TP Group Annual Report 2005

Poland's leading telecoms provider

TP Group is undergoing significant change

TP Group is refocusing to become a customer-centric, service-orientated company. We have laid a strong foundation on which to build the new TP Group. We have strengthened our balance sheet, reduced our costs, aligned our products and services, and created an innovative, forward-focused enterprise.

TP has access to the most advanced FT technology, which we are developing and marketing into exciting new convergent products. Our vision is to become the leading integrated telecom operator in Central and Eastern Europe.

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TP Group Financial and Operational Highlights 2005

All figures in PLN according to IFRS

Revenue
18.3bn
-1.0%

Broadband customers
1.2mn
+70.8%

EBITDA margin
43.6%
-0.8pp

Mobile customers
9.9mn
+33.3%

Net profit
2.6bn
+1.7%

More focused and far stronger

Marek Józefiak
President of the Board

Alain Carlotti
Executive Vice-President of the Board

Dear shareholders

2005 was a year in which the TP Group reached a critical turning-point: we are now poised to enter a new phase in our development, pursuing a far-sighted strategy which will enable us to realise our vision for the Group. The acquisition in the fourth quarter of France Telecom's remaining 34% stake in PTK Centertel, together with the re-branding of our mobile operations under the globally-recognised Orange brand, were major milestones in this regard.

As in 2004, the market environment for our traditional core business was a challenging one. We continued to face considerable revenue pressures in the fixed-line business; but we also continued to demonstrate our ability to mitigate the impact of these pressures through the introduction of innovative market offers and the ongoing migration of fixed-line revenues away from variable, volume-based streams and towards the stability of monthly access fees.

Moreover, we were again the prime beneficiary of the strong growth in Poland's mobile and data markets, which we recognise as crucial to the future development of the business. In both of these vital segments we achieved strong, double-digit growth, and exceeded our subscriber acquisition targets for the year. As a result of this performance, we were able to limit the overall decline in 2005 Group revenues to just 1%.

A critical turning-point

During the last few years, the industry environment in which we operate has become significantly more demanding. The regulatory environment has evolved considerably, not least as a result of Poland's 2004 accession to the European Union. TP is now subject to the same regulation as other European telecom companies, with TP being forced to open up its network to alternative providers and the market becoming a great deal more competitive.

But as well as new competitors and new regulations, we now face new technological challenges. The market is entering a second stage of technological evolution, driven by the rapid adoption of fixed and mobile broadband services. We believe that this will be the key factor in shaping the evolution of the market over the next few years, and have devised a strategic roadmap to ensure that TP is ideally placed to take full advantage of the many exciting opportunities it will create.

A solid platform for growth

We are in a very strong position to implement this new strategy.

TP Group has undergone a fundamental transformation, from a government-owned, fixed-line business to a publicly-listed, integrated fixed voice and data and mobile operator in strategic partnership with one of Western Europe's leading telecom operators.

The financial restructuring we undertook between 2002 and 2005 has put in place a solid foundation for investment in the future of the business. Our key strategic goals during this process were to improve profitability, maximise cash flow and rationalise capital expenditure, particularly in the fixed-line segment. Our success in all of these areas significantly improved the Group's capital structure by allowing us to decrease our debt, excluding loans from related parties by PLN 7 billion. By the end of 2005, we had achieved a 30% net gearing ratio; and as a result, all three rating agencies raised TP's credit rating from BBB- to BBB+.

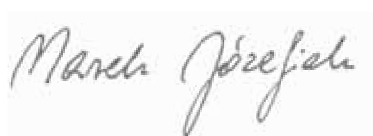
In short, the TP Group today enjoys the benefits of a new financial stability.

A new challenge

Our aim now is to become the leading integrated telecom operator in Central and Eastern Europe.

If we are to realise this ambition, we must be ready to deal with the new market challenges resolutely and effectively. The formal restructuring process is behind us; it is time to launch TP on the next stage in its development.

Based on an integrated approach to the provision of mobile, voice, data and TV services, we are confident that this new strategic roadmap (discussed in more detail in the Strategy section on pages 15 to 18 of this report) will be implemented successfully.



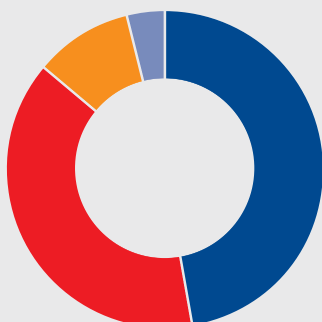
Marek Józefiak
President of the Board
31 March 2006

Alain Carlotti
Executive Vice-President of the Board
31 March 2006

TP Group at a Glance

TP Group is Poland's leading telecommunications provider. We have operations in fixed-line voice and data and mobile networks. TP Group is 47.5% owned by France Telecom. In 2005 we achieved revenues of PLN 18.3bn and a net profit of PLN 2.6bn.

TP Group share capital structure
2005



France Telecom	47.50%
Other shareholders	38.65%
GDR holders represented by Bank of New York*	9.98%
State Treasury**	3.87%

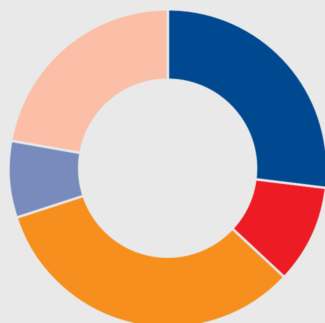
* Data at 6 September 2004 (the last official notification received from the Bank of New York)

** At the General Meeting of Shareholders of TP held on 18 July 2005, the State Treasury registered 54,187,729 shares, constituting a 3.87% interest in the share capital of TP and corresponding to 3.87% of the total voting power.

TP Group revenue composition

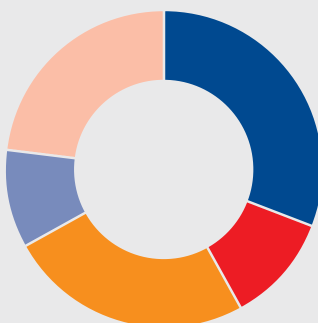
2004

Mobile	27%
Data	10%
Fixed-line traffic	33%
Interconnect & other*	8%
Access fees	22%

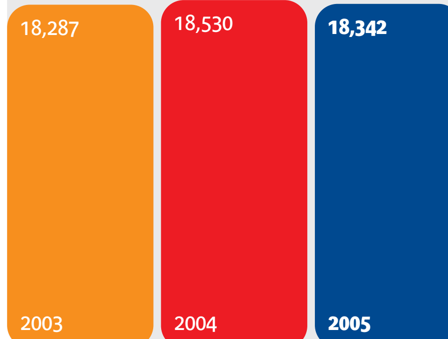


2005

Mobile	31%
Data	11%
Fixed-line traffic	25%
Interconnect & other*	10%
Access fees	23%



Group Revenues
PLN mn



* Including: Fixed-line interconnect, payphone, radio, telecommunications, sales of goods and other revenue
2004 adjusted to IFRS changes introduced in 2005

Revenue by segment (PLN mn)[†]

Fixed PLN mn

12,496

Mobile PLN mn

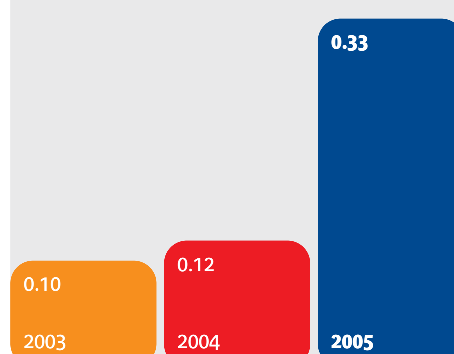
6,424

Other PLN mn

243

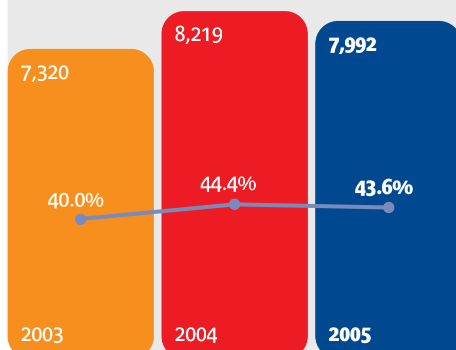
TP Share price
2003 – 2005

Dividends per share
PLN



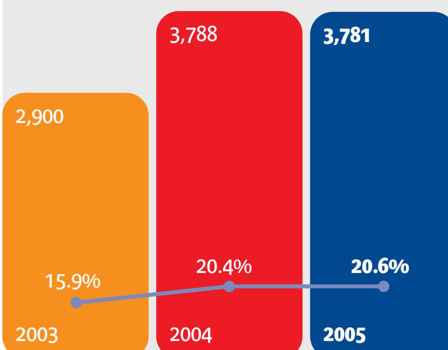
EBITDA and Margin
PLN mn

● Margin

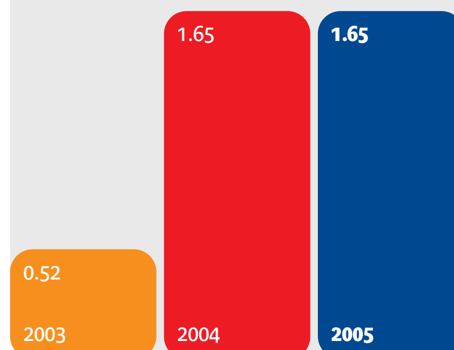


EBIT and Margin
PLN mn

● Margin



Earnings per share
PLN



† TP Group revenues are the sum of revenues from fixed, mobile and other operations adjusted by intersegment transactions.

A strong management team

1 Marek Józefiak
President of the Board of Telekomunikacja Polska
Marek Józefiak graduated in Telecommunications from Wrocław Technical University. From 1990 until 1997 he held the position of CEO in a variety of private sector Polish businesses; he was appointed to the Supervisory Board of the TP Group in 1996. He became CEO of PTK Centertel in 1997, and subsequently, President of the Board. Since 2002, he has been Chairman of PTK Centertel's Supervisory Board. In 2001 he was appointed President and CEO of Telekomunikacja Polska.

2 Alain Carlotti
Executive Vice-President of the Board
He is a graduate of the Ecole Polytechnique and the Ecole Nationale Supérieure des Télécommunications in Paris and of the Chicago Northwestern University. Alain Carlotti is Chief Engineer of Telecommunications and previously appointed President of different companies. Inside TPSA, he is the Executive Vice-President of the Board since December 2005. Before, he was Chairman and CEO of KeyMro. In 1998, he was appointed President of Thomson Multimedia Asia until 2002. He was also Chairman and CEO of the French telecommunications group Pouyet (1993-1998). In 1989, he was the CEO of two Alcatel Group software companies. He started his career at France Telecom and, from 1972 to 1975, he headed FT's International Network Department.

3 Pierre Hamon
Board Member (Marketing, Sales and Customer services)
Pierre Hamon graduated from the Nancy School of Mining Engineering, the French Petroleum Institute (Economy) and HEC/CPA (Executive MBA). He started his career as a project engineer with Somdiaa. He joined Chronar Corporation, USA in 1982, where he became Head of International Marketing. In 1987, he became the President and CEO of Chronar France. He joined France Telecom in 1990 as Director of the Eurodisney project and Regional Operations. From 1993 he held the post of Business Strategic Marketing Director in the France Telecom Corporate Office, and from 1997 to 2003 he was successively FT's Indirect Sales Director, and Director of Sales to Business Customers. From April 2003 to April 2004, Mr. Hamon was Director of International operations of France Telecom and a member of the TP Supervisory Board. He joined TP Management Board in May 2004.

4 Bruno Duthoit
Board Member (Strategy & Investments)
Bruno Duthoit was educated at the Ecole Polytechnique and Ecole Nationale Supérieure des Télécommunications in Paris. He started his career as an engineer with France Telecom. From 1984 to 1990 he worked for the French Government in industrial and trade development, rejoining FT in 1991 to open a representative office in Czechoslovakia. From 1996 to 1999, he was General Manager of Globtel GSM (now Orange Slovensko). He joined TP's Management Board in 2001.

5 Jean-Marc Vignolles
Board Member and Chief Executive Officer of PTK Centertel
A graduate of the Ecole Normale Superieure and Paris Institute for Political Sciences, Jean-Marc Vignolles joined France Telecom in 1983, holding various managerial positions in the IT Division until 1989, and in the Key Accounts Division until 1994, when he was appointed Vice-President of the International Development Division responsible for CEE and CIS countries. He was appointed Vice-President of the Management Board of PTK Centertel, CCO in 2001 and CEO in 2004.

6 Konrad Kobylecki
Board Member (Networks, Carriers & IT)
Konrad Kobylecki is a graduate in Electronics of Warsaw University of Technology. He also completed courses at Northwestern University, St. Gallen Institute and Harvard Business School. He began his career in the banking sector, before joining PTK Centertel in 1999. He became TP S.A. Chief Technology Officer and Board Member in charge of technology in 2004.

7 Jacek Kałłaur
Board Member (Human Resources)
A graduate of Warsaw University, Jacek Kałłaur worked for PHZ Polservice, spending several years in its Algerian office. Back in Poland, he joined Coopers & Lybrand Management Consultants. In 1993 he was appointed Board Member and HR Manager of Kraft Foods Polska. He joined TP's management in 2005.

8 Benoît Mérel
Chief Financial Officer
He is a graduate of the Institut Commercial Superieur in Paris, a qualified Certified Public Accountant andhas completed a Postgraduate study in Institut d'Etude Politiques de Paris. He started his career in 1988 in Audit which included a two year assignment in Hong Kong where he turned around the finance organisation of the Asia Pacific Agence France Press headquarters. He joined France Telecom Group in 1994 holding various positions in the International Network Division until 1999. In 2000 he took over the France Telecom position of Head of Group Controlling. In September 2004, he was nominated Acting CFO of Equant – world wide business communication leader and a member of FT Group (New York Stock Exchange and Euronext Paris listed company). In August 2005, Benoît Mérel joined TP Group initially as deputy CFO and Head of Controlling Division.

1 5
2 6
3 7
4 8

TP S.A. Supervisory Board

The composition at 1 January 2005:

Jan Kulczyk	Chairman
Jean-Paul Cottet	Deputy Chairman
Andrew Seton	Deputy Chairman
Jan Waga	Secretary
Claude Benmussa	Board Member
Jacques Champeaux	Board Member
Jerzy Drozd	Board Member
Bożena Dyjak	Board Member
Stefan Kawalec	Board Member
Michel Monzani	Board Member
Elżbieta Pacuła	Board Member

On 18 January 2005, Mr. Jan Waga resigned his position on the Supervisory Board.

On 1 February 2005, Messrs. André Cathelineau, Yves Le Moüel and Jean-Pierre Temime were appointed by the Extraordinary Shareholders Meeting as Members of the Supervisory Board.

On 26 April 2005, Mr. Stefan Kawalec resigned his position on the Supervisory Board.

On 26 April 2005:
- the mandates of Mr. Jan Kulczyk, Mr. Claude Benmussa, Mr. Jerzy Drozd, Ms. Bożena Dyjak and Ms. Elżbieta Pacuła expired;
- Mr. Pierre Hamon and Mr. Georges Leperchey resigned from the Supervisory Board;
- Messrs. Jan Kulczyk, Claude Benmussa, Timothy Boatman, Jerzy Drozd, Tadeusz Han and Krzysztof J. Ners were appointed by the Annual General Shareholders Meeting as Members of the Supervisory Board.

The composition at 31 December 2005:

Jan Kulczyk	Chairman
Jean-Paul Cottet	Deputy Chairman and Chairman of the Strategy Committee
Andrew Seton	Deputy Chairman and Chairman of the Remuneration Committee
Michel Monzani	Secretary
Claude Benmussa	Board Member
Timothy Boatman	Board Member and Chairman of the Audit Committee
André Cathelineau	Board Member
Jacques Champeaux	Board Member
Jerzy Drozd	Board Member
Tadeusz Han	Board Member
Yves Le Moüel	Board Member
Krzysztof J. Ners	Board Member
Jean-Pierre Temime	Board Member

At present, TP Group has four independent members in the Supervisory Board, namely Mr. Andrew Seton, Mr. Timothy Boatman, Mr. Tadeusz Han and Mr. Krzysztof Ners.

Innovative products, reduced time to market…

Alain Carlotti
Executive Vice-President of the Board

Dear Shareholders,
I am very pleased to be introducing the operational review for 2005, my first as Executive Vice-President of the Board.

2005 has been a challenging year, but one which represents an inflection point in the history of the company as we build upon the excellent successes of the past and grow TP Group towards an exciting future.

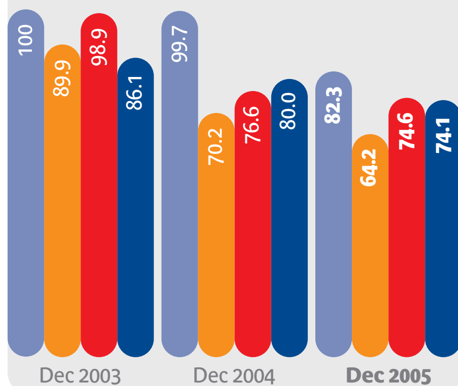
In the following pages I will report to shareholders on the highlights of 2005 and outline TP Group's strategy for the next three years.

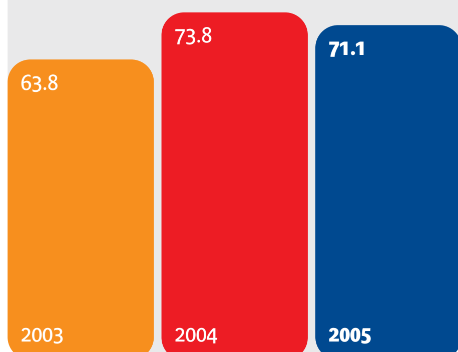
I look forward to communicating on the progress of our company in meeting its new strategic objectives.

TP Change Programme

In 2005 the Group carried out the TP Change programme – a far-reaching initiative to realign operations according to customer-centric principles. In place of the old structure, which divided the Group's operations between Fixed-Line, Mobile and Data business units, we created three new entities, established on 1 May 2005: Home (residential fixed-line voice and Internet access services), Enterprise (fixed-line, mobile and data services and key corporate accounts) and Sales and Service (integrating all customer-facing functions). In addition, TP started to integrate its Networks and IT activities into a single unit.

These actions were major steps in furthering TP's ongoing commitment to getting closer to its customers. They will also make it easier for us to develop targeted marketing offers based on the real integration of business models, and thus to derive enhanced benefits from operational convergence while delivering greater value to all our customers.





