



Annual Report  
2003

URALSVYAZINFORM



# Annual Report 2003

Uralsvyazinform



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# Uralsvyazinform Successful integration of businesses



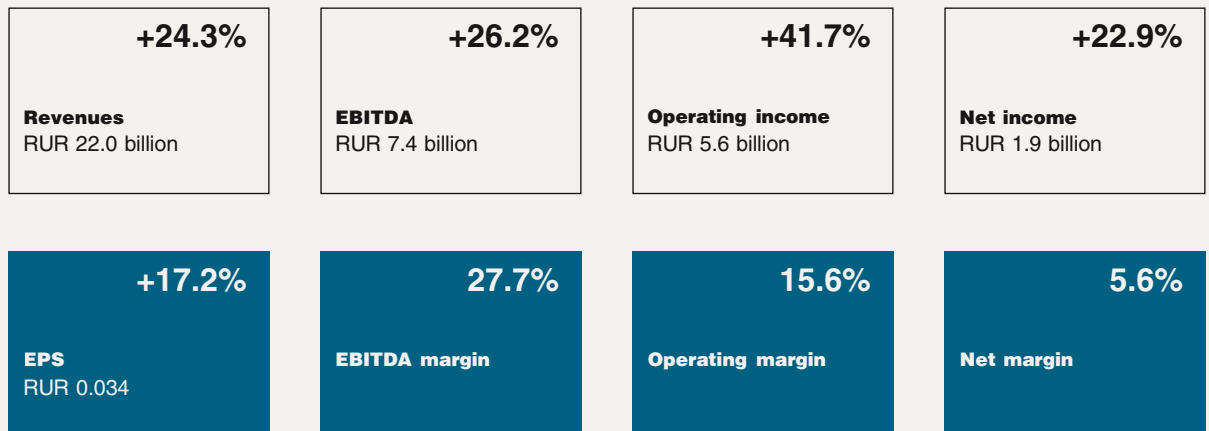
#### Our efficiency results from:

- Meeting telecommunications requirements of our clients;
- Promoting value-added services;
- Reducing costs through introduction of new technologies;
- Optimizing financial services, and improving management information and administration.

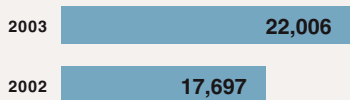
Uralsvyazinform is the leading telecom provider in the Urals Region of Russia. Its key business is local and long-distance communications, GSM mobile telecommunications, value-added telecom services and cable TV. We have been expanding our business through the most advanced technologies, including broadband, multi-service and intelligent networks. While being a universal telecom operator with a sophisticated network, we strive to integrate mobile and fixed telecom as well as Internet services. Our company has 3.2 million subscribers in fixed-line telecommunications and over 1.1 million mobile telecom users.

Uralsvyazinform's strategy is to increase its shareholder value offering high-quality services to individuals and corporate clients.

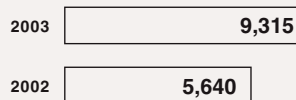
# Key financial results of the year



**Revenues, million RUR**



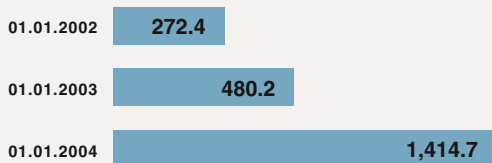
**Capital expenditures, million RUR**



**Net debt, million RUR**

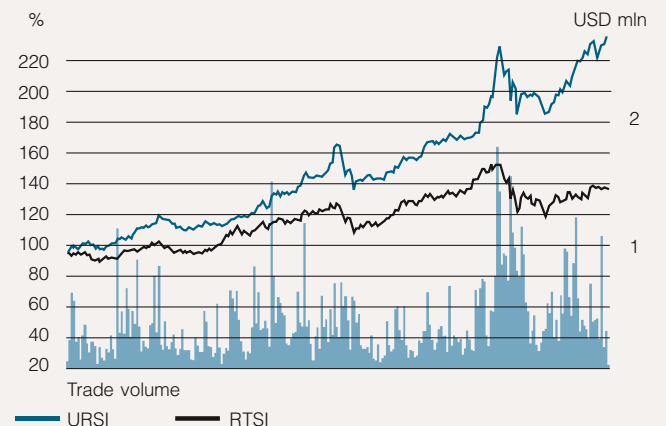


**Capitalization, million US dollars**



Source: RTS

**Price of common stock (URSI) at RTS, million US dollars (January – December 2003)**



Source: RTS, MICEX

# Address by the Chairman of the Board

Leadership, capitalization, mobility  
are the main features of Uralsvyazinform.



## Regions benefited

All regions where the company operates have benefited by the recent merger of the Urals operators. The extent of the Uralsvyazinform capital investments into regional communication systems development (7.7 billion rubles) has increased 1.9 times. In comparison with 2002, the rate of construction for local digital lines has increased 3 times, the expansion rate of the number capacity for the cellular network has increased 2.3 times, and the growth rate of the fixed-line subscriber base has increased 1.3 times.

In 2003 Uralsvyazinform made progress in creating an atmosphere of confidence and cooperation with the Federal regulatory authorities. Five new long-term agreements on cooperation were signed with the administrations and the governments of the Kurgan, Tyumen, Chelyabinsk regions and the Khanty-Mansiisk autonomous region – Yugra.

In cooperation with the government and the local authorities of the Urals Federal district, Uralsvyazinform is making continued progress toward the goals of the federal target program "Electronic Russia", which are to increase quality and openness of regional authorities.

## Shareholders benefited

As a result of the merger, Uralsvyazinform's stock value has increased greatly, which is important for all of the company's shareholders. In comparison with December 2002, during 2003 the capitalization of Uralsvyazinform increased 2.9 times, exceeding \$1.4 billion by the end of the year and \$1.5 billion dollars by the end of the first quarter of 2004. As a result in 2003 Uralsvyazinform took the 4th place among the Russian communication operators in terms of market capitalization (after Mobilnyye TeleSistemy, VypelKom, and Rostelekom). The company also rose up to the 22nd place among the 100 largest Russian publicly-traded companies.

Uralsvyazinform traditionally pays substantial attention to the development of relations with investors, improvement of the corporate management and to the increase of its openness and transparency. During 2003 the company's board of directors considered and approved several documents fundamental to shareholder relations:

- Code of Corporate Conduct;
- Regulation on Dividend Policy;
- Regulation on the Board of Directors' Corporate Governance Committee;
- Regulation on the Board of Directors' Strategic and Investment Planning and Budget Committee;
- Program for the Development of Investor Relations and Secondary Securities Market.

In 2003 the Russian communication industry became one of the leaders responsible for the country's economic growth. Almost all telecommunication sectors were actively developing traditional and especially cellular telephony, local transport systems, new services and Internet connections.

However, against the general positive dynamics in the industry one can distinguish the leaders, and certainly Uralsvyazinform is among them. The company is a leader in both technological development and financial performance. Uralsvyazinform has successfully proved the advantages of creating unified interregional communication operators and of the merging of resources for such development.

Those documents help to define and clarify our company's rules for working with investors in accordance with Russian legislation, and in turn make the company's business clear and transparent for its shareholders and for the investors community as a whole.

It is important to note that since 2001 Standard & Poor's (S&P), the international credit-rating agency, has assigned a corporate governance rating to the company. In 2003 the agency increased that rating from 6.0 to 6.1 on a scale of 10. This is the highest corporate governance rating among the interregional communication companies. When it raised that rating, S&P noted in its report that Uralsvyazinform's management had made efforts to increase the company's market value by improving information disclosure standards and internal control systems.

In 2003 the company's stock was included in two Morgan Stanley global indexes – MSCI Russia and MSCI Telecommunications. This was a recognition of Uralsvyazinform's role and influence in the regional economy as well as the Russian telecom industry. For several years, the company's stock has been included in the RTS (Russian Trade System) index, which tracks the overall economic and investment situation in Russia.

During 2003, the amount of Uralsvyazinform stock converted into level 1 ADRs increased from 6.4% to 11.1% of authorized capital. This points to the increasing interest of foreign investors in the company's securities. The professional investment community noted the efforts that Uralsvyazinform had made to develop relations with its investors and to do business with openness and transparency.

In fact, at the end of 2003, Uralsvyazinform's investor relations program was nominated for an award at *IR Magazine's* annual Investor Relations Awards. The *IR Magazine* awards are highly regarded in the industry as an assessment of best practices.

Due to Uralsvyazinform's positive financial results the company's board of directors recommended that dividend payments would be raised. If management's recommendation is approved at the shareholders' meeting, the total sum of dividend payments in comparison with 2002 will increase 2.3 times – from 198.6 million rubles to 467.8 million rubles (growing from 21.8% to 25.2% of net profit).

### Customers benefited

The company's customers should enjoy the advantages of the merger in full measure. Extended new number capacity helped to solve the problem of setting up telephone service for Urals region residents. The company is determined to keep up the pace it has achieved in solving this important problem. Besides, while implementing the most advanced equipment and technologies, the company is improving the quality of its services and extending their range. Now the company provides its customers the most advanced telecommunication services, which leads to greater business activity and higher living standards. Among the company's near plans are the active advancement of cable television, transition to digital broadcasting and the launch of service packages which include cable television, ADSL access to the Internet and video on demand.

I would like to thank all customers, shareholders, partners and staff of Uralsvyazinform for their fruitful cooperation. The dynamic development and the high intellectual potential open new business possibilities and profit growth opportunities for the company. I am sure Uralsvyazinform will continue to improve its performance for the benefit of shareholders, customers and the region.



Vadim Belov

# Statement by the General Director

**A step towards the future of  
infocommunication infrastructures:  
higher business quality and higher living  
standards.**



The results of the company's work in 2003 validate the strategy of Russian telecommunication reform. The concentration of intellectual and financial resources has raised the country's economic development rate, improved the company's position in the market, raised its productivity and significantly increased its capitalization and dividend payments to shareholders. The company follows with confidence the path of integration into the global information community of the third millennium. In 2003 important steps were taken to create the base of telecommunication infrastructure required for future challenges, including, first of all, the avalanche-like growth of traffic and increase in demand for broadband services.

## Finances

In 2003 the revenues of Uralsvyazinform increased in 24.3% – up to 22.0 billion rubles in comparison with the previous year. Expense control and the growth of highly profitable services led to EBITDA growth of 26.2% – to 6.1 billion rubles – and to net profit growth of 22.9% – to 1.2 billion rubles.

## Technological progress

In 2003 the company extended its investment in communication systems development by 44% – up to 7.7 billion rubles. Three thousand two-hundred kilometers of the fiber-optic and 1.3 km of the digital microwave local communication lines were put into operation. At the same time outmoded analogues and air lines were put out of operation. The new lines improve connection quality and reduce the deficit of long-distance channels. Moreover, they are designed to transmit significantly larger traffic capacities, which marks a good start for the further development.

During the year 369,900 numbers for fixed communication lines were put into operation. At the same time 126,100 numbers switched by ten-step and coordinated exchanges were put out of operation. The installed capacity reached 3.6 million numbers, while the equipped capacity reached 3.2 million numbers. The digitalization increased by 6.1% – up to 61% of total numbers.

Two hundred thirty-one thousand six hundred requests for telephone installation were honored, while the number of the pending requests accounted for 441,800 (99,600 of them were fulfilled in 2003). As of December 31, 2003, the rate of telephone connection supply was 20.9 phones per 100 residents in comparison to 19.3 in 2002.

In 2003 Uralsvyazinform achieved significant results in business development. It was the first full year the company was operating as the unified interregional telecommunication operator of the Urals region.

We have generally completed the formation of our managerial staff and the optimization of our management system. We have learned to live as one business body.

## Securities

In 2003 the positive results of the Uralsvyazinform work led to significant growth in the company's market capitalization. During that year the capitalization increased 195% – from \$480.2 million to \$1.41 billion. Therefore, the company's shares rose at a greater rate than the market as a whole. (The RTS index increased by 57% in 2003.)

The raising of long-term credit ratings by Standard & Poor's (to "B" with a positive outlook) and Fitch (to "B+" with a positive outlook) contributed significantly to the company's market capitalization growth. In March 2004 Fitch again reviewed the credit rating of Uralsvyazinform and raised it to "BB-" with a stable outlook. In July 2003, Uralsvyazinform successfully issued bonds worth 3 billion rubles with a three-year maturity and an annual coupon rate of 14.25% per annum.

## Cellular communication

In 2003 Uralsvyazinform together with its subsidiaries retained leading positions in the cellular communication market in the Urals region. During the year the total amount of customers increased in 2.5 times – from 445,000 to 1,155,000 – 90% of which represent the GSM 900 customer standard.

Last fall Uralsvyazinform rose to fourth place on the list of the Russian cellular operators measured by number of customers, and since then the company has maintained this position confidently. At the same time, according to the company's first quarter 2004 results, the number of customers increased to 1,400 thousand.

The company's investment in cellular communication networks development accounted for 1.1 billion rubles. The capacity of the cellular communication networks of GSM 900/1800 standard was raised by 629,000 numbers. One hundred sixty-four new base stations were put into operation in order to extend the coverage zone and to increase the capacity. During the year the preliminary work was carried out in order to consolidate the cellular business and to extend the license territory. In cooperation with Volgatelecom the company acquired 83.4% of the shares of Tatiikom-T (GSM 900 Tatarstan operator). As a result Uralsvyazinform now owns 33.4% of Tatiikom-T.

In December 2003 Uralsvyazinform received a license to offer GSM 900/1800-standard cellular communication services in the Sverdlovsk region. This event was of special importance because Sverdlovsk was the only region where the company had operated without license coverage.

## Cooperation with authorities

In 2003 Uralsvyazinform paid much attention to the development and the systematization of its cooperation both with the federal authorities and with the regional government bodies. Five new agreements on cooperation were signed with the regional administrations. In cooperation with the office of the Plenipotentiary Representative of the Russian Federation President in the Urals Federal District, with the Federal subjects' administrations and with the local authorities, the company has continued to work toward the goals of the federal target program "Electronic Russia." The total number of state institutes, government bodies and local authorities connected to Internet by the company significantly increased. The company designs and constructs private (internal) networks for large state institutions, for example, for the taxation authorities.

## Social policies

The company traditionally has paid priority attention to the realization of social policies. In June 2003, for the first time, the unified collective agreement was signed. The agreement regulates in detail the social guarantees provided to the staff. In comparison with 2002, the wages and other benefits grew 29% in 2003, exceeding 6.3 billion rubles, while the average monthly salary in the company grew to 10,252 rubles. The collective agreement's payments, including the workers' voluntary medical insurance and non-governmental retirement insurance, rose to 567 million rubles. Following the principles of the social responsibility of business, Uralsvyazinform donated 40.4 million rubles to charitable purposes in 2003.

## Outlooks

For 2004 Uralsvyazinform has set ambitious tasks. However, the company's dynamic development, its intellectual potential and investment capabilities allow us to claim that the plans will be realized. Total investment in 2004 for the company's development is planned at 8.5 billion rubles.

### The following major projects are planned for 2004:

- Extension of the fixed communication network capability. The automatic telephone system for 323,000 numbers is planned to be set into operation;
- Extension of the coverage zone and of the capability of cellular communication networks of GSM 900/1800 standard. Among the plans are the installation of the switchboards for 1,420,000 numbers and 562 base stations, the extension of rendering of GRPS, MMS, IN Comverse services through the whole territory the company operates;
- Commencement of commercial operation for the GSM 900/1800-standard cellular communication network in the Sverdlovsk Region during the fourth quarter of 2004;
- Consolidation of the Uralsvyazinform cellular business and implementation of a common trademark for the company's cellular business;
- Construction of 4,246 km of the local long-distance fiber-optic and radio microwave communication lines;
- Extension of intellectual network services to all regions where Uralsvyazinform operates;
- Establishment of an experimental zone for the new generation network (NGN) in Ekaterinburg;
- Continuation of Oracle E-Business Suite implementation works;
- Extension of rendering of cable television services.

Uralsvyazinform faces the future with confidence and optimism. The company is determined to maintain its high development rates and to seek continued improvement in its business cost efficiency. I am sure that the positions of Uralsvyazinform in the market of fixed and mobile communications not only will be kept up, but also will be improved. We are prepared for the future challenges and determined to offer to our customers the most optimal path of integration into the global information community. Uralsvyazinform right now offers the future of telecommunications, allowing the business sector to rise to a new stage of the development and raising our residential customers' living standards.



Vladimir Rybakin

# Company Profile

Uralsvyazinform is a universal telecom provider with an integrated business of fixed-line, mobile and Internet telecommunications.



## Uralsvyazinform – key facts:

- the leading telecom provider in the Urals Region;
- total installed capacity of 4.8 million numbers, including 1.2 million in the mobile telecom networks;
- there are 3.2 million fixed-line subscribers; and 1.1 million subscribers for GSM services, including those of subsidiaries;
- 36 thousand employees.

Uralsvyazinform is the leader on the Urals telecom market, with a regional market share of more than a 64% (in revenue terms). In 2003 the company generated 22.0 billion rubles in revenues (+ 24.3% compared to 2002).

## Uralsvyazinform offers the following services to individuals and enterprises:

- long-distance and international telephone communications;
- local telephony;
- mobile telecommunications in GSM 900/1800, NMT 450 and DAMPS800 standards;
- Wireless local loop in CDMA (IS-95) and DECT;
- Internet access;
- Intelligent network services;
- Cable television;
- Air TV broadcasting and wired radio;
- Telegraph and fax services.

## The region of Uralsvyazinform activities

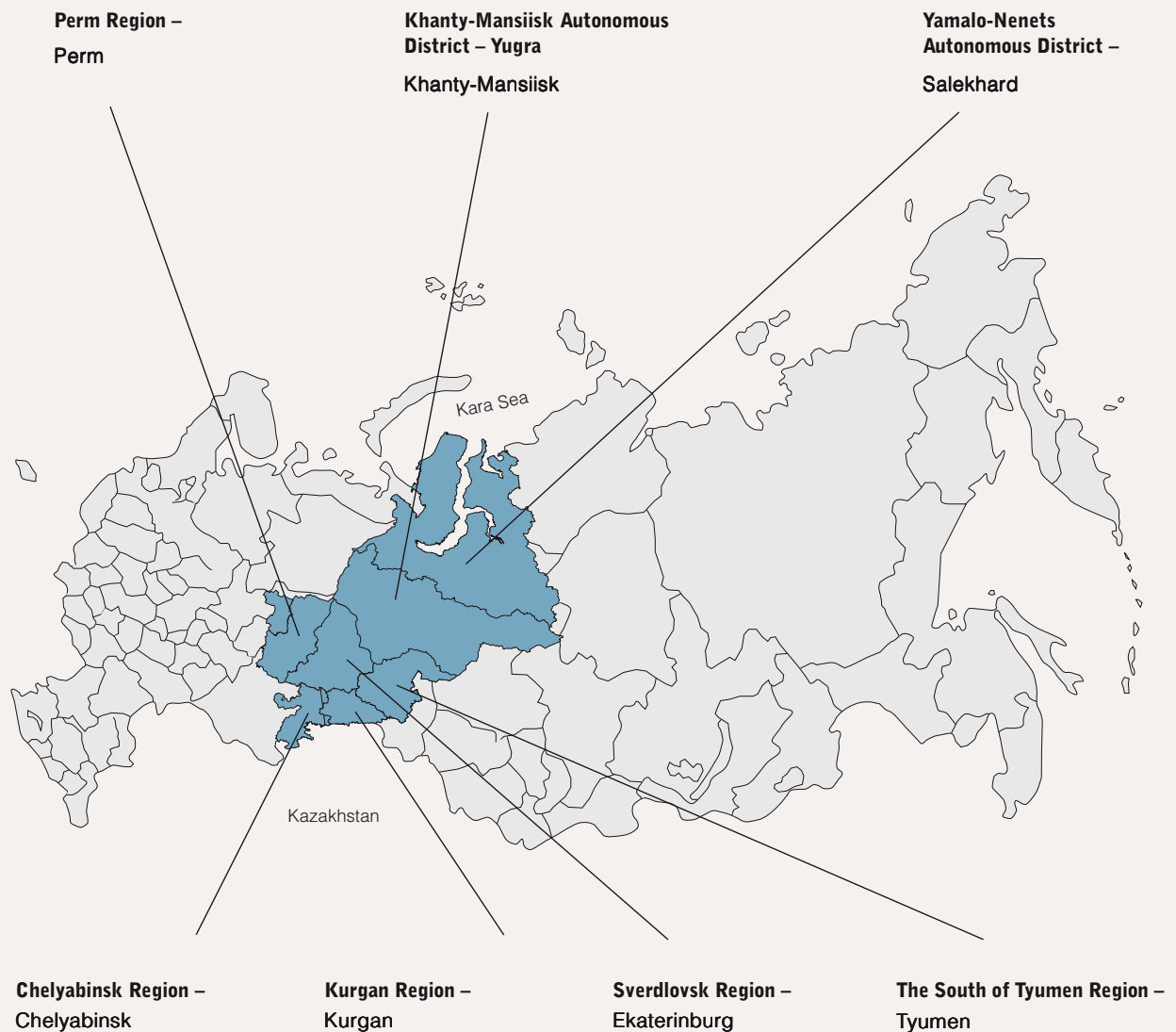
### Description

Territory – 1.9 mln sq. kilometers  
Population – 15.5 mln inhabitants  
(9% of total Russia's population)  
Urban population – 80%

### Economy

Industrial output in 2002 –  
USD 39.4 bln (18% of total  
Russian industrial output)  
Oil (6% of the world reserves/  
65% of Russia's reserves)  
Gas (26% of the world reserves/  
95% of Russia's reserves)  
Ironstone (21%) and copper ore  
(9%), copper, gold, silver,  
diamonds

Source: Goskomstat of Russia



From an economic standpoint, the Company is operating in the Urals, which is one of the fastest-growing regional markets. Moreover, the telecommunications sector within this region is the second fastest growing market in Russia, overall. The company has strong positions in the traditional telephony sector as well as in the mobile and value-added services markets. Uralsvyazinform accounts for 6% of the overall Russian telecom sector's income.

As the owner of the backbone telecom infrastructure in the region as well as the largest sales network, Uralsvyazinform benefits from its priority access to users and the largest customer base in the region. As of December 31, 2003, it had 3.164 million fixed telephony subscribers.

In May 2003 Uralsvyazinform together with its subsidiaries, was ranked fourth among cellular operators in Russia in terms of the number of subscribers. As of December 31, 2003, it offered its mobile telecom services to 1.144 million subscribers (a gain of 700,000 subscribers over 2003).

The company has operations in all regions of the Urals Federal District, namely, in Kurgan, Sverdlovsk, Chelyabinsk and Tyumen, and in the Khanty-Mansiisk – Ugra and Yamal-Nenets autonomous districts, and additionally in the Perm Region and in the Komi-Perm autonomous district that are part of the Volga Federal District.

The Urals has one fifth of the total industrial output in Russia.

In 2003 the Urals Federal District experienced an increasing rate of economic growth. Macroeconomic conditions showed persistent growth of output across the economy. Industrial production in the federal district retained its high and sustainable growth rates. At the year's end, the volume of industrial output was 9.5% more than in 2002 (compared to an increase of 6.8% in 2002 over 2001), while Russia's average was 7%.

Investment in fixed assets in 2003 increased 8%, compared to a decline of 4.3% in the previous year. The total investment in fixed capital from all funding sources exceeded 350 billion rubles in 2003. Foreign investments in the region grew at higher pace. In 2003 foreign investments increased 56% on the year, reaching \$3.7 billion.

