

**Open Joint Stock Company
“CenterTelecom”**

Consolidated Financial Statements
as of December 31, 2003

with Report of Independent Auditors

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Contents

Independent Auditors' Report	1
Consolidated Financial Statements	
Consolidated Balance Sheet	3
Consolidated Statements of Operations	4
Consolidated Statements of Cash Flows	5
Consolidated Statements of Changes in Shareholders' Equity	6
Notes to the Consolidated Financial Statements	7

INDEPENDENT AUDITORS' REPORT

To the Shareholders and Board of Directors of OAO "CenterTelecom":

1. We have audited the accompanying consolidated balance sheet of OAO "CenterTelecom" (a Russian open joint-stock company - hereinafter "the Company"), as of December 31, 2003, and the related consolidated statements of operations, cash flows and shareholders' equity for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.
2. Except as discussed in paragraphs 3 and 4, we conducted our audit in accordance with International Standards on Auditing issued by the International Federation of Accountants. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
3. As described in Note 2 "Summary of Significant Accounting Policies" and Note 27 "Pension Plans and Employee Benefits", the Company has not determined and presented its obligations existing under defined benefits plans in accordance with International Accounting Standard ("IAS") 19, "Employee Benefits". We were not able to quantify the adjustments, if any, to the financial statements. This matter also caused us to qualify our audit opinion on the financial statements for the year ended December 31, 2002.
4. As described in Note 2 "Summary of Significant Accounting Policies" and Note 11 "Property, Plant and Equipment", the Company's accounting records relating to fixed assets are not designed to support their presentation in accordance with IAS 16, "Property, Plant and Equipment", IAS 29, "Financial Reporting in Hyperinflationary Economies" and IAS 36, "Impairment of Assets". As such, certain estimates were made by management to present fixed assets in the accompanying financial statements. Owing to the nature of the Company's records, we were unable to satisfy ourselves as to the adjustments, if any, which might have been determined to be necessary had additional evidence been available to better analyze the assumptions and estimates made by management. This matter also caused us to qualify our audit opinion on the financial statements for the year ended December 31, 2002.

5. We were unable to obtain sufficient audit evidence for revenue transactions in the Luberetsky branch of the Company for the period up to September 30, 2002. This matter caused us to qualify our audit opinion on the financial statements for the year ended December 31, 2002.
6. As a result of the matters described in paragraphs 3 and 4, adjustments, if any, could materially affect the following items: (i) property, plant and equipment, equipment contributions, assets and liabilities existing under benefit plans, deferred income taxes and retained earnings as of December 31, 2003 and the corresponding amounts of depreciation and amortization expense, wages, salaries, other benefits and payroll taxes, income tax expense and net income for the year ended December 31, 2003, (ii) related disclosures, and (iii) the corresponding amounts for 2002.
7. In our opinion, except for the effects on the financial statements of such adjustments, if any, from the matters referred to in paragraphs 3 and 4, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of OAO "CenterTelecom" as of December 31, 2003, and the results of its operations and its cash flows for the year then ended in conformity with International Financial Reporting Standards.
8. Without qualifying our opinion, we draw attention to Note 1 "General Information" referring to an excess of 3,124,673 thousand Rubles of the Company's current liabilities over current assets as at December 31, 2003, and disclosing management's plans in respect to the Company's current liquidity and working capital deficit.
9. As described in Note 1 "General Information", the Company was the subject of a reorganization that was approved by the shareholders on February 22, 2002. The Company accounted for the merger based on the principles of uniting of interests as described in IAS 22 "Business Combinations". In applying this method, the Company reflected amounts in the financial statements as if the entities had been combined from January 1, 2002, the earliest period presented.

Ernst & Young Vnesheaudit ZAO

August 20, 2004

OAO CenterTelecom
Consolidated Balance Sheet

As of December 31, 2003

(in thousand rubles)

	<i>Note</i>	December 31, 2003	December 31, 2002 <i>(as restated, see Note 2)</i>
ASSETS			
Non-current Assets:			
Property, Plant and Equipment	11	23,662,784	20,606,263
Intangible Assets and Goodwill	12	1,033,289	95,477
Investments in Associates	14	30,721	36,107
Long-term Investments	15	8,559	36,104
Other Financial Assets	19	36,780	28,308
Advances to Suppliers of Equipment	16	659,308	248,152
Total Non-current Assets		25,431,441	21,050,411
Current Assets:			
Inventories, net	17	634,647	551,268
Trade Accounts Receivable, net	18	1,486,327	1,291,628
Other Current Assets	20	1,855,701	1,317,635
Cash and Cash Equivalents	21	1,052,589	307,290
Total Current Assets		5,029,264	3,467,821
TOTAL ASSETS		30,460,705	24,518,232
SHAREHOLDERS' EQUITY AND LIABILITIES			
Shareholders' Equity:			
Preferred Shares	22	157,798	157,798
Ordinary Shares	22	473,402	473,402
Inflation Impact on Share Capital		588,166	588,166
Change in the Fair Value of Financial Assets Available-for-Sale		2,624	-
Retained Earnings and Other Reserves		11,883,403	12,027,170
Total Shareholders' Equity		13,105,393	13,246,536
Commitments and Contingences	28	-	-
Minority Interest		23,473	17,569
Non-current Liabilities:			
Loans and Borrowings	23	6,969,276	1,948,117
Finance Lease Obligations	24	1,167,947	390,060
Equipment Contributions		628,486	582,327
Deferred Income Tax Liability	8	372,860	938,173
Other Non-current Liabilities		39,333	17,368
Total Non-current Liabilities		9,177,902	3,876,045
Current Liabilities:			
Trade Accounts Payable and Accrued Liabilities	25	1,617,085	1,848,517
Payables to Rostelecom		381,490	355,471
Taxes and Payroll Related Obligations	26	1,059,998	827,685
Dividends Payable	10	57,149	31,075
Loans and Borrowings	23	3,419,649	2,955,552
Current Portion of Long-Term Loans and Borrowings	23	1,105,797	960,652
Current Portion of Long-Term Finance Lease Obligations	24	512,769	399,130
Total Current Liabilities		8,153,937	7,378,082
Total Shareholders' Equity and Liabilities		30,460,705	24,518,232

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

OAo CenterTelecom

Consolidated Statements of Operations

For the year ended December 31, 2003

(in thousand rubles)

	<i>Note</i>	2003	2002 <i>(as restated, see Note 2)</i>
Revenues	4	21,189,199	17,353,640
Operating Expenses			
Wages, Salaries, Other Benefits and Payroll Taxes		(7,464,178)	(6,174,794)
Depreciation and Amortization		(3,592,387)	(3,478,065)
Materials, Repairs and Maintenance, Utilities		(2,010,300)	(1,820,322)
Taxes Other than Income Tax		(444,631)	(540,413)
Interconnection Charges		(2,752,150)	(1,855,722)
Bad Debts Expense		(801,968)	(376,364)
Loss on Disposal of Property, Plant and Equipment		(80,505)	(196,175)
Other Operating Expenses	5	(2,008,126)	(1,753,896)
Total Operating Expenses		(19,154,245)	(16,195,751)
Operating Income		2,034,954	1,157,889
Loss from Associates		(750)	(6,580)
Interest Expenses, net	6	(1,298,255)	(801,548)
Income (Loss) from Long-Term Investments		(25,097)	65,086
Other Expenses, net	7	(342,298)	(208,545)
Foreign Exchange Loss, net		(88,310)	(561,548)
Net Monetary Gain		–	401,432
Income Before Taxation and Minority Interest		280,244	46,186
Income Tax Expense	8	(116,282)	42,566
Income Before Minority Interest		163,962	88,752
Minority Interest		(5,903)	(8,093)
Net Income		158,059	80,659
Dividends on Preferred Shares	10	(150,256)	(108,430)
Net Income (Loss) Attributable to Ordinary Shareholders		7,803	(27,771)
Basic and Diluted Earnings (Loss) per Share (Russian Rubles)	9	0.005	(0.018)

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

OAo CenterTelecom

Consolidated Statements of Cash Flows

For the year ended December 31, 2003

(in thousand rubles)

	2003	2002 <i>(as restated, see Note 2)</i>
Cash flows from operating activities:		
Income before taxation and minority interest	280,244	46,186
Adjustments to reconcile income to cash generated from operations:		
Foreign currency exchange loss, net	88,310	561,548
Net monetary gain	-	(401,432)
Depreciation and amortization	3,592,387	3,478,065
Loss on disposal of property, plant and equipment	80,505	196,175
(Income) loss from investments in associates	750	6,580
(Income) loss from long-term investments	25,097	(65,086)
Interest expense, net	1,298,255	801,548
Bad debt expense	801,968	376,364
Operating profit before changes in working capital	6,167,516	4,999,948
Decrease (increase) in trade accounts receivable	(1,083,669)	(729,807)
Decrease (increase) in other current assets	(396,592)	(358,967)
Decrease (increase) in inventories	(83,380)	(76,181)
Increase (decrease) in accounts payable and accrued liabilities	(118,412)	(364,431)
Increase (decrease) in taxes and payroll related obligations	218,340	211,185
Cash flows generated from operations	4,703,803	3,681,747
Interest paid	(1,189,510)	(529,130)
Income tax paid	(809,924)	(521,209)
Net cash flows provided by operating activities	2,704,369	2,631,408
Cash flows from investing activities:		
Purchase of property, plant and equipment	(5,333,300)	(3,660,704)
Purchase of intangible assets	(50,597)	(27,376)
Purchase of Oracle software	(919,517)	-
Proceeds from sales of property, plant and equipment	4,484	548,322
Disposal (purchase) of subsidiaries	-	(72,100)
Disposal (purchase) of investments and other financial assets	(2,404)	17,115
Interest received	4,864	6,300
Dividends received	4,469	2,812
Net cash flows used in investing activities	(6,292,001)	(3,185,631)
Cash flows from financing activities:		
Proceeds from borrowings	9,440,760	1,852,284
Repayment of borrowings	(5,092,283)	(771,621)
Proceeds from bonds issued	2,000,000	600,000
Repayment of bonds	(600,000)	-
Repayment of finance lease obligations	(277,850)	(241,964)
Repayment of vendor financing obligations	(882,566)	(704,528)
Proceeds from (repayment of) other non-current liabilities	21,965	(7,296)
Dividends paid	(275,753)	(225,156)
Net cash flows used in financing activities	4,334,273	501,719
Monetary effects on cash and cash equivalents	-	(126,427)
Effects of exchange rate changes on cash and cash equivalents	(1,342)	12
Decrease in cash and cash equivalents	745,299	(178,919)
Cash and cash equivalents at the beginning of the year	307,290	486,209
Cash and cash equivalents at the end of the year	1,052,589	307,290
Non-monetary operations:		
Property, plant and equipment acquired through vendor financing	442,414	566,478
Property, plant and equipment acquired under lease agreements	1,169,376	938,389
Equipment contributions	85,104	61,107

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

OAo CenterTelecom

Consolidated Statements of Changes in Shareholders' Equity

For the year ended December 31, 2003

(in thousand rubles)

		Share Capital		Inflation	Retained	
	Notes	Preferred shares	Ordinary shares	impact on share capital	earnings and other reserves	Total equity
At December 31, 2001						
(as restated, see Note 2)	2	157,798	473,402	588,166	12,172,358	13,391,724
Net income for the year		–	–	–	80,659	80,659
Dividends		–	–	–	(225,847)	(225,847)
(as restated, see Note 2)						
At December 31, 2002						
(as restated, see Note 2)		157,798	473,402	588,166	12,027,170	13,246,536
Net income for the year		–	–	–	158,059	158,059
Dividends	10	–	–	–	(301,826)	(301,826)
Change in the fair value of financial assets available-for-sale		–	–	–	2,624	2,624
At December 31, 2003		157,798	473,402	588,166	11,886,027	13,105,393

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

ОАО CenterTelecom

Notes to Consolidated Financial Statements

as of December 31, 2003

(in thousand rubles, unless otherwise stated)

1. General Information

Authorization of Accounts

The consolidated financial statements of ОАО “CenterTelecom” and its subsidiaries, as disclosed in Note 13 “Investments in Subsidiaries”, (the “Company”) for the year ended December 31, 2003 were authorized for issue by its appointed General Director and Chief Accountant of the Company on August 30, 2004.

