



Interim condensed consolidated financial statements  
(Unaudited)

*For the three months ended 31 March 2016*

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## Auditors' Report on Review of Interim condensed consolidated financial statements

To the Board of Directors and Shareholders  
PJSC MegaFon

### Introduction

We have reviewed the accompanying interim condensed consolidated statement of financial position of PJSC MegaFon (the "Company") and its subsidiaries (the "Group") as at 31 March 2016, and the related interim condensed consolidated statements of comprehensive income, changes in equity and cash flows for the three - month period then ended, and notes to the interim condensed consolidated financial statements (the "interim condensed consolidated financial statements"). Management is responsible for the preparation and presentation of this interim condensed consolidated financial statements in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*. Our responsibility is to express a conclusion on this interim condensed consolidated financial statements based on our review.

### Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim condensed consolidated financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

### Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the interim condensed consolidated financial statements as at 31 March 2016 and for the three - month period then ended is not prepared, in all material respects, in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*.

  
Akylbek Y. A.  
Director, power of attorney dated 16 March 2015 No. 77/15  
JSC "KPMG"

27 April 2016  
Moscow, Russian Federation

Entity: PJSC MegaFon  
Registered by Committee of external economic relations under the Saint Petersburg Town Council on 17 June 1993, Registration No. AOL 51-92.  
Entered in the Unified State Register of Legal Entities on 15 July 2002 by Saint Petersburg Central District Inspectorate of the Ministry for Taxes and Duties of the Russian Federation, Registration No. 1027809169585, Certificate series 78 No. 004009033.  
30 Kadashevskaya Emb., Moscow 115035.

Independent auditor: JSC "KPMG", a company incorporated under the Laws of the Russian Federation, a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.  
Registered by the Moscow Registration Chamber on 25 May 1992, Registration No. 011.585.  
Entered in the Unified State Register of Legal Entities on 13 August 2002 by the Moscow Inter-Regional Tax Inspectorate No 39 of the Ministry for Taxes and Duties of the Russian Federation, Registration No. 1027700125628, Certificate series 77 No. 005721432.  
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# MegaFon

## Interim condensed consolidated statement of comprehensive income

(In millions of Rubles)

	Note	Three months ended 31 March	
		2016 (Unaudited)	2015
<b>Revenues</b>		<b>75,150</b>	<b>73,983</b>
<b>Operating expenses</b>			
Cost of revenues		21,169	19,882
Sales and marketing expenses		4,055	3,578
General and administrative expenses		19,679	18,559
Depreciation		12,715	12,134
Amortisation		1,867	1,800
Loss on disposal of non-current assets	5	105	84
<b>Total operating expenses</b>		<b>59,590</b>	<b>56,037</b>
<b>Operating profit</b>		<b>15,560</b>	<b>17,946</b>
Finance costs		(4,171)	(3,828)
Finance income		278	921
Share of loss of associates and joint ventures		(731)	(49)
Other non-operating expenses		(1,537)	(2,211)
Loss on financial instruments, net		(53)	(162)
Foreign exchange gain/(loss), net		2,083	(3,061)
<b>Profit before tax</b>		<b>11,429</b>	<b>9,556</b>
Income tax expense	7	2,663	2,179
<b>Profit for the period</b>		<b>8,766</b>	<b>7,377</b>

The accompanying notes are an integral part of these interim condensed consolidated financial statements.