The persistent positive growth of investments in the real sector underscores confidence in the future growth of industrial output. An important 2003 result was the growth in public income and the improvement in average living standards. The Urals has retained its leading position among federal districts in terms of per capita cash income.

**Average nominal stated monthly wages  
December 2003, RUR**

<b>Average Russia</b>	<b>5508,6</b>
<b>Urals</b>	<b>8177,8</b>
<b>Moscow</b>	<b>8156,5</b>
<b>Far Eastern Russia</b>	<b>7642,0</b>
<b>North-West</b>	<b>6332,8</b>
<b>Central Russia</b>	<b>5732,2</b>
<b>Siberia</b>	<b>5314,1</b>
<b>Volga</b>	<b>4244,1</b>
<b>Southern Russia</b>	<b>3780,0</b>

Source: Goskomstat

Over the past decade, the Khanty-Mansiisk and Yamal-Nenets autonomous districts, together with the Sverdlovsk Region, have been among the donor regions in the Russian Federation, claiming no budget equalization subsidies from the federal budget. Over the years, the list of donor regions also has featured the Perm, Chelyabinsk and Tyumen regions.

Going forward, the area is expected to become one of the leaders in the implementation of science-intensive technologies and the development of advanced technologies. For that, it has such prerequisites as the largest scientific and R&D potential, highly qualified human resources, and a huge stock of advanced technologies available from research centers and defense projects. The Urals will retain its role as one of the key producers (and exporters) of oil and gas, ferrous and non-ferrous metals, and engineering products.

# Key events in 2003

First steps made by the merged company

02-03	04	05-06
<p><b>February</b></p> <ul style="list-style-type: none"> <li>■ A Cooperation Agreement is signed between Uralsvyazinform and the Administration of the Kurgan Region.</li> <li>■ A Cooperation Agreement is signed between Uralsvyazinform and the Administration of the Chelyabinsk Region.</li> </ul> <p><b>March</b></p> <ul style="list-style-type: none"> <li>■ In the city of Kurgan, transition to six-digit telephone numbers is completed.</li> <li>■ In the city of Khanty-Mansiisk, the MMDS aerial and cable TV broadcasting system is commissioned, offering 21 broadcast channels.</li> </ul>	<p><b>April</b></p> <ul style="list-style-type: none"> <li>■ Standard &amp; Poor's Rating Agency raises its long-term credit rating of Uralsvyazinform from "B-" to "B", with a stable outlook.</li> <li>■ The Tariff Policies Concept Paper, prepared by the company for 2003, is endorsed by the RF Ministry for Anti-Monopoly Policies and Entrepreneurship Support.</li> </ul> <p>Under the proposed concept, the key objective in the company's 2003 tariff policies is to phase out cross-subsidization through a package of changes in the tariffs for local and long-distance telephony.</p>	<p><b>May</b></p> <ul style="list-style-type: none"> <li>■ Fitch Ratings raises its long-term credit rating of Uralsvyazinform from "B" to "B+", with a positive outlook.</li> <li>■ Ordinary shares in the company have been included in the MSCI Russia and MSCI Telecommunications global indices starting May 30, 2003; These Morgan Stanley indices offer guidance to many foreign investors. As a result, the company has become a visible target for investments, boosting valuation of its shares.</li> </ul> <p><b>June</b></p> <ul style="list-style-type: none"> <li>■ Uralsvyazinform holds its Annual General Shareholders Meeting. The AGM approves payment of dividends for 2002; elects its new Board of Directors and Audit Committee, and appoints the company's auditor for 2003.</li> <li>■ Cooperation Agreements are signed between Uralsvyazinform and the Administration of the Tyumen Region.</li> </ul>

\*Standard & Poor's: "The newly merged company <...> will have added benefits from the increased scope of its business, including access to better terms and conditions from the telecommunications vendors."

\*\* Fitch Ratings: "Uralsvyazinform remains one of the more innovative and advanced of the seven newly merged regional operators <...>. The agency expects the company's operational cash flow to increase going forward due to the economic growth and economic effects of the merger."

07

08-09

11-12

### July

- Uralsvyazinform launches its ruble bonds on the MICEX. The 3 billion ruble offering has a maturity of 3 years, and an annual coupon yield of 14.25% .
- Standard & Poor's raises its corporate governance rating of Uralsvyazinform to 6.1 (on a 10 point scale).
- Uralsvyazinform and the Government of the Khanty-Mansiisk – Ugra autonomous district sign a Cooperation Agreement for promote development of rural telecommunications in 2003–2006.

### August

- Pursuant to the resolution of the Ministry for Anti-Monopoly Policies and Entrepreneurship Support, a new system is approved starting August 1, 2003 for a long-distance traffic settlement with Rostelecom, the national long-distance operator. The new inter-operator settlement procedure has enabled a transparent system of direct payments between Rostelecom and Uralsvyazinform both for handling traffic in Rostelecom networks and for traffic termination services in the Uralsvyazinform network. The new inter-operator settlements have improved transparency and accuracy of settlements between operators.

### September

- Capitalization of the company exceeds \$1 billion.
- Uralsvyazinform, together with Volgatelecom, acquires 83.4% interest in the Kazan-based cellular operator Tatinkom-T.
- Uralsvyazinform becomes number four in the rating of top cellular operators in Russia by the number of subscribers.

### November

- In the GSM 900/1800 network, Comverse, a new intelligent platform, is put into operation, allowing the company to offer its clients real-time billing and a wide range of additional services.

### December

- A millionth subscriber is registered in the Uralsvyazinform GSM.
- The RF Telecom and IT Ministry issues Uralsvyazinform a license for the 900/1800 MHz cellular radiotelephony services in the city of Yekaterinburg and in the Sverdlovsk Region. As a result, the licensed zone of the company and its subsidiaries now covers the entire Urals Federal District and the Perm Region.

\*\*\*Standard & Poor's: "We believe that the level of corporate governance practices at Uralsvyazinform is one of the highest among Russian fixed telecom operators. We also note the active position of the Uralsvyazinform management upholding interests of the company and its shareholders".

# Shareholding Capital Structure

Since reorganization – September 30, 2002 – the number of ordinary and preference shares deposited for ADRs has doubled, while the share of ADR holders in the shareholding structure has increased from 6% to 11%.

## Shareholders owning more than 1% of shares in the JSC Uralsvyazinform Charter Capital as at 31 December 2003

Company/Person	Type	Number of common shares	
		Shares	% of common shares
Svyazinvest	Owner / Legal entity	16,608,946,183	51.42%
ING Bank Eurasia ZAO	Nominal holder / Legal entity	4,846,341,682	15.00%
ZAO Depository Clearing Company	Nominal holder / Legal entity	1,480,886,622	4.58%
Russian Federal Property Fund	Owner / Legal entity	1,861,389,451	5.76%
JPMorgan Bank International	Nominal holder / Legal entity	865,090,810	2.68%
National Depository Center	Nominal holder / Legal entity	955,792,164	2.96%
ABN AMRO Bank	Nominal holder / Legal entity	160,800,756	0.50%
Brunswick UBS Warburg Nominees	Nominal holder / Legal entity	42,904,527	0.13%
Vladimir Rybakin	Owner / Individual	414,787,558	1.28%

#### Shareholding Capital Structure

Authorized capital	<b>RUR 4.8 billion</b>
Number of shares	<b>40,134,723,306</b>
including:	
ordinary shares	<b>32,298,782,020 (80.5%)</b>
preference shares	<b>7,835,941,286 (19.5%)</b>
Par value	<b>0.12 ruble</b>

#### Shareholders as of December 31, 2003:

Svyazinvest	<b>41.4% (51.4%) *</b>
Individuals	<b>8.8% (6.5%)</b>
Management	<b>6.0% (5.4%)</b>
State's share	<b>4.7% (5.8%)</b>
ADRs	<b>11.1% (11.0%)</b>
Corporate entities	<b>28.0% (19.9%)</b>

\* share of ordinary stock

According to the company, as of December 31, 2003, it had a free float of 35% to 40% shares on the market.

#### Number of preferred shares

Shares	% of preferred shares	% in charter capital
0	0.00%	41.38%
1,577,448,769	20.13%	16.01%
1,107,531,943	14.13%	6.45%
0	0.00%	4.64%
171,167,818	2.18%	2.58%
211,088,351	2.69%	2.91%
476,128,569	6.08%	1.59%
818,948,564	10.45%	2.15%
0	0.00%	1.03%

# Board of Directors and Management

## Board of Directors of Uralsvyazinform

### Chairman:

**Vadim Belov:** In 1998 and 1999, he was Managing Director in the Moscow Office of Capital Limited. Since 1999 he has been Deputy General Manager at Svyazinvest.

**Vladimir Adzhalov:** In 1996 and 1997 he was General Manager of the privately held company RoSprint. Between 1997 and 1999 he was General Manager at Global One Network. From 1999 to 2001 he was a Vice President at Global One Communications Limited. Since 2000 he has worked with Rostelecom as an advisor to the General Manager.

**Yuri Bilibin:** In 1998 and 1999, he was Deputy Director for Commerce and head of the Investment and Foreign Relations Department at the Petersburg Telephone Network. Since 1999 he has been working as an assistant to the General Manager at Svyazinvest.

**Alla Grigorieva:** Between 1998 and 2000 she was Deputy Head of the Svyazinvest Shares Management Department; since 2000 she has been working as Deputy Director of the Corporate Governance Department at Svyazinvest.

**Vladimir Zholobov:** Since 1998 he has been a leading specialist in the Corporate Governance Department at Svyazinvest.

**Vladimir Kozin:** From 1998 to 2003 he was Deputy Director of the Corporate Finance and Direct Investment Department at Svyazinvest. Currently he is Director of the Department of Direct Investments and Property at Svyazinvest.

**Dmitri Levkovsky:** Since 1995 he has been working as Vice President of the Moscow office of NCH Advisors, Inc.

**Leonid Perminov:** From 1998 to 2002, he headed a department at Gossvyaznadzor in the Perm Region, and he retired in 2002.

**Vladimir Rybakin:** Since 1994 he has been General Manager of Uralsvyazinform.

**Sergei Chernogorodsky:** Between 1997 and 1999 he was an analyst at IFC Optimum-Finance; in 1999 he joined Svyazinvest to work as a leading specialist at its Securities Department. In 1999 and 2000 he was promoted to Chief Specialist in the Securities Department, and in 2000 and 2001 he headed the Investor Relations Department at Svyazinvest. In 2002 and 2003 his position at Svyazinvest was Deputy Manager of the Securities Department; then he was promoted to become the Manager of the Shareholders Capital Department.

**Sergei Yurpalov:** Between 1998 and 2001 he was Deputy Director at the Institute of Economics of the Urals Division of the Russian Academy of Sciences. In 2001 and 2002, he worked as chief advisor to the Office of the Presidential Representative in the Urals Federal District (UFD). Since 2002 he has headed the Finance and Economics Department at the Office of the Presidential Representative in the UFD.

## Management Board of Uralsvyazinform

Chairman:

**Vladimir Rybakin:** Since 1994 he has been General Manager of Uralsvyazinform.

**Sergei Akimenko:** Between 1996 and 2002 he was Deputy General Manager for Legal Affairs and Head Legal Counsel at Chelyabinskvyazinform. Since 2002 he has been Head Legal Counsel at Uralsvyazinform.

**Andrei Belobokov:** In 1998 and 1999, he was First Deputy Governor of Agroprombank. In 1999 and 2000, he headed a department at SBS-Agro. In 2000 he was General Manager at INANKOcentr, as well as advisor to the General Manager of Uralsvyazinform, Deputy General Manager, and head of the Strategic Planning Department of Uralsvyazinform. Since 2002 he has been Deputy General Manager and Commercial Manager of Uralsvyazinform.

**Valery Kashin:** Between 1994 and 2002 he was General Manager at Yamalelekrosvyaz. Since 2002 he has been Deputy General Manager, and Manager of the Yamal branch of Uralsvyazinform.

**Sergei Kuzyaev:** In 1998 he was appointed financial manager and head of the receivables management team at Uralsvyazinform. Between 2000 and 2002 he was Deputy General Manager for Economics and Finance at Uralsvyazinform. Since 2002 he is Deputy General Manager, and the company's CFO.

**Eduard Lebedev:** Between 1993 and 2002 he was General Manager of KhantyMansiiskokrtelkom. Since 2002 he has been Deputy General Manager and Manager of the Khanty-Mansiisk telecom branch of Uralsvyazinform.

**Vladimir Lokhtin:** Since 1999 he has been Manager of the Telecommunications Department at Svyazinvest.

**Lidia Onuchina:** Since 1994 he has been Chief Accountant of Uralsvyazinform.

**Oleg Orlov:** Between 1994 and 2000 he was Manager of Telekomservice. Between 2000 and 2002 he was Deputy General Manager for Capital Construction at Uralsvyazinform. In 2002, he was Uralsvyazinform Manager for Technical and Innovative Policies. Since 2003 he has been Deputy General Manager, and Manager for Technical and Innovative Policies at Uralsvyazinform.

**Dmitry Samoilov:** Between 1997 and 2000 he was Manager of Zebra (Swiss-Russian joint stock company E.K.S. International). In 2000 and 2002 he was Deputy Governor of the Perm Region. In 2002 and 2003 he was appointed Deputy Manager of the Strategic Planning Department and Acting Manager of the Department of Property and Non-Productive Capital Investments at Uralsvyazinform. In 2003 he was appointed Deputy General Manager, and Business Development and Corporate Governance Manager at Uralsvyazinform.

**Viktor Sanachev:** Between 1985 and 1998, he was manager of the Solikamsk Regional Communications Center of the Perm Production and Technical Communications Authority. Between 1998 and 2003 he was First Deputy General Manager and Executive Director at Uralsvyazinform. Since 2003 he is Deputy General Manager and Manager of the Perm Telecommunications branch of Uralsvyazinform.

**Nikolai Sarayev:** Between 1995 and 2002, he was First Deputy General Manager for Technical Issues at Tyumentelecom. Since 2002 he has worked at the Tyumen Telecommunications branch of Uralsvyazinform as its Deputy General Manager and technical director; later in the same year he was promoted to Deputy General Manager and Manager of the Tyumen branch of Uralsvyazinform.

**Vitaly Stoyanov:** Between 1992 and 2002, he was Deputy General Manager of Chelyabinskvyazinform, and Chief Engineer of Poly-Art Commercial Center at the branch of Chelyabinskvyazinform. Since 2002, he has been Deputy General Manager and Manager of the Chelyabinsk branch of Uralsvyazinform.

**Anatoly Ufimkin:** Between 1993 and 2002 he was general manager of the Chelyabinsk Region's Svyazinform. Since 2002 he is first Deputy General Manager of Uralsvyazinform.

**Yuri Shabalin:** In 1995 and 1996, he headed the Telecommunications Department at Electrosvyaz in the Kurgan Region. Between 1996 and 2002, he was Electrosvyaz General Manager. Since 2002 he is Deputy General Manager, and heads the Kurgan branch of Uralsvyazinform.

# Overview of business in 2003

In 2003 Uralsvyazinform strengthened its leadership position on the Urals telecommunications market. Expansion in the market share of the Uralsvyazinform key business segments proved the effectiveness of the company's strategy and its efficient implementation.

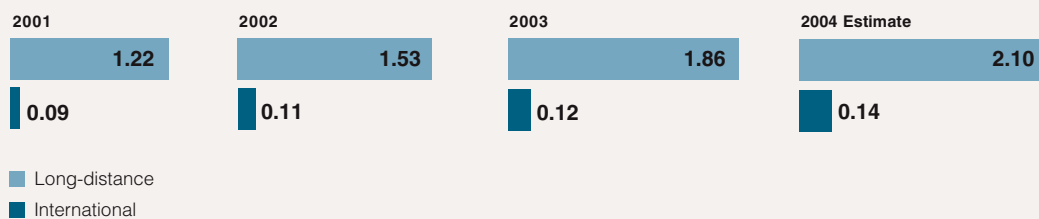
Financial results continued to improve in line with the growing long-distance traffic, bigger fixed and mobile customer base, higher fixed-line tariffs, and improving demand for new services. In 2004, the company expects that its efficiency will continue to improve, together with revenues, cost control and investment in advanced technologies.



# Domestic long-distance/ international long-distance telephony

**As it develops digital transport networks, the company seeks to lay down a strong information and communications infrastructure that can meet the needs of all its potential clients in quality telecommunications and access to information resources.**

Outgoing long-distance/international traffic (billions of minutes)



Currently a major share of company's revenues is coming from long-distance and international traffic. Hence growing long-distance traffic is an important income driver for Uralsvyazinform. In 2003, long-distance and international long-distance traffic grew 21.6% and 13.0%, respectively. The company expects to see long-distance traffic continuing its growth into 2004.

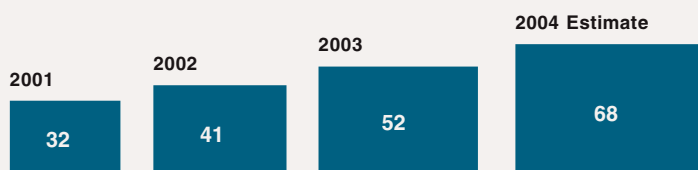
## Building a digital transport network

In its long-distance service, Uralsvyazinform has relied on its own transport network, and leased channels from the long-distance operator Roselecom and other operators.

Developing proprietary infrastructure for transport networks is deemed to be one of the key priorities of technical advancement. In the intra-zonal primary network of its branches Uralsvyazinform continued to build fiber-optic lines and digital radio relay lines (DRRL), and phase in digital SDH STM4/16 bandwidth transmission systems. At the same time, older obsolete analog systems and aerial lines of communication are being decommissioned gradually.

Over the year, the company has built and commissioned 4,455,000 km of intra-zonal transmission lines, of which digital RRL and fiber-optic lines account for 1,299,000 and 3,156,000 km, respectively.

Digitalization of intra-zonal lines of communication (%)



	2002	2003	2004
	availability	actual	estimate
Intra-zonal fiber-optic lines, thous.km	2.9	+3.2	+3.2
Intra-zonal DRRL, thous.km	2.1	+1.3	+1.0

The commissioned digital lines have launched a sustained effort to eliminate the effective shortage of channels inside the zones, and to significantly improve the quality of traditional and value-added services offered to users. In the near future, the company expects to avoid leasing resources from other operators, reduce operational costs, and implement new technologies and telecommunications services.

### Expanding automatic long-distance exchanges

The growing long-distance traffic, helped by the improvements in intra-zonal lines, higher subscriber incomes, and lower long-distance tariffs required significant expansion in long-distance exchange productivity. In 2003 the company increased installed capacities, expanding its auto-matic long-distance exchanges at the Yekaterinburg, Kurgan, Chelyabinsk and Yamal-Nenets branches, and commissioning a new long-distance exchange at the Khanty-Mansiisk branch.

The company added 4,488 new outbound channels, of which 2,208 are in the zonal telecommunications. The total installed capacity of automatic long-distance exchanges at Uralsvyazinform was 68,252 channels. The used capacity of long-distance exchanges across the company was 65.7%, of which the used capacity in the zonal communications was 71.9%.

In 2004 plans to meet the growing demand for long-distance services provide for further expansion of the capacity at automatic long-distance exchanges. These are the plans to install a second exchange in the city of Yekaterinburg with a capacity of 12,000 channels; to upgrade the Tyumen exchange, adding significantly (up to 17,000 channels) to its capacity, and to commission a new 6,000-channel automatic exchange in the city of Noyabrsk.

# Local telephony



**Newly implemented technologies give regional communities access to modern telecommunications services, and meet corporate and individual user demand for new broadband services.**

Together with the expanding local fixed-line networks to accommodate the growing subscription base, the company continued to upgrade the existing obsolete networks with modern technologies, thus expanding the range of new services offered. The emphasis in this sector is on the construction of optic networks offering high-speed subscriber lines.

Newly commissioned capacity in the fixed telecommunications networks allowed the company to make 380,200 new numbers available. The expansion was made possible thanks to the upgrading of the existing and construction of new digital exchanges, construction and expansion of tandem switches and optical access networks, and commissioning of wireless local loops. The company decommissioned antiquated ten-step switches and coordinated automatic exchanges with an overall capacity of 126,100 numbers.

The installed capacity totaled 3.6 million numbers, and the utilized capacity 3.2 million numbers. The capacity utilization factor is 88.9%.

Overall, the local telephony at Uralsvyazinform had 3,164,000 subscribers as of January 1, 2004 (representing an increase of 7.2%, or 212,000 users, achieved in 2003).

Uralsvyazinform has a high level of digitalization in its local networks, allowing the company to offer high value-added services. Digital exchanges accounted for 61.5% of installed capacity in late 2003 and were projected to reach 72.1% in late 2004.

By the end of the year the telephone availability index across the territory of five regions and two autonomous districts (less mobile telephony) stood at 20.9 telephones per 100 residents. There still is a big number of registered applications requiring public network access: the backlog is 441,800 applications as of January 1, 2004, of which 99,600 were submitted in 2003. Over the reported period, 231,600 applications were satisfied. New applications come mostly from communities that had few installed telephones in the past, but now are taking advantage of the commissioning and expansion of local capacities.

Implementation of new equipment and modern technologies, and improved administration, labor organization and cost management, together with a re-balancing of tariffs, helped the company to improve its performance in 2003.

	2001	2002	2003	2004
	availability	actual	actual	estimate
Capacity by numbers (thousands)	3,112	+204	+380	+323
Fixed-line subscribers (thousands)	2,788	+164	+212	+201

## Efficiency indicators

Efficiency measures	Units	2002	2003	growth y-o-y, %
Revenues per line	rubles	4,944	5,866	118.65
Operating profit per line	rubles	1,291	1,668	129.22
Lines per employee	lines	78.9	90.2	114.29

In 2004 the company intends to commission 323,000 numbers of new-user capacity in the fixed-access networks. This expansion will come mostly from optic access networks.

Because of the active expansion of utilized capacities, the biggest city exchanges in the region – in Yekaterinburg, Perm and Chelyabinsk – had to introduce a seven-digit numbering system. This transition was effectively completed at the Yekaterinburg city exchange in the first quarter of 2004; seven-digit numbering will be introduced to city exchanges in Chelyabinsk and Perm in the course of 2004–2005, this completing the decommissioning of ten-step exchanges.

The large number of fiber-optic lines and digital RRL commissioned over 2003 will contribute significantly to the data transmission infrastructure. As a result, the availability of data transmission services in smaller towns and regional centers will be comparable to that of major cities in the region.

The 2004 construction of the regional multi-service network will help promote a significant increase in the number of corporate clients in the region. In parallel with the construction of the data transmission infrastructure, the company is starting to introduce NGN technologies. In 2004 a test zone was set up in the city of Yekaterinburg to refine "three in one" technologies – telephony, data and video transmission through a single network hub – and to offer totally new IP-Centrex services to corporate users.

## Wireless local loop

The wireless local loop systems have been used by the company effectively and efficiently to offer telephony services to private homes in suburbs (cottage villages) or rural townships where laying telephone cables is economically unfeasible.

### There are two types of wireless local loop used by the company:

CDMA (IS-95) – rolled out by two branches:

- In the Tyumen Region, the local loop consists of an LG (Korea) switch for 5,000 numbers, 4 base stations, and 4,268 subscribers as of December 31, 2003. The user number capacity was increased by 1,048 subscribers in 2003.

