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 is a nongovernmental, not-for-profit association, and their Board of Directors comprises representatives of the major cellular communications companies, including us. The Association has not adopted any procedures for collecting such payments, nor have such procedures been established by Russian legislation. To date, we have not made any payments pursuant to any of the current operating licenses issued to us and our consolidated subsidiaries. Further, our management believes that we will not be required to make any such payments in the future. In relation to these uncertainties, we have not recorded a contingent liability in the accompanying audited consolidated financial statements.

Useful Lives of Property Plant and Equipment

We calculate depreciation expense for property, plant and equipment on a straight-line basis over their estimated useful lives. We establish useful lives for each category of property, plant and equipment based on our assessment of the use of the assets and anticipated technology evolution. We review and revise if appropriate the assumptions used in the determination of useful lives of property, plant and equipment at least on an annual basis.

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, we have corrected our accounting practices for 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.

Impairment of Long-lived Assets

We periodically evaluate the recoverability of the carrying amount of our long-lived assets in accordance with Statement of Financial Accounting Standard (“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, we compare 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, we record 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.

Translation Methodology

We use the U.S. dollar as the functional currency for us and most of our subsidiaries because the majority of our and 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, Turkmenistan and Belarus maintains its records and prepares its financial statements in the local currency, either the Russian ruble, the Ukrainian hryvnia, the Uzbek som, Turkmenian manat or the Belarusian ruble, in accordance with the requirements of local statutory accounting and tax legislation.

Translation (re-measurement) of financial statements denominated in local currencies into U.S. dollars has been performed in accordance with the provisions of SFAS No. 52 “Foreign Currency Translation.”

For our subsidiaries where the 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 currency exchange and transaction gains in our consolidated statements of operations.

For UMC and Kuban-GSM, where the functional currency is the local currency, the Ukrainian hryvnia and the 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 the 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. A cumulative translation adjustment, related to the translation of UMC and Kuban-GSM, in the amount of $47.9 million was reported as accumulated other comprehensive income in our audited consolidated balance sheet as of December 31, 2005.

Taxation

Generally, tax declarations remain open and subject to inspection for a period of three years following the tax year. While most of our tax declarations have been inspected without significant penalties, these inspections do not eliminate the possibility of re-inspection.

We believe that we have adequately provided for tax liabilities in our financial statements; however, the risk remains that relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant. See Note 22 to our audited consolidated financial statements.

We recognize deferred tax assets and liabilities 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. We record valuation allowances for deferred tax assets when it is likely that these assets will not be realized.

New Accounting Pronouncements

In March 2005, the Financial Accounting Standards Board, or 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

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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 No. 47 is effective beginning January 1, 2006. We are currently assessing the impact of Interpretation No. 47 on our consolidated financial position and results of operations.

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123 (revised) “Share-Based Payment” (SFAS No. 123R), which requires all companies to measure compensation cost for all share-based payments (including employee stock options) at fair value. In April 2005, the SEC announced that it would provide a phased-in implementation process for SFAS No. 123R. As a result of this phased-in process, the provisions of SFAS No. 123R must be adopted by most public entities no later than the beginning of the first fiscal year commencing after June 15, 2005. SFAS No. 123R applies to all awards granted after the required effective date and to awards modified, repurchased or cancelled after that date. Effective for the fiscal year beginning January 1, 2006, we will adopt the provisions of SFAS No. 123R using a modified version of the prospective application. Under this transition method, compensation cost will be recognized on or after the effective date for the portion of outstanding awards for which the requisite service has not yet been rendered, based on the grant date fair value of those awards previously calculated under SFAS No. 148 for pro forma disclosures. The adoption of SFAS No. 123R does not have a material impact on our consolidated financial position or results of operations.

In March 2005, the SEC issued Staff Accounting Bulletin, or SAB, No. 107, “Share Based Payment” (SAB 107). SAB 107 summarizes the views of the SEC staff regarding the interaction between SFAS 123R and certain SEC rules and regulations, and provides the staff’s views regarding the valuation of share-based payment arrangements for public companies. We adopt SAB 107 concurrently with the adoption of SFAS 123(R) effective from January 1, 2006. The adoption of SAB 107 does not have a material impact on our consolidated financial position or results of operations.