The Company

The Company is an open joint stock company incorporated in accordance with the laws of the Russian Federation.

Open joint-stock company ОАО “Svyazinvest”, a federal holding company majority-owned by the Russian Federation, owns 51% of the Company’s ordinary shares as of December 31, 2003.

The Company’s principal activities are providing telephone services (including local, long-distance and international calls), telegraph, data transfer services, rent of channels and wireless communication services on the territory of Central and Central-Chernozemny regions of the Russian Federation.

The average number of employees in the Company in 2003 was approximately 69,847 persons (2002 – 72,088).

The registered office of the Company is Russia, Moscow region, city of Khimki, Proletarskaya st. 23.

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

1. General Information (continued)

2002 Reorganization

In 2002 the Company's management started the Company's reorganization by obtaining shareholder approval to merge the following regional enterprises of OAO "Svyazinvest" wherein 1,578,006,833 ordinary and 525,992,822 preferred shares of the Company were exchanged for 100% of the outstanding voting shares of the regional enterprises as follows:

Regional Enterprise	Ordinary shares issued by the Company	Preferred shares issued by the Company	Exchange Ratio
OAO "CenterTelecom"	463,773,939	154,658,000	1.00
OAO "Belgorod Electrosvyaz"	76,881,850	25,638,296	19.27
OAO "Bryansksvyazinform"	50,427,950	16,809,937	4.40
OAO "Ivtelecom"	47,121,268	15,713,797	0.45
OAO "Kaluga Region Elektrosvyaz"	68,284,675	22,771,451	22.27
OAO "Kostroma Region Elektrosvyaz"	24,800,276	8,270,063	20.92
OAO "Kursk Region Elektrosvyaz"	45,798,670	15,272,606	6.81
OAO "Lipetskelektrosvyaz"	62,001,975	20,676,240	1.91
OAO "Orel Region Elektrosvyaz"	43,814,499	14,611,007	5.53
OAO "Ryazan Region Elektrosvyaz"	48,774,338	16,265,265	4.55
OAO "Smolensksvyazinform"	60,348,771	20,124,846	5.27
OAO "Tambov Elektrosvyaz"	61,174,948	20,400,253	10.80
OAO "Tulatelecom"	104,016,491	34,460,412	0.38
OAO "Tver Region Elektrosvyaz"	78,535,694	26,189,469	496.41
OAO "Valdimir Region Elektrosvyaz"	75,228,952	25,086,826	0.43
OAO "Voronezhsvyazinform"	157,072,065	52,379,022	47.41
OAO "Yartelecom"	109,950,472	36,665,332	13.57
Total	<u>1,578,006,833</u>	<u>525,992,822</u>	

The merger was completed and effective on November 30, 2002. Transaction costs related to the merger of 165,622 were expensed in 2002.

While International Financial Reporting Standards do not specify accounting principles to be applied to transactions among entities under common control, the Company has accounted for the merger based on the principles of uniting of interests as described in IAS 22, "Business Combinations". In applying this method, the Company has reflected amounts in the financial statements at their historical carrying amounts as if the entities had been combined from January 1, 2002 the beginning of the earliest period presented. Unless otherwise described, all information presented in these financial statements gives retroactive effective to the reorganization.

Liquidity and Financial Resources

As of December 31, 2003, the Company's current liabilities exceeded its current assets by 3,124,673 (2002 – 3,910,261). As a result, significant uncertainties exist as to the Company's liquidity and future capital resources.

Notes to Consolidated Financial Statements (continued)

1. General Information (continued)

Liquidity and Financial Resources (continued)

To date, the Company has significantly relied upon short-term and long-term financing to fund the improvement of its telecommunication network. This financing has historically been provided through bank loans and vendor financing. If needed, management believes that certain projects may be deferred or curtailed in order to fund the Company's current operating needs.

Through 2004, the Company anticipates funding from a) existing cash reserves, b) cash generated from operations, c) placement of ruble bonds in the Russian market, and d) other financing from domestic and international lending institutions. Management also expects to continue to be able to delay payment for certain operating costs to manage its working capital requirements if necessary.

The accompanying financial statements have been presented on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. Accordingly, the financial statements do not include any adjustments related to the recoverability and classification of recorded asset amounts or any other adjustments that might result should the Company either be unable to continue as a going concern or if the Company was to dispose of assets outside the normal course of its operating plan or had problems with regards to timely settlement of its short-term liabilities and short-term portion of long-term liabilities when they became due.

2. Summary of Significant Accounting Policies

Basis of Preparation

The Company maintains its accounting records and prepares its statutory accounting reports in Russian Rubles and in accordance with the Regulations on Accounting and Reporting in the Russian Federation. The accompanying consolidated financial statements presented in accordance with International Financial Reporting Standards (IFRS) are based upon the statutory accounting records that are maintained in accordance with the Russian accounting regulations under the historical cost convention. These statutory accounting records have been adjusted and reclassified to present the accompanying consolidated financial statements in accordance with IFRS. IFRS primarily includes standards and interpretations approved by the International Accounting Standards Board (IASB), International Accounting Standards Committee (IASC) and Standing Interpretations Committee (SIC).

Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Prior Period Adjustments and Reclassifications

Management of the Company chose to restate opening retained earnings and the results for the year ended December 31, 2002 for previously unrecorded adjustments. These adjustments relate to accrual of interconnection costs (these amounts had previously been reflected in the period invoiced), accrual of dividends due to the holders of preferred shares (the dividends had been previously reflected in the reporting period when formally declared) as well as deferred tax effects of temporary differences not previously recognized on fixed assets. The effect of these adjustments on previously reported amounts is as follows:

	As previously reported	Prior period adjustment	As restated
Shareholders' equity, January 1, 2002	14,127,013	(735,289)	13,391,724
Net income	80,659	–	80,659
Dividends	(234,370)	8,523	(225,847)
Shareholders' equity, December 31, 2002	13,973,302	(726,766)	13,246,536
Basic and diluted loss per share (rubles)	(0.023)	0.005	(0.018)

Certain amounts in the prior period consolidated financial statements have been reclassified to conform with the current year presentation.

Basis of Preparation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries drawn up to December 31, 2003 and 2002.

The Company has accounted for the reorganization (see Note 1 "General Information") based on the principles of uniting of interests as described in IAS 22, "Business Combinations".

Subsidiaries are consolidated from the date on which control is transferred to the Company and cease to be consolidated from the date on which control is transferred from the Company. Minority interests reflect the interests in subsidiaries not held by the Company (see Note 13, "Investments in Subsidiaries").

Subsidiaries

A subsidiary is an entity that is controlled by the Company, directly or indirectly, generally through ownership, of more than 50% of the voting share capital of the entity. These consolidated financial statements include the assets and liabilities, and revenues and expenses of the Company and of subsidiary undertakings, on a line-by-line basis.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Subsidiaries (continued)

Where subsidiaries are not controlled throughout the year, consolidated results include the results of those entities for that part of the year during which control existed, except where the Company has applied the uniting of interests method in accordance with IAS 22 “Business Combination”. Under the uniting of interests method, the financial statement items of the combining entities for the period in which the combination occurs are included in the consolidated financial statements as if they had been combined from the beginning of the first period presented.

Where the purchase method is applied to account for the acquisition of subsidiaries, identifiable assets and liabilities of subsidiaries are stated at their fair value as of the acquisition date. Minority interest at the date of acquisition is determined in proportion to minority shareholders' share in the fair value of the assets and liabilities of the subsidiary at this date. The share of minority shareholders is estimated on the basis of the common voting shares and preferred shares owned by shareholders that do not exercise control over the subsidiary.

Balances and transactions between the Company and subsidiary undertakings, as well as any income from intercompany transactions are eliminated. Income (loss) from intercompany transactions is identified and eliminated only in cases where the assets transferred under relevant transactions have not been sold to third parties (i.e. non-Company entities) and are carried in the balance sheet of a Company entity as of the balance sheet date.

Associates

An associate is an entity in which the Company has significant influence, which is usually demonstrated by the Company owning between 20% and 50% of the voting share capital.

Under the equity method, the investments in associates are carried in the balance sheet at cost plus post-acquisition changes in the Company's share of net assets of the associates, less any impairment in value. The income statement reflects the Company's share of the results of operations of the associates.

Unrealized gains and losses arising from transactions with associates are eliminated in proportion to the Company's interest in the associates by adjusting the book value of investments.

Joint control, accounting for joint activities and joint ventures

The Company uses the equity method when it has significant influence in the joint venture in accordance with IAS 31 “Financial Reporting of Interests in Joint Ventures” and IAS 28 “Accounting for Investments in Associates”. The equity method is a method of accounting and reporting whereby an interest in a jointly controlled entity is initially recorded at cost and adjusted thereafter for the post acquisition change in the venture's share of net assets of the jointly controlled entity. The income statement reflects the venture's share of the results of operations of the jointly controlled entity.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Goodwill

For investments in subsidiaries and associates, any excess of the cost of acquisition over the Company's share in the fair value of net identifiable assets and liabilities of the acquired entity is recognized as goodwill. Goodwill is amortized on a straight-line basis over its useful life, which according to management's expectations is approximately 5 years. It is reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Goodwill is stated at cost less accumulated amortization and any impairment in value.

Goodwill on acquisition of associates is included in the carrying amount of investments in associates.

Upon disposal of investments in a subsidiary or an associate the remaining balance of unamortized goodwill is taken to gains or losses from such disposal.

Accounting for the Effects of Inflation

In 2000 – 2002 the Russian Federation met the definition of a hyperinflationary economy, as defined by International Accounting Standard 29 “Financial Reporting in Hyperinflationary Economies” (IAS 29). The inflation rate based on the Russian consumer price index (“CPI”), as calculated by the State Committee on Statistics (Goskomstat), was 15.1% for 2002 (18.6% and 20.2% for 2001 and 2000, respectively). Although the cumulative inflation index for the three-year period ended in 2002 was less than 100%, it was considered that the remaining criteria set forth by IAS 29 indicated that the Russian Federation continued to experience conditions that meet the definition of a hyperinflationary economy during 2002.

IAS 29 requires that financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. In applying IAS 29, the Company used conversion factors derived from the Russian CPI.

The indices used to adjust amounts in these consolidated financial statements with respect to 2002 prices (2002 = 1.0) for the years ended December 31, and the respective conversion factors, are:

Year	Index	Conversion factor
1992	7,541	362.4
1993	67,846	40.3
1994	211,612	12.9
1995	487,575	5.6
1996	594,110	4.6
1997	659,403	4.1
1998	1,216,401	2.2
1999	1,663,091	1.6
2000	1,997,843	1.4
2001	2,374,037	1.2
2002	2,733,087	1.0

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Accounting for the Effects of Inflation (continued)

The main guidelines followed in adjusting the consolidated financial statements as of December 31, 2002 to current purchasing power at December 31, 2002 are:

- § all amounts are stated in terms of the measuring unit current at December 31, 2002;
- § monetary assets and liabilities are not restated as they are already expressed in terms of the monetary unit current at December 31, 2002;
- § non-monetary assets and liabilities which are not carried at amounts current at December 31, 2002 and shareholders' equity are restated by applying the relevant conversion factors;
- § indexation adjustments to property, plant and equipment applicable to prior periods are credited to "Retained earnings and other reserves" in the accompanying balance sheet;
- § all items in the consolidated statements of income and of cash flows are adjusted by applying appropriate conversion factors with the exception of depreciation, amortization and losses from disposal of fixed assets and other assets;
- § the effect of inflation on the Company's net monetary position is included in the consolidated statement of operations as a monetary gain.

