MEGAFON

Condensed Consolidated Financial Statements
(Unaudited)

Three and nine months ended September 30, 2012 and 2011
With Report of Independent Accountants

Ernst & Young LLC
Sadovnicheskaya Nab., 77, bld. 1
Moscow, 115035, Russia
Tel: +7 (495) 705 9700
+7 (495) 755 9700
Fax: +7 (495) 755 9701
www.ey.com/Russia

ООО «Эрнст энд Янг»
Россия, 115035, Москва
Садовническая наб., 77, стр. 1
Тел: +7 (495) 705 9700
+7 (495) 755 9700
Факс: +7 (495) 755 9701
www.ey.com/Russia

Report of Independent Accountants

The Board of Directors and Shareholders
OJSC MegaFon

We have reviewed the condensed consolidated balance sheet of OJSC MegaFon and subsidiaries as of September 30, 2012, and the related condensed consolidated statements of comprehensive income and cash flows for the three and nine months ended September 30, 2012 and 2011. This condensed financial information is the responsibility of the Company's management.

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

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

We have previously audited, in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheets of OJSC MegaFon and subsidiaries as of December 31, 2011, 2010 and 2009, and the related consolidated statements of comprehensive income, shareholders' equity, and cash flows for the years then ended (not presented herein); and in our report dated May 14, 2012, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2011, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

Ernst & Young LLC

November 8, 2012

Contents

MegaFon

Condensed Consolidated Balance Sheets

(In millions of Rubles)

	Note	September 30, 2012 (Unaudited)	December 31, 2011
Assets			
Current assets:			
Cash and cash equivalents		**17,012**	2,887
Short-term investments		**2,213**	84,509
Accounts receivable, net of allowances of 1,487 and 1,447		**10,177**	9,626
Inventory		**4,924**	4,551
Prepaid income taxes		**4,313**	6,957
VAT receivable		**1,910**	1,779
Deferred tax assets		**2,266**	1,972
Prepaid expenses and other current assets		**6,694**	8,012
Total current assets		**49,509**	120,293
Long-term bank deposits		**2**	2,002
Property, plant and equipment, net of accumulated depreciation of 193,568 and 164,765		**213,824**	223,718
Goodwill and intangible assets:			
Goodwill	3, 4	**23,950**	15,393
Intangible assets, net of accumulated amortization of 28,177 and 24,817		**17,876**	19,672
Deferred tax assets		**784**	712
Deferred finance charges	10	**1,255**	729
Other non-current assets	14	**2,132**	949
Total assets		**309,332**	383,468

MegaFon

Condensed Consolidated Balance Sheets (continued)

(In millions of Rubles)

	Note	September 30, 2012 (Unaudited)	December 31, 2011
Liabilities			
Current liabilities:			
Accounts payable		**12,383**	9,997
Accounts payable to equipment suppliers		**3,850**	8,115
Current portion of liability for marketing related licenses		**506**	402
Current portion of liability for deferred and contingent consideration	12	**2,845**	2,550
Accrued compensation		**4,012**	5,360
Subscribers' prepayments		**7,288**	7,903
Taxes payable		**3,235**	3,056
VAT payable		**7,649**	2,965
Deferred revenue		**1,201**	954
Short-term loans and current portion of long-term debt	10	**28,494**	7,415
Other current liabilities		**2,336**	1,256
Total current liabilities		**73,799**	49,973
Debt, less current portion	10	**130,620**	36,294
Deferred tax liabilities		**10,637**	10,543
Asset retirement obligations		**5,567**	5,248
Liability for marketing related licenses, less current portion		**261**	621
Liability for deferred and contingent consideration, less current portion		—	1,829
Deferred revenue, less current portion		**1,193**	1,569
Other non-current liabilities		**628**	759
Total liabilities		**222,705**	106,836
Equity			
MegaFon shareholders' equity:			
Ordinary shares (par value of 0.1 Rubles, 620,000,000 and 620,000,200 shares issued; 530,720,500 and 620,000,200 shares outstanding)	9	**581**	581
Treasury shares (89,279,500 ordinary shares at cost)	9	**(63,883)**	—
Reserve fund		**17**	17
Additional paid-in capital		**13,852**	13,852
Retained earnings	9	**135,987**	261,950
Accumulated other comprehensive loss		**(557)**	(291)
Total MegaFon shareholders' equity		**85,997**	276,109
Noncontrolling interests		**630**	523
Total equity		**86,627**	276,632
Total liabilities and equity		**309,332**	383,468

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
See report of independent accountants

MegaFon

Condensed Consolidated Statements of Comprehensive Income

(In millions of Rubles, except share and per share amounts)
(Unaudited)