# MegaFon

## Interim condensed consolidated statement of comprehensive income (continued)

(In millions of Rubles, except per share amounts)

	Note	Three months ended	
		2016	2015
		31 March	
		(Unaudited)	
<b>Other comprehensive income/(loss)</b>			
<b>Other comprehensive income/(loss) items that may be reclassified to profit or loss in subsequent periods:</b>			
Foreign currency translation difference, net of tax of nil		476	21
Net movement on cash flow hedges, net of tax	6	(255)	(50)
<b>Net other comprehensive income/(loss) that may be reclassified to profit or loss in subsequent periods</b>			
		221	(29)
<b>Total comprehensive income for the period, net of tax</b>		<b>8,987</b>	<b>7,348</b>
<b>Profit/(loss) for the period</b>			
Attributable to equity holders of the Company		8,837	7,402
Attributable to non-controlling interest		(71)	(25)
<b>Total comprehensive income/(loss) for the period</b>			
Attributable to equity holders of the Company		8,967	7,400
Attributable to non-controlling interest		20	(52)
<b>Earnings per share, Rubles</b>			
Basic, profit for the period attributable to equity holders of the Company		15	12
Diluted, profit for the period attributable to equity holders of the Company		15	12

The accompanying notes are an integral part of these interim condensed consolidated financial statements.

# MegaFon

## Interim condensed consolidated statement of financial position

(In millions of Rubles)

		<b>31</b>	<b>31</b>
		<b>March</b>	<b>December</b>
		<b>2016</b>	<b>2015</b>
	<b>Note</b>	<b>(Unaudited)</b>	<b>(Audited)</b>
<b>Assets</b>			
<b>Non-current assets</b>			
Property and equipment	5	232,173	234,417
Intangible assets, other than goodwill		63,068	61,800
Goodwill		33,909	33,909
Investments in associates and joint ventures		47,154	47,885
Non-current financial assets	6	6,385	4,102
Non-current non-financial assets		2,918	2,894
Deferred tax assets		773	832
<b>Total non-current assets</b>		<b>386,380</b>	<b>385,839</b>
<b>Current assets</b>			
Inventory		10,763	8,684
Current non-financial assets		8,182	6,649
Prepaid income taxes		946	2,641
Trade and other receivables		17,622	21,156
Other current financial assets	6	24,807	26,973
Cash and cash equivalents		15,631	17,449
<b>Total current assets</b>		<b>77,951</b>	<b>83,552</b>
<b>Total assets</b>		<b>464,331</b>	<b>469,391</b>
<b>Equity and liabilities</b>			
<b>Equity</b>			
Equity attributable to equity holders of the Company		156,865	147,898
Non-controlling interests		(127)	(147)
<b>Total equity</b>		<b>156,738</b>	<b>147,751</b>
<b>Non-current liabilities</b>			
Loans and borrowings	6	170,372	172,643
Other non-current financial liabilities	6	5,352	5,033
Non-current non-financial liabilities		2,446	2,435
Provisions		4,735	4,603
Deferred tax liabilities		18,937	20,358
<b>Total non-current liabilities</b>		<b>201,842</b>	<b>205,072</b>
<b>Current liabilities</b>			
Trade and other payables		41,566	45,961
Loans and borrowings	6	39,512	47,037
Other current financial liabilities	6	2,680	2,900
Current non-financial liabilities		20,765	20,567
Income taxes payable	7	1,228	103
<b>Total current liabilities</b>		<b>105,751</b>	<b>116,568</b>
<b>Total equity and liabilities</b>		<b>464,331</b>	<b>469,391</b>

The accompanying notes are an integral part of these interim condensed consolidated financial statements.

# MegaFon

## Interim condensed consolidated statement of changes in equity

(In millions of Rubles)