Effective from January 1, 2003, international accounting and financial reporting bodies have determined that the Russian Federation no longer meets the criteria of IAS 29 for hyperinflation. Beginning 2003, the Company ceased applying IAS 29 and only recognizes the cumulative impact of inflation indexing through December 31, 2002, on non-monetary elements of the financial statements. Transactions undertaken subsequent to December 31, 2002 are reported at actual, nominal amounts except for those involving non-monetary assets and liabilities acquired prior to January 1, 2003. Results of operations (including gains and losses on disposal) involving such assets and liabilities are recognized based on the "restated cost", which was calculated by applying through December 31, 2002 the relevant conversion factors to the carrying values of these assets and liabilities.

Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currency are translated into rubles at official Central Bank of the Russian Federation (CBR) exchange rates at the year-end. Transactions denominated in foreign currencies are reported at the CBR rates of exchange at the date of the transaction. Any gains or losses on assets and liabilities denominated in foreign currencies arising from a change in official exchange rates after the date of transaction are recognized as currency translation gains or losses.

Transactions that are conducted in rubles when the related assets and liabilities are denominated in foreign currencies (or conventional units) are recorded in the Company's consolidated financial statements on the same principles as transactions denominated in foreign currencies.

Property, Plant and Equipment

Property, Plant and Equipment is stated at cost less depreciation and any impairment in value.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Property, Plant and Equipment (continued)

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of each group of assets as follows:

Buildings	50 years
Constructions	20 years
Switches and transmission devices	15 years
Other telecommunications equipment	15 years
Vehicles	5 years
Computers	4 years
Other	5 years

For the purpose of disclosure, Property, Plant and Equipment are aggregated into the following groups:

- § Buildings and constructions;
- § Switches and transmission devices;
- § Machines and other, in which computers, vehicles and other items are included.

Construction in progress is recorded as the total of actual expenses incurred by the Company from the beginning of construction to the reporting date, adjusted for the effect of inflation (for the periods prior to January 1, 2003) from the date when such expenses occur to the reporting date in accordance with IAS 29. Accrual of depreciation begins when fixed assets are put into operation.

Borrowing costs that are attributable to the acquisition or construction of fixed assets are capitalized as part of the cost of the related asset when it is probable that they will result in future economic benefits to the Company and the costs can be measured reliably. Capitalization of borrowing costs commences with the beginning of activities to prepare the asset for intended use and lasts until the assets are ready for their intended use.

The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in the statement of operations.

The cost of maintenance, repairs, and replacement of minor items of property is charged to maintenance expense. Renewals and betterments are capitalized. Upon the sale or retirement of property, plant and equipment, the cost and related accumulated depreciation are eliminated from the accounts. Any resulting gains or losses are included in the determination of net income.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Equipment Contributions

Equipment transferred to the Company free of charge by its customers and other entities outside the privatization process is capitalized at market value at the date of transfer, and a corresponding deferred income is recognized as a liability in the balance sheet and credited to the statement of operations on the same basis as the equipment is depreciated. Equipment contributions that do not generate any future income for the Company are not recognized.

Grants received from municipal authorities for the purchase of property, plant and equipment are reflected in the balance sheet as deferred income and recognized as income during the useful life of a respective asset in accordance with IAS 20 "Accounting for Government Grants and Disclosure of Government Aid Information".

When the grants relate to an income item, it is recognized as income over the periods necessary to match the grant on a systematic basis to the cost that it is intended to compensate.

Intangible Assets

Intangible assets acquired separately from the business are capitalized at cost. Intangible assets acquired as part of an acquisition of a business are capitalized separately from goodwill if the fair value can be measured reliably, subject to the constraint that, unless the asset has a readily ascertainable market value, the fair value is limited to an amount that does not create or increase any negative goodwill arising on the acquisition. Intangible assets created within the business are not capitalized and expenditure is charged against profits in the year in which it is incurred.

The carrying values of intangible assets are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Research and Development Costs

Research and development costs are expensed as incurred.

Financial Instruments

Financial investments include the following three categories: held-to-maturity investments, investments available-for-sale and investments held for trading.

All investments are initially recognized at cost, being the fair value of the consideration given and including acquisition charges associated with the investment.

After initial recognition, investments that are classified as trading are measured at their fair value. Gains or losses on trading securities are recognized in the income statement and included into income (loss) from financial investments.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Financial Instruments (continued)

Investments that are intended to be held to maturity, that have fixed maturity, being initially recorded at cost are subsequently measured at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any discount or premium on acquisition, over the period to maturity. For investments carried at amortized cost, gains and losses are recognized in income when the investments are derecognized or impaired, as well as through the amortization process. Those that do not have a fixed maturity are measured at cost.

After initial recognition, investments that are classified as available-for-sale are measured at their fair value. Gains or losses on available-for-sale investments are recognized as a separate component of equity until the investment is sold, collected or otherwise disposed of, or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in income.

Other Financial Assets

Other Financial Assets consist of Long-term Accounts Receivable, Long-term Loans Granted to personnel and other financial assets. If they are being held to maturity, they are accounted at amortized cost using the effective interest rate.

Inventories

Inventories, which are mainly comprised of cable, materials, spare parts for telecommunications equipment and goods for resale, are priced at the lower of cost or net realizable value. Cost is determined using the average cost method.

Transportation, insurance and other similar expenditures incurred to bring inventories to their existing condition and location are included into the cost of raw materials and goods for resale.

Accounts Receivable

Accounts receivable are stated at face value, less an allowance for doubtful accounts. An estimate of doubtful debts is made when collection of the full amount is no longer probable.

Cash and Cash Equivalents

Cash and cash equivalents represent cash on hand and in the Company's bank accounts, as well as cash deposits and short-term investments with original maturities of three months or less.

Interest-Bearing Loans and Borrowings

All interest-bearing loans and borrowings are initially recognized at cost of consideration received. After initial recognition, interest-bearing loans and borrowings are subsequently measured at cost plus accrued interest calculated using the effective interest rate method.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Non Interest-Bearing Loans and Borrowings

The initial recognition of non interest-bearing loans and borrowings and equipment received per non-interest-bearing loans and borrowings are made at their fair market value estimated by discounting future payments to their present value. Market interest rates are approximated by using the prevailing rates of return for the Company's financial instruments having substantially the same terms and characteristics. The subsequent measurement of interest-bearing loans and borrowings are carried at amortized cost using the effective interest rate method.

Provisions.

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, settlement of the obligation may require an outflow of resources embodying economic benefits, and the obligation amount can be reliably assessed. Where the Company expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an interest expense.

Pensions and Other Post-Employment Benefits

State Plans

Social contributions are made through a unified social tax ("UST") calculated by the Company by the application of a regressive rate (from 35.6% to approximately 18 %) to the annual gross remuneration of each employee. The Company allocates the UST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund vary from 28% to 14% depending on the annual gross salary of each employee.

The Company's contributions relating to the UST are expensed in the year to which they relate.

Other pension and post-retirement benefits

Under collective bargaining agreements, the Company also provides post-employment retirement benefits by using defined contribution plans and defined benefit plans. The majority of the Company's employees are eligible to participate under such defined benefit plans based upon a number of factors, including years of service, age and compensation.

A defined contribution plan is a post-employment benefit plan under which the Company's liability is limited solely to the amount of a contribution it agrees to pay into a fund. In this case all actuarial and investment risks will be borne by employees. The Company recognizes contributions under a defined contribution plan in the period to which they are attributable.

Under defined benefit plans, the Company's obligation is to provide the agreed benefits to current and former employees whereby actuarial and investment risks fall, in essence, on the Company.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Pensions and Other Post-Employment Benefits (continued)

Other pension and post-retirement benefits (continued)

The Company does not apply IAS 19 "Employee benefits" to account for defined benefit plans. The Company does not estimate current obligations under additional pension provision agreements thus the amount are not disclosed in the financial statements as of December 31, 2003.

Leases

Finance leases of equipment that transfer substantially all the risks and rewards incidental to ownership of the leased item to the Company are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to interest expense.

Capitalized leased assets are depreciated using the straight-line method over the estimated economic useful life of the asset as for own assets within the same class, with consideration of the contractual terms the assets can be used.

Leases where the lessor retains substantially all the risks and rewards of ownership of the asset are classified as operating leases. Operating lease payments are recognized as an expense in the statement of operations on a straight-line basis over the lease term.

Revenue

Revenue is recognized to the extent that it is probable that economic benefits will flow to the Company and the revenue can be reliably measured.

The Company categorizes the revenue sources in thirteen major categories:

- § Long distance telephone services - domestic;
- § Long distance telephone services - international;
- § Local telephone services;
- § Installation and connecting fees;
- § Documentary services;
- § Mobile telecommunication services;
- § Radio and TV broadcasting;
- § Data transfer and telematic services;
- § New services;
- § Rent of telephone channels;
- § Revenue from national telephone operators;
- § Other telecommunications services;
- § Other revenues.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Revenue (continued)

Long distance services (domestic and international)

Revenues from long distance services depend on time of call, duration of call, destination of call, type of service used, subscriber category and the applied rate plan. The Company charges long distance fees on a per-minute basis. The Company recognizes revenues related to the long distance services in the period when the services are rendered.

Local telephone services

Revenue from the local telephone services depends on the duration of the telephone connections and subscription fee, while time driven billing scheme is applied. If fixed payment scheme is applied then revenue depends on the subscription fee only. The Company recognizes revenues related to the monthly network fees for local services in the month the service is provided to the subscriber.

Installation and connecting fees

The Company recognizes installation and connecting fees for indefinite contracts with its subscribers as revenues when the installation and connection are complete.

Documentary services

Revenues from telegraph services comprise fees for telegram transmissions and other wire line data transmission services. The Company recognizes revenues related to telegraph services in the period when the services are rendered.

Mobile telecommunication services

Major revenues from cellular services arise from airtime services including local, intercity long distance and international long distance calls, subscription fees, value added services, outbound and inbound roaming. The Company recognizes revenues related to mobile telecommunications services in the period when the services are rendered.

Radio and TV broadcasting

The Company maintains a wireline radio broadcasting network. The revenues comprise monthly fees from subscribers and installation fees for wireline radio sets. The Company recognizes the revenues related to radio broadcasting in the period when the services are rendered.

Data transfer and telematic services

The Company recognizes revenues related to data transfer and telematic services in the period when the services are rendered.

New services

Major revenues from new services include internet services, ISDN, IP-telephony, intelligent network services. The Company recognizes revenues related to new services in the period when the services are rendered.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Revenue (continued)

Rent of telephone channels

Major revenues are recognized from the following services: rent of intercity and international, digital, analogue and telegraph channels. The Company recognizes revenues from the rent of channels in the period when the services are rendered.

Revenue from national telephone operators

Revenue from national service providers includes two different groups.

The first group of revenues represents services rendered to OAO "Rostelecom" for termination of long-distance traffic of its operators-partners in the network of the Company.

In 2003, the Ministry of the Russian Federation for antimonopoly policy and entrepreneurial support (MAP) has conducted a reform of the settlements system of multi regional OAO "Svyazinvest" companies with OAO "Rostelecom" for transit of intercity long-distance traffic. Till August 1, 2003, the revenue calculation has been based on the integral settlement rate, multiplied on the total number of minute-distances (transfer of 1 minute of traffic on 50 kilometer intervals of OAO "Rostelecom" network), transferred through the period.

