# MEGAFON

Condensed Consolidated Financial Statements
(Unaudited)

*Three months ended March 31, 2010 and 2009*
*With Independent Accountant's Report*

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# Independent Accountant's Report

The Board of Directors and Shareholders
OJSC MegaFon

We have reviewed the condensed consolidated balance sheet of OJSC MegaFon and subsidiaries as of March 31, 2010, and the related condensed consolidated statements of operations and cash flows for the three months ended March 31, 2010 and 2009. This condensed financial information is the responsibility of the Company's management.

We conducted our reviews in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States, the objective of which is the expression of an opinion regarding the financial information taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the condensed financial information referred to above for it to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheet of OJSC MegaFon and subsidiaries as of December 31, 2009, and the related consolidated statements of operations, shareholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated March 9, 2010, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2009, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

May 24, 2010

Ernst & Young LLC

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# MegaFon

## Condensed Consolidated Balance Sheets

*(In millions of Rubles)*

| | December 31, 2009 | March 31, 2010 (Unaudited) |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | 12,550 | **9,742** |
| Short-term investments | 49,114 | **61,071** |
| Accounts receivable, net of allowance for doubtful accounts of 861 and 942 at December 31, 2009 and March 31, 2010, respectively | 4,085 | **4,251** |
| Inventory | 1,219 | **2,071** |
| VAT receivable | 2,037 | **2,016** |
| Deferred tax assets | 772 | **889** |
| Prepaid expenses | 8,589 | **7,886** |
| Other current assets | 1,784 | **1,897** |
| Total current assets | 80,150 | **89,823** |
| Property, plant and equipment, net of accumulated depreciation of 99,993 and 107,296 at December 31, 2009 and March 31, 2010, respectively | 147,231 | **143,067** |
| Goodwill and intangible assets: | | |
| Goodwill | 498 | **498** |
| Intangible assets, net of accumulated amortization of 17,101 and 17,912 at December 31, 2009 and March 31, 2010, respectively | 16,869 | **16,401** |
| Other non-current assets | 1,432 | **1,509** |
| Total assets | 246,180 | **251,298** |

MegaFon

# Condensed Consolidated Balance Sheets (continued)

*(In millions of Rubles)*

| | Note | December 31, 2009 | March 31, 2010 (Unaudited) |
|---|---|---|---|
| **Liabilities** | | | |
| Current liabilities: | | | |
| Accounts payable | | 4,888 | **6,111** |
| Accounts payable to equipment suppliers | | 7,008 | **2,861** |
| Current portion of liability for marketing related licenses | 3 | 287 | **538** |
| Accrued compensation and social contributions | | 3,435 | **3,177** |
| Subscribers' prepayments | | 7,083 | **5,279** |
| Taxes payable | | 1,880 | **1,744** |
| VAT payable | | 1,240 | **3,734** |
| Deferred revenue | | 358 | **292** |
| Current portion of long-term debt | | 7,811 | **7,284** |
| Other current liabilities | | 645 | **470** |
| Total current liabilities | | 34,635 | **31,490** |
| Debt, less current portion | | 19,335 | **17,178** |
| Deferred tax liabilities, less current portion | | 2,070 | **2,243** |
| Asset retirement obligations | | 3,303 | **3,472** |
| Liability for marketing related licenses, less current portion | 3 | 1,054 | **739** |
| Deferred revenue, less current portion | 3 | 1,568 | **1,598** |
| Other non-current liabilities | | 301 | **377** |
| Total liabilities | | 62,266 | **57,097** |
| **Equity** | | | |
| MegaFon shareholders' equity: | | | |
| Common stock (par value of 10 Rubles, 6,200,002 shares authorized, issued and outstanding) | | 581 | **581** |
| Reserve fund | | 17 | **17** |
| Additional paid-in capital | | 13,870 | **13,870** |
| Retained earnings | | 169,199 | **179,482** |
| Accumulated other comprehensive loss | | (255) | **(246)** |
| Total MegaFon shareholders' equity | | 183,412 | **193,704** |
| Noncontrolling interests | | 502 | **497** |
| Total equity | | 183,914 | **194,201** |
| Total liabilities and equity | | 246,180 | **251,298** |