Fixed-line overview

The fixed-line telecommunications market in Poland was characterised in 2005 by intense competition, which created new pressure on TP's fixed-line revenues. In addition, ongoing tariff reductions by all major operators in the Polish mobile market stimulated increasing fixed-to-mobile substitution, which also had an impact on TP's fixed-line business.

TP's fixed-line revenues in 2005 decreased by 7.0% compared to the previous year. This was due principally to lower usage and lower fixed voice market share, reflecting the migration of traffic to mobile networks and the impact of carrier pre-selection. The decline was partly offset by the strong growth in the data segment (particularly broadband), in which revenues increased by 15.6% compared to 2004.

However, we are making steady progress in transforming our revenue base, i.e. decreasing the reliance on variable traffic revenue and increasing the revenue contribution from stable sources. In 2005, fixed voice traffic represented less than one-third of total revenue.

Migrating revenues away from voice traffic and towards access and interconnection fees helps us to slow down the erosion of fixed voice revenues. This reflects our success in pursuing the goal of introducing innovative tariff packages, as stated in our 2004 annual report.

In the fourth quarter of 2005 we were particularly successful in migrating customers from standard tariff plans towards those with higher monthly fees – New Tariff Plans (NTP). Fixed access fees represented over 43% of fixed-line voice revenues in 2005, compared to 37% in 2004. By January 2006, we had secured more than 3.5 million NTP customer activations. The average NTP customer not only generates higher traffic, but also uses much less pre-selection. As a result, the overall ARPU of NTP customers is higher than that of standard tariff plan customers.

The data segment – broadband in particular – continues to be a key growth driver for the Group. As in 2004, we benefited from exceptionally strong growth in the broadband market in 2005. Our broadband customer base grew by over 480,000 subscribers, to 1.17 million, and broadband revenues increased by 71%.

Overall, data service revenues grew by 15.6% in 2005, and Internet revenues by 24%. Data service revenues constituted 12% of total TP Group revenues in the fourth quarter. During 2005, we benefited from continuing growth in the take-up of data transmission services in our Enterprise business, as detailed overleaf.

Our success in transforming our revenue base has had a major impact on the Home division. The shift away from pay-per-use to access-fee-based revenues has helped to protect ARPU and MoU, while also stabilising TP's market share.

...customer-centric, service-orientated...

Home

2005 saw TP make good progress in continuing to popularise its more advanced ADSL products ("Neostrada"), and thus increase ADSL ARPU. In both spring and early summer, we launched market promotions of the 512 kbps Neostrada option. These were very successful; in June, for example, over 80% of our new broadband Internet access subscribers ordered the Neostrada 512 service.

We also took steps to promote non-standard distribution channels – such as the Internet and the TP Partners sales network – as a means of signing up new Neostrada customers.

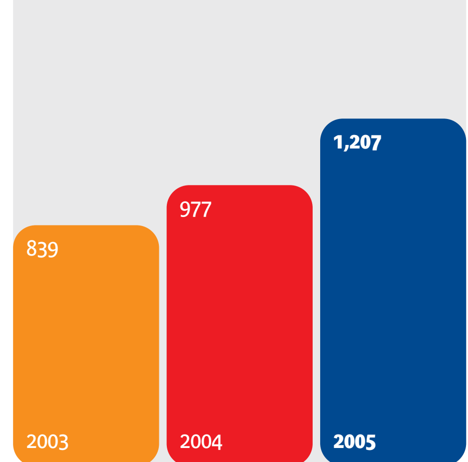
2005 was a particularly eventful year for the data segment of the Home business.

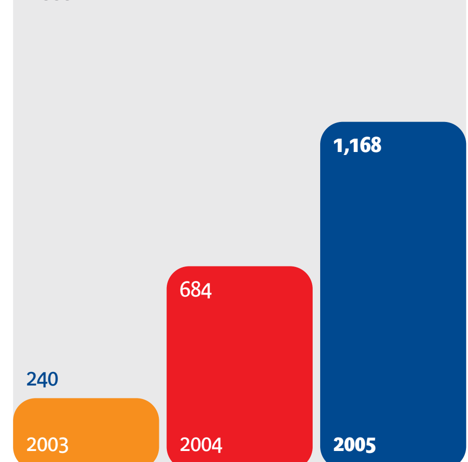
Launched in December 2005, Livebox is a universal multimedia gateway based on Neostrada ADSL, and represents a major milestone in the evolution of TP's offer to residential customers.

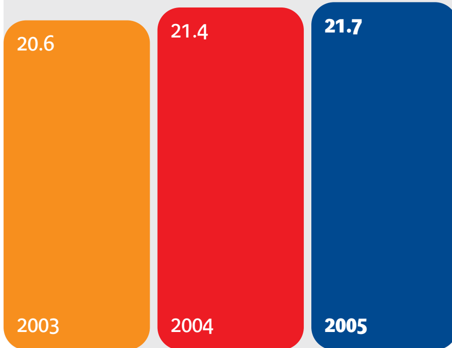
The new modem enables users to connect a range of home appliances to the broadband network and provides access to multimedia services. Currently, it is offered as a Wi-Fi modem that provides wireless access to the Neostrada TP service, but soon new innovative services are to be added. This service will eventually enable subscribers to have access not only to wireless broadband Internet access, but also VoIP voice services (introduced in February 2006), as well as IP TV, Video-on-Demand and a range of other value-added services.

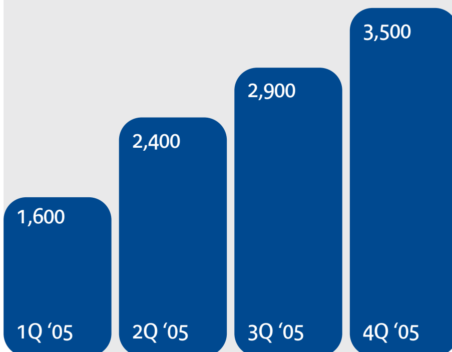
Livebox has already been launched in France by FT in 2004, and as at the end of 2005 FT Group had 1.8 million customers. We thus have access to an invaluable fund of experience to help us exploit the full potential of the product, which represents a revolutionary development for the Polish market.

Innovation and convergence will fuel the growth of TP Group in the coming years. Therefore in 2006 we intend to introduce a number of new products: TV over DSL in 2Q, Video on Demand in 3Q, Common Voicemail (i.e. one voicemail for mobile and fixed) in 2Q, and Common Service Portal with One Address Book for mobile and fixed in 3Q. In 1Q 2006 we launched our VoIP offer and completed the commercial launch of 'Business Everywhere', an initiative described in the next section.









Launched in December 2005, Livebox is a universal multimedia gateway supporting 'triple play' service.

Enterprise

Continuing the progress on tariffs made in 2004, we have successfully implemented a tariff modification strategy for Enterprise customers as well as Home users. We continue to move our business customer base to new tariff packages with a higher monthly fee and built-in value-added services.

Business customers are also making increasing use of our data services. This resulted in growth of over 10% in data transmission revenues in 2005, along with the early take-up of our new IP-VPN services. By the end of the year, we had signed contracts for over 650 ports, and we expect this trend to gather momentum in 2006. We also saw steady growth in xDSL services and in more mature technologies such as Frame Relay and ATM.

Overall, we expect to continue to stimulate growth in the Enterprise segment by capitalising on the introduction of new technologies to our growing customer base.

A prime example of this was the September '05 launch of Business Everywhere, a revolutionary new service which allows business people to access their corporate intranet securely from a remote location – be it at home, in a client's office elsewhere in Poland, or from any of 140 other countries around the world.

Business Everywhere is an ideal solution for both travelling business people and teleworkers. Users can connect to their intranet via a dial-up ISDN or PSTN line, using a broadband ADSL connection, or via wireless access: Wi-Fi, GPRS, EDGE or UMTS. All they need is a PC with the relevant software installed, together with a PIN code supplied by TP. (For wireless access, users must also have either a Wi-Fi, a GPRS or an EDGE card.)

...focused on value creation...

Mobile overview

The Polish Mobile market continued to grow strongly in 2005. By the end of the year, penetration of mobile phones stood at 76.6%, with 29 million mobile users – 26% more than in 2004.

In a highly competitive environment, PTK Centertel outperformed the market in terms of revenue and subscriber growth. We achieved a market-leading 41% share of total net additions in 2005, and our volume share of the market for the year as a whole was at its highest-ever level of 34%.

Revenues increased by 13.9% year-on-year, driven by rising usage as well as our growing subscriber base. Strong volume growth was more than enough to compensate for higher interconnect costs, and we recorded a 16% increase in EBITDA, with EBITDA margin rising to 37.8%.

The price cuts initiated in 2004 continued to put pressure on ARPU in 2005. Falling prices stimulated a migration towards lower-price plans as well as strong growth in the pre-paid segment. As a result, blended ARPU in 2005 decreased by 16%.

However, we took steps to respond to this pressure by introducing new offers to stimulate usage, increase the share of non-voice revenue, and provide more value-added and content-related services. As a result, in the fourth quarter, blended minutes of usage increased year-on-year by almost 25%, and by 5% on a quarterly basis.

Despite our very strong performance in terms of new additions, acquisition costs fell by almost 37%. Good results were achieved in both segments: post-paid SAC improved by 8% and pre-paid by over 60%.

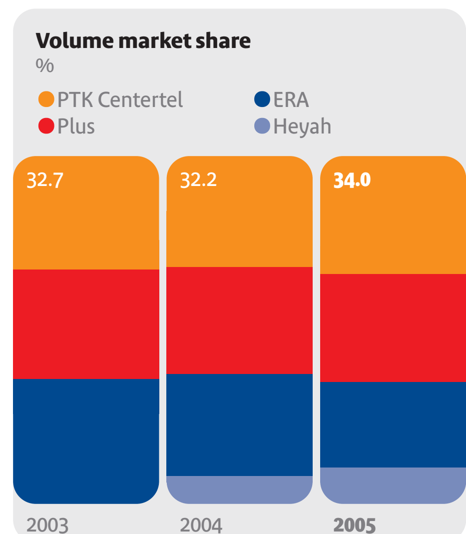
PTK's pre-paid customer base expanded by almost 1.7 mn, and the post-paid by over 800,000. As a result PTK strengthened its overall No.2 market share position in 2005.

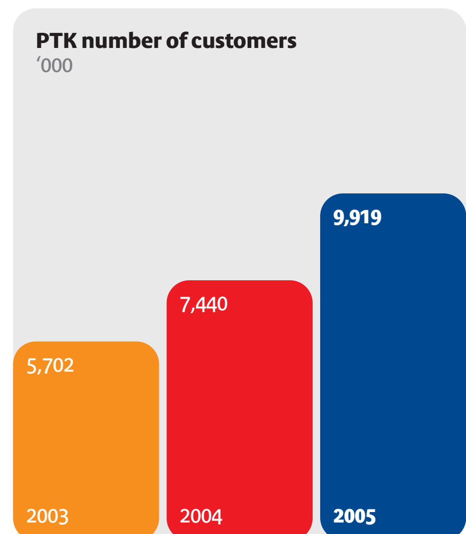
We are broadly satisfied with our post-paid performance in 2005: growth was stronger than in the segment as a whole, and we improved on our 2004 performance.

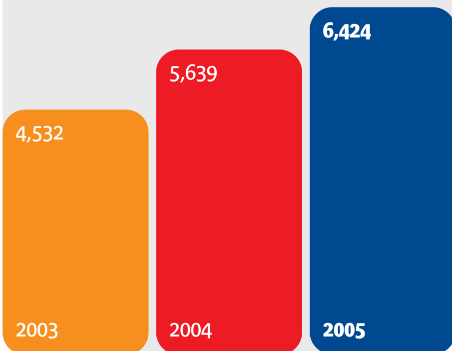
In 2006, we aim to maintain our leading position in terms of market net additions; and to become number one in value market share by 2007. Our recent success in the business market is very encouraging.

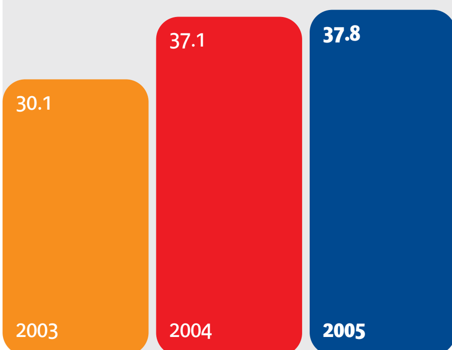
Overall, our operational performance in 2005 was our strongest for some years, and we are particularly proud to have achieved it without compromising our financial performance. We were able to record aggressive revenue growth while investing significantly in our network infrastructure (including EDGE and UMTS).

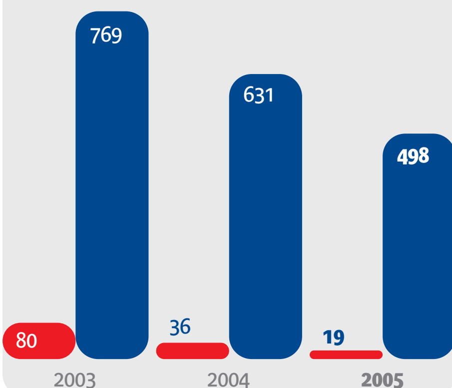
In the second half of 2005 TP established a strong platform for development as an integrated operator, by completing the rebranding of the mobile business to Orange, and acquiring the 34% remaining stake of PTK Centertel.











* Ratio includes effect of changes in accounting policies presented in note 7 of IFRS.

Orange re-branding

The Orange re-branding we carried out in September 2005 was invaluable in helping us to strengthen our market position. Brand launch events across the country were very well received. The new look we introduced at 1,300 stores was a major qualitative step forward in the way we present the mobile brand to the market.

This new point-of-sale design strengthens PTK's market positioning by associating us with an internationally-known brand – the first such in the Polish mobile market – which is synonymous with innovation and customer service. This, in turn, will be a valuable asset in our efforts to win high-value customers.

By the end of December, we already had 44.5% spontaneous brand awareness, while in terms of sales, we were able to achieve a better than market average mix between pre- and post-paid additions. There was also a good start for our new pre-paid Orange GO offer, launched alongside the existing POP offer.

The advent of the Orange brand in the Polish market has allowed us to enhance our focus on both younger, brand- and trend-conscious customers as well as business customers to whom the associations of the brand in terms of quality and service reliability are no less attractive.

During the fourth quarter, our subscriber base grew steadily, by 785,000 customers or 43% of the total net additions in the Polish market – clear evidence of the impact of the newly-introduced Orange brand. It was particularly gratifying that we were able to achieve these results without significantly increasing our advertising spend.

We expect to fully capitalise on the advantages the Orange brand creates in 2006 and beyond, and we are confident that our progress to date establishes a solid foundation for sustainable growth in the years ahead.

Orange is the first international mobile brand in the Polish Market.

PTK Centertel acquisition

A major watershed occurred in 2005 with TP's purchase from France Telecom of its remaining 34% stake in PTK Centertel. This was a key step in the strategic development of the TP Group as an integrated operator providing a full range of convergent services – fixed-line, mobile and Internet access.

The acquisition also allows us to further integrate and reduce costs by introducing a common customer service platform and Internet portal, as well as integrating our sales networks. These savings will contribute to enhancing the Group's overall competitiveness.

Moreover, we are already seeing the benefits of being able to cross-sell TP and PTK products through a fully integrated, shared distribution network, the value of which has been powerfully enhanced by the introduction of the Orange brand – the other key milestone in the Mobile market in 2005.

...delivering cutting-edge telecom solutions...

Mobile network development

Our focus in terms of network development in 2005 was the aggressive rollout of the nation-wide EDGE network. At the end of the year, our EDGE network covered over 75% of the Polish population, positioning us as a clear market leader in terms of broadband-enabled coverage. Our target for 2006 is to take national EDGE coverage beyond the 90% level.

Building on the efforts initiated in 2004, we also continued to roll out Wi-Fi hotspots. There were over 200 hotspots across Poland by the end of 2005, making ours the largest such network in the country. The roll-out will continue in 2006.

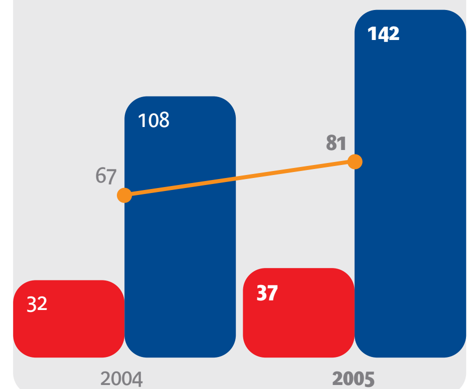
Mobile data

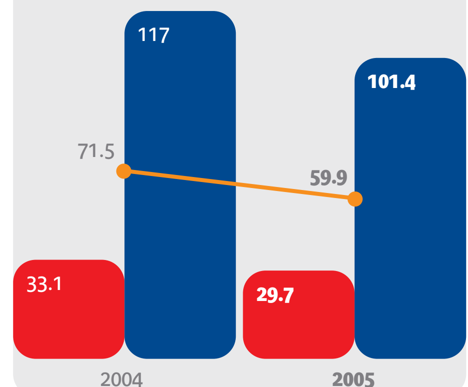
We witnessed the take-off of the mobile data solutions market in 2005, in particular in the business-to-business (B2B) segment. PTK Centertel was first to market with a reliable service, and has taken an early lead in providing innovative offers to this key segment. Our aim here is to become the recognised leader in mobile broadband solutions, to complement the Group's overall broadband leadership. In terms of broadband facilities and capacity (EDGE, Wi-Fi, UMTS), and in terms of subscriber numbers, we believe that we are already out in front.

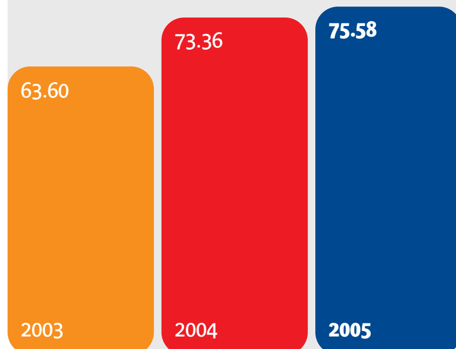
Business users will also be prime beneficiaries of PTK Centertel's rollout of a new UMTS network. In November 2005 we introduced a UMTS data transmission offer focusing mainly on B2B customers. We intend to launch the full service, including voice and video offers, in the first half of 2006.

The new Orange offer incorporates a range of the most up-to-date mobile data services, which are an increasingly important tool to attract and retain 'media-savvy' customers.

We currently offer eight live, videostreamed TV channels that are available to all Orange customers. This is the broadest mobile TV offering in the Polish market. By the end of the first quarter of 2006, it had been supplemented by the largest archive of downloadable music in the market – almost 180,000 titles in all.