	Note	Three months ended September 30, 2012	Three months ended September 30, 2011	Nine months ended September 30, 2012	Nine months ended September 30, 2011
Revenues	5	**71,234**	63,433	**201,098**	177,146
Cost of revenues	6	**17,349**	15,423	**50,145**	42,266
Sales and marketing expenses	7	**5,306**	6,498	**15,727**	15,230
Operating expenses	8	**16,441**	14,965	**49,288**	44,060
Depreciation		**11,921**	10,243	**35,489**	31,253
Amortization		**1,951**	1,238	**4,594**	3,728
Operating income		**18,266**	15,066	**45,855**	40,609
Other income/(expense):					
Interest expense	10	**(2,543)**	(271)	**(4,549)**	(726)
Interest income		**155**	831	**1,047**	2,606
Other gain/(loss), net		**58**	122	**(9)**	83
Gain/(loss) on derivatives, net		—	13	—	(27)
Foreign currency exchange gain/(loss), net		**2,594**	(341)	**(8,758)**	(406)
Total other income/(expense), net		**264**	354	**(12,269)**	1,530
Income before income taxes and noncontrolling interest		**18,530**	15,420	**33,586**	42,139
Provision for income taxes	2	**3,552**	2,980	**7,593**	8,276
Net income		**14,978**	12,440	**25,993**	33,863
Net (gain)/loss attributable to noncontrolling interest		**(52)**	35	**(93)**	46
Net income attributable to MegaFon shareholders		**14,926**	12,475	**25,900**	33,909
Weighted average number of ordinary shares outstanding – basic and diluted	9	**530,720,500**	620,000,200	**567,866,069**	620,000,200
Earnings per share – basic and diluted, Rubles	9	**28**	20	**46**	55
Other comprehensive income/(loss):					
Foreign currency translation adjustment, net of tax of nil		**87**	71	**54**	129
Change in fair value of derivatives, net of tax of nil		**(138)**	—	**(306)**	—
Other comprehensive income/(loss)		**(51)**	71	**(252)**	129
Total comprehensive income		**14,927**	12,511	**25,741**	33,992
Comprehensive (income)/loss attributable to noncontrolling interest		**(74)**	17	**(107)**	14
Comprehensive income attributable to MegaFon shareholders		**14,853**	12,528	**25,634**	34,006

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
See report of independent accountants

MegaFon

Condensed Consolidated Statements of Cash Flows

(In millions of Rubles)
(Unaudited)

	Note	Nine months ended September 30, 2012	2011
Net cash provided by operating activities		**82,170**	74,510
Cash flows from investing activities:			
Purchases of property, plant and equipment and intangible assets		**(33,589)**	(50,419)
Proceeds from sale of property, plant and equipment		**294**	332
Acquisitions of subsidiaries, net of cash acquired of 240 and 192	3	**(8,439)**	(7,362)
Change in short-term investments and long-term bank deposits		**79,381**	(20,491)
Net cash provided by/(used in) investing activities		**37,647**	(77,940)
Cash flows from financing activities:			
Proceeds from short-term and long-term debt	10	**207,547**	18,330
Repayments of short-term and long-term debt	10	**(93,645)**	(10,029)
Deferred finance charges paid	10	**(991)**	(191)
Payments of contingent consideration	12	**(1,490)**	(491)
Payments of liabilities for marketing related licenses		**(283)**	(276)
Purchase of treasury shares	9	**(63,883)**	—
Dividends paid	9	**(151,863)**	—
Net cash provided by/(used in) financing activities		**(104,608)**	7,343
Effect of exchange rate changes on cash and cash equivalents		**(1,084)**	(348)
Net increase in cash and cash equivalents		**14,125**	3,565
Cash and cash equivalents at the beginning of the period		**2,887**	2,667
Cash and cash equivalents at the end of the period		**17,012**	6,232

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
See report of independent accountants

1. Financial Presentation and Disclosures

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

In Russia, MegaFon has constructed and continues to operate a nationwide wireless communications network that operates on the dual band GSM 900/1800 standard. In May 2007, the Company was awarded a license that expires on May 21, 2017, for the provision of 3G wireless telephony services based on IMT-2000/UMTS standards throughout the entire territory of Russia. In July 2012, the Company was awarded a license which expires in July 2022 for the provision of fourth-generation (“4G”) technology services under Long Term Evolution (“LTE”) standard throughout the entire territory of Russia. As of September 30, 2012, the Company is providing and expanding 3G services in almost all of the regions in which it operates throughout Russia and has commenced providing 4G/LTE services in certain cities throughout Russia under a mobile virtual network operator (“MVNO”) agreement with LLC Scartel (“Scartel”), a related party *(see Note 14).*

The Company also holds licenses for local and long-distance telephony services, data transmission, broadband access services, and communication channels leasing covering the whole territory of Russia. The Company has its own land-line and leased satellite transmission network capacities.