- In the Chelyabinsk Region, the installed capacity of the network was expanded by 16,000 numbers during the year. By December 31, 2003, the network consisted of a switch for 58,500 numbers from Qualcomm (USA) and 33 base stations, with 47,150 users. In 2003 the company's user number capacity was increased by 10,505 subscribers (28.5%).

Four branches have deployed DECT wireless local loops:

- At the Perm branch, DECTLink Compact by Siemens offers a capacity of 960 subscribers; the current number of users is 586.

- At the Khanty-Mansiisk branch, in 2003 the installed capacity of the MiniKOM DECTL WLL from Informtekhnik was expanded by 1,000 numbers to 2,000 subscribers during 2003; the current number of users is 1,805.

- At the Kurgan branch, the DECT wireless local loop was expanded in 2003 with the commissioning of another 26,000 numbers capacity by Italtel. The network has the overall installed capacity of 26,250 numbers. The current number of subscribers in the network is 7,866.

- The Chelyabinsk branch commissioned a Goodwin-Borodino network in 2003, with 16 base stations in the cities of Magnitogorsk and Plast.

The number of the total number of wireless local loop users is 62,010, of which:

- IS-95 has 51,418 subscribers; and
- DECT has 10,592 subscribers.



# Mobile telecommunications

**A successful mobile business has transformed the company into one of the leading mobile operators in Russia. Uralsvyazinform (proprietary telecom services in GSM 900/1800 and NMT 450i standards) and its five subsidiaries (Ermak RMS; South-Urals Cellular Phone; TyumenRuscom; UralVestkom; and Kurgan Cellular Phone) have over 1,200 users. This is the fourth biggest telecom customer base in the country. Since 2003 Uralsvyazinform's number of mobile phone users has doubled.**

Uralsvyazinform has become the fourth largest mobile telecom operator in Russia by the number of users. It offers its services in GSM, NMT-450, and DAMPS standards by itself and through its subsidiaries in all of its areas of operations. Besides, outside its principal area of operations, the company partners with Volgatelecom to hold a 83% interest in Tatinkom-T (Uralsvyazinform's share is 33.4%), a closely held company that offers mobile telecom services in GSM-1800 and DAMPS standards in the Republic of Tatarstan. By far most of the users – 96.0% – are serviced in GSM. Other communications standards account merely for 4% (less Tatinkom-T subscribers).

## Mobile business GSM

	<b>Mobile business – GSM 900/1800</b>	
1	<b>Tyumen region</b> Population – 3.3 mln <b>Ermak RMS</b> Stake – 90% 346,500 subscribers	
2	<b>Perm region</b> Population – 2.9 mln <b>Uralsvyazinform</b> Stake – own business 341,300 subscribers	
3	<b>31/12/2003</b> <b>Sverdlovsk region</b> Population – 4.5 mln GSM 900/1800 license acquired	
4	<b>Chelyabinsk and Kurgan regions</b> Population – 4.7 mln <b>South-Urals Cellular Phone</b> Stake – 100% 411,900 subscribers	<b>September 2003</b> Tatarstan Population – 3.8 mln <b>Tatinkom-T</b> 10,000 subscribers

### GSM-900/1800

The company has chosen GSM-900/1800 mobile networks as a priority area for business development because they ensure investment in highly profitable telecom services and strengthen the company's position in this market segment.

Despite the growing competition, the company has retained its firm positions in the region, operating both in its own name and through its two subsidiaries, Ermak RMS and South-Urals Cellular Phone, where Uralsvyazinform has 90% and 100% interest in the authorized capital, respectively.

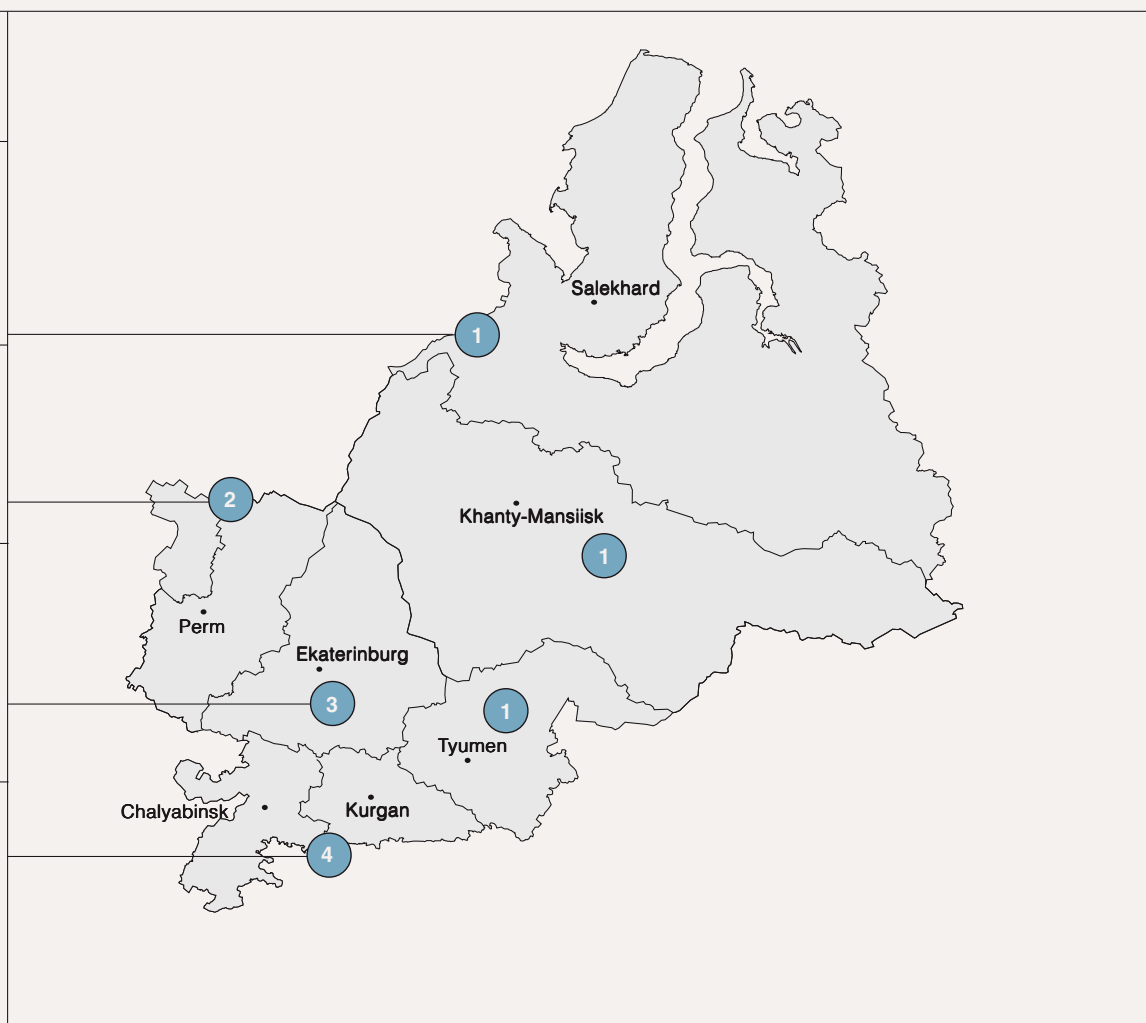
To continue to increase its customer base in the mobile business, Uralsvyazinform has upgraded, built and put into operation switching subsystems with a capacity of 629,000 numbers and 164 base stations in its GSM-900/1800 network:

In the Perm region, Huawei MSC-900/1800 was installed to expand the switching subsystem by another 300,000 numbers, and 82 base stations were put into operation.

#### Ermak RMS:

- The D-900 EWSD multiplexer switch in Salekhard was expanded by 8,000 numbers, and Huawei MSC-900/1800 switches in Noyabrsk and Novy Urengoi, with a total capacity of 60,000 numbers, were put into operation with two base stations.
  - The D-900 EWSD switching capacity has been expanded by 156,000 numbers in Khanty-Mansiisk, Surgut, Nizhnevartovsk, 38 base stations were installed.
  - 42 base stations have been installed and put into operation, together with additional AXE-10 units by Ericsson to expand the switch by 105,000 numbers.
- All regions are now conducting work to expand their infrastructure for the GSM-900/1800 base stations subsystem: putting up towers with hardware containers, and laying down connections between base stations and controllers based on thin-route digital radio relay lines or fiber-optic lines. As a result, both the throughput capacity and the coverage in the GSM-900/1800 networks in each of the above regions were increased, thus improving the quality of mobile telecom services and increasing the number of active users.

	<b>Mobile business Market share as of 31/12/2003</b>
1	<b>Tyumen region</b> Uralsvyazinform – 59% MTS – 13% MegaFon – 28%
2	<b>Perm region</b> Uralsvyazinform – 69% MTS – 28% MegaFon – 3%
3	<b>Sverdlovsk region</b> <b>Uralsvyazinform –</b> the license has been acquired MTS – 48% Vimpelcom – 1% MegaFon – 32% Ekaterinburg-2000 – 19%
4	<b>Chelyabinsk and Kurgan regions</b> Uralsvyazinform – 62% MTS – 31% Vimpelcom – less than 1% MegaFon – 7%



**Largest operators** offering mobile telecom services in the Urals Federal District and over the territory of the Perm Region.

Mobile telecom services in the Urals area are being offered by major federal and regional operators that account for more than half of the Urals mobile telecom market.

The principal competitor of Uralsvyazinform is Mobile TeleSystems (MTS), and as early as in 2004 competition with other federal mobile telecom operators – Megafon and Vypelkom – is expected to grow even stronger as these operators expand their networks.

**Mobile TeleSystems (MTS)** is a federal GSM900/1800 operator, it has been present in the Urals for two years, and has leading positions in the Sverdlovsk Region. In the last quarter of 2003 the company consolidated its subsidiary business in Uraltel (Yekaterinburg) into the MTS brand.

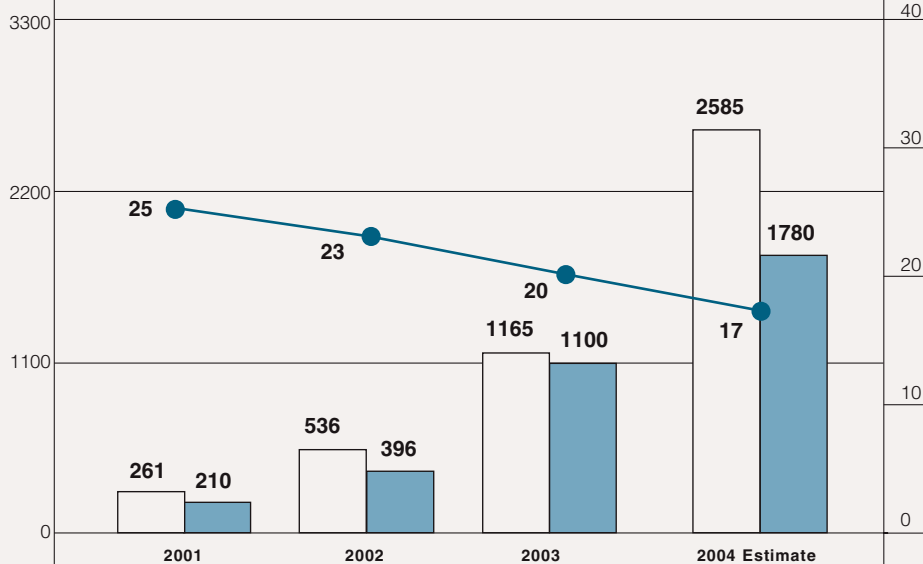
**Megafon**, which in the region is represented by a closely held company Ural GSM, emerged in the Urals cellular market in June 2002. It was the first federal network to offer its services on the Urals. Since then, Megafon has joined the group of leaders on the mobile telecom market in the Urals, with roughly a 20% share.

**Vypelkom-Region** (100% owned by Vypelkom) could be another potentially serious competitor.

In December 2002 it acquired 100% stock of East-West Telecom, a company with a GSM-1800 license covering the entire Urals area, and a GSM-900/1800 license for the Kurgan, Sverdlovsk regions and the Yamal-Nenets autonomous district. At the time of acquisition, the company was not offering any user services. In 2004 Vypelkom plans to launch its coverage of the Urals area, initially starting with the Sverdlovsk and Chelyabinsk regions, and southern Tyumen region.

**Yekaterinburg-2000**, a Yekaterinburg-based company operating under a brand "Motive", may be the only regional enterprise competitive to Uralsvyazinform in the mobile market. The company has about 5% of the overall Urals market.

**Mobile business (GSM 900/1800)**



- Installed capacity \*, thous. lines
- Subscriber base \*, thous. lines
- ARPU, USD

\* including subsidiary businesses

The ambitious plans of the leading federal cellular operators to expand into new regions are expected to increase mobile telecommunications competition in the Urals market. However, Uralsvyazinform intends to retain its share of the mobile telecom market through aggressive marketing policies and competitive pricing. Uralsvyazinform has certain competitive advantages on the mobile telecom market:

- since it can offer the entire range of telecommunications services, the company can exert as a lever its flexible pricing for unregulated telecom services;
- the company has many years of experience in telecom services and network construction across the Urals;
- it has knowledge of the geography, economics and social issues of the regional telecom market;
- the company has branches in all regions of the Urals Federal District and the Perm region, ensuring full coverage of the territory with own sales network;
- the company has the image of a successful business and key supplier of telecom services throughout the Urals Federal District, with a large customer base of fixed access subscribers, who are potential mobile users.

Given its range of services, Uralsvyazinform can afford to reduce their cost. As a universal provider, the company offers a package of services instead of a single product, and tariff policies in unregulated services (mobile telecommunications, Internet) can be very flexible. To promote new services or expand available ones, the company has been relying on existing resources (buildings and equipment), thus reducing expenses and driving down the ultimate cost of its product.

GSM 900/1800 networks currently are among the more important strategic areas of the company's business. To retain its competitive edge, the company intends to arrive at an optimum tariff level and exploit its key non-tariff potential, – i.e. added-value services and contents, quality of service and active promotion – to complete.

In 2004 having obtained the GSM-900/1800 license in the Sverdlovsk Region, the company plans to roll out a new cellular network in the Sverdlovsk Region, together with the installation of an MSC switch with a capacity of 500,000 numbers, and a subsystem of 200 base stations and three controllers (BSC).

With the implementation of the PPS (Comverse) intelligent network late in 2003, the company could start applying efficient tariff plans in the Perm Region. Before year end, the platform will have installed all segments of the Uralsvyazinform mobile network, and its subsidiaries will roll out the PPS technology across the entire area of operations. As a result, the company will be able to expand the range of services offered and quality of service.

The overall plan for 2004 is to expand the switching capacity across the Urals region by 1,420 thousand numbers and set up 562 base stations.

Before the end of the year, the company plans to consolidate its mobile business over the licensed territory and start offering its GSM900/1800 services in a single brand.

Development of cellular business and full implementation of its competitive advantages will help Uralsvyazinform retain its leading positions on the Urals market and maintain its high pace of growth.

# New services

In 2003 the company made significant progress in the establishment of a modern telecommunications infrastructure that supports the fast-growing segment of new services.



In 2003 revenues from new services grew by 183 million rubles over the prior year, of which Internet access services accounted for additional 147 million rubles. Revenue growth of more than 60% came to a large extent from the growing volume of services made possible by new equipment in operation and an improvement in throughput capacity.

## Revenues from new services (million rubles)

Item	2002	Share in revenues as of 2002, %	2003	Growth, %	Share in revenues as of 2002, %
New services, including	297.0	2.0	480.0	161.9	2.5
Internet	224.0	1.5	371.0	165.3	1.9
ISDN	28.4	0.2	48.8	171.8	0.3
Other new services	44.6	0.3	60.2	137.9	0.3

## Internet and data transmission services

Increased capacity for data transmission services, in particular Internet access, came from the expansion of existing networks and the construction of new multi-service networks. Technical solutions for the implementation of multi-service networks are based on IP/MPLS/ATM protocols. At the access point, the technologies used comprise xDSL, and 10/100 Ethernet. Networks offer access to Internet and virtual private networks. In 2003 the company commissioned 29 new nodes and significantly expanded the capacity of the existing 63 nodes in the data network. The overall number of access ports grew by 2,200.

In 2003 the number of Internet users rose by 160,000 to the current 282,000, of which 72 thousand use dedicated channels. In all branches the company continued to build new Internet outlets, some of them were put into operation, and nodes of multi-service access and optic access networks for corporate clients with the equipment from Cisco and Alcatel. This capacity is expected to help respond promptly to growing public and business demand, and to offer a platform for the implementation of broadband services when the demand is there.

One of the key venues to be pursued by the company is content, since provision of transport and access points is not expected to generate much revenue.

The growing numbers of Internet users suggest that Internet access in the near future may become one of the company's most popular services. Broadband access could be made possible with a NGN-based infrastructure and local networks adapted to host connection points to integrated services. Targeting a 50% market share in a few years, Uralsvyazinform has formulated the following strategies: **1.** introduce broadband access, mostly through "optics to homes"; **2.** create content in-house; **3.** target end users.

## Cable television

Throughout the year in cities and regional centers the company continued to lay down HFC cable TV networks, the most appropriate technology for a cable telecom operator. Gradually, all MMDS networks will be migrated to HFC.

In the reporting year, construction projects were started in the city of Chelyabinsk (first and second phases) and the Chelyabinsk Region. A head-end station was put into operations in Chelyabinsk. For 2004 the company plans to complete the ongoing construction projects in these cities and continue to expand cable TV networks in major cities across the Urals. In the course of the year, cable TV systems were undergoing further expansion in the city of Perm and in the Perm Region. There was high demand for the multi-channel TV broadcasting services in the MMDS network offered by the Khanty-Mansiisk branch.

By the end of the year, there were 35,000 subscribers for cable TV and MMDS distribution networks. In 2004 cable TV systems will continue to grow. The network capacity will be increased by 70,000. Networks will be expanded through the implementation of fiber-optic line video connections which also enable a broadband infrastructure.

## Intelligent networks and call centers

In the reporting year the company started to offer the basic set of intelligent services (premium calls, free calls, calling cards, tele-voting), supported by the Perm-based intelligent network, to the entire area of operation. In the first six months of 2004, with the implementation of the second automatic digital exchange in Yekaterinburg, a new digital exchange in Noyabrsk and SSP installation at the Kurgan exchange, the plans will have been completed.

In addition, the Khanty-Mansiisk branch has augmented its client information system capacity, and the number of connections processed simultaneously has been increased to 720.

Implementation of directory and information services through call centers has been started in Yekaterinburg. The 84-operator call center installed in the reporting year earned about 38 million rubles of additional revenues.

The long-term strategic plan is to develop the Uralsvyazinform intelligent network as a component of the national intelligent network, and to implement intelligent services on the NGN platform.

## Competition on the Internet access market

There are about 100 Internet providers in the Urals region with an aggregate market share of 60%. The average share owned by the largest operators is below 3%. Among the leading IP companies are UralRelcom; Global One (Equant); Raid-Internet, Modem, Teleross, and Rustel. These providers offer dial-up and dedicated line access, website services, hosting IP-telephony, and temporary access cards. Market trends seem to suggest that although alternative providers are getting more active, potential users intend to rely on Uralsvyazinform services, and the company may gain additional revenues by leasing its resources to alternative operators. In 2003, the company's share in new services increased from 31% to 39%, and by the end of 2004 it is expected to be up to 45–50%.



# Other services

## Document communications

In 2003, Uralsvyazinform telecommunications branches conducted work to maintain the existing public telegraph and subscriber's telegraphy (AT-TX) networks in line with the required demand and quality standards; the operators continued to implement new telecom technologies and telematics (X.400 electronic mail; IP access, bureau fax, and transmission of graphic and text files via the Messages Processing System Rostelemail). All these projects were implemented in full compliance with their telecommunications licenses.

Along with the growth in new services in the document communications, traditional telegraphy continued to shrink (telegrams, AT/XT subscriber's telegraphy, leasing of telegraph channels) and, as a result, efforts to decommission low-frequency telegraph systems continued.

The priority for 2004–2005 is to replace telegraph channels in the interswitch circuits and periphery segments of the telegraph networks with digital data transmission channels, and to integrate recoding communications services, consolidating them into REX400 postal centers.

## Paging networks

Paging appears to be entering a declining stage of its life cycle, squeezed out by mobile phones and SMS texting. The company's strategy is to liquidate this line of business. Its assets then will be used for other services (e.g., call centers).

Paging services are being offered by the following three Uralsvyazinform branches: Perm, Khanty-Mansiisk and Yamal-Nenets.

The overall paging network capacity is 60,000 users.

The total number of users as of December 31, 2003 was 29,719.

# Overview of strategy

## Marketing policies

Uralsvyazinform is aiming to retain its leadership in the Urals telecommunications market based on its competitive advantages that come from availability and development of its unique infrastructure assets.

### **The company plans to exploit its competitive advantages in the following areas:**

- efficient utilization and development of network and infrastructure assets;
- improved organizational efficiency;
- promotion of the role of marketing and sales in decision making;
- integrated services packages structured and offered so as to help clients to save money;
- comprehensive review of business-sector operations on the basis of long-term relationships, with the active sales model serving as a key competition instrument;
- differentiated promotion to target businesses and the general public.

There were no major changes in the competition on the Urals telecom market in 2003 that could have adversely affected Uralsvyazinform positions. The company's results in 2003 met the benchmarks and forecasts formulated in its marketing strategies.

### **The company's 2003 strategies resulted in the following marketing events:**

- Uralsvyazinform has prepared, and is in the process of implementing, marketing strategies for its subsidiary cellular operations;
- Uralsvyazinform has formulated and is implementing its Priority Services Promotion Program. The company's marketing strategies prioritize expansion of its mobile and fixed-access business, data transmission services, intelligent networks, and promotion of new services on the basis of advanced technological solutions.
- Together with its consultant, the company has completed joint research on Uralsvyazinform's corporate image and mobile telecommunications branding;

- The company has completed its segmentation and established a business sector database;
- Uralsvyazinform has developed, and is implementing a mechanism of interaction with the merged operators and corporate clients, enabling the company to develop its network in line with growing traffic;
- An operational system has been implemented to monitor and account for physical and cost indicators at branches and across the entire company;
- The company has begun monthly monitoring of the rate of return earned by each member of the merged network;
- Procedures have been developed for the selection and implementation of call centers;
- Procedures have been implemented for the CRM system within the framework of the ERP project.
- The company is working on a functional relationship management model in the VIP sector of corporate clients.
- Corporate and VIP client profiles and sales standards are being developed.

### **Marketing policies and goals at Uralsvyazinform have been formulated for the entire period through 2006:**

- Retaining its 65% share of telecom market revenues;
- Retaining a 50% share of the mobile telecom market as Uralsvyazinform enters Sverdlovsk regional market.
- Increasing its business sector share by 10% to 65%.
- Consolidating positions in the strategically significant markets of the Sverdlovsk Region, and the Khanty-Mansiisk – Ugra and Yamal-Nenets autonomous districts.

## Tariff policies

### Uralsvyazinform has identified the following goals in tariff policies:

- Implement a system of per-minute billing of local telephone calls across the entire territory of the Urals regions, offering different tariff plans;
- Bring down the overall tariff level in long-distance and international calls while increasing local telecom tariffs;
- Reduce cross-subsidization of services;
- Introduce uniform tariff policies vis-a-vis merged operators, including mobile operators.