*The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.*
*See independent accountant's report*

MegaFon

# Condensed Consolidated Statements of Operations

*(In millions of Rubles)*
*(Unaudited)*

| | Note | Three months ended March 31, 2009 | 2010 |
|---|---|---|---|
| **Revenue** | 4 | 42,202 | **46,743** |
| Cost of services | 5 | 8,796 | **9,696** |
| **Gross margin** | | 33,406 | **37,047** |
| Sales and marketing expenses | 6 | 2,797 | **4,501** |
| Operating expenses | 7 | 9,678 | **11,124** |
| Depreciation, amortization and accretion | | 7,597 | **8,636** |
| **Operating income** | | 13,334 | **12,786** |
| Other income/(expense): | | | |
| Interest expense | | (409) | **(118)** |
| Interest income | | 708 | **1,030** |
| Other gain, net | | 18 | **22** |
| Gain/(loss) on derivatives, net | 8 | 241 | **(241)** |
| Foreign currency exchange gain/(loss) | | 441 | **(627)** |
| **Total other income/(expense), net** | | 999 | **66** |
| **Income before income taxes and noncontrolling interests** | | 14,333 | **12,852** |
| Provision for income taxes | | 3,225 | **2,577** |
| **Net income** | | 11,108 | **10,275** |
| Net loss attributable to noncontrolling interests | | 18 | **8** |
| **Net income attributable to MegaFon** | | 11,126 | **10,283** |

*The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.*
*See independent accountant's report*

MegaFon

# Condensed Consolidated Statements of Cash Flows

*(In millions of Rubles)*
*(Unaudited)*

| | Three months ended March 31, 2009 | 2010 |
|---|---|---|
| **Net cash provided by operating activities** | 19,122 | **20,384** |
| **Cash flows from investing activities:** | | |
| Purchases of property, plant and equipment and intangible assets | (8,473) | **(8,984)** |
| Proceeds from sale of property, plant and equipment | 39 | **293** |
| Acquisitions of subsidiaries, net of cash acquired | (553) | **(29)** |
| Decrease/(increase) in short-term investments | 7,899 | **(13,495)** |
| Net cash used in investing activities | (1,088) | **(22,215)** |
| **Cash flows from financing activities:** | | |
| Proceeds from long-term debt | 2,768 | **41** |
| Repayments of long-term debt | (594) | **(522)** |
| Deferred finance charges paid | (125) | **(90)** |
| Net cash provided by/(used in) financing activities | 2,049 | **(571)** |
| Effect of exchange rate changes on cash and cash equivalents | 14 | **(406)** |
| **Net increase/(decrease) in cash and cash equivalents** | 20,097 | **(2,808)** |
| Cash and cash equivalents at the beginning of the period | 6,465 | **12,550** |
| **Cash and cash equivalents at the end of the period** | 26,562 | **9,742** |

*The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.*
*See independent accountant's report*

## 1. Financial Presentation and Disclosures

Open Joint Stock Company MegaFon (the "Company" or "MegaFon") is a leading mobile operator in Russia and provides a broad range of voice, data and other telecommunication services to businesses, other telecommunications service providers and retail subscribers, with licenses to operate in all regions of Russia, covering a population of approximately 142 million. The Company intends, wherever possible, to offer its integrated telecommunication services under the "MegaFon" brand, although some services still carry local brand names because of recent acquisitions. In addition to its operations in Russia, the Company provides mobile services through its subsidiaries in the Republic of Tajikistan ("Tajikistan"), the Republic of Abkhazia ("Abkhazia") and the Republic of South Ossetia ("South Ossetia").

The accompanying condensed financial statements of the Company have been prepared in accordance with generally accepted accounting principles in the United States of America ("US GAAP") for interim financial reporting and do not include all disclosures required by US GAAP. The Company omitted certain disclosures which would substantially duplicate the disclosures contained in its 2009 audited consolidated financial statements, such as accounting policies and details of accounts which have not changed significantly in amount or composition. Additionally, the Company has provided disclosures where significant events have occurred subsequent to the issuance of its 2009 audited consolidated financial statements. Management believes that the disclosures are adequate to make the information presented not misleading if these financial statements are read in conjunction with the Company's 2009 audited consolidated financial statements and the notes related thereto. In the opinion of management, the financial statements reflect all adjustments of a normal and recurring nature necessary to present fairly the Company's consolidated financial position, results of operations and cash flows for the interim periods. The results of operations for the three months ended March 31, 2010 are not indicative of the operating results for the full year. These financial statements include information updated and subsequent events evaluated through May 24, 2010, the date these interim condensed consolidated financial statements were issued.

