

**Annex**

to Minutes No. 04-12  
of the meeting of the Board of Directors  
of Sistema JSFC  
dated 26 May 2012

Pre-approved by the  
Board of Directors of  
Sistema JSFC  
on 26 May 2012  
Minutes No 04-12

Approved by the Annual General  
Meeting of  
Sistema JSFC  
on 30 June 2012  
Minutes No 1-12

# **ANNUAL REPORT of Open Joint-Stock Company Sistema Joint-Stock Financial Corporation for 2011**

This report has been compiled pursuant to the requirements of the Federal Law "On the stock market". Financial information set out in this Annual report is based on the accounting data compiled pursuant to the Russian laws, and contains elements of consolidated financial reports compiled under international standards.



**Moscow 2012**

# CONTENTS

1. Company's position in the sector	4
1.1. Profile of Sistema JSFC	4
1.2. Equity capital structure of Sistema JSFC	4
2. Priority business areas and development strategy	7
2.1. Mission and strategy of Sistema JSFC	7
2.2. Portfolio of Sistema JSFC	8
3. Report from the Board of Directors on the results of the Company's development in the priority areas	9
3.1. Key Events in 2011	9
3.2. Events after the reporting period	10
3.3. Russian Accounting Standards (RAS) financial results of Sistema JSFC	12
3.4. US GAAP consolidated financial results of Sistema JSFC	13
3.5. Credit ratings of Sistema JSFC	19
3.6. Report on payment of announced (paid out) dividends on the shares of Sistema JSFC	19
4. Outlook and development strategy of the Sistema Group	20
4.1. Core Assets	20
MTS	21
Bashneft	23
Bashkirenergo	25
4.2. Developing Assets	28
Sistema Mass-media	30
MTS-Bank	31
Detsky Mir	33
Intourist	34
Medsi	35
RTI	37
Binnopharm	39
RussNeft	41
SSTL	43
NIS	45
5. Description of core risk factors	47
5.1. External risks	47
5.2. Risks related to the core activities of Sistema JSFC	48
6. Corporate governance system	50

6.1. General Meeting of shareholders	51
6.2. Board of Directors	53
6.3. President	58
6.4. Management Board	59
6.5. Specifics of the risk management, internal control and audit system	60
6.6. Specifics of corporate governance system development in 2011	61
7. Social responsibility	63
8. Criteria for and amounts of remuneration of the members of the Board of Directors and top executives of the Company	66
9. Annex	67
9.1. Summary biographies of the members of the Board of Directors and their shareholdings in Sistema JSFC	67
9.2. Information on transactions performed by members of the Board of Directors of Sistema JSFC with the shares they hold in the Company over the period from 1 January till 31 December 2010	73
9.3. Summary biographies of the President of Sistema JSFC and the members of the Management Board	74
9.4. Information on the number of shares of Sistema JSFC held by the President and the Management Board members	77
9.5. List of transactions performed by the Company in the reporting year that are recognized as major transactions under the Federal Law "On joint-stock companies", and other transactions covered by the major transactions approval procedure pursuant to the Company's Charter	78
9.6 List of transactions performed by the Company in the reporting year that are recognized as related party transactions under the Federal Law "On joint-stock companies"	78
9.7 Information on the Company's compliance with the requirements of the Corporate Conduct Code from the Federal Service for Financial Markets	85
9.8. Information on the Company's compliance with the requirements of the UK Combined Corporate Governance Code	93

# 1. COMPANY'S POSITION IN THE SECTOR

## 1.1. Profile of Sistema JSFC

Sistema JSFC is Russia's largest publicly listed investment company. Incorporated in 1993, Sistema JSFC is now one of Russia's top-10 companies by revenues and is one of the largest investment companies in the world. It focuses on achieving long-term growth for its shareholders through high returns and diversification of its portfolio of investments. The company's portfolio comprises stakes in predominantly Russian businesses in a range of sectors, including telecommunications, oil, utilities, consumer, high tech and others. Sistema is the controlling shareholder in most of its portfolio companies. The companies of the Sistema Group service more than 100 million customers in their sectors.

Sistema is unique among Russian public investment companies, and provides investors with unique investment opportunities. The Corporation's investment activities support the growth of its shareholder value and provide for the maximum possible returns on its portfolio of assets. Sistema is managed by a highly professional management team, in line with the generally recognized corporate governance standards. The experience of the Board members and the management, as well as the opportunities they have, make it possible for them to gain access to unique objects for investment and funding, to create businesses that take leading positions in their sectors and rely on their long-term success and on a high level of profits for the shareholders.

The portfolio assets of the Sistema Group are grouped into two Business Units: Core Assets and Developing Assets.

The Core Assets business unit includes companies being leaders in their industries which generate a stable high cash flow for the Group. The businesses have well-developed operations and service their liabilities independently. The Core Assets portfolio includes such mature businesses as Bashneft, one of Russia's largest oil companies; MTS, the first telecom company in Russia and the CIS; and Bashkirenergo, the leading energy sector company in the Republic of Bashkortostan.

The Developing Assets business unit includes investments in companies at an earlier stage of their development, typically in high growth sectors. The Developing Assets portfolio includes Detsky Mir-Center, MTS Bank, Medsi Group, RTI, Intourist, Russneft, Sistema Mass Media, Sistema Shyam TeleService Ltd. (SSTL), Binnopharm and NIS.

Sistema continuously monitors opportunities to create value through regular management of its portfolio, investments in new projects, restructuring of current assets and building strategic partnerships. While assessing new investment opportunities, Sistema considers sufficiently large projects\* or transactions in the industries of its current operation. The Corporation seeks to establish partnerships with leading local and international companies to help maximize the growth of its investments.

## 1.2. Equity structure of Sistema JSFC\*\*

Sistema JSFC has 9,650,000,000 ordinary shares outstanding with the par value of RUR0.9 each. Its shareholder capital amounts to RUR 868,500,000.

In February 2005, Sistema JSFC held the initial public offering and listing of its shares on the London Stock Exchange under the SSA ticker. The Company's shares are traded at the London Stock Exchange (LSE) in the form of global depositary receipts (GDRs). One GDR represents 20 ordinary shares. The company's ordinary shares are also traded under the AFKC ticker on the MICEX-RTS Stock Exchange, and under the SIST ticker - on the Moscow Stock Exchange. About 19% of shares are traded as GDRs on the London Stock Exchange, and 7.75% of shares are in circulation at MICEX-RTS.

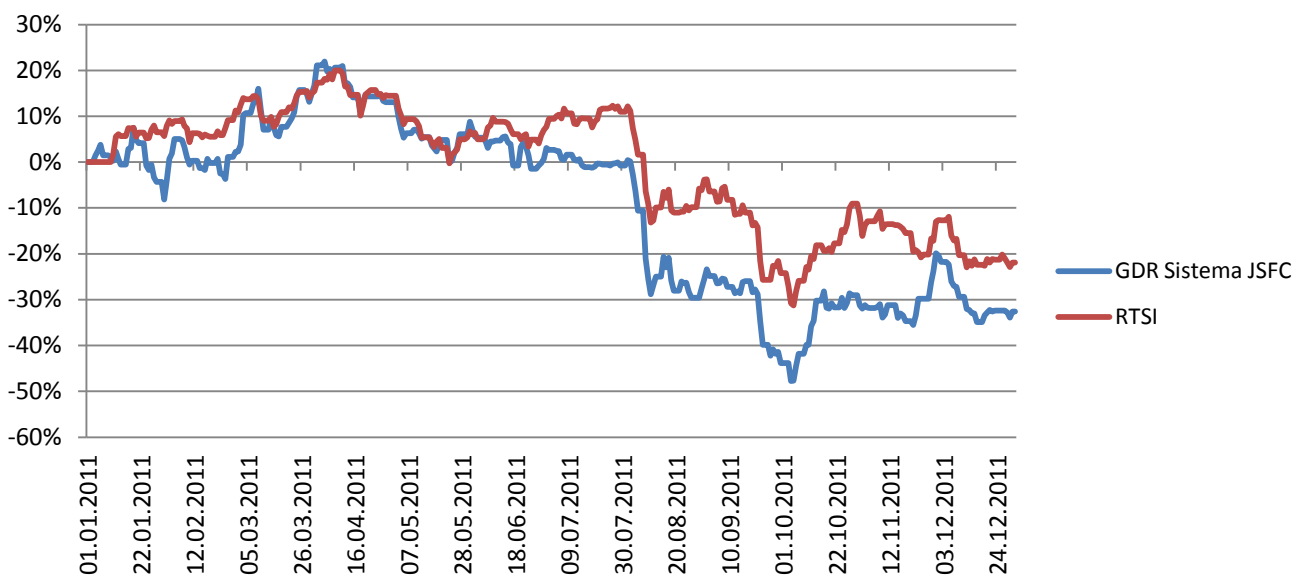
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\* at least USD 300m of value

\*\* as of 31.12.2011

As of 31.12.2012, the Sistema Group included four public subsidiaries: the shares of MTS are traded as ADRs on the New York Stock Exchange and as ordinary shares at MISEX-RTS; the shares of the Bashneft Group and Bashkirenergo are also listed at MICEX-RTS. The shares of Sitronics in the form of GDRs are listed at the London Stock Exchange.

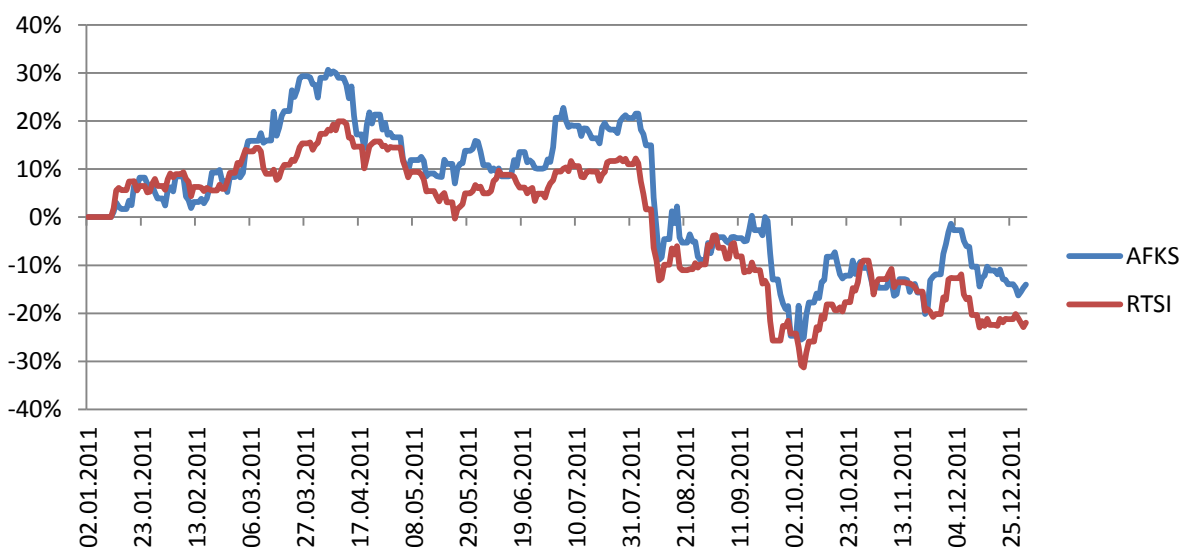
*Comparative performance of the RTS Index and the GDRs of Sistema JSFC at the London Stock Exchange*



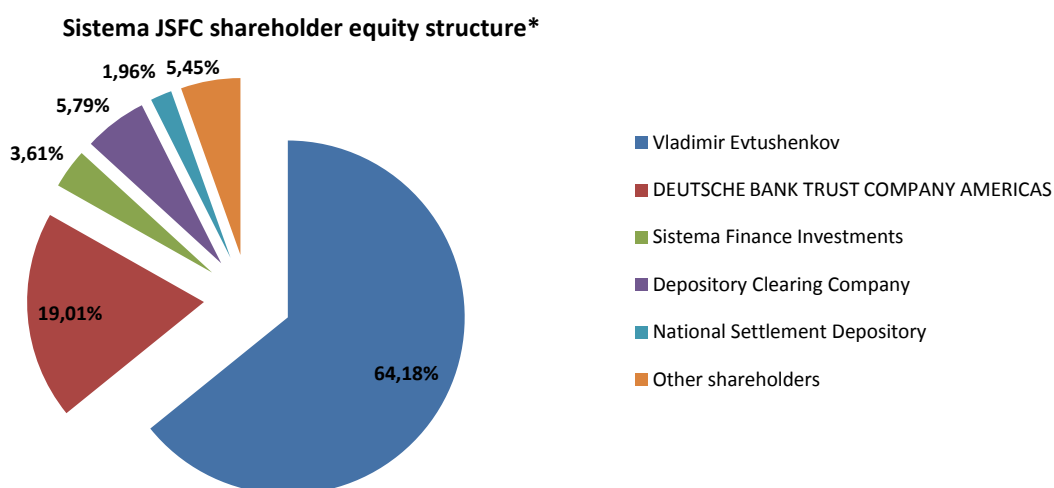
\* according to Bloomberg

The closing price of Sistema's GDR on the London Stock Exchange on the **first day** of trading of 2011 was \$24.93, on the last **day of** trading it was \$16.81. The price of the Corporation's GDRs reached its peak of \$30.4 on 4 April 2011, and its lowest level of \$13.02 on 4 October 2011.

*Comparative performance of the RTS index and the Sistema JSFC share price at MICEX*



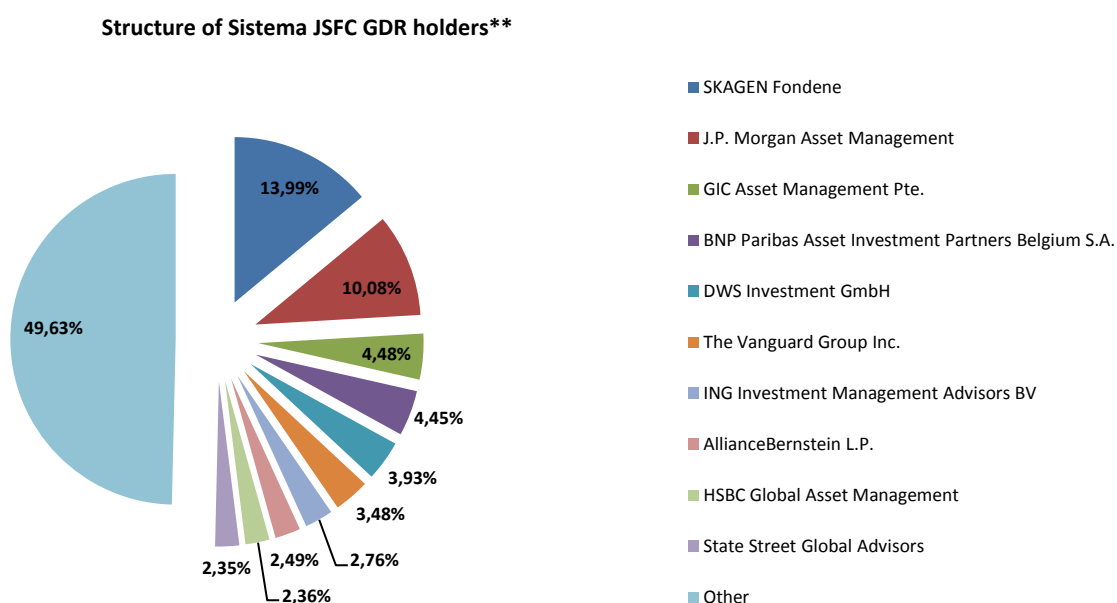
The closing price of the shares of Sistema on the first day of trading of 2011 at MICEX was RUR27.24, and on the last day of trading of 2011 it was RUR23.41. The Corporation's ordinary shares reached their peak of RUR35.58 on 04 April 2011. The Corporation's ordinary shares reached their lowest price of RUR20.30 on 04 October 2011.



\* as of 31.12.2011

As of 31 December 2011, Sistema's shareholder register had 19 individuals and 9 legal entities, including 7 nominal holders, registered as shareholders.

The Chairman of the Board of Directors of Sistema JSFC Vladimir Evtushenkov, with 64.18% of shares, is the principal shareholder of Sistema JSFC.



\*\* of the total number of GDRs of Sistema as of October 2011.

## 2. PRIORITY BUSINESS AREAS AND DEVELOPMENT STRATEGY

### 2.1. Mission and strategy of Sistema JSFC

#### **Mission**

Sistema is focused on achieving long-term growth of shareholder value by deriving high returns on capital through diversified investments. The Group's investment portfolio is composed of unique businesses, including mature companies which generate stable cash flows and developing companies at a more dynamic development stage.

#### **Strategy**

Sistema intends to increase its shareholder value by means of proactive portfolio management and reinvestment of free and third party cash into new projects, and by means of increasing the level of return on invested capital on the existing assets by improving the quality of corporate governance and effective restructuring of the assets.

Sistema is guided by the following principles in taking investment decisions:

#### **Diversified portfolio of assets**

- Sistema aims to maintain a balanced portfolio that includes large cash-generating Core Assets, and Developing Assets that are at the active business development stage.
- The Core Assets constitute the major part of the portfolio of Sistema, which ensures material resources to maintain the financial stability of the Corporation and to implement a balanced investment strategy, including that in high-yield projects.
- Sistema aims towards industrial diversification into protective and cyclical industries in order to reduce the risks and the volatility of the portfolio.

#### **Investment focus on industries and geographies where Sistema has competitive advantages**

- Sistema is focused on industries and geographies of the current portfolio companies, which makes it possible to realize potential synergies.
- Sistema has determined the following attractive sectors for investment: agriculture, mineral fertilizers, infrastructure, transport and logistics, as well as chemicals and petrochemicals.
- In all cases investment decisions are only taken provided that the investment criteria for return on the capital of Sistema are met.

#### **Proactive approach to investment management**

- Sistema proactively manages its portfolio and aims to effect transactions that create the maximum value.
- The following rule is applicable to all investments:  $IRR > WACC$  over the investment horizon of 5-7 years.
- The Corporation takes advantage of the opportunities to restructure assets to create additional value.

#### **Engaging leading international and Russian companies as partners**

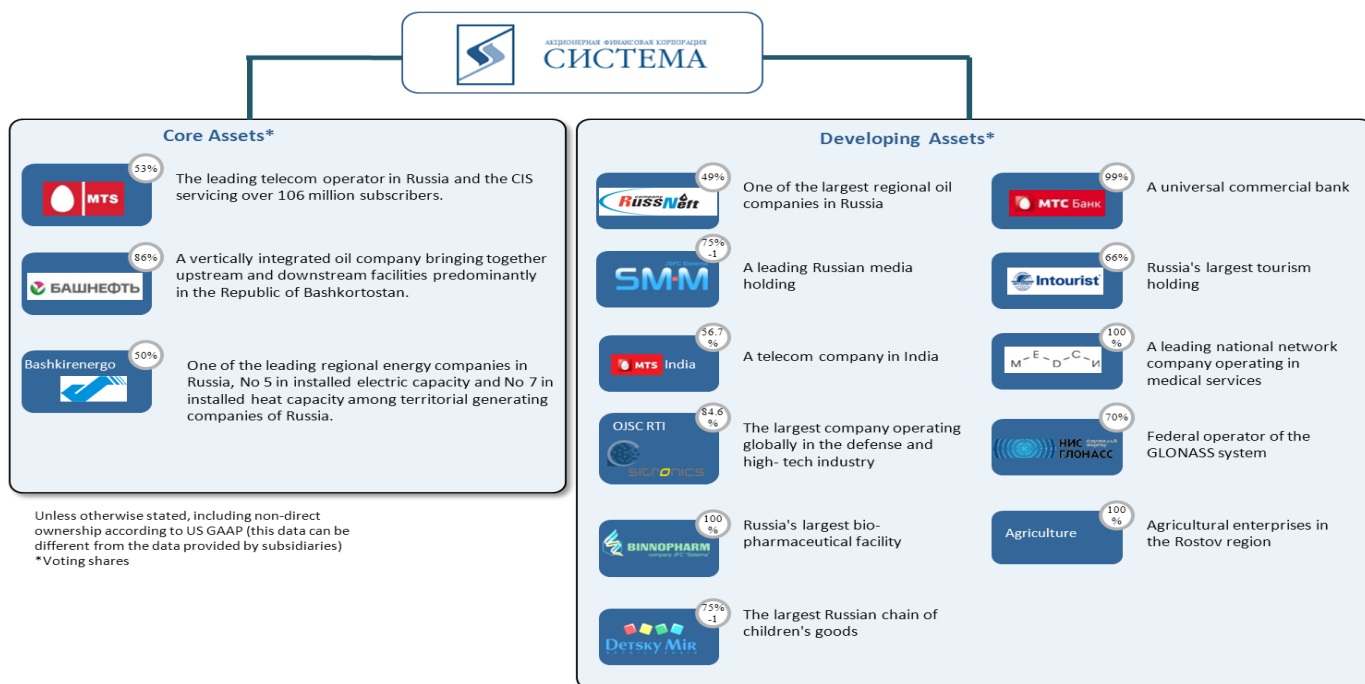
- Sistema continues to search for international and Russian partners for its portfolio companies with the purpose to improve the level of their industry expertise and use the best management practices.
- Engagement of partners also facilitates the diversification of financial risks and freeing up capital for new investments.

### 2.2. Portfolio of Sistema JSFC

The portfolio companies of Sistema are organizationally structured into two business units:

- Core Assets;
- Developing Assets.

The assets are grouped based on the principle of their maturity so as to ensure the target portfolio structure, where 80% of NAV<sup>2</sup> belongs to the mature assets (the Core Assets) generating a stable dividend flow, and 20% is contributed by the developing businesses (the Developing Assets).



<sup>2</sup> NAV – Net Asset Value



### 3. REPORT FROM THE BOARD OF DIRECTORS ON THE RESULTS OF THE COMPANY'S DEVELOPMENT IN THE PRIORITY AREAS

#### 3.1 Key Events in 2011

2011	February	In February 2011 Sistema JSFC and the Bank of Moscow established OJSC RTI. The Bank of Moscow, acting as an investor of RTI, contributed RUR 3bn to the authorized capital of the new company. Sistema JSFC contributed 97% of shares of the RTI Systems Concern and RUR2.88bn in cash in the authorized capital of the new company. As a result the stake of the Bank of Moscow amounted to 15.4% of the authorized capital of RTI, and that of Sistema – 84.6%.
		In March 2011 Mikhail Shamolin was appointed the new President of the Corporation.
	March	In March 2011 the transaction of the RF government acquiring a stake in Sistema Shyam TeleServices Ltd. (SSTL) was completed. During the additional placement of shares in favor of the RF government and the Indian shareholders, SSTL raised INR28, 894.5m (more than \$647m as of the date of the transaction) to its authorized capital. Rosimuschestvo, that represents the RF government, bought out 17.14% of SSTL shares to the total amount of INR26, 988m (about \$600m). Following the additional issue of shares, the stake of the Corporation in the authorized capital of SSTL amounted to 56.88%, and the stake of the Indian partners – 26.05%.
		In March 2011 the Board of Directors of Sistema JSFC approved the sale of the Corporation's stake in Sitronics to RTI. Sistema's Vice President and head of High-Tech and Industry Business Unit, Sergey Boyev, was appointed as the CEO of RTI. The transaction was completed in July.
	April	In April 2011 the Sistema Board of Directors approved a new organizational structure of the Corporation. The approval of the new structure was related to the implementation of the revised development strategy of Sistema JSFC adopted by the Board of Directors in October 2010, built around the migration from the operating holding model towards an investment company model.
	May	In May 2011 a subsidiary of Sistema JSFC, Sistema Invest, was reorganized by means of merging Bashkir United Energy Systems, UNH-EnergoInvest, UNPZ-EnergoInvest and Novoil-Energoinvest into it. Resulting from the reorganization, energy assets were separated from the oil ones.
		In May 2011 the Board of Directors recommended it to the General Meeting of the shareholders of Sistema to determine the amount of dividends on its shares for 2010 as RUR 2.509bn, which equals RUR0.26 per each ordinary share. The dividends were paid out in August 2011.
	July	In July 2011 the Forbes magazine called Sistema the fastest growing Russian company. The consolidated revenue indicator was used as the rating selection criterion. In 2010 Sistema was Number 342 on the rating with its consolidated revenues of \$28.099bn, having moved 118 positions up as compared to the previous list.
		In July 2011 Intourist and Thomas Cook Group completed the establishment of a joint venture. Thomas Cook acquired a 50.1% stake in the authorized capital of JV.
	August	In August 2011 Sistema Finance acquired 0.18% of ordinary shares of Sistema JSFC to be used for corporate purposes.
	Sept	In September 2011 Raphael Nagapetyants was appointed Senior Vice President of Sistema JSFC and Head of the Developing Assets Business Unit.

2011

November

In September 2011 Sistema JSFC received an indicative proposal from MTS regarding the acquisition of Sistema-Inventure for RUR10.56bn. At the moment of closing the transaction the core asset of Sistema Inventure was the block of 29.05% of ordinary shares of MGTS (24.4% of the authorized capital of MGTS). The transaction was completed in December 2011.

In November 2011 the Board of Directors approved the new dividend policy of Sistema JSFC. The recommended amount of dividend payments is determined by the Board of Directors and equals at least 10% of net income of the Corporation according to US GAAP (net of the paid-out special dividends). Following the recommendations of the Board of Directors the Company may also pay special dividends in the minimum amount of 10% of net income of transactions with an incoming cash flow, such as sale of assets, which is determined by the Board of Directors.

In November 2011 Sistema JSFC completed the buyback of its shares and GDRs and the buyout of the ADRs of MTS. In the course of the buyback, a subsidiary of Sistema acquired 375,972 GDRs of Sistema at the average price of \$16.61, and 8,745,100 local shares of Sistema at the average price of RUR20.97, and 4,311,019 ADRs of MTS at the average price of \$13.92.

In November 2011 Sistema JSFC gained the right to acquire 100% in state-owned OJSC Donskoye for RUR476.5m. Donskoye is located in the Rostov Region; the total area of land it uses is 25.4K ha. The transaction was closed in December 2011.

December

In December 2011 Sistema JSFC gained the right to acquire 100% in the state-owned OJSC Horse Farm n.a. the 1st Cavalry Army for RUR 303m. Horse Farm n.a. the 1st Cavalry Army is located in the Rostov Region; the total area of land used for agricultural purposes is 21.5K ha, including 17.5K ha of arable land.

### **3.2. Events after the reporting period**

2012

January

In January 2012 Sistema JSFC, OJSC RTI and LLC NVision Group Management Company signed a framework agreement that regulates the principles of future relations of the parties and defines the terms of the transaction of strategic integration the RTI and NVision Group assets. In accordance with the agreements reached, RTI shall acquire 50% of NVision Group from its shareholders. Moreover, the shareholders of NVision Group shall swap the remaining 50% of the company's shares into the newly issued shares of RTI. Resulting from the transaction the shareholders of NVision Group will get up to \$200m in cash and will become holders of a material share in the equity of RTI, having received a notable representation on the Board of RTI and an opportunity to influence its key decisions.

	<p>In February 2012 MBRD announced a change of its company name with the new name being OJSC MTS Bank, having taken the brand of MTS as the basis for further development.</p>
February	<p>In February 2012 the High Court of India canceled 122 licenses of eight telecom operators in India, including 21 licenses of Sistema Shyam TeleServices Ltd. (SSTL). The court ruled that the licenses had been granted to the operators within procedures that were not consistent with the procedures and requirements of the Indian Department of Telecommunications. The High Court of India ordered the supreme regulator of the Indian telecom market, TRAI (Telecom Regulatory Authority of India), to develop, within four months, new recommendations as to the issuance of 2G licenses and the redistribution of the frequency spectrum via an auction to be organized by the Indian Department of Telecommunications. In March 2012 SSTL filed a request with the High Court of India to have this ruling reviewed. SSTL also filed a petition to have the cancellation of licenses suspended as long as the request on the review of the court ruling is under consideration.</p>
	<p>In February 2012 Sistema sent to the address of the Republic of India an official notice on a dispute under the Agreement between the Government of the Russian Federation and the Government of the Republic of India for the Promotion and Mutual Protection of Investments. The notice was related to the ruling of the High Court of India dated 2 February 2012 on the cancellation of 122 telecom licenses, including 21 licenses held by SSTL.</p>
	<p>In February 2012 Sistema JSFC increased its stake in the authorized capital of NIS from 51% to 70% by purchasing the newly issued shares of the company. Sistema JSFC paid for the shares by contributing its 51% stake in M2M Telematics to the authorized capital of NIS.</p>
2012	<p>In March 2012 Bashneft announced the launch of the program for reorganizing, by means of a merger, of its subsidiaries - UNPZ, Novoil, Ufaneftekhim, Bashkirnefteprodukt and Orenburgnefteprodukt.</p>
	<p>In March 2012 SITRONICS announced its intention to sell 3% in INTRACOM TELECOM. If the transaction is completed, the share of SITRONICS in INTRACOM TELECOM will shrink from 51% to 48%.</p>
March	<p>In March 2012 RTI announced its intention to make a voluntary offer to the minority shareholders of SITRONICS regarding the acquisition of 36.926% of ordinary shares from them at the price of RUR0.55 per share. The offer is applicable to all shares of SITRONICS (including the shares the rights to which are certified with global depositary receipts or GDRs) that are currently not held by RTI directly. The price of the offer represents a 37.5% premium to the closing price of SITRONICS' common shares on MICEX-RTS as of 22 February 2012 (the last trading day on MICEX-RTS before the day of filing the offer with the FSFM) and a 66.7% premium to the three-month volume weighted average price as of 22 February 2012. GDR holders are entitled to participate in the offer.</p>
April	<p>In April 2012 a decision was made to merge the assets of the Medsi Group with the assets of State Unitary Enterprise (GUP) Medical Center of the Moscow Mayor and Government Administration. The GUP will own 25% of the united company, and it is planned to sell another 25% to a strategic partner.</p> <p>In April 2012 Sistema announced the establishment of RZ Agro Holding Ltd., a joint venture with RZ Agro Ltd. that was founded in 2009 and is affiliated to the Sierentz Group. RZ Agro Ltd. and the Sierentz Group are controlled by members of the Louis-Dreyfus family.</p>

### 3.3. Russian Accounting Standards (RAS) financial results of Sistema JSFC

	2011	2010
Revenue, RUR K	29,208,979	42,188,113
Income (loss) from sales, RUR K	20,345,902	32,511,395
Net income (loss) in the reporting period RUR K	-13,605,646	111,694,947

#### Revenue structure:

	2011	RUR K 2010
Shareholdings: dividends receivable	28,658,070	41,390,818
Other income (rental, agent services, guarantees)	550,909	797,295
TOTAL:	29,208,979	42,188,113

The issuer's core business is managing stakes and shares in commercial organizations.

#### Structure of other earnings and expenses:

	2011	RUR K 2010
Interest receivable	2,799,878	2,615,670
Interest payable	- 5,698,818	- 9,912,875
Other income	116,447,056	184,967,477
Other expenses	- 149,036,660	- 97,152,643
TOTAL:	- 35,488,544	80,517,629

Negative re-valuation of investment in the publicly listed shares of MTS acted as the key driver of the reduction in the yield received by Sistema JSFC from non-core activities.

#### Efficiency indicators

	2011	2010
Productivity of labor, RUR K per employee	129,817	126,312
Debt to equity ratio	0.131	0.160
Long-term debt to the sum of long-term debt and equity	0.086	0.101
Coverage of debt with current income (profit) ratio	0.65	-0.23
Level of past-due debt, %	0%	0%

Analysis of the financial solvency and the level of the credit risk of the issuer suggest that in general the issuer has both material own resources and opportunities to raise additional credit resources without the risk of repayment of such funds becoming doubtful.

Long-term liabilities account for a major part in the structure of borrowings (ca 72%). Accounts receivable and payable are recurring.

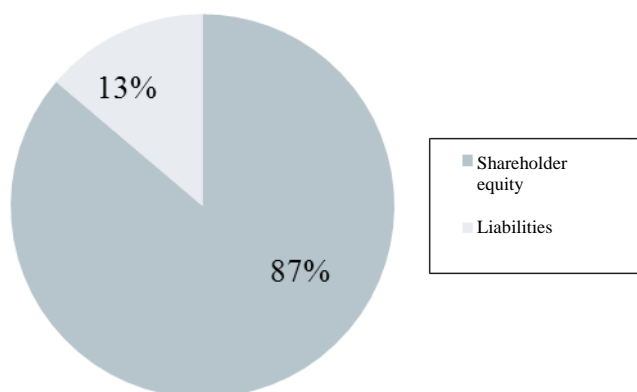
#### Financial stability indicators

	2011	2010
Net working capital, RUR K	68,720,564	
Current ratio	5.33	3.45
Quick ratio	5.32	3.45

The issuer's liquidity and solvency indicators are satisfactory.