The accompanying condensed financial statements of the Company have been prepared in accordance with generally accepted accounting principles in the United States of America (“US GAAP”) for interim financial reporting and do not include all disclosures required by US GAAP. The Company omitted certain disclosures which would substantially duplicate the disclosures contained in its 2011 audited consolidated financial statements, such as accounting policies and details of accounts which have not changed significantly in amount or composition. Additionally, the Company has provided disclosures where significant events have occurred subsequent to the issuance of its 2011 audited consolidated financial statements. Management believes that the disclosures are adequate to make the information presented not misleading if these financial statements are read in conjunction with the Company’s 2011 audited consolidated financial statements and the notes related thereto. In the opinion of management, the financial statements reflect all adjustments of a normal and recurring nature necessary to present fairly the Company’s consolidated financial position, results of operations and cash flows for the interim periods.

1. Financial Presentation and Disclosures (continued)

The results of operations for the three and nine months ended September 30, 2012 are not indicative of the operating results for the full year (e.g. seasonality).

These financial statements include information updated and subsequent events evaluated through November 8, 2012, the date these interim condensed consolidated financial statements were available to be issued.

2. Summary of Significant Accounting Policies and Recent Accounting Pronouncements

Income Taxes

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

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

The difference between income tax expense reported in the accompanying condensed consolidated financial statements and income before taxes for the nine months ended September 30, 2012 and 2011, multiplied by the statutory tax rate, is mainly due to non-deductibility of certain expenses for income tax purposes, recognized tax benefits and preferences and taxable gains from intragroup borrowings since April 2012.

Treasury Shares

Ordinary shares repurchased by the Company are recorded at cost as treasury shares and reduce total equity in the Company's consolidated financial statements.

Earnings per Ordinary Share

Basic earnings per share are computed by dividing income available to shareholders by the weighted-average number of ordinary shares outstanding during the period. The Company does not have any potentially dilutive securities, therefore diluted earnings per share equal basic earnings per share.

Comparative Information

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

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

Recent Accounting Pronouncements

Technical Corrections and Improvements. In October 2012, the FASB issued ASU 2012-04 *"Technical Corrections and Improvements"*. This ASU contains amendments which were made to clarify the Codification, correct unintended application of guidance, or make minor improvements to the Codification that are not expected to have a significant effect on current accounting practice. Additionally, the amendments are intended to make the Codification easier to understand and the fair value measurement guidance easier to apply by eliminating inconsistencies and providing needed clarifications.

The amendments in this ASU that do not have transition guidance are effective upon issuance. For public entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2012. Early adoption is permitted. The adoption of this ASU did not have a material impact on the Company's financial statements.

Intangibles—Goodwill and Other. In July 2012, the FASB issued ASU 2012-02 *"Intangibles—Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment"*. This ASU states that an entity has the option first to assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that an indefinite-lived intangible asset is impaired. If, after assessing the totality of events and circumstances, an entity concludes that it is not more likely than not that an indefinite-lived intangible asset is impaired, then the entity is not required to take further action. However, if an entity concludes otherwise, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test by comparing the fair value with the carrying amount in accordance with Codification Subtopic 350-30, *"Intangibles—Goodwill and Other, General Intangibles Other than Goodwill"*.

Under the guidance in this ASU, an entity also has the option to bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to performing the quantitative impairment test. An entity will be able to resume performing the qualitative assessment in any subsequent period.

The amendments in this ASU are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The Company does not expect this ASU to have a material impact on its financial statements.

Fair Value Measurements. In May 2011, the FASB issued ASU 2011-04, "*Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and IFRSs"*, which clarifies Topic 820, "*Fair Value Measurements and Disclosures*", but also includes some instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed.

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

This ASU results in common principles and requirements for measuring fair value and for disclosing information about fair value measurements in accordance with US GAAP and International Financial Reporting Standards issued by the International Accounting Standards Board ("IFRS").

The amendment is effective for public entities for interim and annual periods beginning after December 15, 2011. The adoption of the guidance did not have a material impact on the Company's financial statements.

3. Business Combinations

VAS Media

In September 2012, the Company completed the acquisition of a 100% ownership interest in Felebior Holding Limited ("VAS Media"), which holds a 100% interest in a group of subsidiaries that supply multi-media content, ring tones, geo-positioning services, mobile payments and other value-added services ("VAS") in Russia for a cash consideration of 9,207, of which 528 was effectively a settlement of pre-existing payable for VAS Media services. Before the acquisition VAS Media partnered with the Company on a variety of projects, such as provision of MegaFon branded VAS to MegaFon customers.

The primary reason for the acquisition was to strengthen the Company's position in VAS market and to accelerate the development, implementation and launch of new services by the Company.

At the time of acquisition of VAS Media, a member of the Company's Board of Directors and the spouse of the Company's member of management beneficially owned an aggregate of approximately 13% of Felebior Holding Limited. In addition, at the time of that acquisition, other sellers of significant interests in Felebior Holding Limited have from time to time been associates of AF Telecom, a shareholder of the Company. The transaction was unanimously approved by Board of Directors of the Company.