The integral settlement rate has been calculated as sum of linear settlement rate between zones and difference between inbound and outbound termination settlement rates of the regional companies. The rate has been calculated and agreed by the MAP once per year according to traffic statistics of the previous year, thus it has not reflected real economical benefits and costs related to changes of the incoming and outgoing structure of the traffic in the current settlement period.

In August 2003, a new and more transparent inter-operators settlement system for intercity traffic has been introduced. The new system separates (i) payments of regional operators for the transfer of intercity traffic in OAO Rostelecom's network and termination of the traffic in the zone, where outgoing intercity calls of its own subscriber reaches its destination, and (ii) payments for the termination of the incoming intercity traffic from other operators in the network of the Company.

Calculation of the costs for the transit of intercity traffic is based on the new settlement rate, that is equal to the sum of linear settlement rate multiplied on the quantity of 50 kilometer intervals between zones using termination settlement rate for the zone where the calls are terminated. Revenue calculation for the transit of intercity traffic from OAO "Rostelecom" to the customers of the regional companies is based on the termination settlement rates. New rates have been defined by the order of the MAP dated July 4, 2003.

The second group of revenues from national operators represents services rendered to interconnected telecom operators that transfer local, intercity and international traffic of their customers via the Company's network.

The Company recognizes revenues from national operators in the period when the services are rendered.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Revenue (continued)

Other telecommunication services

Other telecommunication services primarily consist of revenues received by public switched telephone network (PSTN) stations from the rent of direct lines and local junctions. The Company recognizes revenues related to other services in the period when the services are rendered.

Other services

Other revenues primarily consist of revenues received from manufacturing of the telecommunication equipment and its technical support, transportation services, recreation services and sale of products and services provided by auxiliary units.

Income Tax

Deferred income tax assets and liabilities are calculated in respect of temporary differences in accordance with IAS 12 "Income Taxes".

IAS 12 requires the use of a balance sheet liability method for financial reporting and accounting for deferred income taxes. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values. The Company's principal temporary differences arise in respect of property, plant and equipment. A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized.

Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realized or the liability settled based on tax rates that have been enacted or substantively enacted at the balance sheet date.

A deferred tax liability is recognized for all taxable temporary differences associated with investments in subsidiaries, associates, and interests in joint ventures, except to the extent that both of the following conditions are satisfied: the Company is able to control the timing of the reversal of the temporary difference; and it is probable that the temporary difference will not reverse in the foreseeable future.

Value-Added Tax

Value-added taxes related to sales are payable to the tax authorities on an accrual basis based upon invoices issued to the subscriber. VAT incurred for purchases and paid to suppliers may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT that is not currently reclaimable as of the balance sheet date is recognized in the balance sheet on a gross basis.

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Contingencies

Contingent liabilities are not recognized in the financial statements. They are disclosed in the financial statements unless the possibility of an outflow of resources embodying economic benefit is remote.

Contingent assets are not recognized in the financial statement but disclosed in the financial statements when an inflow of economic benefits is probable.

Subsequent Events

Post-year-end events that provide additional information about the Company's position at the balance sheet date (adjusting events), are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed when material.

3. Segment Information

The Company operates in one industry, i.e. provision of wireline telecommunication services, on the territory of Central and Central-Chernozemny regions of Russia. The Company's structure is based on territorial units, which service the corresponding parts of the Company's network. The Company's management considers that the Company operates in one geographical area and business segment, and evaluates performance and makes investment and strategic decisions based upon a review of profitability for the Company as a whole.

4. Revenues

By revenue types	2003	2002
Long distance telephone services – national	7,121,817	6,269,062
Local telephone services	6,318,677	4,927,284
Installation and connecting fees	1,749,789	1,467,825
Long distance telephone services – international	1,504,012	1,383,918
Revenues from national telephone operators	1,262,533	247,167
New services	576,686	379,115
Mobile telecommunications services	394,372	367,381
Data transfer and telematic services	202,153	129,358
Documentary services	174,848	149,323
Rent of telephone channels	150,919	129,539
Radio and TV broadcasting	29,997	20,997
Other telecommunications services	1,237,767	1,475,576
Other revenue	465,629	407,095
Total	21,189,199	17,353,640

Change to the new scheme of settlements with OAO "Rostelecom" in August 2003 allowed the Company to receive revenue for the termination of the traffic in its network depending on the actual amount of traffic in the period that lead to an increase of revenue by 478,680. The costs for the settlements with OAO "Rostelecom" for transfer of intercity traffic due to the change of the scheme increased by 544,100.

Notes to Consolidated Financial Statements (continued)

4. Revenues (continued)

The Company identifies revenue by the following major customer groups:

Customer groups	2003	2002
Residential customers	11,491,653	9,497,508
Corporate customers	7,015,429	5,633,572
Government customers	1,451,824	1,324,412
Tariff compensation from the state budget	1,230,293	898,148
Total	21,189,199	17,353,640

5. Other Operating Expenses

	2003	2002
General and administrative expenses	(673,398)	(481,746)
Rent of premises	(257,344)	(241,028)
Insurance expenses	(231,278)	(57,254)
Bank charges	(176,843)	(88,592)
Audit and consulting expenses	(147,219)	(114,404)
Cost of goods sold	(78,431)	(155,490)
Contributions to Non-Commercial Partnership	(72,144)	(69,316)
Advertising services	(60,774)	(36,473)
Mobilization activity	(17,433)	(16,465)
Other	(293,262)	(493,128)
Total	(2,008,126)	(1,753,896)

Other expenses primarily consist of expenses for accounting for payments from subscribers, measures to prevent default in payments and general activity for direction and management.

General and Administrative Expenses

	2003	2002
Fire and other security services	(314,337)	(155,637)
Transportation services	(110,405)	(72,060)
Education expenses	(67,078)	(39,934)
Payments to Gossvyaznadzor	(63,667)	(49,317)
Business travel expenses and representation costs	(44,887)	(34,549)
Post services	(21,433)	(38,474)
Other expenses	(51,591)	(91,775)
Total	(673,398)	(481,746)

6. Interest Expense, net

	2003	2002
Interest income	4,864	2,005
Interest expense	(950,703)	(604,188)
Interest expense accrued on financial leases	(352,416)	(199,365)
Total	(1,298,255)	(801,548)

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

7. Other Income (expenses), net

	2003	2002
Charity contributions	(117,120)	(108,387)
Write – off of social property and equipment	(115,890)	(66,783)
Penalties and fines due to breach of contract terms	(26,365)	(17,612)
Other	(82,923)	(15,763)
Total	(342,298)	(208,545)

8. Income Tax

The income tax charge for the years ended December 31, 2003 and 2002 comprised the following:

	2003	2002
Current income tax expense	(682,423)	(563,520)
Prior-year income tax adjustments	–	–
Carry-forward of tax losses and unused tax credits resulting in the decrease of current income tax expense	–	–
Total current income tax expense	(682,423)	(563,520)
Deferred income tax benefit relating to reversal of temporary differences	566,141	606,086
Total deferred income tax benefit	566,141	606,086
Total income tax (charge) benefit for the year	(116,282)	42,566

A reconciliation of the theoretical tax charge to the actual income tax charge is as follows:

	2003	2002
Profit before income tax and minority interest	280,244	46,186
Statutory income tax rate	24%	24%
Theoretical tax charge at statutory income tax rate	(67,259)	(11,085)
Increase (decrease) resulting from the effect of:		
Prior-year income tax adjustments	–	–
Non-taxable income	–	–
Expenses not deductible for tax purposes	(275,473)	(137,523)
Amortization of goodwill	(1,565)	(1,250)
Carry-forward of tax losses and unused tax credits resulting in the decrease of current income tax expense	3,115	18,253
Other permanent differences	224,900	260,693
Reversal of valuation allowance for deferred tax assets	–	358,773
Permanent element of net monetary gain	–	(445,295)
Total income tax charge for the year at the effective rate of 41% (2002: (92%))	(116,282)	42,566

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

8. Income Tax (continued)

The composition of deferred tax assets and liabilities as of December 31, 2003 and 2002, and their movement in the year ended December 31, 2003 and 2002, were as follows:

	December 31, 2003	Difference	December 31, 2002
<i>Tax effects of deferred tax assets:</i>			
Accounts payable	137,624	1,432	136,192
Accounts receivable	100,230	63,376	36,854
Investment valuation effect	7,459	18,215	(10,756)
Others	67,043	51,125	15,918
Deferred tax asset, total	312,356	134,148	178,208
<i>Tax effects of deferred tax liabilities:</i>			
Property, plant and equipment	(683,772)	429,074	(1,112,846)
Inventory	(1,444)	2,091	(3,535)
Deferred income tax liability, total	(685,216)	431,165	(1,116,381)
Net deferred income tax liability	(372,860)	565,313	(938,173)

The movement in net deferred tax liability for the year ended December 31, 2003 was as follows:

Deferred income tax liability, net as of December 31, 2002	(938,173)
Deferred income tax benefit	566,141
Deferred income tax expense related to changes in fair value of investments available-for-sale	(828)
Deferred income tax liability, net as of December 31, 2003	(372,860)

9. Earnings (losses) per Share

Basic and diluted earnings per share are calculated by dividing the net income for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year.

	2003	2002
Net income (losses) attributable to ordinary shareholders (basic and diluted)	7,803	(27,771)
Weighted average number of ordinary shares for basic and diluted loss per share	1,578,006,833	1,578,006,833
Earnings (losses) per ordinary share, Rubles (basic and diluted)	0.005	(0.018)

The Company has no financial instruments that can be converted into ordinary shares.

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

10. Dividends Declared and Proposed for Distribution

Dividends declared in 2003 for the year 2002

Dividends on ordinary shares, 0.096 rubles per share	151,570
Dividends on preferred shares, 0.206 rubles per share	108,430
Total	260,000

Approved at the annual shareholder meeting for the year 2003 (see Note 32, "Subsequent Events")

Dividends on ordinary shares, 0.125 rubles per share	197,040
Dividends on preferred shares, 0.286 rubles per share	150,256
Total	347,296

Earnings available for dividends are limited to profits determined in accordance with Russian statutory accounting regulations.

11. Property, Plant and Equipment

	Buildings and constructions	Switches and transmission devices	Construction in progress and equipment for installation	Machines and other	Total
Cost					
At December 31, 2002	37,570,085	36,156,848	2,058,164	11,620,484	87,405,581
Additions	–	–	6,696,015	–	6,696,015
Disposals	(161,787)	(350,698)	(3,318)	(118,098)	(633,901)
Transfers	1,555,167	4,548,029	(6,900,807)	797,611	–
At December 31, 2003	38,963,465	40,354,179	1,850,054	12,299,997	93,467,695
Impairment					
At December 31, 2002	(2,560,303)	(2,547,961)	(206,791)	(251,268)	(5,566,323)
Transfer	(46,616)	(136,325)	206,791	(23,850)	–
Impairment loss on disposal of Property, Plant and Equipment	2,573	5,770	–	26	8,369
At December 31, 2003	(2,604,346)	(2,678,516)	–	(275,092)	(5,557,954)
Accumulated depreciation					
At December 31, 2002	(26,125,822)	(26,317,736)	–	(8,789,437)	(61,232,995)
Charge for the year	(1,094,047)	(2,154,281)	–	(306,177)	(3,554,505)
Disposals	137,704	289,573	–	113,266	540,543
At December 31, 2002	(27,082,165)	(28,182,444)	–	(8,982,348)	(64,246,957)
Net book value as of December 31, 2002	8,883,960	7,291,151	1,851,373	2,579,779	20,606,263
Net book value as of December 31, 2003	9,276,952	9,493,219	1,850,053	3,042,560	23,662,784

Notes to Consolidated Financial Statements (continued)

11. Property, Plant and Equipment (continued)

The net book value of plant and equipment held under finance leases at December 31, 2003 is 2,013,181 (2002 – 938,389) Leased assets are pledged as security for the related finance lease obligations (see 24 “Finance lease obligations”).