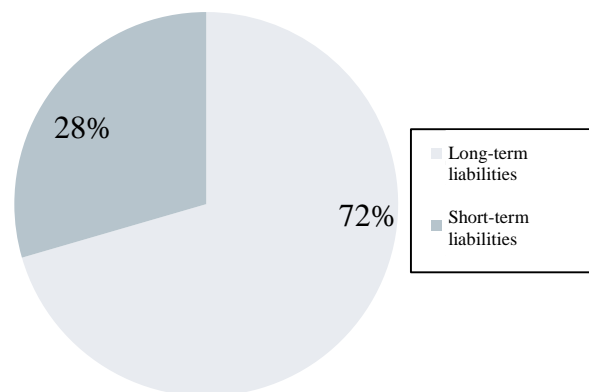
The amount of the issuer's own capital is sufficient to discharge its short-term liabilities and to cover its operating costs. As of 31.12.2011, the company's working capital amounted to RUR 84,587,482K, the volume of its short-term liabilities as of the mentioned date amounted to RUR 15,866,918K, production costs in 2011 amounted to RUR 115,373K

### Liabilities and shareholder equity



The share of own capital in the structure of the company's liabilities amounts to 87%.

### Structure of borrowings



Long-term debts account for 70% of the total volume of the company's liabilities.

### Data on fuel and energy resources and water expenditure

Type of resource	UoM	Spent in 2011	For reference: Spent in 2010
Boiler fuel	tons of fuel equivalent	0	0
Heat energy	G cal	2136,325	2567,724
Electric energy	thousand kW*h	6953,139	7055,029
Water	cubic meters	26582	28020

## 3.4. US GAAP consolidated financial results of Sistema JSFC

- Consolidated revenues grew by 23% up to \$33bn.
- OIBDA net of one-off adjustments increased by 16.2% year-on-year to \$8.3bn, OIBDA margin amounted to 25.1%.
- Net income of Sistema amounted to \$218.0m, net income net of one-off adjustments increased by 58.9% up to \$996.8m.

### Key financial indicators<sup>3</sup>

( \$ m, except for amounts calculated per one share)	2011	2010	Change
Revenue	32,981.2	26,811.3	23.0%
OIBDA <sup>4</sup>	7,223.1	7,165.4	0.8%
Operating income	3,941.5	4,302.6	(8.4%)
Net income (loss), stake of Sistema	218.0	918.7	(76.3%)
Base and diluted earnings per share (in US cents)	2.4	9.9	(76.3%)

<sup>3</sup> Q4 2010 and full year 2010 indicators were re-calculated to reflect the effect of terminated activities.

<sup>4</sup> See Annex A to financial statements: definition of OIBDA and its correlation with US GAAP financial indicators.

### Summary operating results of the Group

In 2011 consolidated revenue of Sistema increased by 23% year-on-year resulting from the substantial growth of the Core Assets and the Developing Assets business units' indicators.

Selling, general and administrative expenses in 2011 went 5.0% up year-on-year and reached \$3,936.6m, mostly due to the growth of commercial and marketing costs of the Developing Assets portfolio.

In 2011 the depreciation and amortization expenses increased by 14.6% vs. 2010 and amounted to \$3,281.6m due to the growth of the RUR/USD rate and the material volume of capital expenses in 2010.

Group 2011 OIBDA remained at the 2010 level as the growth of operating income resulting from the recovery of the margins of MTS and the operational success at Bashneft was offset with the write-offs following the cancellation of the SSTL licenses and the operating losses of companies of the Developing Assets business unit.

In 2011 the consolidated net income in the stake of Sistema went 76.3% down to \$218.0m as compared to \$918.7m in 2010 due to the concerns related to the cancellation of the SSTL licenses.

### 3.4.1. Review of operating results by the Business Unit<sup>6</sup>

#### Core Assets Business Unit<sup>6</sup>

\$ m	2011	2010	Change
Revenue	29,242.3	23,358.2	25.2%
OIBDA	8,617.0	7,598.0	13.4%
Operating income	5,670.5	5,027.5	12.8%
Net income, stake of Sistema	1,983.5	1,745.7	13.6%
Debt <sup>7</sup>	12,093.7	11,088.0	9.1%

\$ m	2011	2010	Change
<b>MTS</b>			
Revenue	12,318.7	11,293.2	9.1%
OIBDA	5,187.0	4,738.8	9.5%
Operating income	2,851.8	2,738.3	4.1%
Net income, stake of Sistema	769.5	756.4	1.7%
<b>Bashneft</b>			
Revenue	16,549.1	11,706.4	41.4%
OIBDA	3,390.7	2,892.9	17.2%
Operating income	2,778.8	2,301.4	20.7%
Net income, stake of Sistema	1,220.7	1,184.6	3.1%
<b>Bashkirenergo<sup>8</sup></b>			
Revenue	387.7	371.2	4.4%
OIBDA	99.3	94.7	4.9%
Operating (loss)/ income	57.7	55.9	3.3%
Net (loss)/ income, stake of Sistema	99.3	23.9	316.0%

The Core Assets business unit includes MTS, Bashneft and Bashkirenergo.

<sup>5</sup> Hereinafter the period-on-period comparison of revenues is shown on an aggregated basis, net of revenues from transactions within a segment (between companies in one segment) but before elimination of turnovers between the segments (companies in different segments) unless the word "consolidated" is present. Amounts attributable to specific companies are shown as necessary though before elimination of turnover within and between segments, and they may differ from respective stand-alone indicators of companies as some adjustments may be made.

<sup>6</sup> The results of the BU are shown in view of the consolidation of the Sistema Invest holding company.

<sup>7</sup> Hereinafter internal debt within the group has been eliminated.

<sup>8</sup> Due to the plans of Sistema regarding the sale of the generating assets of Bashkirenergo and pursuant to the US GAAP standards, all operations of this segment were excluded from the consolidation and reflected in the 'Income from terminated activities' line. The results of Bashkirenergo include operations of the distribution and transmission grids segments.

The revenue of the Core Assets portfolio increased by 25.2% in 2011 due to the substantial operating results of Bashneft against a background of favorable macroeconomic environment and the high oil prices, as well as the organic growth at MTS despite the high level of competition in the telecom industry in 2011.

The OIBDA of the portfolio increased by 13.4% over the year 2011 resulting from the growth of the portfolio's revenues and the optimization of its operating costs. A slight decline in the OIBDA margin from 32.5% in 2010 to 29.5% in 2011 resulted from the recognition of income from the revaluation of Belkamneft in the 2010 results of Bashneft which was virtually fully eliminated with the growth of MTS profitability.

Net income of the Core Assets portfolio in Sistema's stake grew by 13.6% year-on-year in 2011.

The 2011 revenue of MTS increased by 9.1% to \$12.3bn resulting from the growth of voice and data services consumption. The total subscriber base of MTS (including subscribers in the Republic of Belarus) reached 106.1 million subscribers as of 31 December 2011, with the growth amounting to .4 million subscribers.

The OIBDA of MTS increased by 9.5% in 2011 year-on-year resulting from the optimization of operating and marketing expenses and the growth of data consumption. The OIBDA margin stood at 42.1% in 2011 vs. 42.0% in 2010.

The revenue of Bashneft increased by 41.4% in 2011 vs. 2010 due to the growth of production volumes and oil prices against a background of a favorable macro-economic situation and consolidation of new acquisitions - Orenburgnefteprodukt and ASPEK. The share of Bashneft in the aggregated revenue of the portfolio increased to 57.0% in 2011.

The OIBDA of Bashneft went 17.2% up in 2011 as the company's revenues grew. The negative effects from the introduction of the 60-66 tax regime were leveled down with effective sales management actions and control over operating expenses.

In 2011 oil production volumes went 6.8% up as compared to the previous year and reached 15.1 million tons. In 2011 Bashneft achieved the optimum oil production level before the scheduled term. The volume of the company's export amounted to 3.6 million tons of crude oil and 9.2 million tons of oil products in 2011 vs. 3.2 million tons and 7.8 million tons respectively in 2010.

Due to the plans of Sistema to sell the generating assets of Bashkirenergo and in line with US GAAP, the results of Bashkirenergo only include operations of the distribution and transmission grids. All operations of the Generation segment were excluded from the consolidation and reflected in the "Income from terminated activities" line. The final decision on the sale will be announced within due procedures after the negotiations are completed, the binding documents are signed, and the shareholders have voted.

The revenue of Bashkirenergo went 4.4% up over the full year 2011 due to the growth of productive supply in distribution grids and the electricity transmission service tariffs.

The 2011 OIBDA of Bashkirenergo increased by 4.9% year-on-year due to the growth of the RUR/USD rate, with the OIBDA margin going up to 25.6% vs. 25.5% in 2010.

Electric power dissipation went 0.33 p.p. up in 2011 year-on-year due to the growth of supply to the grids and the changes in the methodology for dissipation calculation by the consumers, with dissipation in transmission grids increasing by 0.04 p.p. due to the factors involved in the re-distribution of electric energy from distribution to transmission grids.

#### *Developing Assets Business Unit*

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>4,578.4</b>	3,918.3	<i>16.9%</i>
OIBDA	<b>-1,029.9</b>	-42.8	-
Operating loss	<b>-1,355.6</b>	-327.6-	-

Net loss, stake of Sistema JSFC	-1,286.4	-222.6	-
Debt	3,069.9	2,541.1	20.8%

\$ m	2011	2010	Change
<b>SSTL</b>			
Revenue	262.3	114.6	128.8%
OIBDA	-730.0	-329.0	-
Operating loss	-828.1	-410.8	-
Net loss, stake of Sistema JSFC	-636.1	-349.7	-
<b>Sistema Mass-media</b>			
Revenue	101.9	94.5	7.9%
OIBDA	-32.0	40.5	-
Operating (loss)/ income	-73.7	2.2	-
Net loss, stake of Sistema JSFC	-63.9	-11.5	-
<b>RTI</b>			
Revenue	2,093.0	1,631.8	28.3%
OIBDA	154.4	180.6	-14.5%
Operating income	50.4	82.6	-39.0%
Net (loss)/ income, stake of Sistema	-18.3	-16.6	-
<b>Binnopharm</b>			
Revenue	38.5	32.1	19.9%
OIBDA	1.3	-27.9	104.8%
Operating income (loss)	-3.6	-34.1	-
Net income (loss), stake of Sistema	-4.4	-33.9	-
<b>NIS<sup>9</sup></b>			
Revenue	151.7	67.3	125.6%
OIBDA	8.4	4.6	82.7%
<b>MTS-Bank</b>			
Revenue	560.8	613.7	-8.6%
OIBDA	-6.2	39.9	-
Operating income (loss)	-23.5	21.3	-
Net income (loss), stake of Sistema	-19.9	10.1	-
<b>Detsky Mir</b>			
Revenue	782.9	659.9	18.6%
OIBDA	27.4	40.9	-32.9%
Operating income	9.8	24.4	-60.0%
Net income (loss), stake of Sistema	-5.6	-3.1	-78.2%
<b>Intourist</b>			
Revenue	276.6	518.2	-46.6%
OIBDA	43.8	6.9	538.4%
Operating (loss)/ income	34.5	-4.0	-
Net (loss)/ income, stake of Sistema	8.9	-15.5	-
<b>Medsi</b>			
Revenue	199.0	156.5	27.2%
OIBDA	31.1	17.1	81.4%
Operating income	19.6	8.1	143.0%
Net income (loss), stake of Sistema	6.7	-2.5	-

The Developing Assets business unit manages Sistema Shyam TeleServices Ltd. (SSTL), Sistema Mass-media (SMM), RTI, Binnopharm, MTS-Bank, Detsky Mir Group, Intourist, the Medsi Group (Medsi), Navigation and Information Systems (NIS) etc.

The revenue of the Developing Assets portfolio increased by 16.9% year-on-year in 2011, mostly due to the organic growth of virtually all of the companies of the portfolio. The 2011 OIBDA of the business unit was negative. The OIBDA of the portfolio was mostly affected by the recognition of the impairment of SSTL licenses

<sup>9</sup> The results of NIS are shown with the consolidation of the M2M Telematics results taken into account for presentation purposes.



following the ruling of the High Court of India on the cancellation of 122 telecom licenses, including 21 licenses of SSTL.

The revenue of SSTL increased by 128.8% in 2011 due to the 78% growth of the mobile services and data subscriber base in 2011 which reached the level of 15 million users. The year-on-year increase of the OIBDA loss is predominantly related to the recognition of the impairment of licenses, and the increase of the scale of business in all circles of the country.

Combined ARPU in 2011 reached the level of \$1.78.

In 2011 the revenue of Sistema Mass-media went 7.9% up year-on-year due to the growth of revenue from the distribution and aggregation of content resulting from the organic growth of the Stream TV Company, and the doubled revenue in the advertising segment. The OIBDA of SMM was substantially affected by the decline in the revenue of Russian World Studios (RWS) and the recognition of the impairment of the library of RWS following the revised forecast on secondary sales.

The subscriber base of STREAM-TV grew by 15.8% vs. 2010 and amounted to 6.2 million subscribers. The library of content of RWS grew by 21.6% year-on-year and reached 1,471 hours. The number of hours of proprietary content and the number of content sold by RWS in 2011 was 261 and 295 hours respectively.

RTI consolidates SITRONICS and RTI Systems Concern and includes 5 major business units: Defense Solutions BU, Comprehensive Security Systems BU, Telecom Solutions BU, Microelectronics Solutions BU and System Integration BU.

In 2011, the revenue of RTI increased by 28.3% as a result of successful implementation of the 1st stage of the project for establishment of the Intellectual Transport System of Moscow (Comprehensive Security Systems), additional projects of the System Integration business unit and growth of contract volumes as part of the government defense program (Defense Solutions).

The OIBDA of RTI went down in 2011 as compared to the previous year due to the proactive market expansion of the System Integration BU, the increase of the current expenses of the Microelectronics Solutions BU resulting from the planned growth of expenses related to the 90nm project, and due to the sale of the RTI stake in Watt Drive.

The revenue of Binnopharm increased by 19.9% year-on-year in 2011 thanks to the successful fulfillment of two governmental contracts for the supply of vaccines and the growth in the volumes of distribution in 2H 2011. The OIBDA of Binnopharm demonstrated growth throughout the reporting period as the gross income increased and as selling, general and administrative costs went down. This resulted in Binnopharm breaking even by net income in Q4 2011.

NIS (Navigation and Information Systems) is the federal network operator whose activities are focused on commercializing the GLONASS system (global navigation satellite system). The revenue of NIS in 2011 increased by 125.6% up to \$151.7 due to the implementation of major projects. This also affected the OIBDA indicator which demonstrated an 82.7% growth for the full year 2011 and reached the level of \$8.4m.

In 2011, NIS completed the creation of the prototype for the ERA-GLONASS system, which is its key and major project, and started its testing. Other major projects include creation of the intellectual transport system of Moscow (2,200 vehicles), a logistics and transport center in Sochi (more than 2,500 vehicles), the transport monitoring system for Transneft (6,500 vehicles) etc. In 2011, NIS and its regional partners equipped 150 thousand vehicles in 52 regions of Russia.

After the end of the reporting period in February 2012 MBRD announced a change of its company name with the new name being OJSC MTS Bank, having taken the brand of MTS as the basis for further development.

The revenue of MTS Bank went 8.6% down in 2011 due to the reduction in interest rates on loans and the depreciation of RUR vs. USD. The OIBDA of MTS Bank reduced following the recognition of losses from the revaluation of securities and the increase of provisions for loans due to the growth of the credit portfolio and the

review of the policy for provisions in 2011. The credit portfolio of MTS Bank increased, net of leasing, by 3.6% since 2010 up to \$5,004m as of 31 December 2011.

The revenue of the Detsky Mir Group grew by 18.6% in 2011 due to the implementation of the regional development program and the increase in the number of visitors. The OIBDA of the Detsky Mir Group shrank by 32.9% in 2011 as the operating costs related to opening shops in the regions increased, changes in the pricing policy occurred, the product range was optimized, and the loyalty program was launched. As of 31 December 2011, the network of retail outlets included 150 stores whilst the aggregate retail space was 236 thousand square meters. In 2011 Detsky Mir opened 21 new stores, including its first shop in Astana (Kazakhstan).

The revenue of Intourist fell by 46.6% year-on-year in 2011 due to changes in the method for accounting the tour operator and the retail business after the completion of the deal with Thomas Cook and the sale of the Pekin Hotel and Office Complex. The OIBDA of Intourist increased multi-fold year-on-year in 2011 as the profit from the Thomas Cook transaction was recognized in Q3. In 2011 the tour operation and retail segments serviced 725 thousand clients. The total number of hotel rooms in property, under management and rented was 2,866 as of the end of 2011 vs. 3,054 rooms in 2010. The decline in the room pool resulted from the sale of the Pekin Hotel and Office Complex in March 2011.

The revenue of the Medsi Group increased by 27.2% in 2011 vs. 2010 due to the expansion of the volume and the spectrum of services rendered and the growth in the number of visits. In 2011, Medsi successfully increased its client base thanks to the proactive marketing campaign, the offering of new services and the development of its product line. The OIBDA of Medsi grew by 81.4% in 2011, mostly thanks to the optimization of operating expenses and the reduction of selling, general and administrative costs.

In 2011 the number of patient visits and provided services increased by 19.9% and 24.6% respectively, and the average check went 6.1% up. One of the reasons behind the improvement of performance indicators was an increase in brand recognition from 41% in 2010 to 56% in 2011 (according to the Medsi Brand Health Assessment Report by LLC Indepth). In 2011 the largest family clinic was opened in Moscow and 40 medical stations were launched in various regions of Russia. The floor space of the clinics was expanded by 7.5% vs. 2010 - up to 50,424 square meters. As of 31 December 2011, Medsi was managing 30 clinics and 89 medical stations.

#### *Corporate & Other*

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
OIBDA <sup>10</sup>	<b>-219.0</b>	-281.2	-
Net loss	<b>-380.6</b>	-538.6	-
Debt	<b>1,246.8</b>	1,749.5	-28.7%

The Corporate Center and Other segment include companies that control the stakes of the Group in its subsidiaries and affiliates and manage them. The sum of dividends paid by the subsidiaries to the Corporate Center and Other segment in 2021 amounted to \$1,399.0m.

### **3.4.2. Financial overview**

Net cash flow from operations in 2011 grew by 37.3% up to \$5,571.4m due to the changes in the structure of the working capital.

Net cash flow from investment activities increased to \$5,186.9m in 2011 vs. \$4,839.3m in 2010. In 2011 the Group spent \$4,132.1m on capital investments vs. \$4,179.6m in 2010.

In 2011 the Group spent \$375.3m on acquiring new assets, net of cash received, including the acquisition of TVT and the Altair Group, the largest cable TV and BB operators in the Republic of Tatarstan and Tula, by MTS for \$162.9m and RUR680.0m respectively; acquisition of 94% of shares of Orenburgnefteprodukt by Bashneft for

<sup>10</sup> Hereinafter OIBDA and net income (loss) of the Corporate Center and Other segment are shown net of internal group dividends.

\$119.0m; acquisition of regional fixed communication operators by MTS, along with the acquisition of an alternative operator in Kurgan and the Altai Krai; the acquisition of the Moskovia TV channel by SMM. The Group also used \$341.1m to expand its bank assets.

Net cash-out from financial activities amounted to \$481.9m in 2011 as compared to \$6.9m in 2010. In 2011, the Group received \$6,241.0m of cash from loans and credits, whereas payments towards the repayment of its principal debt amounted to \$4,608.4m.

Cash balance of the Group as of 31 December 2011 amounted to \$2,924.0m (net of \$1,315.1m related to banking activities and cash from terminated activities amounting to \$83.7m) as compared to \$2,245.9m as of 31 December 2010 (net of \$2,308.5m related to banking activities and cash from terminated activities amounting to \$19.2m). Net debt of the Group calculated as the sum of short-term and long-term debt, net of cash and their equivalents and high liquidity deposits, amounted to \$12,478.1m as of 31 December 2011 vs. \$13,138.1m as of the end of 2010.

### **3.5. Credit ratings of Sistema JSFC**

	<i>Rating agency</i>	<i>Date of most recent update of the rating</i>	<i>Long-term credit rating</i>	<i>Forecast</i>
Sistema JSFC	Standard & Poor's	03.02.2012	BB	Stable
	Fitch	28.11.2011	BB-	Stable
	Moody's	12.04.2012	Ba3	Stable

### **3.6. Report on payment of announced (paid out) dividends on the shares of Sistema JSFC**

The resolution on the dividends payment was passed by the Annual General Meeting of the shareholders of Sistema JSFC on 25 June 2011 (Minutes # 2-11). Pursuant to the resolution of the General Meeting of shareholders, the amount of RUR2, 509,000,000.00 was allocated to the payment of the dividends, which corresponds to RUR0.26 per one ordinary registered share of Sistema JSFC.

As of 31 December 2011, the total amount of paid out dividends was RUR2, 508,999,980.64. Tax on dividend income paid to foreign legal entities was subtracted in the amount of RUR89, 539,479.

As of now, the amount of non-paid dividends for 2011 equals RUR19.36. As of 31 December 2011, the total amount of unpaid dividends was RUR276, 776.62. Reasons for non-payment of the announced dividends: lack of information required to remit the respective amounts to the recipients of the dividends.

## 4. OUTLOOK AND DEVELOPMENT STRATEGY OF THE SISTEMA GROUP

### 4.1. Core Assets

#### *Investment approach*

The Core Assets business unit is represented by companies being leaders of their industries which generate stable high cash yield in the form of dividends for the Group. The businesses have well-developed operations and service their liabilities independently. Sistema is the majority shareholder in the Core Assets.

#### *Management*

Felix Evtushenkov, First Vice President.

#### *Portfolio*

The business unit includes OJSC Mobile TeleSystems (MTS), OJSC Joint-Stock Oil Company Bashneft and OJSC Bashkirenergo.

<i>Company</i>	<i>Effective shareholding</i>	<i>Share in voting shares</i>	<i>Description</i>
MTS	53%	53%	The leading telecom operator in Russia and the CIS servicing over 106 million subscribers.
Bashneft	69%	86%	A vertically integrated oil company bringing together upstream and downstream facilities predominantly in the Republic of Bashkortostan.
Bashkirenergo	39%	50%+1	One of the largest regional energy companies in Russia.

#### *2011 results*

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
<b>Business Unit</b>			
Revenue	<b>29,242.3</b>	23,358.2	25.2%
OIBDA	<b>8,617.0</b>	7,598.0	13.4%
Net income	<b>1,983.5</b>	1,745.7	13.6%
Debt	<b>12,093.7</b>	11,088.0	9.1%

#### *Assets*

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
<b>MTS</b>			
Revenue	<b>12,318.7</b>	11,293.2	9.1%
OIBDA	<b>5,187.0</b>	4,738.8	9.5%
Net income, stake of Sistema	<b>769.5</b>	756.4	1.7%
Debt	<b>8,700.4</b>	7,160.6	21.5%
<b>Bashneft</b>			
Revenue	<b>16,549.1</b>	11,706.4	41.4%
OIBDA	<b>3,390.7</b>	2,892.9	17.2%
Net income, stake of Sistema	<b>1,220.7</b>	1,184.6	3.1%
Debt	<b>3,393.3</b>	3,927.2	-13.6%
<b>Bashkirenergo*</b>			
Revenue	<b>387.7</b>	371.2	4.4%
OIBDA	<b>99.3</b>	94.7	4.9%
Net income, stake of Sistema	<b>99.3</b>	23.9	316.0%

*Due to the plans of Sistema to sell the generating assets of Bashkirenergo and in line with US GAAP, the results of Bashkirenergo only include operations of the distribution and transmission grids segments. All operations of the Generation segment were excluded from the consolidation and reflected in the "Income from terminated activities" line.*

#### *Strategy*

The strategy of Sistema JSFC in Core Assets is focused on increasing the capitalization of investment and gaining a stable cash flow by means of keeping the leadership positions in the market and implementing a number of initiatives which will bring substantial strategic and financial benefits and create a foothold for long-term growth. Such initiatives include optimization and reorganization of the companies' structure, expanding the scale of business and achieving higher synergies, working on globalization scenarios, and application of best corporate standards and practices in governance. Businesses in the Core Assets portfolio are fully independent and all operations and business development is driven by their best-in-class management teams.

#### **4.1.1. MTS**

Mobile TeleSystems (MTS) is the largest telecommunications operator in Russia, Eastern Europe and Middle Asia. MTS offers mobile and fixed telephony, broadband Internet access and pay TV, as well as information and entertainment services in one of the most dynamically developing regions globally.

	<i>Effective stake of Sistema JSFC</i>	<i>Share of voting shares of Sistema JSFC</i>
MTS	53%	53%

The President of Mobile TeleSystems is Andrey Dubovskov, and the Chairman of the Board of Directors is Ron Sommer.

##### *Industry*

The Russian mobile telecommunications market is one of the most developed in the world, with the service penetration rate of 157%. The high saturation has led to a gradual shift in marketing efforts of mobile operators towards retaining existing subscribers by enhancing service quality and offering attractive products.

In 2011 the broadband market in Russia gained 10.9% and comprised 18.6m households. MTS ranks second in the Russian BB market by the subscriber base.

As of the end of 2011 the TV market in Russia included 21.7m households, and year-on-year growth reached 8.3%. MTS has a 14% share of the market by the volume of the subscriber base.

##### *Outlook*

Average annual growth on the Russian markets where MTS operates is projected at ~6% up to 2014, the mobile communications market remains the key contributor to revenue growth in absolute numbers (3-5% CAGR), while the highest growth rates are demonstrated by the broadband and the TV segments. One of the development trends is quite a high level of competition. The voice market is expected to demonstrate a slowdown of the aggressive growth of the customer acquisition numbers.

##### *Steady growth in 2011*

Given the strong competition, MTS shifts its sales strategy focus from enhancing sales towards a balanced customer retention strategy.

MTS has covered 14 thousand settlements with its 3G network. Total coverage of 2G and 3G networks of MTS has increased to 97% of the populated territory of Russia. The number of 3G base stations constructed in 2011 increased threefold as compared to 2010. At present, the 3G network of MTS numbers more than 23 thousand base stations.

In Moscow the large-scale GPON project was launched to replace copper cables with fiber-optic ones, which will provide for a multi-fold increase of the data transfer speed.

##### *Operational strategy*

MTS aims to strengthen its position as a leading national mobile operator in Russia and the wider CIS, in terms of both subscriber numbers and revenues.

The company plans to increase its revenues and improve customer loyalty by stimulating the use of MTS services with tariffs like Super 0 and Super MTS and with convergence services offerings within the GPON project of MTS in Moscow.

MTS pays priority attention to the development of the data segment and to launching new products with the purpose of effective monetization of mobile traffic, development of VAS services and improving the margins of content sales. MTS continues the program of 'MTS-Money' banking cards distribution, POS-credits, and other financial services via the federal retail network of MTS.

#### *Investment strategy*

Sistema JSFC views MTS as a core asset with prospects, capable of good growth tempos and increasing the shareholder value by means of successful implementation of its operating strategy. Aiming to get the maximum possible return on investment in the telecom segment, Sistema continuously monitors and analyzes the key trends and opportunities in the global telecom market.

#### *2011 results*

##### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>12,318.7</b>	11,293.2	9.1%
OIBDA	<b>5,187.0</b>	4,738.8	9.5%
Net income, stake of Sistema	<b>769.5</b>	756.4	1.7%
Debt	<b>8,700.4</b>	7,160.6	21.5%

##### **Operating indicators**

	<b>2011</b>	2010	<i>Change</i>
Mobile subscribers (million)	<b>106.1</b>	105.7	0.3%
ARPU (RUR)	<b>273</b>	253	7.9%
MOU (minutes)	<b>269</b>	234	15.0%

#### *Key events in 2011*

In February 2011 Sistema Inventure bought out 1% of MGTS shares within the mandatory tender offer at the price of RUR436.20 per one share. Thus Sistema Inventure spent ca RUR370m (ca USD12.3m) on the buyout. The buyout was performed within the framework of the mandatory tender offer to the minority shareholders of MGTS announced on 13 November 2010.

In March 2011 the MTS Board of Directors appointed Andrey Dubovskov as the President of MTS.

In March 2011 a voluntary buyout of shares was conducted as part of reorganizing MTS and merging it with Comstar-UTS, Dagtelecom and Eurotel.

In April 2011 the MTS brand was ranked as the most expensive Russian brand in the annual BRANDZ™ rating of the top-100 world brands for the fourth time in a row. This year the MTS brand ranked 80th with the brand value of \$10.9bn.

In October 2011 MTS acquired 100% in the authorized capital of OJSC TV and Radio Company TVT from a group of investors. The company renders cable TV, broadband access to the Internet and fixed telephony services in 15 cities of Tatarstan. The amount of the transaction was \$162.87m, excluding net debt of \$17.13m.

In December 2011, MTS completed the transaction for acquiring from Sistema JSFC a 100% stake in Sistema Inventure, which is the direct owner of 29% of ordinary shares of MGTS, for RUR10.56bn (the value of the transaction does not include the net debt of RUR10.41bn).

#### 4.1.2. Bashneft

OJSC Joint-Stock Oil Company Bashneft is a vertically integrated oil company comprising upstream and downstream facilities predominantly in the Republic of Bashkortostan.

	<i>Effective shareholding</i>	<i>Share in voting shares</i>
Bashneft	69%	86%

Alexander Korsik is the President of Bashneft, and Alexander Goncharuk is the Chairman of the Board of Directors.

##### *Industry*

Oil production in Russia increased by 1.3% in 2011 up to 511.4 million tons. Refining volumes grew by 1.8% vs. 2010 to 254.2 million tons.

Hydrocarbons production in Russia demonstrated the following three key trends in 2011. In the first place, a new record in oil production was set for the first time after the collapse of the Soviet Union, moreover, in H2 production outputs continued to grow and reached the current level of more than 10.3 million barrel per day. Secondly, many companies exceeded their own forecasts both for green-field and brown-field oil projects. Thirdly, positive results were achieved at the brown fields where production level demonstrated virtually no decline in 2011.

Because of the shortage of petrol in the petroleum products market, starting from 1 May 2011 the duty rate on high-grade petrol(s) was raised by the Russian Government up to 90% of the oil duty rate.

From 1 October 2011 the new tax plan for the oil industry called '60-66' came into force. The maximum rate of export oil duty went down from 65% to 60%, while the export duty on dark oil products was increased from 47% to 66%. The government provided compensation for the losses incurred by Bashneft and Tatneft as a result of introducing the '60-66' tax regime. The compensation payable to Bashneft for 4 years will amount to RUR10bn.

##### *Outlook*

According to oil companies' forecast, growth of daily production will speed up resulting from the increase in production at the East Siberian oil fields. The key challenge for the industry in the coming years is the need to abide by the requirements of the new tax regime and, consequently, to upgrade oil refining facilities, which will cause a material increase in the investment programs of Russian oil and gas companies.

##### *Steady growth in 2011*

Oil production output at the fields of Bashneft in 2011 amounted to 15.1m tons which represents a 6.8% year-on-year growth. Consequently, in 2011 Bashneft managed to achieve optimum oil production levels of the fields under development ahead of schedule. The company intends to maintain these oil production results in the medium term.

The average daily production of Bashneft in Q4 2011 was 41.8 thousand tons per day which is more than 30% above the level of Q1 2009; at the end of 2009 Sistema took over control in Bashneft. The primary drivers of the growth in oil production were the application of state-of-the-art technologies and the increased efficiency of geological and technical measures.

The Ufa Oil Refining Complex refined more than 21,062 thousand tons of crude oil in 2011, with the average refining depth indicator at 85.9%. The reduction of the light product yield down to 60% was due to the scheduled repair works performed on a number of secondary process units. As part of expanding its product range, Bashneft launched production of RT-grade aircraft fuel in April 2011.

##### *Operational strategy*

The strategy of Bashneft is aimed at increasing its value by boosting production of hydrocarbons and growing the oil and gas reserves, diversifying its asset portfolio, implementing a modernization program for refineries, developing own retail chain across Russia and enhancing efficiency along the whole of the value chain.

The company's upstream strategy provides for stabilization of oil production levels at the operating fields at approximately 15m tons per year, and launch of production as part of the Trebs & Titov field development. At the same time the company expects to obtain licenses for development of fields in some other regions.

The strategy also envisages development of the export logistics and expansion of the Company's retail chain from 440 to almost 1,200 fuel stations thus boosting the profit margins and making it possible to sell up to 80% of motor petrol through retail outlets.

#### *Investment strategy*

Sistema JSFC views Bashneft as having a material potential of growth via the implementation of the operating strategy, the development of the key assets and the improvement of the corporate structure. Sistema JSFC is also looking into new opportunities in the oil and energy sector that would increase the value of its investments in the oil and gas industry, including that via potential strategic partnerships and M&A transactions.

#### *2011 results*

##### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>16,549.1</b>	11,706.4	41.4%
OIBDA	<b>3,390.7</b>	2,892.9	17.2%
Net income, stake of Sistema	<b>1,220.7</b>	1,184.6	3.1%
Debt	<b>3,393.3</b>	3,927.2	-13.6%

##### **Operating indicators**

	<b>2011</b>	2010	<i>Change</i>
Crude production (m tons)	<b>15.1</b>	14.1	6.8%
Export (m tons)	<b>3.6</b>	3.2	12.2%
Refining (m tons)	<b>21.1</b>	21.2	-0.6%
Yield of light oil products, %	<b>60%</b>	62%	-2 p.p.

#### *Key events in 2011*

In February 2011, the Government of the Russian Federation took the decision to grant Bashneft the license for development of the R. Trebs and A. Titov oilfields. The license shall be valid for 25 years. The license field is located in the Nenets Autonomous District and its area is 2,151 km<sup>2</sup>.