The acquisition of VAS Media was accounted for using the acquisition method. The valuation of certain acquired assets and liabilities assumed has not been finalized as of the date these consolidated financial statements were available to be issued; thus, the provisional measurements of certain intangible assets, deferred taxes and goodwill are subject to change.

3. Business Combinations (continued)

The table below represents the preliminary allocation of the purchase price to the acquired net assets of VAS Media based on their estimated fair values.

	VAS Media
Cash and cash equivalents	240
Other current assets	305
Property, plant and equipment	36
Intangible assets	6
Goodwill	8,544
Other non-current assets	183
Total assets acquired	9,314
Current liabilities	(633)
Non-current liabilities	(2)
Total liabilities assumed	(635)
Total consideration transferred	**8,679**

The goodwill recognized is attributable primarily to expected synergies from the acquisition and the value to be attributed to the workforce of VAS Media. Management is still assessing the allocation of goodwill among reporting units. None of the goodwill recognized is deductible for income tax purposes.

The Company has consolidated the financial position and the results of operations of VAS Media from September 1, 2012. Cost of revenues for the year ended December 31, 2011 were 2,518 and for the eight months ended August 31, 2012 were 2,582 related to services the Company received from VAS Media. The amounts of revenue and net income of VAS Media included in the Company's accompanying condensed consolidated statement of comprehensive income from September 1 to September 30, 2012 were 397 and 67, respectively. These amounts are shown before elimination of intercompany transactions, which were mainly revenues from services provided by VAS Media to the Company of 367.

The pro forma combined results of operations data presented below assume that the VAS Media acquisition had been made as of January 1, 2011. These pro forma amounts are provided for information purposes only and are not necessarily indicative of the results of future operations, nor of the actual results that would have been achieved had the acquisition taken place as of January 1, 2011.

	Three months ended September 30,		Nine months ended September 30,	
	2012	**2011**	**2012**	**2011**
Pro forma revenue	**71,459**	63,676	**202,295**	177,456
Pro forma net income	**15,331**	12,735	**27,001**	34,629
Pro forma EPS, Rubles	**29**	21	**48**	56

4. Goodwill

The changes in the carrying value of goodwill for the nine months ended September 30, 2012 are as follows:

	2012
Balance at January 1, 2012:	15,393
Measurement period adjustments	13
Acquisitions *(Note 3)*	8,544
Balance at the end of the period	**23,950**

There were no indicators of impairment for the Company's goodwill or long-lived assets, and the Company was not required to record any impairment charges. The Company considers all current information in determining the need for impairment loss; however, future changes in events or circumstances, such as a continuation or worsening of the current economic instability, or increased competition, could result in decreases in the fair value of its goodwill and may require the Company to record impairment charges in future periods.

In June 2011, the Company completed the acquisition of a 100% ownership interest in Fairlie Holding and Finance Limited, which holds a 100% interest in a group of subsidiaries that provide broadband internet, IP telephony, IP TV and other multimedia services in Russia under the NetByNet brand ("NetByNet") for total consideration having a fair value of 8,731 as of the date of acquisition, consisting of cash consideration of 7,507 and contingent consideration of 1,224. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement.

The primary reason for the acquisition was to facilitate the Company's entry into the broadband internet market in Moscow, the Moscow region and the Central Federal District, where the Company did not previously provide broadband internet services for end-customers.

As of September 30, 2012, the Company's management believes that the carrying amount of the NetByNet reporting unit approximates its fair value. However, if the Company does not achieve planned cost savings assumed in the original fair value calculation, the Company may recognize an impairment loss.

5. Revenues

Revenues for the three and nine months ended September 30 are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2012	**2011**	**2012**	**2011**
Wireless revenues	**63,067**	57,007	**178,608**	161,054
Wireline revenues	**4,560**	4,029	**13,394**	10,555
Sales of handsets and accessories	**3,607**	2,397	**9,096**	5,537
Total revenues	**71,234**	63,433	**201,098**	177,146

6. Cost of Revenues

Cost of revenues for the three and nine months ended September 30 are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2012	**2011**	**2012**	**2011**
Cost of services	**14,096**	12,674	**41,437**	34,025
Cost of handsets, accessories and SIM-cards sold	**3,253**	2,749	**8,708**	8,241
Total cost of revenues	**17,349**	15,423	**50,145**	42,266

7. Sales and Marketing Expenses

Sales and marketing expenses for the three and nine months ended September 30 are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2012	**2011**	**2012**	**2011**
Advertising	**2,145**	1,804	**6,165**	5,037
Commissions to dealers for connection of new subscribers	**1,888**	2,877	**6,069**	6,322
Commissions to dealers for cash collection from subscribers	**1,273**	1,817	**3,493**	3,871
Total sales and marketing expenses	**5,306**	6,498	**15,727**	15,230