## 2. Summary of Significant Accounting Policies and Recent Accounting Pronouncements

*Foreign Currency Translation*

The functional currency of the Company and its subsidiaries domiciled in Russia, the Republic of Abkhazia and the Republic of South Ossetia is the Russian Ruble ("RUR") as a majority of their revenues, costs, property and equipment purchased, debt and trade liabilities is either priced, incurred, payable or otherwise measured in Rubles.

The functional currency of TT-Mobile, the Company's 75% owned subsidiary in Tajikistan, is the US dollar as a majority of its revenues, costs, property and equipment purchased, debt and trade liabilities is either priced, incurred, payable or otherwise measured in US dollars.

**2. Summary of Significant Accounting Policies and Recent Accounting Pronouncements (continued)**

*Income Taxes*

Provision for income taxes is made in the financial statements for taxation of profits in accordance with Russian legislation currently in force. The Company accounts for income taxes using the liability method required by the Financial Accounting Standards Board ("FASB") Accounting Standards Codification™ ("ASC") in ASC 740, *"Income Taxes"*. For interim reporting purposes, the Company also follows the provisions of accounting standard ASC 270, *"Interim Reporting"*, which requires the Company to account for income taxes based on the Company's estimate of the effective tax rate expected to be applicable for the full fiscal year on a current year-to-date basis.

The rate so determined is based on the currently enacted tax rate applicable to the Company, and includes estimates of the annual tax effect of items that do not have tax consequences and the realization of certain deferred tax assets.

The difference between income tax expense reported in the accompanying condensed consolidated financial statements and income before taxes for the three months ended March 31, 2010 and 2009, multiplied by the Russian statutory tax rate, is mainly due to non-deductibility of certain expenses for income tax purposes.

The Company recognizes accrued interest and penalties related to unrecognized tax liabilities in income taxes. As of March 31, 2010, the tax years ended December 31, 2007, 2008 and 2009 remained subject to examination by the tax authorities.

*Management Estimates*

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and the disclosure of contingent liabilities of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates. The most significant estimates with regard to the accompanying condensed consolidated financial statements relate to the allocation of purchase price to the fair value of net assets acquired in connection with business combinations, useful lives related to tangible and intangible assets, impairment tests of long-lived assets, deferred revenue, asset retirement obligations, fair value of derivative financial instruments, recoverability of deferred tax assets, income tax provision and allowance for doubtful accounts.

*Comparative Information*

Certain prior year amounts have been reclassified to conform to the presentation adopted in the current year.

**2. Summary of Significant Accounting Policies and Recent Accounting Pronouncements (continued)**

*Recent Accounting Pronouncements*

**Noncontrolling Interests.** In January 2010, the FASB issued guidance that amends accounting and disclosure requirements for a decrease in ownership in a business under existing US GAAP standards for consolidations. It also clarifies the types of businesses that are in the scope of these consolidations. As required by this guidance, the Company applied the amendments starting with its annual consolidated financial statements as of and for the year ended December 31, 2009 retrospectively to January 1, 2009. The adoption of this guidance did not have a material impact on the Company's financial statements.

**Equity.** In January 2010, the FASB issued an amendment to Topics 505 and 260 (Equity and Earnings Per Share), whereas the Board clarifies that the stock portion of a distribution to shareholders that allows them to elect to receive cash or stock with a limit on the amount of cash that will be distributed is not a stock dividend for purposes of applying Topics 505 and 260. This amendment is effective for the Company from January 1, 2010, and should be applied on a retrospective basis. The adoption of the guidance did not have a material impact on the Company's financial statements.