In April 2011 Bashneft and LUKOIL signed an agreement on setting up a new joint venture for development of the R. Trebs and A. Titov oilfields. According to the agreement, LUKOIL acquires a 25.1% stake in the authorized capital of the subsidiary of Bashneft for RUR4.768bn, and the latter will receive a license for the use of subsoil deposits that include the R. Trebs and A. Titov oil fields in order to perform geological research, to explore and produce hydro-carbon materials. The JV in its turn will buy from LUKOIL 29 exploration wells located in these fields.

In April 2011, the Bashneft Board of Directors approved the new structure and appointed the new President - Alexander Korsik, who until recently was Senior Vice President of Sistema and Head of its Oil and Energy Business Unit.

In April 2011, Bashneft acquired 94.041% of the authorized capital of Orenburgnefteprodukt from RussNeft. As a result of the transaction Bashneft became the owner of 100% of ordinary registered shares and 76.16% of preference registered shares of Orenburgnefteprodukt.

In May 2011, Bashneft increased its stake in the authorized capital of Sistema-Invest up to 49.5%. The stake was increased by converting the shares of the Bashkir United Energy Systems, UNH-Energo-Invest, UNPZ-EnergoInvest, Novoil-EnergoInvest, owned by Bashneft and its subsidiaries, to the shares of Sistema-Invest. Resulting from the reorganization, the energy and the oil assets in the portfolio of the Corporation were separated.

In July 2011 Bashneft gained control over a company of the ASPEK group that operated in retail sales of oil products in the Udmurt Republic.



In October 2011 Bashneft gained rights to develop three subsoil blocks via an auction in the Nenets Autonomous District.

In December 2011 Bashneft gained rights to develop two subsoil blocks via auctions in the Republic of Bashkortostan.

#### **4.1.3. Bashkirenergo**

OJSC Bashkirenergo is one of the largest regional energy companies in Russia.

	<i>Effective shareholding</i>	<i>Share in voting shares</i>
Bashkirenergo	39%	50%+1

Andrey Makarov is the General Director of Bashkirenergo, and Felix Evtushenkov is the Chairman of the Board of Directors.

##### *Industry*

The key event in 2011 was the decision of the government to freeze tariffs for generation till the middle of 2012 with their slight readjustment in the second half year. If rapid growth of gas prices continues, this decision of the regulator will significantly deteriorate financials of companies in the industry for 2012. Moreover, after the capacity tender for 2012 the price of energy in the Center and Urals free power transfer zones reduced by 3.9% vs. the previous year.

##### *Outlook*

It is expected that after the presidential elections of 2012 the pressure of the government on the energy industry will be reduced and the financial situation of electric energy companies will be slightly improved.

Engagement in energy saving programs by consumers of energy may reduce the demand for electric energy and heat, and in the end this may deteriorate the position of heat generating companies with the least efficient production assets. After success in pilot projects is demonstrated, broader implementation of RAB regulation in the heat sector is expected.

In the sector of electric grids it is possible to carry out some actions as a preparation for mass privatization of distribution grid companies and implement pilot projects of privatizing some IDGCs.

##### *Steady growth in 2011*

In 2011 Bashneft implemented a range of projects within its organic growth program and in terms of organizational development and optimization. All the projects were aimed at ensuring the company's competitiveness.

The key achievement of 2011 is a full launch of generation assets on the wholesale electricity and capacity market, and in particular selling the major portion of electricity at free prices.

In December electricity substation Akberdino with 2x40 MVA transformers in the village of Akberdino was finished and commissioned (LLC BashRES). Also, the second line of the 220/110/10kV Zaton substation (LLC BSK) was commissioned in December.

Preparations were carried out for transferring distribution grids to the new method of long-term regulation (RAB regulation) starting from 2012.

## 2011 results

### Financial indicators\*

\$ m	2011	2010	Change
Revenue	387.7	371.2	4.4%
OIBDA	99.3	94.7	4.9%
Net income, stake of Sistema	99.3	23.9	316.0%

Due to the plans of Sistema to sell the generating assets of Bashkirenergo and in line with US GAAP, the results of Bashkirenergo only include operations of the distribution and transmission grids segments. All operations of the Generation segment were excluded from the consolidation and reflected in the "Income from terminated activities" line.

### Operating indicators

	2011	2010	Change
Transmission grids (LLC BSK), effective output (m kW)	21,296	21,425	-0.6%
Transmission grids (LLC BSK), loss (m kW)	315	310	1.6%
Distribution grids (LLC BashRES), effective output (m kW)	17,980	17,198	4.5%
Distribution grids (LLC BashRES), loss (m kW)	1,807	1,664	8.6%

### Operational strategy

The organic growth strategy of Bashkirenergo for 2012-2016 provides for the improvement of operating efficiency in all segments. The next strategic goals of Bashkirenergo are: transferring electric grids to RAB, entering new service markets in the spheres of energy service and energy saving, and introducing automation systems.

The company's strategy is implemented in close cooperation with the authorities of the republic, the region and the city. Activities aimed at increasing operating efficiency will improve the competitiveness of the company amidst restrictions for the growth of tariffs, and will significantly raise its attractiveness for investors.

### Investment strategy

The strategy of Sistema in electric energy is focused on increasing the capitalization of Sistema's investments in electric energy assets and is focused on several areas. The main one is the creation of a large interregional distribution grid company on the basis of one or several IDGCs and distribution grid assets of Bashkirenergo.

Currently grid assets have significant value growth potential due to the expected reduction of the pressure on the industry from the government (in particular - on grid infrastructure companies) after the RF presidential elections, the completion of energy grid companies' migration to long-term pricing under the RAB method, and the optimization of the regulatory framework as a result. Activities aimed at improving the operating efficiency of assets and achieving synergy effects should also contribute to the growth of the value of Bashkirenergo.

Selling generating assets (the sales segment was disposed of in 2011) with subsequent redistribution of funds to the more attractive segment of electric grids is one of the elements of the strategy. We also consider the opportunity of selling distribution grids and expanding to the electric energy markets abroad.

### Key events in 2011

In April 2011 the Board of Directors of Bashkirenergo resolved to recommend the payment of RUR1,084.9m, or 39% of net income, as dividends for 2010, and the allocation of RUR472.3m to financing investment programs.

In May 2011 Sistema JSFC announces reorganization of its subsidiary Sistema-Invest through a merger with the Bashkir United Energy Systems, UNH-EnergoInvest, UNPZ-Energo-Invest and Novoil-EnergoInvest. After the reorganization Sistema-Invest gained ownership of 50.17% of ordinary shares of Bashkirenergo (47.87% of the authorized capital). Resulting from the reorganization, the energy and the oil assets in the portfolio of the Corporation were separated.

In May 2011 the new General Director of Bashkirenergo, Andrey Makarov, was appointed.

In September 2011 the transaction of selling the electricity distribution company LLC ESKB, part of the Bashkirenergo Group, to ESK RusHydro (a subsidiary to OJSC RysHydro) was signed.

## 4.2. Developing Assets

### Investment approach

The Developing Assets business unit comprises investments that have high potential of creating and growing shareholder value and can later be either transferred to the Core Assets business unit, or taken to IPO or sold to a strategic partner to have their value monetized. In some cases developing companies need financing from Sistema JSFC or its guarantees on their debt liabilities.

### Management

Raphael Nagapetians, Senior Vice President.

### Portfolio

The Developing Assets portfolio includes companies that represent the interest of the Group in smaller growing businesses.

	Share	Description
RussNeft	49%	One of the largest regional oil companies in Russia
Sistema Mass-media	75%-1	A leading Russian media holding
Sistema Shyam TeleServices Ltd.	56.7%	A telecom company in India
RTI	84.6%	The largest company globally engaged in the defense industry and high tech
Binnopharm	100%	Russia's largest bio-pharmaceutical facility
Detskiy Mir Group	75%-1	Russia's largest distributor of toys for children
MTS-Bank	99%	A universal commercial bank
VAO Intourist	66%	Russia's largest tourism holding
Medsig Group	100%	A leading national network company operating in medical services
NIS*	70%	Federal operator of the GLONASS system

\*The stake is shown in view of the transaction of increasing the stake of Sistema in NIS in February 2012.

### 2011 results

\$ m	2011	2010	Change
Revenue	4,578.4	3,918.3	16.9%
OIBDA	-1,029.9	-42.8	-
Net loss	-1,286.4	-222.6	-
Debt	3,069.9	2,541.1	20.8%

### Assets contribution

\$ m	2011	2010	Change
<b>RussNeft*</b>			
Revenue	5,590	4,496	24%
OIBDA	1,662	1,359	22%
Net income**	771	574	34%
Debt	5,403	6,364	-15%
<b>SSTL</b>			
Revenue	262.3	114.6	128.8%
OIBDA	-730.0	-329.0	-
Net loss, stake of Sistema JSFC	-636.1	-349.7	-
Debt	1,573.5	1,245.9	26.3%
<b>Sistema Mass-media</b>			
Revenue	101.9	94.5	7.9%
OIBDA	-32.0	40.5	-

Net loss, stake of Sistema JSFC	-63.9	-11.5	-
Debt	46.1	16.3	181.8%
<b>RTI</b>			
Revenue	2,093.0	1,631.8	28.3%
OIBDA	154.4	180.6	-14.5%
Net loss, stake of Sistema JSFC	-18.3	-16.6	-
Debt	1,126.5	917.4	22.8%
<b>MTS-Bank</b>			
Revenue	560.8	613.7	-8.6%
OIBDA	-6.2	39.9	-
Net (loss)/ income, stake of Sistema	-19.9	10.1	-
<b>Binnopharm</b>			
Revenue	38.5	32.1	19.9%
OIBDA	1.3	-27.9	-
Net loss attributable to Sistema JSFC	-4.4	-33.9	-
Debt	6.8	2.7	150.9%
<b>Detsky Mir</b>			
Revenue	782.9	659.9	18.6%
OIBDA	27.4	40.9	-32.9%
Net loss, stake of Sistema JSFC	-5.6	-3.1	-
Debt	125.5	121.3	3.4%
<b>Intourist</b>			
Revenue	276.6	518.2	-46.6%
OIBDA	43.8	6.9	538.4%
Net (loss)/ income, stake of Sistema	8.9	-15.5	-
Debt	102.4	166.0	-38.3%
<b>Medsi</b>			
Revenue	199.0	156.5	27.2%
OIBDA	31.1	17.1	81.4%
Net (loss)/ income, stake of Sistema	6.7	-2.5	-
Debt	69.3	71.9	-3.7%
<b>NIS***</b>			
Revenue	151.7	67.3	125.6%
OIBDA	8.4	4.6	82.7%
Debt	16.1	15.4	3.9%

\* For RussNeft, Net Income is shown in full (not the stake of Sistema JSFC only)

\*\* In line with the IFRS standards

\*\* The results of NIS are shown with the consolidation of the M2M Telematics results taken into account for presentation purposes.

## Strategy

Sistema JSFC views its developing assets as investments having good prospects of substantial value growth. Monetization of developing assets is intended via an IPO or sale of assets (parts of assets) to a strategic investor.

One of the ways of increasing value is M&A transactions, primarily in related industries. Attention will be primarily paid to the scale of projects and to returns on invested capital.

With the aim of developing the assets included in the Developing Assets business unit, Sistema will invest both its own funds and the funds of potential strategic partners. Partners will be expected not only to hold an equity stake but also to contribute operational and financial expertise in the respective industries.

In the medium term, the key areas for strategic development of these assets are as follows: (i) focusing on sustainable organic development of the companies, (ii) control of their debt and (iii) proactive engagement of partners.

### 4.2.1. Sistema Mass-media

Sistema Mass-media (SMM) is a leading media holding of Russia that manages media assets in the area of pay TV, premium cinema and TV content production and advertising.

	<i>Sistema's stake</i>
Sistema Mass-Media	75%-1

Peter Gerwe is the President of Sistema Mass-media, and Andrey Smirnov is its Chairman of the Board of Directors.

#### *Industry*

In 2011 Russian media industry demonstrated material growth - the market volume increased 13% year-on-year having exceeded RUR700bn (according to PWC Global Outlook 2011-2015). The pay TV and the advertising segments were the key market growth drivers.

The key trend in the pay TV market is the growth of the viewers' interest to cable and satellite channels. In 2011 Russia's broadcasting network included more than 300 pay TV channels. The premium content segment saw stronger competition between the players and market consolidation.

#### *Outlook*

In 2012 the penetration of pay TV will reach 50% of all households in Russia. Growth will remain at the level of 12-15% (mostly due to the digital and satellite TV and IPTV segments). Growth in the number of premium TV channels, including channels in the HD format, as well as clear segmentation and emergence of narrower thematic niches will also be observed.

One of the key trends on the premium TV content market in 2012 will be greater competition from Internet portals, as well as tougher competition among market players and, consequently, higher quality of TV series products.

#### *Steady growth in 2011*

In 2011, the volume of the library of content of Russian World Studios grew by 21.6% and reached 1,471 hours. More than 500 hours of TV serials produced by RWS were broadcast by the largest TV channels of Russia.

Following the latest trends in movie and TV production, RWS entered into an agreement with the on-line movie theater NOW.RU for broadcasting the latest releases of the movie industry on the Internet.

In the TV channels segment, the total subscriber base of the nine channels produced by STREAM rose by 15.8% and reached 6.2 million subscribers by the end of 2011.

In 2011, the process of restructuring the Maxima Advertising Agency (RA Maxima) was completed which resulted in revenues doubling in this business segment. During the year Maxima participated in tenders and was awarded contracts for the media budgets of such clients as VTB 24, MTS, Sun InBev, Lifan Motors, Technosila, Supra.

#### *2011 results*

##### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>101.9</b>	94.5	7.9%
OIBDA	<b>-32.0</b>	40.5	-
Net loss, stake of Sistema JSFC	<b>-63.9</b>	-11.5	-
Debt	<b>46.1</b>	16.3	181.8%

##### **Operating indicators**

	<b>2011</b>	2010	<i>Change</i>
Stream TV subscriber base	<b>6.2</b>	5.3	15.8%
Russian World Studios production load ratio, Moscow, %	<b>59.82%</b>	66.00%	- 6.2 p.p.

Russian World Studios production utilization ratio, Saint-Petersburg, %	44.27%	66.00%	- 21.7 p.p.
Library, hours	1,471	1,210	21.6%

### *Operational strategy*

Plans of SMM till the end of 2012 include development in all the segments, both with proactive organic growth of the business and M&A transactions. The key objective for SMM in 2012 is to form a content and distribution platform, as well as integration with the net content businesses of the Sistema Group.

### *Investment strategy*

The investment strategy of Sistema JSFC in relation to SMM is focused on turning the company into the leading media holding in Russia. Russia's media sector is growing at accelerated tempos, and the development of SMM will facilitate growing the shareholder value. In the medium term, Sistema may consider IPO or engaging a strategic partner to SMM.

### *Key events in 2011*

In May 2011, within the special events program of the 64th International Cannes Film Festival, SMM and Huawei announced the establishment of the Russian-Chinese Film Fund. The key area of the Fund's activities is developing cooperation between the two countries in the area of the most mass industry of culture, i.e. the media content production sphere.

In July 2011 the RWS Cinema Company raised a credit from ING Bank N.V. and Sberbank of Russia against a pledge of its video content library. The amount of the three-year credit was RUR1.2bn. This transaction is unique in the Russian corporate crediting market.

In November 2011 the appointment of Peter Gerwe as the CEO of SMM was approved. Andrey Smirnov, the predecessor to Mr. Gerwe in this capacity, will continue with the Sistema Group as the Chairman of the Board of Directors of SMM.

## **4.2.2. MTS Bank**

OJSC MTS Bank is a universal commercial bank, a Top 30 bank of Russia. The service network covers 49 cities of Russia. MTS Bank holds a stake in Dalcombank in Khabarovsk and East-West United Bank in Luxembourg.

	<i>Sistema's stake</i>
MTS Bank	99%

Andrey Shlyakhovoy is the Chairman of the Management Board of MTS Bank, Alexey Buyanov is the Chairman of the Board of Directors.

### *Industry*

The RF banking system is showing signs of recovery from the crisis but its development wholly depends on the current trends in the world economy.

In 2011, the growth rates of corporate lending stood at ca 25%. We can observe a stable decline in the margins, which is the strongest in the corporate sector.

Competition is growing in virtually all segments of the market, besides, in recent years there has been a stable trend towards the reduction in the number of banks and their enlargement (the number of banks is expected to go down to 800 by 2016).

The role of state banks continued getting stronger in 2011, and the presence of foreign capital in the Russian banking sector remained at virtually the same level in financial terms. Still, a range on international players

preferred to leave the market: these include subsidiaries of HSBC, Swedbank, Barclays, KBC (Absolut Bank) and others.

### *Outlook*

Recovery of the corporate lending market started in the large business sector and is gradually shifting towards the middle corporate segment and the small business segment.

The trend of credit cards squeezing out consumer credits in the retail segment continues. VIP crediting (affluent retail) remains the segment with the highest potential.

### *Steady growth in 2011*

In 2011 MTS-Bank continued implementing the approved strategy of building a universal bank of a federal scale. Retail business and services for small and medium businesses were defined as priorities within its strategy.

Joint projects with MTS were launched in terms of targeted express credits to buy user terminals and other goods at 2,400 POS of CJSC RTK. Sales of banking cards with special terms of crediting the account - MTS Money - were launched.

### *2011 results*

#### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>560.8</b>	613.7	-8.6%
OIBDA	<b>-6.2</b>	39.9	-
Net income (loss), stake of Sistema	<b>-19.9</b>	10.1	-

#### **Operating indicators**

	<b>2011</b>	2010	<i>Change</i>
Assets, \$m	<b>6,958</b>	7,880	-11.7%
Credit portfolio, \$m	<b>5,097</b>	4,675	9.0%

### *Operational strategy*

The Banking Group's development strategy is aimed at achieving leading positions among RF retail banks. The key development driver is cooperation with MTS, within which it is planned to intensify cross-selling of banking and the partners' products and services, which will help increase returns on the credit portfolio and the share of non-interest expenses.

Significant attention in terms of implementing strategic objectives is being paid to optimizing internal business processes of the bank, which will make it possible to materially cut costs and improve the quality of client service.

### *Investment strategy*

The strategic development model of the bank provides for complete integration of MTS-Bank and Dalcombank, as well as further expansion of cooperation with MTS. Investment in the re-branding of the Banking Group is an important part of the strategy and is designed to create a uniform concept for promotion of financial products and services under the MTS Bank brand.

### *Key events in 2011*

In November 2011 the Moscow MGTU of the Bank of Russia granted a petition from MTS Bank approving a subordinated loan agreement between MTS Bank and Sistema JSFC and including it as an additional source of capital. The capital was increased by RUR1bn.

In December 2011 Dalcombank started issuing UnionPay banking cards.

In February 2012 MBRD announced a change of its company name with the new name being OJSC MTS Bank, having taken the brand of MTS as the basis for further development.



### 4.2.3. Detsky Mir

The Detsky Mir Group is Russia's largest retail operator in the goods for children segment, whose structure includes the national retail network of Detsky Mir stores and the Yakimanka Children's Goods Gallery luxury center.

	<i>Sistema's stake</i>
Detsky Mir - Center	75%-1

Gennady Levkin is the General Director of the Detsky Mir Group, and Georgiy Kravchenko is the Chairman of the Board of Directors.

#### *Industry*

In 2011 the children's goods market in Russia gained 13% vs. 2010 and is currently valued at \$13bn. The high birth rate observed over the recent years is the main positive factor influencing the market growth and driving the increase in customer spending on children's goods. The toys for the children segment demonstrated robust growth of 22.5%.

The Government of the Russian Federation has taken a firm stand in terms of reducing the share on non-organized retail, infringing merchandise and cheap low quality products, and forms a respective regulatory framework. It should be noted that the development of modern retail formats, including retail networks and large format stores on both national and local level in the children's goods market leads to heightened competition.

#### *Outlook*

Over the next four years the market for children's goods is projected to double to \$23bn with the highest growth expected in the segment of newborn baby goods and toys. In Russia, consumer spending on toys still accounts for only a half of such spending in developed countries.

In the future, specialized stores, hyper- and supermarkets will serve as the key distribution channels for children's goods. The company estimates that by 2015 the share of on-line stores in total children goods sales in Russia will increase from 11% to 13%.

#### *Steady growth in 2011*

In 2011, Detsky Mir was actively enhancing its competitiveness by developing its retail chain and promoting its private labels, upgrading its stores by introducing new merchandising technology, loyalty programs and unique product offers.

In 2011 the Company successfully implemented its development program: 21 new stores were opened.

Also, in 2011, in cooperation with SGC London, a new concept of stores was developed which included improved visual representation, optimized product matrix and merchandising elements, and replacement of shop equipment. When implemented, this concept is expected to improve revenue per square meter and make the shopping experience more comfortable for the clients. Major roll-out of the new concept of stores will start in 2012.

#### *2011 results*

##### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>782.9</b>	659.9	18.6%
OIBDA	<b>27.4</b>	40.9	-32.9%
Net loss, stake of Sistema JSFC	<b>-5.6</b>	-3.1	-
Debt	<b>125.5</b>	121.3	3.4%

##### **Operating indicators**

	<b>2011</b>	2010	<i>Change</i>
Retail floor space, K sq. m.	<b>236</b>	215	10.3%
Number of outlets	<b>150</b>	131	14.5%

### *Operational strategy*

Significant potential for business efficiency improvement lies in further improvement of category management. The developed action plan in this area is expected to improve the revenue, the stock turnover, and to maintain the current trend of gross margin growth by increasing the share of private labels in the total turnover. The company also aims to expand the permanent customer base of the network by means of optimizing the product offering, the pricing model and the layout of the stores, as well as introducing a uniform loyalty program.

Further development of expertise in logistics, store management and head office work organization, as well as the development of proprietary operating platform, are also important tasks for the company in the medium term.

### *Investment strategy*

In the mid-term the children's goods market will maintain its status of one of the most attractive segments of the Russian retail market. The investment strategy of Sistema JSFC is about strengthening the leading position of Detsky Mir in the market and its further development via organic growth and M&A. In the medium term, provided that market situation is favorable, it is possible for the company to go for an IPO.

### *Key events in 2011*

In June 2011 Gennady Levkin was appointed the new General Director of Detsky Mir. He took over from Georgiy Kravchenko, Executive Vice President of Sistema JSFC who had been heading Detsky Mir since October last year, in this position.

In June 2011 Detsky Mir approved the regional development program up to 2013. In the next two years Detsky Mir will open more than 50 new stores in dozens of Russian regions. The total floor space of the chain will increase by more than 70 thousand sq. m. by 2013. The floor space of most shops will be from 1,500 to 3,000 sq.m. depending on the concept of the outlet, its location and the expected flow of visitors. It is expected that new stores will be opened under a new concept using modern selling technologies.

### **4.2.4. Intourist**

OJSC VAO Intourist is Russia's largest tourism holding.

	<i>Sistema's stake</i>
Intourist	66%

Alexander Arutyunov is the President of Intourist, and Sergey Drozdov is its Chairman of the Board of Directors.

### *Industry*

The situation in the tourism market in 2011 was determined by the force-majeure events that took place in Q1 (revolutions in some countries of North Africa and the Middle East, the earthquake and the man-made disaster in Japan). In the outbound tourism segment the demand was redistributed to Thailand, Turkey, India and Europe. The prices of tourism products increased with the exception of tours to Greece and Spain where price competition was extremely strong.

The reorientation of tourist flows and the increase in the average price partially offset the revenue losses incurred by the operators in Q1.

The hotel services market in 2011 demonstrated a trend towards increased capacity utilization which is due to the positive dynamics in inbound tourist flows and intensified domestic business tourism. Hotel operators resumed the implementation of their regional expansion plans.

### *Outlook*

It is forecast that in 2012 the existing demand structure in the tourism market will remain as regards distribution of price segments and concentration in the lower price segments. It is projected that average prices will grow except for the segments with acute fight for the market, that the influence of global European players will get stronger and

further structuring of the market will continue. The tendency of demand shifting toward independent tourism will remain strong.

In the hotel market foreign players will continue to expand in the regions while the prices are expected to rise insignificantly. In Moscow 3-star and 4-star hotels will continue to compete for customers.

The Internet will continue to serve as the communications and sales channel and its role will be increasing both in the tourist and in the hotel industries.

#### *Steady growth in 2011*

The main objective for Intourist in 2011 was to maintain its positions in the hotel market, keep its capacity utilization rates and ensure profitability of the hotels.

In July 2011, Intourist and Thomas Cook Group Plc, one of the leading tourist companies in the world, established a joint venture (JV), which comprises the tour-operating and the retail business of Intourist. Thomas Cook Group Plc. acquired 50.1% in the JV. Resulting from the transaction, Intourist now holds a stake in the JV and owns its hotel business.

#### *Investment strategy*

In the short-term, Intourist is considering an opportunity to engage a strategic partner to strengthen positions in the hotel services market and to then finance the development of the hotel network if the decision is made to expand. The engagement of a partner is also to help to apply best international practices in hotel business management.

#### *2011 results*

##### **Financial indicators**

\$ m	2011*	2010	Change
Revenue	276.6	518.2	-46.6%
OIBDA	43.8	6.9	538.4%
Net (loss)/ income, stake of Sistema	8.9	-15.5	-
Debt	102.4	166.0	-38.3%

*\*The 2011 results reflect the retirement of the tour operation and the retail businesses.*

##### **Operating indicators**

	2011	2010	Change
Rooms (owned and rented), K	2.9	3.1	-6.2%
Number of tourists, K	725	782	-7.3%

#### *Key events in 2011*

In March 2011 Intourist announced a sale of 100% of shares in the Pekin Hotel and Office Complex, proceeds from sales were partially used to cover debt liabilities.

In April 2011 Intourist conducted reorganization through the merger of the two managing companies, Intourist and Intourist Hotel Group. The merger of the two managing companies helped optimize the management structure, eliminate duplication of functions, which resulted in cost reduction of about 30%.

In July 2011 Intourist and Thomas Cook Group Plc completed the establishment of a joint venture (JV). Thomas Cook acquired a 50.1% stake in the authorized capital of the JV. The joint venture will focus its efforts on expanding the market share in tourism services in Russia and other CIS countries, uniting the advantages of two leading tourist brands with a long history.

#### **4.2.5. Medsi**

CJSC Medsi Group (Medsi) together with its subsidiaries is the leading national network rendering healthcare services in Moscow and other Russian regions.

	<i>Sistema's stake</i>
Medsi Group	100%

Tatiana Sergeyeva is the President of the Medsi Group, and Mikhail Shamolin is the Chairman of the Board.

### *Industry*

The Russian market of paid healthcare services continued to expand in 2011, having grown by 14% to RUR535bn year-on-year (according to BusinesStat). The key market growth driver is the growth of healthcare service prices. It is necessary to note that the industry demonstrated stability during the financial crisis of 2008-2010. In 2005-2011 the average annual growth of the market was 16%.

Contraction of the 'grey' market of healthcare services due to the strengthened governmental control and changes in the regulatory framework is seen as an important trend.

On 1 January 2011 the law “On compulsory medical insurance in the Russian Federation” came to force. This law allows private clinics to become a part of the mandatory medical insurance system. The influence of this law on the potential market volume is however still very low as mandatory medical insurance tariffs differ from real service costs.

The market is still very fragmented. But at the same time the trend of consolidation around the largest and most successful independent market players is present, and the economic crisis accelerated the withdrawal of small players from the market. Insurance companies continue to raise requirements for clinics entering into service provision agreements, and this also strengthens the position of the larger players.

### *Outlook*

According to analysts' forecasts, the growth rate of the paid healthcare services sector will be ca 12% per annum till 2015. An increase in the cost of services will still be the main growth driver.

It is expected that in 2012 state-owned medical facilities will become more active in providing paid medical services, and this may strengthen competition in some segments of the market. Starting from 2012 medical institutions are able to enjoy zero rate income tax if they meet certain business parameters.

### *Steady growth in 2011*

In 2011, Medsi continued to expand and remained the number one provider of paid healthcare in Russia. The share of Medsi on the RF market is 1.3% and on the Moscow market - almost 4%.

In 2011 the growth of revenues amounted to 27% year-on-year thanks to the expansion of the service range. The net income results were achieved due to the increase in the total number of patients, the growth of the average check indicators and the increased patient traffic.

In 2011 the company paid a lot of attention to optimizing the organizational structure and business processes. It started the process of standardizing the IT infrastructure and creating a shared information space.

At the end of 2011 a new Medsi clinic was opened at Prechistenka. The launch of this clinic was the first step in the program of standardizing clinics on the basis of a model format designed by the company which would provide for comprehensive healthcare services rendered to the patients using cutting-edge medical technologies.

A lot of new modern medical technologies were introduced at the clinic and diagnostics center at Belorusskaya. In the autumn of 2011 the Neurology Center was opened, the range of surgeries performed at the in-patient clinic of the medical center was expanded; new early diagnostics programs were introduced.

### *Operational strategy*

The key strategic goal of Medsi is to increase the value of the company by strengthening its leadership positions on the commercial healthcare market in Russia and developing high standards of medical services. The increase in the scale of the business, its efficiency and profitability will be achieved by operating on all target markets,

strengthening positions in promising nosologies, developing high-tech areas of medicine, managing quality, developing the system of direct sales to employers and individuals, continuing active cooperation with insurance companies and increasing brand awareness.

The company also plans to continue developing its regional network in Russia and the CIS and to open up to 30 new clinics for adults and children, including by means of potential acquisition of existing regional clinics with a good market position.

#### *Investment strategy*

The Russian market of paid medical services has a large growth potential and is one of the priority areas for Sistema JSFC. The Medsi Group plans to enter new market segments via effective M&As aimed at creating a player with full cycle of medical services.

The planned merger of Medsi with the assets GUP Medical Center, the leading complex of medical centers in Moscow, will allow the company to substantially strengthen its positions in the clinic and diagnostics segment of the Moscow market, enter the segment of high-tech hospital care and develop a new field - aftercare. As a result of the merger of medical assets on the basis of Medsi a new industry leader and the largest player with significant growth potential will be formed.

#### *2011 results*

##### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>199.0</b>	156.5	27.2%
OIBDA	<b>31.1</b>	17.1	81.4%
Net (loss)/ income, stake of Sistema	<b>6.7</b>	-2.5	-
Debt	<b>69.3</b>	71.9	-3.7%

##### **Operating results**

	<b>2011</b>	2010	<i>Change</i>
Visits, K	<b>4.1</b>	3.4	19.9%
Services provided, K	<b>7.5</b>	6.0	24.6%

#### *Key events in 2011*

In September 2011 the neurology center led by V. Shakhnovich, M.D., was opened on the basis of the clinical and diagnostic center at Belorusskaya.

In January 2012 Tatiana Sergeyeva was appointed the new President of the Medsi Group.

#### **4.2.6. RTI**

OJSC RTI is the largest holding operating in the segment of defense, comprehensive communication and security systems, system integration and microelectronics, the leading integrator of high-tech scientific and production companies. The production facilities of RTI have their own R&D infrastructure and implement projects in the area of radio and space technologies, navigation and microelectronic products that are unique in terms of their scale and complexity. OJSC RTI includes RTI Systems Concern (97%) and OJSC Sitronics (63.074%).

	<i>Sistema's stake</i>
RTI*	84.6%

*OJSC RTI includes RTI Systems Concern (97%) and OJSC Sitronics (63.074%).*

Sergey Boyev is the CEO of OJSC RTI, and Mikhail Shamolin is its Chairman of the Board of Directors.

#### *Industry*

**Defense:** The spending of the Russian government in the defense sector in 2011 exceeded \$50bn. Exports of Russian military products totaled more than \$11bn. The main segment of the defense market, where RTI is represented, is aerospace defense informational systems (\$1bn).

Security systems: In 2011 the Russian market of security systems was estimated at approximately \$7bn. The narrower segment of comprehensive security and management systems of the Russian regions is on the threshold of exceptional growth and is under strict control of the Russian Government.

Information technologies: In 2011 the Russian market of information technologies was worth \$22bn according to the analysts' estimations. At present, Russia is lagging behind the developed countries by the IT share in GDP; its market structure is also significantly different: supplies of equipment account for more than 50% of the IT market, the share of IT services and software is lower than in the USA and Europe.

Microelectronics: In 2011 the Russian market of microelectronics was worth \$1.7bn according to the analysts' estimations. The development of the Russian microelectronics market is at the top of the government's agenda, which ensures high growth rates of the industry.

#### *Outlook*

Defense: In accordance with the arms program adopted by the Government, the total public defense spending will reach approximately \$650bn by 2020. In 2012 government defense spending may reach \$60bn.

Security systems: At present, the security systems segment is one of the most fast-growing and promising. Projected market growth rate: 15-20%.

Information technologies: Due to the currently small market share in the segment of IT services and software compared to the developed countries, the growth of the IT market, especially the IT services market, will be exceptional and will reach 15%.

Microelectronics: In 2012-2015 the market for microchips used in RFID cards and tags is expected to grow, as well as the chips for documents with e-carriers of information. In 2012 the market growth rate is expected to reach 12%.

#### *Steady growth in 2011*

In 2011 the revenues of RTI rose by 28% and reached \$2, 093bn. The key drivers of successful development of the United Concern's business in 2011 are: growth in the area of defense solutions, participation in major government security programs and expansion of the company's presence in the systems integration market.

