

OJSC Tattelecom

**International Financial Reporting Standards
Consolidated Financial Statements and Independent
Auditor's Report**

31 December 2009

OJSC TATTELECOM

TABLE OF CONTENTS

INDEPENDENT AUDITOR'S REPORT

CONSOLIDATED FINANCIAL STATEMENTS

| | |
|--|---|
| Consolidated Statement of Financial Position | 1 |
| Consolidated Statement of Comprehensive Income | 2 |
| Consolidated Statement of Changes in Equity..... | 3 |
| Consolidated Statement of Cash Flows | 4 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

| | |
|---|----|
| 1. OJSC TATTELECOM AND ITS OPERATIONS | 5 |
| 2. OPERATING ENVIRONMENT OF THE GROUP | 5 |
| 3. SIGNIFICANT ACCOUNTING POLICIES..... | 6 |
| 4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENT IN APPLYING ACCOUNTING POLICIES..... | 15 |
| 5. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS | 16 |
| 6. NEW ACCOUNTING PRONOUNCEMENTS | 17 |
| 7. SEGMENT INFORMATION..... | 19 |
| 8. BALANCES AND TRANSACTIONS WITH RELATED PARTIES..... | 19 |
| 9. REVENUE..... | 20 |
| 10. OPERATING EXPENSES | 20 |
| 11. FINANCE COSTS..... | 21 |
| 12. PROPERTY, PLANT AND EQUIPMENT..... | 21 |
| 13. INTANGIBLE ASSETS..... | 22 |
| 14. FINANCIAL INVESTMENTS | 22 |
| 15. OTHER NON-CURRENT ASSETS | 23 |
| 16. INVENTORY | 23 |
| 17. TRADE ACCOUNTS RECEIVABLE..... | 24 |
| 18. ADVANCES PAID AND PREPAID EXPENSES | 25 |
| 19. CASH AND CASH EQUIVALENTS..... | 25 |
| 20. SHARE CAPITAL | 25 |
| 21. BORROWINGS..... | 25 |
| 22. BUSINESS COMBINATIONS | 26 |
| 23. FINANCE LEASE OBLIGATIONS | 27 |
| 24. INCOME TAXES..... | 27 |
| 25. DEFERRED REVENUE | 29 |
| 26. POST-RETIREMENT BENEFIT OBLIGATIONS..... | 29 |
| 27. ACCOUNTS PAYABLE AND ACCRUED LIABILITES | 30 |
| 28. OTHER LONG-TERM LIABILITIES | 30 |
| 29. RISK MANAGEMENT..... | 30 |
| 30. COMMITMENTS AND CONTINGENCIES | 32 |
| 31. SUBSEQUENT EVENTS | 33 |

INDEPENDENT AUDITOR'S REPORT

To the Shareholder and Board of Directors of OJSC Tatttelecom:

- 1 We have audited the accompanying consolidated financial statements of OJSC Tatttelecom and its subsidiaries (the "Group") which comprise the consolidated statement of financial position as at 31 December 2009 and the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

- 6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2009, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit


21 May 2010
Moscow, Russian Federation

OJSC TATTELECOM
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
(in thousands of Russian Roubles)