Uralsvyazinform has been benefiting from the gradual elimination of cross-subsidization.

In 2003 the company introduced a package of changes in the tariffs applicable to regulated services in telecommunications. Tariffs for local calls were increased in parallel with the reduction in long-distance tariffs (except in the Sverdlovsk Region).

The main goal of tariff changes is to continue tariff unification throughout the area of operations, to eliminate cross-subsidization of services and classes of users, to implement marginal pricing methods in international calls (when the price of services depends on the traffic size), and to bring tariff policies in line with the general European practices (higher local tariffs and lower prices for long-distance calls).

The tariff reform has resulted in a 20% increase and equalization of regulated tariffs in all Urals regions (except in Yamal-Nenets and Khanty-Mansiisk autonomous districts where the northern climate calls for higher maintenance costs and respectively higher tariffs).

### The Urals groups of branches now have the following user fees:

- 130 rubles for the residential sector;
- 175 rubles for government organizations and businesses.

### In the Northern group of branches (Khanty-Mansiisk and Yamal-Nenets) the subscriber fees have been set at:

- 170–210 rubles for individuals;
- 290–345 rubles for enterprises.

Increased local tariffs are seen as an important reason for higher revenues from local telecom services at the company.

Long-distance tariffs in the Urals declined on average by 10% in the residential sector, and by 17% in the sector of government organizations and commercial enterprises. In the Northern group of branches, the reductions were 18% and 11%, respectively. Long-distance tariff reductions have stimulated higher traffic (up 21.3% over 2003) and helped strengthen competitive positions of the company vis-a-vis alternative operators.

The average calculated per-minute cost in long-distance operations decreased insignificantly (97% of the 2002 cost), but with the 13.3% growth in traffic, revenues from long-distance calls increased overall.

In 2004 the company plans further improvement in its tariff system, introducing package tariff changes in regulated services along with further reductions in long-distance services and connection charges.

The user fee is expected to grow by 20% on average.

Long-distance connections for all user groups are expected to come down on average by 10%.

The connection charge is expected to drop by 30%.

## Tariff policies in the mobile business

Given the growing competition, mobile tariffs are declining. However, with the subscriber base increasing 2.5 times over 2003, and given considerable under-saturation of the market, this business segment is expected to have the highest growth rates.

In 2003 the company continued its persistent efforts to improve its GSM-900/1800 tariffs. In 2003 the main goal in tariff policies was to maintain the market appeal of Uralsvyzinform's services, given its strong competition with MTS and Megafon, and to broaden the subscriber base, winning over residential users with average and low incomes. This was paralleled by further improvements in corporate and VIP tariff groups aiming to strengthen loyalty and motivate higher use of services. The Kapital tariff plan has become key in this user group, offering a higher access price (a connection charge of 6,000 rubles with VAT) offset by a zero user fee and discounted cost of traffic.

In this competitive environment, the reviewed tariff policies helped to raise the number of GSM users by a total of 700,000 subscribers in the company, including its subsidiaries (South Urals Cellular Phone and Yermak RMS), and to reach the 2003 budgeted figures for the GSM consolidated revenues. In 2004 the company will continue the projected tariff reductions to maintain its leadership on the Urals cellular market given strong competition from the three federal operators: MTS, Vypelkom, and Megafon. As a result, the company expects to increase the number of users by another 750,000 to 800,000 and achieve sales targets.

## Investment policies

**In 2003 driven by the company's intention to promote its main operations, and by the technical policies of the telecom company working across several regions of the Urals, Uralsvyzinform's priority strategies included:**

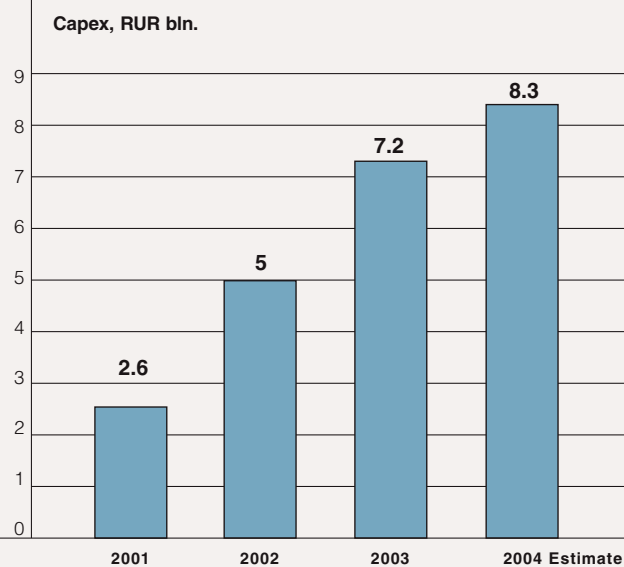
- promoting high-revenue telecom sectors;
- harmonizing telecom networks at branches;
- reducing operational costs;
- consolidating physical and technical infrastructure assets.

In line with the above plans, the following **key investment areas were identified for 2003:**

- expanding and upgrading local networks, with emphasis shifted to optic access network;
- expanding GSM-900 mobile networks;
- pursuing construction of facilities within intra-zonal primary networks;
- implementing new services: Internet and IP-telephony, multi-service networks, intelligent networks and call centers;
- constructing the corporate information system.

As a result, the 2003 operational efforts at Uralsvyzinform were aimed at the comprehensive development of telecommunications in the Urals region: constructing a flexible and scalable infrastructure, fixed and mobile telephony assets, data transmission networks, cable television, and broadband access; and implementing new technologies and advanced telecom services. In 2004 most of the capital expenditures will be used to continue modernization of equipment, expand fixed and mobile networks user capacities, and consolidate Uralsvyzinform's cellular subsidiaries into a single brand to increase future revenues from this business segment.

The 2003 capex amounted to 7.7 billion rubles (93.0% greater than in 2002).



**Investment projects were funded from the following sources:**

1. own capital – 41%;
2. borrowings – 59%

**By type of investment projects, the capex was structured as follows:**

- business development projects – 80%;
- infrastructure upgrading and maintenance projects – 19%;
- social projects – 1%;
- projects under 1 million rubles – less 1%.

The 2004 investment program is planned to be funded 40% from own capital and 60% from borrowed funds, with overall capital expenditures of 8.3 billion rubles. The program aims at a significant increase in the capacity and quality of networks. The user capacity is expected to grow by 323,000 numbers in fixed access and by 1,420,000 mobile numbers. Switching systems are expected to be 72.1% digital by the end of the year.

The key investment regions will comprise Sverdlovsk and Tyumen, including the Khanty-Mansiisk and Yamal-Nenets autonomous districts.

# HR management



**To provide for successful operations at Uralsvyazinform, we place a special emphasis on efficient human resources management. HR policy priorities are to optimize the number of employees and labor intensity, enhance HR quality and introduce effective professional training.**

**Corporate HR policies are structured along the Human Resource Program approved by the Board in 2001 for a period up to 2005. The program promotes optimization of employee strength (HR quantity and quality), and identifies goals in re-training and upgrading, together with uniform HR and social policies across the company.**

In 2003 the number of workers on the payroll decreased 1.2% to 35,998 as of December 31, 2003. The yearly average payroll decreased 2.8% (by 1,050 employees) to 36,884 in 2003. The average payroll workers, including part-time employees, decreased 1.7 % (by 598 employees) to 35,226.

Reductions in the average numbers of employees were achieved thanks to the improved organization, elimination of work places, measures to improve organization and work measurement, implementation of sectoral standards, improved organization and servicing of work places, concurrent operations and job combinations, expanded service areas, implementation of new techniques and advanced technologies.

There is an ongoing effort to study operational regimes at work units and their compliance with the incoming work load, and to analyze employee-numbers estimates. Throughout the year, the company continued to look into employment numbers in production processes, and in separate cost accounting.

## Management incentives

Pursuant to the Board of Directors Regulations, directors are to receive remuneration and compensation of expenses incurred in their capacity as Board members. Allocated rates (percentages) of quarterly and annual remuneration are approved by the general shareholders meeting that elects the incumbent Board.

Each Board member is entitled to a quarterly remuneration estimated as a percentage of company's revenues generated by sales of goods, products, works or services in the reporting quarter, in accordance with the company's statement of accounts. The latest shareholders meeting set the quarterly remuneration to each Board director at 0.0043% of the company's sales for the reporting quarter's accounts. The Chairman of the Board's remuneration will be adjusted by a factor of 1.3; i.e., the Chairman will receive 1.3 times the standard Board member compensation.

Annual remuneration of the entire Board accounts for 0.4% of net income for the financial year according to the company's statement of accounts.

In accordance with the Management Board Regulations, its members in their term shall receive remuneration and compensation of expenses incurred in their capacity as Management Board members. The remuneration of the Management Board members is estimated as a percentage of net income of the company in the reporting period in accordance with the company's statement of accounts, and is payable each quarter. The amount of due remuneration and its allocation among Management Board members are approved by the Board of Directors based on the proposal by the chair of the Management Board.

There are no ongoing management or Board incentive options schemes in the company.

## HR training and promotion

Uralsvyazinform has worked continuously to improve its employees' qualifications. Every three years each specialist is offered off-site educational opportunities to upgrade his or her skills. For HR professional development, the company has been partnering with the St. Petersburg State University of Telecommunications and its Professional Development Department; with the Volga Academy of Telecommunications; Siberian State University of Telecommunications and Information Technologies, and with duly licensed educational establishments. As part of the top telecom management training programs groups of Uralsvyazinform workers were enrolled in the MBA course at the Russian Government's Academy of the National Economy, and at the Moscow Higher Business School MIRBIS.

In 2003 together with Svyazinvest, an evaluation was carried out for the employees of the legal, marketing and PR services that resulted in a plan for the professional development and training of Uralsvyazinform employees in these services. The company conducted a monitoring analysis of regional educational establishments that offer such services in telecommunications and functional disciplines (management, economics, finances, accounting, etc.), and defined conceptual approaches and selection criteria vis-a-vis dilatational establishments. Branches have their own training centers supporting continuous professional training, development and retraining.

The Ministry of Communications of the Russian Federation appreciates the true value of the workers' contribution to the telecommunication development. In 2003, 18 workers were honored with the title of "The Master of Communication", 4 workers with "The Honorary Operator", and 8 workers with "The Honored Telecommunication Worker of the Urals". Four men were honored with the government medal "For Great Services in Conducting the All-Russian Population Census". Other kinds of encouragement as honorary diplomas and letters of appreciation, are also used in order to enhance the prestige of active, conscientious work.

# Social commitments

We are convinced that the well-being of our employees is one of the key indicators of the corporate success. This aim is achieved through higher wages, social assistance, functioning social infrastructure assets, and other assistance in social security and living conditions of corporate employees.

The Uralsvyazinform employee conference on June 18, 2003 approved the collective bargaining agreement, which was signed on June 26, 2003. The company allocated 566.7 million rubles in 2003 to implement provisions of the Collective Agreement.

On December 30, 2003 the employer and the representative of the employees signed an agreement on the prolongation of the unified collective agreement until the signing of a new one for 2004.

At present the text in some clauses of the agreement is under revision. The company considers the unified collective agreement in its current form to be the optimal document meeting the requirements of both sides.

## Charity

Over the past year the company has implemented a program of voluntary medical insurance for its employees. Pursuant to the Regulations "on medical security and medical insurance," the company provided medical vouchers for sanatoriums and spa treatment, and paid for kindergarten services. For the health and recreation of its employees, the company rents sports facilities, swimming pools, and organizes tournaments in various sports.

In line with the pension reform, the company converted its employees' pension entitlements and transferred the investment part of pension entitlement (as part of the unified social tax) to management companies duly licensed by the RF Government.

The company continued its partnership with the private pension fund Telekom-Soyuz that was contracted to handle private pensions for the company's employees.

The company's priority list of charities includes social assistance to the most needy groups in the society: orphaned and handicapped children; pensioners; surviving relatives; and centers of education, culture, healthcare and sports.

The decision to support KVN-games in the Urals was dictated by the need to care about creative advancement of the young people. One of the charity directions is investing in the rebuilding of churches and monasteries. The company is sympathetic to the work of non-profit organizations dealing with social problems. Uralsvyazinform has been supporting gifted children and teenagers to help them develop their technical and artistic talents, and participate in games, contests, tournaments and festivals.

Believing that charity is an instrument that can bring down social tensions, Uralsvyazinform has assisted correctional institutions with text books, law books, and fictional literature. Contributions to charitable and sponsorship programs attest to the socially responsible business run by the company and its work for the public good. In 2003 charity contributions amounted to 40,437,000 rubles.

# Corporate Governance

The company pays great attention to the quality of its corporate governance practices and disclosures. At its November 10, 2003 meeting, the Board of Directors at Uralsvyazinform approved the company's Corporate Governance Code. The Code was prepared in line with the Model Code recommended by the Securities Commission and corporate governance best practices. The company has been fully compliant with the provisions of the Corporate Governance Code. The purpose of the code is to ensure protection of interests and rights of Uralsvyazinform shareholders: their property rights, their right to participate in management and corporate profits, and their right to disclosures.

## Principles of corporate governance

The company adheres to the following principles of corporate governance:

- Establish an atmosphere of trust and respect among all participants in corporate relations at Uralsvyazinform;
- Fully comply with the universally accepted standards of business ethics in entrepreneurial activities;
- Ensure equitable treatment of all shareholders in the company, including minority and foreign investors;
- Expand and enforce shareholder rights protection;
- Optimize the structure of corporate governance and apply advanced methods and techniques;
- Ensure timely and accurate disclosures of the activities of the company to corporate stakeholders;
- Provide for continuous improvement of corporate governance standards.

The assumption Uralsvyazinform makes in its activities is that its shareholders have a set of rights and entitlements vis-a-vis the company, and it is the responsibility of the Board of Directors, Management Board and the CEO to ensure compliance with and protection of such rights.

Uralsvyazinform observes the shareholders' right to participate in the profits of the company. The company intends to make sure that money that cannot be invested in quality projects creating value for the company and increasing its valuation will be paid out in dividends on ordinary and preference shares.

In its meeting on February 25, 2004, the Board of Directors approved its Provisions for the Dividend Policies drafted in line with the Federal Company Law and Corporate By-Laws. The Provisions regulate procedures for the announcement, assessment and payment of dividends on all classes of shares in Uralsvyazinform.

Uralsvyazinform believes it needs to ensure regular and timely disclosures to its shareholders on the company's business to the extent required for balanced and well-substantiated shareholding decisions.

The aim of the disclosure policies at Uralsvyazinform is to provide the disclosed information to all parties concerned to the extent needed for a balanced investment decision or other actions that may impact financial and operational activities of the company.

Uralsvyazinform's underlying disclosure principles include availability of disclosures to all shareholders and all concerned parties; accuracy and authenticity of disclosed data, given a reasonable balance between company's openness and security of its commercial interests; and promptness in disclosure. By providing such disclosures, Uralsvyazinform ensures equitable treatment of all stakeholders and gives no preferences to any of them.

The company pledges not to disclose any confidential information and monitors insider information. The duty to observe confidentiality and comply with the rules on insider information applies to all employees at Uralsvyazinform.

The Board meeting on February 25, 2004 approved procedures for the dissemination of documents to Uralsvyazinform shareholders. The document defines procedures for the shareholders' access to documents to which they are entitled under Russian legislation and pursuant to the disclosure policies approved by the company.

The purpose of the Board is to provide efficient guidance to the company to ensure long-term sustainable growth of profitability and net assets, and to protect rights and lawful interests of its shareholders.

**The Board of Directors pursues the following objectives:**

- Articulate corporate strategies and monitor their implementation;
- Promote efficiency of internal mechanisms and their regular modification;
- Ensure company disclosures to shareholders and other stakeholders;
- Encourage corporate compliance with the effective legislation;
- Regularly assess performance of the company's executive bodies, top management and the Board itself;
- Approve and update the system of remuneration for top managers.

In its decision-making, the Board strives to incorporate the interests of employees, partners, creditors, local communities and other company stakeholders. The company assumes that candidates for Board membership must enjoy trust on the part of its shareholders, and have knowledge, skills and experience to pass decisions within the competence of the Board; have good faith, sufficient

time and personal qualities that ensure efficient performance of duties and to help structure relations with other Board members and executive management.

In accordance with the Corporate Governance Code, in its meeting of December 25, 2003 the Board approved terms of reference for two its committees:

- Committee on Corporate Governance
- Committee on Strategic and Investment Planning and Budgeting.

The composition of the committees was approved by the Board in its meeting on February 25, 2004.

The key objective of financial and business monitoring is to protect shareholders investments and Uralsvyazinform assets.

The objective is achieved with the growing efficiency and transparency of management and internal controls, and with the implementation of the corporate information system.

One of the company's monitoring priorities is to prevent, identify and limit financial and operational risks.

In 2003, the Board approved terms of reference for the Internal Audit Department in the company. In 2003 the Internal Audit Department conducted 77 examinations of finance and operations, including two joint checks together with the company's Audit Commission. The audited periods included the first six months of 2001, the year 2002, and part of 2003. Checks were run at Kurgan, Chelyabinsk, Tyumen, Yekaterinburg, Yamal-Nenets and Perm branches of the company.

**Examined areas included primarily:**

- Management of accounts receivable;
- Compliance with effective rules in financial and tax accounting;
- Random inventory checks;
- Observance of cash handling rules;
- Internal controls administered by the accounts service;
- Compliance with internal rules and regulations in contracting.

Basing on the results of branch examinations, measures were recommended and taken to eliminate identified violations.

Annual statements of accounts are examined and audited by a professional auditor, which has no shared property interests with company or its shareholders, and which is appointed every year by the company.

Audit at Uralsvyazinform is conducted so as to obtain unbiased and accurate statement of the company's business.

# Finance overview



- **Revenue growth totaled 24.3% as compared to 2002, mainly due to the following:**
  - Increase in revenues from mobile services by 34.6 %. Net additions as of 2003 totaled 700 thous. As of Jan 1, 2004 the mobile subscriber base totaled 1.1 mln (1.5 mln as of July 1, 2004).
  - Fixed-line revenues grew by 23.6 %. Fixed-line net additions over the year – 212 thous.
  - Long-distance segment saw 17.4 % rise. DLD traffic hike – by 21.3 %, ILD traffic hike – by 13.2 %.
  - New services (Internet, broadband, ISS, ISDN, etc.) demonstrated 2.9 fold increase in revenues versus 2002.
  - Revenues from operators (interconnection services) saw 46.4% rise.
- **EBITDA grew by 26.2% versus 2002 driving EBITDA margin to 27.7%.**
- **23.8% of revenues came from mobile services.**
- **Capex increased by 93.0% versus 2002 and totaled RUR7.7 bln.**

**2002–2003 Financial Highlights:**

	2002	2002	Change, %
Revenues, RUR mln	22,006.3	17,697.9	+24.3%
EBITDA, RUR mln	6,089.1	4,825.9	+26.2%
EBITDA margin	27.7%	27.3%	-
EBITDA (excluding allowance for bad debts), RUR mln	6,695.9	4,911.8	+36.3%
EBITDA margin (excluding allowance for bad debts)	30.4%	27.8%	-
Operating profit, RUR mln	3,437.1	2,425.2	+41.7%
Operating margin	15.6%	13.7%	-
Profit before taxation and minority interest, RUR mln	2,151.8	1,860.6	+15.7%
Net profit, RUR mln	1,223.9	995.5	+22.9%
Net margin	5.6%	5.6%	-

**Revenues: revenue growth in new services and mobile segments**

In general, the company revenues as of 2003 totaled RUR22,006.3 mln (+24.3% versus 2002), where revenues from telecommunications – RUR19,780.1 mln (+22.7%), revenues from telecommunication operators – RUR1,412.8 mln (+88.3%), others – RUR813.4 mln (-1.2%).

The revenues from DLD services increased by RUR969.4 mln, up 20.8% on 2002, reflecting the growth of outgoing paid traffic (as of 2003 DLD traffic totaled 1,856.7 mln minutes, 21.3% up on the previous year). The changes in DLD tariffs in effect as of May 16, 2003 and Aug 1, 2003 were another driver for the revenue growth. The traffic growth contributed RUR993.4 mln to the revenues, while the revised tariffs and lower average per line rates brought the revenue down by RUR24.0 mln.

The revenues from ILD services grew by RUR60.0 mln, mainly due to traffic growth (ILD traffic increased by 13.2% and equaled 122.4 mln minutes in 2003), which added up RUR165.0 mln. On the other hand, the decrease in average rates brought about the reduction of these revenues by RUR105.0 mln.

Generally, the share of DLD and ILD services in the revenues from telecommunications tend to go down – 35.1% in 2003 versus 36.6% in 2002, contrary to the growing share of mobile services (from 24.1% in 2002 to 26.5% in 2003) and new services, including data transmission and telematic services (from 2.0% in 2002 to 3.8% in 2003).

In the course of 2003 the monthly subscription fees for local services were increased twice – on May 16, 2003 and August 1, 2003; the average local tariff growth totaled 20% across the Urals region. Together with the growth of local subscriber base by 212 thousand, this provided for the steady growth of local revenues amounting to RUR1,012.2 mln, where monthly subscription fees contributed RUR798.6 mln (RUR588.8 mln of which came from the increased average rates, and RUR208.8 mln – from additions to subscriber base), while new installations contributed RUR213.6 mln.

In contrast to RAS, Uralsvyazinform's IAS statements consolidate the financial results of the subsidiary businesses, including 4 mobile operators – South Urals Cellular Phone, Ermak RMS (both GSM900/1800), TyumenRusscom (DAMPS 800), and UralWestcom (NMT450). Over 2003, mobile revenues increased by 34.6%, adding up to RUR5,233.8 mln. The share of mobile services in the revenues from telecommunications services increased from 24.1% to 26.5%.

The highest growth rates were seen in the sector of new services and data transmission. As of 2003, the number of Internet subscribers grew by 160 thous., and totaled as of Jan 1, 2004 282 thous., including 72 thous. dedicated channels. Internet traffic amounted to 647 mln minutes (a x1,5 rise on 2002). Data transmission volume increased 4 times, and totaled 157 TB. Revenues from new services increased 2.9 times compared to 2002, uprising their share in the revenues from telecommunications services to 2.4% from 1.0% in the previous year. Revenues from data transmission services increased by RUR118 mln, 70.2% up on 2002, and their respective share reached 1.4%.

Generally, the company's revenues were positively impacted by a consistent policy in relations with other operators, including tariff policies. The policies adopted, together with the increased transmission of traffic generated by other operators, were the important factors to push the revenues from operators by 46.4% at RUR1,098.1 mln (excluding the effects of new settlement system with Rostelecom).