In 2003, the Company received equipment on supplier credit terms in the amount of 442,414 (2002 – 566,478).

In 2003, the Company increased construction in progress by the amount of capitalized interest totaling 121,500 (2002 – 34,771) (see Note 6 “Interest expenses”).

Net book value of Property, Plant and Equipment in the amount of 4,667,431 (2002 - 2,415,932) as of December 31, 2003 is pledged as security for the Company’s borrowings (see Note 23 “Loans and Borrowings”).

The Company's accounting records relating to fixed assets are not designed to support their presentation in accordance with IAS 16, “Property, Plant and Equipment”, IAS 29, “Financial Reporting in Hyperinflationary Economies” and IAS 36, “Impairment of Assets”. As such, certain estimates and assumptions were made by management to present fixed assets in the accompanying consolidated financial statements.

In the future, the Company expects to hire an independent appraiser to assist in reconstruction of the fair value of the Property, Plant and Equipment, in order to make the necessary adjustments to the Group’s books and records, to comply with IFRS.

12. Intangible Assets and Goodwill

	Goodwill	Licenses	Software	Total
Cost				
At December 31, 2002	29,319	3,816	80,617	113,752
Additions	–	10,408	961,517	971,925
Disposals	–	–	(1,056)	(1,056)
At December 31, 2003	29,319	14,224	1,041,078	1,084,621
Accumulated amortization				
At December 31, 2002	(5,207)	(291)	(12,777)	(18,275)
Charge for the year	(6,520)	(2,056)	(25,464)	(34,040)
Disposals	–	–	983	983
At December 31, 2003	(11,727)	(2,347)	(37,258)	(51,332)
Net book value at				
December 31, 2002	24,112	3,525	67,839	95,477
Net book value at				
December 31, 2003	17,592	11,877	1,003,820	1,033,289

Goodwill arising on the acquisition of ZAO “CenterTelecomService of Moscow Region” on April 30, 2002 is amortized on a straight-line basis over the entire useful life estimated by the Company's management at 5 years.

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

12. Intangible Assets and Goodwill (continued)

In accordance with the Board decision of OAO “Svyazinvest”, the Company’s parent, dated April 14, 2003, the Company was instructed to proceed with the purchase and implementation of an enterprise management system (ERP) based on Oracle E-business Suite software. The Company’s Board of Directors confirmed this decision on May 28, 2003 and approved a supply contract with ZAO “Otkrytye tekhnologii 98” in the amount of 30,323 thousand US Dollars excluding VAT (approximately 928,450 at the exchange rate as of May 28, 2003).

In accordance with the supply contract, the Company has been provided with non-exclusive licenses for 18,049 users of E-business Suite among other license applications.

The Company will commence amortization of these costs upon substantial completion of implementation. Prior to this time management will periodically assess this intangible asset for impairment. The Company expects to complete this system implementation in 2007.

13. Investments in subsidiaries

The consolidated financial statements include the assets, liabilities and financial results of OAO “CenterTelecom” and its subsidiaries listed below:

Subsidiary	Main Activity	Voting Shares	
		2003	2002
OOO “Mobilcom”	Communication services	100%	100%
OOO “Teleport Ivanovo”	Communication services	100%	100%
OOO “Telecom-Terminal”	Repair and maintenance services	100%	100%
OOO “Telecom-stroy”	Construction services	100%	100%
OOO “Vlad Page”	Communication services	75%	75%
ZAO “CenterTelecom Service”	Communication services	75%	–
OOO “Svyaz-Service-Igra”	Repair and maintenance services	70%	70%
ZAO “CenterTelecomService of Moscow Region”	Communication services	51%	51%
OOO “Vladimirsky Taksophon”	Communication services	51%	51%
ZAO “Telecom of Ryazan Region”	Communication services	51%	51%
ZAO “Teleross Voronej”	Communication services	50%	50%
ZAO “Vladimir Teleservice”	Communication services	50%	50%

All the above companies are Russian legal entities registered in accordance with Russian legislation.

In 2003 the Company made a contribution of 75 to acquire a 75% equity interest in ZAO “CenterTelecomService”.

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

14. Investments in Associates

Investments in associates at December 31, 2003 and 2002 comprised the following:

Associate	Activity	As of December 31, 2003		As of December 31, 2002	
		Voting shares	Carrying value	Voting shares	Carrying value
Joint activity	Communication services	30%	14,579	30%	14,579
OAO "Gazenergobank"	Banking	25%	8,264	25%	5,321
OOO "Tver Telecom"	Communication services	26%	6,556	26%	11,807
OAO "Telecommunication company Rinfotels"	Data transmission services	26%	1,291	26%	1,196
Others			31		3,204
Total			30,721		36,107

In accordance with IAS 28 "Accounting for Investments in Associates" the Company reduced the carrying value of the associates to zero in cases when the Company's share in accumulated loss exceeded the cost of the respective investment. These investments are reported as "Others" as of December 31, 2003.

Movement in investments in associates in 2003 is presented below:

Investments in associates at December 31, 2002	36,107
Acquisition of associates	-
Share in net assets of associates, net of dividends received (2003 - 4,265)	(5,015)
Sale of investments in associates	(9)
Impairment of investments recognized in 2003	(362)
Investments in associates at December 31, 2003	30,721

The carrying value of investments in associates shown in these consolidated financial statements is equivalent to the Company's share in the net assets of investees less impairment reserve.

The company has a 30% investment in joint activity on establishment, development, and commercial use of CDMA switching system in Ivanovo city with OOO "Topsnabinvest" and OOO "Bowling-Center". The contract on the joint activity was concluded on December 31, 1998 with a term of 12 years.

Notes to Consolidated Financial Statements (continued)

14. Investments in Associates (continued)

Investment in the joint activity is accounted for using equity method. Table below presents additional financial information on the joint activity as of 31 December 2003 and 2002:

	<u>2003</u>	<u>2002</u>
Share in joint activity	30%	30%
Long-term assets	45,466	43,813
Current assets	20,700	5,930
Current liabilities	17,570	1,147
Total Net assets	48,596	48,596
Company's share in Net assets	14,579	14,579
Revenues	22,067	17,903
Operating expenses	8,503	8,533
Net profits	13,564	9,370
Company's share in Net profits	4,070	2,811

15. Other Long-term Investments

As of December 31, 2003 and 2002, the Company's investments comprised the following:

	<u>2003</u>	<u>2002</u>
Long-term investments held-to-maturity	163	182
Long-term investments available-for-sale	8,396	35,922
Total	8,559	36,104

In 2003 the Company created impairment reserve for AOOT "Krugozor" in the amount of 17,472, for ZAO "Oskol-Telecom" in the amount of 2,147, for MKB "Svyazbank" in the amount of 1,137 and 664 for other investments. Carrying value of the investments disposed during 2003 has amounted to 6,163.

16. Advances to Suppliers of Equipment

As of December 31, 2003 advances to suppliers of equipment comprised of the following:

	<u>2003</u>	<u>2002</u>
Advances for purchase of property and equipment	373,249	140,698
Advances for construction in progress	280,990	105,920
Advances for materials for construction in progress	5,069	1,534
Total	659,308	248,152

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

17. Inventories

Inventories at December 31, 2003 and 2002 included the following:

	2003	2002
Cable, materials and spare parts for telecommunications equipment	603,972	509,883
Finished goods and goods for resale	21,358	30,396
Other inventories	9,317	10,989
Total	634,647	551,268

18. Trade accounts receivable

Accounts receivable at December 31, 2003 and 2002 comprised the following:

	2003	2002
Trade receivables – telecommunication services	2,733,872	1,850,515
Allowance for doubtful accounts	(1,247,545)	(558,887)
Total	1,486,327	1,291,628

The Company identified trade receivables by the following major customer groups:

	2003	2002
Corporate customers	502,918	470,895
Residential customers	865,353	633,316
Government customers, including tariff compensation from the state budget	1,365,601	746,304
Total	2,733,872	1,850,515

The Company invoices its governmental and corporate customers on a monthly basis. For residential customers, the Company sends monthly payment requests and substantially relies upon these customers to remit payments based on the received payment requests. All customer payments are based upon tariffs, denominated in rubles, in effect at the time the calls are made. In limited circumstances, the Company has billed and collected penalties associated with delays in payment and have been able to obtain certain payments through the Arbitrage Court.

19. Other financial assets

As of December 31, 2003 and 2002, other financial assets included:

	2003	2002
Long-term accounts receivable	3,603	5,848
Long-term loans given	33,177	22,460
Total	36,780	28,308

Long-Term Loans Given are primarily comprised of interest-free loans given to employees of the Company and loans given to legal entities earning 25% per annum. As of December 31, 2003 the outstanding amounts comprised 30,763 and 2,414, respectively.

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

20. Other current assets

As of December 31, 2003 and 2002 other current assets comprised the following:

	2003	2002
VAT recoverable	1,068,332	806,098
Prepaid income tax	238,349	93,367
Prepaid expenses	206,023	119,315
Prepayments and advances paid	195,521	175,848
Other prepaid taxes	21,389	22,330
Settlements with personnel	11,084	6,245
Other receivables	115,003	94,432
Total	1,855,701	1,317,635

21. Cash and cash equivalents

As of December 31, 2003 and 2002 cash and cash equivalents comprised the following:

	2003	2002
Cash at bank and on hand	1,028,494	287,980
Short-term deposits with original maturities of three months or less	23,940	19,310
Other cash equivalents	155	-
Total	1,052,589	307,290

Short-term deposits range in maturity from one to three months, depending on current cash requirements.

22. Share capital

	2003		2002	
	Shares	Share capital	Shares	Share capital
Preferred shares at par value 0.30 Rubles:				
• Shares authorized, issued and outstanding as of December 31	525,992,822	157,798	525,992,822	157,798
Ordinary shares at par value 0.30 Rubles				
• Shares authorized, issued and outstanding as of December 31	1,578,006,833	473,402	1,578,006,833	473,402
Total share capital		631,200		631,200

As a result of the reorganization (see Note 1 “General Information”), the state registration of amendments to the charter documents was completed on November 30, 2002.

The share capital account represents the authorized capital of the Company as stated in the charter documents. The Company had 1,578,006,833 ordinary shares and 525,992,822 Class A preferred shares as of December 31, 2003.

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

22. Share capital (continued)

All shares have a par value of 0.30 Rubles per share. Of the share capital issued as of December 31, 2003, 75% was attributable to ordinary shares, and 25 % attributable to Class A preferred shares. The ordinary shareholders are allowed one vote per share. Class A preferred shares are non-voting.

All ordinary shares and Class A preferred shares are eligible for distribution of ruble earnings available in accordance with Russian statutory accounting regulations. Each Class A preferred share is entitled to a minimum annual dividend in the amount 10 % of statutory net income available for dividends. Dividends on Class A preferred shares may not be less than dividends on ordinary shares. Shareholders of Class A preferred shares have a preferential right to recover the par value of preferred shares in liquidation.

In 2001 the Company concluded a Depositary Agreement with JP Morgan Chase Bank in respect of American Depositary Receipts (ADRs), Level 1. In accordance with the depositary agreement each ADR is equal to 100 ordinary shares of the Company. As at the end of 2003, ADRs represented 24,936,100 deposited ordinary shares, which constituted 1.58 % of total ordinary shares issued.

