Translation differences resulting from the use of these rates have been accounted for as foreign currency exchange gains and losses 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 $23.0 million was reported as accumulated other comprehensive income in our audited consolidated balance sheet.

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 23 to our audited consolidated financial statements and "Item 8. Financial Information—B. Significant Changes" for information regarding a recent tax audit and related assessment by the tax authorities.

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 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" ("FIN46"), 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. We were required to apply the provisions of FIN. 46R in the first quarter 2004. As we 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 our financial condition or results of operations as of December 31, 2004.

In September 2004, the Emerging Issues Task Force (or 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. EITF Issue No. 04-1 is effective for reporting periods beginning after October 13, 2004. We do not anticipate that the adoption of EITF Issue No. 04-1 will have a material impact on our financial position or results of operations.

At the September 2004 meeting of the EITF, the SEC staff issued an announcement D-108 "Use of the residual method to value acquired assets other then 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, we performed our annual impairment test to measure the fair value of our 900 and 1800 MHz licenses in our national footprint using the residual value approach. Under this new accounting guidance, we 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, FASB issued SFAS No. 123R (revised 2004), "Share-Based Payment," a revision of SFAS No. 123, "Accounting for Stock-Based Compensation." SFAS No. 123R supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees." The statement focuses primarily on accounting for translations in which we obtain 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, we will apply this new standard to our interim reporting period beginning July 1, 2005. We have not yet determined the amount of impact on the consolidated statements of operations following adoption and subsequent to 2005 or the transition method we will use. We do not believe that results of the adoption of SFAS No. 123R will be significant to our consolidated financial position or results of operations.

In March 2005, the SEC released Staff Accounting Bulletin 107, "Share-Based Payments," or SAB 107. The interpretations in SAB 107 express views of the SEC staff regarding the interaction between SFAS No. 123R and certain SEC rules and regulations, and provide the SEC 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 non-employees, 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 and the modification of employee share options prior to adoption of SFAS No. 123R.

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. We are currently in the process of assessing effects of Interpretation 47 on our consolidated financial position and results of operations.

Trend Information

Sales

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%. Our revenues for the year ended December 31, 2003 grew by 87.0% to $2,546.2 million in comparison to $1,361.8 million for the year ended December 31, 2002. Our subscriber base increased from 6.6 million subscribers as of December 31, 2002 to 16.7 million as of December 31, 2003, or by 153.0%.

Average monthly service revenue per subscriber in Russia fell from $23 in 2002 to $17 in 2003 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, 2004 as average monthly service revenue per subscriber in Russia decreased to $12 for the year ended December 31, 2004.

In 2003 and 2004, 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 of 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 1.7 million subscribers at December 31, 2002 to 3.4 million subscribers at December 31, 2003 and 7.4 million at December 31, 2004, and we expect this trend to continue, assuming the Ukrainian economy continues to grow. The significant increase in subscriber growth is also the result of a change in the definition of a subscriber with respect to UMC's prepaid tariff subscribers, which starting in the fourth quarter of 2004 includes an individual or organization whose account shows chargeable activity within 183 days, rather than the previous 90-day period. Average monthly service revenue per subscriber decreased in 2004 to $13 from $15 in 2003 as a result of an extensive marketing campaign that promoted various new tariff offerings. We generally expect to see a continued decline in average monthly service revenue per subscriber in Ukraine due to increased competition

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 increased from 33.9% in 2002 to 47.3% in

2003. We believe that this trend reversed in the year ended December 31, 2004 as a result of decrease in internal churn and certain marketing initiatives we launched with the aim of increasing subscriber loyalty. Our subscriber churn for the year ended December 31, 2004 was 27.5%, as compared to 47.3% for 2003. Although our subscriber churn in Russia decreased for the year ended December 31, 2004, 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. In order to decrease subscriber churn, in 2004, we launched a new marketing campaign that provides a 15% discount for services rendered to certain contract subscribers if they do not terminate their contracts within one year of activation. Other initiatives taken to limit the churn rate include preventive SMSs or call center calls to subscribers offering different packages and services.

Off-balance Sheet Arrangements

Obligations under guarantee contracts

As of December 31, 2004 and 2003, our off-balance sheet arrangements consisted of debt guarantees issued to related parties as follows:

	Guaranteed amount outstanding at December 31,	
	2004	**2003**
	(in millions)	
Invest-Svyaz Holding	$21.6	$21.6
MTS Belarus	25.0	14.5
Total	**$46.6**	**$36.1**

We issued guarantees to various financial institutions on behalf of Invest-Svyaz Holding, our shareholder and 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 audited 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, 2004, 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. These guarantees are not reflected in our consolidated balance sheet due to the insignificance of their fair values.

Obligations under derivative contracts

In connection with our acquisition of 51% of the common shares and 50% of the preferred shares of TAIF Telecom 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 $0.9 million as of December 31, 2004.

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, 2004, we 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.

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, 2004:

	2005	2006-2007	2008-2009	2010-thereafter	Total
Contractual Obligations:					
Notes payable	$—	$—	$400,000	$400,000	$800,000
Bank loans	370,845	592,944	87,340	73,511	1,124,640
Interest payments	124,454	224,315	129,338	58,849	536,959
Capital leases	10,547	4,059	340	451	15,397
Operating leases and service agreements	45,889	32,053	18,028	35,475	131,445
Committed Investments:[(1)]					
Purchases of property, plant and equipment	164,700	—	—	—	164,700
Total	**$716,435**	**$853,371**	**$635,046**	**$568,286**	**$2,773,141**

(1) Under non-binding purchase commitments.

In addition, as of December 31, 2004, we had guaranteed indebtedness of related parties not reflected in our financial statements, due to the insignificance of its fair value, under which we could be potentially liable for $46.6 million. See Note 21 to our audited consolidated financial statements.