The structure of revenues from telecommunication services in 2002–2003 is as follows (RUR, mln):

Revenues	2003	Share in revenues	2002	Share in revenues	Change
Domestic long distance services	5,631.6	28.5%	4,662.2	28.9%	+20.8%
International long distance services	1,300.3	6.6%	1,240.3	7.7%	+4.8%
Monthly subscription fees for local services	4,150.3	21.0%	3,351.7	20.8%	+23.8%
Installation and connection fees	1,159.6	5.9%	946.0	5.9%	+22.6%
Telegraph services	202.0	1.0%	214.8	1.3%	-6.0%
Mobile services	5,233.8	26.5%	3,889.5	24.1%	+34.6%
Radio and TV broadcasting	765.8	3.9%	701.6	4.4%	+9.1%
Data transmission and telematic services	286.1	1.4%	168.1	1.0%	+70.2%
New services (Internet, ISS, ISDN)	480.5	2.4%	166.2	1.0%	+189.1%
Channel rent	85.9	0.4%	66.1	0.4%	+30.0%
Other telecommunication services	484.2	2.4%	718.4	4.5%	-32.6%
<b>TOTAL</b>	<b>19,780.1</b>	<b>100.0%</b>	<b>16,124.8</b>	<b>100.0%</b>	<b>+22.7%</b>

Item	2003	Share in revenues	2002	Share in revenues	Change
Revenues from telecommunications services	19,780.1	89.9%	16,124.8	91.1%	+22.7%
Revenues from operators	1,412.8	6.4%	750.1	4.2%	+88.3%
Revenues from operators, excluding the effects of new settlement system with Rostelecom	1,098.1	5.0%	750.1	4.2%	+46.4%
Other revenues	813.4	3.7%	823.0	4.7%	-1.2%
<b>TOTAL</b>	<b>22,006.3</b>	<b>100.0%</b>	<b>17,697.9</b>	<b>100.0%</b>	<b>+24.3%</b>

**Operating expenses:  
cost control helped decrease the growth rate  
of expenses, compared to this of revenues**

Operating expenses grew by 21.6% and totaled RUR3,296.5 mln as of 2003, however the company managed to reduce the expenses per 1 ruble of revenues to RUR0.84 in 2003 versus RUR0.86 in 2002.

On the whole, the company achieved a significant slowdown in the growth rate of expenses (up 21.6%) compared to this of revenues (up 24.3%).

The main contributors to the growth of expenses as of 2003 were interconnection charges, paid to domestic operators. These expenses grew primarily due to the increase of Rostelecom charges for channels and traffic transmission in connection with the reform of settlement system in effect since Aug 1, 2003, as well as continued growth of traffic. The increase of expenses from other domestic operators (up 138.1%) was mainly due to the growth of Internet services.

Wages and other benefits increased by RUR799.7 mln, while the share of this item of expenditure decreased to 33.9% in 2003, compared to 36.0% in 2002, being indicative of the measures to optimize the number of personnel.

Material expenses grew by RUR566.5 mln, reflecting the growth of prices for materials, accessories and spare parts.

The company set up the bad debts reserve for accounts that are assumed irrecoverable. The amounts due from the federal budget to compensate for the state-sponsored privileges for certain telecommunications services were reflected in the increase of the accounts receivable. In turn, this translated into RUR520.9 mln growth of allowance for doubtful accounts.

**Capex: up 93.0%**

In adhering to an aggressive investment policy and allocating significant investment resources for new technologies and mobile telephony, Uralsvyazinform increased the amount of Capex by 93.0% to add up to RUR7,738.4 mln as of 2003. As of the reporting year, the capital expenditure totaled 35.2% of the company's revenues, as compared to 22.7% in 2002.

**Cash flows: cash flows  
from operating activities increased by 70.6%**

Net cash flows provided by operating activities as of 2003 grew by 70.6% and amounted to RUR5,140.1 mln. However, free cash flows were negative (-RUR2,598.3 mln) due to the increase in Capex by RUR3,728.4 mln.

**Debt: Capex growth  
by 93.0% pushed the debt up by 63.5%**

The consolidated debt of the company as of 2003 year-end totaled RUR10,146.9 mln, up 63.5% on 2002. Net debt as of year-end amounted to RUR9,314.7 mln. (up 65.1%). The financial leverage ratio (Debt/Equity) as of the end of 2003 equaled 50.9%. The growth in the amount of borrowed funds is aimed at financing the investment program.

Expenses breakdown as of 2003 is as follows:

Operating expenses	2003	Share	2002	Share	Change, Y-o-Y
Wages, salaries, other benefits and payroll taxes	<b>6,303.5</b>	33.9%	5,503.8	36.0%	+14.5%
Impairment of property, plant and equipment	<b>19.3</b>	0.1%	87.6	0.6%	-78.0%
Depreciation and amortization	<b>2,652.0</b>	14.3%	2,400.8	15.7%	+10.5%
Materials, repairs, maintenance and utilities	<b>2,019.6</b>	10.9%	1,453.1	9.5%	+39.0%
Taxes other than income tax	<b>384.8</b>	2.1%	472.9	3.1%	-18.6%
Interconnection charges -International	<b>68.6</b>	0.4%	38.9	0.3%	+76.1%
Interconnection charges -Domestic	<b>3,296.4</b>	17.8%	2,282.2	14.9%	+44.4%
Including Rostelecom charges in connection with channel rentals and traffic transmission	<b>2,001.1</b>	10.8%	1,664.3	10.9	+20.2%
Bad debts expense	<b>606.8</b>	3.3%	85.9	0.6%	+606.4%
Loss on disposal of property, plant and equipment	<b>73.3</b>	0.4%	112.4	0.7%	-34.8%
Other operating expenses	<b>3,144.9</b>	16.9%	2,835.1	18.6%	+10.9%
<b>TOTAL operating expenses</b>	<b>18,569.2</b>	<b>100.0%</b>	<b>15,272.7</b>	<b>100.0%</b>	<b>+21.6%</b>

# Independent auditors' report

To the Shareholders and Board of Directors  
of OAO "Uralsvyazinform"

1. We have audited the accompanying consolidated balance sheet of OAO "Uralsvyazinform" (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 4 and 5, 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 11 "Intangible Assets and Goodwill" and Note 13 "Investments in Associates", the Company accounted for the purchase of a subsidiary and an associate based on historical cost of their net assets. The Company did not identify and estimate the fair value of the purchased net assets as required by IAS 22, "Business Combinations". The effect of this departure from IAS 22 on the consolidated financial statements is not estimated.

**4.** Our report on the financial statement for the year ended December 31, 2002 contained a qualification with respect to departure from IAS 19, "Employment Benefits". As discussed in Note 28 "Pension Plan and Employee Benefits", in 2003 the Company changed its method of accounting for pension liabilities and related expenses and restated its corresponding financial statements for the effect of such change. The Company introduced accounting for pension liabilities and related expenses based on preliminary actuarial estimates. Management did not provide us with sufficient support for the preliminary actuarial estimates. We were therefore 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.

**5.** As described in Note 10 "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 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, 4 and 5, adjustments, if any, could materially affect the following items: (i) property, plant and equipment, equipment contributions, intangible assets and goodwill, investments in associates, pension liabilities, deferred income taxes, and retained earnings as of December 31, 2003 and the corresponding amounts; (ii) depreciation expense, income from associates, wages, salaries, other benefits and payroll

taxes, income tax expense and net income for the year ended December 31, 2003 and the corresponding amounts, and (iii) related disclosures.

**7.** In our opinion, except for the effects on the financial statements of such adjustments, if any, from the matters referred to in the paragraphs 3, 4 and 5, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of OAO "Uralsvyazinform" 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 further qualifying our opinion, we draw attention to Note 1 "Corporate Information" to the consolidated financial statements which discloses that the current liabilities of OAO "Uralsvyazinform" exceeded its current assets by 3,238,356 thousand rubles as of December 31, 2003. Management's plans in regard to this matter are also described in Note 1.

**9.** As described in Note 1 "Corporate Information", the Company was the subject of a reorganization that was approved by the shareholders on September 27, 2001. 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.

June 18, 2004

# Consolidated Financial Statements

## Consolidated Balance Sheet

As of December 31, 2003 (in thousands of rubles)

Item	Notes	2003	2002, as restated
1	1a	2	3
<b>ASSETS</b>			
<b>Non-current assets:</b>			
Property, plant and equipment, net	10	31,617,851	26,434,611
Intangible assets and goodwill, net	11	742,604	336,543
Investments in associates	13	349,308	2,650
Long-term investments	15	308,002	235,217
Advances to suppliers of equipment		545,667	448,652
Non-current receivables and other non-current assets		6,425	-
<b>Total non-current assets</b>		<b>33,569,857</b>	<b>27,457,673</b>
<b>Current assets:</b>			
Inventories, net	16	895,591	790,139
Trade accounts receivable, net	17	1,368,351	1,250,348
Short-term investments	18	147,324	69,833
Prepayments and other current assets	19	2,332,647	2,007,142
Cash and cash equivalents	20	684,809	495,917
<b>Total current assets</b>		<b>5,428,722</b>	<b>4,613,379</b>
<b>TOTAL assets</b>		<b>38,998,579</b>	<b>32,071,052</b>
<b>SHAREHOLDERS' EQUITY AND LIABILITIES</b>			
<b>Shareholders' equity:</b>			
Share capital, preferred shares	21	940,313	940,313
Share capital, ordinary shares	21	3,875,854	3,875,854
Treasury stock	21	(5,013)	(27,438)
Inflation impact on share capital		3,933,136	3,933,136
Retained earnings and other reserves		9,539,918	8,439,234
<b>Total shareholders' equity</b>		<b>18,284,208</b>	<b>17,161,099</b>
<b>Commitments and contingencies</b>	29	-	-
<b>Minority interest</b>	22	<b>179,455</b>	<b>182,084</b>
<b>Non-current liabilities:</b>			
Long-term borrowings	23	7,778,690	3,626,192
Finance lease obligations	24	753,863	328,866
Pension liabilities	28	609,000	445,000
Equipment contributions		97,412	97,740
Deferred income tax liability	7	2,381,925	2,300,688
Other non-current liabilities		246,948	145,207
<b>Total non-current liabilities</b>		<b>11,867,838</b>	<b>6,943,693</b>
<b>Current liabilities:</b>			
Trade accounts payable and accrued liabilities	25	3,824,159	2,689,804
Payable to Rostelecom		344,169	287,577
Taxes and payroll related obligations	26	794,015	660,477
Dividends payable		11,206	26,149
Short-term borrowings	23	2,079,208	1,869,292
Current portion of long-term borrowings	23	1,256,520	1,724,986
Current portion of finance lease obligations	24	357,801	525,891
<b>Total current liabilities</b>		<b>8,667,078</b>	<b>7,784,176</b>
<b>TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES</b>		<b>38,998,579</b>	<b>32,071,052</b>

## Consolidated Statement of Cash Flows

For the year ended December 31, 2003 (in thousands of rubles)

Item	Notes	2003	2002, as restated
1	1a	2	3
<b>Revenues</b>	4	<b>22,006,277</b>	<b>17,697,863</b>
<b>Operating expenses</b>			
Wages, salaries, other benefits and payroll taxes		(6,303,455)	(5,503,822)
Impairment of property, plant and equipment		(19,286)	(87,596)
Depreciation and amortization		(2,651,967)	(2,400,767)
Materials, repairs, maintenance and utilities		(2,019,630)	(1,453,050)
Taxes other than income tax		(384,810)	(472,892)
Interconnection charges – international		(68,566)	(38,944)
Interconnection charges – domestic		(3,296,417)	(2,282,204)
Bad debts expense		(606,805)	(85,906)
Loss on disposal of property, plant and equipment		(73,307)	(112,396)
Other operating expenses	5	(3,144,921)	(2,835,123)
<b>Total operating expenses</b>		<b>(18,569,164)</b>	<b>(15,272,700)</b>
<b>Operating income</b>		<b>3,437,113</b>	<b>2,425,163</b>
Income from associates		29,056	4,840
Interest expenses, net	6	(1,316,361)	(776,446)
Income from other investments		3,547	(6,319)
Foreign exchange loss, net		(1,512)	(389,201)
Net monetary gain		-	602,536
<b>Income before taxation and minority interest</b>		<b>2,151,843</b>	<b>1,860,573</b>
<b>Income tax expense, net</b>	7	<b>(928,531)</b>	<b>(788,786)</b>
<b>Net income before minority interest</b>		<b>1,223,312</b>	<b>1,071,787</b>
<b>Minority interest</b>		614	(76,259)
<b>Net income</b>		<b>1,223,926</b>	<b>995,528</b>
Dividends on preferred shares	9	(144,837)	(71,307)
<b>Net income attributable to ordinary shareholders</b>		<b>1,079,089</b>	<b>924,221</b>
<b>Basic and diluted earnings per share (Russian Rubles)</b>	8	<b>0.034</b>	<b>0.029</b>

Item	2003	2002, as restated
<b>Cash flows from operating activities:</b>		
Net income (loss) before taxation and minority interest	2,151,843	1,860,573
<b>Adjustments to reconcile income (loss) to cash generated from operations:</b>		
Foreign currency exchange loss, net	1,512	389,201
Net monetary gain	-	(602,536)
Depreciation and amortization	2,651,967	2,400,767
Loss from disposal of property, plant and equipment	73,307	112,396
Loss (income) from associates	(29,056)	(4,840)
Income from financial assets available for sale	(3,547)	6,319
Interest expense, net	1,316,361	776,446
Bad debt expense	606,805	85,906
Inventory obsolescence reserve	5,682	-
Impairment of property, plant and equipment	19,286	87,596
<b>Operating profit before working capital changes</b>	<b>6,794,160</b>	<b>5,111,828</b>
Decrease (increase) in trade accounts receivable	(731,232)	(416,545)
Decrease (increase) in other current assets	(325,505)	(1,368,141)
Decrease (increase) in inventories	(111,134)	(249,997)
Increase (decrease) in trade accounts payable and accrued liabilities	1,177,606	1,260,835
<b>Net cash generated from operations</b>	<b>6,803,895</b>	<b>4,337,980</b>
Interest paid	(927,309)	(643,968)
Income tax paid	(736,534)	(681,630)
<b>Net cash flows provided by operating activities</b>	<b>5,140,052</b>	<b>3,012,382</b>
<b>Cash flows from investing activities:</b>		
Purchase of property, plant and equipment	(7,240,963)	(3,974,204)
Purchase of intangible assets	(497,399)	(35,775)
Disposal (purchase) of subsidiaries/ associates, net	(316,069)	(478,847)
Disposal (purchase) of other investments, net	(150,276)	(113,411)
Interest received	133,438	36,740
Dividends received	2,131	-
<b>Net cash flows used in investing activities</b>	<b>(8,069,138)</b>	<b>(4,565,497)</b>
<b>Cash flows from financing activities:</b>		
Cost of purchased treasury stock	(235,849)	-
Revenue received from sales of treasury stock	333,595	-
Proceeds from borrowings	12,595,909	3,772,472
Repayments of borrowings	(11,086,994)	(1,711,908)
Proceeds from debt securities issued	3,000,000	1,000,000
Payments under financial leases	(459,257)	(416,912)
Repayment of vendor financing liabilities	(916,609)	(888,622)
Proceeds from (payment of) other non-current liabilities	101,741	-
Dividends paid	(212,543)	(145,610)
Dividends paid to minority shareholders	(2,015)	-
<b>Net cash flows generated from financing activities</b>	<b>3,117,978</b>	<b>1,609,420</b>
<b>Monetary effects on cash and cash equivalents</b>	<b>-</b>	<b>(75,892)</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>188,892</b>	<b>(19,587)</b>
<b>Cash and cash equivalents at the beginning of the year</b>	<b>495,917</b>	<b>515,504</b>
<b>Cash and cash equivalents at the end of the year</b>	<b>684,809</b>	<b>495,917</b>
<b>Non-monetary operations:</b>		
Non-cash additions to property, plant and equipment	904,652	1,176,915
Equipment contributions	3,027	-

## Consolidated Statement of Changes in Shareholders' Equity

For the year ended December 31, 2003 (in thousands of rubles)

Item	Notes	Share Capital		Treasury Stock	Inflation impact on share capital	Retained earnings and other reserves	Total equity
		2	3				
1	1a	2	3	4	5	6	7
		Preferred shares	Ordinary shares				
At December 31, 2001 as reported		940,313	3,875,854	(27,438)	3,933,136	7,965,870	16,687,735
Correction of pension liabilities (Note 28)						280,000	(280,000)
Correction of other errors						(100,585)	(100,585)
At December 31, 2001 as restated		940,313	3,875,854	(27,438)	3,933,136	7,585,285	16,307,150
Net income (loss) for the year		-	-	-	-	995,528	995,528
Dividends paid	9	-	-	-	-	(141,579)	(141,579)
At December 31, 2002 as restated		940,313	3,875,854	(27,438)	3,933,136	8,439,234	17,161,099
Net income (loss) for the year		-	-	-	-	1,223,926	1,223,926
Dividends paid	9	-	-	-	-	(198,563)	(198,563)
Proceeds received from sales of treasury stock		-	-	258,274	-	75,321	333,595
Cost of purchased treasury stock		-	-	(235,849)	-	-	(235,849)
At December 31, 2003		940,313	3,875,854	(5,013)	3,933,136	9,539,918	18,284,208

## Notes to Consolidated Financial Statements

(in thousands of rubles)

### 1. Corporate Information

#### Authorization of Accounts

The consolidated financial statements of OAO "Uralsvyazinform" and its subsidiaries (the "Company") for the year ended December 31, 2003 were authorized for issue by its appointed General Director and Chief Accountant on June 18, 2004.

#### The Company

The Company is an open joint stock company incorporated in accordance with the laws of the Russian Federation. The Company was privatized in 1994 and its principal activity is providing local and long-distance and international telephone services (including domestic and international telecommunication services, cellular services of GSM, NMT, and AMPS standards, and paging services), telegraph and data transfer services (including Internet over the territory of Ural region of Russian Federation). Other types of activity of the Company include motor transport repair and maintenance of recreational facilities and other social infrastructure. Associated companies provide cellular services in the Ural Region and Republic of Tatarstan of the Russian Federation.

On October 1, 2002 the Company was reorganized by merging 7 regional operators of Ural federal re-

gion. In 2003 structure of the incorporated company included the Headquarters, 7 branches "Elektrosvyaz" of Kurgan region, "Svyazinform" of Chelyabinsk region, "Uraltelecom" of Sverdlovsk region, "Yamalelectrosvyaz", "Tumentelecom", "Khantyanskiytelecom", "Uralsvyazinform" of Perm region.

Open joint-stock company Svyazinvest, a federal holding company majority-owned by the Russian Federation, owns 51% of the Company's ordinary shares. Domestic and international long-distance telecommunication services are provided by OAO "Rostelecom", a subsidiary of OAO "Svyazinvest".

The average number of employees in the Company in 2003 was approximately 37,800 persons.

The registered office of the Company is in the city of Perm in the Russian Federation, 68 Lenin St.

#### 2002 Reorganization

In 2001 the Company's management started the Company's reorganization. After obtaining shareholder approval to merge the regional enterprises of OAO "Svyazinvest", wherein 23,554,844,291 ordinary and 7,835,941,286 preference shares of the Company were exchanged for 100% of the ordinary and preference shares of the merged enterprises as follows:

Regional Enterprise	Shares Issued by the Company		Exchange Ratio
	Ordinary	Preference	
OAO "Elektrosvyaz" of Kurgan region	978,871,953	326,641,525	133.30259734
OAO "Svyazinform" of Chelyabinsk region	6,540,810,860	2,175,262,321	1,316.73752298
OAO "Uraltelecom" of Sverdlovsk region	6,180,053,956	2,054,528,433	604.55185921
OAO "Yamalelectrosvyaz"	2,487,523,682	829,142,081	220.75756257
OAO "Tumentelecom"	4,557,209,787	1,515,692,862	169.26463472
OAO "Khantyanskiytelecom"	2,810,374,053	934,674,064	161.22295530
<b>TOTAL</b>	<b>23,554,844,291</b>	<b>7,835,941,286</b>	

The merger was completed and effective on October 1, 2002. Transaction costs related to the merger were approximately 167 million rubles and were expensed.

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 earliest period presented. Unless otherwise described, all information presented in these financial statements gives retroactive effect to the reorganization.

Total assets, liabilities, revenues, and pre-tax income (loss) of the regional operations for the year ended December 31, 2002 are presented below:

	Total assets	Total liabilities	Revenue	Pre-tax income (loss)
The Company	7,424,170	(6,682,540)	3,602,693	431,514
OAO "Elektrosvyaz" of Kurgan region	1,039,113	(189,855)	510,072	(23,021)
OAO "Svyazinform" of Chelyabinsk region	8,406,344	(2,455,003)	3,546,834	312,167
OAO "Uraltelcom" of Sverdlovsk region	5,648,407	(1,602,569)	3,324,220	202,673
OAO "Yamalektrosvyaz"	982,178	(499,619)	1,048,472	(11,934)
OAO "Tumentelcom"	3,707,557	(1,400,278)	1,893,112	243,875
OAO "Khanty-mansiyskokrtelcom"	4,957,099	(1,991,821)	5,045,116	705,299
Eliminations and other adjustments	(93,816)	93,816	(1,272,656)	-
<b>TOTAL</b>	<b>32,071,052</b>	<b>(14,727,869)</b>	<b>17,697,863</b>	<b>1,860,573</b>

## 2. Summary of Significant Accounting Policies

### Liquidity risk

As of December 31, 2003, the Company's current liabilities exceeded its current assets by 3,238,356 thousand rubles. As a result, significant uncertainties exist as to the Company's liquidity and future capital resources.

Primarily due to ongoing investments in network maintenance and construction programs, the Company requires cash flows from operations, debt and other long-term financing resources, including hard currency borrowings for which no commercially viable hedging instruments are available.

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)** other financing from domestic lending institutions, **d)** household deposits in subsidiary bank. 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.

### 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 include standards and interpretations approved by the International Accounting Standards Board (IASB), International Accounting Standards Committee (IASC) and Standing Interpretations Committee (SIC); interpretations approved by the International Accounting Standards Committee Fund (IASCF) that remain in effect. Significant differences exist between the Russian Accounting Regulations and IFRS.

### Management Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of 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.

### Prior Period Adjustments and Reclassification

In the course of preparation of the consolidated financial statements for the year ended December 31, 2003, the Company discovered certain errors. The effect of such errors was reported as correction of opening balance of Retained earnings.

Certain amounts in the Company's consolidated financial statements as of December 31, 2002 and for the year ended December 31, 2002 were reclassified to conform to presentation adopted in current year. Such reclassifications did not have material effect on the corresponding amounts.

### Basis of Consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries drawn up to December 31 each year.

**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 subsidiaries, on a line-by-line basis.

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 Combinations". 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 in accordance with IAS 22, identifiable assets and liabilities of subsidiaries are stated at their fair value as of the acquisition date.

If the Company applies the purchase method to account for the acquisition of subsidiaries in accordance with IAS 22, 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.

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.

The annual financial statements of subsidiaries are prepared for the same reporting periods; whenever necessary, the financial statements of the subsidiaries are adjusted to bring their accounting policies in line with those applied by the Company.

Balances and transactions between the Company and subsidiaries, 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. The Company's investments in associates are accounted for under the equity method from the beginning of significant influence over the associate until the time when the Company ceases to have such significant influence.

Under the equity method, the book value of investments in an associate represents the Company's interest in the net assets of the associate plus unamortized portion of goodwill.

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.

**Goodwill**

For investments in subsidiaries and associates, any excess of the cost of acquisition over the Company's interest in the fair value of the identifiable assets and liabilities of the acquired entity is recognized as goodwill. Goodwill is amortized over its useful life, which cannot exceed 20 years, on a straight-line basis. 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.

## Negative goodwill

Negative goodwill is the excess of the Company's interest in the fair value of acquired assets and liabilities of a subsidiary or an associate at the date of acquisition over the purchase price paid. Negative goodwill is allocated to income on the basis of a review of the circumstances giving rise to it, as follows:

- to the extent that negative goodwill is related to future losses or expenses projected at the date of acquisition it is charged to income in the period when such losses or expenses arise;
- to the extent that negative goodwill is included in acquired amortized assets it is recognized as income on a straight-line basis over the remaining weighted average useful life of such amortized assets; and
- negative goodwill amount in excess of the fair value of all acquired non-monetary assets is directly recognized as income.