The Company's shareholding structure as of December 31, 2003 was as follows:

	Ordinary shares		Preferred shares		Total
	Number	%	Number	%	
OAO Svyazinvest	799,867,813	51%	–	–%	799,867,813
Other legal entities	656,447,790	42%	426,359,901	93%	1,082,807,691
Individuals	121,691,230	8%	99,632,921	7%	221,324,151
Total	1,578,006,833	100%	525,992,822	100%	2,103,999,655

23. Loans and borrowings

As of December 31, 2003 and 2002 borrowings consisted of the following:

	Interest rate	Maturity date	2003	2002
<u>Short-term borrowings</u>				
<u>Bank loans:</u>				
Bank loans (Rubles)	16.84%	2004	1,980,470	1,273,954
Bank loans (US Dollars)	18.00%	2004	97,784	103,819
Bank loans (Euro)	7.44%	2004	623,756	641,305
Total bank loans			2,702,010	2,019,078
Bonds (Rubles)		2004	78,699	636,184
<u>Vendor financing</u>				
Vendor financing (Rubles)	18.26%	2004	32,084	87,641
Vendor financing (US Dollars)	8.91%	2004	44,419	162,241
Vendor financing (Euro)	8.59%	2004	26,531	50,408
Total vendor financing			103,034	300,290
Promissory notes (Rubles)	14.22%	2004	535,906	–
Total short-term borrowings			3,419,649	2,955,552

Notes to Consolidated Financial Statements (continued)

23. Loans and borrowings (continued)

	Interest rate	Maturity date	2003	2002
<u>Long-term borrowings</u>				
Bank loans:				
Bank loans (Rubles)	14.56%	2004-2008	3,465,443	207,325
Bank loans (US Dollars)	8.74%	2004-2007	710,900	551,017
Bank loans (Euro)	7.85%	2004-2007	607,444	420,654
Bank loans (other currencies)	4.79%	2005	16,302	25,726
Total bank loans			4,800,089	1,204,722
Bonds (Rubles)		2006	2,559,028	600,000
Vendor financing:				
Vendor financing (Rubles)	18.26%	2004-2007	4,905	5,347
Vendor financing (US Dollars)	8.73%	2004-2006	157,949	286,448
Vendor financing (Euro)	8.11%	2004-2007	385,828	616,727
Total vendor financing			548,682	908,522
Borrowings from related parties (OAo Syvazinvest, Note 30)	14.05%	2004-2005	33,015	63,399
Restructured connection fees from customers (Rubles)		2004-2011	134,259	132,126
Less: Current portion of long-term borrowings			(1,105,797)	(960,652)
Total long-term borrowings			6,969,276	1,948,117

As of December 31, 2003 short-term borrowings included interest payable in the amount of 419,333 (2002 – 181,606). This amount includes coupon interest payable on 02 Series bonds in the amount of 6,291 and on 03 Series bonds – 72,408.

As of December 31, 2003 long-term borrowings had the following maturity schedule:

	Bank loans	Bonds	Vendor financing	Other	Total
2004	768,433	–	333,349	4,015	1,105,797
2005	2,088,202	600,000	46,943	29,528	2,764,673
2006	512,054	1,959,028	41,541	3,018	2,515,641
2007	103,494	–	126,849	17,120	247,463
2008 and thereafter	1,327,906	–	–	113,593	1,441,499
Total	4,800,089	2,559,028	548,682	167,274	8,075,073

Notes to Consolidated Financial Statements (continued)

23. Loans and borrowings (continued)

Short-term borrowings

Bank loans

Short-term ruble borrowings mainly represent bank loans received for working capital financing purposes. Most of these loans are collateralized with telecommunications equipment.

Sberbank

In 2002-2003 the Company entered into short-term loan agreements with Sberbank of RF. The loans mature in 2004. As of December 31, 2003 the outstanding liability under these agreements amounted to 420,883. Interest is accrued at 14%-22% per annum. The loans are secured by property and equipment.

Promsvyazbank

In 2002-2003 the Company entered into loan agreements with Promsvyazbank. The loans mature in 2004. As of December 31, 2003 the outstanding liability under these agreements amounted to 573,373. Interest is accrued at 14%-19% per annum. The loans are secured by property and equipment.

Trustbank

In 2003 the Company entered into a loan agreement with Trustbank. As of December 31, 2003 the outstanding liability under these agreements amounted to 502,411. Interest is accrued at 16% per annum. The loan is not secured.

Vneshekonombank

In 1995-1997 the Ministry of Finance (hereafter “the Ministry”) granted the Company long-term financing for purchases of telecommunication equipment from various foreign vendors. Vneshekonombank has been acting as an agent of the Ministry on collection of payments from the Company. The liability was initially denominated in Deutsche Marks (DM), and later in Euro after introduction of the Euro.

Following the crisis of 1998 and the significant increase of the exchange rate of DM to ruble, repayments on these agreements were ceased. As a result, as at December 31, 2003 approximately 373,133 of payables, including interest payable of 59,720 due to Vneshekonombank were overdue.

As of December 31, 2003 the outstanding short-term liability, including overdue amounts, under these agreements amounted to 599,177. Interest is accrued at Plafond C + 2%. In 2003 the interest rate applied varied in the range of 6%-7%. The loan was not secured.

Notes to Consolidated Financial Statements (continued)

23. Loans and borrowings (continued)

Short-term borrowings (continued)

Bank loans (continued)

Vneshtorgbank

In 2001-2003 the Company has entered into loan agreements with Vneshtorgbank. The loans mature in 2004. The loans are denominated in Russian rubles, US dollars and Euro. Interest for loans denominated in Russian rubles is accrued at 14%-20% per annum, for loans denominated in US dollars – 8%-9% per annum, for loans denominated in Euro – 8%-9% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 15,680 for loans denominated in Russian rubles, 2,706 - for loans denominated in US dollars and 98,720 – for loans denominated in Euro. The loans are secured by property and equipment.

Guta-bank

In 2001-2003 the Company entered into loan agreements with Guta-bank. The loans mature in 2004. The amount payable under the agreements are denominated in Russian rubles and US dollars. Interest for loans denominated in Russian rubles is accrued at 14%-21% per annum, for loans denominated in US dollars – 7%-9% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 181,601 for loans denominated in Russian rubles and 3,530 – for loans denominated in US dollars. The loans are not secured.

Vendor financing

ZAO “Sokol-ATS”

In April 2003 the Company entered into a short-term agreement with ZAO “Sokol-ATS”, under which Sokol-ATS delivered telecommunication equipment to the Company. The agreement matures in 2004. As of December 31, 2003 the outstanding liability under these agreements amounted to 32,084.

Promissory notes

In 2003 the Company issued promissory notes at par value of 606,082. The notes were purchased by OAO “Vneshtorgbank” and ZAO “RTC-Invest”. A discount of 76,569 was applied to the notes upon issue. Interest on the notes is accrued at 14%. The notes mature in November-December 2004.

Long-term borrowings

Bank loans

Sberbank

In 2001-2003 the Company entered into long-term loan agreements with Sberbank of RF. The loans mature in 2004. As of December 2003 the outstanding liability under these agreements amounted to 2,965,762, including current portion of 182,800 payable in 2004. Interest is accrued at 14%-22% per annum. The loans are secured by property and equipment.

Notes to Consolidated Financial Statements (continued)

23. Loans and borrowings (continued)

Long-term borrowings (continued)

Bank loans (continued)

Vneshekonombank

In 1995-1997 the Ministry of Finance (hereafter “the Ministry”) granted the Company long-term financing for purchases of telecommunication equipment from various foreign vendors. Vneshekonombank has been acting as an agent of the Ministry on collection of payments from the Company. The liability was initially denominated in Deutsche Marks (DM), and later in Euro after introduction of the Euro.

As of December 31, 2003 the outstanding long-term liability under these agreements amounted to 346,420, including current portion of 120,692 payable in 2004. Interest is accrued at Plafond C + 2%. In 2003 the interest rate applied varied in the range of 6%-7%. The loan was not secured.

Vneshtorgbank

In 2001-2003 the Company has entered into loan agreements with Vneshtorgbank. The loans mature in 2004-2006. The loans are denominated in US dollars and Euro. Interest for loans denominated in USD is accrued at 8%-9% per annum, for loans denominated in Euro – 6%-9% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 499,722 for loans denominated in US dollars, and 261,024 – for loans denominated in Euro. Current portion of 394,341 is payable in 2004. The loans are secured by property and equipment.

Guta-bank

In 2001-2003 the Company entered into loan agreements with Guta-bank. The loans mature in 2005-2007. The amount payable under the agreements are denominated in Russian rubles and US dollars. Interest for loans denominated in Russian rubles is accrued at 15% per annum, for loans denominated in US dollars – LIBOR + 7%. As of December 31, 2003 the outstanding liability under these agreements amounted to 480,077 for loans denominated in Russian rubles and 211,783 – for loans denominated in US dollars. Current portion of 70,599 is payable in 2004. The loans are not secured.

Bonds

On August 1, 2003, the Company registered the issue of 2,000,000 interest-bearing bearer's bonds, Series 03, par value of 1,000 rubles each. Bonds have 6 coupons. Payments against the first coupon are made on the 183rd day from the date of issue; interest per second coupon - 366th day, per third – 549th day, per fourth – 731st day, per fifth – 931st day, per sixth – 1095th day. Coupon interest rate is determined at 12.35%. The bonds mature in 1,095 days from the date of issue, on September 14th, 2006.

In November 2003 the Company redeemed 600,000 bonds, series 01, par value of 1,000 rubles per each.

Notes to Consolidated Financial Statements (continued)

23. Loans and borrowings (continued)

Long-term borrowings (continued)

Vendor Financing

Iskratel

In 1999-2003 the Company entered into a number of agreements with Iskratel, under which Iskratel undertook to deliver telecommunications equipment. The outstanding amount under these agreements is denominated in US dollars and Euros. Interest is accrued at 7%-8% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 232,220, including current portion of 193,032 payable in 2004. The loans are not secured.

Mashpriborkom.

In 1997 the Company entered into a number of agreements with Mashpriborkom, under which Mashpriborkom undertook to deliver telecommunications equipment. The agreements mature in 2005-2007. The outstanding amount under these agreements is denominated in Euros. The interest is accrued at 9% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 132,581. The loans are not secured.

Siemens

In 1994-1998 the Company entered into a number of agreements with Siemens, under which Siemens undertook to deliver telecommunications equipment. The agreements mature in 2004-2007. The outstanding amount under these agreements is denominated in Euros. The interest is accrued at 6%-7% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 86,632, including current portion of 53,498 payable in 2004. The loans are not secured.

Alcatel

In 1996-2002 the Company entered into a number of agreements with Alcatel, under which Alcatel undertook to deliver telecommunications equipment. The agreements mature in 2004-2007. The outstanding amount under these agreements is denominated in Euros. The interest is accrued at fixed rate of 6% per annum and floating rate LIBOR + 3%. As of December 31, 2003 the outstanding liability under these agreements amounted to 31,996, including current portion of 23,631 payable in 2004. The loans are not secured.

Quantintercom

In 2001-2003 the Company entered into a number of agreements with Quantintercom, under which Quantintercom undertook to deliver telecommunications equipment. The agreements mature in 2004. The outstanding amount under these agreements is denominated in US dollars. The interest is accrued at 8% per annum. As of December 31, 2003 the outstanding liability under these agreements amounted to 15,848, which is payable in 2004. The loans are not secured.

Notes to Consolidated Financial Statements (continued)

23. Loans and borrowings (continued)

Long-term borrowings (continued)

Restructured customer payments for telephone installation

In 1997-2003 the Company entered into loan agreements with individuals for financing of the development of communication infrastructure. Under the terms of the agreements the Company settles the loans by telephone installation and payments. The agreements mature in 2004-2011. As of December 31, 2003 the outstanding liability under these agreements amounted to 134,259.