Sales and Service Poland is an important part of the TP Change programme aimed at increasing service levels to our customers.

Sales and Service Poland

The key achievement in TP's Sales and Service Poland (SSP) business unit was the implementation of a new regional organisation from 1 January 2005. Five regional teams now encompass the full range of SSP's activities, from sales and installation to repairs and HR. The SSP organisation itself has achieved significant improvements in customer satisfaction by combining all customer contact functions, in both the business and mass markets, into a single entity. Common activities are now managed more consistently, and to the same benchmarks and KPIs.

This reorganisation was entirely in keeping with the stated objectives of the TP Change programme – namely, to simplify internal processes and realign our operations more closely with the needs and wishes of our customers. Indeed, SSP itself was one of the four vital components of the programme; and as with the creation of the Personal, Home and Enterprise business units, SSP offers two complementary advantages: it makes it easier for TP to foster innovation in the delivery of existing and new services; and by adopting the same organisational structure as France Telecom, it ensures that the two companies are properly aligned for the most efficient and mutually productive exchange of ideas and best practice.

Implementing the new regional structure occupied us for the first half of 2005; certain aspects of the process took longer, especially those relating to the redefinition and reallocation of technical functions between network and customer-facing functions. During the second half of the year, we brought key PTK business processes under the same organisational umbrella – for example, we now have a single management centre for fixed and mobile sales to the mass market segment.

In conjunction with these major structural refinements, we renegotiated all subcontracting agreements for maintenance and repairs with our technical support partners. The renewed agreements clearly define the basis of the partnership in order to assure the highest possible standards of service for our customers. Suppliers are now effectively in constant competition with each other.

Throughout the year, we nurtured several projects which will have a significant impact on our business in the year to come.

In the Home division, the key development was the Livebox, which is discussed under the "Home" section on pages 7 and 8.

In the Enterprise business, we launched IP-VPN for national/domestic and international companies in partnership with Equant. TP now offers a range of VPN options to Polish companies.

...and market-leading performance.

The launch of Business Everywhere was another key milestone, integrating mobile, fixed and Internet access technologies to enable business users to access their corporate intranet remotely.

The introduction of higher bandwidth (6 Mbps and 15 Mbps) broadband connection options offers both Home and Enterprise customers improved line quality and faster download times.

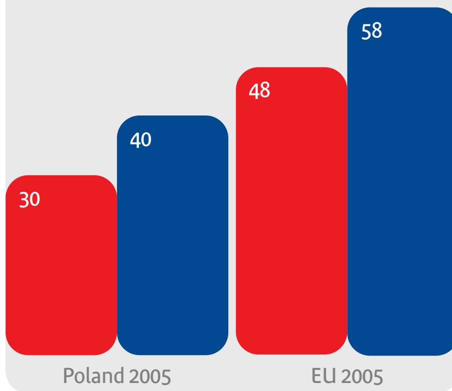
During 2005, we made substantial gains in internal efficiency. In particular, we reduced our time to market. Improving internal efficiency is a key element of the ongoing TP Change and TOP (process transformation) programmes. TP now benefits from a very strong, process-management-based organisational model, which offers significant scope to increase productivity.

The heart of TP's customer relations function is the CRM system. Two dedicated lines – TP Blue Line 9393 for residential, and TP Business Blue Line 9330 for business – enable customers across Poland to deal with virtually all service-related issues over the phone. For example, they can get information about the company's services, place orders, change tariff plans, submit complaints, report faults and get information about their account and its balance. Alternatively, customers can submit complaints, report faults and notify the company of changes of address via the TP website.

The CRM platform's performance in terms of call availability is now in line with Western European industry benchmarks. The CRM system has met its main performance targets, and the overall customer satisfaction ratio to stand at 61.5% by the end of 2005. The second half of the year saw the intensification of efforts to add new functionality to the TP Business Blue Line, to enable business customers to check their payment balance, last billing and invoice, as well as services activated for a given number.

At the same time, it supports our renewed focus on internal mobility – redirecting human resources to bring TP people closer to the customer. There is still work to be done in integrating all Group products and services into the Blue Line customer relationship management system, and we need to improve our culture of speed and responsiveness in the field. In general terms, however, we can be proud of the steady increase in customer satisfaction indices during 2005.

The 'Strategic Scorecard' introduced in 2005 is increasingly used across the organisation, and will be a valuable tool in helping us to measure further improvement against the key benchmarks we have developed within and across all SSP operating regions.



Network and IT improvements make life easier for TP's customers, as well as improving internal efficiency.

Networks, Carriers and IT

In the Networks, Carriers and IT division, our priority in 2005 was to enhance access by improving our network infrastructure. The success of our efforts is reflected in the increase in ADSL customers (up to 1.1 million ADSL) and in IP traffic (up by 85%, principally through the higher volume of data transmission, especially in the Enterprise segment). This latter statistic is particularly important, since in general terms, the more IP a network can carry, the closer it is to 'next generation' status.

We now operate the largest data centre in Poland at Łódź, which alone represents almost half of the total TP data centre capacity. We plan to offer this capacity to Enterprise customers as well as continuing to use it for internal and back-up security purposes. The transfer of the bulk of PTK Centertel's data to the Łódź facility in 1H 2006 is the first step in an ongoing initiative to centralise the Group's data centres.

TP network is being developed also to be in line with the schedule of government requirements. A national emergency call system (number 112) was introduced in co-operation with Health Care, Police and Fire Brigades. A new national numbering plan for Poland was implemented on 5 December 2005, in accordance with the stipulations of the Telecom Law. The new system creates additional numbering capacity to accommodate new customers and new technologies.

Billing was another area in which we achieved significant efficiency improvements, reducing the time it takes to process and deliver a customer's bill by around 30%.

As part of the implementation of the national Sales and Service Poland operating structure, we transferred 'last mile' support personnel out of the Networks function and into the customer-facing organisation, in order to improve customer satisfaction by increasing service activation efficiency. Network people are now much closer to the customer, in line with the overall Group mission.

Leaner management in field operations and the renegotiation of supplier contracts for last mile maintenance and repairs contributed to the reduced cost of network maintenance.

Going forward, we do not expect network maintenance capex to be very high. On 29 December we completed the digitalisation of the Polish fixed-line telecom infrastructure. As a result, we have the most modern TDM switch infrastructure in Europe. Further network investment, apart from access, will be driven by increasing IP traffic capacity.

Setting the pace in the new market...

Strategy, 2006 to 2008

The first technology revolution in the domain of telecommunications was the shift from analogue to digital. Today, we are seeing a second such revolution, driven by all the possibilities offered by the internet protocol.

Having successfully completed a far-reaching process of financial and operational restructuring, the TP Group is in a strong position to take on the challenges presented by this second technology revolution.

We have therefore devised a comprehensive strategic roadmap for the years 2006 to 2008, the key features of which are set out below. All the key elements are now in place to execute this successfully – not least, a sound investment case with a clear focus on capex for growth.

Our main strategic objectives are to retain our leadership in the telecommunication market, by focusing on forward-looking business areas (namely broadband Internet access and mobile telephony), and to maintain our position in the fixed-line segment. At the same time, we intend to prioritise customer service quality and the development of innovative services and products, as well as convergent offers.

TP Group's strategic roadmap for 2006–2008 is based on a single, overriding priority: value creation. We are determined to achieve this by developing sources of revenue, while continuing to stress maintaining Group profitability as a vital strategic focus.

First, TP will fuel growth by continuing to introduce innovative products. We will accelerate broadband access penetration and increase take-up of our Livebox and Business Everywhere offers.

Second, we will move into content aggregation (data, images and music), and offer access to this content to both fixed-line and mobile customers.

TP will grow by increasing the mass-market penetration of innovative products like Livebox.

Third, TP will adopt an opportunistic approach to implementing profitable external growth.

Achieving these strategic goals will enable the Group to meet its key objectives, which are:

- to become the leading integrated operator in Eastern and Central Europe;
- to fully develop TP Group's potential for the benefit of all stakeholders;
- to maintain a strong financial standing;
- to optimise cash flow allocation.

Each of our strategic priorities is discussed in more detail below; it is important to remember that TP remains committed to fixed and mobile, rather than one or the other.

Growth in broadband Internet access and value-added services

In order to strengthen our market position and increase revenues, we intend to expand our portfolio of services related to data transmission and other technologically advanced communication and IT solutions. In this way, we will address the decline in our fixed-line business base by selling broadband capacity in the fixed network.

It is the Group's stated ambition to popularise the Internet, making it available across Poland. In 2006 we plan to increase our broadband customer base by half a million subscribers, to over 1.6 million.

In the Home segment, by leveraging innovative Livebox features, we will introduce new offers, based on simplicity and modularity, which will allow our customers to "personalise" their ADSL services and to enrich their Internet access with VoIP, TV and video-telephony, step by step and at very attractive prices.

In the Enterprise segment, we will continue to introduce more and more convergent offers, tailored to customer needs on the basis of IP-VPN technology and the Business Everywhere concept.

Since the Internet and value-added services will be TP Group's growth engines in 2006–2008, the development of user-friendly, easily available and competitive offers remains our top priority.

Mobile business growth

One of the most important elements of our new strategy is to win the leading position in the Polish mobile market, which continues to grow rapidly. We estimate that this growth will be sustained over the next three years, with penetration of mobile services (76.6% in 2005) probably reaching nearly 100% in 2008.

In 2005 PTK Centertel was the leading player in the mobile Internet access segment. PTK was equally the first mobile operator in Poland to introduce a global brand. We expect this to be a key factor in driving subscriber base and revenue growth.

We are particularly well placed to target media-savvy customers with an enhanced offer of mobile multimedia content, including eight live TV channels. Expanding our offer of music downloads will be a core initiative in 2006, to ensure that PTK benefits from the most comprehensive and attractive music/TV/content/portal offer.

In 2006 we intend to exceed our year-end target of 11.5 million mobile customers. We also expect to increase customer revenues by developing wireless broadband and content aggregation capacity. As a result, we expect the contribution of non-voice services to PTK Centertel's total revenues to grow, and estimate that its share of aggregate ARPU will pass the 20% mark in 2006.

Based on our achievements to date, we are confident of success.

...investing in growth, investing in Poland's future.

Marketing, sales and customer service
Increasing customer satisfaction and loyalty remains a key element of our operational strategy. We will continue our efforts to introduce new customer communication channels and to leverage our entire distribution network to ensure better and more friendly customer relations.

In addition, we are working on strategic marketing, including a variety of new products for launch in the next three years, utilising both new and existing technologies.

Integrated services
In response to growing customer expectations, the TP Group intends to meet all the telecommunication needs of its customers, by adding new integrated telecommunication solutions and service packages to its portfolio.

The re-branding of our mobile arm and the acquisition of the remaining interest in PTK Centertel puts the Group in a very strong position to capitalise on its integrated operator strategy. Looking ahead, we may also consider extending our Enterprise offer to incorporate IT competencies.

Capital expenditures and financial performance
Between 2006 and 2008 the Group will focus on maintaining profitability by continuing tight cost control, reducing non-productive operating expenditure, and rebalancing capital expenditures in favour of growth businesses.

VoIP, TV over DSL, and other aspects of TP's emerging next-generation network will require significant investment effort, especially in 2006 and 2007.

We have identified four principal capex categories:
1. investment in fixed and mobile broadband networks (ADSL access, EDGE/UMTS capacity);
2. the development of innovative services;
3. increasing GSM mobile traffic capacity; and
4. increasing access in order to accelerate broadband penetrations.

In the mobile business, we believe that capex will remain relatively stable over the next three years. While continued investment is required to improve network capacity and coverage in support of our mobile broadband strategy, the bulk of EDGE investment was made in 2004-05; what remains is relatively marginal. Our core broadband investment from 2006 onwards will be in rolling out our UMTS network.

Roadmap of innovation and convergent service

Main innovative products and convergent offers during 2006:

Q1 2006: VoIP
Q2 2006: TV over DSL
Q3 2006: Video on Demand

For convergence:

Q1 2006: Business Everywhere – full commercial launch
Q2 2006: Common Voicemail (single voicemail for mobile and fixed)
Q3 2006: Common Service Portal with one address book for mobile and fixed

We are investing in the future of TP Group, and for the next generation of consumers.

An equal priority for the Group's financial development will be strong cash flow generation, which remains the Management Board's primary concern. Good operational and financial results will facilitate meeting the requirements of the increasingly competitive market, and will enhance TP's value to shareholders.

Performance monitoring

We will continue to measure our strategic progress through three 'strategic scorecard' KPIs followed at Group level: overall product time-to-market, innovation time-to-market, and TP's overall 'innovative image'. Targets have been identified for all three measures.

Our people

Our strategy cannot be implemented without the support of committed employees. Our employees bring strategies to life, deliver reliable customer service and through innovative efforts create the convergence technology that will drive our future. I wish to thank them all for their hard work and dedication to TP Group in 2005 and in the years to come.

Alain Carlotti
Executive Vice-President of the Board
31 March 2006

A solid financial platform...

Benoît Mérel
Chief Financial Officer

Introduction

2005 saw TP complete a period of focus on the balance sheet and financial restructuring. Our key strategic goals during this process were to improve profitability, maximise cash flow and rationalise capital expenditure, particularly in the fixed-line segment.

In 2005, Group EBITDA reached 43.6%, while our capex optimisation programme allowed us to reduce our capex-to-sales ratio to 16.6%. Most importantly, we met our primary objective of generating strong free cash flow before financing. By the end of 2005, excluding the purchase of non-current financial assets (including acquisition of a 34% stake in PTK), TP Group cash flow amounted to over PLN 4 billion, and we had a 30% gearing ratio. At the same time TP Group had unused credit facilities amounting to PLN 2.2 billion. Thus the Company maintained a very strong level of liquidity and financial stability.

Recognising TP Group's financial achievements, in 2005 all three Rating Agencies decided to upgrade the Company's corporate rating, Moody's from Baa2 to Baa1 with a Stable outlook, and both Standard & Poor's Ratings Services and Fitch Rating from BBB to BBB+ with a Stable outlook.

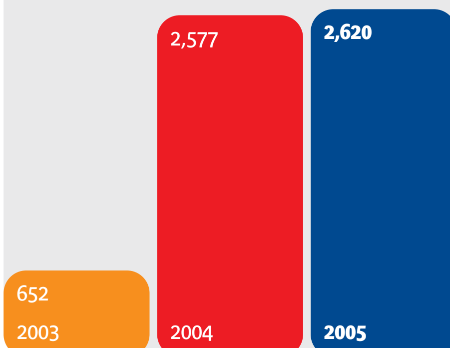
2005 Results: Overview

Despite top line pressure (full–year revenue fell by 1% compared to 2004) we have continued to make steady progress in transforming the Group's revenue base to focus on growth areas and respond effectively to market trends. The Data and Mobile segments, which rose by 16.6% and 15.6% respectively, are our key growth drivers, while access and interconnection fees help us to slow down the decline in fixed voice revenues, which represented less than a third of total Group revenue in 2005. Other revenue lines also delivered good results, reflecting the value of TP's complete telecoms portfolio.

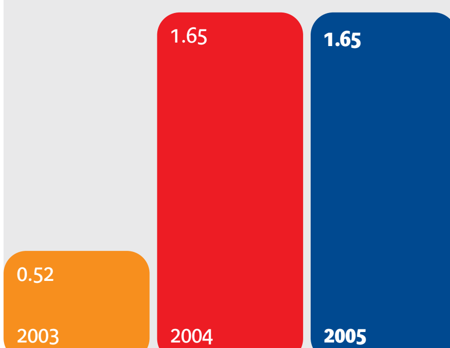
Thanks to strict cost control, we were able to maintain our EBITDA margin at a high level of 43.6% despite higher provisions for litigation and other claims created in the fourth quarter 2005.

Net profit*
PLN mn

*before minority interest



Earnings per share
PLN



In 2005 an opex reduction of PLN 181 million (or 1.2%) almost compensated for the revenue decline.

We achieved a significant cost reduction in three principle areas:

– Labour costs were down PLN 206 million due to headcount reduction, mainly in the fixed-line business, and the changes in the Collective Bargaining Agreement as negotiated by the Company in the third quarter 2005;
– Third-party services, down PLN 85 million, resulting primarily from the Company's efforts to reduce external services such as consulting and IT services;
– Goods purchased for resale were down PLN 142 million. This is the consequence of lower handset costs.

In 2005 TP Group completed a project of verification of accounting for its property, plant and equipment. Consequently the depreciation charge starting from 1 January 2005 was calculated based on the useful lives of assets. As a result of the project depreciation charges were lower by PLN 143 million for the year 2005.

Capital expenditure

Group capital expenditure decreased to PLN 3 billion in 2005 – a reduction of 7.4%. The Group's capex-to-sales ratio was 16.6%.

Fixed Line capital expenditures decreased by over 18% year-on-year, while the capex-to-sales ratio in the segment stood at 14.5%, which is more in line with industry benchmarks.

In the Mobile business, our commitment to investing in 3G technologies led to an increase in capex to around PLN 1.2 billion, compared to PLN 1.1 billion in 2004.

Overall, this reflects the "rebalancing" of capex towards growth areas – principally the Mobile segment.

Group cash flow

Cash flow from operating activities remained at a high level of over PLN 8 billion.

Excluding the PTK and WP acquisitions, and including net interest expenses, we generated positive free cash flow before financing of over PLN 4 billion in 2005.

Cash flow generation will remain a key priority in 2006 and beyond.

...a well managed, solid investment.

Group debt structure

Net debt repayments in 2005 amounted to PLN 787 million; the cash position decreased by PLN 1.3 billion to just over PLN 1.7 billion, reflecting the consideration paid for acquisition of a 34% stake in PTK.

At the end of 2005, taking into account the PTK Centertel acquisition, our net gearing ratio stood at 30%, compared to 18% at the end of the third quarter.

We continue to focus on optimising our debt structure and reducing financial costs. In February 2006, we concluded a revolving loan agreement for a total of PLN 2.5 billion, on attractive terms, in order to increase duration of our debt portfolio and improve current liquidity, following a €500 million bond redemption in March 2006.

Internal efficiency

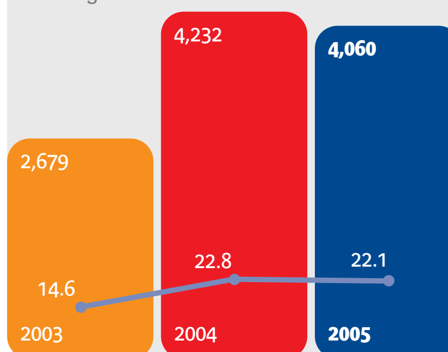
A major achievement in 2005 was the strengthening of our internal reporting processes. We now capture trends very quickly, which help us to prepare more accurate budget forecasts and establish close linkage between our capex budget and revenue.