#### *Operational strategy*

The strategy of RTI is aimed at building a large Russian high-tech industrial concern.

The company will strengthen its positions in the government defense market by offering the state more cost-effective, high-tech and innovative solutions in defense and security and by breaking into new promising markets abroad. In the segment of civil security systems RTI will achieve its goals through the use of the best technologies, their localization and gradual replacement with own developments. One of the most important goals is to boost profitability by increasing the share of intellectual property in the value of the end product.

#### *Investment strategy*

Sistema plans to continue the integration and development of its high-tech assets in order to create the biggest player on the Russian high-tech market. With the purpose of implementing this strategy Sistema intends to simplify its asset ownership structure and improve the efficiency of asset management. RTI was chosen as a platform for uniting such assets, as it has the required management, operational and financial capabilities.

#### *2011 results*

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>2,093.0</b>	1,631.8	28.3%
OIBDA	<b>154.4</b>	180.6	-14.5%
Net loss, stake of Sistema	<b>-18.3</b>	-16.6	-
Debt	<b>1,126.5</b>	917.4	22.8%

### *Key events in 2011*

In February 2011, Sistema JSFC and the Bank of Moscow acted as the co-founders of OJSC RTI. The Bank of Moscow, acting as an investor of OJSC RTI, contributed RUR 3bn to the authorized capital of the new company. Sistema JSFC contributed its 97% stake in OJSC RTI-Systems Concern and RUR 2.88bn in cash to the authorized capital of the new company. Consequently, the stake of the Bank of Moscow amounted to 15.4% of the authorized capital of OJSC RTI, while the stake of Sistema JSFC amounted to 84.6%.

In March 2011, the Board of Directors of Sistema JSFC approved the sale of the Corporation's stake in Sitronics to OJSC RTI. Sistema's Vice President and Head of High-Tech and Industry Business Unit, Sergey Boyev, was appointed as CEO of RTI. The transaction of selling 63.074% of Sitronics shares to OJSC RTI was completed in July 2011.

In April 2011, SITRONICS signed a contract with the Moscow government for conducting works as part of the creation of the Intellectual Transport System of Moscow worth approximately RUR 6.2bn.

In June 2011, SITRONICS signed a partnership agreement with Rostelecom within the framework of the E-Government project.

In August 2011, RTI Systems Concern was again included in the 2010 ranking of 100 largest defense companies of the world.

In October 2011, SITRONICS together with MTS and LUKOIL launched the Express Filling Station project: the first in Russia touch-free payment system that uses the NFC technology at LUKOIL petrol stations.

In November 2011, RTI Systems Concern signed an agreement with the Brazilian corporation WEG on selling the stake equal to 74.9% of the authorized capital of the Austrian Group Watt Drive.

In December 2011, RTI and the Bank of Moscow signed a long-term financing agreement according to which the Bank of Moscow, a shareholder of RTI holding 15.4% of its authorized capital, provides RTI with long-term funding of \$115m and RUR 3.6bn for seven years for the purposes of RTI business development.

In January 2012, Sistema, RTI and NVision Group Management Company signed a framework agreement that regulates the principles of future relationship of the parties and defines the terms of the transaction of strategic integration of the RTI and NVision Group assets. In accordance with the agreements reached, RTI shall acquire 50% of NVision Group from its shareholders. Moreover, the shareholders of NVision Group shall exchange the remaining 50% of the company's shares into the newly issued shares of RTI. As a result of the transaction the shareholders of NVision Group shall receive up to US \$200m in cash and will become the owners of a substantial portion of the authorized capital of RTI thus obtaining broad representation on the Board of Directors and major decision-making powers.

In February 2012, RUSNANO and SITRONICS launched the production of microchips on the basis of 90nm technology. Launching the new line will double the production capacity of the plant and make it possible to reach the figure of 36K plates with the diameter of 200mm per year. The total budget of the project is RUR 16.5bn including co-financing from RUSNANO in the amount of RUR 6.5bn.

### **4.2.7. Binnopharm**

Binnopharm is a pharmaceutical company operating the largest in Russia full-cycle manufacturing of biotechnology drugs in line with the international quality standards GMP (Good Manufacturing Practice). The priority production areas of the company are the development and manufacturing of drugs for treatment of socially important diseases (oncology, hematology, infectious and respiratory diseases), as well as genetically engineered drugs, vaccines and cellular and tissue technology products for regenerative medicine.

	<i>Sistema's stake</i>
Binnopharm	100%

Aleksey Chupin is the CEO of Binnopharm, and Dmitry Zubov is the Chairman of the Board of Directors.

### *Industry*

The stable economic situation helped the Russian pharmaceutical market to develop steadily in 2011. Numerous legislative initiatives stimulated significant changes both in the structure of the market and in its quality.

The Government continues to pursue an import-substitution policy in the pharmaceutical industry by allocating grants to the Russian producers so that they could develop innovative products, and also stimulates domestic manufacturing of those pharmaceutical products which account for the main share of consumer spending.

The state is the key consumer of pharmaceutical products and it allocates substantial funding for government procurement of drugs (the government procurement segment demonstrated 11% growth compared to 2010).

However, in the past year the commercial retail sector became the key driver of the development of the Russian pharmaceutical market; it grew by 16% and reached the level of \$15.4bn. Significant growth was also demonstrated by the key market for Binnopharm – the inpatient care sector (\$4.57bn) – 14% growth vs. 2010 in cash terms.

### *Outlook*

The Russian pharmaceutical market continues to grow at a high rate and it is possible to forecast 10-12% growth for 2012. The healthcare modernization program launched in 2011 was designed for 2 years. Consequently, its implementation will determine the trends in the inpatient care sector of the pharmaceutical market in 2012 as well. Provided that the revenues of the Russian budget remain stable the segment may be expected to exhibit growth of up to 16%.

The commercial retail market will be growing at a slower rate: the population's incomes grow relatively slowly; the epidemiologic situation is also stable.

### *Steady growth in 2011*

In the second half of 2011 the company successfully restructured the business. Organizational changes were made and commercial and administrative expenses reduced. The drugs portfolio was optimized with the focus on high-margin biotechnological products. The team of Binnopharm's scientists prepared three new drugs for registration and launch on the market. Binnopharm started actively participating in government auctions for drug supplies. In 2011 more than 150 government tenders for supplies of pharmaceutical products were won. In 2011 two government contracts for supply of 10m Regevac B vaccines worth more than RUR 600m were fulfilled.

The Company's revenue growth in 2011 amounted to 20%; in Q4 2011 the company reached break-even. This was achieved, among other things, due to the government contracts for supply of Hepatitis B vaccines. New bronchial asthma drugs also significantly influenced revenue growth. In addition, the company significantly strengthened its positions in the drugs distribution segment which covers not only the sales of own products, but also distribution of products from external manufacturers.

### *Operational strategy*

Binnopharm has a goal of becoming one of the largest Russian developers and manufactures of pharmaceuticals and of conquering 50% of the Russian biotech drugs market. At the first stage of biotech production development the company expands the range of manufactured vaccines and launches its own production of erythropoietin  $\beta$  and interferon  $\alpha$ .

A proprietary distribution network in the Russian regions will make it possible to significantly increase sales volumes and capture up to 20% of the state procurement market of Russian medicines.



### *Investment strategy*

The investment strategy of the company provides for entering related segments by establishing the production of new promising medicines (erythropoietin, interferon, vaccines etc.) and expanding the geography of the business.

Creation of strategic alliances and joint ventures with large foreign producers of pharmaceuticals is an important part of the growth strategy. The goal is localization of the production of innovative medicines, transfer of technologies and their promotion on the Russian market. The company is also considering the options for acquiring local producers with a promising portfolio of medicines.

### *2011 results*

#### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>38.5</b>	32.1	19.9%
OIBDA	<b>1.3</b>	-27.9	-
Net loss, stake of Sistema	<b>-4.4</b>	-33.9	-
Debt	<b>6.8</b>	2.7	150.9%

#### **Operating results**

	<b>2011</b>	2010	<i>Change</i>
Capacity utilization, ampules	<b>16%</b>	11%	5 p.p.
Capacity utilization, tablets	<b>0.1%</b>	0.3%	-0.2 p.p.
Capacity utilization, aerosols	<b>3.5%</b>	1.8%	1.7 p.p.

### *Key events in 2011*

In March 2011, Binnopharm and Rosgosstrakh became partners of the Biocity cluster. The goal of the project is to build national innovative infrastructure for the development of drugs and commercialization of scientific developments in the spheres of pharmacology and biotechnology; development of existing and establishment of new research and educational organizations, participation in government programs.

In April 2011, UCB Pharma and Binnopharm signed a memorandum of strategic partnership designed to promote production localization and import substitution in Russia according to the government's 'Pharma-2020' strategy.

In November 2011, Binnopharm and Pharmimex signed a cooperation agreement. The companies will combine their efforts to study the pharmaceutical market, determine promising products in order to launch their joint development, manufacturing and distribution in the markets of Russia and the CIS. At the first stage of cooperation Pharmimex will organize the distribution of Binnopharm's products.

### **4.2.8. RussNeft**

RussNeft is an oil company, one of the top 10 largest oil holdings in Russia. Its proven and probable oil reserves exceed 2.2bn barrels, production output in 2011 was more than 13.6m tons.

	<i>Effective shareholding</i>
RussNeft	49%

Mikhail Gutseriev is the President of RussNeft, and Leonid Melamed is its Chairman of the Board of Directors.

### *Industry*

Oil production output in Russia reached 511.4m tons in 2011, which is 1.3% above the 2010 level.

Production of hydrocarbons in Russia in 2011 was characterized by three aspects. In the first place, a new record in oil production was set for the first time after the collapse of the Soviet Union, moreover, in H2 production outputs continued to grow and reached the current level of more than 10.3m barrel per day. Secondly, many companies

exceeded their own forecasts both for green-field and brown-field oil projects. Thirdly, positive results were achieved at the brown fields where a decline in production outputs was prevented in 2011.

Because of the shortage of petrol in the petroleum products market, starting from May 1st the duty rate on high-grade petrol was raised by the Russian Government to up to 90% of the oil duty rate.

From 1 October 2011, the new tax plan for the oil industry called '60-66' came into force. The maximum rate of export oil duty went down from 65% to 60%, while the export duty on dark oil products was increased from 47% to 66%.

### *Outlook*

According to the forecasts of oil companies the growth of daily production outputs at new Russian oil fields will be accelerated mainly due to the increase in production at the fields in East Siberia. Consequently, the production of liquid hydrocarbons in Russia will continue to grow in the next several years.

Compliance with the requirements of the new tax legislation and the consequent necessity to modernize oil refining capacities will pose the greatest challenges to the industry in the nearest future. Accordingly, we can expect a significant growth of the investment budgets of Russian oil and gas companies.

### *Steady growth in 2011*

In 2011 RussNeft increased its production of oil by 5% up to 13.6 m tons. The company became one of the leaders of the oil industry by production growth, exceeding the industrial average market rate of 2-3%. Revenue in 2011 went up by 24%, OIBDA – by 22%.

In 2011 the company completed the restructuring of its debt to Sberbank of Russia and Glencore and fulfilled all its accelerated payment obligations. The operating and management achievements made it possible to reduce the debt burden by \$ 0.96bn down to \$5.4bn as of the end of 2011.

### *Operational strategy*

In 2012 the company intends to maintain a steady and dynamic growth of production volumes. In 2012 RussNeft plans to reach oil production level of 14m tons with \$610m in capex. In the mid-term RussNeft expects its annual production output to reach 16m tons. The company also intends to speed up the process of debt repayment and reduce its interest payments.

### *Investment strategy*

Sistema JSFC believes that RussNeft has significant value growth potential. The key to realizing this value lies in the implementation of its operational and financial strategy which provides for an increase in production volumes, reduction of debt and expansion of reserves.

### *2011 results*

#### **Financial indicators\***

\$ m	2011	2010	Change
Revenue	5,590	4,496	24%
OIBDA	1,662	1,359	22%
Net income**	771	574	34%
Debt	5,403	6,364	-15%

\* In accordance with IFRS standards

\*\*Net income is shown in full and not as attributable to Sistema

#### **Operating results**

	2011	2010	Change
Oil production (m tons)	13.6	12.9	5%
Oil reserves (2P), bbl m	2,273	2,250	1%
Gas reserves, m cu ft	1, 313, 212	1, 217, 509	8%

### *Key events in 2011*

In December 2011, RussNeft refinanced some of its debt at LIBOR+ 4.5% per annum. The signing of the loan agreement demonstrates the improved financial situation of RussNeft and sets the interest rate benchmark for potential creditors of the holding.

In July 2011, RussNeft sold its subsidiary refinery, Orsknefteorgsintez. The revenues from the sale of the refinery were allocated to the settlement of some of RussNeft's debt.

In January 2011, RussNeft signed a loan restructuring agreement with its main creditors – Sberbank and Glencore International AG. Prior to signing the agreement the total amount of debt stood at \$6.2bn. The maturity of the debt was extended to 2020. The interest rates became equal for both lenders and were reduced to 9% per annum.

### **4.2.9. SSTL**

Sistema Shyam TeleServices Ltd. (SSTL) is an Indian mobile operator providing services in 22 license circles, which include 28 administrative states and 7 union territories in India with the total population of approximately 1.16bn people.

	<i>Sistema's stake</i>
SSTL	56.7%

Vsevolod Rozanov is the President of SSTL, and Ron Sommer is its Chairman of the Board of Directors.

### *Industry*

In 2011, the mobile subscriber base in India gained 19% and reached 894m subscribers. The level of mobile penetration in India in 2011 increased from 62% to 74%; the revenue of the telecom industry in India also grew by 15%.

The number of broadband customers (fixed and mobile) in 2011 grew by 21%, but the penetration of the BB services is still low - 1.1%.

In 2011, the number of mobile subscribers continued to increase, but growth slowed down significantly. At the end of 2011, for the first time over the recent years GSM operators increased their mobile tariffs thus stimulating the growth of the mobile market's revenue.

The operators who had received 3G frequencies rolled out their networks and launched services with the focus mainly on users of phones with the Internet access. The market of smartphones, tablets and mobile applications started expanding rapidly.

### *Outlook*

The number of voice mobile customers continues to increase actively, but in the second half year of 2011 the growth rates began to decline. Further reduction of the growth rates of the number of voice customers is possible.

The broadband market is at the initial stage of development, in the nearest years significant growth of the mobile data market is probable due to the roll-out of 3G and EVDO networks and entry of the 4G (LTE) operators into the market in 2012.

At the beginning of 2012 the Supreme Court of India passed a ruling revoking 122 licenses, which created great uncertainty in the sector. SSTL took legal steps to protect its investments and waits for the Indian Government to issue guidelines on the new auction procedure.

### *Steady growth in 2011*

In 2011 the mobile network of the company was rolled-out in all of the 22 circles of India and a high-speed data network was made available in more than 300 Indian cities, 83% of the potential data market was covered.

In 2011 the SSTL business was developed in three main focus areas: development of data services, partnership and searching for consolidation opportunities.

The focus on the priority segment of data services included:

- 1) development of mobile data network covering more than 300 Indian cities and towns,
- 2) full coverage of the largest highways in the country: Delhi-Jaipur and Mumbai-Bangalore,
- 3) launching high-speed mobile data services under the Rev.B technology in Rajasthan,
- 4) development of distribution channels,
- 5) expansion of branded retail and engagement of new partners: Reebok, Levi's, HP, Kingfisher for stimulating the growth of the base of subscribers with high ARPU and improving the brand awareness.

The company started developing mobile data services together with Vodafone on the basis of the SSTL network.

### *Operational strategy*

The market strategy of SSTL is focused on the development of mobile data services and high-margin voice services in priority circles. The operating targets of SSTL include searching for partnership opportunities with GSM operators following the example of the partnership with Vodafone. As part of the consolidation strategy the company is negotiating with a number of operators and their shareholders, but the process is impeded by the uncertainty regarding the ruling of the Supreme Court of India on the revocation of licenses and by the delay in the issue of the new telecom policy that would facilitate the consolidation of the market.

### *Investment strategy*

The recent events related to the revocation of licenses created uncertainty in the Indian telecom market. Sistema JSFC continues to regard India as a promising growing market but it needs certainty and expects a fair ruling from the Indian regulator which will make it possible to continue this growth. Sistema JSFC fully supports SSTL and hopes to see the license dispute speedily resolved. After this issue is settled and other regulatory changes take place Sistema plans to expand the scale of SSTL's business through consolidation with a major telecom operator.

### *2011 results*

#### **Financial indicators**

\$ m	2011	2010	Change
Revenue	262.3	114.6	128.8%
OIBDA*	-730.0	-329.0	-
Net loss, stake of Sistema *	-636.1	-349.7	-
Debt	1,573.5	1,245.9	26.3%

*\*Taking into account the write-off of 21 licenses and the goodwill of SSTL following the decision of the Supreme Court to revoke 122 licenses including the 21 licenses of SSTL.*

#### **Operating results**

	2011	2010	Change
Mobile subscribers (m)	13.7	8.0	70.6%
Data subscribers (m)	1.3	0.4	-

### *Key events in 2011*

In March 2011, the transaction of the RF government becoming a shareholder of Sistema Shyam TeleServices Ltd. was completed. In the course of the additional issue of shares for the RF Government and the Indian shareholders, SSTL raised INR 28,894.5m (more than \$647m). On behalf of the RF Government Rosimushchestvo acquired 17.14% of the SSTL shares for the total sum of INR 26,988m (about \$600m). After the additional issue the stake of Sistema JSFC in the SSTL equity equals 56.68% and the stake of the Indian shareholders of SSTL – 26.05%.

In July 2011, Sistema Shyam TeleServices Ltd. started providing uninterrupted mobile broadband services along the Delhi-Jaipur highway.

In July 2011, Sistema Shyam TeleServices Ltd. expanded its cooperation with Ericsson in the Indian market. In September 2010 the companies signed a contract according to which Ericsson took over the management and servicing of multi-vendor wireless CDMA network of SSTL in two telecom circles of India: Delhi and Harayana. The new agreement prolongs the previous agreement for three more years and allows Ericsson to provide its services in four new telecom circles: Gujarat, Rajasthan, Eastern and Western Uttar Pradesh.

In August 2011, Sistema Shyam TeleServices Ltd. launched the most affordable smartphones on the Indian market on the basis of the Android operating system.

In September 2011, MTS India became the first CDMA operator in the world that uses the new-generation technological platform – EV-DO Rev. B Phase II.

In September 2011, Sistema Shyam TeleServices Ltd. took out a \$200m loan, \$100m of which was provided to the company by the ICICI Bank and \$100m by Barclays Bank. The three-year loan was secured proportionately by the letter of credit and the guarantee of Gazprombank.

#### **4.2.10. NIS**

NIS is a federal operator of the GLONASS navigation system which in its purposes may be compared to GPS. GLONASS provides positioning services to an unlimited number of land, sea, air, and space-based users in real time.

	<i>Sistema's stake*</i>
NIS	70%

*\*The data takes into account the acquisition of additional shares of NIS in February 2012.*

Aleksander Gurko is the CEO of OJSC NIS, and Evgeny Primakov is the Chairman of the Board of Directors.

##### *Industry*

At its present stage the navigation and information market is characterized by the following trends: the emergence of alternatives to GPS, the implementation of large-scale state projects in transport security on the basis of satellite navigation technologies, the use of navigation technologies for modernization of transport infrastructure, reduction of prices and improvement of the technical characteristics of products and services. Nowadays the domestic navigation market (motor vehicles) is already formed to a large extent and at the same time has significant growth potential for the following years. The key drivers of development (from 2013) are such major government initiatives as ERA-GLONASS and introduction of toll road systems for heavy transport.

##### *Outlook*

Today, the world navigation and information market is formed on the junction of a number of high-tech industries: microelectronics, car industry, IT and telecom sector, thus predetermining a fast growth of this segment of the global market. According to the report of the European Commission, the volume of the global market of navigation and information services will increase three-fold from EUR 41bn to EUR 125bn for the period 2008-2016. The largest segment is motor transport, which accounts for more than 56% of the market.

##### *Steady growth in 2011*

In 2011 NIS achieved significant progress in stepping up the introduction of GLONASS technologies in Russia and abroad, capitalizing on opportunities of the growing domestic market, creating the foundation of the future operating business and strengthening its leadership position. The revenue of the company increased more than twofold in 2011 vs 2010 and the headcount of NIS in 2010 doubled.

##### *Operational strategy*

NIS is an economically efficient public-private partnership, the leader of the Russian market, a large player of the global navigation and information market and a reliable technical operator of ERA-GLONASS.

One of the strategic development goals of the Company for the period until 2016 is to become an undisputed leader of the navigation and information market in Russia and the CIS and gain a firm foothold in the global market of navigation and information services. In order to achieve its strategic development goals, NIS actively stimulates competitive development and scaling of the navigation industry in Russia, and expands its competencies in the sphere of navigation (including by means of potential M&A deals).

The strategy of NIS is focused on four key business areas:

- 1) ERA-GLONASS is a governmental project that envisages the creation of an automated hardware and software complex and infrastructure for the emergency agencies' response to road traffic accidents.
- 2) Creating and introducing navigation and information systems.
- 3) Operator business for provision of navigation and information services on the basis of positioning for different categories of users: drivers, pedestrians and businesses.
- 4) Individual major projects related to the use of GLONASS technologies in Russia and abroad, such as: (i) the road toll collection system for heavy transport based on GLONASS, (ii) the system of tachographic control of truck drivers in terms of compliance with the work-rest regime on the basis of GLONASS (iii) other.

#### *Investment strategy*

We expect to achieve exponential growth of the shareholder value of OJSC NIS through organic growth and M&A partnerships.

With the view to fulfill this potential NIS plans to engage an international strategic partner, attract key players of the security and tracking systems market, capture leading positions in the international navigation and geoinformatics market.

#### *2011 results*

##### **Financial indicators**

<i>\$ m</i>	<b>2011</b>	2010	<i>Change</i>
Revenue	<b>151.7</b>	67.3	125.6%
OIBDA	<b>8.4</b>	4.6	82.7%
Debt	<b>16.1</b>	15.4	3.9%

##### **Operating results**

	<b>2011</b>	2010	<i>Change</i>
Equipped transport (thousand vehicles)*	<b>150</b>	60	150%

*\*Jointly with regional partners*

#### *Key events in 2011*

In March 2011, the Ministry of Economic Development of the Russian Federation and NIS GLONASS entered into an agreement for cooperation in developing new technologies to be applied in external economic activities.

In August 2011, as per the directive of the Russian Government, NIS GLONASS was awarded the government contract for conducting works related to equipping transport vehicles used for public purposes.

In September 2011, the federal network operator NIS GLONASS announced that starting from 16 September 2011 it was installing GLONASS devices in all of the transport vehicles to be used during the Olympic Games in Sochi.

In December 2011, NIS GLONASS registered a subsidiary, NIS GLONASS Pvt Ltd in the Maharashtra state of India, Mumbai. The aim of the subsidiary is to conduct the localization of equipment production and create software products, as well as ensure the roll-out and maintenance of a pan-Indian partner network of NIS Glonass.

In February 2012, Sistema JSFC increased its stake in OJSC NIS from 51% to 70% by purchasing the newly issued shares of the company. Sistema JSFC paid for the shares by contributing its 51% stake in M2M Telematics to the authorized capital of NIS. Consequently, NIS became the controlling shareholder of M2M Telematics.

## 5. DESCRIPTION OF CORE RISK FACTORS

The risks that may be faced by the business of the Corporation are diverse. Sistema JSFC has no or limited influence on many of the potential risk factors, therefore, efficient risk assessment and management remains an important element of Sistema's strategy.

The Corporation has introduced an integrated enterprise risk management system (ERM) that is designed to keep the level of risk within the limits that are acceptable for the shareholders and the management of the Corporation. The ERM system at Sistema JSFC was built in compliance with international standards, recommendations and best practices in risk management.

### 5.1. External risks

The external risks of Sistema JSFC include: risk related to the political situation and legislative changes in Russia and the countries of the Corporation's presence; risks related to the economic situation in Russia and the countries of the Corporation's presence; risks related to the situation on the financial markets.

#### *Political climate in Russia and the CIS*

The risks related to the political situation in Russia and the CIS are material for Sistema JSFC because most of the Corporation's business is conducted on the territory of the Russian Federation and the CIS countries. The Russian Government acts as a partner in several projects important for the Corporation.

Sistema JSFC estimates the political situation in Russia as stable and believes that at the moment there are no risks of any negative changes.

At the same time, there is instability in a number of neighboring CIS countries. Potential alterations in the laws of the countries where the Corporation operates, following some changes in the political situation, pose certain risks to Sistema JSFC; especially so, because private companies in these countries remain vulnerable to the influence of various political forces.

#### *Political climate in other countries*

Since the companies of the Corporation conduct their businesses and have partnerships with companies in India, South-East Asia, Africa and Central and Eastern Europe, in case of any major political turmoil in these regions the operations of the Corporation in the regions may be put on hold, which may lead to material losses. Besides, the operations of the Tourism business segment are also vulnerable to any major political risks.

#### *Economic situation*

The following factors can impact negatively on the economy of Russia and the countries of the Corporation's presence, and, accordingly, on the performance results of Sistema JSFC:

- 1) Considerable reduction in GDP.
- 2) Inflation rate
- 3) FX rate volatility
- 4) State budget deficit and high level of sovereign debt compared to GDP.
- 5) Insufficiently developed banking system which cannot ensure sufficient liquidity of national economy.
- 6) High level of capital outflow.
- 7) High level of corruption in the economy.
- 8) Quite high unemployment

#### *Financial risks*

The financial risks of Sistema JSFC include the following elements:

- 1) Forex risk:

Changes in the rate of the ruble, hryvna, euro and US dollar may have a considerable impact on the financial results of Sistema JSFC.

2) Interest rate risk:

In the current conditions the alteration of interest rates in the capital market will not lead to any considerable increase of our expenses because the predominant part of Sistema's borrowings has a fixed interest rate.

However, when raising funds for investments in the future we may encounter the situation when borrowing becomes more expensive. This prospect depends, in the first place, on the level of the future credit rating of the Russian Federation, the interest rates in the capital markets and the level of liquidity both in the Russian Federation and the world financial system.

3) Liquidity risk:

In order to service and refinance the current and future liabilities it may become necessary to permit considerable cash outflows. The ability to repay the debt may depend on many factors which are not always in our control. There is a risk of deepening world financial crisis (the risk of the so called "double dip" recession) which may lead to more severe borrowing rules and restricted access to liquidity. Another factor may be an undermined financial stability in a number of countries of the European Union.

4) Inflation risks:

Inflation may be another driver of the rise in expenses of Sistema JSFC. For quite a while the Russian economy has been showing high inflation rates.

In 2011, consumer market inflation amounted to 6.1%. The decline in inflation was ensured by a relatively low growth of food prices after significant growth in the previous year. The measures which were timely taken by the Russian government to overcome the imbalances of the grain market and stimulate import in the problem markets (fruits and vegetables) in conditions of stable ruble rate contributed to the reduction of price growth rates and inflation.

5) Stock markets:

There is a risk that the shares of Russian companies will be growing slower than those of their counterparts in other emerging markets. The key reason of that may be a substantial outflow of capital from the Russian market caused both by the political and economic factors inside the country and the situation on the world stock exchanges.

### *Legal risks*

The main material legal risks of Sistema JSFC include:

- 1) Risk related to forex regulations, customs control rules and duties, in particular, increase in the amount of cash that should be reserved when conducting operations with foreign currencies, increase in duties on goods, tightened customs control rules.
- 2) Risks of changes in tax legislation, in particular, increased tax burden, more complicated procedure for filing tax documents and new interpretation of the existing tax legislation.
- 3) Risk of changes in the legislation regulating the activities of the companies which have a significant stake in Sistema's revenues (telecom and oil sector companies).
- 4) Risk of changes in the legislation on stock exchanges and protection of investor rights, in particular, changes that can have a negative effect on the number of opportunities accessible to Sistema JSFC for conducting stock operations.
- 5) The unstable and insufficiently developed judicial and legal system of the Russian Federation, which may result in limited opportunities for protecting the rights of companies controlled by Sistema JSFC in court.



## **5.2. Risks related to the core activities of Sistema JSFC**

### *Implementation of the adopted strategy*

There are risks related to the inconsistency of the actual timeframes and parameters of M&A deals with the adopted portfolio strategy of the Corporation. The quality of the acquired assets may turn out to be significantly lower than expected. There are also risks related to volatility in the markets of the Corporation's presence, which can make the implementation of the current strategy inefficient.

### *Investment risks*

The investment risks of the Corporation arise from a combination of unfavorable economic and market conditions and factors that hinder the development of certain assets of the Corporation. This risk includes the following factors:

- 1) Stronger competition in the market and lack of opportunity to acquire assets meeting the strategic goals of the Corporation.
- 2) Potentially insufficient level of new investment and, as a consequence, inability of companies to meet targets.
- 3) The risk of inaccurate valuation of assets, incorrect price formation and timing of M&A deals.
- 4) Potential shortage of funding required for taking up attractive investment opportunities. Potential deficit of financial resources for conducting specific M&A transactions including the potential need to borrow cash on conditions that are not attractive for the Corporation.
- 5) Excessive dependence on a specific sector, economy and/or geography of presence.

### *Operational risks*

Operational risks include:

- 1) The risk of incomplete or untimely integration of newly acquired companies which makes it impossible to achieve planned synergies and retain the value of the acquired assets. The risk that the top management of Sistema will have to spend a lot of time to integrate the acquired companies.
- 2) Reputational risks related to implementing the Corporation's strategy and conducting operations of the portfolio companies. Risks related to recruiting and retaining qualified managers in the Corporate Center and portfolio companies.
- 3) Risk of inefficient cross-functional interaction, breach of the approved business processes or weakened control over the implementation of business processes.
- 4) Risk of fraud at the level of Corporate Center and the companies of the Corporation.

## 6. CORPORATE GOVERNANCE SYSTEM

### *Corporate Governance Principles*

Maintaining the corporate governance and the information transparency system at the highest international level is one of the elements of the strategy of Sistema JSFC as an investment company. The structure of the Corporation's corporate governance is based on the following core principles:

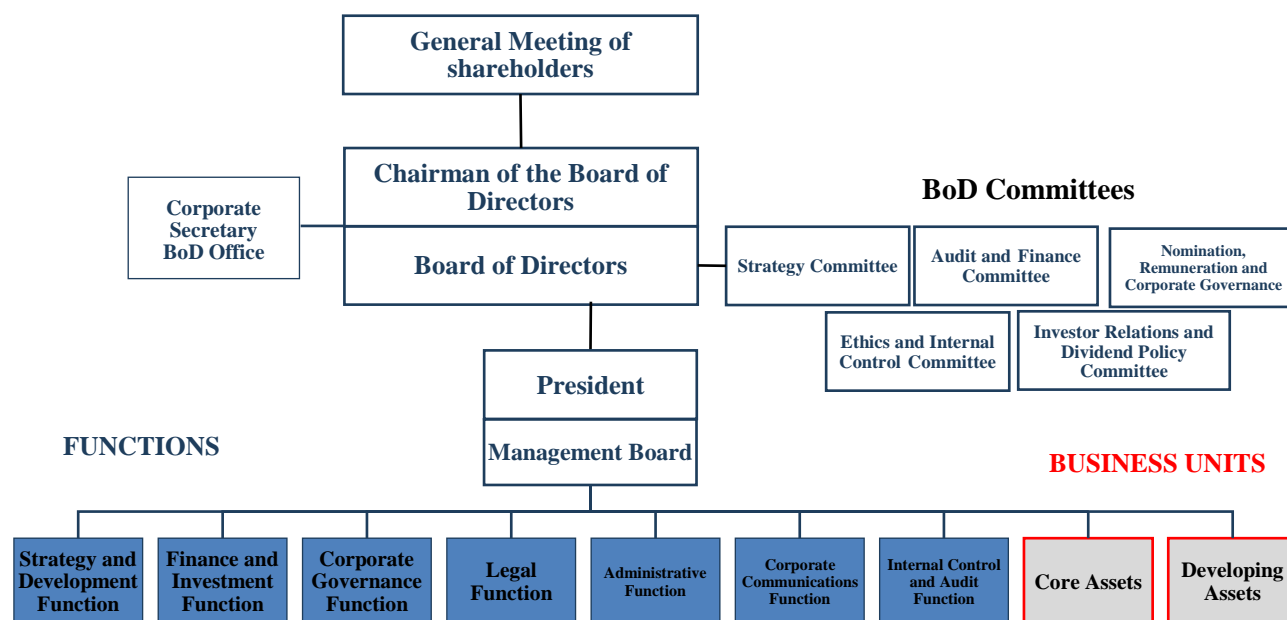
- 1) transparency of all processes for investors and partners,
- 2) a proactive and professional Board of Directors,
- 3) a consistent and collective approach to decision-making.

Sistema JSFC is guided by these principles in all of its activities, including strategic and financial management, corporate governance throughout the group, reporting, control and audit, risk management, HR and social policy.

The principles and procedures of Sistema's corporate governance are set out in its Charter and in a number of publicly available bylaws that, all together, determine the structure and the remit of the Corporation's governance and control bodies. The Corporate Conduct Code and the Ethics Code contain additional commitments of Sistema JSFC in the area of transparency, social responsibility, and ethical business principles.