| | Note | 31 December | |
|--|------|-------------------|-------------------|
| | | 2009 | 2008 |
| ASSETS | | | |
| Non-current assets | | | |
| Property, plant and equipment | 12 | 10,415,453 | 10,344,765 |
| Intangible assets | 13 | 138,145 | 70,753 |
| Financial investments | 14 | 198,421 | 130,495 |
| Other non-current assets | 15 | 57,265 | 208,184 |
| Total non-current assets | | 10,809,284 | 10,754,197 |
| Current assets | | | |
| Inventory | 16 | 144,282 | 130,759 |
| Trade accounts receivable | 17 | 772,549 | 665,160 |
| Advances paid and prepaid expenses | 18 | 193,086 | 108,392 |
| Prepaid income tax | | 71,197 | 51,633 |
| Prepaid taxes, other than income tax | | 23,823 | 68,220 |
| Financial investments | 14 | 400,725 | 41,396 |
| Cash and cash equivalents | 19 | 81,701 | 117,557 |
| Total current assets | | 1,687,363 | 1,183,117 |
| TOTAL ASSETS | | 12,496,647 | 11,937,314 |
| EQUITY | | | |
| Ordinary shares | 20 | 2,104,799 | 2,104,799 |
| Treasury shares | 20 | (81,892) | (82,109) |
| Revaluation reserve for available-for-sale investments | 14 | (5,267) | (10,791) |
| Additional paid in capital | 20 | 232,275 | - |
| Retained earnings | | 3,792,124 | 3,379,703 |
| TOTAL EQUITY | | 6,042,039 | 5,391,602 |
| LIABILITIES | | | |
| Non-current liabilities | | | |
| Long-term borrowings | 21 | 826,917 | 1,675,789 |
| Long-term obligations under finance lease | 23 | 12,157 | 30,152 |
| Deferred income tax liability | 24 | 459,965 | 261,643 |
| Deferred revenue | 25 | 344,999 | 713,444 |
| Post-retirement benefit obligations | 26 | 199,068 | 228,627 |
| Government grants | 3 | - | 162,139 |
| Other long-term liabilities | 28 | 92,955 | 55,811 |
| Total non-current liabilities | | 1,936,061 | 3,127,605 |
| Current liabilities | | | |
| Current portion of long-term borrowings | 21 | 2,876,063 | 1,787,973 |
| Short-term obligations under finance lease | 23 | 31,379 | 46,827 |
| Accounts payable and accrued liabilities | 27 | 1,123,280 | 1,227,803 |
| Taxes payable, other than income tax | | 201,703 | 160,050 |
| Deferred revenue, current portion | 25 | 286,122 | 195,454 |
| Total current liabilities | | 4,518,547 | 3,418,107 |
| TOTAL LIABILITIES | | 6,454,608 | 6,545,712 |
| TOTAL EQUITY AND LIABILITIES | | 12,496,647 | 11,937,314 |

Approved for issue and signed on behalf of the Board of Directors on 21 May 2010.


L.N. Shafigoullin
General Director


M.N. Agafonova
Head of Finance

The accompanying notes on pages 5 to 34 are an integral part of these consolidated financial statements.

OJSC TATTELECOM
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(in thousands of Russian Roubles)

| | Note | For the year ended 31 December | |
|--|------|--------------------------------|------------------|
| | | 2009 | 2008 |
| Revenue | 9 | 5,519,614 | 5,298,479 |
| Operating expenses | 10 | (4,118,993) | (4,196,054) |
| Operating profit | | 1,400,621 | 1,102,425 |
| Finance income | | 24,012 | 29,171 |
| Finance cost | 11 | (497,752) | (268,970) |
| Foreign exchange loss | | (55,242) | (118,694) |
| Profit before income tax | | 871,639 | 743,932 |
| Income tax expense | 24 | (194,107) | (178,278) |
| Profit for the year | | 677,532 | 565,654 |
| Other comprehensive income: | | | |
| Actuarial gain, net of deferred tax charge of RR 2,962 (2008: RR 11,168) | 26 | 11,848 | 44,661 |
| Gain (loss) on revaluation of available-for-sale investments, net of deferred tax charge of RR 1,381 (2008: deferred tax credit of RR 8,509) | 14 | 5,524 | (34,038) |
| Total comprehensive income for the year attributable to the owners of the Company | | 694,904 | 576,277 |
| Weighted average number of outstanding ordinary shares | | 20,419,338,080 | 20,421,581,719 |
| Earnings per ordinary share, basic and diluted, in roubles per share | | 0.034 | 0.028 |

The accompanying notes on pages 5 to 34 are an integral part of these consolidated financial statements.

OJSC TATTELECOM
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(in thousands of Russian Roubles)