Negative goodwill arising from acquisition of an associate is charged to the carrying amount of investments in this associate.

Negative goodwill arising from acquisition of a subsidiary is recognized in the balance sheet as reduction to assets.

### Accounting for the Effects of Inflation

Based on the characteristics of the economic situation in Russia, since January 1, 2003, Russia no longer meets the definition of a hyperinflationary economy. Effective January 1, 2003, the Company discontinued the use of IAS 29 "Financial Reporting in Hyperinflationary Economies". Amounts of all non-monetary assets and liabilities, as well as equity, reported as of December 31, 2002, will be treated as the basis for the carrying amounts in the periods subsequent to December 31, 2002.

The adjustments and reclassifications made to the statutory records for the purpose of IFRS reporting in 2002 included the restatement for changes in the general purchasing power of the ruble in accordance with IAS 29. IAS 29 requires that financial information prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current "at the balance sheet date. These adjustments were calculated using conversion factors derived from the Russian Federation Consumer Price Index ("CPI") published by the Russian State Committee on Statistics.

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

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

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

- all amounts were stated in terms of the measuring unit current at December 31, 2002;
- monetary assets and liabilities at December 31, 2002 were not restated as they were already expressed in terms of the monetary unit current at December 31, 2002;
- non-monetary assets and liabilities which were not carried at amounts current at December 31, 2002 and shareholders' equity were restated by applying the relevant conversion factors;
- indexation adjustments to property, plant and equipment applicable to prior periods were credited to the opening balance of "Retained earnings and other reserves" in the accompanying balance sheet;
- all items in the consolidated statements of operations and cash flows were 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 were included in the consolidated statement of operations as a gain or loss on net monetary position.

## 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 foreign exchange 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 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
Analogue switches	15 years
Digital switches	15 years
Other telecommunications equipment	15 years
Vehicles	5 years
Computers, office and other equipment	5 years

Land is not depreciated.

Construction in progress is recorded as the total of actual expenses incurred by the Company from the beginning of construction to the balance sheet date. Accrual of depreciation begins when fixed assets are put into operation.

Borrowing costs that are directly 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 that 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.

The period of validity of the Company's operating licenses is significantly shorter than the useful lives used for depreciation of the cost of property, plant and equipment. Management believes that the operating licenses will be renewed without significant cost, which would allow the Company to realize the cost of its property, plant and equipment through normal operations.

## 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".

### 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, excluding development costs, 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.

### Investments

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 held for trading and available for sale are measured at fair value. Gains or losses on investments held for trading are recognized in income. 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 long-term investments that are intended to be held to maturity, such as bonds, are subsequently measured at amortized cost using the effective interest rate method.

The majority of the Company's investments are in securities that are not actively traded on organized financial markets. Management believes that fair value for these investments approximates their carrying amount.

### Inventories

Inventories are priced at the lower of cost or net realizable value. Cost is determined using the specific identification method.

### 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.

### Treasury Shares

Treasury shares are recorded in the balance sheet as a decrease of the shareholders' equity in the amount of the acquisition costs. The Company does not recognize gains/losses from transactions with treasury shares. The differences arising from transactions with treasury shares are charged to the capital accounts.

### 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.

### Non Interest-Bearing Loans and Borrowings

Non interest-bearing loans and borrowings are carried at their fair market value estimated by discounting future payments to their present value. Weighted average interest rates are used as an approximation to market interest rates.

## 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

Social contributions (including contributions to the state pension fund) are made through a unified social tax ("UST") calculated by the Company by the application of a regressive rate from 2% to approximately 35.6% 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.

In addition, post-employment benefits also include defined contribution plans and defined benefit plans.

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. 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.

### Defined Benefit Plans and Defined Contribution Plans

The Company operates defined benefit pension plans and defined contribution plans. The defined benefit plans are funded on a discretionary basis. The defined benefit pension accounting costs are assessed using the projected unit credit method. Under this method, the cost of providing pensions is charged to the income statement, so as to attribute the total pension cost over the service lives of em-

ployees in accordance with the benefit formula of the plan. The defined contribution pension costs are expensed based on actual contributions made by the Company into its employees' individual pension accounts.

### 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 over the shorter of the estimated useful life of the asset or the lease term.

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:

1. Long distance services – national;
2. Long distance services – international;
3. Monthly subscription fees for local services;
4. Installation and connection fees;
5. Telegraph services;
6. Mobile telecommunications services;
7. Radio and TV broadcasting;
8. Data transfer and telematic services;
9. New services (Internet, ISS, ISDN);
10. Rent of channels;
11. Revenue from telecommunication operators;
12. Other telecommunications services;
13. Other revenue.

**Long distance services  
(national and international)**

Revenues from long distance services are based on time used by the caller, the destination of the call and the services utilized. 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.

**Monthly subscription fees for local services**

The Company recognizes revenues related to the monthly network fees for local services in the month the service is provided to the subscriber.

**Installation fees and connection fees**

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

**Telegraph services**

Revenues from telegraph services comprise fees for cable 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 telecommunications services**

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 and TV broadcasting network. The revenues comprise monthly fees from subscribers and installation fees for wireline radio sets. The Company recognizes the revenues related to radio and TV 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 (Internet, ISS, ISDN)**

The Company recognizes revenues related to new services in the period when the services are rendered.

**Rent of channels**

The Company recognizes revenues from the rent of channels in the period when the services are rendered.

**Revenues from telecommunication operators**

Revenues collected from telecommunication operators for transmission of their traffic (incoming calls), and interconnection payments to the operators for the Company's traffic are recorded separately as Revenue from telecommunication operators and Interconnection charges, correspondingly, when the services are provided.

**Other telecommunication services**

Other telecommunication services mainly include revenues from payphones network, rent of channels, and sales of handsets and accessories.

**Other revenue**

Revenues other than telecommunication revenues primarily consist of transportation services, maintenance of recreational facilities and other social infrastructure and sale of goods and services provided by non-core 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.

Deferred tax liabilities relating to retained earnings of associates are recognized when it is probable that such earnings will be remitted to the Company in the foreseeable future.

**Value-Added Tax**

Output VAT amounts are payable on an accrual basis based upon invoices issued to subscribers. Input VAT may be offset, subject to certain restrictions, against output VAT. Input VAT that is not offsettable as of the balance sheet date is recognized in the balance sheets on a gross basis.

**3. Segment Information**

The Company's operating businesses are organized and managed separately according to the nature of the services provided, where each segment represents a strategic business unit that services different markets. The Company operates in 3 business segments – wireline telecommunication services, wireless telecommunication services and other services. Other services contain banking, transport, construction services, sales of marketable securities and other goods.

The revenue and operating result from discontinuing operation, and assets and liabilities of discontinuing operations are included into Wireless telecommunication services segment. For more information see Note 27 "Discontinuing operations".

The Company provides wireline telecommunication services and wireless telecommunication services, as well as other services. Management believes that the Company operates in one geographical segment. Certain services provided between the wireline and wireless segments are not invoiced, and accordingly not recognized, between the subsidiaries of the Company performing such services.

The following tables present financial information for segments.

Item	2003							2002, as restated							
	Wireline services	Wireless services	Other	Intercompany eliminations	Total for the Company	Wireline services	Wireless services	Other	Intercompany eliminations	Total for the Company	Wireline services	Wireless services	Other	Intercompany eliminations	Total for the Company
<b>REVENUE</b>															
Sales to third parties	16,191,538	5,070,106	744,633	-	22,006,277	13,531,016	3,699,270	467,577	-	17,697,863					
Inter-segment sales	2,124,768	17,169	-	(2,141,937)	-	1,036,700	-	8,690	(1,045,390)	-					
<b>Total revenue</b>	<b>18,316,306</b>	<b>5,087,275</b>	<b>744,633</b>	<b>(2,141,937)</b>	<b>22,006,277</b>	<b>14,567,716</b>	<b>3,699,270</b>	<b>476,267</b>	<b>(1,045,390)</b>	<b>17,697,863</b>					
<b>SEGMENT PROFIT</b>	<b>3,317,794</b>	<b>952,280</b>	<b>23,162</b>		<b>4,293,236</b>	<b>1,970,274</b>	<b>1,052,265</b>	<b>32,302</b>		<b>3,054,841</b>					
<b>Unallocated expenses</b>					<b>(856,123)</b>					<b>(578,987)</b>					
<b>Operating income</b>					<b>3,437,113</b>					<b>2,475,854</b>					
Income from associates					29,056					4,840					
Interest expense, net					(1,316,361)					(776,446)					
Income (loss) from revaluation of investments					3,547					(6,319)					
Foreign exchange loss, net					(1,512)					(389,201)					
Net monetary gain					-					602,536					
Income tax expense					(928,531)					(788,786)					
Minority interest					614					(76,259)					
<b>Net income</b>					<b>1,223,926</b>					<b>995,528</b>					
<b>ADDITIONAL INFORMATION</b>															
Segment assets	31,607,7123,892,910602,565			36,103,187	28,109,175	2,675,358	512,420		31,296,953	774,099					
Unallocated corporate assets					2,895,393										
<b>Consolidated total assets</b>					<b>38,998,580</b>					<b>32,071,052</b>					
Segment liabilities	7,452,488	1,261,946	577,266		9,291,700	11,097,268	838,456	436,335		12,372,059					
Unallocated corporate liabilities					11,422,671					2,537,894					
<b>Consolidated total liabilities</b>					<b>20,714,371</b>					<b>14,909,953</b>					
Capital expenditure	8,114,012	1,177,527	21,232		9,312,771	5,398,427	661,036	39,199		6,098,662					
Depreciation and amortization	2,345,473	268,181	38,313		2,651,967	2,258,592	129,970	12,205		2,400,767					

#### 4. Revenues

	2003	2002
<b>REVENUES FROM SUBSCRIBERS</b>		
Long distance calls – national	5,631,559	4,662,181
Long distance services – international	1,300,347	1,240,254
Monthly subscription fees for local services	4,150,267	3,351,696
Installation and connection fees	1,159,634	946,034
Telegraph services	201,974	214,765
Mobile telecommunication services	5,233,783	3,889,461
Radio and television broadcasting	765,831	701,647
Data transfer and telematic services	286,060	168,066
New services (Internet, ISS, ISDN)	480,538	166,190
Rent of channels	85,879	66,062
Other telecommunication services	484,188	718,405
<b>Total revenues from subscribers</b>	<b>19,780,060</b>	<b>16,124,761</b>
<b>REVENUES FROM TELECOMMUNICATION OPERATORS</b>		
Incoming calls	1,412,803	750,13
<b>OTHER REVENUES</b>	<b>813,414</b>	<b>822,964</b>
<b>TOTAL</b>	<b>22,006,277</b>	<b>17,697,863</b>

Mobile telecommunication services primarily consist of air time charges, fees for additional mobile services and roaming charges to other mobile operators for services to visiting roaming clients.

Other telecommunication services mainly include revenues from payphone network, one time services like up-dating subscriber's data, sales of handsets and accessories.

Revenue from telecommunication operators consists primarily of Rostelecom charges for incoming traffic (Note 30).

Other revenues primarily consist of revenue from transportation services, maintenance of recreational facilities and other social infrastructure and sale of goods and services provided by non-core subsidiaries.

The Company identifies revenue by the following major customer groups:

	2003	2002
Residential customers	11,961,116	8,350,962
Corporate customers	6,693,062	7,096,335
Telecommunication providers	1,412,803	750,138
Government customers	1,269,996	977,241
Tariff compensation from the state budget	669,300	523,187
<b>TOTAL</b>	<b>22,006,277</b>	<b>17,697,863</b>

## 5. Other Operating Expenses

	2003	2002
Rent of premises	173,080	166,895
Fire and other security services	250,585	128,559
Payments to Gossvyaznadzor	74,516	83,463
Cost of goods sold	387,922	443,670
Transportation services	44,562	23,463
Audit and consulting fees	32,298	22,139
Training expenses	52,699	36,075
Advertising	171,946	184,829
Business travel expenses	88,142	51,587
Post services	22,432	25,037
Social expenses	52,699	36,075
Insurance	228,533	234,329
Information services	67,010	30,954
Research and development expenses	20,344	36,379
Obsolescence inventory provision	6,172	33,699
Dealers commission	253,118	-
Payments to Non-commercial partnership	188,992	147,000
Construction of social sphere	53,854	96,801
Mobilization expenses	10,710	2,983
Civil defense expenses	9,233	2,573
Other	938,868	1,054,573
<b>TOTAL</b>	<b>3,144,921</b>	<b>2,835,123</b>

Other expenses primarily consist of expenses for bank services, contract execution with subscribers of mobile communication, commission and agent fees, expenses related to cash collection with nonpayer, encashment, other general and administration expenses.

## 6. Interest expense, net

	2003	2002
Interest income	(133,438)	(36,740)
Interest expense	1,269,741	733,222
Interest expense accrued on financial leases	222,247	84,670
Less capitalized interest	(42,189)	(4,706)
<b>TOTAL</b>	<b>1,316,361</b>	<b>776,446</b>

## 7. Income Tax

The following tables present financial information for segments.

	2003	2002
Current income tax expense	847,294	509,841
Prior-year income tax adjustments	-	-
Carry forward of tax losses and unused tax credits	-	-
<b>Total current income tax expense</b>	<b>847,294</b>	<b>509,841</b>
Deferred income tax benefit (charge) relating to origination of temporary differences	81,237	278,945
<b>Total deferred income tax (benefit) charge</b>	<b>81,237</b>	<b>278,945</b>
<b>Total income tax charge for the year</b>	<b>928,531</b>	<b>788,786</b>

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

	2003	2002
<b>Profit before income tax and minority interest</b>	<b>2,151,843</b>	<b>1,860,573</b>
Statutory income tax rate	24%	24%
Theoretical tax charge at statutory income tax rate	516,442	446,538
<b>Increase (decrease) resulting from the effect of:</b>	-	-
Prior-year income tax adjustments	-	-
Non-taxable income	-	-
Expenses not deductible for tax purposes	286,290	114,550
Carryforward of tax losses and unused tax credits	-	-
Deductible tax losses and tax credits	-	-
Inflation effect on deferred tax at beginning of year	-	(63,477)
Other reconciling items	125,799	291,175
<b>Total income tax charge for the year at the effective rate of 43% (2002: 42%)</b>	<b>928,531</b>	<b>788,786</b>

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	December 31, 2002
<b>Tax effects of deferred tax assets:</b>		
Accounts payable	60,812	3,480
Accounts receivable	126,561	-
Other	2,796	32,995
Tax loss carryforward	-	-
<b>Deferred tax asset, total</b>	<b>190,169</b>	<b>36,475</b>
<b>Tax effects of deferred tax liabilities:</b>		
Property, plant and equipment	(2,494,339)	(2,119,257)
Accounts receivable	-	(31,440)
Investment valuation difference	(13,218)	(18,043)
Inventory	-	(9,610)
Other	(64,537)	(158,813)
<b>Deferred income tax liability, total</b>	<b>(2,572,094)</b>	<b>(2,337,163)</b>
<b>Net deferred income tax liability</b>	<b>(2,381,925)</b>	<b>(2,300,688)</b>

Differences between IFRS and statutory taxation and reporting regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for consolidated financial reporting purposes and for profits tax purposes. The tax effect of these temporary differences is recorded at the rate of 24% effective as of January 1, 2002.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current deferred tax liabilities, and the deferred income tax assets and deferred income tax liabilities relate to the income taxes levied by the same fiscal authority on the same taxable entity.

## 8. Earnings per Share

The following tables present financial information for segments.

	2003	2002
Net income	1,223,926	995,528
Less dividends on preferred shares	(144,837)	(71,307)
Net income attributable to ordinary shareholders (basic and diluted)	1,079,089	924,221
Weighted average number of ordinary shares for basic and diluted earnings per share	32,159,959,344	32,080,542,660
Earnings per ordinary share, Rubles (basic and diluted)	0.034	0.029

Basic and diluted earnings per share are calculated by dividing the net income for the year attributable to ordinary shareholders (net income for the period less preferred dividends declared in the corresponding

period) by the weighted average number of ordinary shares outstanding during the year. The Company has no financial instruments that can be converted into ordinary shares.

## 9. Dividends Paid and Proposed

Declared and paid during the year (for the year 2002)	
Dividends on ordinary shares, 0.0039 rubles per share	127,257
Dividends on preferred shares, 0.0091 rubles per share	71,307
<b>TOTAL</b>	<b>198,564</b>
Proposed by the Board of Directors for the year 2003 (Note 32, Subsequent Events)	
Dividends on ordinary shares, 0.01 rubles per share	322,988
Dividends on preferred shares, 0.0185 rubles per share	144,837
<b>TOTAL</b>	<b>467,825</b>
Dividends paid to shareholders are determined by the Board of Directors and declared and officially approved at the annual shareholders' meeting. Earn-	ings available for dividends are limited to profits determined in accordance with Russian statutory accounting regulations.

## 10. Property, Plant and Equipment

Item	Buildings and constructions	Switches and transmission-devices	Construction in progress and equipment for installation	Machines and other	Total
Cost					
At December 31, 2002	27,530,690	27,367,264	1,905,980	6,119,819	62,923,753
Additions	-	-	7,937,890	-	7,937,890
Disposals	(159,698)	(950,081)	(5,975)	(156,446)	(1,272,200)
Transfers	2,955,183	3,929,125	(7,718,797)	834,489	-
At December 31, 2003	30,326,175	30,346,308	2,119,098	6,797,862	69,589,443
Impairment					
At December 31, 2002					
Accrued provision for the year	(1,888,193)	(1,744,630)	(152,436)	(393,228)	(4,178,487)
Reversal of provision	-	-	(18,925)	-	(18,925)
At December 31, 2003	9,179	51,900	-	7,398	68,477
Accumulated depreciation	(1,879,014)	(1,692,730)	(171,361)	(385,830)	(4,128,935)
At December 31, 2002	(15,306,576)	(13,102,235)	-	(3,901,844)	(32,310,655)
Charge for the year	(524,037)	(1,620,818)	-	(428,822)	(2,573,677)
Disposals	126,667	814,010	-	100,998	1,041,675
At December 31, 2003	(15,703,946)	(13,909,043)	-	(4,229,668)	(33,842,657)
Net book value as of December 31, 2002	10,335,921	12,520,399	1,753,544	1,824,747	26,434,611
Net book value as of December 31, 2003	12,743,215	14,744,535	1,947,737	2,182,364	31,617,851

The net book value of plant and equipment held under finance leases at December 31, 2003 is 1,793,042 (2002 – 1,306,379). Leased assets are pledged as security for the related finance lease obligations (Note 24).

In 2003, the Company increased construction in progress by the amount of capitalized interest totaling 42,189 (2002 – 4,706) (Note 6).

Property, plant and equipment for a total of 6,461,195 (2002 – 4,166,220) as of December 31, 2003 secure the Company's borrowings (Note 23).

Property, plant and equipment for a total of 346,416 (2002 – 437,361) as of December 31, 2003 were received on supplier credit terms.

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.

The Company plans to engage an independent appraiser to assist in reconstruction of the fair value of the Property, Plant and Equipment, in order to make the necessary adjustments, if any, to the Company's books and records, to comply with IFRS.

## 11. Intangible Assets and Goodwill

	Goodwill	Licenses	Software and Other	Total
Cost				
At December 31, 2002	174,595	1,217	231,292	407,104
Additions	-	1,362	499,278	500,640
Disposals	-	-	(19,804)	(19,804)
At December 31, 2003	174,595	2,579	710,766	887,940
Accumulated amortization				
At December 31, 2002	(13,095)	(239)	(57,227)	(70,561)
Charge for the year	(17,459)	(378)	(60,453)	(78,290)
Disposals	-	-	3,515	3,515
At December 31, 2003	(30,554)	(617)	(114,165)	(145,336)
Net book value at December 31, 2002	161,500	978	174,065	336,543
Net book value at December 31, 2003	144,041	1,962	596,601	742,604

### Oracle

In accordance with Board decision № 10 of OAO Svyazinvest 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 and approved a supply contract with ZAO Otkrytye tekhnologii 98 in the amount of 550,831 (approximately 18,701,078 US dollars).

In accordance with the supply contract, the Company has been provided with non-exclusive licenses for 9,242 users of E-business Suite among other license applications.

The Company expects to complete this system implementation in 2006.

### Goodwill

Goodwill arising on the acquisition of OOO "Yuzhno-Uralskiy Sotoviy Telefon" on 2002, was amortized consistent with IAS requirements over 10 years.

The Company did not estimate the fair value of the purchased net assets of OOO "Yuzhno-Uralskiy Sotoviy Telefon" as required by IAS 22 "Business Combinations". For determination of goodwill, the management used an assumption that historical value of investment is equal to fair value.

### Licenses and software

Licenses and software are amortized on a straight-line basis over their estimated useful lives determined equal to the term of the license or the license agreement for software. Useful lives of other intangible assets are 5-10 years.

## 11. Intangible Assets and Goodwill

The consolidated financial statements include the assets, liabilities and financial results of OAO "Uralsvyazinform" and its subsidiaries listed below:

Subsidiary	Main Activity	Voting Shares	
		2003	2003
OOO "Perminform"	Data transfer	100%	100%
OOO "Ural Inform TV"	Radio-, TV broadcasting	100%	100%
ZAO "Ininvest"	Installation of telecommunication equipment	100%	100%
ZAO "Svyazinformkomplekt"	Trade and purchasing agents	100%	100%
OOO "Tumentelecominvest"	Professional activity on securities market	100%	100%
ZAO "Centr vnedreniya specializirovanih specsistem"	Development of education system	100%	100%
OOO "Uzhno-Uralskiy sotoviy telefon"	Cellular communication services	100%	100%
ZAO "Ermak RMS"	Cellular communications services	90%	90%
ZAO "AKIB Pochtobank"	Bank activity	68%	68%
NPF "Svyazist"	Pension plans	63%	63%
ZAO "VSNET"	Internet services	52%	52%
ZAO "Uralwestcom" (see Note 27 "Discontinued Operations")	Cellular communication services	51%	51%
ZAO "Tumenruscom"	Cellular communication services	51%	51%

### 13. Investments in Associates

Associate	Activity		As of December 31, 2003		As of December 31, 2002	
			Voting shares	Carrying value		
OAO "Tatincom-T"	Cellular communication services	Share in net assets	33%	396,407	-	-
		Negative goodwill		(76,454)		
				319,953		
ZAO "Uralskaya telefontnaya kompaniya"	Communication services		23%	17,621	23%	50
ZAO "Teleross-Ekaterinburg"	Communication services		50%	5,742	50%	1,522
ZAO "Teleross-Tyumen"	Communication services		50%	4,377	50%	275
ZAO "Ural-Teleservis"	IT services		25%	1,170	25%	105
Other				445		698
<b>TOTAL</b>				<b>349,308</b>		<b>2,650</b>

In 2003 the Company paid 316,069 to acquire a 33,34% equity interest in OAO "Tatincom-T" (Note 14). Movement in investments in associates in 2003 is presented below:

Balance at December 31, 2002	2,650
Associate's acquisition cost (Note 14)	316,069
Share in income net of income tax	29,056
Amortization of negative goodwill	1,533
Balance at December 31, 2003	349,308

The Company did not estimate the fair value of the purchased net assets as required by IAS 22, "Business Combinations". The financial statements were presented based on assumption that historical value of investment is equal to the fair value.