Building on our actions in 2004, we met formally with all divisional heads to secure their commitment to taking full responsibility for P&L performance in their respective areas. In tandem, we have improved our KPI monitoring processes and introduced 'Strategic Scorecards' to enhance and simplify performance assessment.

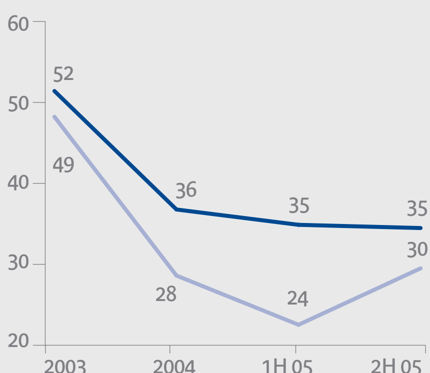
Of course, excellence in external reporting remains a fundamental priority. TP has established a programme to review, assess and evaluate its internal control in financial reporting processes. This work is carried out in parallel with the France Telecom programme to secure compliance with the Sarbanes-Oxley Act.

FCF before financing and FCF margin*
PLN mn

* Cash flow from operating activities – purchase of tangible and intangible assets plus interest paid net

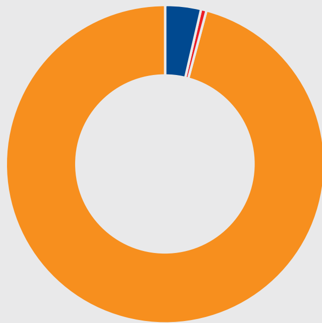


Gearing and net gearing ratios
%



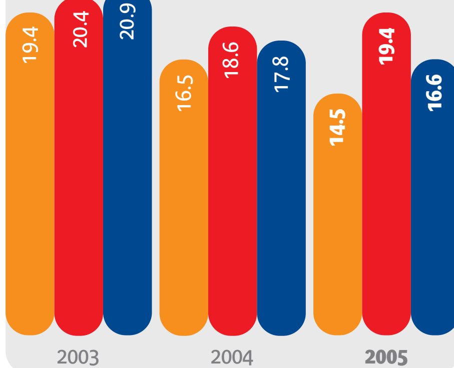
Debt structure after hedging
%

EUR	3.9%
USD	0.6%
PLN	95.6%



TP Group Capex to Sales
%

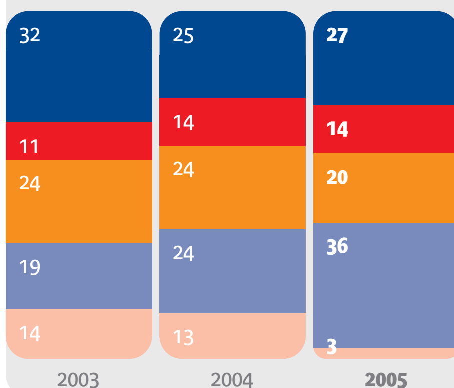
TP Group Mobile Fixed



2003 2004 **2005**

TP Group Capex breakdown %

Fixed Voice IT Group Other
Fixed Data Mobile Network



2003 2004 **2005**

Risk management and Insurance

We continued to refine our monitoring of significant and material risk, whether legal, regulatory, environmental or operational.

At present, risk management is mostly co-ordinated by Internal Audit. Going forward however the Management Board is considering a full implementation of the ERM (Enterprise Risk Management) approach.

As a result, TP today is an organisation that is more reliable and more accountable than ever before.

Outlook

TP Group's new strategic roadmap is based on the single overriding principle of value creation for shareholders. We are determined to increase the company's value to shareholders by developing new and alternative sources of revenue while maintaining profitability and optimising operating expenditure. Maintaining TP Group profitability is, and will remain, one of the most important cornerstones of TP strategy.

Between 2006 and 2008 the Group will focus on maintaining strong financial standing through rigorous cost control and reducing non-productive operating expenditure, as well as rebalancing capital expenditures in favour of growth businesses.

An equal priority for the Group's financial development will be strong cash flow generation, which remains the Management Board's primary concern. Good operational and financial results will make it easier for us to meet the requirements of an increasingly competitive market.

Benoît Mérel
Chief Financial Officer
31 March 2006

Corporate Social Responsibility (CSR)

TP's Strategic Rule is to Get Closer
This means getting closer to both customers and other stakeholders (local communities, employees, suppliers, investors, environment). Corporate responsibility remains at the core of our values.

In 2005, TP became a Strategic Partner of the Responsible Business Forum, which is the national partner of CSR Europe, an organisation promoting the concept of responsible business in Europe. In addition, PTK Centertel became a Strategic Partner and ORE S.A. a Partner of the Responsible Business Forum.

TP and Local Communities
TP organises its own social programmes as well as nationwide charity campaigns. In addition, every year, TP contributes a portion of its profits to a special grant fund; in 2005 this was PLN 12 million. The TP Group's long-term commitment to social initiatives led to the establishment of the TP Group Foundation in September 2005.

In 2005, TP was awarded the 'Benefactor of the Year' title in a competition organised by the Academy for Philanthropy Promotion in the category 'Strategic Corporate Social Responsibility Programmes.' Some examples of TP's charitable and social endeavours are given below.

Charity projects
In 2003 TP launched its own charity programme called 'Telekomunikacja Polska for Children'. The programme aims to support young people in the field of health protection and modern education, using state-of-the-art telecommunication techniques.

'Telekomunikacja Polska for Children' includes the 'Call Mum' project which TP started in 2003 to give sick children access to telephones in their hospital wards. So far, over 1,000 colourful, child-friendly phones have been installed, in almost every child's ward in Poland.

In 2005, TP provided children in hospitals with over 220,000 free 'TP for Children' phone cards, which allowed them to talk to their families for over 8 million minutes in total.

Also, as part of the pilot stage of TP's 'Internet Smile' project, Internet kiosks were established in five children's hospitals.

Charity on the phone
TP has dedicated special telephone numbers for use by charity campaigns. Telephone lines are made available to a variety of organisations, enabling them to raise funds. In addition, toll-free hotlines are provided for use by national charity campaigns and to support information centres dealing with natural disasters.

Educational projects – our contribution to the development of the information society
The idea lying behind the programme is a firm conviction that broadband Internet access is a crucial tool in eliminating barriers to regional development and providing equal opportunities to all young people. The 'TP Education with Internet' programme offers promotional Internet access services to primary and junior/senior secondary schools, as well as teacher training. In the school year 2004/2005, schools paid just PLN 1 (net of VAT) monthly for the high-end option of TP's Internet access service.

The programme is carried out in co-operation with the Ministry of National Education and Sport, which facilitates nationwide co-ordination of IT educational initiatives. By 31 January 2006, over 9,500 schools with over 3 million pupils had signed up for the TP Education with Internet programme.

Teacher training
The TP Education with Internet programme includes teacher training. The aim of the programme is to encourage teachers to use multimedia tools in the classroom.

TP and the environment
Since 1998, TP has implemented procedures aimed at limiting the environmental impact of its activities and achieving compliance with Polish environmental regulations. In 2002 and 2003, an environmental audit confirmed compliance with Polish laws and highlighted the Company's achievements in limiting its environmental impact. Environmental monitoring teams were established within the TP Group to control the Group's infrastructure and equipment, monitor emission levels and provide training in environmental protection. In addition, the teams monitor legislation and assure compliance with environmental regulations.

TP and dialogue with consumer organisations
TP builds its external relations on the basis of dialogue and holds regular meetings of TP representatives with consumer organisations and spokespeople.

TP has also appointed a Spokesperson for TP Customers, whose role is to represent customers interests. The Spokesperson identifies areas that are subject to recurrent complaints and initiates improvement programmes.

TP and Polish business
Entrepreneurship Academy
In 2003, TP inaugurated the first series of free workshops called the Entrepreneurship Academy. They aim to provide professional advice to managers of small to medium size Polish enterprises in the areas of technology, management, Human Resources, and marketing. The underlying principle is educating entrepreneurs in how running and growing their businesses will create demand for modern telecommunication and IT solutions. Approximately 3,000 entrepreneurs had been trained in the Entrepreneurship Academy workshops by the end of 2005.

Throughout the year TP ran a number of CSR programmes in line with our philosophy of "Getting Closer" to the consumer.

The TP Employee Retirement Plan covered over 22,000 people at the end of 2005.

TP and suppliers

TP plays an active role in the FT Group supplier evaluation programme, QREDIC. The programme includes the supplier evaluation process, including suppliers' activities related to business ethics and environmental protection. The programme aims at better co-operation between FT Group companies, and usually results in an action plan to enhance such co-operation.

Code of Ethics

Please refer to the 'Corporate Governance' Section for details.

TP and employees

Health and safety

TP is conscientious in observing all of the legal occupational safety and health duties which arise from its status as an employer. Employees regularly undertake safety and health training. The number of work-related accidents remains low. There were no fatal accidents in 2005.

Equal opportunities

Our goal is for the TP Group to be a fair employer which does not discriminate on grounds of disability, nationality or gender. About 46% of all employees at TP are women, as are 37% of all managers.

Skills development

TP runs many training programmes which help our employees advance their careers, including:

Talent Review

The programme aims at comprehensive preparation of managers for the pursuit of business objectives of both TP and the entire FT Group. The most talented employees identified in the programme will have the opportunity for further development, e.g. through financing of their MBA studies.

E-learning and Development Product Library (DPL)

Electronic training delivered directly to one's own workstation (PC) plays an increasingly important role in TP personnel education. The Development Product Library, integrated with the e-learning platform, offers an opportunity to develop and improve skills, as well as acquire additional knowledge.

Internal mobility

The Professional Mobility Programme was launched in 2004 as a long-term corporate initiative to provide adequate human resources for the pursuit of the Company's strategic business objectives.

As part of the Professional Mobility Programme, TP managers are encouraged to use the internal labour market as the preferred source of recruitment.

568 people in 2004 and almost 3,900 in 2005 (approximately 14% of the Company's workforce) joined the Professional Mobility Programme.

Employee Retirement Plan

The TP Employee Retirement Plan (TP ERP) is an organised group retirement savings plan. It is part of the third pillar of the social insurance system and the employee premiums are paid by the employer. The premium depends on the basic salary. At the end of 2005, over 22,000 people were covered by the plan and had their basic premiums paid into their accounts; an additional premium was declared by 2,700 participants in TP ERP. The value of the TP ERP unit increased by 14.8% in 2005.

Central Welfare Fund

The purpose of the Fund is to provide assistance to TP employees and pensioners, and their families who may be facing difficulties as a result of an accident (e.g. fire, flood, serious illness).

Corporate Governance summary

The governance framework

The framework of TP Group's corporate governance is set by the provisions of Polish law, the company's articles of association, and the regulations of the Warsaw Stock Exchange, as well as the London Stock Exchange (where the company's GDRs are quoted and traded). In February 2003, TP Group began a 12-month process to develop a Corporate Governance Charter. This is the most effective way of organising TP Group's governance system and ensuring that the long-term interests of the company and its shareholders are properly aligned. Initially, an external corporate governance audit was conducted to reveal how TP's practices were viewed by investors and financial regulators. Interviews were then conducted with members of the TP Supervisory Board to test the findings of the audit, and a Corporate Governance Steering Group was formed to oversee the drafting of the Charter. The draft Charter was then reviewed by both the TP Supervisory Board and the Management Board. In addition, the institutional investor community, including Polish, European and US institutions also provided feedback on the draft. The revisions recommended by the institutions were reviewed by the Corporate Governance Steering Group, and the amended Charter was then passed to the TP Supervisory Board for final approval. It was formally adopted on 12 March 2004.

Key functions of the Corporate Governance Charter

- The Statement of Purpose enshrines shareholder value as the overriding purpose of TP, but also clearly identifies how that objective is to be pursued. It is consistent with TP's mission, vision and corporate values statement.
- The Management Responsibilities cover key areas of concern and risk to the Group: internal control and risk management; information policies, systems and procedures; ethical framework and policies; and transactions with shareholders.
- The Governance Process Principles emphasises the role of the Management Board in preparing and validating information for the Supervisory Board and various committees, including the Audit Committee.

1 The role of shareholders

TP encourages shareholders to play an active role in the company's corporate governance.

Indeed, shareholder consent is required for key decisions, including: the review and approval of the financial statements and Management Board Report on Activities; the election of the members of the Supervisory Board (and, if necessary, their dismissal); amendments to the articles of association; the raising of capital; and the buy-back of shares.

At the company's General Meetings, each share in TP entitles its owner to one vote. Holders of the company's GDRs are also encouraged to submit their voting instructions to the company's Depository Bank. In addition to their participation in General Meetings, members of the company's Management Board and senior executives engage in active dialogue with the company's shareholders. To ensure that investors receive a balanced view of the company's performance, Management Board members – led by the Executive Vice-President of the Management Board and the Chief Financial Officer – also make regular presentations to institutional investors and representatives of the domestic and international financial community.

2 The Supervisory Board

As of 31 December 2005, the Supervisory Board comprises thirteen members. At present, TP has four independent members on the Supervisory Board, Mr Andrew Seton, Mr Timothy Boatman, Mr Tadeusz Han and Mr Krzysztof J. Ners. The term of office of each member of the Supervisory Board is three years, and their remuneration is determined by the General Meeting of Shareholders. The Supervisory Board meets at least once a quarter and is responsible for the appointment and remuneration of the members of the Management Board, the appointment of the company's independent auditors, and the supervision of the company's business. As part of this process, it examines the company's strategic plan and annual budget and monitors the company's operating and financial performance. In considering these matters, the Board takes into account the social, environmental and ethical considerations that relate to TP Group's businesses.

The work of the Supervisory Board is co-ordinated by the Board Chairman, with the assistance of the Board Secretary; and the responsibilities and obligations of the Board, together with its rules of procedure, are defined in a formal statement of the Board's role. Although the Board performs its tasks collectively, it delegates some of the work. The persons and committees to whom these tasks are delegated are described in further paragraphs.

The Supervisory Board assessment of the Group's situation in 2005 appears on pages 28 and 29.

The Audit Committee is a Committee of the Supervisory Board and reviews reports from the Chief Financial Officer and internal and external auditors. The Audit Committee is chaired by Mr. Timothy Boatman, an independent member of the Supervisory Board. He has relevant and up to date financial experience. The Audit Committee report appears on pages 31 and 32 of this annual report.

The Remuneration Committee's task is to advise the Supervisory Board and Management Board on the general remuneration policy of TP Group, determining the conditions of employment and remuneration (including the setting of objectives) of the Members of Management Board and giving recommendations to the Supervisory Board regarding salaries and the amounts of bonuses for the members of the Management Board. The Remuneration Committee met seven times in 2005. The Committee is chaired by Mr. Andrew Seton – an independent member of the Supervisory Board. The Committee report appears on page 30 of this annual report.

The Strategy Committee was created in 2005. The task of the Committee includes:

- giving its opinion and recommendation to the Supervisory Board on the strategic plans put forward by the Management Board and any further suggestions made by the Supervisory Board regarding such strategic plan(s), and in particular on the main strategic options involved;
- consulting on all strategic projects related to the development of TP Group, the monitoring of the evolution of industrial partnerships within TP Group and projects involving strategic agreements for TP Group. It then reports and makes recommendations on each of these projects to the Supervisory Board.

In particular, the Committee is invited to consider projects such as:

- strategic agreements, alliances, and technological and industrial co-operation agreements, including aspects of the strategic partnership between France Telecom and TP Group;
- significant acquisitions and sales of assets.

The Committee is chaired by Mr. Jean-Paul Cottet.

3 The Management Board

The current Management Board is composed of seven members. The scope of the Board's remit includes the management of all aspects of the company's affairs, with the exception of those matters which are stipulated by the Polish Commercial Code and the company's Articles of Association as being within the competence of the General Meeting of Shareholders or the Supervisory Board.

The responsibilities and obligations of the Board, together with its rules of procedure, are defined in a formal statement of the Board's role. The members of the Board share collective responsibility for managing the company, but the work of the Board is co-ordinated by its President and the Executive Vice-President of the Board.

4 Internal control and risk management

The Supervisory Board is responsible for reviewing the effectiveness of the Group's system of internal control and risk management established by the Management Board. Such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material mis-statement or loss. The key elements of this system include the following procedures:

- An internal audit function, which reports both to the Management Board and the Audit Committee. The external auditors also report to the Audit Committee on control weaknesses which they find during their financial statements audit. The recommendations arising from the review of risk management procedures and systems of internal controls are successively implemented.
- The company's internal auditors conduct ongoing assessments of the quality of risk management and control. As part of this process, they maintain a Risk Map which identifies and classifies the Group's financial and non-financial risks. This Map was developed as a self-assessment exercise, but also includes findings from the risk assessment project carried out with the support of external experts.
- Procedures were implemented in order to identify, report and monitor significant risks (i.e. legal, regulatory, environmental and operational) effectively on an ongoing basis. It provides a framework for the internal audit department's ongoing risk-controlling activities.

In addition, TP Group insurance was developed, in order to protect the Company's assets and to mitigate or eliminate insurable risk. As well as implementing an insurance Policy for the Group, together with FT, we have developed individual policies for the whole Group (including a Civil Liability policy and a Property Damage and Business Interruption policy).

Key developments in 2005

Further work was done to improve the system of risk identification and assessment. As a result of this work, the Group has a detailed, on-going risk management process, for identifying, evaluating and managing the significant risks it faces. The detailed risk documentation which is the basis for final risk assessment and valuation is prepared quarterly by risk owners.

In 2005, TP Group continued to define and document internal control processes relating to financial reporting. Compliance with the documented processes has been assessed by means of tests of a sample of transactions. This process of assessment will be continued in 2006 to cover all critical internal control procedures as well as environmental controls.

Following the implementation of insurance policies in 2004 to limit the Group's exposure to civil liability and property damage claims, and to protect the Group against business interruption, steps were taken to increase the security of the network infrastructure by introducing full back-up capacity at the main Łódź data centre.

In 2005, TP Internal Audit Department conducted cyclical audits of the Group's transactions with related parties that were reviewed by independent directors on the Audit Committee. The company has developed procedures for identifying, approving and accepting such transactions.