24. Finance lease obligations

The Company has finance lease contracts for telecommunication equipment. Future minimum lease payments under finance lease contracts together with the present value of the net minimum lease payments as of December 31, 2003 and 2002 are as follows:

	2003		2002	
	Minimum payments	Present value of payments	Minimum payments	Present value of payments
Current portion	877,871	512,769	482,905	399,130
2 to 5 years	1,700,217	1,167,947	689,023	390,060
Total minimum lease payments	2,578,088	–	1,171,928	–
Less amounts representing finance charges	(897,372)	–	(382,738)	–
Present value of minimum lease payments	1,680,716	1,680,716	789,190	789,190

In 2003 and 2002, the Company's primary lessors were RTC-Leasing and Promsvyazleasing. In 2003, effective interest rate on the Company's leasing liabilities were 34% in Rubles and 30% in hard currency per annum (2002 - respectively 35% and 31%).

RTC-Leasing purchases telecommunication equipment from domestic and foreign suppliers and leases the equipment. The Company's obligations under capital leases to RTC-Leasing as at December 31, 2003 comprised 1,362,038 (2002 – 321,498) (See Note 30 "Related parties disclosures").

Pursuant to agreements concluded with RTC-Leasing and Promsvyazleasing, the lessor is entitled to adjust the lease payment schedule in the event of change in certain changes in economic environment, in particular, change in the refinancing rate of the Central Bank of Russian Federation.

Notes to Consolidated Financial Statements (continued)

25. Trade Accounts Payable and Accrued Liabilities

As of December 31, 2003 and 2002, the Company's trade accounts payable and other current liabilities comprised:

	<u>2003</u>	<u>2002</u>
Trade accounts payable	442,833	521,783
Accounts payable for capital investments	405,808	402,167
Advances received from subscribers	396,045	403,802
Salaries and wages payable	178,409	150,552
Other accounts payable	193,990	370,213
Total	1,617,085	1,848,517

26. Tax and Payroll Related Obligations

As of December 31, 2003 and 2002, the Company had the following taxes outstanding:

	<u>2003</u>	<u>2002</u>
Value-added tax accrued	412,513	233,109
Value-added tax payable	238,037	187,424
Income tax	121,474	139,340
Property tax	92,561	71,836
Unified social tax	78,369	72,112
Sales tax	41,401	53,689
Personal income tax	35,077	29,594
Tax penalties accrued	34,261	21,593
Other taxes	6,305	18,988
Total	1,059,998	827,685

27. Pension plans and employee benefits

In 2003 the Company made various payments to employees in addition to salary. These payments generally represent financial aid to the Company's employees with limited abilities and bonuses to employees, which had made no breaches of internal policies during the last fiscal year. Such benefits were included in salary, benefits, salary taxes and other social expenditures in the accompanying consolidated statements of operations for the year ended December 31, 2003.

In addition to statutory pension benefits, the Company also contributes to defined benefit plans, which covers most of its employees. Non-government pension fund Telecom-Soyuz, which is related to the Company, maintains the plan (see Note 30 "Related parties disclosures"). In addition to Telecom-Soyuz, Tulski Regionalni non-governmental pension fund and Tver non-governmental pension fund "Sodruzhestvo", which are not related to the Company, maintain the plans. The plans provide for payment of retirement benefits starting from statutory retirement age, which is currently 55 for women and 60 for men. The benefits are based on a formula recognizing minimal statutory pension, length of service both in the Company and in the telecommunications industry, as well as final average earnings and position in the Company at retirement. The benefits are not vesting and are subject to the employee retiring from the Company on or after the above-mentioned ages. The Company makes contributions to the pensions funds as a set percentage of the employees' salaries or in the amount set forth in the agreement with the pension fund subject to a specific pension arrangement.

Notes to Consolidated Financial Statements (continued)

27. Pension plans and employee benefits (continued)

The Company has not made an actuarial determination of current debt under these agreements as is required by accounting policy (see Note 2 “Summary of Significant Accounting Policies”), and hence has not recorded its obligations or made disclosures required under IAS 19, “Employee Benefits”, pertaining to the value of obligations and assets of the plan as of December 31, 2003.

28. Commitments and contingencies

General contingencies

The Russian economy while deemed to be of market status beginning in 2002, continues to display certain traits consistent with that of a market in transition. These characteristics have in the past included higher than normal historic inflation, lack of liquidity in the capital markets, and the existence of currency controls, which cause the national currency to be illiquid outside of Russia. The continued success and stability of the Russian economy will be significantly impacted by the government’s continued actions with regard to supervisory, legal, and economic reforms.

Management cannot predict what effect changes in fiscal, political or tariffing policies may have on the Company’s current financial position or its ability to make future investments in property, plant and equipment. The consolidated financial statements do not include any adjustments that might result from these uncertainties. Related effects will be reported in the financial statements, as they become known and estimable.

Tax laws and regulations

Legislation and regulations regarding taxation and foreign currency transactions in Russia continue to evolve as the government manages the transformation from a command to a market-oriented economy.

During 2002, the Russian Federation enacted a new tax code with significant modifications from the prior law.

The various legislation and regulations are not always clearly written and their interpretation is subject to the opinions of the local, regional and national tax authorities, the Central Bank and Ministry of Finance. Instances of inconsistent opinions are not unusual.

The current regime of penalties and interest related to reported and discovered violations of Russia’s laws, decrees and related regulations are severe. Interest (at the Central Bank of RF official rates) and fines are levied when an understatement of tax liability is discovered. As a result, penalties and interest can result in amounts that are multiples of any unreported taxes.

The Company believes that it has paid or accrued all taxes that are applicable. Where practice concerning the provision of taxes was unclear, the Company has accrued tax liabilities based on management’s best estimate. The Company’s policy is to accrue for contingencies in the accounting period in which a loss is deemed probable and the amount is reasonably determinable. No such accruals have been made as at 31 December 2003.

Notes to Consolidated Financial Statements (continued)

28. Commitments and contingencies (continued)

Tax laws and regulations (continued)

Because of the uncertainties associated with the Russia tax and legal systems, the ultimate amount of taxes, penalties and interest assessed, if any, may be in excess of the amount expensed to date and accrued as at 31 December 2003 and 2002.

Insurance coverage

The Russian insurance industry is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. During 2003, the Company did not maintain insurance coverage on a significant part of their property, plant and equipment asset bases, business interruption, or third party liability in respect of property or environmental damage arising from accidents on the Company's property or relating to the Company's operations. Until the Company obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Company's operation and financial position.

Litigation, claims and assessments

The Russian legal system is characterized by (1) inconsistencies between and among laws, Presidential decrees, and Russian governmental, ministerial and local orders, decisions, and resolutions and other acts; (2) conflicting local, regional and federal rules and regulations; (3) the lack of judicial and administrative guidance on interpreting legislation; (4) the relative inexperience of judges and courts in interpreting legislation; and (5) a high degree of discretion on the part of governmental authorities.

Management is unable to estimate what developments may occur in respect of the Russian legal system or the resulting effect of any such developments on the Company's financial condition or future results of operations. The financial statements do not include any adjustment that may result from these uncertainties.

Telecommunication Reforms

On January 1, 2004, a new law on telecommunications came into effect in Russia. The law sets the legal basis for the telecommunications business in Russia and defines the status that state bodies have in the telecommunications sector. The new law may increase the regulation of the Company's operations and until such time as appropriate regulations consistent with the new law are promulgated, there will be a period of confusion and ambiguity as regulators interpret the legislation.

Under the new law, the Company is obliged to provide services under similar circumstances and equal conditions for connecting telecommunications networks and for carrying traffic from communications operators rendering similar services and to render connection services and the services involved in carrying traffic to these operators under the same terms and of the same standard, like for its own structural subdivisions and for affiliated parties.

According to the new telecommunication law, the individual subscriber has an option for local service to be paid based on subscription or by-the-minute payment system.

Management cannot predict with any certainty to what degree (if it all) the new law will affect the Company.

Notes to Consolidated Financial Statements (continued)

29. Outstanding contract obligations

Oracle E-Business Suite

The Company contracted to invest approximately 4 million US dollars into installation of Oracle E-Business system in 2004.

Finance Leasing

In 2003, the Company entered into several leases with OAO "RTC-Leasing". The equipment under these leases will be delivered in 2004. Cost of equipment acquired through these leases, inclusive of installation and other capitalized services approximated 776,841.

Capital Investments

At December 31, 2003 the Company had commitments of 924,659 for capital investments into modernization and expansion of its network.

Guarantees Issued

As of December 31, 2003 the Company was acting as guarantor of third parties in the amount of 1,550,466 (2002 – 1,528,458). Management does not expect occurrence of any material obligations relating to these guarantees.

30. Related parties disclosures

OAO "Svyazinvest"

The Company regards OAO "Svyazinvest" as its parent entity. Svyazinvest was wholly owned by the Russian Government until July 1997 when the Government sold 25% plus one share of the Charter Capital of Svyazinvest to the private sector.

An effectively operating telecommunications and data transmission facility is of great importance to Russia for various reasons including economic, strategic and national security considerations. Consequently, the Government has and may be expected to continue to exercise significant influence over the operations of Svyazinvest and its subsidiary companies.

The Government's influence is not confined to its share holdings in Svyazinvest. It has general authority to regulate tariffs and does regulate domestic long distance tariffs to a limited extent. In addition, the Ministry of Communications and Informatization of the Russian Federation has control over the licensing of providers of telecommunications services.

As at December 31, 2003 and 2002 the Company had an outstanding amount payable to Svyazinvest according to a loan agreement (see Note 23 "Loans and borrowings").

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

30. Related parties disclosures (continued)

OAO “Rostelecom”

OAO “Rostelecom”, a majority owned subsidiary of OAO “Svyazinvest”, is the primary provider of domestic long distance and international telecommunications services in the Russian Federation. The annual expense associated with traffic carried by OAO “Rostelecom” and terminated outside of the Company’s network is stated as interconnection charges. Further, OAO “Rostelecom” uses the Company’s network to provide incoming long-distance and international traffic to its subscribers and partner operators.

Transactions undertaken by the Company with OAO “Rostelecom” reported in the accompanying consolidated financial statements as at December 31, 2003 and 2002 and for the years then ended were as follows:

	2003	2002
Expenses on traffic transfer and rent of channels from Rostelecom	2,258,166	1,390,196
Revenue received from Rostelecom	534,666	55,986
Accounts payable to Rostelecom as at the year-end	381,490	355,471

OAO “RTC-Leasing”

OAO “RTC-Leasing” purchases telecommunication equipment from domestic and foreign suppliers and leases the equipment. In October 2003, OAO “Rostelecom” which owned 27% of ordinary shares of OAO “RTC-Leasing and exercised financial and operational control over the company’s activities, sold all shares of OAO “RTC-Leasing” to a third party.

As a result of this transaction, starting from December 1, 2003 OAO “RTC-Leasing” is not considered to be the Company’s related party and is not included into the Group of companies owned by OAO “Svyazinvest”.

The Company’s obligations under capital leases to OAO “RTC-Leasing” as at December 31, 2003 comprised 1,362,038 (2002 – 321,498), was 81% (2002 – 41%) of the Company’s total obligations for finance leases (see Note 24 “Finance Lease Obligations”).

OAO “RTComm.RU”

During 2003 cost of services for traffic transit provided by the Company to OAO “RTComm.Ru” which is an entity related to OAO “Svyazinvest” in the amount of 67 (2002 – 11). During 2003 OAO “RTComm.Ru” provided traffic transit services to the Company in the amount of 36,776 (2002 – 26,850). As at December 31, 2003 the outstanding amount payable comprised 1,099 (2002 – 0).

Notes to Consolidated Financial Statements (continued)

30. Related parties disclosures (continued)

OAO “MGTS”

During 2003 OAO “MGTS”, which is an entity related to OAO “Svyazinvest”, provided the Company with the following services: rent of conduit for telephone wiring service in the amount of 1,135; rent of space for equipment and offices in the amount of 536; catering services in the amount of 698. Total cost of services provided by OAO “MGTS” is 2,369. As at December 31, 2003 the outstanding amount payable comprised 116 (2002 – 101).