For the three months ended 31 March 2016 and 31 March 2015

	Attributable to equity holders of the Company									
	Ordinary shares		Treasury shares		Capital surplus	Retained earnings	Other capital reserves	Total	Non-controlling interests	Total equity
	Number of shares	Amount	Number of shares	Amount						
<b>As of 1 January 2015</b>	<b>620,000,000</b>	<b>526</b>	<b>24,299,033</b>	<b>(17,387)</b>	<b>12,567</b>	<b>161,422</b>	<b>561</b>	<b>157,689</b>	<b>144</b>	<b>157,833</b>
Profit/(loss) for the period	—	—	—	—	—	7,402	—	7,402	(25)	7,377
Other comprehensive loss	—	—	—	—	—	—	(2)	(2)	(27)	(29)
<b>Total comprehensive income/(loss)</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>7,402</b>	<b>(2)</b>	<b>7,400</b>	<b>(52)</b>	<b>7,348</b>
Dividends to non-controlling interests	—	—	—	—	—	—	—	—	(7)	(7)
<b>As of 31 March 2015 (unaudited)</b>	<b>620,000,000</b>	<b>526</b>	<b>24,299,033</b>	<b>(17,387)</b>	<b>12,567</b>	<b>168,824</b>	<b>559</b>	<b>165,089</b>	<b>85</b>	<b>165,174</b>
<b>As of 1 January 2016</b>	<b>620,000,000</b>	<b>526</b>	<b>24,299,033</b>	<b>(17,387)</b>	<b>12,567</b>	<b>152,425</b>	<b>(233)</b>	<b>147,898</b>	<b>(147)</b>	<b>147,751</b>
Profit/(loss) for the period	—	—	—	—	—	8,837	—	8,837	(71)	8,766
Other comprehensive income	—	—	—	—	—	—	130	130	91	221
<b>Total comprehensive income</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>8,837</b>	<b>130</b>	<b>8,967</b>	<b>20</b>	<b>8,987</b>
<b>As of 31 March 2016 (unaudited)</b>	<b>620,000,000</b>	<b>526</b>	<b>24,299,033</b>	<b>(17,387)</b>	<b>12,567</b>	<b>161,262</b>	<b>(103)</b>	<b>156,865</b>	<b>(127)</b>	<b>156,738</b>

The accompanying notes are an integral part of these interim condensed consolidated financial statements.

# MegaFon

## Interim condensed consolidated statement of cash flows

(In millions of Rubles)

	Note	Three months ended 31 March	
		2016 (Unaudited)	2015
<b>Operating activities</b>			
Profit before tax		11,429	9,556
Adjustments to reconcile profit before tax to net cash flows:			
Depreciation		12,715	12,134
Amortisation		1,867	1,800
Loss on disposal of non-current assets		105	84
Loss on financial instruments, net		53	162
Net foreign exchange (gain)/loss		(2,083)	3,061
Share of loss of associates and joint ventures		731	49
Change in impairment allowance for receivables and other non-financial assets		599	481
Finance costs		4,171	3,828
Finance income		(278)	(921)
Working capital adjustments:			
Increase in inventory		(2,079)	(1,617)
Decrease/(increase) in trade and other receivables		2,043	(144)
Increase in current non-financial assets		(52)	(2,421)
Decrease in trade and other payables		(2,010)	(413)
Decrease in current non-financial liabilities		(1,651)	(3,245)
Change in VAT, net		1,447	266
Income tax received		—	102
Income tax paid		(1,216)	(1,834)
Interest received		100	570
Interest paid, net of interest capitalised		(3,258)	(2,928)
<b>Net cash flows from operating activities</b>		<b>22,633</b>	<b>18,570</b>
<b>Investing activities</b>			
Purchase of property, equipment and intangible assets	5	(17,359)	(10,196)
Proceeds from sale of property and equipment	5	33	83
Payment of contingent consideration		(180)	(33)
Loans granted	6	(3,388)	—
Net change in short-term demand deposits		—	4,751
<b>Net cash flows used in investing activities</b>		<b>(20,894)</b>	<b>(5,395)</b>
<b>Financing activities</b>			
Proceeds from borrowings, net of fees paid	6	6,898	5,790
Repayment of borrowings	6	(9,637)	(1,637)
Finance lease payments		(22)	—
Dividends to non-controlling interests		—	(7)
<b>Net cash flows (used in)/received from financing activities</b>		<b>(2,761)</b>	<b>4,146</b>
Net (decrease)/increase in cash and cash equivalents		(1,022)	17,321
Net foreign exchange difference		(796)	(1,150)
Cash and cash equivalents at beginning of period		17,449	22,223
<b>Cash and cash equivalents at end of period</b>		<b>15,631</b>	<b>38,394</b>

The accompanying notes are an integral part of these interim condensed consolidated financial statements.