Disclosure

TP Group is diligent in its approach to reporting financial results and its ongoing communication with the Polish and international investment community, as well as fulfilling its disclosure obligations. In 2003/2004, the Disclosure Committee Statute was drafted, and the Committee began its activities in February 2004. Its role is to oversee public disclosures made by TP Group, ensuring that they are timely, exact, transparent, complete, and presented in accordance with all relevant laws, applicable regulations and recognised practices, as well as being properly representative of the financial and operational condition of the Group.

In 2005 the TP Group Disclosure Committee met six times and worked on the following:

- development and adoption of the TP Group Manual For The Disclosure And Use Of Information;
- evaluation and approval of the statutory financial reports (quarterly, half-year, full year);
- evaluation and acceptance of quarterly investors' presentations.

In 2005 TP published 222 current reports (as well as quarterly and half-year statements of results) that were sent to the Warsaw and London Stock Exchanges. Moreover, in the field of Investor Relations activities, TP Group held two non-transaction-related roadshows with investors and some 100 meetings with investors and analysts.

Code of Ethics

In April 2004, the TP Management Board decided to develop and implement within the Group the Code of Ethics, which was adopted in 2005. The TP Group's key values are closeness, solidarity and innovativeness. Key principles set out by the Code include:

- abiding by ethical principles in business activities;
- fair competition;
- employee care;
- high corporate governance and management standards;
- absolute resistance to corruption;
- apolitical stance;
- environmental care.

Based on results of the Fraud Diagnostic Project launched in 2005, the processes and policies for the prevention and reporting of potential or actual fraud, including a "whistleblowers' charter", will be formalised by the Company in 2006.

Assessment of the Group's situation in 2005 prepared by TP S.A. Supervisory Board

This report is the Supervisory Board evaluation of TP S.A. performance in 2005 in accordance with clause 18 of the Best Practices code, introduced by the Warsaw Stock Exchange and adopted by the Company. The assessment is based on the Company's 2005 Financial Results, as well as, on information obtained by the Supervisory Board during its statutory tasks.

Throughout 2005 the Supervisory Board focused on the following issues:

- the Group's present and future image with its customers;
- the Group's financial results and performance;
- the Group's internal controls and approach to risk management;
- the Group's relations with the investor community;
- the Group's position in the Polish regulatory environment;
- the Group's strategy for future success in an increasingly competitive world.

TP Group operational review
During the year, several major initiatives were proposed and/or implemented by management, in particular:

1. the TP Change programme;
2. re-branding of Idea to Orange;
3. purchase of the remaining stake in PTK Centertel.

The Supervisory Board, through the work of its committees and independent members (who now number four in total following the 2005 Annual Meeting), was actively engaged in the process of evaluation of some of the most important initiatives, having in mind the interests of all the Group's shareholders. In addition, it maintained oversight of the Group's operational and financial goals through management reporting at its quarterly meetings and was able, through the Audit Committee, to observe and challenge the control, risk management and budgeting functions performed by management.

In 2005 despite a solid market position in the fixed-line segment in the face of ongoing market liberalisation, TP's fixed-line revenues came under pressure due to increasing fixed-to-mobile substitution, the loss of market share and decrease in call prices. The Supervisory Board's concern about these key threats and its wish to ensure ever stronger commitment to budget goals, enhance internal controls and improve market guidance, influenced its decision to strengthen the management team at the end of the year. In particular, the Supervisory Board sought a stronger commitment to budgeted targets and control processes throughout the company.

At the same time, the Supervisory Board noted that TP's data segment, including Internet access, is becoming increasingly important to the company's fixed-line business, while the share of the mobile segment in TP Group's revenue continued to increase.

The implementation of the TP Change programme
Throughout 2005 the TP Group continued its implementation of the TP Change programme, an initiative to realign the Group's operations according to customer-centric principles, creating three new divisions: Home (residential fixed-line voice and Internet access services), Enterprise (business fixed-line, mobile and data services and key corporate accounts) and Sales and Services (in which all customer facing functions were integrated). In addition, TP started to integrate its Networks and IT activities into a single business unit.

The Supervisory Board considers these actions, through their offer of the benefits of operational convergence, as important steps that strengthen further the Group's commitment to its customers.

Fixed-line
The Supervisory Board noted with satisfaction that TP successfully implemented several retention and loyalty programmes in 2005. TP Group continued to migrate variable traffic revenue to stable access revenue and also achieved a total of more than 3.5 million New Tariff Plan activated customers. Furthermore, the Supervisory Board noted that the Group is migrating its Enterprise customer base to higher monthly fees and value-added services.

The Group devoted substantial time and resources to developing the Polish broadband market – for example, over 80% of TP's wire lines are now ADSL enabled. The share of this segment in the Group's total revenue increased in 2005 by 71% compared to 2004.

In 2005 TP successfully stabilised the CRM system, a major concern of the Supervisory Board in 2004, and has monitored by it on a regular basis since. In 2005 the main performance targets for the CRM system were attained and the general satisfaction ratio grew to 61.5% by the year-end, an 8.5% improvement year-on-year. At the same time, TP continued to develop its own modern retail network space, thus helping to promote a more customer-friendly image for the Group. The Supervisory Board also kept abreast of TP's launch of major initiatives aimed at development of data transmission for the business market including an IP VPN network that enables integrated data transfer (data/voice/video transmission) via single access to the network, in co-operation with EQUANT.

Mobile
The Supervisory Board monitored the development of TP's mobile business with keen interest, especially in the light of negative trends in fixed-line revenues, and with an eye on likely future convergent trends. It notes with satisfaction that in an increasingly competitive market environment, PTK Centertel remained the leading force for innovation in 2005, competing principally on the quality of its products and services and the transparency and simplicity of its tariff structures. As a result, Centertel outperformed the market in terms of revenue growth, and maintained its strong second place, in terms of subscribers, in the market overall. In 2005 PTK was also the leader in the mobile Internet access segment, introducing the UMTS network to launch 3G mobile services.

In the second half of 2005 the Supervisory Board supported TP in establishing a strong platform for development as an integrated operator. In this period, the Group:

- completed the rebranding of the mobile business to Orange with the involvement of the Audit Committee, including its independent members, taking part in an evaluation of the brand licence arrangements with the support of an external consultant;

– acquired the 34% remaining stake of PTK Centertel, with the independent Supervisory Board members taking part in the evaluation of the terms of the transaction with the support of investment banking advisors, and subsequently forming an ad hoc committee to deliver the Supervisory Board's vote on the transaction.

Rebranding of Idea to Orange

The Supervisory Board believes there is now evidence that the Orange re-branding carried out in September 2005 truly helped PTK Centertel to strengthen its market position. Brand launch events across the country appear to have been well received by PTK subscribers, while the new look introduced at 1,300 stores is a major qualitative step forward. By the end of December, Orange had 44.5% spontaneous brand awareness independently confirmed, while in terms of sales, PTK was able to achieve a healthier mix of pre- and post-paid additions. During the fourth quarter, the PTK subscriber base grew steadily, by 785,000 customers or 41% of the total net additions in the Polish market. It was particularly gratifying that PTK was able to achieve these results without significantly increasing advertising costs.

Purchase of the remaining stake in PTK Centertel

On 26 October 2005, following a positive vote in favour of the transaction by the Supervisory Board, TP S.A. concluded an agreement with France Telecom Mobile International S.A., a wholly-owned subsidiary of France Telecom, for the purchase by TP S.A. of the 34% stake in PTK Centertel Sp. z o.o. The acquisition of 34% of Centertel, combined with the re-branding of the mobile arm into Orange, puts TP Group in a very strong position to capitalise on the Group's integrated operator strategy. TP Group is now able to fully exploit the growth potential of the wireless market in Poland and this way also further hedge against fixed-to-mobile substitution.

TP Group financial overview

Facing increasing competitive pressure and responding to targets approved by the Supervisory Board, the Group's key strategic goals in 2005 were:
– to improve profitability,
– to maximise cash flow,
– to optimise opex through rationalisation of TP's businesses,
– to optimise capex to prioritise investments with shorter payback periods and higher revenue generation,
– to promote growth areas (mobile, broadband)
– to introduce innovative offers in both mobile and fixed telephony.

As a result of operational initiatives and reinforced financial discipline, which reduced the fixed-line cost-base and the Group's capex level, TP Group generated strong free cash flow. Two major transactions were completed: the purchase of the remaining 34.0% of PTK for PLN 4.9 billion (of which PLN 1 billion was financed by a non-cash loan granted by France Telecom S.A.) and the purchase of Wirtualna Polska (WP) for PLN 0.2 billion. Excluding these acquisitions, TP Group's free cash flow before financing amounts to PLN 4.1 billion. Since 2002, the Supervisory Board notes that the Group has managed to optimise its capital structure and improve its credit profile: net debt was reduced by nearly PLN 7 billion in that period. At December 31, 2005, the gearing ratio was 30%, a solid base from which to build the Group's new strategic development cycle. Recognising TP Group's financial achievements, in 2005 all three Rating Agencies decided to upgrade the Group's corporate rating.

At various points during the year, the Supervisory Board debated the need for a more clearly articulated shareholder return policy, in the light of TP Group's financial position, and bearing in mind that 2004 was the last year in which the dividend restrictions imposed by the privatisation agreement applied. The Supervisory Board has recommended a higher dividend than in any previous year, taking into account expected upcoming capex demands and the overall operating climate.

Conclusions and 2006 recommendations

2005 showed that the Group can respond to the demands of the marketplace with the right products and services, improving customer loyalty and satisfaction along with market share. However, the Supervisory Board believes there is still some way to go to improve TP Group's image with its customers so as to mitigate the risk of dissatisfaction. There is, moreover, scope for more efficient investment processes within the Company to ensure that capital spending is focused on the most promising growth areas. This, in turn, should create a stronger, innovative image for the Group and ensure a much greater likelihood of sustaining and increasing customer appreciation and revenues. At the same time, the Group will have to make continuing strong efforts to create a deserved and rightful position for itself in Poland's competitive environment and regulatory climate. In particular the Group should focus on:
– optimisation of operating expenses through further rationalisation of TP Group's businesses;
– optimisation of capex investments and its prioritisation based on payback period and revenue generating capabilities;
– growth areas (i.e., mobile, broadband);
– introduction of innovative and convergent services in mobile and fixed-line;
– continued customer-centric operating principles;
– efficiency of IT as a key lever for business flexibility;
– delivering a return to shareholders which is a reasonable reflection of TP's financial position and of market expectations following the post-privatisation period;
– promotion of predictable regulation according to the European Regulatory Framework and consistent with comparable benchmarks;
– financial controls and risk management measures.

Despite increased competition across all segments, as well as regulatory pressure, TP Group delivered satisfactory results in 2005. The Supervisory Board believes TP's Management Board has made reasonable efforts to attain its 2005 strategic objectives and expects to re-visit the dividend policy during 2006, depending on the results achieved in the early months, with the benefit of the newly enhanced management team. The team now in place started its work by adopting a more thoroughgoing approach to the 2006 budget exercise, a process which was accompanied by a clearer vision of the challenges ahead.

Report of the Remuneration Committee of the Supervisory Board of Telekomunikacja Polska S.A. in 2005

Andrew Seton
Deputy Chairman and Chairman of the Remuneration Committee

Andrew Seton joined the Supervisory Board of TP in 2003 and later became a Vice-Chairman as well as Chairman of the Remuneration Committee. He previously had a career spanning some 21 years in investment banking with Morgan Grenfell, London, later part of Deutsche Bank Group, where he rose to become a main board Director in the late 1980s/early 1990s. He held various posts at Morgan Grenfell, including head of project and corporate finance for Russian and East European countries, as well as Director in charge of the New York office. He later worked full-time as the EBRD's Director for Ukraine, based in Kiev from 1999 - 2002. Since leaving EBRD in 2002, he has served on the boards of MDM Bank, one of Russia's largest private financial groups, where he chaired the Remuneration and Nomination Committee, and of Unionbank, Bulgaria, a commercial and retail bank. He also served on the board of a UK-based oil and gas exploration and development company with interests in Ukraine. Mr. Seton had experience of the telecommunications sector while at Morgan Grenfell and EBRD, and also has a working knowledge of Polish.

In June 2005, the Supervisory Board elected Mr. Andrew Seton, Vice-Chairman of the Supervisory Board and an independent member, to the post of Chairman of the Remuneration Committee. Other Supervisory Board members who were elected to the Committee and who served as members in 2005 are Messrs. Andre Cathelineau and Michel Monzani. During 2005, the Remuneration Committee met seven times.

The Remuneration Committee ("Rem Comm") is charged with determining employment and remuneration terms for members of the Management Board ("MB"). In particular, it is required to make recommendations to the Supervisory Board on bonus awards for the Management Board. It also has a more general remit to consider remuneration policy for a larger range of employees. The Rem Comm reports, and makes recommendations, to the Supervisory Board.

Activities during 2005 included recommending bonus awards for Management Board members for the second half of 2004 and the first half of 2005, as well as setting objectives for Management Board members for the second half of 2005. The bonus and MBO system was kept under review with the objective of lowering the number of individual goals for each individual, as well as sharpening the thresholds for achievement in each case, all in an attempt to achieve a stronger focus on budgeted targets. The trend set by the Committee in this direction has continued much enhanced in the early months of 2006, following changes in the Management Board. In line with the Company's refreshed strategy, there has been an increased emphasis on personal responisibility in setting MBOs for H12006, as well as increasingly objective results-driven measures of achievement.

The Committee also devoted time in the second half of the year to consideration of the Company's proposed Stock Option Plan and to its conception and implementation, leading to a recommendation from management, supported by the Committee, to the Supervisory Board in December 2005.

Owing to the need to strengthen further the Management Board, the Committee became involved in in-depth discussion of the potential importance of an experienced person with the necessary leadership and technology credentials playing the role of Executive Vice-President on the Management Board. The Chairman himself met and assessed the qualifications of the proposed candidate. The Committee made a recommendation to the Supervisory Board in December.

The Committee also discussed a variety of other questions, including the appropriate route for evaluation and remuneration of the heads of certain central corporate departments (for example, Internal Audit), possible improvements to the Company's contracts with senior employees and the Company's benefit policies. Conclusions, with opinions and recommendations, are expected on some of these and other matters in 2006.

Andrew Seton
Deputy Chairman and Chairman of the Remuneration Committee
31 March 2006

Report of the Audit Committee of the Supervisory Board of Telekomunikacja Polska S.A. in 2005

Timothy Boatman
Chairman of the Audit Committee of the Supervisory Board

Member of the TP Supervisory Board
Timothy Boatman is a Chartered Accountant. From 1974 to 2001 he was a partner in the UK firm of PricewaterhouseCoopers. From 2002 to 2005 he acted as an advisor to PWC in Central and Eastern Europe and Russia. He joined the Supervisory Board of TP S.A. in 2005 as an independent director and is Chairman of the Audit Committee. He also attends the Strategy Committee meetings. He is also an independent non-executive director and chairman of the audit committee of John Laing plc in the UK. Timothy has a broad range of industry sector knowledge, including telecommunications, entertainment and media, utilities, distribution, financial services and property.

The Audit Committee was established by virtue of the Resolution of the TP Supervisory Board no. 324/V/2002 dated 14 June 2002 regarding the establishment of the Audit Committee as a consultative body acting under the Supervisory Board.

The task of the Committee is to advise the Supervisory Board on correct implementation of budgetary and financial reporting and internal control principles of the TP Group and to co-operate with the auditors of TP.

In 2005, the Audit Committee was composed of the following persons:

Chairman
– Mr. Claude Benmussa – Chairman until 15 June 2005,
– Mr. Timothy Boatman – appointed independent member of the Audit Committee 26 April 2005, appointed Chairman 15 June 2005

Members
– Mr. Andrew Seton - independent,
– Mr. Michel Monzani
– Mr. Jan Waga – until 18 January 2005
– Mr. Stefan Kawalec – until 26 April 2005

Secretary
– Mr. Cezary Klimont – appointed 15 June 2005

As of 31 December 2005 the composition of the Audit Committee was as follows:

Chairman
– Mr. Timothy Boatman

Members
– Mr. Claude Benmussa
– Mr. Andrew Seton
– Mr. Michel Monzani

Secretary
– Mr. Cezary Klimont

The key functions of the Audit Committee include:

1. monitoring the work of the Company's external auditors and presentation of recommendations to the Supervisory Board with regard to selection and remuneration of the Company's auditors;
2. discussion with the Company's auditors before the start of each annual audit on the nature and scope of the audit and monitoring co-ordination of the auditors' work;
3. review of interim and annual financial statements of the Company (TP's accounts as well as TP Group's consolidated accounts), focusing in particular on:
   a. any changes to accounting standards, policies and practices;
   b. major judgement areas;
   c. significant adjustments arising from the audit;
   d. compliance with accounting regulations.
4. discussion (with or without the presence of the Company Management Board) of any problems or reservations resulting from the financial statement audit;
5. review of the external Auditors' management letter, the independence and objectivity of their review and the response of the Management Board;
6. review of the Group's system of internal control (including financial, operational, compliance, risk assessment and management controls) as formulated by the Management Board;
7. review of contracts, transactions and arrangements between the Company and related parties;

8 annual review of the internal audit programme, co-ordination between the internal and external auditors and adequacy of resources available to the internal auditors;

9 analysis of reports of the Company's internal auditors and major findings of any other internal investigations and response of the Management Board to them, including review of freedom allowed to internal auditors;

10 consideration of any other significant matters observed by the Committee or the Supervisory Board;

11 informing the Supervisory Board about all important issues within its scope of activity.

The Audit Committee held 15 meetings in 2005, nine regular meetings and six dedicated, ad hoc meetings, and in particular performed the following:

- adopted a formal policy governing the independence of the Company's external auditors and defining those non-audit services that may be provided to the Group, including those which require the prior approval of the Audit Committee;
- reviewed the Company's and Group's financial statements;
- reviewed the Group's 2006 budget and reported to the Supervisory Board
- reviewed reports from the Executive Managers of the Group and from both the internal and external auditors, keeping under review the scope and results of the audit (both internal and external) and the cost-effectiveness, independence and objectivity of the auditors and reported its conclusions to the Supervisory Board;
- reviewed the Group's system of internal control and risk management as reported by the Management Board. Further, the Audit Committee received reports from Management on action plans in response to comments on internal controls from the internal and external auditors. It also reviewed management's progress in documenting the internal control system;
- In the year under review, the Audit Committee, especially its two independent members, reviewed and approved related party transactions and received reports from Internal Audit. In particular, two contracts related to Idea rebranding into Orange and the purchase of the minority interests of PTK Centertel from France Telecom were carefully reviewed.

The brand licence agreement was independently reviewed by PricewaterhouseCoopers, which concluded on the fairness of the agreement from a financial point of view. The Audit Committee, including its two independent members, unanimously approved the signature of the agreement on 19 April 2005.

