not been yet finalized at the date of these statements.

**Tax Audit** – In March 2005, the Russian tax authorities audited MTS OJSC’s compliance with tax legislation for the year ended December 31, 2002. Based on the results of this audit, the Russian tax authorities assessed that 372,152 thousand roubles (approximately \$13.4 million as at December 31, 2004) of additional taxes, penalties and fines were payable by the Group. The Group has prepared and filed with the Arbitrary Court of Moscow a petition to recognize the tax authorities’ resolution as partially invalid. The amount of disputed taxes and fines equals 281,504 thousand roubles (approximately \$10.1 million).

## OJSC MOBILE TELESYSTEMS AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) FOR THE YEARS ENDED DECEMBER 31, 2004, 2003 AND 2002

(Amounts in thousands of U.S. dollars except share and per share amounts or if otherwise stated)

*CSFB Loan* – In April 2005, the loan due to Credit Swiss First Boston in the amount of \$140.0 million was fully repaid.