# MegaFon

## Notes to interim condensed consolidated financial statements

*(In millions of Rubles)*

### **1. General**

Public Joint Stock Company MegaFon (“MegaFon” or the “Company” and together with its consolidated subsidiaries the “Group”) is a leading integrated telecommunications operator in Russia and provides a broad range of voice, data and other telecommunication services to retail customers, businesses, government clients and other telecommunication services providers.

MegaFon lists its ordinary shares on the Moscow Exchange and its ordinary shares represented by Global Depositary Receipts, or GDRs, on the London Stock Exchange, in each case under the symbol “MFON”.

### **2. Basis of preparation**

These interim condensed consolidated financial statements have been prepared in accordance with IAS 34, *Interim Financial Reporting*, and should be read in conjunction with the annual consolidated financial statements of the Group for the year ended 31 December 2015.

These interim condensed consolidated financial statements are unaudited and do not include all the information and disclosures required in the annual IFRS financial statements. The Company omitted disclosures which would substantially duplicate the information contained in its 2015 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 subsequently to the issuance of its 2015 audited consolidated financial statements. Management believes that the disclosures in these interim condensed consolidated financial statements are adequate to make the presented information not misleading if these interim condensed consolidated financial statements are read in conjunction with the Group’s 2015 audited consolidated financial statements and the notes related thereto. In the opinion of management, the interim condensed consolidated financial statements reflect all adjustments necessary to present fairly the Group’s financial position, financial performance and cash flows for the interim reporting period in accordance with IAS 34, *Interim Financial Reporting*.

The accompanying interim condensed consolidated financial statements are presented in millions of Rubles, except for per share amounts which are in Rubles, unless otherwise indicated.

The interim condensed consolidated financial statements were authorised for issue by the Company’s Chief Executive Officer (“CEO”) and Chief Accountant on 27 April 2016.

### **3. Significant accounting policies**

The accounting policies and methods of computation applied in the preparation of these interim condensed consolidated financial statements are consistent with those disclosed in the annual consolidated financial statements of the Group for the year ended 31 December 2015.

*The accompanying notes are an integral part of these interim condensed consolidated financial statements.*

# MegaFon

## Notes to interim condensed consolidated financial statements (continued)

### 4. Segment information

The Group manages its business primarily based on eight geographical operating segments within Russia, which provide a broad range of voice, data and other telecommunication services, including wireless and wireline services to clients, interconnection services, data transmission services and value added services (“VAS”). The Chief Operating Decision Maker (“CODM”) evaluates the performance of the Group’s operating segments based on revenue and operating income before depreciation and amortisation (“OIBDA”). Total assets and liabilities are not allocated to operating segments and not analysed by the CODM. Operating segments with similar economic characteristics have been aggregated into an integrated telecommunication services segment, which is the only reportable segment. Less than 1% of the Group’s revenues and results are generated by segments outside of Russia. No single customer represents 10% or more of the consolidated revenues.

Reconciliation of consolidated OIBDA to consolidated profit before tax for the three months ended 31 March:

	<u>2016</u>	<u>2015</u>
<b>OIBDA</b>	<b>30,247</b>	<b>31,964</b>
Depreciation	(12,715)	(12,134)
Amortisation	(1,867)	(1,800)
Loss on disposal of non-current assets	(105)	(84)
Finance costs	(4,171)	(3,828)
Finance income	278	921
Share of loss of associates and joint ventures	(731)	(49)
Other non-operating expenses	(1,537)	(2,211)
Loss on financial instruments, net	(53)	(162)
Foreign exchange gain/(loss), net	2,083	(3,061)
<b>Profit before tax</b>	<b>11,429</b>	<b>9,556</b>