In connection with the stake purchase transaction, Citigroup Global Markets Limited acted as the sole financial advisor to TP and the TP Group Management Board, and Merrill Lynch International acted as the sole financial advisor to the Independent Directors of the TP Group Supervisory Board. Both advisors issued two separate fairness opinions regarding the financial terms of the transaction. The ad hoc committee composed of the independent Directors unanimously recommended the approval of the transaction by the Supervisory Board.

Timothy Boatman
Chairman of the Audit Committee
of the Supervisory Board
31 March 2006

Consolidated balance sheets
as at 31 December 2005

(in PLN millions)	Note	31 December 2005	31 December 2004
Assets			
Current assets			
Cash and cash equivalents	8	1,702	3,033
Prepayments and advances	9	98	34
Receivables	10	2,123	2,590
Other financial assets	11	133	93
Current income taxes		61	126
Inventories	12	245	177
Current assets		4,362	6,053
Non-current assets			
Prepayments and advances	9	7	12
Investments accounted for under equity method	2	3	3
Other financial assets	11	15	211
Property, plant and equipment	13	24,057	25,412
Intangible assets	14	7,138	3,002
Deferred tax assets	20	42	168
Non-current assets		31,262	28,808
Total assets		**35,624**	**34,861**
Equity and Liabilities			
Current liabilities			
Interest–bearing liabilities	15	2,139	765
Loan from related party	15	1,000	–
Interest accrued on interest-bearing liabilities		247	261
Trade and other payables	16	4,015	3,821
Current income taxes		126	5
Provisions	18	757	632
Deferred income	19	410	423
Current liabilities		8,694	5,907
Non-current liabilities			
Interest–bearing liabilities	15	6,347	8,823
Trade and other payables	16	2,028	2,288
Provisions	18	127	65
Deferred income	19	346	402
Deferred tax liabilities	20	92	495
Non-current liabilities		8,940	12,073
Shareholders' equity			
Common stock	21	4,200	4,200
Share premium		832	832
Hedging reserve	30	(92)	(78)
Financial assets available for sale		–	8
Retained earnings		13,037	11,183
Equity attributable to equity holders of the parent		17,977	16,145
Minority interest		13	736
Shareholders' equity		17,990	16,881
Total liabilities and shareholders' equity		**35,624**	**34,861**

The notes to the consolidated financial statements are an integral part of these Consolidated Balance Sheets

Consolidated profit and loss accounts
for the year ended 31 December 2005

(in PLN millions)	Note	12 months ended 31 December 2005	12 months ended 31 December 2004
Revenue	22	**18,342**	**18,530**
Operating expenses:			
Employee related expenses	17	(2,447)	(2,653)
Depreciation and amortisation		(4,211)	(4,431)
Payments to other operators		(2,464)	(2,159)
Purchased services		(2,949)	(3,034)
Raw materials and consumables		(421)	(454)
Goods purchased for resale		(995)	(1,137)
Work performed and capitalised		37	59
Other operating expenses, net	23	(1,111)	(933)
Total operating expenses		**(14,561)**	**(14,742)**
Operating profit		**3,781**	**3,788**
Interest expense and other financial charges, net	24	(900)	(1,073)
Foreign exchange gain / (loss), net	24	124	562
Share of loss of associate		–	–
Profit before income tax		**3,005**	**3,277**
Income tax	20	(385)	(700)
Net profit		**2,620**	**2,577**
Attributable to:			
Equity holders of the parent		2,316	2,306
Minority interest		304	271
Basic and diluted earnings per share for profit attributable to equity holders of the parent		1.65	1.65
Weighted average common stock outstanding (millions)		1,400	1,400

The notes to the consolidated financial statements are an integral part of these Consolidated Profit and Loss Accounts

Consolidated cash flow statements
for the year ended 31 December 2005

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Cash flows from operating activities		
Net profit	2,620	2,577
Adjustments for:		
Depreciation and amortisation	4,211	4,431
Foreign exchange (gains) / losses, net	(17)	(487)
Interest and dividend charges, net	1,000	1,170
Gain/loss on investment activities	195	60
Income tax on current year profit	385	700
Income tax paid	(503)	(308)
Other non-cash items, net	8	16
Net cash flows from operating activities before changes in working capital	**7,899**	**8,159**
Changes in working capital:		
Decrease/(increase) in receivables, net of allowance	418	152
Decrease/(increase) in inventories	(68)	44
(Decrease)/increase in provisions	127	(171)
(Decrease)/increase in payables and other short-term liabilities	(26)	331
Decrease/(increase) in prepayments and advances	(59)	(6)
(Decrease)/increase in deferred income	(69)	3
Net cash flows generated from operating activities	**8,222**	**8,512**
Cash flows from investing activities		
Proceeds from sale of property, plant, equipment and intangible assets	110	35
Proceeds from sale of non-current financial assets	25	238
Sale of subsidiaries, net of cash sold	4	–
Interest received	–	2
Purchase of property, plant, equipment and intangible assets	(3,209)	(3,059)
Purchase of shares in PTK Centertel (Note 2)	(3,919)	–
Purchase of shares in Wirtualna Polska (Note 2)	(217)	–
Purchase of other non-current financial assets	–	(62)
Proceeds from sale of short-term financial assets	–	38
Other cash flows applied in investing activities, net	(42)	111
Net cash flows applied in investing activities	**(7,248)**	**(2,697)**
Cash flows from financing activities		
Proceeds from loans and borrowings	5	250
Issuance of long-term bonds	–	1,327
Interest received on derivative transactions	485	593
Repayment of loans and borrowings	(481)	(2,647)
Redemption of long-term bonds	(300)	(2,190)
Redemption of short-term securities	(11)	(2)
Interest paid	(1,438)	(1,814)
Dividends paid	(463)	(169)
Other cash flows applied in financing activities, net	(104)	98
Net cash flows applied in financing activities	**(2,307)**	**(4,554)**
Effects of exchange rate changes on cash and cash equivalents	**2**	**(46)**
Net increase/(decrease) in cash and cash equivalents	**(1,331)**	**1,215**
Cash and cash equivalents at the beginning of the period	**3,033**	**1,818**
Cash and cash equivalents at the end of the period	**1,702**	**3,033**

The notes to the consolidated financial statements are an integral part of these Consolidated Cash Flow Statements

Consolidated statements of shareholders' equity
for the year ended 31 December 2005

(in PLN millions)	Common Stock (Note 21)	Share premium	Hedging reserve (Note 30)	Financial assets available for sale	Retained earnings	Total	Minority interest	Total shareholders' equity
	Attributable to equity holders of the parent							
1 January 2004 as previously reported	**4,200**	**832**	**(116)**	**–**	**9,311**	**14,227**	**504**	**14,731**
Change in accounting policies *	–	–	–	–	(266)	(266)	(38)	(304)
1 January 2004 adjusted	**4,200**	**832**	**(116)**	**–**	**9,045**	**13,961**	**466**	**14,427**
Net profit for 12 months ended 31 December 2004	–	–	–	–	2,306	2,306	271	2,577
Revaluation of financial assets	–	–	–	131	–	131	–	131
Sale of financial assets	–	–	–	(123)	–	(123)	–	(123)
Effect of cash flow hedge accounting	–	–	38	–	–	38	–	38
Dividends paid out of 2003 profit	–	–	–	–	(168)	(168)	(1)	(169)
31 December 2004	**4,200**	**832**	**(78)**	**8**	**11,183**	**16,145**	**736**	**16,881**
1 January 2005 as previously reported	**4,200**	**832**	**(78)**	**8**	**11,383**	**16,345**	**755**	**17,100**
Change in accounting policies *	–	–	–	–	(200)	(200)	(19)	(219)
1 January 2005 adjusted	**4,200**	**832**	**(78)**	**8**	**11,183**	**16,145**	**736**	**16,881**
Net profit for 12 months ended 31 December 2005	–	–	–	–	2,316	2,316	304	2,620
Effect of cash flow hedge accounting	–	–	(14)	–	–	(14)	–	(14)
Dividends paid out of 2004 profit	–	–	–	–	(462)	(462)	(1)	(463)
Sale of financial assets	–	–	–	(8)	–	(8)	–	(8)
Sale of a subsidiary	–	–	–	–	–	–	(16)	(16)
Purchase of shares in PTK Centertel **	–	–	–	–	–	–	(1,010)	(1,010)
31 December 2005	**4,200**	**832**	**(92)**	**–**	**13,037**	**17,977**	**13**	**17,990**

*see Note 7
**see Note 2

The notes to the consolidated financial statements are an integral part of these Consolidated Statements of Shareholders' Equity

1. The Telekomunikacja Polska Group

Telekomunikacja Polska S.A. ("Telekomunikacja Polska" or "the Company"), a joint stock company, was incorporated and commenced its operations on 4 December 1991. With effect from this date, the Company assumed the telecommunications business of Polska Poczta Telegraf i Telefon ("PPTiT"), its legal predecessor. The Telekomunikacja Polska Group ("the Group") comprises Telekomunikacja Polska and its subsidiaries (see Note 2).

The Group is the principal supplier of telecommunications services in Poland. Telekomunikacja Polska obtained its permit from the Telecommunications and Postal Service Regulatory Office ("URTiP") for the provision of all telecommunications services in Poland. On the basis of this permit, Telekomunikacja Polska provides services, including fixed-line telecommunication services (local calls and long distance calls – domestic and international), Integrated Services Digital Network ("ISDN"), voice mail, dial-up and fixed access to the Internet and Voice over Internet Protocol ("VoIP"). Through its subsidiary, Polska Telefonia Komórkowa-Centertel Sp. z o.o. ("PTK Centertel"), the Group is one of Poland's three DCS 1800 and GSM 900 mobile telecommunications providers. On 20 December 2000, PTK Centertel was granted a concession for third generation UMTS services. In addition, the Group provides leased lines, radio-communications and other telecommunications value added services, sells telecommunications equipment, produces fibre optic cables and electronic phone cards and provides data transmission, multimedia services and various Internet services.

Telekomunikacja Polska's registered office is located in Warsaw at 18 Twarda St.

The number of employees in the Group was 33,603 and 36,589 at 31 December 2005 and 2004, respectively.

Since January 2001 the Polish telecommunications market had been regulated by the Telecommunications Act, enacted in 2000, which was replaced by the New Telecommunications Act in September 2004. The Telecommunications Act of 2000 introduced an extensive liberalisation of the telecom market in Poland, restricting those activities for which a permit from the regulatory authorities is required and authorising the provision of telecommunications services in specified forms on the basis of notification alone. The numerous amendments to the Polish telecommunications law were entered into force on 1 October 2003, including full carrier pre-selection, number portability, an obligation to disclose by operators the results of operations of various types of telecommunications networks and businesses and an obligation to unbundle the local loop to allow access to other service providers. The changes of 2004 were intended to both further liberalise Polish telecommunications regulations and align the Polish telecommunications market with European Union ("EU") standards by implementation of a new set of EU 2002 Directives into the Polish law. In particular, the New Telecommunications Act introduced tight regulatory control over cost calculations and pricing for telecommunications services, a wide range of obligations related to providing access to telecommunications networks and a stable basis for activities of virtual telecommunications providers.

The Telecommunications Act imposes certain legal obligations on telecommunications operators having a significant market power ("SMP operators"). Among others, other operators and service providers, including virtual operators, may have the right to demand access to SMP operators' network. SMP operators cannot refuse to interconnect a legally constructed telecommunications network of another operator to its network. Additionally, the President of URTiP is entitled to reject the tariffs or changes in tariffs proposed by SMP operators. The significant market power shall be assessed on 18 relevant markets.

Based on decisions issued by URTiP under the previous Telecommunications Act, Telekomunikacja Polska has significant market power on the domestic market for public telecommunications services, on the domestic leased lines market as well as on the domestic interconnect market, whereas PTK Centertel has a significant market power on the domestic market for public mobile telecommunications services. Additionally, URTiP in conjunction with the Office for Protection of Competition and Customers ("UOKiK") issued a decision, which is currently being challenged by the Group, stating that PTK Centertel has significant market power in the domestic interconnect market. The transitory provisions uphold certain obligations resulting from the above decisions imposed on SMP operators until designation of SMP operators on new defined markets under the New Telecommunications Act.

Under the Act of 29 December 2005 on transformations and modifications to the division of tasks and powers of state bodies competent for communications and broadcasting (Official Journal of 30 December 2005, No 267, 2258), a new central-level government administration body – the President of the Office of Electronic Communications (President of UKE) was established as of 14 January 2006 in place of the central-level government administration body – the President of the Office of Telecommunications and Post Regulation (President of URTiP) which was liquidated as of 13 January 2006.

2. Entities of the Group

In 2005, the Group comprised Telekomunikacja Polska and the following subsidiaries and associates:

Entity	Location	Scope of activities	Share capital owned by the Group 31 December 2005	Share capital owned by the Group 31 December 2004
PTK Centertel Sp. z o.o.	Warsaw, Poland	Construction and operation of mobile telecommunications networks and services.	100.00%	66.00%
TP EmiTel Sp. z o.o.	Kraków, Poland	Radio-diffusion, radio-communication, data transmission, teleinformatics and lease of technical infrastructure.	100.00%	100.00%
– Paytel Sp. z o.o. (previously Contact Center Sp. z. o.o.)	Warsaw, Poland	Call center services.	100.00%	100.00%
DITEL S.A.	Warsaw, Poland	Maintenance of subscribers' database, production and distribution of telephone directories.	100.00%	100.00%
OTO Lublin Sp. z o.o.	Lublin, Poland	Production of fibre optic cables and electronic phone cards.	100.00%	100.00%
Incenti S.A.	Warsaw, Poland	Data transmission, lease of telecommunications infrastructure and distribution of IT equipment.	–	51.00%
Otwarty Rynek Elektroniczny S.A.	Warsaw, Poland	Data transmission, operation of e-commerce platform, teleinformatics, data processing.	100.00%	100.00%
TP Edukacja i Wypoczynek Sp. z o.o.	Warsaw, Poland	Hotel services, training facilities.	100.00%	100.00%
– TP Sircom Szkolenia i Rekreacja Sp. z o.o.	Warsaw, Poland	Hotel services, training facilities.	–	100.00%
TP Internet Sp. z o.o. ("TP Internet")	Warsaw, Poland	Internet services, data transmission and multimedia.	100.00%	100.00%
– Parkiet Media S.A.	Warsaw, Poland	Publications on capital markets and economy.	–	99.45%
– Wirtualna Polska S.A. ("WP")***	Gdańsk, Poland	Internet portal and database services, software and advertising services.	100.00%	80.46%
– Sklep Wirtualnej Polski S.A. in liquidation*	Gdańsk, Poland	Company in liquidation.	100.00%	100.00%
– Becomo S.A.	Kraków, Poland	Internet services, software and computer systems advisory, advertising services.	–	77.13%
– Analizy Finansowe Sp. z o.o.*	Warsaw, Poland	Publishing of marketing and financial analysis periodicals.	–	100.00%
TP Invest Sp. z o.o.	Warsaw, Poland	Advisory and consulting services provided to the Group entities and owner's supervision of investment portfolio.	100.00%	100.00%
– Tel – Arp Sp. z o.o. in liquidation	Warsaw, Poland	Publishing and advertising services.	100.00%	100.00%
– Telefon 2000 Sp. z o.o.	Warsaw, Poland	Design and development of telecommunications systems.	95.38%	95.38%
– Telefony Podlaskie S.A.	Sokołów Podlaski, Poland	Local fixed-line telecommunications operator.	55.11%	55.11%
– Telefony Opalenickie S.A.**	Opalenica, Poland	Local fixed-line telecommunications operator.	25.00%	25.00%
– Radomska Wytwórnia Telekomunikacyjna S.A. in a state of insolvency**	Radom, Poland	Manufacturing of telephones.	25.09%	25.09%
– TP TelTech Sp. z o.o.	Łódź, Poland	Monitoring of alarm signals, servicing local networks.	100.00%	100.00%
TP MED Sp. z o.o.	Warsaw, Poland	Medical and health care services.	100.00%	100.00%
Pracownicze Towarzystwo Emerytalne Telekomunikacji Polskiej S.A.	Warsaw, Poland	Development and management of employee pension fund.	100.00%	100.00%
TP Group Foundation	Warsaw, Poland	Charity foundation.	100.00%	–
Virgo Sp. z o.o.	Warsaw, Poland	Advisory services, financial operations and property investments management.	100.00%	–
TPSA Finance B.V.	Amsterdam, The Netherlands	Financial and investment operations.	100.00%	100.00%
TPSA Eurofinance B.V.	Amsterdam, The Netherlands	Financial and investment operations.	100.00%	100.00%
– TPSA Eurofinance France S.A.	Paris, France	Financial and investment operations.	99.96%	99.96%

* excluded from consolidation due to immateriality of amounts involved
** associates accounted for under the equity method
*** excluded from consolidation in 2004 (as follows)

2. Entities of the Group (continued)

In 2005, the voting power held by the Group was equal to the Group's interest in the share capital of all of its subsidiaries.

On 26 January 2005, the Group sold its interest in Becomo S.A. The gain resulting from this transaction was not significant.

On 31 January 2005 the District Court for the Capital City of Warsaw, registered an increase in the share capital of TP Edukacja i Wypoczynek Sp. z.o.o. The share capital was increased from PLN 65,150 thousand to PLN 98,754 thousand, through the issue of 67,208 new shares of nominal value of PLN 500 each. The shares have been acquired by the existing shareholder, i.e. Telekomunikacja Polska. On the same day the District Court for the Capital City of Warsaw, registered the merger between "TP Edukacja i Wypoczynek" Sp. z.o.o. and "TP SIRCOM – Szkolenia i Rekreacja" Sp. z o.o. effected through a takeover of the latter by "TP Edukacja i Wypoczynek" Sp. z o.o.

On 7 March 2005, the Group sold its interest in Incenti S.A. to Prokom Software S.A. The gain resulting from this transaction was not significant.

On 23 June 2005, the Company acquired 100.0% of the share capital of Virgo Sp. z o.o. from TMF Holding Poland Sp. z o.o. The total purchase price was fixed at PLN 70 thousand. There was no goodwill recognised on this transaction.

On 8 September 2005, the District Court in Gdañsk, 6th Commercial Department, terminated the proceedings in bankruptcy with respect to Wirtualna Polska S.A. The court's decision was a consequence of the settlement agreement providing for the satisfaction of the WP minority shareholders in whole, which was accepted by the WP minority shareholders on 2 August 2005 and approved by the court on 23 August 2005 (see also Note 30). Under the settlement, the Group acquired 19.54% of WP shares from WP minority shareholders.