8. Operating Expenses

Operating expenses for the three and nine months ended September 30 are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2012	**2011**	**2012**	**2011**
Salaries and social charges	**6,494**	5,487	**19,461**	17,222
Rent and utilities	**4,102**	3,587	**11,871**	10,315
Operating taxes	**1,768**	1,449	**5,053**	4,263
Network repairs and maintenance	**1,330**	1,476	**3,789**	3,817
Radio frequency fees	**974**	903	**3,012**	2,633
Office maintenance	**435**	460	**1,329**	1,166
Bad debt expense	**392**	346	**1,205**	1,085
Professional services	**265**	285	**1,114**	963
Vehicle costs	**155**	163	**480**	460
Materials and supplies	**49**	60	**167**	197
Insurance	**21**	27	**66**	83
Other expenses	**456**	722	**1,741**	1,856
Total operating expenses	**16,441**	14,965	**49,288**	44,060

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

9. Shareholders' Equity

Ordinary Shares

In August 2012, Federal Commission for Financial Markets, the Russian market's regulator, registered a 1-to-100 split of the Company's shares. As a result, the total amount of authorized and issued shares of the Company became 620,000,000, each with a par value of 0.1 Rubles. Accordingly, all share and per share amounts for all periods presented in these unaudited condensed consolidated financial statements and notes thereto, have been adjusted retroactively, where applicable, to reflect this share split.

In July 2012, the Company retired 200 of its treasury shares held by MegaFon Investments (Cyprus) Limited ("MICL"), a wholly-owned subsidiary of the Company.

Equity Transactions

In April 2012, the Company's shareholders agreed to a series of transactions to permit the payment of the Company's first dividend and re-organize the shareholding structure. The principal impacts of these agreements on the Company's financial position were as follows:

- the special dividend, paid on April 24, 2012, resulted in an aggregate distribution of 151,863 to the shareholders (or 245 Rubles per ordinary share);

9. Shareholders' Equity (continued)

- on April 24, 2012, the Company re-purchased (through MICL) from Allaction Limited, part of the Alfa Group of companies, 89,279,700 or 14.4% of the Company's ordinary shares for 63,883, including transaction costs.

The transactions described above were financed from the Company's existing cash and short-term investments, and additional borrowings of approximately 142,400, net of repayments *(see Note 10)*.

As a result of the dividend payment and the re-purchase of 14.4% of its ordinary shares, and the additional new borrowings *(see Note 10)*, the Company has substantially depleted its working capital, including available cash and short-term investments. As of November 8, 2012, the Company believes it will continue to be able to generate significant operating cash flows and have access to undrawn lines of credit of approximately 79,000 that can be used to cover capital and operating expenditures. Additionally, the Company can defer capital expenditures if necessary in order to meet short-term liquidity requirements. Accordingly, management believes that cash flows from operating and financing activities will be sufficient for the Company to meet its obligations as they become due.

In April 2012, the Company's Board of Directors approved a number of other capital raising options. While the Company believes that financing options will be available, the timing and ultimate completion of any financing will be dependent on a number of factors beyond its control. Accordingly, there is no guarantee that the Company will be able to obtain financing on favorable terms or otherwise.

Voting Agreement

In accordance with a Voting Agreement executed between the Company's shareholders and MICL on April 24, 2012, TeliaSonera Group, one of the Company's shareholders, will direct the voting of the shares in the Company held by MICL on any issues other than the appointment or removal of the CEO until the first to occur of (a) the completion of an initial public offering ("IPO") of the Company, (b) the date at which the TeliaSonera Group or AF Telecom Group reduce their interests in the Company below 25% plus one share, or (c) December 31, 2014. In certain circumstances this period can be extended beyond this date.

Put and Call Option Agreement

On April 24, 2012, the shareholders of the Company signed an agreement (the "Put and Call Option Agreement") to the effect that, if an IPO of the Company has not been consummated by December 31, 2014, Sonera Holding B.V., a member of TeliaSonera Group, will have the right to sell to MICL (the "Put Option") and MICL will have the right to buy from Sonera Holding B.V. (the "Call Option") the lesser of (a) such number of shares in the Company as are equal to approximately 10.6% of the Company and (b) such number of shares in the Company by which the total number of shares in the Company that are directly or indirectly owned by the TeliaSonera Group in aggregate exceeds 25% plus one share of the entire issued share capital of the Company (the "Option Shares"). The price payable to exercise the

9. Shareholders' Equity (continued)

Put and Call Options will be based on the fair value of the Company's shares as determined at the date of exercise. Telecominvest Holdings Limited, a company controlled by AF Telecom Group, at its sole discretion can elect to purchase any or all of the Option Shares under the Put and Call Options.

Sonera Holding B.V., Telecominvest Holdings Limited or MICL may only exercise the Put and Call Options during the period from January 1, 2015 to February 1, 2015. The Company has given a guarantee to Sonera Holding B.V. of the performance of MICL's obligations under the Put and Call Option Agreement.

The Company assesses the fair values of the Put and Call Options as immaterial.