**Fair Value Measurement and Disclosures.** In January 2010, the FASB issued Accounting Standards Update ("ASU") 2010-6, "*Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*" that amends Topic 820, *Fair Value Measurements and Disclosures*, of the FASB Codification. ASU 2010-6 requires separate disclosure of significant transfers between Level 1 and Level 2 fair value measurement inputs and a description of the reasons for the transfers, and amends existing disclosure requirements in regards of level of disaggregation and inputs and valuation techniques. ASU 2010-6 is effective for the Company from January 1, 2010. The adoption of the guidance did not have a material impact on the Company's financial statements.

**Derivatives and Hedging.** In March 2010, the FASB issued an amendment to Subtopic 815-15, whereby the Board has provided the clarifications and related additional examples to improve financial reporting by resolving potential ambiguity about the breadth of the embedded credit derivative scope exception. The amendment is effective for each reporting entity at the beginning of its first fiscal quarter beginning after June 15, 2010. The Company is currently evaluating the impact of this guidance on its financial statements.

**Subsequent events.** In February 2010, the FASB issued an amendment to Subtopic 855-10, whereby the Board has clarified that if the financial statements have been revised, then an entity that is not an SEC filer should disclose both the date that the financial statements were issued or available to be issued and the date the revised financial statements were issued or available to be issued. The amendment is effective upon issuance, and its adoption did not have a material impact on the Company's financial statements.

**Variable Interest Entities ("VIE").** In June 2009, the FASB issued an accounting standard that amends the consolidation guidance for variable interest entities (ASC 810). The amendments significantly changed the overall consolidation analysis under the existing

**2. Summary of Significant Accounting Policies and Recent Accounting Pronouncements (continued)**

guidance. For the Company, this standard became effective from January 1, 2010. Accordingly, the Company reconsidered its previous conclusions, including (1) whether an entity is a VIE, (2) whether the enterprise is the VIE's primary beneficiary, and (3) what type of financial statements disclosures are required. The adoption of the standard did not have a material impact on the Company's financial statements.

**Revenue Arrangements with Multiple Deliverables.** In October 2009, the FASB issued ASU 2009-13, "*Multiple-Deliverable Revenue Arrangements",* which addresses how revenues should be allocated among all products and services included in the Company's multiple element sales arrangements. It establishes a selling price hierarchy for determining the selling price of each product or service included in a sale arrangement. The selling price used for each deliverable will be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific objective evidence is not available, or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. It replaces "fair value" with "selling price" in revenue allocation guidance. ASU 2009-13 will be effective prospectively for sales entered into or materially modified in fiscal years beginning on or after June 15, 2010. The FASB permits early adoption of ASU 2009-13, applied retrospectively to the beginning of the year of adoption. The Company is currently evaluating the impact of this ASU on its financial statements.

**3. Marketing Related Intangible Assets**

In April 2009, the Company and OJSC Rostelecom ("Rostelecom") entered into an agreement with the Organizational Committee of the 2014 XXII Olympic Winter Games and XI Paralympic Winter Games in Sochi to acquire rights and licenses to use the Olympic mascot, logos and other Olympic symbols and, in the case of the Company, to be referred to as "the General Mobile Partner of the 2014 XXII Olympic Winter Games". Under the agreement the Company committed to a payment of $65 million (1,909 at the exchange rate as of March 31, 2010) in cash to be made in several installments from 2009 through 2014. In addition, the Company and Rostelecom are jointly responsible to provide equal amounts of services in-kind of up to a combined total of $130 million (3,817 at the exchange rate as of March 31, 2010) from 2009 through 2014. The management of the Company believes that the risk of non-performance by Rostelecom of its responsibilities under the agreement is remote.

The Company obtained the rights and licenses in the third quarter of 2009, at which time the Company assumed a liability at the net present value of future cash installments of 1,334 and deferred revenue with a fair value of 1,516. The recognition of the intangible asset is treated as a non-cash item to the extent of the amount of the liability and deferred revenue recorded. The intangible asset is amortized using the reverse sum-of-the-years'-digits method over a period of approximately 5 years.