### *Seasonality of operations*

The Company’s services are impacted by seasonal trends throughout the year. Higher revenues and operating profits are usually expected in the second half of the year rather than in the first six months. Higher revenues during the period July to September are mainly attributable to increased demand for telecommunication services during the peak holiday season. Higher revenues also occur in the month of December, due to increased demand for telecommunication services and equipment from private customers. Also the number of working days is significantly higher in the second half of a calendar year than in the first half of the year due to long public holidays in January and May in Russia, which further contributes to higher revenues in the second half of the year. This information is provided to allow for a better understanding of the Group’s results; however, management has concluded that these impacts on the results are not ‘highly seasonal’ as considered by IAS 34.

Notes to interim condensed consolidated financial statements (continued)

**5. Property, equipment and intangible assets**

During the three months ended 31 March 2016, the Group acquired property and equipment with a cost of 11,150 (31 March 2015: 7,646). Assets with a net book value of 119 were disposed of by the Group during the three months ended 31 March 2016 (31 March 2015: 120), resulting in a net loss on disposal of 99 (31 March 2015: 70). Interest capitalised and paid was 430 and 361 for the three months ended 31 March 2016 and 2015, respectively.

In February 2016 the Company submitted successful bids for 2,570-2,595 MHz band spectrum in forty regions of the Russian Federation pursuant to a frequency distribution auction conducted by the Federal Service for Supervision of Communications, Information and Mass Media (“Roskomnadzor”). Under the terms and conditions of these spectrum licences, the Company is obligated to compensate other operators for surrendering frequencies in an aggregate amount of 378. The total consideration for the spectrum including the compensation due to the other operators is 2,199.

**6. Financial assets and liabilities**

*Loan receivable*

In February 2016 the Group granted Strafor Commercial Ltd (“Strafor”) a loan in the amount of \$43.8 million (2,961 at the exchange rate as of 31 March 2016). The loan is repayable in February 2018 with interest at 7% paid annually. The loan was granted after performance of all necessary credit checks and satisfactory assessment of refinancing risks. The loan is secured by a pledge of 50% of the shares of Strafor and 50% of the shares of North Financial Overseas Corp., both companies related to Svyaznoy Group, the second largest telecommunications retailer in Russia, and was granted in the context of the Company’s long term relations with the retailer.

*Cash flow hedges of foreign currency risk*

In March 2016 the Company entered into a number of US dollar forward purchase agreements with a total notional amount of \$423 million (28,598 at the exchange rate as of 31 March 2016) that limits the exposure from changes in US dollar exchange rates on certain long-term debts.

The forwards have been designated and qualified as cash flow hedges of foreign currency risk. The effective portion of changes in the fair value of the forwards of 294 (loss) for the period ended 31 March 2016 has been recorded in other comprehensive income/(loss) and will subsequently be reclassified into earnings in the period in which the hedged forecast transaction affects earnings. There has been no ineffective portion in the reporting period.

# MegaFon

## Notes to interim condensed consolidated financial statements (continued)

### 6. Financial assets and liabilities (continued)

#### *Fair values*

Set out below is a comparison by class of the carrying amounts and fair values of the Group's financial instruments and certain non-financial assets that are carried in the interim condensed consolidated financial statements.