Sistema JSFC takes every effort to bring its corporate governance practices in line with the guidelines set out in the Corporate Conduct Code recommended in Executive Order from the Federal Commission for the Securities Market of Russia No. 421/r dated 4 April 2002,<sup>11</sup> and in the UK Combined Code on Corporate Governance.<sup>12</sup> The consistency of the corporate governance practice of Sistema JSFC with the standards set out in the Corporate Conduct Code and the UK Combined Code on Corporate Governance is analyzed in the annex to this report. Should the corporate governance practice of Sistema JSFC diverge from the standards recommended in the above documents, the Corporation provides an explanation as to how else it makes sure that the balance of interests fixed in the applicable corporate governance standards is observed.

### *Corporate governance structure of Sistema JSFC*



<sup>11</sup> The text of the Corporate Conduct Code is available at the following address:

[http://www.fcsn.ru/ru/legislation/corp\\_management\\_study/corp\\_codex/](http://www.fcsn.ru/ru/legislation/corp_management_study/corp_codex/)

<sup>12</sup> The text of the UK Combined Code on Corporate Governance is available at the following address:

[http://www.fsa.gov.uk/pubs/ukla/lr\\_comcode2003.pdf](http://www.fsa.gov.uk/pubs/ukla/lr_comcode2003.pdf)

The Corporation's core governance bodies are: the General Meeting of shareholders, the Board of Directors, the President and the Management Board. The Board of Directors and the President have committees that work out recommendations for forming Sistema's policy in the respective areas. The organizational structure of Sistema JSFC includes seven functions and two business units that manage the Core Assets and the Developing Assets portfolios.

The current organizational structure was adopted in April 2011 and reflects the migration of Sistema JSFC towards the Investment Company model. As of the beginning of 2011 the organizational structure of Sistema JSFC comprised nine functions and four industrial business units.

## **6.1. General Meeting of Shareholders**

### *Principles of operation*

The General Meeting of shareholders is the supreme governance body of Sistema JSFC. Its operation is regulated by the laws of the Russian Federation on joint-stock companies, the provisions of its Charter, and the Corporation's bylaws. The procedure of conducting the General Meeting of shareholders aims to make sure that the rights of the shareholders are respected and all the legal requirements, as well as best practices in corporate governance, are observed.

Information and materials for the meeting are made available to the shareholders in Russian and in English, and are published on the official web site of Sistema JSFC. Along with the notice of the forthcoming meeting, shareholders acquire voting ballots. Venues of all meetings of Sistema's shareholders are conveniently located not far from the Corporation's head office. Holders of the company's depositary receipts have the opportunity to vote on the agenda items by means of proxy voting via Deutsche Bank Trust Company Americas, the depositary of Sistema JSFC GDR program.

*Global Equity Services,  
Trust and Securities Services,  
Email: gm.communications@db.com*

### *Observance of shareholders' rights to participate in running the company*

Sistema JSFC aims to ensure maximum protection of the shareholders' rights to participate in running the Company. The fundamental right of a shareholder in this respect is the right to participate in the work of the General Meeting of shareholders and the right to vote on items on the agenda. For this right to be secured a notice of the conduct of the General Meetings of Sistema JSFC is circulated to all the shareholders at least 30 days before the meeting, all materials are published on the website of the company in Russian and in English ([www.sistema.ru](http://www.sistema.ru)). Besides the notice on the General Meeting, Sistema JSFC also sends a voting ballot to each shareholder. The ballot can be filled out by the shareholder in advance and mailed to the Company to the address specified in the ballot. In this case the vote of the shareholder will be taken into account when counting the voting results.

Holders of depositary receipts for the Corporation's shares have the opportunity to vote by means of proxy voting via Deutsche Bank Trust Company Americas, the depositary of Sistema JSFC GDR program. The votes are collected by the depositary, Deutsche Bank Trust Company Americas, via clearing systems and are included in the general voting ballot of the depositary, with all votes cast for the proposed draft resolution, against it, and abstentions specified.

Each shareholder can also attend General Meetings of shareholders in person<sup>13</sup> and vote on the agenda items directly at the meeting.

One of the important rights of the shareholder in relation to participating in running the Company is the right to access documents that the Company is obliged to keep in line with the provisions of the Federal Law "On Joint-Stock Companies". To exercise this right, a shareholder should send a written request to the Corporate Secretary of

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<sup>13</sup> Or via a representative.

the Company asking for access to the documents that the shareholder is interested to see. After the time for providing the documents is agreed upon, the requested documents will be provided to the shareholder.

Holders of material blocks of shares are entitled to make proposals on the agenda of the General Meeting of shareholders, and to nominate candidates to the Corporation's governance and control bodies.<sup>14</sup> Proposals on the agenda of the Annual General Meeting of shareholders of Sistema JSFC are accepted in a written form, within 100 days after the end of the financial year.<sup>15</sup> Proposals received from shareholders are considered by the Board of Directors and, if the proposals meet the legal requirements to the work of the General Meeting of shareholders, the proposed items are included in its agenda.

### *General Meetings held in 2011 and their results*

In 2011 *two* General Meetings of the Company's shareholders were held.

*The Annual General Meeting of the shareholders of Sistema JSFC took place on 25 June 2011.*

The Annual General Meeting of shareholders approved the annual report, the annual accounts including the profit and loss report of Sistema JSFC for 2010, approved the amount, the procedure, the forms and the timelines for paying dividends on the shares of the Company, elected members of the Board of Directors and the Revision Commission, and approved the auditors of the Corporation.

Proceeding from the amount of the consolidated net income of Sistema JSFC for 2010 (RUR 27,900m (\$ 918.7m )), the Board of Directors of Sistema JSFC recommended that RUR 2,509m be allocated to pay out the 2010 dividends on the shares, which accounted for 8.99% of the consolidated 2010 net income of the Corporation according to US GAAP and is in line with the principles of the Corporation's dividend policy.

As resolved by the Annual General Meeting of shareholders following the recommendation made by the Board of Directors, RUR2,509,000,000.00 were allotted to pay out the dividends, which equaled RUR 0.26 per each ordinary share of Sistema JSFC. The amount of the dividend was more than 4.5 times as much as in 2010.<sup>16</sup>

The following auditors of Sistema JSFC were elected for 2011:

- CJSC BDO – to conduct the Russian accounting standards audit;
- CJSC Deloitte and Touche CIS – to conduct the US GAAP audit.

The auditors were suggested following an open tender organized by the Audit Committee of the Board of Directors of Sistema JSFC.

In 2010, *one Extraordinary General Meeting of shareholders* was also held in the form of a letter ballot:

18 March 2011	<p>The following agenda item was considered: Approval of a related party transaction: acquisition of the OJSC RTI shares issued upon incorporation of the company.</p> <p>The establishment of OJSC RTI has the goal of laying the foundation for a new Russian high-tech industrial Concern being a supplier of comprehensive innovative engineering, IT and microelectronics solutions for control and monitoring systems, systems for identifying and responding to threats to the state, business and individuals.</p> <p>At the stage of incorporating OJSC RTI it is planned to place its shares with two founders with the following target ownership structure:</p> <ul style="list-style-type: none"><li>- Sistema JSFC: 84.6% of the shares placed;</li></ul>
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<sup>14</sup> Holders of 10 and more % of the Company's voting shares also have the right to request an Extraordinary General Meeting of shareholders to be conducted.

<sup>15</sup> In the event an Extraordinary General Meeting of shareholders is conducted with its agenda containing an item on the election of the Board of Directors, holders of sufficient blocks of shares have the right to nominate candidates to the Board of Directors. Proposals to this effect must be received by the Company no later than 30 days before the date of such a meeting.

<sup>16</sup> In 2010, RUR 530,750,000.00 were allotted to pay out dividends.

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- Bank of Moscow: maximum 15.4 % of the shares placed.

It is proposed that Sistema JSFC shall contribute 97% of ordinary shares of OJSC RTI-Systems Concern at the valuation of RUR 13,600,000 and cash in the amount equivalent to \$96 million in rubles at the exchange rate of the Bank of Russia as of the date of the transaction – as payment for the shares of RTI that are being acquired. The value of the controlling stake in OJSC RTI-Systems Concern for the valuation purposes was defined based on the independent valuation by Ernst&Young.

Consolidation of the controlling stake in OJSC RTI-Systems Concern at the new company is the first step towards creating the new Concern.

The General Meeting of shareholders approved the proposed transaction

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## 6.2. Board of Directors

The Board of Directors of Sistema JSFC is responsible for strategic management of Sistema JSFC. It determines the strategy of the Corporation's development, works out strategic and financial development plans, sets the principles for investing, appraises executive performance and assesses risks, approves principles for corporate governance procedures, approves transactions and controls the work of the Corporation in general. The scope of powers of the Board of Directors is set out in the Charter of Sistema JSFC.

### *Board of Directors membership*

The Board of Directors in place as of 31.12.2011 was elected by the General Meeting of shareholders on 25 June 2011. The Board of Directors has 12 members:

#### BoD membership as elected on 25 June 2011\*

1	Vladimir Evtushenkov	<i>Chairman</i>
2	Alexander Goncharuk	
3	Ron Sommer	
4	Dmitry Zubov	<i>Deputy Chairman</i>
5	Vyacheslav Kopiev	
6	Robert Kocharyan	
7	Roger Munnings	
8	Leonid Melamed	<i>Deputy Chairman</i>
9	Evgeny Novitsky	
10	Serge Tchuruk	
11	Mikhail Shamolin	
12	David Iakobachvili	

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#### Overall membership of the Board of Directors includes:

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Executive director	1 (8.3%)	M. Shamolin
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\* See Annex for brief biographical notes and information on the stakes of the Board members in the authorized capital of Sistema JSFC

Non-executive directors	6 (50.0%)	V. Evtushenkov, A. Goncharuk, R. Sommer, D. Zubov, V. Kopiev, L. Melamed**
Independent directors	5 (41.7%)	R. Kocharyan, R. Munnings, E. Novitsky, S. Tchuruk, D. Iakobachvili

\*\* The powers of L. Melamed as the President and the Chairman of the Management Board of Sistema JSFC were terminated on 09 March 2011. R. Sommer was relieved of his duties as First Vice President of Sistema JSFC on May 13, 2011.

### *Changes in the membership of the Board of Directors*

The new Board of Directors does not include former members R. Mehrotra and S. Cheremin. At the same time, new independent directors have been elected to the Board: S. Tchuruk, D. Iakobachvili, who have extensive practical experience in managing large companies, as well as M. Shamolin as the President of Sistema JSFC.

### *Meetings of the Board of Directors*

Meetings of the Board of Directors are pre-scheduled. The Corporation has an Annual Calendar Planning Cycle (from January 1 through December 31). This practice makes it possible for the newly elected Board of Directors to maintain continuity and act on the basis of the previously approved plan. The agendas of the Board meetings are set proceeding from the logics of the strategic planning and reporting cycle of Sistema JSFC. Extraordinary meetings are called when it becomes necessary to review any urgent issues. The unplanned issues which may arise in the course of the Corporation's operations and which had not been included in the work plan of the Board of Directors are put on the agendas of the Board meetings as necessary upon the decision of the Board Chairman.

In 2011 the Board of Directors had ten sessions: eight scheduled meetings and two extraordinary sessions in the form of a letter ballot on urgent matters. In 2010 the Board of Directors considered 108 items in total.

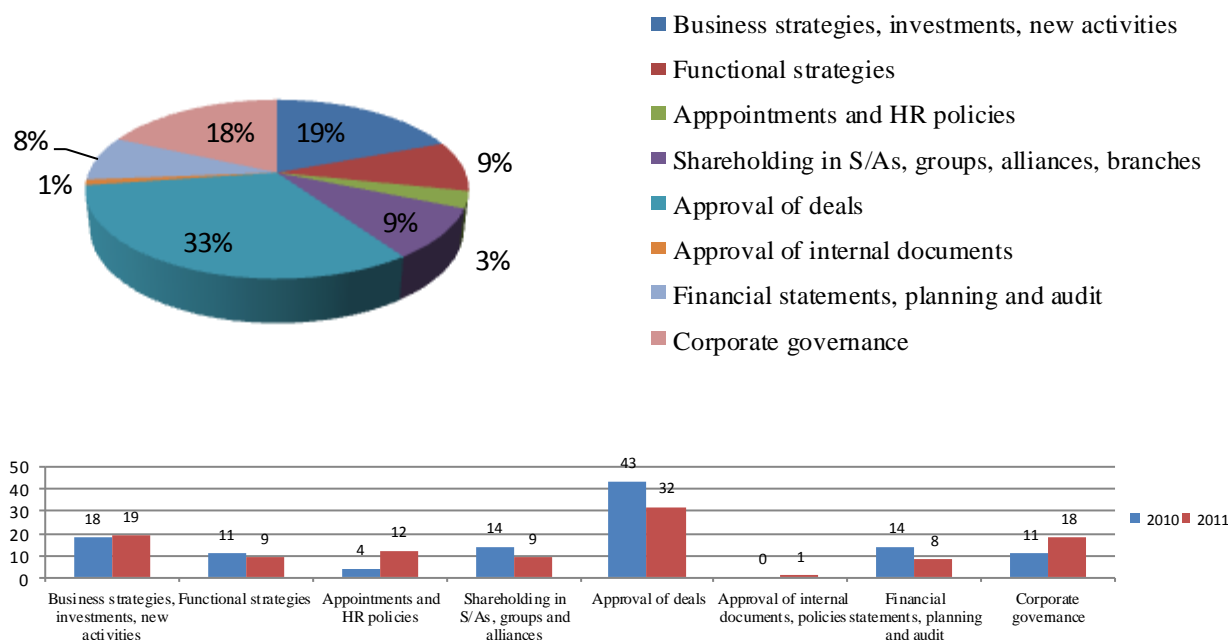
	<b>2011</b>	<b>2010</b>
Number of meetings held	<b>8</b>	8
Number of letter ballots	<b>2</b>	8
Number of items on the BoD work plan	<b>44</b>	46
Number of items considered by the BoD	<b>108</b>	115

In 2011 the Board of Directors considered the following key items:

- 1) Strategy of Sistema JSFC.
- 2) Development strategies of the Business Units of Sistema JSFC.
- 3) Development strategy of the main portfolio assets:
  - banking industry;
  - telecom assets;
  - oil assets;
  - electric power and grid assets;
  - development of the pan-Indian project on the basis of Sistema Shyam TeleServices Limited;
  - healthcare assets;
  - pharmaceutical assets;
  - implementation status of the RTI-Sitronics merger project.
- 4) Entering the agricultural industry.
- 5) The results of the analysis of the world regions and/or countries from the viewpoint of opportunities for entering new markets and selling and acquiring undervalued assets or assets that have synergies with the current assets of the Sistema Group.
- 6) Development of innovations and R&D activities of Sistema JSFC companies.
- 7) Implementation status of the strategy for managing the subsidiaries and affiliates of Sistema JSFC.
- 8) Financial performance results.
- 9) Approval of the consolidated budget of Sistema and Key Performance Indicators of the management for 2012.

- 10) Long-term financial and economic model of the Corporation's development.
- 11) The dividend policy of the Corporation.
- 12) Approval of a new organizational structure and new Management Board membership of Sistema JSFC.
- 13) Improving the performance of the Sistema Board of Directors and its Committees.
- 14) Implementation of the Corporation's strategy in HR, approval of the long-term incentive program and improvement of the existing incentive systems for the personnel of Sistema JSFC and the Sistema Group of companies.
- 15) Report on risk management in the Corporation.
- 16) Program of preparations for compliance with the UK Bribery Act.
- 17) Functional strategy in internal control and audit.
- 18) Sistema's strategy in the sphere of GR and participation in the national projects and federal target programs of the government.
- 19) Sistema's strategy in the sphere of public relations and investor relations.
- 20) Corporate social responsibility.
- 21) Convening the Annual General Meeting of shareholders, reports from the Committees of the Board of Directors, report on the quality of corporate governance.
- 22) Approval of transactions.

### *Issues reviewed by the Board of Directors in 2011*



In addition to transactions approval, most of the items reviewed by the Board in 2011 are related to strategy, corporate governance, shareholdings in subsidiaries and review of functional strategies aimed at supporting and improving the efficiency of efforts taken by the business subdivisions of the Corporation.

The high proportion of the items related to corporate governance and functional strategies reviewed by the Board in 2011 shows that the Board members devote particular attention to the process of the company's transformation to the new 'investment company' governance model, which makes it necessary to change some elements of corporate governance and refocus some of the functional units.

The high proportion of the items related to equity holdings in subsidiaries reviewed by the Board shows that the Board members closely followed the investment activities of the Corporation, which represent one of the key characteristics of the new governance model.

### *Preparation for the meetings and quorum of the Board of Directors*

In 2011 the process of preparation for the Board meetings underwent significant transformation. As before, the materials on the agenda items are provided to the Board members 10 days before the meeting, allowing them to form their voting positions. However, from 2011 all the items of the main agenda are subject to mandatory review at the Board Committee meetings, while the Board of Directors determines in advance the Committees which should be responsible for considering certain items.

Members of the Board of Directors meet with the key speakers and the management at a business dinner the evening before the meeting, so that they can get explanations on the materials of the Board of Directors and clarify the voting positions of the parties in an informal environment.

The meetings of the Board of Directors usually have quite high attendance rates. No cases when a Board meeting had to be rescheduled due to the lack of quorum have been registered over the past few years.

### *Participation of the members of the Board of Directors in meetings of the Board of Directors and its committees in 2011*

Board of Directors		Strategy Committee	Audit and Finance Committee	Nomination, Remuneration and Corporate Governance Committee	Ethics and Internal Control Committee	Investor Relations and Dividend Policy Committee
Participation in meetings						
V. Evtushenkov	10/10	4/5				
A. Goncharuk	10/10	0/1		10/10		1/1
R. Sommer	10/10	2/5	2/3			3/4
D. Zubov	10/10		3/3	8/10		
V. Kopiev	9/10			2/2	7/7	1/1
R. Kocharyan	10/10			6/10	2/2	3/3
R. Munnings	10/10		10/10	4/4	7/7	1/1
L. Melamed	10/10	4/5		10/10	2/2	
E. Novitsky	9/10	1/1	7/10			
S. Tchuruk	4/4	0/1				1/1
M. Shamolin	4/4	1/1		3/4	0/2	
D. Iakobachvili	4/4		2/3			1/1
R. Mehrotra	6/6		6/7			
S. Cheremin	6/6	0/4		6/6		2/3

Note. The first number denotes the number of meetings attended by the Board member, the second number stands for the total number of meetings the member could participate in.

### *Committees of the Board of Directors<sup>17</sup>*

In 2011, after the new Board members were elected, the Board took the decision to renew the profiles of the Board Committees. The Corporation needs to complete its transition to the Investment Company model. For successful transition to this new model it was also necessary to increase the engagement of the Board of Directors in the important aspects of the Corporation's work according to the new model. To achieve this, the procedural powers of the Committees were specified and the remit of the existing Committees of the Board of Directors updated.

Sistema JSFC has five committees of the Board of Directors:

- Strategy Committee.
- Audit and Finance Committee.
- Nomination, Remuneration and Corporate Governance Committee.
- Ethics and Internal Control Committee
- Investor Relations and Dividend Policy Committee

<sup>17</sup> All the information provided regarding the work of the committees is as of 31.12.2011.



Starting from 2011, as a rule, only members of the Board of Directors are elected to Committees. The main role of the Committees is to provide assistance in preparation and adoption of concepts and solutions in the respective functional areas, as well as in ensuring detailed scrutiny of the issues submitted for consideration of the Board of Directors. The Board Committees have considerable procedural powers, have a right to bring in external experts and use other resources of the Corporation.

#### *Strategy Committee*

The Strategy Committee includes seven Board members: Chairman of the Committee: V. Evtushenkov, Committee members: A. Goncharuk, R. Sommer, E. Novitsky, L. Melamed, M. Shamolin, S. Tchuruk

The Committee conducts analysis of strategic management issues of Sistema and also monitors the strategic planning cycle, including:

- strategic planning methodology;
- preliminary approval of the strategy;
- preliminary approval of Sistema's strategic goals;
- reviewing M&A transactions and large investment projects of Sistema JSFC

The Committee also reviews important investment projects, conducts assessment of risks, sets priorities and takes decisions on project development. The Committee recommends projects to be submitted to the Board, performs assessment and makes adjustments in projects' implementation.

In 2011, five meetings of the Committee were held where eight items were considered including: five items related to the strategy of the Corporation, three– non-organic growth deals and projects.

#### *Audit and Finance Committee*

The Audit and Finance Committee includes five Board members: Chairman of the Committee: R. Munnings, Committee members: R. Sommer, D. Zubov, E. Novitsky and D. Iakobachvili

The Audit Committee supervises preparation of financial reports and the internal audit of Sistema JSFC and its subsidiaries. Moreover, the Committee oversees the work of external auditors, makes recommendations for their appointment and the amount of remuneration, and also performs appraisal for the risk management system and monitors its operation. The Committee monitors compliance with the legislation and regulations in the sphere of finance and reporting. The new function of the Committee is to assist in the budgeting process: preliminary review of the materials at the budget development stage, preliminary review of the financial model of Sistema and also approval of the valuation of related-party and large-scale transactions.

In 2011 the Audit and Finance Committee held nine meetings where 55 items were considered, including 16 items related to financial accounting and reporting, five items – to internal control and audit, 14 items– consideration of related-party and major transactions, five items dealt with financial planning and risk management, 15 items – with housekeeping matters.

#### *Nomination, Remuneration and Corporate Governance Committee*

The Nomination, Remuneration and Corporate Governance Committee includes six Board members: Committee Chairman – L. Melamed, Committee members – A. Goncharuk, D. Zubov, R. Kocharyan, R. Munnings, M. Shamolin

The Nomination, Remuneration and Corporate Governance Committee is in charge of preliminary consideration of the nominees to the top management positions in Sistema JSFC and the candidates to the boards of directors of the main subsidiaries, participation in development and preliminary consideration of draft policies in HR and incentive and remuneration programs for the company's personnel; it also provides the results of the appraisal of the top management's performance to the Board of Directors. The Committee also facilitates development of corporate governance practices in Sistema and its subsidiaries and affiliates.

In 2011 the Nomination, Remuneration and Corporate Governance Committee held ten meetings. The Committee considered 17 items, including seven items related to improving the incentive system, four – HR policy and approval of the key nominees to the top management positions in Sistema JSFC, two items touched upon changes in the organizational structure of Sistema JSFC, two items dealt with the key performance indicators (KPIs) and two items – with development of corporate governance.

#### *Ethics and Internal Control Committee*

The Ethics and Internal Control Committee includes five Board members: Chairman of the Committee: R. Kocharyan, Committee members: V. Kopiev, R. Munnings; L. Melamed, M. Shamolin

The Ethics and Internal Control Committee serves the purpose of forming an efficient system of economic security, internal control and prevention of fraud and other misconduct which involves violations of the current legislation. Moreover, the Committee monitors compliance with the requirements of the Code of Ethics of Sistema JSFC.

In 2011 the Ethics and Internal Control Committee held two meetings where seven items were considered, of which four items were related to functional strategies in internal control and security, two items – to compliance with the requirements of legislation and corporate governance and one item dealt with housekeeping matters.

#### *Investor Relations and Dividend Policy Committee*

The Investor Relations and Dividend Policy Committee includes six Board members: Chairman of the Committee: D. Iakobachvili; Committee members: A. Goncharuk, R. Sommer, V. Kopiev, R. Munnings, S. Tchuruk.

The main task of the Committee is to facilitate the formation of a system aimed at maintaining effective relations with the financial community, the public and government agencies, as well as increasing the appeal of Sistema's shares to investors. At the same time, the Committee provides assistance in forming and maintaining a transparent and stable dividend policy of Sistema JSFC. The activities of the Committee should contribute to the growth of the Company's capitalization and promotion of the shareholders' interests.

In 2011 the Committee held six meetings where 14 items were reviewed, including 11 items related to investor relations and dividend policy, one item related to public relations and two housekeeping matters.

### **6.3. President**

The President of Sistema JSFC is a permanent sole executive body with the core objective of managing the day-to-day activities aimed at ensuring profitability of the Corporation and securing the rights and legitimate interests of its shareholders. The President acts within his remit and reports to the Board of Directors and the General Meeting of the Company's shareholders.

The President of Sistema JSFC is Mikhail Shamolin appointed by the Board of Directors on 10 March 2011. As of the beginning of the year the post of the President of Sistema JSFC was held by Leonid Melamed\*.

<b>Mikhail Shamolin</b>	Mikhail Shamolin was born in 1970.
President of Sistema JSFC. Chairman of the Sistema JSFC Management Board.	In 1992 he graduated from the Moscow Automobile and Road Technical Institute.
	In 1993 Mikhail received his second diploma from the Russian Academy of Public Administration under the President of the Russian Federation.
	In 1996-97 he completed the finance and management course for top managers

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at the Wharton Business School.

In 1998-2004 he worked at the international consulting company McKinsey&Co.

In 2004-05 Mikhail held the position of the Managing Director for the Ferroalloys Division at Interpipe Corp (Ukraine).

From 2005 Mr. Shamolin was Vice President for Sales and Customer Service and Head of the MTS Russia business unit. From 2008 to March 2011 he worked as President of MTS.

On 10 March 2011 Mikhail Shamolin was appointed President of Sistema JSFC.

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#### **6.4. Management Board**

The Management Board of Sistema JSFC is responsible for the day-to-day management of Sistema JSFC. It determines the methods of implementing the development strategy of the Corporation, works out development plans, sets investment procedures and controls their observance, appraises the performance of the personnel, and pre-considers items submitted to the Board of Directors. Meetings of the Management Board are normally held once a week.

##### ***Members of the Management Board:***

1	M. Shamolin	<i>Chairman of the Management Board, President of Sistema JSFC</i>
2	A. Abugov	
3	A. Buyanov	
4	A. Goldin	
5	S. Drozdov	
6	F. Evtushenkov	
7	R. Nagapetyants	
8	A. Terebenin	

In 2011, the Management Board of the Company held 39 meetings and considered 124 agenda items dealing with all the areas of business activity of the Corporation. In 2011 the Management Board considered the agenda items in the following key areas:

- 6) preliminary consideration of items put forward to the Board of Directors; the strategies of the Corporate Center and the Business Units were reviewed in the first place.
- 7) financial activities, forecasts and performance on the quarterly, half-year and annual budgets of Sistema JSFC Group; risk management and a risk map; internal control; financial and economic model of the Corporation's development;
- 8) procedures for the investment projects management;
- 9) analysis of the organizational maturity of subsidiaries and affiliates;
- 10) HR and social policies; training and development of the employees of Sistema JSFC Group; charity work;
- 11) consideration and preliminary approval of transactions;
- 12) analytical reviews of the media's and investment community's perception of the performance results of the Corporation.

### *Changes in top management in 2010*

There were a number of changes in the top management of the Company in 2011:

*L. Melamed* was relieved of his duties as President of Sistema JSFC on March 9, 2011.

*M. Shamolin*, was appointed President of Sistema JSFC on March 10, 2011.

*S. Boyev*, on February 17, 2011, was relieved of his duties as Vice President, Head of the High Technology and Industry Business Unit and was appointed Vice President and Head of the High Technologies and Industry Business Unit on March 1, 2011.

*A. Korsik* was relieved of his duties as Vice President and Head of the Oil and Energy Business Unit on April 6, 2011 and was appointed President of Bashneft.

*F. Evtushenkov*, on April 21, 2011, was transferred from his position of Vice President, Head of the Consumer Assets Business Unit to the position of First Vice President, Head of the Core Assets Business Unit.

*R. Sommer* was relieved of his duties as First Vice President, Head of the Telecom Assets Business Unit on May 13, 2011.

*R. Almakayev* was relieved of his duties as Vice President, Head of Administrative Function on May 31, 2011.

*A. Krupkin* was appointed Executive Vice President, Head of Internal Control and Audit Function of Sistema JSFC on May 23, 2011.

*R. Nagapetyants* was appointed Senior Vice President, Head of the Developing Assets Business Unit on August 22, 2011.

### **6.5. The specifics of the risk management, internal control and audit system**

The risk management system of Sistema JSFC is based on the ERM (COSO) principles that include the following key functional elements:

- identification of risks at all levels of the management (from the top to the line management), which includes finding the risk owner and making a risk passport;
- assessment and analysis of the identified risks (based on VaR methodology), ranging the risks by management level;
- development of risk mitigation plans and further monitoring of their implementation;
- risk monitoring, quarterly reports on the risks of the company.

The risk management procedures of Sistema JSFC are carried out by a dedicated unit - the Risk Management Division of Sistema JSFC.

Regular monitoring of the Corporation's risks is performed at the level of the Management Board and the Risk Management Sub-Committee of Sistema JSFC by reviewing the effects of the mitigation and response measures taken and by reassessing the already identified and/or new risks.

The President of Sistema JSFC presents a regular report on risk management in the Corporation to the Audit Committee of the Board of Directors of Sistema JSFC. A similar report and a risk map are presented to the members of the Board of Directors.

In 2011 the Board of Directors took the decision to separate the functions of internal control and internal audit of the Corporation.

The Internal Control Service reports to the President and the Ethics and Internal Control Committee of the Sistema JSFC Board of Directors. The Internal Control Service is responsible for:

- Targeted actions for control of business processes and financial and administrative activities;
- Control of elimination of the systemic deficiencies of business processes;
- Control of compliance with internal procedures and legal requirements;
- Control of reports on the results of the operational activity and fulfillment of functional KPIs;
- Functioning of the Hot Line as a tool for timely detection and efficient prevention of different types of fraud.

The main tools of the Internal Control Service are checks and analysis of the data received as a result of such checks. The results obtained by the Internal Control Service are reported to the President of Sistema JSFC and the Ethics and Internal Control Committee to ensure that decisions are taken to eliminate the identified deficiencies.

*The Internal Audit Service reports to the Audit and Finance Committee of the Sistema JSFC Board of Directors.*

The Internal Audit Service is responsible for:

- assessing the efficiency of the risk management system and preparing recommendations on improving it;
- auditing the quality of the management business processes;
- assessing the efficiency of the internal control system.

The main tools of the Internal Audit Service include obtaining information on the above processes, analyzing the received information and preparing recommendations and assessments for the Sistema JSFC management. The results obtained by the Internal Audit Service are reported to the Audit and Finance Committee and the Board of Directors for taking decisions on building the internal control system and for increasing the quality of risk management and corporate governance.

The Internal Audit Service submits to the Audit and Finance Committee of the Sistema JSFC Board of Directors a quarterly report on the work carried out.

Pursuant to the decision of the Audit and Finance Committee the following procedures have been developed at Sistema JSFC for purchasing external audit services for the purposes of audit of the financial/ accounting reports of Sistema JSFC. The Audit and Finance Committee performs annual assessment of the quality of audit services. If the quality of services provided by the current auditor is recognized to be unsatisfactory, the Audit and Finance Committee arranges a tender for selection of a new auditor. If the quality of services of the current auditor is recognized as satisfactory, negotiations are conducted on the price of audit services for the next period. In the meantime, to ensure impartiality and objectivity of the auditor, the Audit Committee of Sistema JSFC took the decision that a tender for the audit of the RAS and US GAAP financial statements shall be conducted at least once every five years.

## **6.6. Specifics of corporate governance system development in 2011**

In 2011 the Corporation took a number of measures to further develop its corporate governance system.

After electing its new members the Board of Directors took the decision to update the profile of the Board of Directors' committees. The Corporation needs to complete its transition to the Investment Company model. For successful transition to this new model it was also necessary to increase the engagement of the Board of Directors in the important aspects of the Corporation's work according to the new model. To achieve this, the procedural powers of the Committees were specified and the remit of the existing Committees of the Board of Directors updated.

Starting from 2011, as a rule, only members of the Board of Directors are elected to Committees. The Committees of the Board of Directors have extended procedural powers, the right to use external expertise and other resources of the Corporation. Every Committee is responsible for a specific field of the Corporation's activity, which is constantly monitored by every member of a Committee. These developments have helped to increase involvement of the Board of Directors in the process of the strategic management of the Corporation.

In June 2011 a number of new individuals became members of the Board of Directors. Independent directors Serge Tchuruk and David Iakobachvili were for the first time elected to the Board. Mikhail Shamolin was also elected a member of the Board of Directors as the President of Sistema JSFC. With their vast practical experience in organizing and managing large companies the new members of the Board of Directors will significantly strengthen business competencies of the Sistema JSFC Board of Directors.

In 2011, in accordance with best practices in corporate governance, the Board of Directors made the decision to separate the internal control and internal audit services. The Internal Control Service retained the functions of carrying out regular audits of the business activity. The Internal Audit Service kept the functions of assessing the

efficiency of the risk management system, the quality of the management business processes and assessment of the efficiency of internal control.