10. Short-Term and Long-Term Debt

Short-term and long-term debt is as follows:

Lender	Currency	Nominal Annual Effective Rate	Maturity	September 30, 2012	December 31, 2011
Bank Loans:					
(1) VTB Bank	Ruble	MosPrime plus 2.20%	2013	**30,000**	—
(2) Sberbank	Ruble	9.02 %	2015-2016	**46,693**	—
(3) Sberbank	Ruble	8.71 %	2014-2015	**29,512**	—
(4) Gazprombank	Ruble	9.05%	2016	**6,300**	—
(5) Nordic Investment Bank	Euro	EURIBOR plus 2.05%	2019	**3,198**	—
(6) Nordea Bank Moscow	U.S. dollar	LIBOR plus 2.0%	2015	**1,546**	**1,610**
(7) UniCredit Bank Moscow	U.S. dollar	LIBOR plus 3.5%	2012-2013	**464**	**805**
Equipment Financings:					
(8) China Development Bank and Bayerische Landesbank	U.S. Dollar	LIBOR plus 1.1% to 2.7%	2012-2016	**26,945**	**25,042**
(9) BNP Paribas, London branch and Nordea Bank Finland	U.S. dollar	2.91% to 4.54%	2012-2016	**6,965**	**9,239**
(10) Bayerische Landesbank, Bayerische Landesbank Filiale Di Milano, Commerzbank Aktiengesellschaft	Euro	3.74% and EURIBOR plus 0.35%	2012-2015	**2,715**	**3,490**
(11) Cisco Systems Finance International	U.S. dollar	3.50% to 4.11%	2012-2017	**1,239**	**1,219**
(12) Fortis Bank, Nordea Bank Finland and Skandinaviska Enskilda Banken	U.S. dollar	1.92%	2013-2017	**2,893**	**1,078**
Other				**644**	**1,226**
Total long-term debt				**159,114**	**43,709**
Less current portion				**(28,494)**	**(7,415)**
Non-current portion				**130,620**	**36,294**

10. Short-Term and Long-Term Debt (continued)

(1) VTB Bank

In April 2012, the Company entered into a revolving credit facility with VTB Bank ("VTB Credit Facility") for up to 30,000. The VTB Credit Facility was fully drawn for a one-year period subject to an interest rate of 3-months MosPrime plus 2.2% which is payable every three months.

Subsequently, in October 2012 the Company issued ruble-denominated bonds in an aggregate principal amount of 10,000, which was applied immediately in prepayment in part of the VTB Credit Facility. The bonds bear interest at a rate of 8.05% per annum, payable semi-annually. The bonds are due in 2022, subject to a two-year put option. The portion of the VTB Credit Facility in the amount of 10,000, which was refinanced is included in long-term debt in the accompanying condensed consolidated balance sheets.

(2, 3) Sberbank

In April 2012, the Company entered into two credit facility agreements with Sberbank, one for up to the Ruble equivalent of $1 billion (30,917 at the exchange rate as of September 30, 2012) and the other for up to the Ruble equivalent of $1.5 billion (46,375 at the exchange rate as of September 30, 2012) (together, the "Sberbank Credit Facilities").

As of September 30, 2012, the Company has fully drawn both the $1 billion Credit Facility in an amount of 29,512 and the $1.5 billion Credit Facility in the amount of 46,693. A payment of 564 as an arrangement fee was made for the Sberbank Credit Facilities.

(4) Gazprombank

In April 2012, the Company and Gazprombank modified the terms of the existing revolving credit facility agreement ("Gazprombank Credit Facility") by increasing the debt limit on the facility from 15,000 to 30,000. The Gazprombank Credit Facility is subject to fees of 0.15% per annum on the amount of the unutilized balance.

On April 18, 2012, the Company drew the entire 30,000 and subsequently, on April 25, 2012, voluntarily repaid 23,700. The Gazprombank Credit Facility carries an interest rate of 9.05% per annum which is payable every three months. The interest rate can be changed by Gazprombank unilaterally in an event of revision of the refinancing rate by the Central Bank of Russia. The principal is due for repayment in September 2016.

The principal purpose of the VTB Credit Facility, the Sberbank Credit Facilities, the Gazprombank Credit Facility and the Bridge Facility (see in "Other" below) is the funding of the dividend payout and the re-purchase of shares by the Company. Any excess will be used to fund operating, investment and financial activities. The covenants of these Credit Facilities are substantially consistent with those which the Company has in its other existing loan agreements.

10. Short-Term and Long-Term Debt (continued)

(5) Nordic Investment Bank

In June 2012, the Company entered into a credit facility with Nordic Investment Bank ("NIB Credit Facility") for up to 80 million Euros. The NIB Credit Facility carries interest at a rate of EURIBOR plus 2.05% per annum. The NIB Credit Facility is subject to payment of a commitment fee of 0.4% per annum on the amount of the unutilized balance and a front-end fee of 0.25% on the principal amount. The NIB Credit Facility can only be used for updating the network of the Company in the Moscow region and other regions of Russia preparing for the launch of 4G/LTE. In September 2012, the Company fully drew Nordic Investment Bank facility in the amount of 80 million Euros (3,198 at the exchange rate as of September 30, 2012).