| | Note | Ordinary shares | Additional paid in capital | Revaluation reserve for available for sale investments | Treasury shares | Retained earnings | Total |
|--|--------|--------------------|----------------------------------|--|--------------------|----------------------|------------------|
| Balance at 31 December 2007 | | <u>2,104,799</u> | <u>–</u> | <u>23,247</u> | <u>(81,064)</u> | <u>3,026,643</u> | <u>5,073,625</u> |
| Total comprehensive income for the year | 14, 26 | – | – | (34,038) | – | 610,315 | 576,277 |
| Dividends declared | | – | – | – | – | (257,255) | (257,255) |
| Purchase of treasury shares | | – | – | – | (1,045) | – | (1,045) |
| Balance at 31 December 2008 | | <u>2,104,799</u> | <u>–</u> | <u>(10,791)</u> | <u>(82,109)</u> | <u>3,379,703</u> | <u>5,391,602</u> |
| Adjustment to property, plant and equipment contributed by ultimate parent | 3 | – | 232,275 | – | – | (70,136) | 162,139 |
| Total comprehensive income for the year | 14, 26 | – | – | 5,524 | – | 689,380 | 694,904 |
| Dividends declared | | – | – | – | – | (206,823) | (206,823) |
| Sale of treasury shares | | – | – | – | 217 | – | 217 |
| Balance at 31 December 2009 | | <u>2,104,799</u> | <u>232,275</u> | <u>(5,267)</u> | <u>(81,892)</u> | <u>3,792,124</u> | <u>6,042,039</u> |

The accompanying notes on pages 5 to 34 are an integral part of these consolidated financial statements.

OJSC TATTELECOM
CONSOLIDATED STATEMENT OF CASH FLOWS
(in thousands of Russian Roubles)

| | Note | For the year ended 31 December | |
|--|------|--------------------------------|--------------------|
| | | 2009 | 2008 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Profit before income tax | | 871,639 | 743,932 |
| Adjustments for: | | | |
| Depreciation of property, plant and equipment | 12 | 1,000,376 | 720,144 |
| Amortization of intangible assets | 13 | 95,895 | 62,405 |
| Loss on disposal of property, plant and equipment | | 86,583 | 89,949 |
| Finance income | | (24,012) | (29,171) |
| Finance costs | 11 | 497,752 | 268,970 |
| (Gain) loss on impairment of trade accounts receivable | | (142,040) | 28,215 |
| Loss on write off of financial investments | 14 | - | 109,300 |
| Foreign exchange loss | | 55,242 | 118,694 |
| Other non-cash operating expenses | | 8,298 | 24,819 |
| Operating cash flows before changes in working capital: | | 2,449,733 | 2,137,257 |
| Decrease (increase) in trade accounts receivable | | 34,651 | (76,405) |
| Increase in inventory | | (9,874) | (3,927) |
| (Increase) decrease in advances paid and prepaid expenses | | (72,379) | 13,273 |
| Decrease in prepaid taxes, other than income tax | | 44,397 | 15,211 |
| Decrease in accounts payable and accrued liabilities | | (258,803) | (76,008) |
| Increase in taxes payable, other than income tax | | 41,653 | 111,526 |
| Decrease in deferred revenue | | (277,777) | (77,275) |
| Changes in working capital | | 1,951,601 | 2,038,830 |
| Income taxes paid | | (19,692) | (231,527) |
| Interest paid | | (504,003) | (288,694) |
| Net cash from operating activities | | 1,427,906 | 1,523,431 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Purchases of property, plant and equipment | | (886,712) | (1,525,745) |
| Purchases of intangible assets | | (118,232) | (25,303) |
| Proceeds from sale of property, plant and equipment | | 82,328 | - |
| Interest received | | 11,743 | 8,152 |
| Purchases of investments | | (525,587) | (371,636) |
| Acquisition of subsidiaries, net of cash acquired | | (16,970) | - |
| Proceeds from repayment of investments | | 30,000 | 240,003 |
| Net cash used in investing activities | | (1,423,430) | (1,674,529) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Proceeds from bonds issue | | 1,620,131 | - |
| Repayment of bonds | | (219,187) | (1,481,590) |
| Proceeds from borrowings | | 1,111,620 | 3,567,169 |
| Repayment of borrowings | | (2,332,388) | (1,709,259) |
| Finance lease payments | | (33,443) | (94,500) |
| Dividends paid | | (187,065) | (143,390) |
| Net cash (used in) from financing activities | | (40,332) | 138,430 |
| NET DECREASE IN CASH AND CASH EQUIVALENTS | | (35,856) | (12,668) |
| CASH AND CASH EQUIVALENTS, beginning of the year | | 117,557 | 130,225 |
| CASH AND CASH EQUIVALENTS, end of the year | | 81,701 | 117,557 |

The accompanying notes on pages 5 to 34 are an integral part of these consolidated financial statements.