A new dividend policy was adopted by the Board of Directors in September 2011. It sets out a new principle of calculating the recommended dividends on the shares of Sistema JSFC. The recommended amount of dividends shall be determined by the Board of Directors based on the annual financial results of the Corporation and shall amount to 10% of the Company's net income under US GAAP (net of the special dividends paid). Following the recommendations of the Board of Directors the Company may pay special dividends in the minimum amount of 10% of net income of the transactions with incoming cash flow such as sale of assets determined by the Board of Directors. Meanwhile, according to the Russian legislation the aggregate amount of the paid dividends is limited by the amount of the non-consolidated net income under the Russian accounting standards (RAS).<sup>18</sup>

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<sup>18</sup> According to the requirements of the Russian legislation the dividends are payable to the Company shareholders from the Company income after tax (net income) which is calculated on the basis of financial statements compiled in accordance with the Russian legislation. When recommending the amount of dividends to the shareholders' meeting the Company's Board of Directors is also guided by the net income indicators determined on the basis of the consolidated financial statements of Sistema JSFC and subsidiaries and compiled according to the US generally accepted accounting principles (GAAP) under the guidance of the requirements of the Russian law.

## 7. SOCIAL RESPONSIBILITY

The philosophy of corporate social responsibility (CSR) of Sistema JSFC is based on the aspiration to the long-term and sustainable development of the Corporation that would allow for a harmonious combination of successful business practices with basic human values and national development priorities.

Corporate social responsibility of Sistema JSFC is a comprehensive system that comprises all of its activities. While adhering to the fundamental documents and standards in CSR, like the GRI, the UN Global Compact and the Social Charter of the Russian Business, the Corporation also focuses on the following four key areas:

- 1) **Responsibility of a corporate citizen** as contribution to the development of society and the state in general.
- 2) **Responsibility of an employer** towards employees and their families, ensuring good working conditions necessary for building a high quality of life.
- 3) **Responsibility of a business partner** implying adherence to business ethics, application of best practices in corporate governance and information disclosure, which makes it possible to provide sufficient protection and respect for the rights of partners and shareholders, including minority shareholders.
- 4) **Responsibility of a party to social relations** which allocates funding for science and education, culture and sports, as well as for support of social initiatives and projects.

The corporate social responsibility matters are annually reviewed by the Board of Directors of the Corporation. Importantly, the core CSR principles approved at the Corporation's level are being implemented and applied at all of its subsidiaries and affiliates. The Corporation has designed a system for cascading the CSR functions that includes forming standards, building the management structure, training personnel, and controlling implementation via a system of indicators.

Below there is a brief description of the last year's CSR performance results and achievements of Sistema JSFC:

### *Responsibility of a corporate citizen*

Sistema JSFC is one of the largest national taxpayers, and its portfolio companies are often notable contributors to the budgets in the regions of their presence.

The companies of Sistema JSFC produce material influence on the development of the national intellectual potential and growth in areas related to innovations and state-of-the-art technologies. For instance, in 2011 SITRONICS alone invested ca \$55m in advanced research and development and almost \$69m more in the development of knowledge-intensive manufacturing facilities.

Being a participant to the GLONASS federal program, the E-Government and the Multi-Service Information Educational Environment projects and other large-scale federal programs, the Corporation plays a key role in developing the high-tech industry, as it creates high-quality jobs, develops the entrepreneurial environment, and participates in forming the national intellectual elite.

The Corporation rigorously abides by the ecology principles, and its participation in environmental programs is set out in the Ethics Code of Sistema JSFC. Being participants of the hydrocarbon market, the Corporation's companies invest substantial funds in environmental protection. For instance, in 2011 Bashneft alone spent RUR2.1bn on these purposes. In the reporting period the company adopted a strategy in the area of health, safety and environment (HSE). Besides other matters, it provides for the construction of a unit for oil sludge processing, upgrade of waste treatment facilities and other actions aimed at minimizing the man-made environmental impact.

### *Responsibility of an employer*

Sistema JSFC, together with its subsidiaries and affiliates, is also one of the largest employers in Russia. In 2011, the headcount of the subsidiaries and affiliates of the Corporation exceeded 143 thousand people. With the family members of the employees taken into account, the Corporation is responsible for the welfare of about half a million citizens of the Russian Federation. Provision of good working conditions necessary for building a high quality of life is an unquestionable priority and the cornerstone of the Company's CSR policy.

We believe that the quality of a workplace comprises a number of components, such as the compensation level, the motivation system, working conditions, social guarantees, professional development and growth opportunities.

For instance, employees' salaries are differentiated according to a grade system designed by **the** Hay Group, a leading international consultancy, on the basis of monitoring salaries across various reference groups in the labor market. Total annual compensation of the employees is aligned with the advanced motivation system adopted in the Corporation.

Besides the social guarantees stipulated in the Labor Code of the Russian Federation, each of the Corporation's companies offers additional guarantees and benefits to its employees in line with its Social Policy fixed in the bylaws. In particular, the employees of Sistema JSFC and its subsidiaries can use the services of one of the best private healthcare networks, Medsi, at a discount or free of charge.

The Corporation is the founder of the Sistema private pension fund that offers a range of pension programs to portfolio companies. Such programs make it possible for their participants to accumulate pensions on much better terms than those offered by the governmental pension system.

The Corporation pays special attention to the development of each employee's intellectual potential. The Group cooperates with major national higher educational establishments and finances its own Corporate University. About 90 thousand employees of Sistema JSFC companies are trained annually. The Corporation also creates all the necessary conditions for professional and career development. Managers of Sistema JSFC and its portfolio companies are regularly included in the Russia's Top-1000 Best Managers annual rating of the Association of Managers of Russia and the Kommersant newspaper.

### *Responsibility of a business partner*

In its Corporate Ethics Code the Corporation has set a number of principles that reflect responsibility in business relations, and follows them rigorously.

These principles include: sound business practice, adherence to professional, legal and ethical standards of doing business, adherence to corporate governance standards, and respect for the rights of minority shareholders, transparency and high quality of disclosure.

Sistema JSFC was one of the first companies in Russia to join the UN Global Compact, and it has recently confirmed its membership as it submitted a report that was approved by a special UN commission. Today Sistema JSFC is a member of the Steering Committee of the Global Compact Network Russia. The Corporation and its subsidiaries have adopted an Ethics Code and a Corporate Conduct Code.

Sistema JSFC plays an active role in fighting corruption, which is reflected in its procedures and bylaws. In 2011 the Board of Directors of Sistema JSFC adopted the Anti-corruption Policy which sets out rules and restrictions in the following areas: business gifts and entertainment expenses, participation in charitable and sponsorship activities, participation in political activities, interaction with civil servants.

Sistema JSFC and its subsidiaries use transparent mechanisms and procedures for purchasing and tenders. In 2011 the company designed and enacted the Tender Procedures and Purchasing Code in order to improve the efficiency of procurement procedures. Besides, in the reporting period Sistema JSFC aggressively increased the share of purchasing from electronic trading floors.



The business practices of Sistema JSFC are positively assessed by the market. In 2011 the Expert Rating Agency rated the corporate governance of Sistema JSFC as 7+ ("Developed corporate governance practice") on a national scale. Besides, the Corporation was the 2011 winner in the nomination "Best level of disclosure on the corporate governance practice (RID nomination)" among non-financial sector companies. In 2011 MTS was granted the GAMMA-7 rating in "Analysis and assessment of efficiency in corporate governance, accountability and management". This is the highest rating among the companies of Russia and the CIS.

#### *Responsibility of a party to social relations*

The Corporation is one of the major philanthropists and investors in the Russian social sphere. Such investments totaled RUR2,000m in 2011. Social investments were mostly made in the following areas:

- Science and education;
- Culture;
- Sport;
- Direct support to social initiatives and projects.

Sistema JSFC considers it important to render substantial and consistent support to talented, intellectually gifted and active young people. In 2011 the Corporation started the all-Russian program for forming and developing the national talent pool entitled "Lift to the Future". The project will be implemented as an organized Russian national social network for the young whose purpose is to search for, support and develop talented young people.

Being aware of the importance of supporting education and science, the Corporation is a patron of the Higher School of Management of the Saint-Petersburg State University, the European University, the Russian Geographical Society, and many other educational and scientific institutions and projects. The most gifted students of a number of technical higher educational establishments are covered by a scholarship program.

Sistema JSFC is a major sponsor of numerous Russian cultural events. Since 2003 the Corporation has been the main sponsor of the State Russian Museum, the sponsor of the Mariinsky Theatre festivals, the annual Musical Kremlin concerts, and the international ballet contest Benois de la Danse. Sistema JSFC also sponsors the Sovremennik Theater.

The Corporation traditionally provides support to Russian sports: the Russian Olympians Foundation, the Russian Rugby Union, the Federation of Cycling Sport of Russia, the Sports Federation of the Russian Ministry of the Interior, and a number of junior sport schools.

Projects in the social sphere are an important component of our charitable activities: Sistema JSFC finances a number of orphanages and shelters, and is in close cooperation with several charitable foundations that support the disabled and veterans.

Social projects are implemented via the Sistema Charitable Foundation that was established in 2003 to ensure effective management of the Corporation's and its subsidiaries' social investments.

In 2011 the Corporation became a laureate of the Corporate Social Responsibility Leaders contest run by PricewaterhouseCoopers and (the) Vedomosti.

## **8. CRITERIA FOR AND AMOUNTS OF REMUNERATION OF THE MEMBERS OF THE BOARD OF DIRECTORS AND TOP EXECUTIVES OF THE COMPANY**

The remuneration of the members of Sistema JSFC Board of Directors is calculated on the basis of the Policy on remuneration and compensations payable to the members of the Board of Directors of the Company, approved with a resolution of the General Meeting of shareholders of Sistema JSFC on 30 June 2006 (Minutes No1-06) as amended with the resolution of the General Meeting of the shareholders of Sistema JSFC on 16 February 2009 (Minutes No1-09). The Policy provides for the payment of the following to the Board of Directors members:

- fixed amounts for participation in the meetings of the Board of Directors and its committees;
- fixed amounts for acting in the capacity of Chairman or Deputy Chairman of the Board of Directors, and for chairmanship of the committees under the Board;
- based on the annual performance members of the Board of Directors get additional performance-related remuneration in the form of a fixed amount, half of which is payable in shares (US\$ 250,000 - 325,000);
- also, given the capitalization of the Corporation has grown over the year, members of the Board of Directors get additional remuneration amounting to 0.1% of the incremental capitalization.

The short-term (up to one year) incentive scheme for the top managers of Sistema JSFC in 2011 consisted of the following elements:

- monthly fixed salary determined in line with the internal system of job categories (grades);
- four quarterly bonuses payable for meeting functional key performance indicators set individually for each top executive of Sistema JSFC for the respective reporting period;
- an annual bonus paid for the achievement of investment key performance indicators set for the Corporation as a whole and its Business Units for a respective reporting period (Investment KPIs of Sistema JSFC in 2011 include: iTSR, TSR, Revenue of Sistema (dividends and funds from the sale of businesses), SG&A / NAV, Net Income of Sistema JSFC, Debt of Sistema JSFC).
- additional remuneration paid for generation of cash income of the Corporation based on annual performance results and paid only in the event that the key performance indicators for the year are met;
- additional bonus which may only be paid following a decision of the Board of Directors.

Following the three-year Long-term Incentive Program (2009-2011), about 1% of ordinary shares of Sistema JSFC were distributed to the top and middle managers of Sistema JSFC. The new holders of the shares may dispose of them at their own discretion in line with the regulatory restrictions, rules and requirements set out in the laws of Russia and the UK, and the policy of Sistema JSFC on insider information.

In 2011, the Board of Directors of Sistema JSFC approved two new long-term incentive programs for the management:

- a new three-year Long-term Incentive Program (2012-2014) aimed at building the shareholder value of Sistema JSFC and at creating preconditions for maintaining long-term employment and corporate relations between the Company and its management;
- an option program for initiating and developing M&A projects aimed at strengthening the interest of the management towards searching for, acquiring and developing new assets that increase the shareholder value and the market capitalization of Sistema JSFC.

No remuneration is paid for the executive work of the managers sitting on the Management Board of Sistema JSFC.

The top executives of the Corporation were paid the total of RUR 3,450,065,590 in remuneration for the calendar year 2011. The remuneration paid to the Board of Directors' members of Sistema JSFC in 2011 totaled RUR 118, 580, 297.

## 9. ANNEX

### 9.1. SUMMARY BIOGRAPHIES OF THE MEMBERS OF THE BOARD OF DIRECTORS AND THEIR SHAREHOLDINGS IN SISTEMA JSFC

<i>Full name, Title</i>	<i>Brief Professional Background</i>
<b>Vladimir Evtushenkov</b>  Chairman of the Board of Directors, non-executive director	<p>Vladimir Evtushenkov was born in 1948 in the Smolensk region.</p> <p>In 1973 he graduated from the Moscow Mendeleyev Chemical-Engineering Institute, in 1980 – Economic Faculty of the Moscow State University n.a. M. Lomonosov. Doctor of Science in Economics.</p> <p>In 1975-1982 Mr. Evtushenkov worked as a Machine Shop Manager, Deputy Director, Chief Engineer of the Karacharovo Factory of Plastics, from 1982 to 1987 – Chief Engineer, First Deputy Director General of Polymer Scientific and Production Association. In 1987 he was appointed Head of Technical Department, in 1988 – Head of the Chief Department of Science and Technology of the Moscow City Executive Committee, in 1990 – the Chairman of the Moscow Municipal Committee for Science and Technology.</p> <p>In 1993 together with a group of associates Mr. Evtushenkov formed the Sistema Joint-Stock Financial Corporation. At present he is the principal shareholder, the Chairman of the Sistema JSFC Board of Directors and the Chairman of the Strategy Committee of the Board of Directors.</p> <p>Mr. Evtushenkov is an active member of a number of government commissions for improvement of the competitiveness of the Russian industry, development of high technologies and innovations, science and culture; a member of the National Council for corporate governance, member of the management boards of the main associations of entrepreneurs in Russia: the Russian Union of Industrialists and Entrepreneurs, the Russian Chamber of Industry and Commerce, Chairman of the Russian side of the Russian-Arab Business Council.</p> <p>In 2004 Mr. Evtushenkov was elected Chairman of the Council of Trustees of the Fund for Development of the State Russian Museum “Friends of the Russian Museum”. He also heads the Board of Trustees of the Sistema Charitable Foundation.</p> <p>Share in the authorized capital of Sistema JSFC – 64.1830%.</p>
<b>Alexander Goncharuk</b>  Non-executive Director	<p>Alexander Goncharuk was born in 1956 in Sevastopol.</p> <p>In 1978 he graduated from the Sevastopol Higher Navy and Engineering School, and in 1987 – the Grechko Navy Academy.</p> <p>From 1987 to 1991 Mr. Goncharuk served in the Navy Headquarters in the position of senior officer. Later he was the Head of Leader Joint-Stock Insurance Company.</p> <p>From 1995 to 1998 – Vice-President of Sistema JSFC, from March 2006 to May 2008 – President of Sistema JSFC. While working for the Corporation he was the Chairman of the Board of Directors of MTS (in 1998 and from 2002 to 2003), Sistema Telecom (1998 - 2003) and Sitronics (2003 - 2006).</p> <p>At present Mr. Goncharuk is a member of the Board of Directors of ANK BashNeft, Chairman of the Board of Directors of Polief, member of the Board of Trustees of the</p>

Sistema Charitable Foundation.

Mr. Goncharuk has been serving on the Board of Directors of Sistema JSFC since 1996. He is a member of the Strategy Committee, member of the Nomination, Remuneration and Corporate Governance Committee, member of the Investor Relations and Dividend Policy Committee of the Sistema Board of Directors.

Share in the authorized capital of Sistema JSFC - 1.0019%.

<b>Ron Sommer</b> <b>(Sommer)</b>	Ron Sommer was born in 1949.
Non-executive Director	<p>In 1971 he graduated from the Vienna University and received a Doctor's Degree in mathematics.</p> <p>In 1980 he was appointed Managing Director of the German branch of Sony Group (Sony Deutschland); in 1986 he became Chairman of the Management Board of Sony Deutschland, and in 1990 he was appointed President and Chief Operating Officer of Sony Corporation, USA. From 1993 to 1995 – Sony Europe, President and COO. From May 1995 to July 2002 – Deutsche Telekom AG, Chairman of the Management Board. In 2003 Mr. Sommer was elected Chairman of the International Advisory Board of Sistema JSFC.</p> <p>In 2005 Mr. Sommer became an independent director on the Board of Sistema JSFC where he also performed the duties of the Chairman of the IR Committee.</p> <p>From May 2009 to May 2011 – First Vice President of Sistema JSFC, Head of Telecom Assets Business Unit, Chairman of the Board of Directors of MTS, Chairman of the Board of Directors of SMM, Chairman of the Board of Directors of Sistema Shyam Teleservices Ltd. (SSTL), member of the Strategy Committee, member of the Investor Relations Committee of Sistema JSFC.</p> <p>From May 2011 – Chairman of the MTS Board of Directors, Chairman of the Board of Directors of Sistema Shyam Teleservices Ltd. (SSTL). Being a non-executive director of the Board of Sistema JSFC he is also a member of the Strategy Committee, Audit and Finance Committee, Investor relations and Dividend Policy Committee.</p> <p>Ron Sommer serves on the Boards of Directors of Tata Consultancy Services and Munich Reinsurance, and he is also a member of the International Advisory Board of Blackstone Group.</p> <p>Share in the authorized capital of Sistema JSFC – 0.0215%.</p>

<b>Dmitry Zubov</b>	Dmitry Zubov was born in 1954 in the Gorkiy region.
Deputy Chairman of the Board of Directors, Non-executive Director	<p>In 1977 he graduated from the Moscow Automobile and Road Technical Institute. Doctor of Science in Economics.</p> <p>In 1978-79 Mr. Zubov worked as a foreman at the Lukhovitsy Engineering Plant, in 1979-1983 – Secretary of the Young Communist League's Committee. From 1983 to 1988 he worked in the Department of Working Youth of the Central Committee of the Young Communist League, in 1988-1989 he was the Head of the All-Union Centre of Housing Cooperatives for Youth. In 1989-1991 he worked in the capacity of Deputy Director General of the All-Union Centre of Cinema and Television for Children and Youth. In 1992-1999 Mr. Zubov was the Director General of Alon Close-Type Joint-Stock Company, later he held senior positions in MosEximBank, IBN Sistema and PromChemVest.</p>

In 1999 Mr. Zubov was elected member of the Board of Directors of Sistema JSFC, from 2000 – Deputy Chairman of the Board of Directors; member of the Nomination, Remuneration and Corporate Governance Committee, member of the Audit and Finance Committee. Member of the Board of Trustees of the Sistema Charitable Foundation.  
Share in the authorized capital of Sistema JSFC - 0.9751%.

<b>Vyacheslav Kopiev</b>	Vyacheslav Kopiev was born in 1954 in Moscow.
Non-executive Director	<p>He graduated from the Cybernetics Department of the Moscow Institute of Engineering and Physics in 1977 and from the Law Department of the Russian Academy of Management in 1993. Mr. Kopiev also graduated with honors from the Economics Department of the International Marketing and Management Academy. Mr. Kopiev holds PhD in Technical Sciences, PhD in Legal Sciences. Author of more than 70 scientific works.</p> <p>From 1977 to 1990 Mr. Kopiev occupied various positions in the Komsomol organization of the USSR: Secretary of the Krasnogvardeiskiy District Committee of the Young Communist League, First Secretary of the Moscow City Committee of the Young Communist League, Second Secretary of the Central Committee of the Young Communist League.</p> <p>In 1989-97 Mr. Kopiev occupied leading positions at the Administrative Board of the Union of Engineering Societies, including Director for International Relations and Innovation from 1992 to 1997. He also served as Chairman of the Board of Directors of JSC Sputnik from 1990 to 1997. From 1995 – Deputy Chairman of the Executive Committee of the Russian-British Chamber of Commerce and Industry.</p> <p>In 1997 Mr. Kopiev was appointed Vice-President of Sistema JSFC, from 2000 to 2003 – Senior Vice-President, Head of the External Business Environment Complex. From 2003 to 2010 – Deputy Chairman of the Sistema JSFC Board of Directors. President of the Sistema Charitable Foundation.</p> <p>Mr. Kopiev is member of the Presidential Council of the Russian Federation for development of physical education and sports, professional sports, preparations for the XXII Olympic Games and XI Paralympic Games in 2014 in Sochi, President of the Russian Rugby Union.</p> <p>Member of the Sistema JSFC Board of Directors since 1997. Member of the Ethics and Internal Control Committee, member of the Investor Relations and Dividend Policy Committee.</p> <p>Share in the authorized capital of Sistema JSFC – 0.0556%.</p>
<b>Robert Kocharyan</b>	Robert Kocharyan was born in 1954 in Stepanakert, the Nagorno-Karabakh autonomous district.
Independent Director	<p>In 1982 he graduated from the Yerevan Polytechnic Institute.</p> <p>From 1971 to 1980 he served in the Soviet Army, worked at the Stepanakert Electrotechnical Plant as an assembly fitter, and later – a mechanical engineer. In 1981-1990 held various positions in the Komsomol and communist party bodies of Nagorny Karabakh.</p> <p>From February 1988 he was one of the leaders of the movement for separation of the Nagorny Karabakh autonomous district from the Soviet Republic of Azerbaijan and its further annexation to Armenia. In 1989 and 1990 Mr. Kocharyan was elected deputy of Armenia's Supreme Council and member of the Presidium of the Supreme Council of the Armenian SSR.</p>

In 1991- 1994 – deputy of the first Supreme Council of the Nagorny-Karabakh Republic (NKR), Chairman of the State Defense Committee of NKR and Prime Minister of NKR. From 1994 to 1997 – President of NKR.

In 1997-1998 Mr. Kocharyan was the Prime Minister of the Republic of Armenia, in 1998–2008 – the President of the Republic of Armenia.

Mr. Kocharyan is a member of the Sistema JSFC Board of Directors since 2009. He is also Chairman of the Ethics and Internal Control Committee, Chairman of the Nomination, Remuneration and Corporate Governance Committee of the Sistema Board of Directors.

Share in the authorized capital of Sistema JSFC – 0.0019%.

<b>Roger Munnings</b>  Independent Director	<p>Roger Munnings was born in 1950 in the United Kingdom. He graduated from the Oxford University with a degree of Master of Arts in politics, philosophy, and economics.</p> <p>At present Mr. Munnings is a member of the UK Government's working group on trade and investments between Great Britain and Russia, as well as Chairman of the Institute of Audit Committees in Russia.</p> <p>Roger Munnings has had a long and successful career (from 1974) with an international auditor KPMG, especially during his time in the office of the President and Managing Partner of KPMG in Russia and the CIS (1996-2008), as well as Chairman of the world energy and natural resources committee of KPMG (1993-2008). Mr. Munnings is Deputy Chairman of the management board of the Association of European Business (AEB) and member of the Institute of certified accountants of England and Wales.</p> <p>Roger Munnings is actively involved in the social activities in Russia being a member of the Russian National Council on Corporate Governance, the Russian Union of Industrials and Entrepreneurs, the Russian institute of directors, the management board of the American-Russian business council, the management board of the Russian-British chamber of commerce etc.</p> <p>Mr. Munnings is a member of the Board of Directors of Sistema JSFC from 2010. He is also Chairman of the Audit and Finance Committee, member of the Nomination, Remuneration and Corporate Governance Committee and the Ethics and Internal Control Committee of the Board of Directors.</p> <p>Share in the authorized capital of Sistema JSFC – 0.0009%.</p>
<b>Leonid Melamed</b>  Deputy Chairman of the Board of Directors, non-executive director.	<p>Leonid Melamed was born in 1967 in Moscow. In 1992 he graduated from the Moscow Medical Academy n.a. I. Sechenov. Doctor of Medicine.</p> <p>From 1992 to 1997 Mr. Melamed worked at ROSNO and held the positions of CEO and Chairman of the Management Board.</p> <p>In 2004-2006 he headed the Expert Council on insurance legislation of the Duma Committee of the Federal Assembly of the Russian Federation on credit organizations and financial markets.</p> <p>In 2006-2008 – President, Chairman of the Management Board, member of the Board of Directors of MTS.</p> <p>From May 2008 to March 2011 – President, Chairman of the Management Board of Sistema JSFC. Member of the Board of Directors of Bashneft, Chairman of the Board of Directors of RussNeft.</p>



Executive Director

In 1992 he graduated from the Moscow Automobile and Road Technical Institute. In 1993 Mikhail received his second diploma from the Russian Academy of Public Administration under the President of the Russian Federation.

In 1996-97 he completed the finance and management course for top managers at the Wharton Business School.

In 1998-2004 he worked at the international consulting company McKinsey&Co.

In 2004-05 Mikhail held the position of the Managing Director for the Ferroalloys Division at Interpipe Corp (Ukraine).

In 2005 Mr. Shamolin was appointed Vice President for Sales and Customer Service and Head of the MTS Russia business unit. From 2008 to 2011 he was the President of MTS.

On 10 March 2011 Mikhail Shamolin was appointed President and Chairman of the Management Board of Sistema JSFC. He holds the positions of Executive Director, Deputy Chairman of the Strategy Committee, member of the Ethics and Internal Control Committee, Nomination, Remuneration and Corporate Governance Committee of the Sistema Board of Directors, member of the Board of Trustees of the Sistema Charitable Foundation.

Share in the authorized capital of Sistema JSFC – 0.0326%.

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**David Iakobachvili**  
Independent Director

David Iakobachvili was born in 1957 in Georgia.

He graduated from the Civil and Industrial Engineering Department of the Georgian Technical University in Tbilisi.

From 1986 to 2000 – private entrepreneur involved in various projects: official dealership of General Motors cars, tourism and hotel business, timber processing, management of furniture supplies, retail management, communications and banking.

In 1992 David Iakobachvili became one of the founders of a famous dairy company, Wimm-Bill-Dann.

Mr. Iakobachvili serves on the Boards of Directors of a number of companies: CJSC Gorki-2 Agro-Complex, Airport Financial Services Limited, OJSC Melnichniy kombinat No4 (grain mill), LLC Kolmogorovskaya-2 mine, LLC Promuglesbyt Managing Company, OJSC Bashneft.

From 2000 – member of the Management Board of the Russian Union of Industrialists and Entrepreneurs (employers), from June 2004 – member of the Management Board's Bureau of the Union.

Mr. Iakobachvili serves on the Board of Directors of Sistema JSFC from 2011. He is also a member of Investor Relations and Dividend Policy Committee, member of the Audit and Finance Committee of the Board of Directors of Sistema JSFC.

Share in the authorized capital of Sistema JSFC – 0.006 %.



**9.2. INFORMATION ON TRANSACTIONS PERFORMED BY MEMBERS OF THE BOARD OF DIRECTORS OF SISTEMA JSFC WITH THE SHARES THEY HOLD IN THE COMPANY OVER THE PERIOD 1 JANUARY - 31 DECEMBER 2011**

<i>Board member</i>	<i>Date of the transaction</i>	<i>Transaction</i>	<i>Subject of the transaction</i>
V. Evtushenkov	19.07.2011	Crediting securities to the holder's account	83,653 ordinary registered shares
D. Zubov	19.07.2011	crediting securities to the holder's account	83,653 ordinary registered shares
V. Kopiev	19.07.2011	crediting securities to the holder's account	83,653 ordinary registered shares
A. Goncharuk	08.02.2011	debiting securities from the holder's account	28,950,000 ordinary registered shares
	21.02.2011	debiting securities from the holder's account	19,300,000 ordinary registered shares
	19.07.2011	crediting securities to the holder's account	83,653 ordinary registered shares
E. Novitsky	19.07.2011	crediting securities to the holder's account	83,653 ordinary registered shares
	24.11.2011	debiting securities from the holder's account	337,565,000 ordinary registered shares
R. Sommer	19.07.2011	crediting securities to the holder's account	87,500 ordinary registered shares
R. Kocharyan	19.07.2011	crediting securities to the holder's account	87,500 ordinary registered shares
L. Melamed	19.07.2011	crediting securities to the holder's account	83,653 ordinary registered shares

### 9.3. SUMMARY BIOGRAPHIES OF THE PRESIDENT OF SISTEMA JSFC AND THE MEMBERS OF THE MANAGEMENT BOARD

<i>Full name, Title</i>	<i>Brief Professional Background</i>
<b>Mikhail Shamolin</b>  President of Sistema JSFC Chairman of the Sistema JSFC Management Board	<p>Was born in 1970.</p> <p>In 1992 he graduated from the Moscow Automobile and Road Technical Institute. In 1993 Mikhail received his second diploma from the Russian Academy of Public Administration under the President of the Russian Federation.</p> <p>In 1996-97 he completed the finance and management course for top managers at the Wharton Business School.</p> <p>In 1998-2004 he worked at the international consulting company McKinsey&amp;Co.</p> <p>In 2004-05 Mikhail held the position of the Managing Director for the Ferroalloys Division at Interpipe Corp (Ukraine).</p> <p>Since 2005 Mr. Shamolin was Vice President for Sales and Customer Service and Head of the MTS Russia business unit. Since 2008 to March 2011 he worked as President of MTS.</p> <p>On 10 March 2011 Mikhail Shamolin was appointed President and Chairman of the Management Board of Sistema JSFC. Holds positions of Executive Director, Deputy Chairman of the Strategy Committee, member of the Ethics and Internal Control Committee, Nomination, Remuneration and Corporate Governance Committee of the Sistema Board of Directors, member of the Board of Trustees of the Sistema Charitable Foundation.</p>

#### *Members of the Management Board:*

<i>Full name, Title</i>	<i>Brief Professional Background</i>
<b>Anton Abugov</b>  First Vice President, Head of the Sistema JSFC Strategy and Development Function  Member of the Sistema JSFC Management Board	<p>Was born in 1976 in Mytishchi, the Moscow Region.</p> <p>In 1998 he graduated from the Academy of the National Economy under the Government of the Russian Federation with a degree in management.</p> <p>1995-99 – Closed-Type Joint-Stock Company United Financial Group, Deputy Executive Officer of the Department of Transactions with Securities, Trader.</p> <p>1999-2002 – Closed Joint-Stock Company United Financial Group, Head of the Corporate Finance Department</p> <p>2003-06 – JSCB ROSBANK, Managing Director, Head of the Corporate Finance Division.</p> <p>Since August 2006 – Sistema JSFC, First Vice President, Head of the Strategy and Development Function.</p>
<b>Alexei Buyanov</b>  Senior Vice President, Head of the Finance and	<p>Was born in 1969 in Moscow.</p> <p>In 1992 he graduated from the Moscow Physics and Technology Institute with a degree in Applied Mathematics and Physics, Engineering Physicist.</p> <p>1992-1994 – Trainee Researcher at the Institute of Problems of Mechanics, the Russian Academy of Sciences.</p>

Investment Function of Sistema JSFC	1994-1995 – Sistema JSFC, Chief Specialist, Lead Specialist, Executive Director.
Member of the Sistema JSFC Management Board	1995-1998 – Sistema Invest, Head of Division, Vice President, First Vice President.
	1998-2002 – Mobile TeleSystems, Vice President for Investments and Securities.
	2002-2002 – Sistema JSFC, Vice President, Head of the Financial Restructuring Department.
	2002-2005 – Sistema JSFC, First Vice President.
	From April 2005 – Sistema JSFC, Senior Vice President, Head of Finance and Investment Function
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<b>Anna Goldin</b>	Was born in 1963 in Leningrad.
	Graduated from the University of California in Berkeley, Boalt Hall, Doctor of Law.
Vice President, Head of the Sistema JSFC Legal Group	1988 – Baker & McKenzie, Lawyer/Trainee.
	1989 – Gibson, Dunn & Crutcher, Lawyer/Trainee.
Member of the Sistema JSFC Management Board	1989 – Morrison & Foerster, Lawyer/Trainee.
	1990-1998 – Latham & Watkins, Lawyer.
	1999-2007 – Latham & Watkins, Partner, Managing Partner.
	Since June 2007 – Sistema JSFC, Vice President, Head of the Legal Group.
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<b>Sergey Drozdov</b>	Was born in 1970 in Arkhangelsk.
	In 1993 he graduated from the Ordzhonikidze State Academy of Management with a degree in Engineering and Economy. Candidate of Economic Sciences.
Senior Vice President, Head of the Corporate Governance Function of Sistema JSFC	1993- 1994 – Yugorskiy Joint-Stock Bank, Economist in the Division of Trust Operations and Funds, Deputy Head of the Division of Securities and Trust Operations, Head of the Securities Department.
Member of the Sistema JSFC Management Board	1994-1995 – Moscow Property Fund, Head of the Financial Innovations and Marketing Department.
	1995-1998 – Sistema JSFC, Executive Director, Deputy Head of the Department of Development and Investments.
	1998-2002 – Sistema Invest, Vice President, First Vice President.
	2002 – Sistema JSFC, Head of the Corporate Property Department, Acting First Vice President.
	2002-2005 – Sistema JSFC, First Vice President.
	2005 – Sistema JSFC, Senior Vice President, Head of the Property Function.
	Since April 2011 – Sistema JSFC, Senior Vice President, Head of the Corporate Governance Function.
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<b>Felix Evtushenkov</b>	Was born in 1978 in Moscow.
	In 2000 he graduated from the Griboyedov Institute of International Law and Economy with a degree in law.
First Vice President, Head of the Core Assets Business Unit	1999-2000 – Sistema Invest, Assistant to the President.
	2000 – Sistema JSFC, Executive Director of the Industry Department.
	2000-2006 – Sistema-Hals, Deputy Director General, Director General.
	2006-2008 – Sistema Hals, President.
Sistema JSFC,	Since July 2008 – Sistema JSFC, Vice President, Head of the Consumer Assets Business Unit.
Member of the Sistema JSFC Management Board	Since April 2011 – Sistema JSFC, First Vice President, Head of the Core Assets Business Unit.