(8) China Development Bank and Bayerische Landesbank

In April and June 2012, the Company drew an aggregate amount of $107 million (3,308 at the exchange rate as of September 30, 2012) under the credit facility agreement with China Development Bank which bears interest at a rate of LIBOR plus 2.4% per annum. This credit facility can only be used to purchase Huawei equipment.

(12) Fortis Bank, Nordea Bank Finland and Skandinaviska Enskilda Banken

In April and September 2012, the Company drew down $63 million (1,948 at the exchange rate as of September 30, 2012) under its credit facility agreement with Fortis Bank, Nordea Bank Finland and Skandinaviska Enskilda Banken which bears interest at a rate of 1.92% per annum. This credit facility can only be used to purchase Nokia Siemens Networks equipment.

Other

In April 2012, the Company entered into a Bridge Facility with Barclays Bank PLC, BNP Paribas and Citibank N.A., London branch ("Bridge Facility") to facilitate the payment of dividends and repurchase of the Company's shares described above. The Bridge Facility carried interest at a rate of LIBOR plus 1.5% which is increased by 0.5% every three months. The Bridge Facility was subject to mandatory earlier repayment upon the completion of certain debt or capital raising transactions. A payment of 241 as an arrangement fee was made for the Bridge Facility. In April 2012, the Company drew $1.5 billion (46,375 at the exchange rate as of September 30, 2012) under the Bridge Facility. In June and July 2012, the Company voluntarily repaid the Bridge Facility using part of the proceeds from the Sberbank Credit Facilities *(see Notes 10 (2, 3) above)*.

On April 6, 2012, the Company drew down and subsequently, on April 24, 2012, repaid in full 11,000 under its revolving credit facility with UniCredit Bank Moscow which carried interest at a rate of 8.87% per annum.

10. Short-Term and Long-Term Debt (continued)

Also, in April 2012, the Company drew down 5,500 under its agreement with Nordea Bank at an interest rate of 1-month MosPrime plus 2.95% per annum. In May 2012, the Company repaid the amount borrowed under the agreement in full.

11. Cash Flow Hedges of Interest Rate Risk

The Company's objective in using interest rate derivatives is to add certainty and stability to its interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without the exchange of the underlying principal amount of long-term debt.

As at September 30, 2012 and December 31, 2011, the Company had the following outstanding interest rate derivatives stated at their notional amounts that were designated as cash flow hedges of interest rate risk:

	September 30, 2012		**December 31, 2011**	
	Millions of original currency	**Millions of Rubles**	**Millions of original currency**	**Millions of Rubles**
Euro-denominated interest rate swaps	**45**	**1,799**	57	2,375
USD-denominated interest rate swaps	**693**	**21,425**	693	22,312

Interest rate swaps are recorded on the balance sheet at fair value (Level 2). The effective portion of changes in the fair value of derivatives designated and qualifying as cash flow hedges is recorded in other comprehensive income/(loss) and is subsequently reclassified into earnings in the period that the hedged forecast transaction affects earnings. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. For derivative instruments that are not designated as hedges or do not qualify as hedged transactions, the changes in the fair value are reported in the consolidated statement of comprehensive income.

As at September 30, 2012, the fair values of the Company's interest rate swaps in the amounts of 117 and 184 were recorded in other current and other non-current liabilities, respectively, in the accompanying consolidated balance sheets. The fair values of the swaps are based on a forward yield curve and represent the estimated amounts the Company would receive or pay to terminate these agreements at the reporting date, taking into account current interest rates, creditworthiness, nonperformance risk, and liquidity risks associated with current market conditions. The amount reclassified into earnings during the nine months ended September 30, 2012 was immaterial. All movements in fair values are reflected in other comprehensive income/(loss). At September 30, 2012, the amount recorded in other comprehensive income/(loss) which is expected to be reclassified to interest expense in the next twelve months is 117.

12. Settlement of Contingent Consideration

In June 2012, the Company paid approximately $44 million (1,431 at the exchange rates as of payment dates) in full and final settlement of all contingent consideration liability due in respect of the NetByNet acquisition completed in June 2011.

13. Commitments, Contingencies and Uncertainties

Russian Environment and Current Economic Situation

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

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. In 2011 and during the nine months ended September 30, 2012, the Russian Government continued to take measures to support the economy in order to overcome the consequences of the global financial crisis.

Despite some indications of recovery there continues to be uncertainty regarding further economic growth, access to capital and cost of capital, which could negatively affect the Company's future financial position, results of operations and business prospects.