OAO “Central Telegraph”

During 2003 costs of services for traffic transit provided to OAO “Central Telegraph”, an entity related to OAO “Svyazinvest”, amounted to 9,322 (2002 – 8,753). OAO “Central Telegraph” provided traffic transit services to the Company in the amount of 226 (2002 – 360). As at December 31, 2003 the outstanding amount receivable was 2,083 (2002 – amount payable of 33).

OAO “Giprosvyaz”

During 2003 OAO “Giprosvyaz”, a company related to OAO “Svyazinvest”, provided services in the amount of 14,820 (2002 – 6,829). As at December 31, 2003 the amount of accounts payable comprised 8,184 (2002 – accounts receivable of 509).

OAO “Kostromskaya GTS”

During 2003 OAO “Kostromskaya GTS”, an entity related to OAO “Svyazinvest”, provided services in the amount of 8,477 (2002 – 6,450). As at December 31, 2003 the Company’s outstanding amount payable was 16,609 (2002 – 0).

ZAO “RusLeasingsvyaz”

ZAO “RusLeasingsvyaz” is wholly controlled by companies related to OAO “Svyazinvest”. ZAO “RusLeasingsvyaz” acquires telecommunication equipment from domestic and foreign suppliers and leases the equipment. During 2003 the Company entered into several agreements with ZAO “RusLeasingsvyaz” in the total amount of 19,479. The payments are due in 2003-2006.

As at December 31, 2003 the Company’s payables amounted to 32,242, including principal debt of 18,853 and interest of 13,389 (2002 – 16,610, including principal debt of 15,500 and interest of 1,110).

OAO “Natsionalnaya taksophonnaya set”

In 2003 OAO “Natsionalnaya taksophonnaya set” supplied the Company with pay-phone cards in the amount of 2,270 (2002 – 0). As at 31 December 2003 the Company’s payable to the supplier amounted 1,807 (2002 – 0).

Notes to Consolidated Financial Statements (continued)

30. Related parties disclosures (continued)

Transactions with government organizations

Government organizations are a significant element in the Company's customer base, purchasing services both directly through numerous authorities and indirectly through their affiliates. Certain entities financed by the Government budget are users of the Company's network. These entities are generally charged lower tariffs as approved by the Ministry of Antimonopoly Policies and Entrepreneurship Support than those charged to other customers. In addition, the Government may by law require the Company to provide certain services to the Government in connection with national security and the detection of crime.

Government subscribers accounted for approximately 7% of trade accounts receivable as of December 31, 2003 (2002 – 10%) Amounts outstanding from government subscribers as of December 31, 2003, amounted to 58,535 (2002 – 212,098).

Associates

The Company also provided services to its associates, including connection to public network, and rent of space for equipment and premises.

The Company's consolidated financial statements included the following amounts as of December 31, 2003 and 2002:

	2003	2002
<i>Accounts receivable from associates:</i>		
OOO "Tver Telecom"	2,927	–
ZAO "Ryazanskaya Sotovaya Svyaz"	1,513	–
Other	1,319	–
Total:	5,759	–
<i>Accounts payable to associates:</i>		
ZAO "Bryanskiye sotoviye seti"	222	–
ZAO "Tverskaya Sotovaya Svyaz"	66	–
Total:	288	–
<i>Sales to associates:</i>		
OOO "Tver Telecom"	5,913	4,698
OAo "Telecommunication Company "Rinfotels"	3,129	1,511
ZAO "Kalujskaya Sotovaya Svyaz"	1,989	863
ZAO "Bryanskiye sotoviye seti"	1,537	852
ZAO "Tverskaya Sotovaya Svyaz"	1,345	986
ZAO "Ryazanskaya Sotovaya Svyaz"	1,250	896
OAo "Gazenergobank"	933	120
Total:	16,096	9,926
<i>Purchases from associates:</i>		
ZAO "Byanskiye Sotoviye Seti"	1,921	794
OAo "Telecommunication Company "Rinfotels"	1,106	895
ZAO "Tverskaya Sotovaya Svyaz"	865	431
Total:	3,892	2,120

Notes to Consolidated Financial Statements (continued)

30. Related parties disclosures (continued)

Non-commercial partnership Center for Research of Problems in Development of Telecommunications

Non-commercial partnership Center for Research of Problems in Development of Telecommunications (hereinafter “the Partnership”) is an entity related to OAO “Svyazinvest”. The Company has an agreement with the Partnership, under which it provides financing for mutually beneficial projects undertaken by the Partnership on behalf of the Company and other subsidiaries and associates of Svyazinvest. Payments to the Partnership included in other operating expenses in accompanying consolidated statement of operations for the year ended December 31, 2003 amounted to 72,144 (2002 – 69,316).

NPF “Telecom-Soyuz”

Contributions to NPF “Telecom-Soyuz” in 2003 amounted to 131,439 (2002 – 113,714).

Compensation of the Company's management

In 2003, compensation to the members of the Company’s Board of Directors totaled 35,633 (2002 – 7,005).

31. Financial Instruments

Fair Value

The management believes that the value at which the financial instruments are carried in the accompanying consolidated balance sheet as of December 31, 2003 and 2002, approximates their fair value.

Interest rate risk

The following table presents the carrying amount, by maturity, of the Company’s financial instruments that are exposed to interest rate risk:

Year ended December 31, 2002:

	< 1 year	1-5 years	> 5 years	Total
<i>Fixed rate</i>				
Short-term borrowings	2,862,078	–	–	2,862,078
Long-term borrowings	821,166	1,477,516	120,794	2,419,476
Finance lease obligations	399,130	390,060	–	789,190
<i>Floating rate</i>				
Short-term borrowings	93,474	–	–	93,474
Long-term borrowings	139,486	349,807	–	489,293

OAO CenterTelecom

Notes to Consolidated Financial Statements (continued)

31. Financial Instruments (continued)

Year ended December 31, 2003:

	<u>< 1 year</u>	<u>1-5 years</u>	<u>> 5 years</u>	<u>Total</u>
<i>Fixed rate</i>				
Short-term borrowings	3,314,101	–	–	3,314,101
Long-term borrowings	970,297	6,616,884	121,078	7,708,259
Finance lease obligations	512,769	1,167,947	–	1,680,716
<i>Floating rate</i>				
Short-term borrowings	105,548	–	–	105,548
Long-term borrowings	135,500	231,314	–	366,814

32. Subsequent events

Bonds

On April 28, 2004, the Board of Directors approved the issue of 7,000 bearer bonds, each with 1,000 Rubles face value. The bonds have 10 coupons. On June 29, 2004, the bond issue was registered by FCFM (Federal Commission for Financial Markets). The coupon rate amounted to 13.8% a year.

Loan Agreements

On February 20, 2004, the Company entered into a loan agreement with AKB “RosBank” for the amount of 1,424,740. The loan agreement matures in 12 months. The Company accrues and pays interest on the loan to the bank at the rate of 13.5 % per annum.

On April 5, 2004 the Company entered into a loan agreement with OAO “Trustbank” for the amount of 500,000. The loan matures on April 5, 2005. The Company accrues and pays interest on the loan to the bank at the rate of 14% per annum.

On February 16, 2004 the Company entered into a loan agreement with OAO “Sbergatelny bank of Russian Federation” for the amount of 542,094. The loan matures on December 4, 2008. The Company accrues and pays interest on the loan to the bank at the rate of 14.5 % per annum. The loan is collateralized with telecommunications equipment at fair value of 900,852 and collateral value of 630,596 as of October 1, 2003.

On August 9, 2004 the Company entered into a loan agreement with OAO “Sbergatelny bank of Russian Federation” for the amount of 570,000. The loan matures in 5 years. The Company accrues and pays interest on the loan to the bank at the rate of 14 % per annum. The loan is collateralized with telecommunications equipment at collateral value of 663,074.

Promissory Notes

In January-March 2004 the Company issued promissory notes payable to RTC-Invest in the amount of 825,000 maturing January-March 2005.

Notes to Consolidated Financial Statements (continued)

32. Subsequent events (continued)

Finance lease agreements with OAO “RTC-Leasing”

In 2004, the Company entered into a significant number of new finance lease agreements with RTC-Leasing. Total cost of equipment leased under these agreements, inclusive of installation and other capitalized services, approximated 1,260,254, with the respective non-discounted future cash flows totaling approximately 2,007,507.

Purchase of OAO “Russian Telecommunication Network”

In March 2004 the Company acquired 775,227 ordinary shares of OAO “Russian Telecommunication Network” (RTS) which owns the trademark and network “ROSNET” for 25.9 million US dollars representing 88.45% of its share capital.

Sale of Investments

On May 21, 2004 the Board of Directors approved the decision to sell its 40% share in ZAO “Tverskaya Sotovaya Svyaz” and its 25% share in OAO “Gazenergobank”.

On July 13, 2004 the Board of Directors approved the decision to sell its 42% share in ZAO “Kaluzhskaya Sotovaya Svyaz”, 40% share in ZAO “Ryazanskaya Sotovaya Svyaz”, 34% share in ZAO “Bryanskije Sotoviye Seti”, and 60% share in ZAO “Sotovaya Svyaz Chernozemya”.

Purchase of Investments

On May 21, 2004 the Board of Directors approved the decision to purchase an additional 59% share in OOO “TverTelecom” and the remaining 50% share in OOO “VladimirTeleservice” .

On June 10, 2004 the Board of Directors approved the purchase of 100% of the shares of OAO “Aerocom” and ZAO “ATS”.

Dividends

On June 11, 2004, the general meeting of the Company's shareholders approved dividends for 2003 in the amount of 0.28 rubles per preferred share and 0.12 rubles per ordinary share. Total dividends declared amounted to 150,256 and 197,040 rubles for preferred and ordinary shares, respectively. Preferred dividends were accrued as of December 31, 2003 based on the preferred shareholders' minimum dividend interest. Ordinary dividends were accrued when declared in 2004.

Share capital increase

On July 11, 2004, the general meeting of the Company's shareholders approved share capital increase by the change of the face value of one share from 0.3 rubles to 3 rubles per ordinary share and preferred share “A” using the assets revaluation in the amount of 5,680,799. Increase of share capital will be accomplished by means of conversion of existing shares into shares with higher nominal value.

Notes to Consolidated Financial Statements (continued)

32. Subsequent events (continued)

Installation of Oracle E-Business Suite

In March 2004 the Board of Directors approved an agency agreement in the amount of 1,063 thousand US dollars with Non-commercial partnership “Center for Research of Problems in Development of Telecommunications” providing installation of enterprise management system (ERP) based on Oracle E-business Suite software.

Tariffs for telecom services

In 2004 tariffs for local telephony did not change. Tariffs for long-distance domestic services were increased on the average by 29.67% only for entities financed by the government.

OAO “Svyazinvest” audit by the Audit Chamber

In 2003 the RF Federal Assembly instructed the Audit Chamber to audit OAO “Svyazinvest”, a majority shareholder of the Company. As part of the assignment, apart from OAO “Svyazinvest” the Audit Chamber also audited the Company itself. As of the issue date of these financial statements management has not been notified about conclusions made by the Audit Chamber and action steps that might be required from the Company based on the results of the audit. The potential impact of the contingency, if any, is impossible to determine at present.

Constitutional Court Resolution 169-O

In July 2004, Resolution No. 169-O of the Constitutional Court of the Russian Federation dated April 8, 2004 has become publicly available. The resolution has the possible effect of deferring the timing in which companies are able to offset input VAT to the extent the creation of such VAT is deemed to be attributable to the utilization of borrowed funds. In the event local taxing authorities would assert and successfully defend such an interpretation in arbitration courts, the result could have a material adverse impact on the Company's financial condition. As of the date of this report, management is unable to predict the outcome of this uncertainty.

Decrease of VAT rate

Effective from January 2004 the VAT rate decreased from 20% to 18%.