OAO "Tatincom-T" is a provider of cellular telecommunication services, which operates in Republic of Tatarstan. At the beginning of 2003 it was rated as second operator at the cellular services market there having 31% of market share. Due to high competitive environment (the main competitors are MTS, Vimpelcom and Megafon) the market share of OAO "Tatincom-T" decreased to 12% in December 2003. It raises uncertainties about possibility of future operation of OAO "Tatincom-T".

Management of OAO "Uralsvyazinform" plans to enhance its GSM network in 2004 by covering major cities and towns and main highways in the Republic. Afterwards it plans to cover major district centers of Tatarstan. This would attract subscribers and cause increase of cellular market share.

The excess of share in the historical value of net assets (liabilities) of OAO "Tatincom-T" over the paid acquisition price (negative goodwill) was defined as follows:

The financial year of all associates terminates on December 31, 2003.

The accounting policies of associated companies are not fully consistent with the accounting policy of the Company used for these consolidated financial statements. The management of the Company is certain that differences in accounting policies of associates do not have a material effect on the amount of identifiable income from participation in such companies.

Investments in other associates were accounted at cost as amount of profit or loss is immaterial to the Company' consolidated financial statements.

#### 14. Acquisition of associate

In October 2003 the Company acquired 33,34% share of OAO "Tatincom-T" and gained significant influence over its financial and operational activities (Note 13). Accordingly, the share of the Company in its results of operations and financial position has been accounted based on equity method since October 1, 2003.

Acquisition price	303,413
Transaction costs	12,656
<b>Total paid</b>	<b>316,069</b>
<b>Total net assets</b>	<b>1,181,932</b>
Company's share in acquired net assets	33,34%
Value of acquired share in identifiable net assets	394,056
<b>Negative goodwill</b>	<b>(77,987)</b>
Amortization of negative goodwill since the acquisition date to December 31, 2003	1,533
<b>Amount of negative goodwill at December 31, 2003 (net)</b>	<b>(76,454)</b>

## 15. Long-term investments

	2003	2002
Other long-term investments	122,943	99,531
Long-term loans	190,932	107,448
Government, municipal and third-party bonds	29,619	61,118
Less: allowance for long-term investments	(35,492)	(32,880)
<b>TOTAL</b>	<b>308,002</b>	<b>235,217</b>

As of December 31, 2003 and 2002, loans and bonds issued are recognized at fair value.

Other long-term investments include investments in the following companies:

	2003		2002	
	Share	Current value	Share	Current value
Commercial Bank "Svyaz-Bank"	7%	28,638	7%	28,638
ZAO TK-Ural	24.8%	12,622	24.8%	12,622
Investments of NPF Svyazist		22,243		-
Others		81,566		80,397
Less: Allowance of other long-term investments		(22,126)		(22,126)
<b>TOTAL</b>		<b>122,943</b>		<b>99,531</b>

Other available-for-sale financial assets do not have quoted market prices in an active market. Management believes that their fair value equal to investment cost less allowance.

## 16. Inventories

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

	2003	2002
Cable, spares and materials for telecommunications equipment	518,993	408,639
Finished products and goods for resale	78,317	66,509
Other inventories	310,135	318,421
Less: Provision for obsolescence	(11,854)	(3,430)
<b>TOTAL</b>	<b>895,591</b>	<b>790,139</b>

## 17. Trade accounts receivable

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

	2003	2002
Trade receivables – telecommunication services	2,280,452	1,596,666
Trade receivables – other	22,402	7,548
Less: Allowance for doubtful accounts	(934,503)	(353,866)
<b>TOTAL</b>	<b>1,368,351</b>	<b>1,250,348</b>

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

	2003	2002
Corporate customers (including operators)	671,045	529,593
Residential customers	1,422,837	905,373
Governmental customers	186,570	161,700
<b>TOTAL</b>	<b>2,280,452</b>	<b>1,596,666</b>

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. In order to further reduce a portion of the risk associated with customer non-payment, the Company has in certain circumstances negotiated arrangements wherein the Company has accepted payment in goods and services, which are utilized in its non-core business.

## 18. Short-term investments

Short-term investments are recognized at fair value. As of December 31, 2003 and 2002, short-term investments include the following:

	2003	2002
Corporate customers (including operators)	671,045	529,593
Residential customers	1,422,837	905,373
Governmental customers	186,570	161,700
<b>TOTAL</b>	<b>2,280,452</b>	<b>1,596,666</b>

## 19. Prepayments and other current assets

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

	2003	2002
Prepayment and advance payments	290,612	357,531
Settlements with personnel	44,373	19,759
VAT recoverable	1,280,291	1,046,778
Income tax	161,183	218,242
Other taxes prepaid	53,891	63,727
Prepaid Expenses	289,083	138,441
Other receivables	213,345	253,806
Less: Allowance for other current assets	(131)	(91,142)
<b>TOTAL</b>	<b>2,332,647</b>	<b>2,007,142</b>

## 20. Cash and cash equivalents

	2003	2002
Cash at bank and in hand	647,910	391,667
Short-term deposits	4,334	17,196
Other cash equivalents	32,565	87,054
<b>TOTAL</b>	<b>684,809</b>	<b>495,917</b>

The fair value of the Company's cash and cash equivalents equals its book value.

## 21. Share capital

	Shares	Thousand rubles
Preferred shares at par value 0.12 Rubles		
Outstanding shares as of December 31, 2003	7,835,941,286	940,313
Authorized shares, not issued	7,164,058,714	
Less: treasury shares	4,112,276	(1,726)
Ordinary shares at par value 0.12 Rubles		
Outstanding shares as of December 31, 2003	32,298,782,020	3,875,854
Authorized shares, not issued	11,445,155,709	
Less: treasury shares	3,285,572	(3,287)
<b>Total share capital</b>		<b>4,811,154</b>

The state registration of amendments to the charter documents was completed on January 15, 2003. However, the change in charter capital was recognized as a material event, and in accordance with IAS 10, "Events After the Balance Sheet Date", was carried in the accompanying consolidated financial statements as of December 31, 2002.

The share capital account represents the authorized capital of the Company as stated in the charter documents. The Company had 32,298,782,020 ordinary shares and 7,835,941,286 Class A preferred shares as of December 31, 2003.

All shares have a par value of 0.12 Rubles per share. Of the share capital issued as of December 31, 2003 80 % was attributable to ordinary shares, and 20 % 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 shares 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.

Treasury shares are held by OOO "Tumentelecominvest" and ZAO "AKIB Pochtobank", the subsidiaries of the Company.

### 21. Share capital (continued)

In June 1997 the Company signed a Deposit agreement with The Bank of New York as a Depositary and Owners and Holders of American Depositary Receipts. At the same time, the Securities and Exchange Commission (SEC) registered a Level 1 ADR program for ordinary shares. In August 2002 the Company changed the Depositary by signing new Deposit agreement with JP Morgan Chase Bank as the successor Depositary.

In September 2002, the SEC registered the Level 1 ADR program for preference shares on the basis of a Depositary agreement signed between the Company, JP Morgan Chase Bank as a Depositary and Holders of American Depositary Receipts.

Each ADR is equal to 200 ordinary and preference shares correspondingly.

#### As at the end of 2003:

- 17,636,451 ADRs represented 3,527,290,200 deposited ordinary shares, which constituted 10.92 % of total ordinary shares issued.

- 4,959,754 ADRs represented 991,950,800 deposited preference shares, which constituted 2.47 % of the Charter capital of the Company.

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

	Ordinary shares		Preferred shares		Total
OA0 Svyazinvest	16,608,946,183	51%	-	-	16,608,946,183
Other legal entities	11,819,809,509	37%	5,658,346,773	72%	17,478,156,282
Individuals	3,870,026,328	12%	2,177,594,513	28%	6,047,620,841
<b>TOTAL</b>	<b>32,298,782,020</b>	<b>100%</b>	<b>7,835,941,286</b>	<b>100%</b>	<b>40,134,723,306</b>

## 22. Minority interest

	Shares	Thousand rubles
As of beginning of year	182,084	105,825
Minority interest in net income of subsidiaries	6,847	40,309
Minority interest in discontinued operation (see to Note 27)	(7,461)	35,950
Dividends paid to minority shareholders of subsidiaries	(2,015)	-
As of end of year	<b>179,455</b>	<b>182,084</b>

## 23. Loans and borrowings

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

	Effective interest rate	Maturity	2003	2002
<b>SHORT-TERM BORROWINGS</b>				
<b>Bank loans:</b>				
Bank loans (Rubles)	13-22%	2004	1,836,249	1,575,422
Bank loans (US Dollars)	8%	2004	103,297	105,129
Bank loans (Euro)	10%	2004	52,807	116,897
<b>Total bank loans</b>			<b>1,992,353</b>	<b>1,797,448</b>
Vendor financing (Euro)	8%	2004	69,303	-
Promissory notes (Rubles)	10-13.5%	2004	17,552	71,844
<b>Total short-term borrowings</b>			<b>2,079,208</b>	<b>1,869,292</b>
<b>LONG-TERM BORROWINGS</b>				
<b>Bank loans:</b>				
Bank loans (Rubles)	10%-20.5%	2007-2008	3,146,772	1,803,845
Bank loans (US Dollars)	8%	2007	191,856	445,542
Bank loans (Euro)	10%	2005-2007	580,165	993,138
Bank loans (other currencies)			-	-
<b>Total bank loans</b>			<b>3,918,793</b>	<b>3,242,525</b>
<b>Bonds (Rubles)</b>	<b>14.25%-17.5%</b>	<b>2005-2006</b>	<b>4,236,030</b>	<b>1,064,404</b>
<b>Vendor financing:</b>				
Vendor financing (Rubles)		2005	1,300	91,998
Vendor financing (US Dollars)	7%	2005-2007	498,536	694,809
Vendor financing (Euro)	8%	2005-2007	164,817	110,553
<b>Total vendor financing</b>			<b>664,653</b>	<b>897,360</b>
Restructured connection fees from customers (Rubles)	0%-30%	2011-2016	32,093	32,093
Promissory notes (Rubles)		2004-2007	183,641	114,796
Less: Current portion of long-term loans and borrowings		2004	(1,256,520)	(1,724,986)
<b>Total long-term borrowings</b>		<b>7,778,690</b>	<b>3,626,192</b>	

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

	Borrowings other than vendor financing	Vendor financing	Total
Overdue	13,650	292,172	305,822
2004	700,831	249,867	950,698
2005	4,215,927	42,919	4,258,846
2006	3,083,493	47,625	3,131,118
2007	324,563	32,070	356,633
2008 and thereafter	32,093	-	32,093
<b>TOTAL</b>	<b>8,370,557</b>	<b>664,653</b>	<b>9,035,210</b>

### Short-term borrowings

Most of short-term borrowings denominated in Rubles represent bank loans received to finance working capital. Most of these loans are collateralized with telecommunications equipment. The largest are:

#### Alfabank

In March 2003, the Company signed a credit contract № 4707 with OAO "Alfabank" in the amount of 300,000 thousand rubles. The loan maturity date is April 25, 2004. The annual interest rate on this loan was 14%. As of December 31, 2003 the Company's outstanding balance on this loan was 276,000. Property plant and equipment for the amount 369,000 thousand rubles were pledged as collateral for this loan.

In July 2003, the Company signed a credit contract № 225 with OAO "Alfabank" in the amount of 500,000 thousand rubles. The loan maturity date is May 31, 2005. The annual interest rate on this loan was 13.75%. As of December 31, 2003 the Company's outstanding balance on this loan was 250,000. Property plant and equipment for the amount 620,000 thousand rubles were pledged as collateral for this loan.

### Long-term bonds

In June 2003, the Company registered the issue of 3,000,000 interest-bearing bearer's bonds par value of 1 thousand Rubles each. Bonds have 6 coupons. Payments against the first coupon are made on the 182 th day from the date of issue; interest per other coupons are payable every subsequent 182 th day. Coupon interest rate is determined at 14.5 % per annum. The bonds mature in 1092 days from the date of issue, in July 2006.

In July 2003, the Company entered into a preliminary agreement with a Russian limited liability company (LLC) to conclude a binding agreement to purchase 1,400,000 of the Company's bonds. As a condition precedent to concluding the binding agreement, the Company's Board of Directors was to approve such purchase. The Company deposited 2,000,000 with the LLC as an advance for the future bond purchase. In October 2003, the parties agreed not to execute the binding agreement. Also in October 2003 the LLC returned the deposit with interest.

### Long-term borrowings

#### Sberbank

In August 2002, the Company signed a credit line contract № 113-НКЛ with AKB "Sberbank" in the amount of 390,000. The line is opened till August 13, 2005. The annual interest rate on this credit line reduced during 2003 from 19.5% to 14%. As of December 31, 2003 the Company's outstanding balance on this credit line was 390,000. Property plant and equipment for the amount 515,795 were pledged as collateral for this credit line.

In October 2002, the Company signed a credit line contract № 135-НКЛ with AKB "Sberbank" in the amount of 370,000. The line is opened till October 5, 2005. The annual interest rate on this loan reduced during 2003 from 19% to 14%. As of December 31, 2003 the Company's outstanding balance on this credit line was 370,000. Property plant and equipment for the amount 474,099 were pledged as collateral for this credit line.

In December 2002, the Company signed a credit line contract № 163-НКЛ with AKB "Sberbank" in the amount of 450,000. The line is opened till December 9, 2005. The annual interest rate on this loan reduced during 2003 from 19% to 14%. As of December 31, 2003 the Company's outstanding balance on this credit line was 450,000. Property plant and equipment for the amount 534,395 were pledged as collateral for this credit line.

In November 2003, the Company signed a credit line contract № 165-НКЛ with AKB "Sberbank" in the amount of 400,000. The line is opened till July 7, 2005. The annual interest rate on this loan was 12.5%. As of December 31, 2003 the Company's outstanding balance on this credit line was 400,000. Property plant and equipment for the amount 450,029 were pledged as collateral for this credit line.

In December 2003, the Company signed a credit line contract № 180-НКЛ with AKB "Sberbank" in the amount of 235,000. The line is opened till June 14, 2005. The annual interest rate on this loan was 12.5%. As of December 31, 2003 the Company's outstanding balance on this credit line was 235,000. Property plant and equipment for the amount 264,441 were pledged as collateral for this credit line.

#### Vneshtorgbank

In June 2003, the Company signed a credit contract № K-31/03 with OAO "Vneshtorgbank" in the amount of 5,392 thousand US dollars. The loans' maturity date is July 21, 2007. The annual interest rate on this loan was 7.65%. As of December 31, 2003 the Company's outstanding balance on this loan was 158,809 (including short-term portion of 39,702).

In December 2003, the Company signed a credit contract № K-109/03 with OAO "Vneshtorgbank" in the amount of 317,000. The loans' maturity date is June 24, 2005. The annual interest rate on this loan was 15%. As of December 31, 2003 the Company's outstanding balance on this loan was 317,000. Property plant and equipment for the amount 572,022 were pledged as collateral for this loan.

#### Promstroybank

In December 2003, the Company signed a credit contract № 174/03 with OAO "Promstroybank" in the amount of 300,000. The loans' maturity date is June 21, 2005. The annual interest rate on this loan was 15%. As of December 31, 2003 the Company's outstanding balance on this loan was 300,000. Property plant and equipment for the amount 366,578 were pledged as collateral for this loan.

#### Vnesheconombank

In 1995–1996, the Russian Ministry of Finance (hereinafter, "Minfin") provided long-term financing to the Company to purchase telecommunications equipment from various foreign vendors. Vnesheconombank acted as the Company's lending agent on be-

half of Minfin. Initially the agreements were denominated in Deutschmark (DM). After transition to Euro, the loans were converted to Euro. The interest under these agreements is accrued at LIBOR, plus 6.5%. The loans are not collateralized. As of December 31, 2003 the Company's principal debt outstanding balance on these loans was in total 215,723. The loans' maturity date is July 2007.

#### National Reserve Bank

In October 2003, the Company signed a credit contract № 959-DG with АКБ "National Reserve Bank" in the amount of 3,154 thousand euros. The loans' maturity date is October 13, 2006. The annual interest rate on this loan was 9.75%. As of December 31, 2003 the Company's outstanding balance on this loan was 106,551 (including short-term portion of 53,027). Property plant and equipment for the amount 109,588 were pledged as collateral for this loan.

#### Promissory notes

In addition, OAO "Uralsvyazinform" issued promissory notes in amount of 201,192 as of December 31, 2003 which have short-term portion of 17,551.

#### Vendor financing

##### Alcatel

The Company entered into several agreements with Alcatel, under which Alcatel delivered and installed telecommunication equipment. The related liability is denominated in Euro. Part of these loans bears interest at 4.5-6.5% per annum. Interest on financing with below market rates is accrued at a weighted average interest rate on the Company's interest bearing borrowings obtained in appropriate periods and denominated in Euro, which approximated 6% per annum.

Vnesheconombank, London Forfeiting Company PLC and Drezdner Bank purchased the amounts due to Alcatel under the vendor financing agreement, including accrued interest and penalties in 2003.

In 2001, the Company entered into several agreements with Siemens AG, under which Siemens AG delivered telecommunication equipment to the Company. The amounts payable under these agreements are denominated in Euro. The agreements don't provide for interest payments thus the amount of liability as at December 31, 2003 represents the present value of future payments. Interest is accrued at a weighted average interest rate on the Company's interest bearing borrowings obtained in appropriate periods and denominated in Euro, which approximated 6% per annum.

#### Other

Other vendor financing comprises amounts payable to various vendors and includes several overdue amounts for which the date of legal extinguishment of a liability has not occurred as of December 31, 2003.

## 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
Within one year	573,763	357,801	562,046	525,891
After one year but not more than five years	1,113,746	753,863	577,730	328,866
Total minimum lease payments	1,687,509		1,139,776	
Less amounts representing finance charges	(575,845)		(285,019)	
Present value of minimum lease payments	<b>1,111,664</b>	<b>1,111,664</b>	<b>854,757</b>	<b>854,757</b>

In 2003, the Company's primary lessor was OAO "RTC-Leasing". In 2003, effective interest rate on these liabilities ranged from 18% to 41% per annum.

Pursuant to agreements concluded with OAO "RTC-Leasing", 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.

## 25. Trade accounts payable and accrued liabilities

The Company's trade accounts payable and other current liabilities comprised:

	2003	2002
Trade accounts payable	544,013	358,869
Advances received from subscribers	630,971	453,457
Accounts payable for capital investments	1,538,192	838,263
Salaries and wages payable	551,518	360,991
Other	559,465	678,224
<b>Total</b>	<b>3,824,159</b>	<b>2,689,804</b>

## 26. Tax and social security payable

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

	2003	2002
Value-added tax	441,832	401,118
Income tax	152,737	46,348
Property tax	63,084	50,009
Personal income tax	46,892	30,095
Sales tax	18,606	33,016
Unified social tax	45,291	61,476
Road users tax	-	548
Other	25,573	37,867
<b>TOTAL</b>	<b>794,015</b>	<b>660,477</b>

## 27. Discontinued Operations

As part of management's efforts to concentrate on the wireless segment on GSM standard and to increase profitability of the wireless segment, the Company discontinued a cellular operator that provides services using NMT standard. The operations on NMT standard were conducted through ZAO "Uralwestcom". In April 2004 the Company's Board of Directors approved a decision to sell 51% share in ZAO "Uralwestcom" to Russian Telecommunication Development Holding Corporation for 3.5 million US dollars. The disposal of ZAO "Uralwestcom" was completed June 2004.

The result of operations of ZAO "Uralwestcom" was included in the accompanying consolidated statement of operations for the year ended December 31, 2003 and reported as discontinued operations. The corresponding result of operations of the discontinued operation for the years ended December 31, 2002 is represented in the accompanying statements of operations, to conform to the current year presentation.

The accompanying statement of operations include reconciliation of continuing and discontinuing operations of the Company:

	2003		
	Continuing Operations	Discontinuing Operations	Company as a whole
<b>Revenues</b>	<b>21,843,469</b>	<b>162,808</b>	<b>22,006,277</b>
<b>Operating expenses</b>			
Wages, salaries, other benefits and payroll taxes	(6,268,258)	(35,197)	(6,303,455)
Impairment of property, plant and equipment	(19,286)	-	(19,286)
Depreciation and amortization	(2,624,295)	(27,672)	(2,651,967)
Materials, repairs, maintenance and utilities	(2,001,508)	(18,122)	(2,019,630)
Taxes other than income tax	(382,052)	(2,758)	(384,810)
Interconnection charges – international	(68,566)	-	(68,566)
Interconnection charges – domestic	(3,269,838)	(26,579)	(3,296,417)
Interconnection charges – associates	-	-	-
Bad debts expense	(605,845)	(960)	(606,805)
Loss on disposal of property, plant and equipment	(76,325)	3,018	(73,307)
Other operating expenses	(3,080,178)	(64,743)	(3,144,921)
<b>Total operating expenses</b>	<b>(18,396,151)</b>	<b>(173,013)</b>	<b>(18,569,164)</b>
<b>Operating income (loss)</b>	<b>3,447,318</b>	<b>(10,205)</b>	<b>3,437,113</b>
Income from associates	29,056	-	29,056
Interest expenses, net	(1,308,787)	(7,574)	(1,316,361)
Income from other investments	3,547	-	3,547
Foreign exchange loss, net	(4,080)	2,568	(1,512)
Net monetary gain	-	-	-
<b>Income before taxation and minority interest</b>	<b>2,167,054</b>	<b>(15,211)</b>	<b>2,151,843</b>
<b>Income tax expense, net</b>	<b>(928,516)</b>	<b>(15)</b>	<b>(928,531)</b>
<b>Net income before minority interest</b>	<b>1,238,538</b>	<b>(15,226)</b>	<b>1,233,312</b>
<b>Minority interest</b>	<b>(6,847)</b>	<b>7,461</b>	<b>614</b>
<b>Net income</b>	<b>1,231,691</b>	<b>(7,765)</b>	<b>1,223,926</b>
Dividends on preferred shares	(144,837)	-	(144,837)
<b>Net income attributable to ordinary shareholders</b>	<b>1,086,854</b>	<b>(7,765)</b>	<b>1,079,089</b>
<b>Basic and diluted earnings per share (Russian Rubles)</b>	<b>0.034</b>		<b>0.034</b>

The accompanying statement of operations include reconciliation of continuing and discontinuing operations of the Company:

	2002, as restated		
	Continuing Operations	Discontinuing Operations	Company as a whole
<b>Revenues</b>	<b>17,402,082</b>	<b>295,781</b>	<b>17,697,863</b>
<b>Operating expenses</b>			
Wages, salaries, other benefits and payroll taxes	(5,467,704)	(36,118)	(5,503,822)
Impairment of property, plant and equipment	(87,596)	-	(87,596)
Depreciation and amortization	(2,379,532)	(21,235)	(2,400,767)
Materials, repairs, maintenance and utilities	(1,421,399)	(31,651)	(1,453,050)
Taxes other than income tax	(467,161)	(5,731)	(472,892)
Interconnection charges – international	(38,944)	-	(38,944)
Interconnection charges – domestic	(2,230,874)	(51,330)	(2,282,204)
Interconnection charges – associates	-	-	-
Bad debts expense	(86,552)	646	(85,906)
Loss on disposal of property, plant and equipment	(109,810)	(2,586)	(112,396)
Other operating expenses	(2,793,527)	(41,596)	(2,835,123)
<b>Total operating expenses</b>	<b>(15,083,099)</b>	<b>(189,601)</b>	<b>(15,272,700)</b>
<b>Operating income (loss)</b>	<b>2,318,983</b>	<b>106,180</b>	<b>2,425,163</b>
Income from associates	4,840	-	4,840
Interest expenses, net	(765,993)	(10,453)	(776,446)
Income from other investments	(6,319)	-	(6,319)
Foreign exchange loss, net	(385,987)	(3,214)	(389,201)
Net monetary gain	595,010	7,526	602,536
<b>Income before taxation and minority interest</b>	<b>1,760,534</b>	<b>100,039</b>	<b>1,860,573</b>
<b>Income tax expense, net</b>	<b>(762,114)</b>	<b>(26,672)</b>	<b>(788,786)</b>
<b>Net income before minority interest</b>	<b>998,420</b>	<b>73,367</b>	<b>1,071,787</b>
<b>Minority interest</b>	<b>(40,309)</b>	<b>(35,950)</b>	<b>(76,259)</b>
<b>Net income</b>	<b>958,111</b>	<b>37,417</b>	<b>995,528</b>
Dividends on preferred shares	(71,307)	-	(71,307)
<b>Net income attributable to ordinary shareholders</b>	<b>886,804</b>	<b>37,417</b>	<b>924,221</b>
<b>Basic and diluted earnings per share (Russian Rubles)</b>	<b>0.029</b>		<b>0.029</b>

The net cash flows for the years ended December 31, 2003 and 2002 pertaining to the discontinued business as reported in the accompanying consolidated financial statements, were as follows:

	2003	2002
<b>Balance of cash at the beginning of the year</b>	<b>3,250</b>	<b>3,840</b>
Net cash flows from operating activities	6,210	64,191
Net cash flows from investing activities	(4,517)	(29,450)
Net cash flows from financing activities	(2,350)	(35,331)
<b>Balance of cash as of the end of the reporting period</b>	<b>2,593</b>	<b>3,250</b>

Total assets and liabilities of discontinued operations as of December 31, 2003 and December 31, 2002 as reported in the accompanying consolidated financial statements, were as follows:

	2003	2002
<b>NON-CURRENT ASSETS:</b>		
Property, plant and equipment, net	220,510	238,239
Other non-current assets	13,644	13,326
<b>Total non-current assets</b>	<b>234,154</b>	<b>251,565</b>
<b>Current assets</b>	<b>44,402</b>	<b>37,635</b>
<b>Total assets</b>	<b>278,556</b>	<b>289,200</b>
<b>NON-CURRENT LIABILITIES:</b>		
Long-term borrowings	(28,851)	-
Deferred income tax liability	(32,000)	(32,151)
<b>Total non-current liabilities</b>	<b>(60,851)</b>	<b>(32,151)</b>
<b>Total current liabilities</b>	<b>(47,370)</b>	<b>(71,488)</b>
<b>Total liabilities</b>	<b>(108,221)</b>	<b>(103,639)</b>
<b>Minority interest</b>	<b>(83,431)</b>	<b>(90,925)</b>
<b>Total net assets from discontinued operations</b>	<b>86,904</b>	<b>94,582</b>

## 28. Pension Plans and Employee Benefits

The Company performed a preliminary actuarial estimate of pension and other post employment and post retirement benefits in June 2004. The valuation of pension liabilities and expenses was made as of January 1, 2002, December 31, 2002 and December 31, 2003.