		Carrying amount		Fair value	
		31 March 2016 (Unaudited)	31 December 2015	31 March 2016 (Unaudited)	31 December 2015
<b>Financial assets</b>					
Financial assets at fair value through profit or loss:					
Cross-currency swap not designated as hedge	Level 2	688	1,456	688	1,456
Financial assets at fair value through OCI:					
Cross-currency swap designated as cash flow hedge	Level 2	1,105	1,903	1,105	1,903
Loans and receivables at amortised cost:					
Short-term bank deposits	Level 2	18,799	20,236	18,799	20,236
Loans receivable from Garden Ring and Strafor	Level 2	7,170	4,061	7,170	4,061
Other deposits	Level 2	3,430	3,419	3,242	3,178
<b>Total financial assets</b>		<b>31,192</b>	<b>31,075</b>	<b>31,004</b>	<b>30,834</b>
<b>Financial liabilities</b>					
Financial liabilities at amortised cost:					
Loans and borrowings	Level 2	172,285	182,107	171,640	185,841
Ruble bonds	Level 1	37,600	37,573	36,523	35,696
Deferred and contingent consideration	Level 3	2,828	3,209	2,828	3,209
Finance lease obligations	Level 3	3,472	3,504	3,472	3,504
Long-term accounts payable	Level 3	826	1,048	946	1,200
Financial liabilities at fair value through profit or loss:					
Cross-currency swap not designated as hedge	Level 2	88	7	88	7
Financial liabilities at fair value through OCI:					
Interest-rate swaps designated as cash flow hedges	Level 2	16	41	16	41
Foreign currency forwards and cross-currency swap designated as cash flow hedges	Level 2	573	15	573	15
Due to employees and related social charges, non-current	Level 3	228	109	228	109
<b>Total financial liabilities</b>		<b>217,916</b>	<b>227,613</b>	<b>216,314</b>	<b>229,622</b>

*The accompanying notes are an integral part of these interim condensed consolidated financial statements.*

Notes to interim condensed consolidated financial statements (continued)

**6. Financial assets and liabilities (continued)**

Management has determined that cash, short-term deposits, trade receivables, trade payables, bank overdrafts and other current liabilities approximate their carrying amounts largely due to the short-term maturities of these instruments.

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

The GARS Holding Limited (“GARS”) escrow account (included in ‘Other deposits’ in the above table) holds cash reserved for deferred and contingent consideration settlements under the sale and purchase agreement with the sellers of GARS. The fair value of the account approximates its carrying value.

The Group estimated the fair value of the GARS contingent consideration of 325 and the SMARTS deferred consideration of 60 using a probability-weighted cash flow model. These fair value measurements are based on significant inputs not observable in the market and thus represent a Level 3 measurement. The fair value of the Garden Ring deferred consideration approximates its carrying value.

The fair value of the Group’s other deposits relating to cash received under certain contracts with customers is determined by using a discounted cash flow method using a discount rate that reflects the bank deposit rates the Group would get in the market as at the end of the reporting period.

The fair values of the Group’s loans and borrowings and other liabilities carried at amortised cost, except for market quoted Ruble bonds, are determined by a discounted cash flow method using a discount rate that reflects the issuer’s borrowing rate as at the end of the reporting period. The own nonperformance risk as at 31 March 2016 and 31 December 2015 was assessed to be insignificant.

During the three months ended 31 March 2016 there were no transfers between levels of the fair value hierarchy.

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

***Valuation techniques and assumptions***

The fair values of interest rate swaps, cross-currency swaps and forwards are based on a forward yield curve and represent the estimated amount the Group would receive or pay to terminate these agreements at the reporting date, taking into account current interest rates, foreign exchange spot and forward rates, creditworthiness, nonperformance risk, and liquidity risks associated with current market conditions.

# MegaFon

## Notes to interim condensed consolidated financial statements (continued)

### 7. Income tax

The Group calculates the income tax expense for the period using the tax rate that would be applicable to the expected total annual earnings.

The major components of income tax expense for the three months ended 31 March in the interim condensed consolidated statement of comprehensive income are as follows:

	<u>2016</u>	<u>2015</u>
Current income tax	3,938	3,138
Deferred income tax	(1,275)	(959)
<b>Total income tax expense</b>	<b><u>2,663</u></b>	<b><u>2,179</u></b>

### 8. Related parties

As of 31 March 2016 and 31 December 2015, the Group is primarily owned by USM Group, an indirect controlling shareholder, and TeliaSonera Group, another major shareholder with significant influence over the Group, a publicly owned Swedish company.