From 9 April 2004 until 8 September 2005 WP was excluded from the consolidation as the Group ceased to exercise control over this entity. WP is fully consolidated with effect from 9 September 2005. At that date, the WP assets amounted to PLN 24 million and WP liabilities amounted to PLN 50 million. The amount paid for 19.54% of WP shares was set at PLN 221 million in line with the settlement agreement with WP minority shareholders. Based on an external valuation the fair value of WP enterprise was assessed at PLN 59 million. As a result of the above transaction, the Group recognised goodwill which, after impairment, amounted to PLN 85 million.

On 21 September 2005, the Group sold its interest in Parkiet Media S.A. to Presspublica Sp. z o.o. As a result, the Group ceased to exercise control over Analizy Finansowe Sp. z o.o., as Parkiet Media S.A. controls 100.0% share in that entity. The gain resulting from this transaction was not significant.

On 26 September 2005, Contact Center Sp. z o.o. changed its name to Paytel Sp. z o.o. In September 2005, the Group incorporated also its charity foundation, Fundacja Grupy TP.

On 16 November 2005, the Company acquired 34.0% of the share capital of PTK Centertel Sp. z o.o. from a subsidiary of France Telecom S.A. The purchase price was fixed at PLN 4,880 million, of which PLN 3,880 million was paid in cash and PLN 1,000 million was financed by a non-cash loan granted by France Telecom S.A. (see Note 15c). The Company capitalised the costs directly attributable to this transaction amounting to PLN 39 million. The Company's share in the net assets of PTK Centertel was increased by PLN 1,010 million. The Group has recognised goodwill amounting to PLN 3,909 million on this transaction. As a result of the above Telekomunikacja Polska holds 100.0% of share capital in PTK Centertel.

3. The Management Board of the Company

The Management Board of the Company at the date of the preparation of these consolidated financial statements was as follows:

Marek Józefiak – President,
Alain Carlotti – Executive Vice-President,
Pierre Hamon – Board Member (Marketing & Sales),
Konrad Kobylecki – Board Member (Networks, Carriers & IT),
Jacek Kałłaur – Board Member (Human Resources),
Bruno Duthoit – Board Member (Strategy & Investments),
Jean-Marc Vignolles – Board Member (CEO PTK Centertel).

Jean-Marc Vignolles and Jacek Kałlaur were appointed Board Members on 26 April 2005. At the same time Wojciech Roman ended his term of office as a Member of the Management Board. Roger de Bazelaire resigned from the Management Board as CFO with effect from 31 December 2005. On 8 December 2005, Alain Carlotti was appointed as the Executive Vice-President of the Board. With effect from 1 January 2006 Benoît Mérel has been appointed to be acting CFO.

4. Authorisation of the financial statements

These consolidated financial statements were authorised for issuance by the Management Board on 27 March 2006.

5. Statement of compliance and basis for preparation

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and all applicable IFRSs as adopted for use in the EU. IFRS comprise standards and interpretations approved by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC").

Effective 1 January 2005, the change in the Polish Accounting Act requires the Group to prepare its consolidated financial statements in accordance with IFRS as adopted for use in the EU. At this particular time, due to the endorsement process of the EU, and the activities of the Group, there is no difference in the policies applied by the Group between IFRS and IFRS that have been adopted by the EU.

The comparative financial data as of 31 December 2004, included in these consolidated financial statements are based on the audited IFRS consolidated financial statements for the year ended 31 December 2004.

Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial years except for changes described in Note 7.

In 2004 and 2005, the IFRIC issued several interpretations, which should be applied for annual periods beginning on or after 1 January 2006. The Group reviewed the practical implications of those interpretations and identified that IFRIC 4, IFRIC 6 and IFRIC 8 may impact the consolidated financial statements in the period of initial application. At the date of the preparation of these financial statements, the Group is in the process on analyzing the impact of the adoption of these interpretations on its consolidated financial statements. The Company believes that the adoption of these interpretations will not have a material impact on its consolidated financial statements.

Basis for preparation

The consolidated financial statements have been prepared under the historical cost convention, except for the fair value applied to derivative financial instruments and financial assets available for sale.

The preparation of financial statements in accordance with IFRS requires the use of estimates and assumptions that affect the amounts reported in the financial statements and notes thereto. Although these estimates are based on management's best knowledge of current events and actions, the actual results may differ from those estimates.

These consolidated financial statements are prepared in millions of Polish zloty ("PLN").

6. Statement of accounting policies

(a) Principles of consolidation

The consolidated financial statements include all material subsidiaries that are controlled by Telekomunikacja Polska (see Note 2).

Control is presumed to exist when Telekomunikacja Polska owns, directly or indirectly through its subsidiaries, more than half of the voting rights of a given entity, unless it can be clearly demonstrated that such ownership does not constitute control. Control is also exercised where the Group has power to govern the financial and operating policies of an entity. Subsidiaries are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group.

6. Statement of accounting policies (continued)

(a) Principles of consolidation (continued)

All significant inter-company balances and transactions have been eliminated on consolidation. The consolidated financial statements are prepared using uniform accounting policies for similar transactions and other events in similar circumstances.

(b) Cash and cash equivalents

Cash and cash equivalents comprise cash in bank and on hand and all highly liquid deposits and commercial papers with an original maturity of three months or less.

For the purposes of the consolidated cash flow statements, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(c) Trade and other receivables

Trade receivables are carried at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts allowance is made when collection of the full amount is no longer probable, based on historical collection patterns or alternatively having regard to the age of the receivable balances.

(d) Inventories

Inventories are stated at the lower of acquisition cost (on a weighted average basis) and net realisable value, except for mobile handsets sold in promotional offers. Inventories of mobile handsets sold in promotional offers are stated at the lower of cost or probable net realisable value, taking into account future revenues expected from subscriptions. The Group provides for slow-moving or obsolete inventories based on inventory turnover ratios and current marketing plans.

(e) Investments

All investments are initially recognised at the fair value of the consideration given and including acquisition charges related to the investment.

After initial recognition, investments at fair value through profit or loss and available-for-sale are measured at fair value. Gains or losses on investments at fair value through profit or loss are recognised in the profit and loss account in the period of the change in their fair value. Gains or losses on investments available-for-sale are recognised as a separate component of equity until an investment is sold, collected or otherwise disposed of or until an investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the profit and loss account.

Other investments that are intended to be held-to-maturity are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any discount or premium on acquisition, over the period to maturity. For investments carried at amortised cost, gains and losses are recognised in the profit and loss account when the investments are derecognised or impaired.

For investments that are actively traded in organised financial markets, fair value is determined by reference to stock exchange quoted market bid prices at the close of business on that balance sheet date. Fair values for unlisted equity securities are estimated using applicable price/earnings or price/cash flow ratios modified to reflect the specific circumstances of the issuer. Equity securities for which fair values cannot be measured reliably are recognised at cost less impairment.

(f) Investments accounted for under the equity method

Investments accounted for under the equity method are measured on initial recognition at cost. The Group's share in post acquisition profits or losses of associates is recognised in the income statement and its share in post-acquisition movements in associate's equity is recognised in reserves. Associates are entities in which the Group has between 20% and 50% of the voting rights, or over which the Group has significant influence, but which it does not control. When the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

(g) Property, plant and equipment

Property, plant and equipment are stated at historical cost less accumulated depreciation and any impairment in value.

The initial cost of property, plant and equipment comprises its purchase price, any directly attributable costs of bringing the asset to its working condition and location for its intended use and the initial estimate of the costs of dismantling and removing

the asset. Expenditures incurred after property, plant and equipment have been put into operation, such as repairs, maintenance and overhaul costs, as well as costs of cabling within customers' premises are charged to the profit and loss account in the period in which the costs are incurred. In situations when it may be clearly demonstrated that the expenditures have resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment, the expenditures are capitalised as an additional cost of property, plant and equipment if the recognition criteria are met.

The Group has revalued certain property, plant and equipment and used their fair value as deemed cost as at 1 January 2003, which is the date of transition to IFRS under IFRS 1.

Telekomunikacja Polska received certain property, plant and equipment from Public Telephone Committees (Społeczne Komitety Telefonizacji – "SKT"). This infrastructure is recorded in the books as fixed assets at the acquisition costs of these assets with a corresponding entry in liabilities. Sales of services to SKT members are recorded as revenues and corresponding amounts are deducted from liabilities.

Property, plant and equipment are depreciated over their estimated useful lives. Upon their withdrawal from use or sale, the cost of assets disposed and the related accumulated depreciation are removed from the books of account, and any resulting gains or losses are taken to the profit and loss account.

Property, plant and equipment are depreciated using the straight-line method. Depreciation periods are as follows:

Buildings	10-30 years
Duct, cable and other outside plant	10-30 years
Telephone exchanges and other plant and equipment	5-10 years
Computer equipment	3-5 years
Vehicles and other	5-10 years

Perpetual usufruct rights are amortised over the period for which the right was granted.

During the first half-year of 2005, the Company completed a project of verification of accounting for its property, plant and equipment. The main goals of the project were to reassess the useful lives of property, plant and equipment and to ensure that all significant parts of an item of property, plant and equipment which have different useful lives or depreciation methods are identifiable for the calculation of the depreciation. Consequently, the depreciation charge starting from 1 January 2005 was calculated based on the useful lives which have been modified in respect to certain property, plant and equipment as a result of the project.

The effect of the above change, together with the change related to a verification of the useful lives of intangibles (see Note 6(h)), resulted in a reduction in the total depreciation charge by approximately PLN 143 million for the year 2005. Thereafter, the expected depreciation charge should be stabilised at the current level subject to the effect of additions, disposals and liquidations of the assets in the normal course of business.

Construction-in-progress represents property, plant and equipment under construction and is stated at cost. This comprises the cost of construction or acquisition of property, plant and equipment and other direct costs. Construction-in-progress is not depreciated until the relevant assets have been completed and placed into operational use.

(h) Intangible assets

1 Goodwill

Goodwill represents the excess of the costs of acquisition over the fair value of identifiable net assets of a subsidiary, associate or joint-venture at the date of acquisition. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. In case of acquisition of interest in a subsidiary which is already controlled by the TP Group, the goodwill is calculated as the difference between the purchase consideration and the acquired share of the minority shareholders in the subsidiary's net assets at the acquisition date.

2 Research and development

Research and development costs are generally expensed as incurred. In the twelve months ended 31 December 2005 and 2004 research and development costs recognised in the profit and loss account amounted to PLN 55 million and PLN 68 million, respectively. Development expenditure incurred on an individual project is capitalised when its future recoverability can reasonably be regarded as assured. Any expenditure capitalised is amortised over the period of expected future sales from the related project. The amortisation begins when the projects are commercially implemented.

6. Statement of accounting policies (continued)

(h) Intangible assets (continued)

3 Computer software

Costs that are directly associated with identifiable and unique software products controlled by the Group and which will probably generate economic benefits exceeding the related costs, beyond one year, are recognised as intangible assets. Software is amortised using the straight-line method over their useful lives.

4 Concessions and other intangibles

Expenditure on acquisition of telecommunications concessions and other intangible assets is capitalised and amortised using the straight-line method over their useful lives. Amortisation begins when the related technology is commercially implemented. The concessions are amortised over the remaining period of concession. Other intangibles are amortised over their useful lives not exceeding 5 years.

In the first half-year of 2005, the Company has completed a project of reassessment of the useful lives of intangibles. Consequently, the depreciation charge starting from 1 January 2005 was calculated based on the useful lives which have been modified in respect to certain intangibles as a result of the project (see Note 6(g)).

(i) Impairment of non-current assets

Property, plant and equipment and other non-current assets, including goodwill, intangible assets and financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets not ready for use and goodwill are subject to an annual impairment test regardless of conditions. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's fair value less cost to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separable identifiable cash flows ("cash-generating unit").

(j) Interest-bearing liabilities

Interest-bearing liabilities are recognised initially at their cost, being the fair value of the consideration received. Transaction costs are included in the initial measurement of these financial liabilities. After initial recognition, interest-bearing liabilities are measured at amortised cost, except for financial liabilities designated as hedged items, which are subject to measurement under the hedge accounting provisions as described in Note 6(s).

(k) Provisions

A provision is recognised when the Group has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate may be made of the amount of the obligation. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate. Where the effect of the time value of money is material, the amount of the provision is the present value of the expenditures expected to be required to settle the obligation. When discounting is used, the increase in the carrying amount of a provision reflecting the passage of time is recognised as a financial expense.

(l) Deferred income

Investment contributions received in cash as contributions to the cost of network construction or constructed telephone infrastructure from local authorities (further referred to as "grants") are deferred and amortised to other operating revenue over the life of the asset to which the investment contributions relate. Deferred income also includes deferred revenues from subscriptions relating to future periods, connection fees and the sale of telephone cards in the "prepaid" fixed line and mobile telephony systems.

(m) Leases

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the profit and loss account. If there is no reasonable certainty that the Group will obtain ownership by the end of the lease term, capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term. In other cases, capitalised leased assets are depreciated over their economic useful lives.

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

(n) Revenue recognition

1 Revenue from sale of services and goods
Revenue, net of value added tax ("VAT"), rebates and discounts, from the sale of services and goods is recognised when:
a) the amount of revenue may be reliably measured,
b) it is probable that the economic benefits associated with the transaction will flow to the enterprise,
c) the stage of completion of the transaction at the balance sheet date may be reliably measured, and
d) the costs incurred for the transaction and the costs to complete the transaction may be reliably measured.

Revenue earned from interconnect charges to other telecommunication operators is not netted off with interconnect costs paid by the Group to other operators. Revenue earned from connecting subscribers to the network is deferred and recognised over the expected subscription period ranging from 1.5 to 9 years. The Group leases lines to its customers. Lease income is recognised as revenue on a straight-line basis over the lease term.

Revenue from activation fees for prepaid services is recognised upon the activation of the service. Revenues from the sale of telephone cards in the "prepaid" fixed line and mobile telephony systems are deferred and recognised when earned.

The total arrangement consideration on contracts with multiple revenue-generating activities is allocated to each separate unit of accounting based on their relative fair values. The revenue from the sale of mobile handsets is recognised upon activation of the service. The revenue from the sale of telecommunication services is recognised over the period of the contract.

2 Interest
Interest income is recognised as the interest accrues, taking into account the effective yield on assets.

3 Dividends
Dividends are recognised when the Group's right to receive the payment is established.

(o) Operating expenses

Operating expenses are charged in the period to which they relate.

Discounts on mobile handsets sold on promotional terms are recognised at the moment of sale and activation of the service.

In line with Polish business practice, the shareholders are allowed to distribute profits in order to increase the Social Fund established for the welfare of the Company's employees. The Group allocates part of its net profit to the Social Fund. Final authorisation of the profit distribution to the Social Fund is given after the year end during the General Shareholders' Meeting, when the annual profit available for distribution is approved. In these financial statements such distributions are recognised as an operating expense of the period to which the profit to be distributed relates.

(p) Borrowing costs

Borrowing costs are expensed in the profit and loss account as incurred.

(q) Employee benefit plans

Certain employees of the Group are entitled to jubilee awards and retirement bonuses. Jubilee awards are paid to employees upon completion of a certain number of years of service whereas retirement bonuses represent one-off payments paid upon retirement in accordance with the Group's remuneration policies. Both items vary according to the employee's average remuneration and length of service. Jubilee awards and retirement bonuses are not funded. In accordance with the Collective Bargaining Agreement with its employees the Group is obliged to make additional annual contributions to the Social Fund in respect of its retired employees. The Group is also obliged to provide certain post-employment benefits such as medical care to its retired employees.

The cost of providing benefits mentioned above is determined separately for each plan using the projected unit credit actuarial valuation method. Actuarial gains and losses on jubilee awards plans are recognised as income or expense when they occur. Actuarial gains and losses on plans other than for jubilee awards are recognised as income or expense when the net cumulative unrecognised actuarial gains and losses for each individual plan at the end of the previous reporting year exceeded 10% of the defined benefit obligation at that date. These gains or losses are recognised over the expected average remaining working lives of the employees participating in the plans. The present value of the defined benefit obligations is verified at least annually by an independent actuary. Demographic and attrition profiles are based on historical data.

6. Statement of accounting policies (continued)

(r) Foreign currency transactions

Transactions denominated in foreign currencies are recorded in the functional currency of the Company (Polish zloty) at the following exchange rates:

1 The bid or offer rates used by the bank where the transaction is conducted – to record transactions involving the sale or purchase of foreign currencies and settlements of receivables or liabilities; or
2 The average exchange rates as quoted by the National Bank of Poland ("NBP") on the day of the transaction, unless a different rate has been determined on an appropriate document.

Monetary assets and liabilities denominated in foreign currencies are translated at the balance sheet date at the average rate quoted by the NBP as at that date. Any gains or losses arising from a change in exchange rates subsequent to the date of recognition of the transaction are presented as foreign exchange gains or losses in the profit and loss account.

The Group translates for the purpose of consolidation the monetary assets and liabilities in the financial statements of foreign subsidiaries at the current average NBP exchange rates prevailing at the balance sheet date. Non-monetary items are translated using the historical rates. Profit and loss account items are translated using average rates for the reporting period.

(s) Derivative financial instruments

Swap, forward and option contracts are valued at fair values and presented as financial assets or financial liabilities in the balance sheet. Fair value is calculated using the net present value of future cash flows related to these contracts, quoted market forward interest rates, quoted market forward foreign exchange rates or, if quoted forward foreign exchange rates are not available, forward rates calculated based on spot foreign exchange rates using the interest rate parity method.

Except when contracts qualify as hedges, changes in the fair value of financial instruments are recognised as other financial income/expenses in the profit and loss account in the period of the change. When contracts qualify as fair value hedges, related gains and losses offset symmetrically the effects on the net profit or loss of the change in the fair value of the hedged items. A gain or loss on the hedged item attributable to the hedged risk is included in the net profit or loss for the period.

When contracts qualify as cash flow hedges, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in equity. The ineffective portion is immediately recognised in the profit and loss account. The amounts that have been recognised in equity are included in the profit and loss account in the same period during which the hedged firm commitment or forecasted transactions affect the profit and loss account for financial items or enter into the initial measurement of the acquisition cost or other carrying amount of the non-financial asset or liability as appropriate.

The Group entities enter into contracts which do not constitute financial instruments but which include embedded derivatives. These instruments primarily relate to purchase contracts for equipment and services denominated in foreign currencies.

Embedded derivatives are separated from the host contracts and accounted for as derivatives if all of the following conditions are met:
- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract,
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and
- a hybrid instrument is not measured at fair value with changes in the fair value reported in the net profit or loss.