The Company restated its consolidated financial statements as of December 31, 2002 in the following way:

	2003
Pension liabilities in the consolidated balance sheet as of December 31, 2001	nil
Restated Pension liabilities	280,000
Total adjustment	280,000
Net expense for pension plan in consolidated statement of operations for the year ended December 31, 2002	nil
Restated Net expense for pension plan	165,000
Total adjustment	165,000

The postemployment and post retirement program of the Company mainly consists of the occupational pension plan. For most participants, this is a defined benefit plan, under which the participants accrue pension entitlements on the basis of a formula, which is specific to each branch of the Company. According to the formula, the pension benefit is dependent on several parameters including the relative pay of participants and their past service. There were approximately 35,500 employees eligible to some part of the postemployment and post retirement program of the Company, of which 16,800 active participants to the defined benefit pension plan, as at December 31, 2003 (as at December 31, 2002: 35,900 employees of which 17,100 participating in the defined benefit pension plan).

The defined benefit pension plan provides old age retirement pension and disability pension. The plan's old age retirement pension is conditional to the mem-

ber qualifying for the State old age pension. The Company also provides several long-term employee benefits such as a death-in-service benefit and lump-sum payments upon retirement of a defined benefit nature.

Additionally the company provides financial support, of a defined benefit nature, to its old age and disabled pensioners.

For the head office, the cellular branch in Perm and the branches in Chelyabinsk and Perm, the company provides pensions based on defined contribution principles. During 2003 the company made 9.1 mln. rubles (2002: 8.3 mln. rubles) of contributions to such defined contribution pension arrangements, which are in addition to the defined benefit plan related service cost shown below.

For the purposes of June 2004 valuation, members' census data as at January 1, 2002, December 31, 2002 and December 31, 2003 was collected for all branches of the Company.

The amounts recognized in the consolidated balance sheet are as follows:

	2003	2002
Present value of defined benefit obligation (DBO)	1,249,000	1,185,000
Fair value of plan assets	(112,000)	(75,000)
Present value of unfunded obligations	1,137,000	1,110,000
Unrecognised actuarial gains/(losses)	152,000	10,000
Unrecognised past service (cost) / asset	(680,000)	(675,000)
<b>Net liability in the balance sheet</b>	<b>609,000</b>	<b>445,000</b>
Employees' average remaining working life (years)	12	12

The amounts recognized in the consolidated statement of operations, which included in "Wages, salaries, other benefits and payroll taxes", are as follows:

	2003	2002
Service cost	30,000	30,000
Interest cost	111,000	100,000
Expected return on plan assets	(8,000)	(5,000)
Net actuarial losses/(gains) recognised in year	-	-
Amortisation of past service cost	75,000	75,000
Vested past service cost	-	-
<b>Net expense for the DB pension plan</b>	<b>208,000</b>	<b>200,000</b>
<b>Contribution to the defined contribution schemes</b>	<b>9,000</b>	<b>8,000</b>
<b>Net expense for pension plan (total)</b>	<b>217,000</b>	<b>209,000</b>

Movements in the net liability recognized in the consolidated balance sheet are as follows:

	2003	2002
Net liability at the start of the year	445,000	280,000
Net expense recognised in the statement of operations	208,000	200,000
Contributions	(44,000)	(35,000)
<b>Net liability at the end of the year</b>	<b>609,000</b>	<b>445,000</b>

Principal actuarial assumptions at the valuation dates:

	01/01/2002	31/12/2002	31/12/2003
Discount rate	9.18% p.a.	9.18% p.a.	9.18% p.a.
Expected return on plan assets	9.58% p.a.	9.51% p.a.	9.26% p.a.
Salary increases	9.18% p.a.	9.18% p.a.	9.18% p.a.
Relative pay increase (career progression)	1% p.a.	1% p.a.	1% p.a.
Rate used for calculation of annuity value	6% p.a.	6% p.a.	6% p.a.
Staff turnover	5% p.a.	5% p.a.	5% p.a.
Mortality tables (source of information)	USSR 1985–1986	USSR 1985–1986	USSR 1985–1986

Movements in the pension account:

	2003	2002
Fair value of plan assets at year start	75,000	35,000
Actual return on plan assets	13,000	10,000
Employer contribution	44,000	35,000
Benefits paid	(20,000)	(5,000)
<b>Fair value of plan assets at end of year</b>	<b>112,000</b>	<b>75,000</b>

## 29. Commitments and Contingencies

### Economic and political environment in Russia

The present status of the Russian economy continues to display certain characteristics consistent with that of a market in transition. These attributes have in the past included higher than normal historic inflation, lack of liquidity in capital markets, and the existence of currency controls that 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.

The Company could be affected, for the foreseeable future, by these risks and their consequences. As a result, there are significant uncertainties that may affect future operations, the recoverability of the Company's assets, and the ability of the Company to maintain or pay its debts as they mature. The accompanying financial statements do not include any adjustment that may result from these uncertainties. Such adjustments will be carried in the financial statements as and when they occur and become measurable.

### **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. Due to the lack of time and examination of findings by tax authorities it is unknown how many aspects of the new tax code will be interpreted. 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 Company believes that it has paid or accrued all taxes that are applicable. In cases where interpretations of specific rules are unclear, the Company has accrued tax liabilities based on management's best estimate. The effect of possible discrepancies in interpreting the legal requirements may approximate 8,508. 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 of December 31, 2003.

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 of December 31, 2003.

Currently the Company is inspected by local tax authority. The effect of possible disagreements that may arise under this inspection could not be determined. If needed management of the Company intends to defend its position in court.

### **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.

Property, plant and equipment insured as of December 31, 2003, totaled 6,421,683 (2002 – 3,568,125) (see Note 10).

### **Litigations, 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.

Currently the Company expects notification of claim from GU "Baykalovsky Ieshos" amounted 30,196. In case if court accepts this claim, management of the Company intends to demand decrease of amount of the claim.

In 2003 the Company filed a claims to Ministry of Labor and Social protection to recover tariff compensation related to services rendered to privileged customers in 2001 and 2002 amounted 96,014. By the decision of Moscow arbitration court these claims were satisfied in 2004. In June 2004 the Company filed next claim to Ministry of Labor and Social protection to recover tariff compensation related to services rendered to privileged customers in 2003 amounted 40,416. Management believes that this claim will be also satisfied.

### **Finance leasing**

In 2003 the Company entered into several finance 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 74,703.

### **Capital commitments**

#### **Oracle E-business**

Under its budget for 2004 the Company plans to invest into further installation of Oracle E-business about 370 mln. rubles.

#### **Property, plant and equipment**

At December 31, 2003 the Company has commitments of 1,202,927 for capital investments into modernization and expansion of its network.

#### **Guarantees issued**

As of December 31, 2003 the Company issued the guarantees of third party' obligations for the amount of 2,083,213 (December 31, 2002 – 705,553).

### 30. Related parties

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

	2003	2002
<b>DUE FROM RELATED PARTIES:</b>		
ZAO "Telefonnaya kompaniya – Ural"	810	484
ZAO "Uralskaya telefonnaya kompaniya"	7,485	5,534
ZAO "Teleross-Ekaterinburg"	238	120
ZAO "Ural-Teleservis"	877	1,518
ZAO "Kurganskiy sotoviy telefon"	396	226
ZAO "Teleross-Tyumen"	157	502
ZAO "Rostelegraph"	48	-
<b>TOTAL</b>	<b>10,011</b>	<b>8,384</b>
<b>DUE TO RELATED PARTIES:</b>		
ZAO "Teleross-Ekaterinburg"	-	136
ZAO "Telefonnaya kompaniya – Ural"	771	-
ZAO "Uralskaya telefonnaya kompaniya"	2,767	112
ZAO "Ural-Teleservis"	11	11
ZAO "Kurganskiy sotoviy telefon"	97	34
OAo "Rostelecom"	344,169	287,577
OAo "RTC-Leasing"	1,530,041	887,528
OAo "Sviazinvest"	1,421	1,421
<b>TOTAL</b>	<b>1,879,277</b>	<b>1,176,819</b>

Consolidated statement of operations includes the following transactions for the year ended December 31, 2003 and 2002:

	2003	2002
<b>SALES TO RELATED PARTIES:</b>		
ZAO "Telefonnaya kompaniya – Ural"	6,756	4,769
ZAO "Uralskaya telefonnaya kompaniya"	52,597	18,231
ZAO "Teleross-Ekaterinburg"	2,182	1,501
ZAO "Ural-Teleservis"	2,717	3,010
ZAO "Kurganskiy sotoviy telefon"	352	468
ZAO "Teleross-Tyumen"	3,208	2,964
OAo "Rostelecom"	350,493	10,511
ZAO "Rostelegraph"	48	-
<b>TOTAL</b>	<b>418,353</b>	<b>41,454</b>

<b>PURCHASES FROM RELATED PARTIES:</b>		
ZAO "Telefonnaya kompaniya – Ural"	5,773	2,626
ZAO "Uralskaya telefonnaya kompaniya"	21,784	4,415
ZAO "Kurganskiy sotoviy telefon"	149	104
OAo "Rostelecom"	2,001,136	1,664,321
OAo "Sviazinvest"	61,519	38,203
OAo "RTC-Leasing"	813,942	804,981
<b>TOTAL</b>	<b>2,904,303</b>	<b>2,514,650</b>

Sales to and purchases from related parties are made at normal market prices.

### OAQ Svyazinvest

The Company regards OAQ 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.

### OAQ Rostelecom

Rostelecom, a majority owned subsidiary of Svyazinvest, is the primary provider of domestic long distance and international telecommunications services in the Russian Federation. The Company has negotiated agreements with Rostelecom for interconnection of domestic long distance and international telecommunications, and other services, including lease of channels.

In 2003, Rostelecom reformed its system of settlements with regional operators for domestic long-distance traffic. Prior to July 31, 2003, settlements between the Company and Rostelecom were based on the integral settlement rate (ISR) per one minute of domestic transit traffic sent through 50 km of Rostelecom networks.

The ISR contains two components – a linear component and a termination charge, which is calculated based on the weighted average of incoming and outgoing traffic. The ISR was set once a year by the Ministry of Antimonopoly Policies and Entrepreneurship Support based on the traffic data for the preceding year and did not reflect the real economic benefits and costs associated with traffic changes in subsequent periods.

Beginning from August 1, 2003, the Company began to settle with Rostelecom using the linear settlement rate (LSR) which includes the cost of Rostelecom carrying and benefits to the Company in terminating domestic long-distance traffic. LSR implementation allowed the Company to receive revenues for terminating domestic long-distance traffic based on actual volumes of traffic in the current period, which increased revenue by 314,700.

### RTC-Leasing

OAQ RTC-Leasing was a subsidiary of OAQ Rostelecom at the beginning of the year. OAQ RTC-Leasing purchases telecommunications equipment from Russian and foreign vendors and leases the equipment. The Company's obligations under capital leases to OAQ RTC-Leasing included in accompanying consolidated balance sheet as at December 31, 2003 amounted to 835,542 of which 721,490 is the principal and 114,051 is the accrued interest.

The Company issued guarantees for certain loans received by RTC-Leasing from Sberbank for total amount of 1,833,695.

### 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 8% of trade accounts receivable as of December 31, 2003. Amounts outstanding from government subscribers as of December 31, 2003, amounted to 186,570.

### Associates

The Company provided services to associates, including connection to public network, and rent of space for equipment and offices. The total effect of these transactions on the Company's financial position is insignificant.

The Company issued guarantees for certain loans received by OOO "Uzhno-uralsky sotoviy telefon" from OAQ "Chelyndbank" for total amount of 29,250.

Non-commercial partnership Center for Research of Problems in Development of Telecommunications Non-commercial partnership Center for Research of the Problems in Development of Telecommunications (hereinafter "the Partnership") is an entity related to OAQ 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 income (expenses) in accompanying consolidated statement of operations for the year ended December 31, 2003 amounted to 188,992 (2002 – 147,000).

### NPF "Telecom-Soyuz"

The Company has concluded several pension plans agreements with NPF "Telecom-Soyuz" which is a related party of Svyazinvest (see Note 28 "Pension Plans and Employee Benefits"). Payments to this pension fund in 2003 amounted 35 955 ( 2002 – 29,575).

### Compensation of the Company's management

The Company's Board of Directors included the following persons during the year:

Chairman	Belov V.E.
Member of board of directors	Rybakin V.I.
Member of board of directors	Adjalov V.I.
Member of board of directors	Bilibin Y.A.
Member of board of directors	Grigorieva A.B.
Member of board of directors	Jolobov V.S.
Member of board of directors	Kozin V.V.
Member of board of directors	Levkovsky D.V.
Member of board of directors	Perminov L.M.
Member of board of directors	Chernogorodsky C.V.
Member of board of directors	Urpalov S.Y.

In 2003, compensation to the members of the Board and to the Company's management totaled 45,454 (2002 – 17,989).

## 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, 2003:

	< 1 year	1-5 years	> 5 years	Total
<b>FIXED RATE</b>				
Short-term borrowings	2,045,474	-	-	2,045,474
Long-term borrowings	1,256,520	7,710,876	-	8,967,396
Finance lease obligations	357,801	753,863	-	1,111,664
<b>FLOATING RATE</b>				
Short-term borrowings	33,734	-	-	33,734
Long-term borrowings	-	35,721	32,093	67,814
<b>TOTAL</b>	<b>3,693,529</b>	<b>8,500,460</b>	<b>32,093</b>	<b>12,226,082</b>

Year ended December 31, 2002:

	< 1 year	1-5 years	> 5 years	Total
<b>FIXED RATE</b>				
Short-term borrowings	1,869,292	-	-	1,869,292
Long-term borrowings	1,724,986	3,501,932	-	5,226,918
Finance lease obligations	525,891	328,866	-	854,757
<b>FLOATING RATE</b>				
Short-term borrowings	-	-	-	-
Long-term borrowings	-	92,167	32,093	124,260
<b>TOTAL</b>	<b>4,120,169</b>	<b>3,922,965</b>	<b>32,093</b>	<b>8,075,227</b>

Interest on financial instruments classified as floating rate is repriced at intervals less than one year.

Interest on financial instruments classified as fixed rate is fixed until maturity of the instrument.

The other financial instruments of the Company that are not included into the above tables are non-interest bearing and are therefore not subject to interest rate risk.

## 32. Subsequent events

### Contracts

#### (1) Loan agreement with Gazprombank

On January 13, 2004, OAO "Uralsvyazinform" entered into a loan agreement with Gazprombank for 490,000. The loan matures on May 27, 2004. OAO "Uralsvyazinform" pays interest on loan to the bank at the rate of 12 % per annum. The loan is collateralized with telecommunications equipment valued at 596,400 thousand rubles.

#### (2) Loan agreement with Sberbank

On January 30, 2004, OAO "Uralsvyazinform" entered into a loan agreement with Sberbank for 173,000. The loan matures on January 29, 2009. OAO "Uralsvyazinform" pays interest on loan to the bank at the rate of 14.5 % per annum. The loan is collateralized with telecommunications equipment valued at 198,112 thousand rubles.

#### (3) Loan agreement with Promstroybank

On May 26, 2004, OAO "Uralsvyazinform" entered into a loan agreement with Promstroybank for 400,000. The loan matures on May 26, 2005. OAO "Uralsvyazinform" pays interest on loan to the bank at the rate of 13.5 % per annum. The loan is not collateralized.

### Finance lease agreements with OAO RTC-Leasing

In 2004, the Company entered into several finance lease agreements with OAO RTC-Leasing with the respective non-discounted future cash flows totaling approximately 1,115 million Rubles.

### Dividends

On May 20, 2004, the Company's Board of Directors approved dividends for 2003 in the amount of 0.01848 rubles per preferred share and 0.01 rubles per ordinary share. Total dividends declared amounted to 144,837 and 322,988 for preferred and ordinary shares, respectively. Dividends for the year ended December 31, 2003, are payable during 2004 and shall be carried in the financial statements for the year ended December 31, 2004 (see also Note 9, "Dividends Paid and Proposed").

### Tariffs for telecom services

The Company has not changed the tariffs for monthly subscribers fees for local services and long distance calls – national in 2004. There was increase in tariff for telegraph services by 20% for Ural region and by 30% for Northern regions effective from January 10, 2004. Tariffs for long distance call – international were changed on April 1, 2004: the tariffs increased by 12% for individuals, the tariffs decreased by 15% for commercial entities. The tariff for Internet decreased by 15% in Khanty-Mansiysk's branch of the Company, and remained on the same level for other branches of the Company. The tariffs for cellular communication services decreased by 25-30% starting from February till May 2004.

### Telecommunication Law

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 establish 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 how the new law will affect the Company.

### Decrease of VAT rate

Effective from January 2004 there was VAT rate decrease from 20% to 18%.

# Information for shareholders

## General enquiries

For enquiries on all matters not covered below please contact:

**Adresse**

68, Lenin St., Perm, 614096, Russia

**Telephone**

+7 (3422) 136 598  
+7 (3422) 343 872

**Facsimile**

+7 (3422) 343 336

**E-mail**

investor@usi.ru

## IR Department Uralsvyazinform

## American Depositary Receipts (ADR)

Uralsvyazinform common and preferred shares are listed on the Berlin and Frankfurt Stock Exchanges. In the US they trade on OTC market in the form of Level 1 American Depositary Receipts. Ticker symbols are UVYZY for common shares, UVYPY for preferred shares.

Each ADR, both common and preferred is equivalent to 200 ordinary or preferred shares. Enquiries regarding ADR holders' accounts and dividend payments should be directed to Depositary:

### JP Morgan Chase Bank

Trinity Tower, 9 Thomas More Street, London E1W 1YT  
Tel: +44 20 7777 2020,  
Fax: +44 20 7777 2989

## Voting at the Annual General Meeting

On June 24, 2004, Uralsvyazinform will hold its 2003 Annual General Meeting in Ekaterinburg, Russia. ADR holders could authorize JP Morgan Chase Bank for regulation of ADR voting. For that ADR holders should fill and return the voting paper in accordance with published instructions.

### Holders of common and preferred shares

Administrative enquiries concerning shareholdings, such as dividend payments and notification of change of address, should be addressed to

### OAO Registrator-Svyaz

15A, Kalanchevskaya St.,  
Moscow, 107014, P.O. Box 128  
Telephone: +7 (095) 975 36 05  
Web-site: [www.regsv.ru](http://www.regsv.ru)  
E-mail: [regsw@asvt.ru](mailto:regsw@asvt.ru)

Shareholders can obtain details about their shareholdings through transfer-agent services provided by:

#### **Perm**

ZAO VRK (Shareholder Register Services)  
Perm branch  
61, Kim Street, Perm 614107 Russia  
Telephone: **+7 (3422) 603 494**

#### **Ekaterinburg**

ZAO VRK (Shareholder Register Services)  
Ekaterinburg branch  
28, Lenin Avenue, Ekaterinburg 620014 Russia  
Telephone: **+7 (3432) 766 723**

#### **Kurgan**

ZAO VRK (Shareholder Register Services)  
Kurgan branch  
Office 35, 9, Pitchugin Street, Kurgan 640018 Russia  
Telephone: **+7 (3522) 418 589**  
**+7 (3522) 418 859**

#### **Tyumen**

ZAO VRK (Shareholder Register Services)  
Tyumen branch  
2/5, 8 marta Street, Tyumen 625000 Russia  
Telephone: **+7 (3452) 395 434**  
**+7 (3452) 395 433**  
**+7 (3452) 296 253**

#### **Share price information**

Uralsvyazinform share price information is available from the RTS web-site at [www.rts.ru](http://www.rts.ru)

#### **Website**

[www.uralsviainform.ru](http://www.uralsviainform.ru)

#### **Financial calendar**

Annual General Meeting date:  
**June 25, 2004**

Announcement of 1H2004 results:  
**August 15, 2004**

Announcement of 2004 preliminary results:  
**December 15, 2004**

**Uralsvyazinform**  
[www.uralsvyazinform.ru](http://www.uralsvyazinform.ru)

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[www.roslinknet.com](http://www.roslinknet.com)

**Uralsvyazinform**  
[www.uralsvazinform.ru](http://www.uralsvazinform.ru)

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