The fair value of deferred revenue recognized by the Company was estimated using the Discounted Cash Flow ("DCF") analysis (Level 3). The basis for the Company's cash flow

## 3. Marketing Related Intangible Assets (continued)

assumptions includes forecasted amounts and timing of services to be provided under the agreement. The Company used 7% as a discount rate. The Company recognized revenue from services in-kind in the amount of 45 for the three months ended March 31, 2010 and 18 for the year ended December 31, 2009. Payments to the Organizational Committee of the 2014 XXII Olympic Winter Games and XI Paralympic Winter Games in Sochi totaled $15.4 million as of March 31, 2010.

## 4. Revenues

Revenues for the three months ended March 31 are as follows:

| | 2009 | 2010 |
|---|---|---|
| Revenues from local subscribers | 34,853 | **38,583** |
| Revenues from interconnection charges | 6,006 | **6,471** |
| Sales of handsets and accessories | 618 | **939** |
| Roaming charges to other wireless operators | 393 | **303** |
| Connection fees | 15 | **76** |
| Other revenues | 317 | **371** |
| **Total revenues** | 42,202 | **46,743** |

## 5. Cost of Services

Cost of services for the three months ended March 31 are as follows:

| | 2009 | 2010 |
|---|---|---|
| Interconnection charges | 7,294 | **8,089** |
| Cost of handsets and accessories sold | 678 | **871** |
| Roaming expenses | 537 | **482** |
| Cost of SIM-cards | 259 | **244** |
| Other costs | 28 | **10** |
| **Total cost of services** | 8,796 | **9,696** |

## 6. Sales and Marketing Expenses

Sales and marketing expenses for the three months ended March 31 are as follows:

| | 2009 | 2010 |
|---|---|---|
| Advertising | 1,105 | **1,507** |
| Commissions to dealers for connection of new subscribers | 1,022 | **2,028** |
| Commissions to dealers for cash collection from subscribers | 670 | **966** |
| **Total sales and marketing expenses** | 2,797 | **4,501** |

## 7. Operating Expenses

Operating expenses for the three months ended March 31 are as follows:

| | 2009 | 2010 |
|---|---|---|
| Salaries and social charges | 3,304 | **4,327** |
| Rent | 2,075 | **2,532** |
| Operating taxes | 1,131 | **1,151** |
| Network repairs and maintenance | 889 | **877** |
| Radio frequency fees | 617 | **753** |
| Office maintenance | 319 | **365** |
| Bad debt expense | 384 | **298** |
| Professional services | 148 | **153** |
| Materials and supplies | 43 | **43** |
| Insurance | 52 | **28** |
| Other expenses | 716 | **597** |
| **Total operating expenses** | 9,678 | **11,124** |

Rent represents expenses related to the lease of premises for offices, base stations and switches.

## 8. Derivative Financial Instruments

The Company measures financial assets and financial liabilities at fair value on a recurring basis.

US GAAP standards establish a three-level fair value hierarchy, which prioritizes the inputs used in measuring fair value. These levels include:

Level 1: Quoted prices for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

## 8. Derivative Financial Instruments (continued)

Level 2: Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are non-active; inputs other than quoted prices that are observable and derived from or corroborated by observable market data.

Level 3: Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

During 2009 and the three months ended March 31, 2010, the Company entered into a number of dual-currency deposits with various banks. The dual-currency deposits are financial instruments which combine features of a time deposit and a sold foreign currency put option. The dual-currency deposits are settled either in the original deposit currency (Euro or US Dollar) or in another pre-agreed currency (Ruble, US Dollar or Euro) depending on which currency has depreciated relative to the other currency since the date of entering into the dual-currency deposit. All dual-currency deposits bear over-the-market interest rates which include a put option premium payable upon settlement. The purpose of entering into these financial instruments is for yield enhancement on the Company's foreign currency cash investments.

The Company held the following amounts of dual-currency deposits which are classified as cash and cash equivalents in the accompanying condensed consolidated balance sheets.

| | **December 31, 2009** | | **March 31, 2010** | |
|---|---|---|---|---|
| | **Deposited currency** | **Millions of Rubles** | **Deposited currency** | **Millions of Rubles** |
| Euro (in millions) | 25 | 1,084 | **45** | **1,787** |
| US Dollar (in millions) | 30 | 907 | — | — |
| Total | | 1,991 | | **1,787** |

The respective embedded derivative financial instrument, which is the put option, is bifurcated and measured at fair value using the Black-Scholes model (Level 2). For accounting purposes, the Company reports all gains and losses from the change in fair value of these derivative financial instruments directly in the accompanying condensed consolidated statements of operations.