In May 2005, the FASB issued Statement of Financial Accounting Standards No. 154, “Accounting Changes and Error Corrections” (SFAS No. 154), which replaces APB Opinion No. 20, “Accounting Changes” and SFAS No. 3, “Reporting Accounting Changes in Interim Financial Statements.” SFAS No. 154 changes the requirements for the accounting and reporting of a change in accounting principle and is applicable to all voluntary changes and to changes required by an accounting pronouncement if such pronouncement does not specify transition provisions. SFAS No. 154 requires retroactive application to the prior periods’ financial statements of changes in accounting principle. In cases when it is impracticable to determine the period-specific or cumulative effects of an accounting change, the statement provides that the new accounting principle should be applied as of the earliest period for which retroactive application is practicable or, if impracticable to determine the effect of a change to all prior periods, prospectively from the earliest date practicable. This Statement shall be effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

In June 2005, the Emerging Issues Task Force, or EITF, reached a consensus on EITF Issue No. 05-6, “Determining the Amortization Period for Leasehold Improvements.” As part of a business combination, the acquiring entity will often assume existing lease agreements of the acquired entity and acquire the related leasehold improvements. The issues are whether the “lease term” should be reevaluated at consummation of a purchase business combination and whether the amortization period for acquired leasehold improvements should be reevaluated by the acquiring entity in a business combination. The consensus reached by EITF No. 05-6 is effective for leasehold improvements that are purchased or acquired in reporting periods beginning June 29, 2005. The adoption of EITF No. 05-6 did not have a material impact on our financial position and results of operations.

In October 2005, the FASB issued FASB Staff Position, or FSP, FAS 13-1, “Accounting for Rental Costs Incurred during a Construction Period.” Under the provisions of FSP FAS 13-1, lessees may not capitalize rental costs incurred on building or ground operating leases during a construction period. Instead, rental costs should be expensed on a straight-line basis starting at the beginning of the lease term, *i.e.*, when the lessee takes possession of or is given control of the leased property. The provisions of FSP FAS 13-1 are effective starting with the first reporting period beginning after December 15, 2005. We are currently assessing the impact of FSP FAS 13-1 on our consolidated financial position and results of operations.

Trend Information

Sales

In 2005, our revenues increased by 28.9% from $3,887.0 million to $5,011.0 million. Our subscriber base increased to 58.2 million subscribers as of December 31, 2005, from 34.2 million as of December 31, 2004, or by 70.2%. In 2004, our revenues increased by 52.7% from $2,546.2 million to $3,887.0 million. Our subscriber base increased to 34.2 million subscribers as of December 31, 2004 from 16.7 million as of December 31, 2003, or by 104.8%.

Average monthly service revenue per subscriber in Russia fell from $17 in 2003 to $12 in 2004 due to the introduction of lower tariffs in the Moscow license area and generally lower tariffs in regions, as well as penetration to mass-market. This trend continued in the year ended December 31, 2005, as average monthly service revenue per subscriber in Russia decreased to $8 for the year ended December 31, 2005.

In 2004 and 2005, more than half of our subscriber growth occurred outside of the Moscow license area. However, as a result of competition and the tariff structure providing for lower price levels in the Russian regions outside of the Moscow license area, average monthly service revenue per subscriber in the Russian regions remains lower than in the Moscow license area (though costs are generally lower there, as well). See “Item 3. Key Information—D. Risk Factors—Risks Relating to Our Business—Increased competition and a more diverse subscriber base have resulted in decreasing average monthly service revenues per subscriber, which may materially adversely affect our results of operations.” We generally expect to see a continued decline in average monthly service revenue per subscriber due to the growth in the regional subscriber base outside Moscow and introduction of lower tariff plans or decrease in prices of the existing tariff plans in connection with our competitive marketing efforts.

UMC experienced subscriber growth from 3.4 million subscribers at December 31, 2003, to 7.4 million subscribers at December 31, 2004, and 13.3 million at December 31, 2005, and we expect this trend to continue, assuming the Ukrainian economy continues to grow. Average monthly service revenue per subscriber decreased in 2005 to $10 from $13 in 2004 as a result of an extensive mass-marketing campaign focused on Ukraine’s youth.

Uzdunrobita experienced an 87.1% increase in subscriber growth from 310,000 subscribers at December 31, 2004 to 580,000 subscribers at December 31, 2005, and we expect this trend to continue due to Uzdunrobita’s leading position in terms of subscribers and Uzbekistan’s low penetration rate. Average monthly service revenue per subscriber peaked at $16 in 2005.

Inventory

Overall, our inventory was $156.7 million at December 31, 2005, as compared to $89.5 million at December 31, 2004. The increase is mainly explained by a significant increase in purchases made in 2005 as part of our capital expenditure spending to support expansion and network maintenance requirements.