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

3G License Capital Commitments

In May 2007, MegaFon was awarded a license that expires on May 21, 2017, for the provision of 3G wireless communications services for the entire territory of the Russian Federation. The 3G license was granted subject to certain capital and other commitments. The three major conditions were that the Company builds a specified number of base stations that support 3G standards, starts commercial exploitation of the 3G technology in each region of the Russian Federation over the period from May 2008 through May 2010, and also builds a certain number of base stations by the end of the third, fourth and fifth years from the date of granting of the license. As of November 8, 2012, the Company believes it is in full compliance with these license conditions, including constructing the number of base stations required at this time.

13. Commitments, Contingencies and Uncertainties (continued)

4G/LTE License Capital Commitments

In July 2012, the Federal Service for Supervision in Communications, Information Technologies and Mass Media granted the Company a license and allocated frequencies to provide services under the 4G/LTE standard in Russia.

Under the terms and conditions of this license, the Company is obligated to provide 4G/LTE services in each population center with over 50,000 inhabitants in Russia by 2019. The Company is also obligated to make capital expenditures of at least 15,000 annually toward the 4G/LTE roll-out until the network is fully deployed, to clear frequencies currently allocated to the military at its own cost and to compensate other operators for surrendering frequencies in an aggregate amount of 401. In July 2012, the Company has fully paid the compensation due to the other operators. It is currently not able to reasonably estimate the amount of the cost of clearing military frequencies.

Taxation

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

The Company's management believes that its interpretation of the relevant legislation is appropriate and is in accordance with the current industry practice and that the Company's tax, currency and customs positions will be sustained. However, the interpretations of the relevant authorities could differ. As of November 8, 2012, the Company's management estimated the possible effect of additional income taxes, before fines and interest, if any, on these condensed consolidated financial statements, if the authorities were successful in enforcing different interpretations, in the amount of up to approximately 950.

Litigation

The Company is not a party to any material litigation, although in the ordinary course of business, the Company and some of its subsidiaries may be party to various legal and tax proceedings, and subject to claims, certain of which relate to the developing markets and evolving fiscal and regulatory environments in which they operate. In the opinion of management, the Company’s and its subsidiaries’ liability, if any, in all pending litigation, other legal proceedings or other matters, will not have a material effect on the financial condition, results of operations or liquidity of the Company.

13. Commitments, Contingencies and Uncertainties (continued)

Apple Commitment

In August 2008, the Company entered into a two-year fixed commitment with Apple Sales International ("Apple"), an Irish affiliate of Apple Computer Inc., to purchase a total of one million unlocked iPhone handsets over a two-year period for further resale in Russia. The Company fulfilled this requirement with respect to the fourth quarter of 2008, but due to the significantly reduced handset demand caused by the economic crisis in Russia, the Company experienced difficulty re-selling these iPhones.

While the Company placed several orders for iPhone handsets thereafter, none of these orders fulfilled the minimum quarterly requirement for the applicable quarters.

The contract with Apple terminated in August 2010 and, since such date, Apple has not asserted any claim against the Company with respect to any alleged non-fulfillment of its obligation to purchase iPhone handsets, and the Company has no basis to believe that any such claim will be asserted.

14. Scartel Agreement

In February 2012, MegaFon entered into a MVNO agreement with Scartel, a related party of the Company since July 2012, which operates under the "Yota" brand, for the joint development and provision of 4G/LTE services in Russia.

The MVNO agreement enables the Company to provide 4G/LTE services to its customers using the network of Scartel and enables Scartel to use network infrastructure of MegaFon to provide voice services to its customers.

In March and April 2012, the Company prepaid Scartel an aggregate amount of $50 million (1,546 at the exchange rate as of September 30, 2012) for the provision of future interconnection services under the MVNO agreement. 584 of the advance amount were included in prepaid expenses and 855 were included in other non-current assets in the accompanying consolidated balance sheets as at September 30, 2012.

15. Segment Information

The Company conducts its business activities in three operating segments, which are wireless, wireline and retail, of which only the wireless segment meets quantitative thresholds as a reportable segment. Less than 1% of the Company's revenues and results are generated by segments outside of Russia. No single customer represents 10% or more of the consolidated revenues.

16. Subsequent Events

Long-Term Incentive Program 2012

In October 2012, the Company's Board of Directors approved a long-term motivation and retention program for certain key executive and senior level employees under which the parties selected to participate are awarded phantom share options. In the aggregate, the value ascribed to the full package of phantom share options for which options may be awarded is 1.1% of the share capital of OJSC MegaFon (equal to 7,000,000 phantom shares) at the base price of $17.86 per share. The plan has a three-year duration and the awarded share options shall vest in April-May 2014 and 2015 and be settled in cash upon vesting. Payments shall be made on the basis of the difference between the base price and the weighted average price of the Company's shares in the period between 15 January and 15 March of the relevant year of vesting. Vesting of the options is contingent upon the recipient's continuing employment with the Company.