In the third quarter of 2006 and the second quarter of 2007, the Company entered into several long-term fixed-to-fixed rate cross-currency swaps. These derivative financial instruments are used to limit exposure to changes in foreign currency exchange rates on certain long-term debt denominated in foreign currencies.

The swaps effectively converted, using the then-effective foreign currency exchange rates, some of the Company's outstanding fixed-to-fixed rate long-term US dollar and Euro denominated loans (specifically the EKN, Finnvera, Finnvera II and Finnvera III Credit Facilities) into synthetically equivalent Ruble long-term loans with fixed rates ranging from 3.95% to 6.65%. The carrying amount of such long-term loans was 3,501 as of December 31,

## 8. Derivative Financial Instruments (continued)

2009 and 3,258 as of March 31, 2010. For accounting purposes, the Company has chosen not to designate these derivatives as hedging instruments, and therefore reports all gains and losses from the change in fair value (Level 2) of these derivative financial instruments directly in the consolidated statements of operations.

Gains/(losses) on derivatives for the three months ended March 31 are as follows:

| | 2009 | 2010 |
|---|---|---|
| Put options sold | — | **57** |
| Foreign currency swaps | 241 | **(298)** |
| **Total gain/(loss) on derivatives, net** | 241 | **(241)** |

The derivatives are valued using standard valuation techniques as no quoted market prices exist for the instruments. The principal technique used to value these instruments is through comparing the foreign currency exchange rates at the time that the derivatives were acquired to the forward exchange rates quoted in the existing market which is inactive as of the valuation date. The key inputs include interest rate yield curves, foreign exchange spot and forward rates. The fair value of these derivatives includes the effects of the counterparty's non-performance risk, including credit risk.

Fair values of these derivative financial instruments in the accompanying condensed consolidated balance sheets are presented below:

| Derivative instruments | Balance sheet location | December 31, 2009 | March 31, 2010 |
|---|---|---|---|
| Put options sold | Other current assets | 6 | **8** |
| Foreign currency swaps | Other current assets | 406 | **240** |
| | Other non-current assets | 328 | **196** |
| **Total derivatives** | | 740 | **444** |

The fair value of financial instruments, including cash, cash equivalents and derivative financial instruments, which are included in current assets and liabilities, accounts receivable and accounts payable approximates the carrying value of these items due to the short-term nature of these amounts.

The Company, using available market information and appropriate valuation methodologies, where they exist, has determined the estimated fair values of financial instruments. However, judgment is necessarily required to interpret market data to determine the estimated fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. While management has used available market information in estimating the fair value of financial instruments, the

## 8. Derivative Financial Instruments (continued)

market information may not be fully reflective of the value that could be realized in the current circumstances.

The Company, in connection with its current activities, is exposed to various financial risks, such as foreign currency risks, interest rate risks and credit risks. The Company manages these risks and monitors their exposure on a regular basis.

## 9. Commitments, Contingencies and Uncertainties

*Russian Environment and Current Economic Situation*

Russia continues to engage in economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Russian government.

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. The recent global financial crisis has resulted in a decline in the gross domestic product, capital markets instability, significant deterioration of liquidity in the banking sector, and tighter credit conditions within Russia. While the Russian government introduced a range of stabilization measures aimed at providing liquidity to Russian banks and companies, there continues to be uncertainty regarding the access to capital and cost of capital for the Company and its counterparties, which could affect the Company’s financial position, results of operations and business prospects.

While management believes it is taking appropriate measures to support the sustainability of the Company’s business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Company’s results and financial position in a manner not currently determinable.