Churn

Churn, as we define it, includes internal churn within our subscriber base, *i.e.*, it includes subscribers who disconnect from our network in order to enroll in another tariff plan offered by us. Internal churn increased following the launch in November 2002 of our “Jeans” tariff plan. See “—Subscriber Data” above. Our subscriber churn in Russia decreased from 47.3% in 2003 to 27.5% in 2004 as a result of certain marketing initiatives we launched with the aim of increasing subscriber loyalty, and this trend continued in 2005 as our subscriber churn for the year ended December 31, 2005, was 20.7%. Although our subscriber churn in Russia decreased for the year ended December 31, 2005, we believe that subscriber churn is highly dependent on competition and the number of mass-market subscribers in our overall subscriber mix. Mass-market subscribers generally choose to prepay their mobile phone usage by purchasing pre-paid packages and are more likely to switch providers to take advantage of low-tariff promotions. As a result, competition for these subscribers will likely lead to sustained downward pressure on tariffs. Other factors influencing subscriber churn include the absence of connection fees and long-term service contracts between us and our subscribers in Russia, both of which prevent early subscriber churn.

Off-balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Obligations under guarantee contracts

As of December 31, 2005 and 2004, our off-balance sheet arrangements consisted of debt guarantees issued to related parties as follows:

	Guaranteed amount outstanding at December 31,	
	2005	2004
	(in millions)	
Invest-Svyaz Holding	$3.5	$21.6
MTS Belarus	9.0	25.0
Total	**$12.5**	**$46.6**

We issued guarantees to various financial institutions on behalf of Invest-Svyaz Holding, a wholly-owned subsidiary of Sistema. Invest-Svyaz Holding's primary business is leasing various types of telecommunications and other assets to us. See Note 17 to our audited consolidated financial statements for additional information regarding these transactions. We classify these leases as capital leases in our consolidated financial statements and the present value of future lease payments is reflected as a liability in our consolidated balance sheet.

We issued financial guarantees on behalf of MTS Belarus, our equity investee to assist it with its financing needs. See Note 19 to our audited consolidated financial statements. Under each of the guarantees outstanding as of December 31, 2005, we could be required to compensate financial institutions in the event of the borrower's default. We are currently not aware of any events, and do not anticipate that any event will occur, that would cause a default of the borrowers and, therefore, require us to fulfill our obligations to make payments under these guarantees. As of December 31, 2005, these guarantees are reflected in our consolidated balance sheet at their fair values of $0.6 million.

Obligations under derivative contracts

In connection with our acquisition of 51% of the common shares and 50% of the preferred shares of TAIF Telcom in April 2003, we entered into call and put option agreements with shareholders of TAIF Telcom to acquire the remaining 49% of the common shares and 50% of the preferred shares of TAIF Telcom. The exercise periods for the call option on the common shares was 48 months from the acquisition date and for the put option on the common shares was 36 months following an 18-month period after the acquisition date. The call and put option agreements for the common shares stipulated a minimum purchase price of $49.0 million plus 8% per annum commencing from the acquisition date. The exercise periods for the call option on the preferred shares was 48 months following a 24-month period after the acquisition date and for the put option on the preferred shares was a 24-month period from the acquisition date. The call and put option agreements for the preferred shares stipulated a minimum purchase price of $10.0 million plus 8% per annum commencing from the acquisition date. We exercised our call option to acquire the remaining shares in September 2004 and completed the acquisition in October 2004.

In connection with our acquisition of 74% of the shares in Uzdunrobita in August 2004, we entered into call and put option agreements with the existing shareholders of the company to acquire the remaining 26% of the shares. See Note 3 to our audited consolidated financial statements. The exercise period for the 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. The fair value of the put option was approximately $5.9 million as of December 31, 2005.

In December 2004, we entered into two variable-to-fixed interest rate swap agreements with ABN AMRO Bank N.V and with HSBC Bank plc to hedge our exposure to variability of future cash flows caused by the change in LIBOR related to the syndicated loan. We agreed with 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. We 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, 2005, we recorded an asset of $3.6 million in relation to these contracts in the accompanying consolidated balance sheet and a gain of $2.8 million net of tax of $0.8 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 December 2005, we acquired a 51.0% stake in Tarino for $150.0 million in cash. Tarino was at that time the indirect owner, through its wholly-owned subsidiaries, of Bitel, a Kyrgyz company holding a GSM 900/1800 license for the entire territory of Kyrgyzstan. Concurrently with the purchase of a 51.0% stake, we entered into a put and call option agreement with the shareholder of Tarino to acquire the remaining 49.0% interest in Tarino. The call option is exercisable by us from November 22, 2005 to November 17, 2006, and the put option is exercisable by the seller from November 18, 2006 to December 8, 2006. The call and put option price is $170.0 million. The put and call option were recorded at fair value, which approximated $nil at December 31, 2005, in the consolidated balance sheet.

Tabular Disclosure of Contractual Obligations

We have various contractual obligations and commercial commitments to make future payments, including debt agreements, lease obligations and certain committed obligations. The following table summarizes our future obligations (including capital lease interest) under these contracts due by the periods indicated as of December 31, 2005:

	2006	2007-2008	2009-2010	2011-thereafter	Total
Contractual Obligations:					