The following tables provide the total amount of transactions that have been entered into with related parties and balances of accounts with them for the relevant financial periods:

	<b>Three months ended 31 March</b>	
	<u>2016</u>	<u>2015</u>
Revenues from USM Group	5	6
Revenues from TeliaSonera Group	106	176
Revenues from Euroset	198	6
	<b><u>309</u></b>	<b><u>188</u></b>
Services from USM Group	306	160
Services from TeliaSonera Group	189	413
Services from Euroset	329	288
Services from Garden Ring	392	—
	<b><u>1,216</u></b>	<b><u>861</u></b>
Other non-operating expenses from USM Group	1,293	1,826

*The accompanying notes are an integral part of these interim condensed consolidated financial statements.*

# MegaFon

## Notes to interim condensed consolidated financial statements (continued)

### 8. Related parties (continued)

	31 March 2016	31 December 2015
Due from USM Group	1,002	477
Due from TeliaSonera Group	365	305
Due from Euroset	531	403
Due from Garden Ring	4,316	4,643
	<b>6,214</b>	<b>5,828</b>
Due to USM Group	1,156	809
Due to TeliaSonera Group	297	414
Due to Euroset	52	12
Due to Garden Ring	15	63
	<b>1,520</b>	<b>1,298</b>

#### *Terms and conditions of transactions with related parties*

Outstanding balances as of 31 March 2016 and 31 December 2015 are unsecured. There have been no guarantees provided or received for any related party receivables or payables. As of 31 March 2016 and 31 December 2015, the Group has not recorded any impairment of receivables relating to amounts owed by related parties.

#### *USM Group*

The outstanding balances and transactions with USM Group relate to operations with Garsdale Services Investment Limited (“Garsdale”), the Group’s parent, USM Holdings Limited, an indirect owner of Garsdale, and their consolidated subsidiaries.

The Group has an agreement with Telecominvest, a member of the USM Group, for provision of legal and personnel services in 2015 and 2016. In addition, the Group purchased billing system and related support services from PeterService, another member of the USM Group, in the amount of 987 and 631 during the three months ended 31 March 2016 and 2015, respectively.

The Group is a member of the not-for-profit partnership “Development, Innovations, Technologies” (the “Partnership”) which was established by companies in the USM Group. The Partnership may determine to incur education, science and other social costs as well as to maintain certain social infrastructure assets in Skolkovo Innovation Centre which are not owned by MegaFon and not recorded in the consolidated statement of financial position. The Group’s accrued contributions to the Partnership of 1,293 and 1,826 during the three months ended 31 March 2016 and 31 March 2015, respectively, are included into other non-operating expenses in the interim condensed consolidated statement of comprehensive income.

#### *TeliaSonera Group*

The outstanding balances and transactions with TeliaSonera Group relate to operations with various companies in that Group. Revenues and cost of services are principally related to roaming agreements between MegaFon and members of the TeliaSonera Group located outside Russia and a wireline interconnection agreement with TeliaSonera International Carrier Russia.

*The accompanying notes are an integral part of these interim condensed consolidated financial statements.*

Notes to interim condensed consolidated financial statements (continued)

**8. Related parties (continued)**

*Euroset*

Euroset is the Group's joint venture with PJSC VimpelCom. The Group has a dealership agreement with Euroset which qualifies as a related party transaction.

*Garden Ring*

Garden Ring is the Group's joint venture with Sberbank. The Group has a lease agreement with Garden Ring which qualifies as a related party transaction. This building will become the new corporate headquarters of the Group, permitting the consolidation of the Group's operations in Moscow into a single location. The Group also has loan receivable from Garden Ring. The balance due from Garden Ring at 31 March 2016 consists of the loan receivable and an advance payment under the lease agreement.