*Telecom licenses capital commitments*

In May 2007, MegaFon was awarded a license that expires on May 21, 2017, for the provision of 3G mobile radiotelephony communications services for the entire territory of the Russian Federation. The 3G license was granted subject to certain capital and other commitments. The three major conditions are that the Company will have to build a specified number of base stations that support 3G standards, will have to start commercial exploitation of the 3G technology in each region of the Russian Federation over the period from May 2008 through May 2010, and will also have to build a certain number of base stations by the end of the third, fourth and fifth years from the date of granting of the license. As of May 24, 2010, the Company is in full compliance with these license conditions, including constructing the required number of base stations required at this time.

**9. Commitments, Contingencies and Uncertainties (continued)**

*Taxation*

Russian tax, currency and customs legislation are subject to varying interpretations and changes, which can occur frequently. Management's interpretation of such legislation as applied to transactions and activities of the Company may be challenged by the relevant regional and federal authorities. Recent events within Russia suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may now be challenged. Therefore, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for the three calendar years preceding the current year. Under certain circumstances reviews may cover longer periods.

Based on tax examinations of other telecommunications companies operating in Russia, the tax authorities are currently focusing on a number of specific areas, which include, but are not limited to revenues from interconnection charges and marketing initiatives. As a result of such examinations, the tax authorities are claiming additional taxes which are currently being disputed in the courts by these other Russian telecommunications companies. Depending on the outcome of such examinations, the Company could also become the subject of an examination.

Management believes that the Company and its subsidiaries are in compliance with the tax laws affecting its operations; however, the risk remains that governmental authorities could take differing positions with regard to interpretative issues.

*Litigation*

The Company is not a party to any material litigation, although in the ordinary course of business, some of the Company's subsidiaries 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 they operate. In the opinion of management, the Company's and its subsidiaries' liability, if any, in all pending litigation, other legal proceedings or other matters, will not have a material effect on the financial condition, results of operations or liquidity of the Company.

*Apple Commitment*

In August 2008, the Company entered into a two-year fixed commitment with Apple Sales International ("Apple"), an Irish affiliate of Apple Computer Inc., to purchase a total of one million unlocked iPhone handsets over a two-year period for further resale in Russia. The Company fulfilled this requirement with respect to the fourth quarter of 2008, but due to the significantly reduced handset demand brought about by the economic crisis in Russia, the Company experienced difficulty re-selling these iPhones. As a result, the Company did not purchase any additional quarterly minimum quantities of iPhones as per the contract, however, it was agreed with Apple that a new model of iPhone handsets will be supplied under the existing contract.

## 9. Commitments, Contingencies and Uncertainties (continued)

The Company has had several discussions with Apple, and believes that Apple is interested in a continuing business relationship with the Company. There can be no assurance, however, that Apple will not bring a claim against the Company in respect of the contract. In light of the uncertainty as to whether a claim will be made and, if made, as to the amount which Apple may be able to claim, the Company is not able to estimate the amount of loss, if any, that the Company may sustain.

*Prepaid distribution contract*

In March 2009, the Company entered into an eighteen-month distribution contract with Euroset, one of the largest Russian mobile retailers, to connect approximately 7.2 million subscribers. The total cash consideration for this deal was approximately $146 million, of which approximately $97 million (3,292 as of April 9, 2009, the date of the payment) has been prepaid and a promissory note has been issued for the remaining amount. Management believes that as of May 24, 2010, Euroset is in full compliance with these contract conditions.

*Regulatory contingencies*

In March 2010 the Federal Anti-Monopoly Service ("FAS") has launched formal investigation on the roaming charges levied by the Company and the other two major mobile operators, MTS and VimpelCom, under Part 1 of Article 10 and Article 11 of Federal Law No 135-FZ "On Protection of Competition" ("Federal Law on Protection of Competition"). FAS asserted that the charges were "unreasonably overpriced", on the basis that an analysis carried out by the Interstate Council for Anti-Monopoly Policy showed that the roaming charges levied by the three operators were 2 to 2.5 times higher than comparable tariffs charged by other international operators and also 3 to 6 times higher than the European Commission would permit in the European Union. If the roaming charges and practices are found to be anti-competitive, the Company could face certain fines (under Article 14.31 and Article 14.32 of the Russian Federation Administrative Code, the maximum amount of such fine is 15% of overall roaming revenues). The Company does not believe that it is in violation of the Federal Law on Protection of Competition and believes it will sustain its position against this claim.