<b>Rafael Nagapetyants</b>  Senior Vice President, Head of the Developing Assets Business Unit  Member of the Sistema JSFC Management Board	<p>Was born in 1962 in Moscow.</p> <p>Graduated from the Moscow Financial Institute - department of economic relations (1984), legal department of the Lomonosov Moscow State University (1995), Amsterdam Institute of Finance (1996). Doctor of Science in Economics.</p> <p>In 1984-90 he held various positions from expert to chief expert at Foreign Currency and Economy Directorate of the USSR Ministry of Finance.</p> <p>In 1991-93 was a Deputy Chairman of the Foreign Investment Committee (later - the Russian Agency of International Cooperation and Development).</p> <p>From 1994 to 2011 he worked at Inkombank as Vice President, head of the Investment and International Business Block.</p> <p>From 2001 to 2005 he was a director at SUN Capital Partners in Russia, a private equity fund.</p> <p>From 2005 to 2008 he was employed by Alfa Bank as Managing Director for Corporate Finance and during some period of time was chairing the Investment Committee. At the same time, in 2007-09 he was Chairman of the Supervisory Council of Amtel-Vredestein.</p> <p>Since 2009 to August 2011 he was Managing Director, head of the Investment Banking division of Societe Generale in Russia.</p> <p>Since August 2011 – Sistema JSFC, Senior Vice President, Head of Developing Assets Business Unit.</p>
<b>Andrei Terebenin</b>  Vice President, Head of the Corporate Communications Function of Sistema JSFC  Member of the Sistema JSFC Management Board.	<p>Born in 1962 in Moscow.</p> <p>In 1985 he graduated from the Moscow State Institute of International Relations with a degree in international relations and Arabic.</p> <p>Held a number of management positions at the Publishing House Ekonomicheskaya Gazeta, Dun&amp;Bradstreet CIS and AIG Russia. In 1999 became a partner at the Triangle Porter Novelli Communications Agency, since 2003 to January 2006 was Director General and Partner at the R.I.M. Porter Novelli Communications Holding.</p> <p>January 2006 - May 2011 – Vice President for Corporate Communications of MTS.</p> <p>Since May 2011 - Vice President, Head of the Sistema JSFC Corporate Communications Function.</p>

#### **9.4. INFORMATION ON THE NUMBER OF SHARES OF SISTEMA JSFC HELD BY THE PRESIDENT AND THE MANAGEMENT BOARD MEMBERS**

<i>Management Board member</i>	<i>Number of owned shares</i>
Mikhail Shamolin	3,147,750 shares of Sistema JSFC
Anton Abugov	5,029,243 shares of Sistema JSFC
Alexei Buyanov	6,526,627 shares of Sistema JSFC
Anna Goldin	11,027,030 shares of Sistema JSFC
Sergey Drozdov	23,545,381 shares of Sistema JSFC
Felix Evtushenkov	5,739,688 shares of Sistema JSFC
Rafael Nagapetyants	1,143,315 shares of Sistema JSFC
Andrei Terebenin	400,160 shares of Sistema JSFC

**9.5. LIST OF TRANSACTIONS PERFORMED BY THE COMPANY IN THE REPORTING YEAR THAT ARE RECOGNIZED AS MAJOR TRANSACTIONS UNDER THE FEDERAL LAW "ON JOINT-STOCK COMPANIES", AND OTHER TRANSACTIONS COVERED BY THE MAJOR TRANSACTIONS APPROVAL PROCEDURE PURSUANT TO THE COMPANY'S CHARTER**

During 2011 Sistema JSFC has not performed any transactions which, in accordance with the Federal Law "On Joint-Stock Companies", are recognized as major transactions, and other transactions which, in accordance with the Company's Charter, are covered by the procedure for approval of major transactions.

**9.6. LIST OF TRANSACTIONS PERFORMED BY THE COMPANY IN THE REPORTING YEAR THAT ARE RECOGNIZED AS RELATED PARTY TRANSACTIONS UNDER THE FEDERAL LAW "ON JOINT-STOCK COMPANIES"**

<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 01-11 31.01.2011 Item 1.3.	Making contribution to the charter capital of the newly established OJSC RTI	Sistema JSFC, OJSC RTI	RUR 16,480,000,000.00	OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 01-11 31.01.2011 Item 2.4.	Acquiring regular registered shares of OJSC RTI-Systems Concern	Sistema JSFC, CJSC Sistema-Inventure	RUR 52,000.00	OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 02-11 05.02.2011 Item 5.3.2	Making an additional agreement No.2 to the Agreement on rendering paid information and consultation services between Sistema JSFC and OJSC Region.	Sistema JSFC, OJSC Region	RUR 106,531,866.24 annually	R. Almakayev S. Drozdov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 02-11 05.02.2011 Item 5.3.4	Making an additional agreement No.4 to the Agreement on paid provision of personnel between Sistema JSFC and OJSC Region.	Sistema JSFC, OJSC Region	RUR 45,952,992.00 annually	R. Almakayev S. Drozdov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 02-11 05.02.2011 Item 5.4.2	Granting a loan to CJSC Sistema-Inventure	Sistema JSFC, CJSC Sistema-Inventure	Up to \RUR 710,000,000.00	OJSC Sistema Finance Investments

<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 03-11 05.03.2011 Item 6.4.3	Execution of Additional Agreement #10 to the Securities (Shares) Pledge Agreement #3559/1 dtd 15.12.2005 between OJSC Sberbank of Russia and Sistema JSFC.	Sistema JSFC, OJSC Sberbank of Russia	-	S. Drozdov A. Abugov
Minutes of the Board of Directors No. 03-11 05.03.2011 Item 6.5.1.2.5	Termination of the shareholding of Sistema JSFC in the authorized capital of OJSC Sitronics.	Sistema JSFC, OJSC RTI	Equivalent of USD 111,135,451.00	S. Boyev OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 03-11 05.03.2011 Item 6.5.6.5.	Granting a loan to OJSC RTI	Sistema JSFC, OJSC RTI	Equivalent of USD 111,135,451.00	S. Boyev OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 04-11 16.04.2011 Item 8.2.2.	Approval of a transaction to indemnify the President, the Chairman of the Management Board of Sistema JSFC for possible legal and other expenses or losses associated with potential actions or claims brought against him for acts committed in his official capacity.	Sistema JSFC, Ecu Gest, M. Shamolin	Equivalent of up to USD 20,000,000.00	M. Shamolin
Minutes of the Board of Directors No. 04-11 16.04.2011 Item 8.3.4.	Entering into an agreement for transferring real estate property of Sistema JSFC under the management of CJSC Leader-Invest.	Sistema JSFC, CJSC Leader-Invest	1.5 % per annum of the market value of the transferred real estate property.	V. Evtushenkov F. Evtushenkov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 04-11 16.04.2011 Item 8.5.3.	The company's stake in the authorized capital of OJSC Dalcombank	Sistema JSFC, OJSC Dalcombank	RUR 999,290,000.00	V. Evtushenkov F. Evtushenkov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 04-11 16.04.2011 Item 8.2.6.	Entering into an agreement with OJSC Region regarding provision of skilled employees to Sistema JSFC to support the work of the Administration Department.	Sistema JSFC OJSC Region	RUR 17,816,102.06	R. Almakayev S. Drozdov OJSC Sistema Finance Investments

<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 06-11 21.05.2011 Item 6.2.2.	Entering by Sistema JSFC and OJSC Sberbank of Russia into supplementary agreement No.11 to the earlier signed Securities Pledge Agreement (the shares of OJSC RussNeft) No3559/1 as of 15.12.2005.	Sistema JSFC, CJSC Milanfo CJSC Mlada OJSC IK Nadezhnost SHADDOCK TRADING LIMITED OJSC Sberbank of Russia RussNeft	-	L. Melamed S. Drozdov A. Abugov
Minutes of the Board of Directors No. 06-11 21.05.2011 Item 6.3.3.	Agreement with OJSC REYESTR on keeping the register of owners of registered shares.	Sistema JSFC, OJSC Reyestr	RUR 250,000.00 per month plus expenses for every Annual General Meeting of shareholders	S. Drozdov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 06-11 21.05.2011 Item 6.2.4.	Bank Deposit Agreement with OJSC MBRD.	Sistema JSFC, MBRD	RUR 938,595,000.00	V. Evtushenkov S. Cheremin A. Buyanov F. Evtushenkov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 06-11 21.05.2011 Item 6.5.2.	Issuance of a guarantee by Sistema JSFC for Goldman Sachs International	Sistema JSFC, Goldman Sachs International	USD 70,000,000.00	V. Evtushenkov F. Evtushenkov A. Buyanov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 07-11 25.06.2011 Item 6.3.3.	Entering into a guarantee agreement between Sistema JSFC and Gazprombank (Open Joint-Stock Company) to secure the obligations of Sistema Shyam TeleServices Limited.	Sistema JSFC, OJSC Gazprombank	up to USD 230,000,000.00	R. Sommer M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 07-11 25.06.2011 Item 6.4.2	Granting an interest-bearing loan to CJSC Binnopharm.	Sistema JSFC, Binnopharm	up to RUR 110,000,000.00	D. Zubov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.4.4.	Termination of the shareholding in CJSC Sistema-Inventure.	Sistema JSFC, LLC Telecom Projects, Mobile TeleSystems B.V.	RUR 10,560,000,000.00	R. Sommer M. Shamolin L. Melamed OJSC Sistema Finance Investments



<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.5.2.	Granting a loan to LLC Management Company Sistema-Venture Capital	Sistema JSFC, LLC MC Sistema-Venture Capital	up to RUR 985,000,000.00	OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.6.2.	Extension of the agreement on the letter of credit guaranteed by Sistema JSFC for the purposes of securing the credit liabilities of Sistema Shyam TeleServices Limited under the credit facility from ING Vysya Bank Limited.	Sistema JSFC, ING Vysya Bank Limited	INR 7,000,000,000.00	V. Evtushenkov R. Sommer M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.7.2.	Surety agreement on liabilities of Sistema Shyam TeleServices Limited	Sistema JSFC, Bank of China Limited	USD 50,000,000.00	V. Evtushenkov R. Sommer M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.7.5.	Surety agreement between Sistema JSFC and Sistema Shyam TeleServices Limited	Sistema JSFC Sistema Shyam TeleServices Ltd.	The Guarantor's fee is 3(three) % per annum accrued to the day-to-day balances of the principal debt amount	V. Evtushenkov R. Sommer M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.8.2.	Entering into a direct guarantee agreement with Deutsche Bank AG Singapore, and a guarantee for the counter-guarantee of Sberbank of Russia issued as a security for credit agreements or borrowings in other formats, on the basis of which Deutsche Bank AG Mumbai or another entity of the Deutsche Bank Group shall issue loans to Sistema Shyam TeleServices Limited.	Sistema JSFC, Deutsche Bank AG Singapore, Sberbank of Russia	Equivalent of USD 329,000,000.00	V. Evtushenkov R. Sommer M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 08-11 24.09.2011 Item 9.8.2.	Agreement on the transfer of debt between Sistema JSFC and OJSC Sistema Finance Investments.	Sistema JSFC, OJSC Sistema Finance Investments S. Cheremin	RUR 455,000,000.00	OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 09-11 29.10.2011 Item 4.7	Sistema acquires ordinary registered uncertified shares of CJSC Binnopharm by conducting an additional share issue.	Sistema JSFC, Binnopharm	RUR 1,300,000,000.00	D. Zubov R. Nagapetyants OJSC Sistema Finance Investments

<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 09-11 29.10.2011 Item 4.10	Providing free-of-charge financial aid to CJSC Binnopharm.	Sistema JSFC, Binnopharm	RUR 2,400,000,000.00	D. Zubov R. Nagapetyants OJSC Sistema Finance Investments
09-11 29.10.2011 Item 7.3.2.	Providing free-of-charge financial aid to CJSC Medsi Group	Sistema JSFC CJSC Medsi Group	RUR 450,000,000.00	M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 09-11 29.10.2011 Item 7.4.4.	Entering into a purchase and sales agreement between OJSC Sistema and OJSC NIS in the process of additional issue of ordinary registered shares of CJSC NIS.	Sistema JSFC, NIS	RUR 899,963,000.00	A. Abugov OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 09-11 29.10.2011 Item 7.5.5.	Acquiring stakes in the Rent Real Estate Close-End Investment Fund in the course of their initial placement.	Sistema JSFC, LLC MC Trust-Finance	RUR 2,890,000,000.00	OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 8.6	Granting a loan to OJSC Donskoye	Sistema JSFC OJSC Donskoye	RUR 450,000,000.00	OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.3.2.	Entering into an indemnification agreement regarding the legal and other expenses or losses of the members of the Board of Directors of Sistema JSFC between Sistema JSFC, Ecu Gest and each of the Sistema Board members mentioned above	Sistema JSFC, Ecu Gest Holding S.A.	Not more than USD 26,000,000.00 for every Agreement	M. Shamolin S. Tchuruk D. Iakobachvili
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.3.7.	Entering into an indemnification agreement regarding the legal and other expenses or losses of the members of the Management Board of Sistema JSFC between Sistema JSFC, Ecu Gest and each of the Sistema Board members mentioned above	Sistema JSFC, Ecu Gest Holding S.A.	Not more than USD 20,000,000.00 for every Agreement	A. Terebenin R. Nagapetyants

<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.4.2	Granting an interest-bearing loan to CJSC Binnopharm.	Sistema JSFC, Binnopharm	RUR 200,000,000.00	D. Zubov R. Nagapetyants OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.1.2.	Provision of the Corporate Guarantee under which the Guarantor shall be liable to the Bank for the fulfillment by the Borrower of its obligations under the Guarantee Facility Agreement on the basis of which the Bank will provide/prolong, inter alia, the FBGs in favor of the Department of Telecommunications (DoT) of the Indian Ministry of Communications to guarantee the fulfillment by the Borrower of its obligation under the license agreements	Sistema JSFC, ICICI Bank Limited, Sistema Shyam TeleServices Ltd.	Up to INR 2,464,200,000.00	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.1.4.	Corporate Guarantee Agreement under which the Guarantor undertakes to issue the Corporate Guarantee to the Bank	Sistema JSFC, Sistema Shyam TeleServices Ltd.	Fee payable to the Guarantor equals 3 (three) % per annum	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.2.2.	Agreement on the letter of credit guaranteed by Sistema JSFC signed for securing the credit liabilities of Sistema Shyam TeleServices Limited	Sistema JSFC, Raiffeisen Bank International, CJSC Raiffeisenbank	Up to INR 10,300,000,000.00	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.3.3.	Issue of a guarantee by Sistema JSFC in favor of GasEnergo Capital Limited (project company of Gazprombank (OJSC), Gazprombank (OJSC), Gazprombank (Switzerland) Ltd. or another company affiliated with Gazprombank (OJSC) or GasEnergo Capital Limited.	Sistema JSFC, Gazprombank (Switzerland) Ltd., Sistema Shyam TeleServices Ltd.	USD 230,000,000.00	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments

<i>No. of the Minutes of the body that approved the transaction and date of taking the decision</i>	<i>Subject of the transaction</i>	<i>Transaction counterparties</i>	<i>Amount of the transaction</i>	<i>Persons that are considered as related parties to the transaction</i>
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.4.2.	Extension of the agreement on the letter of credit guaranteed by Sistema JSFC for the purposes of securing the credit liabilities of Sistema Shyam TeleServices Limited	Sistema JSFC ING BANK N.V. Sistema Shyam TeleServices Ltd.	Under the Letter of Credit Prolongation Agreement between Sistema JSFC and ING Bank N.V.	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.5.2.	Entering into interrelated agreements: agreements for guaranteed credit facility to be granted by Deutsche Bank AG Singapore Branch or any other entity of the Deutsche Bank Group, agreement on the parent company liabilities related to the borrowings of Sistema Shyam TeleServices Limited, and agreement for provision of a guarantee by OJSC Sberbank of Russia.	Sistema JSFC, Deutsche Bank AG Singapore Branch IDBI Trusteeship Services Limited, OJSC Sberbank of Russia Sistema Shyam TeleServices Ltd.	Equivalent of USD 292,000,000.00	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments
Minutes of the Board of Directors No. 10-11 17.12.2011 Item 10.6.6.2.	Entering into an agreement on opening a letter of credit and securing the letter of credit for guaranteeing the loan liabilities of Sistema Shyam TeleServices Limited	Sistema JSFC The Royal Bank of Scotland N.V. Sistema Shyam TeleServices Ltd.	up to RUR 10,000,000,000.00	R. Sommer V. Evtushenkov M. Shamolin OJSC Sistema Finance Investments
Extraordinary general meeting of shareholders Minutes No. 1-11 18.03.2011 Item 1	Making contribution to the charter capital of the newly established OJSC RTI from Sistema JSFC	Sistema JSFC OJSC RTI	RUR 16,480,000,000.00	OJSC Sistema Finance Investments

## 9.7. INFORMATION ABOUT THE COMPANY'S COMPLIANCE WITH REQUIREMENTS OF THE CODE OF CORPORATE CONDUCT OF THE FEDERAL SERVICE FOR FINANCIAL MARKETS

<i>Provisions of the Corporate Conduct Code</i>	<i>Observed / not observed</i>	<i>Comment</i>
<b>General Meeting of Shareholders</b>		
1 A notice of the forthcoming Annual General Meeting of shareholders shall be distributed not later than 30 days before the day of the Meeting unless a longer term is provided for by legislation.	Observed	This provision was added to the Charter of Sistema JSFC (hereinafter - the Company).
2 The procedure of announcement on holding the Annual General Meeting of shareholders shall allow shareholders to properly prepare for participation in the meeting.	Observed	Announcement about the meeting is sent to shareholders by mail and is published on the Company's website.
3 Shareholders may familiarize themselves with the list of persons who have the right to attend the Annual General Meeting of shareholders, starting from the date of announcement of holding the General Meeting of Shareholders and till the closure of the Annual General Meeting of shareholders, and in case of holding the meeting in the form of a letter ballot – till the deadline for acceptance of ballot papers.	Observed	Shareholders have the right to familiarize themselves with the list of persons who may attend the Annual General Meeting of shareholders by addressing the Company's Corporate Secretary. Such possibility is provided for by the Terms of Reference of the Annual General Meeting of shareholders.
4 Shareholders can familiarize themselves with the information (materials) which is subject to presentation during preparation for the Annual General Meeting of shareholders, through electronic means of communication	Observed	The Company publishes such information on the Company's website (in) on the Internet.
5 Shareholders may introduce an agenda item for the Annual General Meeting of shareholders or demand convocation of the Annual General Meeting of shareholders without presenting an extract from the register of shareholders if his/her rights for shares are accounted for in the system of keeping the register of shareholders, and in the event when his/her rights for shares are registered in the depo account - an extract from the depo account shall be sufficient for exercising the above-said rights.	Observed	There is no requirement that shareholders should prove their right with specific documents, with the exception of the extract from the depo account. Provided for by the Terms of Reference of the Annual General Meeting of Sistema JSFC shareholders (approved by the Annual General Meeting of Sistema JSFC shareholders, Minutes No. 2-10 dtd 30.06.2010).
6 Joint-Stock Company's internal documents should set out procedures for registering participants of the Annual General Meeting of shareholders.	Observed	Regulated by the Terms of Reference of the Annual General Meeting of shareholders.
<b>Work of the Board of Directors</b>		
1 The Joint-Stock Company's Charter should define the authority of the Board of Directors regarding annual approval of the Joint-Stock Company's financial and business plan.	Observed	In accordance with the Company's Charter, the competence of the Board of Directors includes: "determining the priority areas of the Company's activity, determining the strategy of the Company's development, approving the Company's annual budgets (financial plans), considering the main areas of activities and development strategy of subsidiaries."

2	The risk management procedure should be approved by the Board of Directors of the Joint-Stock Company.	Observed	Appendix 3 to the Minutes of the Board of Directors No. 03-09 of 22.04.2009. Resolution of the Board of Directors dtd 5 March 2011, Minutes No.03-11.
3	The Board of Directors shall have the right to determine requirements to qualification and remuneration of the General Director and heads of the Joint-Stock Company's main structural divisions.	Observed	The competence of the Board of Directors includes: appointment of the President of the Company; determining the number of members of the Management Board, election of its members; approving the terms of the agreement with the President and with members of the Company's Management Board; early termination of authority of the President of the Company and members of the Company's Management Board, approving the principles of performance assessment and the remuneration system, as well as controlling activity of the Company's top officials who are directly reporting to the Company's President.
4	The Joint-Stock Company's Charter of the Board of Directors shall provide for the right of the Board to approve terms of agreements with the General Director and members of the Management Board.	Observed	In accordance with the Company's Charter, terms of agreements with the President and members of the Company's Management Board shall be approved by the Board of Directors.
5	The Joint-Stock Company's Board of Directors shall consist of not less than three independent directors who meet requirements of the Code of Corporate Conduct.	Observed	As of the end of 2011, the Board of Directors includes five members of the Board of Directors who meet criteria of the Code of Corporate Conduct for independent directors.
6	No members of the Joint-Stock Company's Board of Directors shall have criminal record for economic crimes or crimes against the state, interests of the state and local governments or on whom administrative penalties were imposed for offenses in the areas of entrepreneurial activity, finances, taxes and duties or equity markets.	Observed	The Company has reviewed this issue and does not have any information on such offenses committed by members of its Board of Directors.
7	In the Board of Directors there are no persons who are shareholders, general directors (managers), members of governing bodies or employees of legal entities which compete with the Company.	Observed	According the information available to Sistema JSFC, the Sistema Board of Directors does not include persons being shareholders, general directors (managers), members of a governing body or employees of a legal entity which competes with Sistema JSFC.
8	Joint-Stock Company's internal documents set out the requirement on holding the Board of Directors meetings at least once in six weeks.	Observed	According to the Company's Charter, meetings of the Board of Directors are held as necessary but at least two times per quarter. Ten meetings of the Board of Directors were held in 2011.
9	Meetings of the Joint-Stock Company's Board of Directors shall be held at least once in six weeks during the year for which the Joint-Stock Company's Annual Report is compiled.	Observed	In 2011 ten meetings of the Board of Directors were held.
10	Joint-Stock Company's internal documents set out the procedure for holding meetings of the Board of Directors.	Observed	The procedure to hold meetings of the Board of Directors is determined by the Terms of Reference and Working Procedures of the Sistema JSFC Board of

		Directors.
11 Joint-Stock Company's internal documents provide for the right of the Board members to get information necessary for performing their functions from executive bodies and heads of the Joint-Stock Company's main structural divisions.	Observed	The right of members of the Board of Directors to get any information on activity of Sistema JSFC is stipulated by the Terms of Reference of the Board of Directors.
12 The company shall establish a committee of the Board of Directors responsible for strategic planning.	Observed	The Company has established the Strategy Committee of the Board of Directors.
13 The company shall establish a committee of the Board of Directors which recommends the auditor to the Board of Directors and interacts with the latter, as well as with the Joint-Stock Company's Revision Commission.	Observed	The Company has established the Audit and Finance Committee of the Board of Directors.
14 The company shall establish a committee of the Board of Directors responsible for determining the criteria for selecting candidates to be appointed to the Board of Directors and for developing the Joint-Stock Company's remuneration policy.	Observed	The Company has established the Nomination, Remuneration and Corporate Governance Committee of the Board of Directors. The Committee's functions are determined in the Terms of Reference of the Committee.
15 The Nomination and Remuneration Committee shall be chaired by an independent director.	Not observed	The Committee is chaired by non-executive director L. Melamed.
16 The Joint-Stock Company shall have approved by the Board internal documents which set out a procedure for forming committees of the Board of Directors and their working procedures.	Observed	The Company has approved the Terms of Reference that set out the competence of the Board Committees, procedure of their establishment and their working procedures.
17 The Joint-Stock Company's Charter sets out a procedure to determine the quorum of the Board of Directors that ensures participation of independent directors in meetings of the Board of Directors.	Not observed	The quorum of the Board of Directors is determined according to the number of members of the Board of Directors attending the sitting regardless of their status of an independent, non-executive or executive director.
18 The issuer's internal documents shall provide for obligations of members of the Board of Directors, members of a collective executive governing body, person who carries out functions of the sole executive body, including the governing organization and its officials, to disclose information on the possession of the issuer's securities as well as sale and (or) purchase of the issuer's securities.	Observed	This requirement is included in the Corporate Conduct Code of Sistema JSFC, the Terms of Reference of the Board of Directors and the Management Board of Sistema JSFC, as well as internal documents that set out liabilities of the Company in implementing requirements of the legislation on preventing illegal use of insider information.

#### Executive bodies

1 The Joint-Stock Company shall have a collective executive body (Management Board).	Observed	The Company has formed a collective executive body – the Management Board (provided for by the Charter)
2 Joint-Stock Company's internal documents set out procedures for approval of transactions outside of the Joint-Stock Company's financial and business plan.	Observed	Procedures for approval of transactions outside of the budget are set out in the Corporation's budget policy, the Regulation on contracts approval and the Regulation on mergers and acquisitions. All such

		transactions are preliminary reviewed by the Finance and Investment Committee. When necessary, resolution of the Board of Directors introduces amendments to the budget.
3	Executive bodies shall not include persons who are shareholders, general directors (managers), members of a governing body or employees of a legal entity which competes with the Joint-Stock Company.	Observed According to available information, executive bodies of Sistema JSFC do not include persons being shareholders, directors general (manager), members of a governing body or employees of a legal entity which competes with the Company.
4	The Joint-Stock Company's executive bodies do not include persons with criminal record for economic crimes or crimes against the state, interests of the state and local governments or on whom administrative penalties were imposed for offenses in the area of entrepreneurial activity or finances, taxes and receipts or equity market.	Observed According to the information available to Sistema JSFC, executive bodies of Sistema JSFC do not include such persons.
5	The Joint-Stock Company's Charter or internal documents prohibit the management company (the manager) from performing similar functions in a competing company as well as from having any other property relations with the Joint-Stock Company apart from the provision of services to the management company (the manager).	Observed Provided for by the Company's Charter.
6	Joint-Stock Company's internal documents shall set out obligations of executive bodies to refrain from actions which lead or may lead to a conflict between their interests and interests of the Joint-Stock Company, and in case of such conflict of an obligation to inform the Board of Directors of that.	Observed Such requirements are contained in the Terms of Reference of the Board of Directors, Terms of Reference of the Management Board, Terms of Reference of the President and in the agreement with the President and members of the Company's Management Board.
7	The Joint-Stock Company's charter or internal documents shall set out criteria to select the management company (manager).	Not observed It is not necessary because there is no managing company and there are no plans to engage the same to perform functions of the Company's sole executive body.
8	Joint-Stock Company's executive bodies shall monthly present reports on their work to the Board of Directors.	Observed The Board of Directors quarterly reviews financial results of the Company's activity. The Company's management weekly compiles a report on the most important events and provides it to members of the Board of Directors.
9	Agreements concluded by the Joint-Stock Company with the General Director (management organization, manager) set out his/her liability for failure to comply with regulations on the use of confidential and insider information.	Observed There is a requirement regarding protection of confidential information in the Agreements with the President and members of the Company's Management Board.



<b>Corporate Secretary</b>		
1. The Joint-Stock Company shall have an official (company secretary) whose duty is to ensure compliance of the Joint-Stock Company's bodies and officials with procedural requirements which guarantee implementation of rights and legal interests of the Company's shareholders.	Observed	The Company has appointed the Corporate Secretary.
2. Joint-Stock Company's Charter or internal documents shall set out a procedure to appoint (elect) the secretary of the Company and his/her responsibilities.	Observed	The Board of Directors has approved the Terms of Reference of the Corporate Secretary which sets out responsibilities of the Corporate Secretary and procedure of his/her appointment.
3. The Joint-Stock Company's Charter shall set out the requirements for the candidate for the position of a Company's secretary.	Partially observed	These requirements are included in the Terms of Reference of the Corporate Secretary.
<b>Material corporate actions</b>		
1. The Joint-Stock Company's charter or internal documents shall include a requirement to approve large transactions prior to performing them.	Partially observed	Regardless of absence of this norm in the Charter, this requirement is always observed in practice.
2. Mandatory engagement of an independent appraiser for assessing the market value of the property which is a subject of a large transaction.	Observed	In the above cases the Sistema Board of Directors engages an independent appraiser.
3. The Joint-Stock Company's charter shall prohibit from undertaking any actions during acquisition of large stakes of the Joint-Stock Company's shares (takeover) which are directed at protection of rights of executive bodies (members of such bodies) and members of the Board of Directors of the Joint-Stock Company and actions which aggravate the shareholders' position (in particular, prohibiting the Board of Directors from adopting, before the end of the period allocated for shares acquisition, resolutions on issuing additional shares, securities convertible shares or securities granting the right to acquire the Company's shares, even if the right to adopt such resolutions is given to the Board of Directors by the Charter).	Not observed	Such actions are hardly probable because there is a controlling shareholder.
4. The Joint-Stock Company's charter or internal documents shall include a requirement regarding mandatory engagement of an independent appraiser to determine the ratio for converting shares during reorganization.	Not observed	There is no such provision in the Charter, but in case of reorganization, in accordance with the Terms of Reference of the Board of Directors, the Board of Sistema JSFC will be taking the decision on defining the ratio for converting shares only if there are substantial grounds for this, for example, the opinion of an independent appraiser.
<b>Disclosure of information</b>		
1. The Joint-Stock Company shall have an approved by the Board internal document which sets out its rules and approach to information disclosure (the Regulations on the Information Policy).	Observed	The Board of Directors has approved the Regulations on the Information Policy.
2. The Joint-Stock Company's internal documents shall contain a list of information, documents and materials which should be provided to shareholders for taking decisions on agenda items presented to the Annual General Meeting of shareholders.	Observed	The list of additionally provided information is contained in the Code of Corporate Conduct, the Regulations on the Information Policy and the Terms of Reference of the Annual General Meeting of shareholders of Sistema JSFC.

3	Disclosure of financial information on the Joint-Stock Company's activities.	Observed	RAS financial statements are disclosed annually. GAAP financial statements are disclosed quarterly.
4	The use of additional forms and methods of information disclosure.	Observed	The Company has established the IR Department. It regularly holds meetings with investors and organizes road shows. The Department maintains the corporate website in the Internet with extensive information about the Company's activities.
5	The issuer shall disclose information about the remuneration received by members of the Board of Directors, members of the collective executive body and by the person who performs functions of the sole executive body, including the management company and the manager.	Observed	The said information is disclosed in the issuer's annual report, quarterly reports and the prospectus. The Company has adopted and published the Policy on remuneration and compensations paid to members of the Company's Board of Directors.
6	The Joint-Stock Company shall have a website in the Internet and regularly disclose information on its activity.	Observed	The address of the Sistema JSFC website on the Internet: <a href="http://www.sistema.ru/">www.sistema.ru/</a> <a href="http://www.sistema.com">www.sistema.com</a> .
7	The Joint-Stock Company's internal documents shall contain a requirement for disclosure of information on the Company's transactions with persons who, in accordance with the Charter, are considered the Joint-Stock Company's top officials as well as on the Joint-Stock Company's transactions with companies where Joint-Stock Company's top officials directly or indirectly own 20 and more percent of the Joint-Stock Company's authorized capital or on which such persons may otherwise exert substantial influence.	Partially observed	Observed according to the legal requirement on related party transactions.
8	The Joint-Stock Company's internal documents shall include a requirement for disclosure of information on all transactions which may affect the market value of the Joint-Stock Company's shares.	Observed	Observed according to requirements of the Russian legislation on security markets and requirements of the UK security market regulator. Disclosure principles are set out in the Regulations on the Information Policy of Sistema JSFC.
9.	The company shall have an internal document approved by the Board of Directors for the use of material information on the Joint-Stock Company's activities, shares and other securities of the Company and transactions with them when such information is not commonly available and when its disclosure may exert substantial influence on the market value of the Joint-Stock Company's shares and other securities.	Observed	There is a corresponding section in the Regulations on the Information Policy of Sistema JSFC.
<b>Control of financial and business activities</b>			
1	The company shall have procedures approved by the board of directors for internal control over the Joint-Stock Company's financial and business activities.	Observed	The Company has approved the Functional Strategy in internal control.
2.	The Joint-Stock Company shall have a special division which ensures compliance with procedures of internal control (control and audit service).	Observed	The Company has established the Internal Control Function and the Internal Audit Service.
3	The Joint-Stock Company's internal documents shall contain a requirement for the Board of Directors to determine the structure and composition of the Joint-Stock Company's control and audit service.	Observed	In accordance with the Company's Charter, the Head of the Internal Control division and the Internal Audit division is to be approved by the Company's Board of Directors.