**9. Commitments, contingencies and uncertainties**

*Operating environment*

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

During 2015 and the three months ended 31 March 2016, the Russian economy was negatively impacted by significant declines in crude oil prices and the value of the Russian Ruble, as well as sanctions imposed on Russia by several countries. Ruble interest rates have fluctuated significantly and as of 31 March 2016 the key rate of the Central Bank of Russia was at 11%. The combination of the above resulted in reduced access to capital, a higher cost of capital, increased inflation and uncertainty regarding economic growth in Russia, any or all of which could negatively affect the Group's future financial position, results of operations and business prospects. Management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

*4G/LTE licence capital commitments*

In July 2012, Roskomnadzor granted the Company a licence and allocated frequencies to provide services under the 4G/LTE standard in Russia.

Under the terms and conditions of this licence, 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 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.

*The accompanying notes are an integral part of these interim condensed consolidated financial statements.*



Notes to interim condensed consolidated financial statements (continued)

**9. Commitments, contingencies and uncertainties (continued)**

*Equipment purchases agreements*

In 2014 the Group entered into two separate 7-year agreements with two suppliers to purchase equipment and software for 2G/3G/4G network construction and modernisation. The software usage agreements contain various termination options, however the Group is specifically committed under the agreements to pay at least 3 years' worth of fees plus an amount equal to 50-60% of the fees due for years four through seven of the agreements for each base station in use as at the date of termination while receiving a credit against these commitments for fees already paid. The amount of the commitments at 31 March 2016 is 9,711.

*Social infrastructure expenses*

From time to time, the Group may determine to maintain certain social infrastructure assets which are not owned by the Group and not recorded in the interim condensed consolidated financial statements as well as to incur education, science and other social costs. Such activities may be conducted in collaboration with non-governmental organisations. These expenses are presented in other non-operating expenses in the consolidated statement of comprehensive income (*Note 8*).

*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 Group 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.

In 2014 a law "On controlled foreign companies" (the "CFC law") was enacted aimed at fiscal stimulation by decreasing the number of the entities involved in the Russian economy but registered abroad, and took effect on 1 January 2015. Under the CFC law retained profits of foreign companies and non-corporate structures controlled by Russian tax residents (companies and individuals) may be subject to Russian taxation. Russian taxpayers (controlling parties) must inform the tax authorities of the foreign companies controlled by them, while the tax authorities may impose additional tax liabilities on taxpayers failing to include retained profit of the foreign controlled companies in their taxable base, where necessary.

The Group's management believes that its interpretation of the relevant legislation is appropriate and is in accordance with the current industry practice and that the Group's tax, currency and customs positions will be sustained. However, the interpretations of the relevant authorities could differ.

Notes to interim condensed consolidated financial statements (continued)

**9. Commitments, contingencies and uncertainties (continued)**

As of 31 March 2016 the Group's management estimated that the possible effect of additional taxes, before fines and interest, if any, on the interim condensed consolidated financial statements, if the authorities were successful in enforcing different interpretations, is in the amount of up to approximately 848.

*Litigation*

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

**10. Events after the reporting date**

*Ruble bonds*

On 12 April 2016 the Group re-purchased 1,636,213 Series 05 Ruble denominated bonds at their nominal value of 1,000 Rubles each under a mandatory put option exercisable by the bond holders following a coupon rate reset on 23 March 2016.

The Group initially issued 10,000,000 Series 05 Ruble denominated bonds in October 2012. In October 2014 the Group re-purchased 8,249,296 Series 05 Ruble denominated bonds at their nominal value of 1,000 Rubles pursuant to a mandatory put option following a coupon rate reset on 24 September 2014.

The re-purchased bonds are kept in treasury and may be further placed in the market should the Group decide to do so. The remaining 114,491 Series 05 Ruble denominated bonds will continue trading in the market with a coupon rate of 0.1% p.a. for a period of six months, after which the rate will be subject to further reset and the bonds will be subject to a further put option.