1. OJSC TATTELECOM AND ITS OPERATIONS

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) for the year ended 31 December 2009 for OJSC Tatttelecom (“Tatttelecom” or the “Company”) and its subsidiaries (together referred to as the “Group”).

The Company was incorporated on 22 July 2003 as an open joint stock company and is domiciled in the Russian Federation.

Tatttelecom is the largest telecommunications operator in the Republic of Tatarstan (“RT”). The Company operates through seven regional branches: Almetyevsky, Arsky, Buinsky, Nizhnekamsky, Chistopolsky, Kazansky and Naberezhno-Chelninsky zonal telecommunication nodes.

The Company’s registered and principal place of business is N. Ershova street, 57, 420061, Kazan, Republic of Tatarstan, Russian Federation.

As of 31 December 2009 and 2008, the Company’s major shareholders were as follows:

| | <u>% of ownership</u> |
|---------------------------|-----------------------|
| OJSC Svyazinvestneftekhim | 87.2% |
| Other | 12.8% |
| Total | <u>100.0%</u> |

The Company’s ultimate parent and controlling party is the Republic of Tatarstan.

The Group consists of the Company and the following subsidiaries. All Group companies are incorporated in the Russian federation.

| Subsidiary | % of ownership as at 31 December | | | Immediate parent |
|----------------------|----------------------------------|------|--|-------------------|
| | 2009 | 2008 | | |
| LLC Kamatel-K | 100 | – | | OJSC Tatttelecom |
| LLC Kamatel K | 100 | – | | OJSC Tatttelecom |
| LLC LiNet | 100 | – | | OJSC Tatttelecom |
| LLC Elemte Invest | 100 | 100 | | OJSC Tatttelecom |
| LLC StroiRemKompania | 89 | – | | LLC Elemte Invest |

2. OPERATING ENVIRONMENT OF THE GROUP

The Russian Federation displays certain characteristics of an emerging market, including relatively high inflation and high interest rates. The global financial crisis has had a severe effect on the Russian economy since mid-2008:

- Lower commodity prices have resulted in lower income from exports and thus lower domestic demand. Russia’s economy contracted in 2009.
- The rise in Russian and emerging market risk premia resulted in a steep increase in foreign financing costs.
- The depreciation of the Russian Rouble against hard currencies (compared to RR 25.3718 for 1 US Dollar at 1 October 2008) increased the burden of foreign currency corporate debt, which has risen considerably in recent years.
- As part of preventive steps to ease the effects of the situation in financial markets on the economy, the government incurred a large fiscal deficit in 2009.

The volume of financing available has significantly reduced since 2008. Such circumstances may affect the ability of the Group to obtain new borrowings and re-finance its existing borrowings at terms and conditions similar to those applied to earlier transactions.

2. OPERATING ENVIRONMENT OF THE GROUP (CONTINUED)

The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and frequent changes, and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

Management is unable to predict all developments in the economic environment which could have an impact on the Group's operations and consequently what effect, if any, they could have on the future financial position of the Group.

3. SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

The accompanying consolidated financial statements have been prepared under the historical cost convention as modified by the initial recognition at the fair value of financial instruments and the carrying amounts of equity items in existence at 31 December 2002 which include the adjustment for the effects of hyperinflation, calculated using conversion factors derived from the Russian Federation Consumer Price Index published by the Russian Statistics Agency.

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below.

The preparation of the consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The area involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

The Company and its subsidiaries maintain their accounts and prepare financial statements for regulatory purposes in accordance with Russian accounting legislation. The accompanying consolidated financial statements are based on statutory accounting records, which are maintained under historical cost convention. At each reporting date, the Company makes appropriate adjustments and reclassifications to its stand-alone statutory financial statements and those of its subsidiaries for the purpose of fair presentation in accordance with IFRS.

Revised accounting and changes in presentation

In 2009 the Company revised its accounting for contributions of property, plant and equipment received from the Company's ultimate parent to treat them as capital contributions. Previously, these contributions were credited to the government grants caption of the consolidated statement of financial position and accreted into income over the life of the respective assets, in accordance with IAS 20 "Accounting for Government Grants and Disclosure of Government Assistance". The effect of this revision as of 31 December 2009 resulted in retained earnings being reduced by RR 70,136; government grants balance reduced by RR 162,139 and additional paid in capital increased by RR 232,275.