4	The Joint-Stock Company's control and revision services do not include persons with criminal record for economic crimes or crimes against the state, interests of the state and local governments or on whom administrative penalties were imposed for offenses in the area of entrepreneurial activity, finances, taxes and duties or equity market.	Observed	The Company reviewed this issue and does not dispose of information about such offenses committed by employees of its control and audit services.
5	Control and revision services do not include persons being shareholders, general directors (managers), members of a governing body or employees of a legal entity which competes with the Joint-Stock Company.	Observed	The above persons are not members of the Revision Commission of Sistema JSFC.
6	The Joint-Stock Company's internal documents shall set out a deadline for presentation to the control and audit service of documents and materials for assessing financial and business transactions, as well as a liability of the Joint-Stock Company's officials and employees for their failure to present the same by the deadline.	Observed	The Internal Control and Audit Function and the Internal Audit Service have constant access to the current information on the financial and business transactions and have the right to independently determine the deadline for presenting such information.
7	The Joint-Stock Company's internal documents shall set out an obligation of the control and audit service to inform the audit committee, and if the latter is not available – the Joint-Stock Company's board of directors, about identified irregularities.	Observed	In accordance with the Terms of Reference of the Audit and Finance Committee, the Internal Audit Department on a regular basis submits audit results to the Committee.
8	Internal documents shall contain a requirement for the control and audit service to perform preliminary assessment of the reasonability of operations which are not included in the Joint-Stock Company's financial and business plans.	Observed	The Internal Audit Service reviews all operations of the Company before they are performed.
9	The company shall have an internal document approved by the Board of Directors which determines the procedure for the revision commission to carry out audits of the Joint-Stock Company's financial and business activities	Observed	The Company has approved the Regulation on the Revision Commission of Sistema JSFC.
10	The Audit Committee shall assess the audit report prior to its presentation to shareholders at the Annual General Meeting of shareholders.	Observed	In accordance with the Terms of Reference of the Audit and Finance Committee, on 20 April 2012 the Committee assessed the audit opinion on results of 2011.

## Dividends

1	The company shall have an internal document approved by the board of directors which is used as a guideline by the board when making recommendations on the amount of dividends (The Regulations on the Dividend Policy).	Observed	The Company has approved the Regulations for the Dividend Policy.
2	Publishing the information on the Joint-Stock Company's dividend policy and amendments therein in a periodical provided for by the Joint-Stock Company's Charter for publishing notices of holding Annual General Meetings of shareholders, as well as placement of the said information on the Joint-Stock Company's website on the Internet.	Observed	The Regulations on the Dividend Policy is published on the Company's website in the Internet.

## 9.8. INFORMATION ON THE COMPANY'S COMPLIANCE WITH THE REQUIREMENTS OF THE UK COMBINED CORPORATE GOVERNANCE CODE

<i>Provisions of the Code</i>	<i>Observed / not observed</i>	<i>Comment</i>
<b>A. DIRECTORS</b>		
<b>A.1 Board of Directors</b>		
A.1.1. The work of the Board of Directors shall be organized efficiently. The board shall meet regularly enough to discharge its duties effectively.	Observed	The Board of Directors of Sistema JSFC (hereinafter - the "Company") meets at least eight times per year, and this allows reviewing and taking decisions on issues within the sphere of its competence.
There should be a formal schedule of matters specifically reserved for decisions of the Board of Directors.	Observed	The competence of the Board of Directors is set out in the Charter of Sistema JSFC (p.32 of the Charter).
The annual report should include a statement of how the board operates, including a statement of which types of decisions and on which issues were taken by the board of directors and the management board.	Observed	The Annual Report of the Company for 2011 includes statement on how the Board operates, including the report on key issues, issues on which decisions were taken by the Board of Directors and the Management Board (pp. 6.2, 6.4 of the Annual Report).
A.1.2 The annual report should identify the chairman, the deputy chairman, the chief executive, the senior independent director and the chairmen and members of the board committees.	Observed	The Annual Report of the Company for 2011 includes information on election of V. Evtushenkov Chairman of the Board of Directors of the Company and on election of Deputy Chairmen of the Board of Directors (p. 6.2 of the Annual Report). The 2011 Annual Report of the Company also includes information on the President of the Company, Chairmen and members of all Board Committees, including the Nomination, Remuneration and Corporate Governance Committee and the Audit and Finance Committee (p.6.2 of the Annual Report). Company's statutory documents does not provide for the position of a senior independent director.
The annual report should set out the number of meetings of the board and its committees and individual attendance by directors.	Observed	The Annual Report of the Company for 2011 includes information on the number of meetings of the Board of Directors and Board Committees, as well as their attendance by members. (p. 6.2.)
A.1.3. From time to time the chairman should hold meetings with the non-executive directors without the executives present.	Partially observed	Formal meetings of the Board of Directors without the executives present are not held, but there are regular informal meetings of the Chairman of the Company's Board of Directors with independent directors.
Led by the senior independent director, the non-executive directors should meet without the chairman present at least once a year to appraise the chairman's performance and on such other occasions as are deemed appropriate.	Partially observed	Company's statutory documents do not provide for the position of a senior independent director. Prior to every meeting of the Board of Directors, independent members of the Board hold an informal meeting in the form of a business dinner, which is also attended by the management of the Company, for discussing urgent matters of governing the Company and organizing the work of the Board of Directors.
A.1.4. Where directors have special opinions about decisions taken by the board; they should ensure that their opinions are recorded in the minutes of the meeting.	Observed	The whole course of the meeting of the Board of Directors is recorded in writing in the form of statements from participants and is subsequently analyzed to ensure that all elements of decisions that were made are reflected in the minutes. According to the Working Procedures of the Board of Directors of the Company (approved by

		the Board 27.10.2007), directors have an opportunity to express their special opinion within 24 hours after the meeting. All Board members are provided with a copy of minutes of every Board meeting.
If Board members have comments or specific proposals regarding efficiency of running the company, they should send a letter with such comments and proposals to the Chairman of the Board of Directors. Other Board members should have access to the information contained in such letter.	Observed	Members of the Company's Board of Directors regularly send to the Board Chairman letters with their comments and proposals on different aspects of running the Company and organization of the work of the Company's Board of Directors.
A.1.5 The Company shall ensure due indemnification coverage for members of the Board of Directors.	Observed	According to p. 2.4.5. of the Terms of Reference of the Board of Directors, the Company insures liability of the Board members from legal actions or claims in relation to business decisions or other actions taken in connection with the performance of his/her functions as a member of the Board of Director of the Company or its affiliates (D&O Policy). Additionally members of the Board of Directors signed Indemnification Agreements.
<b>A.2. Chairman of the Board of Directors and President</b>		
A.2.1 The same person cannot at the same time hold the position of the Chairman of the Board of Directors and the President. The division of responsibilities between the board chairman and the president should be clearly established and set out in internal documents of the Company.	Observed	According to the Russian legislation and the Company's Charter, the person carrying out functions of the Company's sole executive body cannot at the same time serve as the Chairman of the Board of Directors. The division of responsibilities between the Board Chairman, Board members and the President are clearly set out in the Charter of the Company.
A.2.2 The chairman should on appointment meet the independence criteria. A chief executive should not be chairman of the same company. If exceptionally a board decides that a chief executive should become chairman, the board should consult major shareholders in advance and should set out sufficient reasons to shareholders and include this information in the next annual report.	Partially observed	According to the legislation of the Russian Federation and the Company's Charter, the person carrying out functions of the Company's sole executive body cannot at the same time serve as a Chairman of the Board of Directors. Chairman of the Board of Directors of the Company is a non-executive member of the Board, but does not meet the independence criteria. At the same time he does not holds positions in executive governance bodies of the Company.
<b>A.3 Board balance. Independence of directors.</b>		
A.3.1 The board should identify in the annual report each non-executive director it considers to be independent.	Observed	Information on every non-executive director that meets independence criteria is included in the 2011 Annual Report (p.6.2.). There are five directors among members of the Board of Directors that meet independence criteria: R. Kocharyan, R. Munnings, E. Novitsky, S. Tchuruk, D. Iakobachvili.
The board should determine regarding all the directors whether the director is independent.	Observed	According to p. 2.5.7. of the Terms of Reference of the Board of Directors on the first meeting of the Board after the Annual General Meeting of shareholders, during which the members were selected, the Board identifies the status of every director (independent, non-executive, executive).

		Status of every member of the Board of Directors was defined by the Board's decision (Minutes of 25.06.2011).
A.3.2 In large companies (according to FTSE 350 list) at least half the board, excluding the chairman, should comprise non-executive directors determined by the board as independent.	Partially observed	Half of the Board members are non-executive directors. Five members of the Company's Board of Directors out of 12 meet the independence criteria, and this constitutes more than 40% of the total number of Board members.
A.3.3. The board should appoint one of the independent non-executive directors to be the senior independent director. The senior independent director should be available to shareholders if they have concerns which contact through the normal channels of chairman, chief executive or finance director has failed to resolve.	Partially observed	Statutory documents of the Company do not provide for the position of a senior independent director, but the information about members of the Board of Directors that meet independence criteria is available to shareholders on the Company's website. If shareholders have relevant questions they may address any of them.
<b>A.4 Appointments to the Board</b>		
A.4.1 There should be a nomination committee which should lead the process for board appointments and make recommendations to the board.	Partially observed	The Nomination, Remuneration and Corporate Governance Committee has been established and is active. The terms of Reference of the Committee defines the sphere of competence of the Nomination, Remuneration and Corporate Governance Committee. One of the key functions of the Committee is provisional review of candidates presented to the Board of Directors for appointment to top positions in the Company. But the Committee does not review appointments to the Board of Directors, as it is in the sphere of competence of shareholders.
A majority of members of the nomination committee should be independent non-executive directors.	Not observed	A majority of the members of the Nomination, Remuneration and Corporate Governance Committee are non-executive directors, and only two member of the Committee meet independence criteria - R. Munnings and R. Kocharyan.
The chairman or an independent non-executive director should chair the committee, but the chairman should not chair the nomination committee when it is dealing with the appointment of a successor to the chairmanship.	Not applicable	L. Melamed, non-executive member of the Board, is a chairman of the Nomination, Remuneration and Corporate Governance Committee. The Nomination, Remuneration and Corporate Governance Committee is not responsible for selecting candidates to the Board of Directors. This is in the sphere of competence of shareholders.
The nomination committee should make available its terms of reference, explaining its role and the authority delegated to it by the board. (The requirement to make the information available should be met by satisfying requests of any interested person and by including the information on a website of the company).	Observed	The Terms of Reference of the Nomination, Remuneration and Corporate Governance Committee is posted on the Company's website ( <a href="http://www.sistema.ru">www.sistema.ru</a> / <a href="http://www.sistema.com">www.sistema.com</a> ) and is available on demand from shareholders.
A.4.2. The nomination committee should evaluate the balance of skills, knowledge and experience on the board and, in the light of this evaluation, prepare a description of the role and capabilities required for a particular appointment.	Partially observed	Candidates for members of the Board of Directors are proposed by the Company's shareholders according to pp. 23, 28 of the Charter. Requirements to the Company's Board members are set out in the Terms of Reference of the Company's Board of Directors. Among other things, a candidate should have sufficient

		<p>professional experience, should not be previously convicted of economic crimes, not be under a ban on taking managerial positions. The candidate should not be a member of governance and control bodies of the companies that are competitors of the Company or be an affiliated person of such companies.</p> <p>The Nomination, Remuneration and Corporate Governance Committee does not develop formal requirements to candidates to the Board of Directors, as a candidate proposed to the Board Membership by shareholders must be included in the voting list according the legislation of the Russian Federation.</p>
A.4.3 For the appointment of a chairman, the nomination committee should prepare a job specification, including an assessment of the time commitment expected.	Observed	<p>Type of work and tasks of the Board Chairman are set out in the Terms of Reference of the Board of Directors of the Company.</p> <p>A Chairman of the Board of Directors is selected by the decision of all member of the Board at the first meeting after the Annual General Meeting of shareholders.</p>
<p>A chairman's other significant commitments should be disclosed to the board before appointment and included in the annual report. Changes to such commitments should be reported to the board as they arise, and their impact explained in the next annual report.</p> <p>A full time executive director should not take on more than one chairmanship in a FTSE 100 company.</p>	Observed	<p>Information on all positions held by the Chairman of the Company's Board of Directors is disclosed and included into the 2010 Annual Report. (p. 9.1) Chairman of the Company's Board of Directors V. Evtushenkov does not hold a position of a chairman of other significant companies except Sistema JSFC.</p>
A.4.4. The terms and conditions of appointment of non-executive directors should be made available for inspection to any interested parties at the company's office and during the Annual General Meeting of shareholders.	Observed	<p>Terms and conditions of appointment of non-executive directors of the Board of Directors is available on the Company's website (<a href="http://www.sistema.ru">www.sistema.ru</a> / <a href="http://www.sistema.com">www.sistema.com</a>), at the Company's office and during the Annual General Meeting of shareholders to its participants.</p> <p>According to the Russian legislation all Board members are elected for one year and could be re-elected unlimited number of times.</p>
The letter of appointment should set out the expected time commitment. Elected board members should undertake that they will have sufficient time to meet what is expected of them.	Partially observed	<p>Before candidates are proposed for appointment to the Board they familiarize themselves with the working plan of the Board of Directors for the coming year, rights and obligations of the Board members and provisional membership in the Board committees.</p> <p>During the induction, a Corporate Secretary of the Company explains to every new member of the Board its procedures and preliminary time commitments for their fulfillment. Before the election, all candidates sign a document confirming their agreement with the proposal that includes, among other issues, an agreement to follow all norms of internal documents of the Company applicable to the Board members.</p> <p>Attendance of meetings and involvement of the Board members in discussion of agenda items is recorded and analyzed for subsequently including this information into the report on the quality of corporate governance.</p>

Information on all other positions held by Board members in other companies should be disclosed to the Board of Directors and included in the Annual Report. Information on changes to such data should be available when they arise.	Observed	<p>Biographies of candidates to the Company's Board, including information on positions held in other organizations, are presented at the Annual General Meeting of shareholders, and information on acting Board members is included in the Annual Report.</p> <p>All candidates to the Board of Directors fill in the questionnaire for candidates for providing the Company with the necessary information.</p> <p>The obligation to disclose any changes to the information provided by members of the Board of Directors is set out in the Terms of Reference of the Company's Board of Directors (p. 2.3).</p>
A.4.5 An executive director should not take on more than one directorship in a FTSE 100 company.	Observed	<p>As of 31.12.2011 the Board of Directors include 12 members, one of them is an executive director (M. Shamolin).</p> <p>M. Shamolin is President of the Company and Board member of Bashneft and MTS.</p> <p>Membership in the Board of the companies of the Sistema group is one of the main duties of executive directors, that is why this does not create conflict of interest for work at the Company.</p>
<p>A.4.6. A separate section of the annual report should describe the work, sphere of competence, procedures and key issues of the nomination committee, including the process it has used in relation to board appointments.</p> <p>An explanation should be given if neither an external search consultancy nor open advertising has been used in the appointment of a chairman or a non-executive director.</p>	Partially observed	<p>The 2011 Annual Report of the Company (p.6.2) includes information on powers and competence of the Nomination, Remuneration and Corporate Governance Committee of the Company's Board of Directors and key issues reviewed by the Committee.</p> <p>At the same time, the Nomination, Remuneration and Corporate Governance Committee does not have powers to directly propose candidates to the Company's Board of Directors, as this is in the sphere of competence of shareholders.</p>
<b>A.5 Information and professional development</b>		
A.5.1. The chairman should ensure that new directors receive full induction on joining the board.	Observed	<p>Every candidate to the Board of Directors before the election meets the Board Chairman, Board members and the management and receives information on work of the Board of Directors, his/her role in the Board of Directors and the Company's business.</p> <p>The Corporate Secretary gives consultation to new members of the Board on procedures and organization of work of the Board and its committees and gives out necessary statutory documents, documents describing the company's strategy, business, markets of presence and financial reports.</p> <p>The above induction procedure for new Board members is not formalized.</p>
As part of this, the company should offer to major shareholders the opportunity to meet a new non-executive director.	Observed	<p>The main shareholder of the Company always meets a candidate to the Board of Directors before the election. This procedure is not formalized.</p>
A.5.2 The Board of Directors should ensure directors have access to independent professional consultation at the expense of the company when fulfilling their professional duties.	Observed	<p>The Terms of Reference of the Board of Directors (p.2.2.1) gives Board members the right to engage external independent experts for assessing materials and decisions on any agenda items. When needed, independent expertise is organized by the secretariat of the Board of Directors.</p>



Board committees should be provided with sufficient resources to undertake their duties, including organizational, human and financial resources.	Observed	Board Committees have access to necessary human, financial and organizational resources of the Company.
A.5.3 If needed, all board members should have access to the advice and services of the company secretary, who is responsible to the board for ensuring that board procedures are complied with.	Observed	According to the Terms of Reference of the Corporate Secretary of the Company, the last version of which was approved by the Board of Directors (Minutes dtd 14.02.2004), one of the functions of the Corporate Secretary is facilitating the work of the Board of Directors, including: providing Board members with requested information and documents regarding Company's work, distribution among Board members of materials for meetings of the Board, facilitation of the work of the Board Committees.
Both the appointment and removal of the company secretary should be a matter for the board as a whole.	Observed	The appointment and removal of the Corporate Secretary is in the sphere of competence of the Board of Directors according to the Charter of the Company (p.32).
<b>A.6 Performance evaluation</b>		
A.6.1. The Annual Report shall contain the information on procedures for assessing the performance of the Board of Directors, its Committees and every director.	Observed	The process of performance evaluation of the Board of Directors is set out in p.6.5 of the 2009 Annual Report of the Company. Since 2009 there is a process of self-evaluation of the Board of Directors work. Board members fill in questionnaires giving their opinion on organization of work of the Board of Directors: membership, structure, process and organization of work of the Board of Directors, work of committees of the Board of Directors, quality of decisions of the Board of Directors in relevant areas. The Board Secretariat annually surveys all members of the Board, analyses results and provides the final analysis to the Corporate Governance and Ethics Committee, the Board Chairman and the members of the Board of Directors.
Non-executive directors led by the senior independent director shall assess the performance of the Chairman of the Board of Directors. In addition, they shall take into account the views of other members of the Board of Directors.	Not applicable	Performance evaluation of the Board of Directors Chairman is carried out during evaluation of performance of the Board of Directors in general.
<b>A.7 Re-election</b>		
A.7.1 All nominees to the Board of Directors shall be approved at the regular Annual General Meetings of shareholders. Thereafter members of the Board of Directors shall be re-elected at intervals of no more than three years.	Observed	According to the Russian legislation Board members are elected at the Annual General Meeting of shareholders for 1 year (for the period till the next Annual General Meeting of shareholders) and could be re-elected unlimited number of times.
Information about nominees to the Board of Directors shall include biographic data about nominees and/or any other information to enable shareholders to take an informed decision about electing or re-electing members of the Board of Directors.	Observed	Information on candidates to the Board of Directors including their biographical details is provided among other materials for the Annual General Meeting of shareholders which elects members of the Board of Directors of the Company.

A.7.2. Non-executive directors shall be elected for specified terms and thereafter may be re-elected or dismissed from office in accordance with applicable corporate legislation.	Observed	According to the Russian legislation, Board members are elected at the Annual General Meeting of shareholders for one year (for the period till the next Annual General Meeting of shareholders) and could be re-elected unlimited number of times.
The board of directors should explain to shareholders why they believe an individual should be elected as a non-executive member of the Board of Directors.	Partially observed	Shareholders are provided with biographical details and professional skills of candidates and shareholders make independent conclusions on their competence and advisability to elect them to the Board.
The chairman should confirm to shareholders when proposing re-election that, following formal performance evaluation, the individual's performance continues to be effective.	Partially observed	Every year when new membership of the Board is appointed, information on the work of the Board of Directors in the previous year is disclosed, including attendance of meetings by the Board members and the work of Committees where Board members participated. Shareholders take independent decisions on the quality of work of the Board of Directors and their members.
Any term beyond six years for a non-executive director should be subject to particularly rigorous review, and the need for progressive refreshing of the board should be taken into account.	Not applicable	<p>According to the Russian legislation, Board members are elected at the Annual General Meeting of shareholders for one year (for the period till the next Annual General Meeting of shareholders) and could be re-elected unlimited number of times.</p> <p>Every year when new membership of the Board is appointed information on the work of the Board of Directors in the previous year is disclosed, including attendance of meetings by the Board members and the work of Committees where Board members participated and shareholders take independent decisions on the quality of work of the Board of Directors and their members.</p>
A non-executive director may hold his/her position for not longer than nine years if he/she is re-elected every year. If an executive director serves more than nine years, his/her status should not be defined by the Board of Directors as independent.	Observed	<p>According to the Russian legislation Board members are elected at the Annual General Meeting of shareholders for one year (for the period till the next Annual General Meeting of shareholders) and could be re-elected unlimited number of times.</p> <p>The Terms of Reference of the Board of Directors (p.2.5.5) defines independence criteria for members of the Board of Directors, according to which a person who is a Board member for longer than nine years cannot be considered independent.</p>

## B. REMUNERATION

### B.1 Level and make-up of remuneration

B.1.1. The performance-related elements of remuneration should form a significant proportion of the total remuneration package of executive directors to give the keen incentives to perform at the highest levels.	Observed	If the Company generates income, members are paid remuneration according to performance results in the year of USD 250-325K. 50% of this remuneration consists of cash and 50% - of the Company's shares. If the Company's capitalization grows, Board members are paid additional remuneration equaling 0.1% from the amount of the capitalization growth which was achieved between two Annual General Meetings of shareholders.
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		Besides they are paid remuneration for participating in meetings of the Board of Directors and meetings of the Board Committees. These incentive mechanisms allow aligning the size of remuneration of the Board members with fulfillment of shareholder goals of the Company.
The Nomination and Remuneration Committee should participate in developing the system of remuneration for the Board members.	Observed	The Policy on remuneration and compensations for the Company's Board members sets out a clear formula for calculating their remuneration. Currently there are no amendments to the above mentioned Policy under consideration. If it is necessary to make changes to the above Policy, the Nomination, Remuneration and Corporate Governance Committee of the Board of Directors plays a key role in developing such changes.
B.1.2 If share options are provided for by the existing remuneration system, they should not be offered at a discount rate.	Observed	Executive share options are not provided for work in the Board of Directors.
B.1.3 The size of remuneration of non-executive directors shall depend, among other things, on their duties and the level of responsibility. Non-executive directors shall not receive stock options. If, exceptionally, options are granted, shareholder approval should be sought in advance. A member of the Board who acquired shares by exercising an option shall hold them until at least one year after he/she leaves the Board. If a non-executive director receives a stock option, it may mean that he/she does not meet independence criteria any longer.	Observed	Board members receive additional remuneration for serving as Chairman of the Board of Directors, Deputy Chairman and Chairman of the Board Committee. Special remuneration is paid for participation in the Board meetings and meetings of the Board Committees. Executive share options are not provided for work in the Board of Directors.
B.1.4 Where a company releases an executive director to serve as a non-executive director elsewhere, the remuneration report should include a statement on his earnings in such company.	Partially observed	Members of the Management Board who are members of Boards of Directors of subsidiaries do not receive additional remuneration for work in such Boards of Directors. Members of the Management Board (executive directors) who are members of Boards of Directors in other companies receive remuneration for work in Boards of Directors of such companies according to their regulations. The information on the size of remuneration received by employees of the Company for acting as a Board member at other companies is not disclosed.
B.1.5 The remuneration committee should consider what compensation commitments their directors' terms of appointment would entail in the event of early termination. The remuneration should be paid on a pro rata basis.	Observed	According to p.1.6 of the Policy on remuneration and compensations for the Board members of the Company, in the event of early termination of the director's appointment, remuneration is calculated on a pro rata basis.
B.1.6 Notice or contract periods should be set at one year or less. If it is necessary to offer directors longer notice or contract periods, such periods should reduce to one year or less after the initial period.	Observed	According to the Russian legislation, Board members are elected at the Annual General Meeting of shareholders for 1 year (for the period till the next Annual General Meeting of shareholders) and could be re-elected unlimited number of times.

<b>B.2 Procedure</b>		
B.2.1 The Board of Directors should establish a Remuneration Committee consisting of at least three independent non-executive directors (for large companies).	Partially observed	The Nomination, Remuneration and Corporate Governance Committee has been established and is active. The Committee includes <b>six</b> directors, most of whom - A. Goncharuk, D. Zubov, R. Kocharyan, R. Munnings, L. Melamed - are non-executive directors and two of whom meet independence criteria: R. Kocharyan, R. Munnings
The remuneration committee should make available its terms of reference, explaining its role and the authority delegated to it by the board. (The requirement to make the information available should be met by satisfying requests of any interested person and by including the information on a website of the company).	Observed	The sphere of competence of the committee is set out in the Terms of Reference of the Nomination, Remuneration and Corporate Governance Committee, the last version of which was approved by the decision of the Board of Directors (Meeting on 24.09.2011). The Terms of Reference of the Nomination, Remuneration and Corporate Governance Committee is posted on the Company's website ( <a href="http://www.sistema.ru">www.sistema.ru</a> / <a href="http://www.sistema.com">www.sistema.com</a> ) and is available on demand from shareholders.
Where remuneration consultants are appointed, a statement should be made available of whether they have any other connection with the company.	Not applicable	In 2011 no external remuneration consultants were engaged in the work of the Company's Board of Directors.
B.2.2 The remuneration committee should have delegated responsibility for setting remuneration for all executive directors and the chairman.	Observed	Amount and procedure for paying out remuneration and compensation to the Company's Board member are set out in the Policy on remuneration and compensations, the last version of which was approved by the Annual General Meeting of shareholders (Minutes of 30.06.2006). If changes should be made to the above Policy, the Nomination, Remuneration and Corporate Governance Committee develops necessary changes.
The committee should also recommend and monitor the level and structure of remuneration for senior management. The definition of 'senior management' for this purpose should be determined by the board but should normally include the first layer of management below board level.	Observed	One of the key functions of the Nomination, Remuneration and Corporate Governance Committee according to the respective Terms of Reference is preliminary review of terms of labor contracts of the President and Board members presented for consideration of the Company's Board of Directors, evaluation of performance of the Company's top management and defining the size of their remuneration.
B.2.3 The board itself or, where required by the Charter, the shareholders should determine the remuneration of the non-executive directors within the limits set in the Articles of Association. Where permitted by the Ch, the board may however delegate this responsibility to the remuneration committee.	Observed	The Policy on remuneration and compensations for the Company's Board members, the last version of which was approved by decision of the general meeting of shareholders (Minutes of 30.06.2006), sets out a clear formula for calculating remuneration of the Board members. A special decision of the Nomination, Remuneration and Corporate Governance Committee for such payments is not required.
B.2.4 Shareholders should be invited specifically to approve all new long-term incentive schemes and significant changes to existing schemes.	Observed	Long-term incentive schemes are approved by the Board of Directors and, when needed, by the Annual General Meeting of shareholders, and

shareholders discuss such matters both at the level of the Board of Directors and the level of the Annual General Meeting of shareholders.

## **C. ACCOUNTABILITY AND AUDIT**

### **C.1 Financial reporting**

C.1.1 The annual report should include financial reports and the auditor's opinion.	Observed	Financial reports of the Company are disclosed annually and include the auditor's opinion.
C.1.2 Board members should prepare a report on results of the development of the company over the year.	Observed	Report of the Board of Directors on development of the Company is included in the text of the Company's Annual Report.

### **C.2 Internal control**

C.2.1 The board should, at least annually, conduct a review of the effectiveness of the group's system of internal controls and should report to shareholders that they have done so. The review should cover all material controls, including financial, operational and compliance controls and risk management systems.	Observed	The Board of Directors annually reviews the report from the department of Internal Control of the Company on results of the year with analysis of existing control systems and detected deficiencies. A report from the Revision Commission is attached to materials of every Annual General Meeting.
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### **C.3 The Audit Committee and Auditors**

C.3.1 The board should establish an audit committee of at least three independent non-executive directors (for large companies). At least one member of the audit committee shall have relevant financial experience.	Partially observed	The Nomination, Remuneration and Corporate Governance Committee of Sistema JSFC has been established and is active. The Committee includes five members of the Board of Directors, three of whom meet independence criteria - R. Munnings, E. Novitsky and D. Iakobachvili, and two of whom are non-executive directors - R. Sommer and D. Zubov. R. Munnings is Chairman of the Audit Committee of the Board of Directors. He meets independence criteria and has vast experience in financial audit.
C.3.2 The main role of the audit committee should be set out in the terms of reference.	Observed	The sphere of competence of the Audit and Finance committee is set out in the Terms of Reference of the Committee, the last version of which was approved by the Board of Directors (Meeting on 24.09.2011).
C.3.3 The terms of reference of the audit committee, including the authority delegated to it by the board, should be made available. (The requirement to make the information available should be met by satisfying requests of any interested person and by including the information on a website of the company).	Observed	The terms of reference of the Audit and Finance Committee is posted on the Company's website ( <a href="http://www.sistema.ru">www.sistema.ru</a> / <a href="http://www.sistema.com">www.sistema.com</a> ) and is available on demand from shareholders.
A separate section of the annual report should describe the work of the committee.	Observed	The report on the work of the Audit and Finance Committee is included in the Company's 2011 Annual Report (p. 6.2).
C.3.4 The audit committee should make sure that staff of the company may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters.	Observed	The Audit and Finance Committee reviews issues of the functioning of the hot line used by the Company's employees and other interested parties for raising concerns about possible

		improprieties in the financial sphere on a confidential basis.
C.3.5 The audit committee should monitor and review the effectiveness of the internal audit process. Where there is no internal audit function, the audit committee should consider annually whether there is a need for an internal audit function and make a recommendation to the board.	Observed	According to the Terms of Reference of the Audit and Finance Committee of the Company's Board of Directors, one of the key functions of the Committee is monitoring the internal audit system of the Company. The Internal Audit Service carries out internal audit functions. The Audit and Finance Committee together with the head of the above mentioned Service and the Company's management analyzes implemented activities aimed at removing deficiencies of internal business processes.
C.3.6 The audit committee should have primary responsibility for making a recommendation on the appointment of the external auditors.	Observed	According to the Terms of Reference of the Audit and Finance Committee of the Company's Board of Directors, the Committee analyzes the work of external auditors and makes recommendations for the Board of Directors on appointment, re-appointment and removal of external auditors.
C.3.7 The annual report should include information on independence criteria for auditors and explain to shareholders how, if the auditor provides non-audit services, auditor independence is safeguarded.	Observed	The 2011 Annual Report of the Company includes statement on the policy of safeguarding objectivity and independence of the Company's auditor.
<b>D. RELATIONS WITH SHAREHOLDERS</b>		
<b>D.1 Dialogue with main shareholders</b>		
D.1.1 The chairman should ensure that the views of shareholders on the development of the company are communicated to the board. The chairman should regularly discuss strategy with major shareholders. Non-executive directors should be offered the opportunity to attend meetings with major shareholders and should expect to attend them if requested by major shareholders.	Observed	Representatives of the majority of large shareholders are members of the Board of Directors of the Company. The IR department of the Company works with the largest institutional investors. Results of its work, including views of main institutional investors of the Company on strategy and development outcomes of the Company, are regularly reviewed by the Board of Directors within the IR strategy of the Company. It is mandatory for all members of the Board of Directors, including non-executive directors, to attend the Annual General Meeting of shareholders.
The senior independent director should hold sufficient meetings with shareholders to discuss development of the company.	Not applicable	Company's statutory documents does not provide for the position of a senior independent director. Prior to every meeting of the Board of Directors independent members of the Board hold an informal meeting in the form of a business dinner, which is also attended by the management of the Company. Information on independent members of the Board of Directors is available to shareholders via the Company's website. If shareholders have relevant questions they may address any of them.
D.1.2 The annual report should state how the members of the board develop an understanding of the views of major shareholders about development of the company.	Observed	Representatives of the majority of large shareholders are members of the Company's Board of Directors. The IR department of the Company works with largest institutional investors. Results of its work, including views of main institutional investors of the Company on

		development of the Company, are regularly reviewed by the Board of Directors within the IR strategy of the Company. It is mandatory for all members of the Board of Directors, including non-executive directors, to attend the Annual General Meeting.
<b>D.2 Constructive use of the AGM</b>		
D.2.1 The company should ensure that votes of all persons that participated in the general meeting are properly recorded. The minutes of the meeting should include the number of persons that participated in the voting on every agenda item and the number of votes "for", "against" and "abstained".	Observed	All votes of shareholders are registered by the Teller Committee and this information is included in the Minutes of the Company's Annual General Meeting of shareholders. All "for", "against" and "abstained" votes on every agenda item are recorded separately, voting results for every item are disclosed.
D.2. At any general meeting, the company should propose a separate draft resolution on each separate issue.	Observed	According to the Russian legislation and the Company's Charter, every agenda item at the general meeting is accompanied by a separate draft resolution with voting options "for", "against" and "abstained".
D.2.3 All members of the Board of Directors are to attend the general meeting. Committee chairmen should be available for answering questions of shareholders.	Observed	According to p. 2.3. of the Terms of Reference of the Board of Directors, all members of the Board of Directors are to attend the General Meeting and be able to answer questions from the participants of the meeting. Shareholders that participate in the Annual General Meeting may put questions to any member of the Board of Directors attending the meeting.
D.2.4 The company should arrange for the Notice of the AGM and related papers to be sent to shareholders at least 20 working days before the meeting.	Observed	According to its Charter, the Company circulates the Notice of the AGM and publishes related materials not later than 30 days before the meeting.

**President**

**M.Shamolin**

**Chief Accountant**

**V. Platoshin**