Embedded derivatives are measured at fair value.

(t) Income tax

The corporate income tax charge is based on profit for the period and takes into account deferred taxation. Deferred tax is calculated using the liability method. Under the liability method the expected tax effects of temporary differences are determined using enacted tax rates and reported either as liabilities for tax payables or assets representing future reductions in tax charges. Temporary differences are the differences between the carrying amount of assets or liabilities in the balance sheet and their taxable base. The calculation of deferred tax also includes tax losses from previous years, which according to tax regulations may decrease taxable profits. The net deferred tax liabilities or assets are included under non-current liabilities or non-current assets, respectively. Deferred tax liabilities and deferred tax assets are presented net if the entities constituting the Group have a legally enforceable right to offset the recognised amounts.

Deferred tax assets are only recognised on temporary differences provided it is probable they will be realised.

The Group recognises a deferred tax asset for all deductible temporary differences arising from investments in subsidiaries and associates to the extent that it is probable that:
a) the temporary differences will reverse in the foreseeable future; and
b) taxable profit will be available against which the temporary differences can be utilised.

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

(u) Net profit per share

The net profit per share for each period is calculated by dividing the net profit for the period attributable to the equity holder of the parent by the weighted average number of shares outstanding during that period. The Group does not present diluted profit/loss per share, as there are no dilutive instruments issued.

7. Effect of changes in accounting policies

In line with IAS 8, changes in accounting policies are applied retrospectively. These consolidated financial statements include the following adjustments to net assets and net profits for prior reporting dates related to changes in accounting policies:

(in PLN millions)	Net assets as at 1 January 2004	Net assets as at 31 December 2004	Net profit for 12 months ended 31 December 2004
Data previously reported*	**14,227**	**16,345**	**2,240**
(a) Connection fee	(190)	(162)	28
(b) Loyalty costs	(22)	(16)	6
(c) Commissions to dealers	(41)	(9)	32
(d) Sale of scratch cards	(13)	(13)	–
Data adjusted	**13,961**	**16,145**	**2,306**

* in line with the accounting policies as reported in the financial statements for the year ended 31 December 2004
The amounts of the adjustments include an effect of deferred tax.
As a result of the above changes the EPS ratio for 2004 increased from 1.60 to 1.65

(a) Revenue recognition on connection fees

Telekomunikacja Polska charges one-off non-refundable fees for the connection of a subscriber into its fixed line network. The Group's previous policy was to recognise connection fees and the related costs in its profit and loss account at the moment of activation. Following the change, the revenue related to the connection fees is deferred and recognised over the expected subscription period ranging from 1.5 to 9 years. The Group has elected to change its accounting policy as it believes that such change will provide more adequate information.

In line with IAS 8, the change in accounting policy was applied retrospectively. However, as it is impracticable to determine the effects of the change in accounting policy on the financial data before 2001, the Company applied the new accounting policy as at the beginning of the earliest period for which retrospective application is practicable, i.e. the new accounting policy was applied to revenue on connection fees for 2001 and further periods. Determination of the effects of the change in accounting policy on the financial data before 2001 is impracticable among others due to limitations of accessibility or a lack of enough detailed information for periods prior to 2001.

As a result, the revenue and tax charge for 2004 increased by PLN 35 million and PLN 7 million, respectively. Additionally, as at 31 December 2004, deferred income increased by PLN 200 million, deferred tax liabilities decreased by PLN 38 million and the retained earnings decreased by PLN 162 million.

7. Effect of changes in accounting policies (continued)

(b) Revenue recognition – loyalty costs
PTK Centertel loyalty programs enable subscribers to gain bonus points redeemable against certain benefits. The Group's previous policy was to value the bonus points at the estimated costs of the benefits and present the value of all accrued points as cost of sales. Following the change, the value of the points, which are expected to be redeemed as free minutes or SMSs is estimated using the current charges per minute/SMS and is recognised as a deferred revenue up to the point, when subscribers utilise these benefits.

The Group has elected to change its accounting policy as it believes that such change will provide more adequate and reliable information. As a result, the revenue, tax charge and minority interest charge for 2004 increased by PLN 3 million, PLN 3 million and PLN 3 million, respectively, whereas the purchased services decreased by PLN 9 million. Trade and other payables decreased by PLN 24 million and deferred income increased by PLN 53 million as at 31 December 2004. Deferred tax assets increased by PLN 5 million, the retained earnings and minority interest decreased by PLN 16 million and PLN 8 million, respectively.

(c) Commissions to dealers
PTK-Centertel pays a commission to its dealers for the activation and retention of a subscriber payable 6, 12 and 18 months after a subscriber's activation. Previous policy was to accrue for the part of the commission earned up to the balance sheet date adjusted by the churn rate. Following the change, the commissions adjusted by the churn rate are accrued at the activation date whatever the payment date.

The Group has elected to change its accounting policy as it believes that such change will provide more adequate and reliable information. As a result, the operating costs for 2004 decreased by PLN 59 million and the tax charge and minority interest increased by PLN 11 million and PLN 16 million, respectively. As at 31 December 2004 deferred tax assets and trade and other payables increased by PLN 4 million and PLN 18 million, respectively. Additionally, as at 31 December 2004 the retained earnings and minority interest decreased by PLN 9 million and PLN 5 million, respectively.

(d) Sales of POP scratch cards
PTK Centertel recognises revenue from the sale of scratch cards on the usage basis deferring the immediate sales receipts until that moment. Following the change, a sale of scratch cards through distributors is recognised gross with parallel recognition of costs of distrubition (costs of commission of distributors' caption). The previous policy was to recognise indirect sales net of distribution costs treating them as trade discounts allowed.

The Group has elected to change its accounting policy as it believes that such change will provide more adequate and reliable information. As a result, as at 31 December 2004 the retained earnings and minority interest decreased by PLN 13 million and PLN 6 million, respectively. Additionally, deferred income and deferred tax assets increased by PLN 23 million and PLN 4 million, respectively. The change did not significantly impact the net profit for 2004.

Reclassifications

Certain reclassifications were made as the Group believes that the new presentation will provide more adequate and reliable information. None of the changes in the presentation affected net profit for 2004 or shareholders' equity at 31 December 2004.

(a) Revenue and cost presentation on a lease of transponders
Telekomunikacja Polska acts as an agent (not as a principal) in some agreements relating to leasing of transponders from satellite organizations to broadcasters. Previously, these transactions have been presented gross. Following the change, revenue from these services is presented net in the profit and loss account. As a result, both the revenue and operating costs for 2004 decreased, by PLN 72 million, respectively.

(b) Presentation of foreign exchange differences, interest and other gains or losses on non-financial items
Previously, all foreign exchange differences, interest and impairment charges on interest receivable were presented as part of financial activities in the profit and loss account. Following the change, gains and losses on non-financial items are presented as part of operational activities. As a result, other operating expenses (net) for 2004 decreased by PLN 182 million, with a corresponding decrease in the foreign exchange gains (net) by PLN 163 million, increase in the interest expense by PLN 29 million and decrease in the impairment charges on interest on non-financial items by PLN 10 million.

8. Cash and cash equivalents

(in PLN millions)	31 December 2005	31 December 2004
Cash on hand	6	1
Current bank accounts	54	58
Overnight deposits	529	368
Deposits up to 3 months	924	718
Securities with a maturity of less than 3 months	186	1,883
Other	3	5
Total	**1,702**	**3,033**

As at 31 December 2005 and 31 December 2004, cash and cash equivalents include an equivalent of PLN 515 million and PLN 1,133 million denominated in foreign currencies, respectively.

The concentration of credit risk related to cash and cash equivalents is limited as the Group primarily places its cash in institutions with high investment grade rating.

In accordance with Polish Law, the Group's entities registered in Poland administer a Social Fund on behalf of their employees. The contributions paid to the Social Fund are deposited in separate bank accounts held in the name of various Group entities. As at 31 December 2005 and 31 December 2004, cash earmarked for the Social Fund amounted to PLN 26 million and PLN 25 million, respectively. Receivables concerning Social Fund loans to employees as at 31 December 2005 and 31 December 2004 amounted to PLN 109 million and PLN 107 million, respectively (see Note 10). Liabilities related to the Social Fund amounted to PLN 135 million and PLN 132 million, respectively, and were presented as a part of trade and other payables (see Note 16).

Except for the amounts related to the Social Fund presented above, restricted cash amounted to PLN 15 million and PLN 100 million as at 31 December 2005 and 31 December 2004, respectively. As at 31 December 2005, restricted cash related mainly to the special purpose deposits. As at 31 December 2004, the amount of restricted cash related mainly to the deposit placed by Telekomunikacja Polska as a result of a swap transaction.

9. Prepayments and advances

Prepayments and advances primarily consist of commissions paid for unused bank loans, prepayments for information technology services, insurance and the costs of unactivated mobile phones maintained in the dealership network of PTK Centertel.

10. Receivables

(in PLN millions)	31 December 2005	31 December 2004
Trade receivables	2,574	3,160
Tax receivables	59	24
Social Fund loans to employees (see Note 8)	109	107
Other receivables	65	139
Subtotal	**2,807**	**3,430**
Less allowance for trade receivables	(656)	(812)
Less allowance for other receivables	(28)	(28)
Total	**2,123**	**2,590**

Trade receivables relate primarily to billings for telecommunications services. Credit terms of typical sales are 14 to 21 days. Tax receivable balances comprise mainly of recoverable VAT on capital purchases.

As at 31 December 2005 and 31 December 2004, total receivables include PLN 189 million and PLN 194 million of receivables denominated in foreign currencies, respectively.

10. Receivables (continued)

The concentration of credit risk relating to trade receivables is limited due to the large number of customers comprising the Group's customer base and their dispersion, principally in Poland.

In the twelve months periods ended 31 December 2005 and 2004, the impairment loss on receivables charged to the profit and loss account amounted to PLN 252 million and PLN 468 million, respectively (see Note 23).

11. Other financial assets

(in PLN millions)	31 December 2005	31 December 2004
Investments available for sale	5	34
Investments at fair value through profit or loss	4	2
Swap contracts (see Note 30)	131	254
Forward contracts (see Note 30)	2	–
Embedded derivatives	6	12
Options (see Note 30)	–	1
Investments held to maturity	–	1
Total	**148**	**304**
Current portion	133	93
Non-current portion	15	211

12. Inventories

(in PLN millions)	31 December 2005	31 December 2004
Cables, engineering inventory and other materials		
– value at cost	24	40
– value at NRV	5	6
Goods for resale		
– value at cost	219	130
– value at NRV	6	6
Subtotal	**254**	**182**
Less allowance for obsolete inventory	(9)	(5)
Total	**245**	**177**

As at 31 December 2005 and 31 December 2004, goods for resale include mobile handsets with a value of PLN 149 million and PLN 99 million, respectively.

In the twelve months periods ended 31 December 2005 the impairment loss on inventories charged to the profit and loss account amounted to PLN 7 million. In the twelve months ended 31 December 2004 the reversal of impairment charge on inventories in the profit and loss account amounted to PLN 1 million (see Note 23).

13. Property, plant and equipment

(in PLN millions)	Land, buildings, duct, cable and other outside plant	Telephone exchanges and other plant and equipment	Vehicles and other	Construction in progress	Total
Cost					
1 January 2004	**15,335**	**16,509**	**518**	**1,957**	**34,319**
Additions	752	2,348	60	(738)	2,422
Disposals and other	(82)	(315)	(44)	(29)	(470)
31 December 2004	**16,005**	**18,542**	**534**	**1,190**	**36,271**
1 January 2005	**16,005**	**18,542**	**534**	**1,190**	**36,271**
Additions	358	1,638	29	536	2,561
Disposals and other	(39)	(266)	(34)	(28)	(367)
31 December 2005	**16,324**	**19,914**	**529**	**1,698**	**38,465**
Accumulated depreciation					
1 January 2004	**1,050**	**5,466**	**240**	**249**	**7,005**
Charge for the period	836	3,015	128	–	3,979
Impairment charge	283	25	1	(154)	155
Disposals and other	(47)	(187)	(26)	(20)	(280)
31 December 2004	**2,122**	**8,319**	**343**	**75**	**10,859**
1 January 2005	**2,122**	**8,319**	**343**	**75**	**10,859**
Charge for the period	895	2,798	51	–	3,744
Impairment charge	(39)	13	(1)	18	(9)
Disposals and other	(27)	(119)	(16)	(24)	(186)
31 December 2005	**2,951**	**11,011**	**377**	**69**	**14,408**
Net book value 31 December 2004	**13,883**	**10,223**	**191**	**1,115**	**25,412**
Net book value 31 December 2005	**13,373**	**8,903**	**152**	**1,629**	**24,057**

The line "Additions" includes additions of property, plant and equipment and transfers from construction-in-progress to other categories of property, plant and equipment.

As at 31 December 2005 and 31 December 2004, there were no property, plant and equipment pledged as security for loans or bank guarantees.

International Accounting Standard 36 "Impairment of assets" requires that the recoverable amount of an asset should be estimated whenever there is an indication that the asset may be impaired and an impairment loss should be recognised whenever the carrying amount of an asset exceeds its recoverable amount. The Group has identified certain indicators, including market liberalization and other regulatory and economic changes in the Polish telecommunications market that could act as triggering factors for the potential impairment of assets. Where possible, the recoverable amount was estimated for individual assets. The recoverable amount of such assets was determined at their fair value less cost to sell or their value in use. If it was not possible to estimate the recoverable amount of the individual asset, the Group identified the cash-generating unit ("CGU") to which the asset belongs. The recoverable amount of a CGU was determined as its value in use being the present value of estimated future cash flows expected to arise from the continuing use and the residual value of a CGU from its disposal at the end of its useful life. For the purpose of the impairment test, the entire fixed network, the entire mobile network and the entire radio diffusion network were treated as separate cash-generating units.

13. Property, plant and equipment (continued)

In February 2005, the Group implemented a new insurance programme covering property damage and business interruption risks related to the majority of its assets and activities. The programme, led by international insurers, also covers extra expenses related to casualty and consequential loss of profit.

In 2005, the reversal of the impairment loss on property, plant and equipment charged to the profit and loss account amounted to PLN 9 million. In 2004, the impairment loss on property, plant and equipment charged to the profit and loss account amounted to PLN 155 million (see Note 23). As at 31 December 2005 and 2004, total impairment on property, plant and equipment amounted to PLN 342 million and PLN 432 million, respectively.

14. Intangible assets

(in PLN millions)	DCS 1800 concession	GSM 900 concession	UMTS concession	Software and other	Goodwill	Total
Cost						
1 January 2004	**333**	**380**	**1,633**	**1,713**	**222**	**4,281**
Additions	–	–	–	866	–	866
Disposals	–	–	–	(58)	(166)	(224)
31 December 2004	**333**	**380**	**1,633**	**2,521**	**56**	**4,923**
1 January 2005	**333**	**380**	**1,633**	**2,521**	**56**	**4,923**
Additions	–	–	–	726	4,156	4,882
Disposals	–	–	–	(241)	(15)	(256)
31 December 2005	**333**	**380**	**1,633**	**3,006**	**4,197**	**9,549**
Accumulated amortisation						
1 January 2004	**132**	**101**	**–**	**1,224**	**222**	**1,679**
Charge for the period	21	27	–	404	–	452
Impairment charge	–	–	–	6	–	6
Disposals	–	–	–	(50)	(166)	(216)
31 December 2004	**153**	**128**	**–**	**1,584**	**56**	**1,921**
1 January 2005	**153**	**128**	**–**	**1,584**	**56**	**1,921**
Charge for the period	22	26	8	411	–	467
Impairment charge	–	–	–	(6)	162	156
Disposals	–	–	–	(118)	(15)	(133)
31 December 2005	**175**	**154**	**8**	**1,871**	**203**	**2,411**
Net book value 31 December 2004	**180**	**252**	**1,633**	**937**	**–**	**3,002**
Net book value 31 December 2005	**158**	**226**	**1,625**	**1,135**	**3,994**	**7,138**

Mobile concessions held by PTK Centertel include concessions for rendering mobile telephony services using the following technologies:
- DCS 1800 – acquired in 1997, expires 2012,
- GSM 900 – acquired in 1999, expires 2014,
- UMTS – acquired in 2000, expires 2023.

Some of these mobile concessions require PTK Centertel to fulfil certain conditions, including the number of subscribers and coverage of the network by a set deadline. If these conditions are not met, the concessions may be withdrawn. The Group believes that all significant requirements as stipulated in the telecommunication concessions were met as at 31 December 2005.

Telekomunikacja Polska's rights to provide telecommunications services are based on a permit granted free of charge on the basis of the Telecommunications Act. The permit expires in 2026.

Goodwill recognised in 2005 relates to purchase of shares in WP and PTK Centertel (see Note 2). At 31 December 2005, the recoverable amount of goodwill was determined based on external valuations of the fair value of these entities.

In 2005 and 2004 the impairment loss on intangible assets charged to the profit and loss account amounted to PLN 37 million and 6 million, respectively (see Note 23). As at 31 December 2005 and 2004, total impairment on intangibles amounted to PLN 216 million and to PLN 74 million, respectively.

15. Interest-bearing liabilities

(in PLN millions)	Note	31 December 2005	31 December 2004
Bank borrowings	(a)	1,739	2,271
Bonds	(b)	6,747	7,317
Loan from related party	(c)	1,000	–
Total		**9,486**	**9,588**
Short-term portion		3,139	765
Long-term portion		6,347	8,823

As at 31 December 2005, the maturity of non-current interest-bearing liabilities was as follows:

(in PLN millions)	
12 months ended 31 December:	
2007	1,952
2008	2,325
2009	218
2010	218
Thereafter	1,634
Total	**6,347**

The amounts presented in the above schedule of debt repayments include the effect of the application of hedge accounting principles in the valuation of hedged items (see Note 6(s)).

(a) Bank borrowings

As at 31 December 2005, bank borrowings borrowed by the Group are as follows:

Creditor	Agreement	Currency (millions)	Outstanding balance of loan PLN (millions)	Interest rate	Repayment date
International Bank for Reconstruction and Development	33190 POL	19 USD	63 PLN	4.79%*	15 March 2008
European Investment Bank	1.5286	5 USD	16 PLN	6.454%	10 June 2008
European Investment Bank	1.5286	11 EUR	42 PLN	7.112%	10 June 2008
European Investment Bank	1.9251	83 EUR	322 PLN	2.44%**	15 December 2015
European Investment Bank	0.2218	12 EUR	47 PLN	3.81%	18 August 2006
European Investment Bank	20.887	217 EUR	836 PLN	2.44%**	15 June 2012
European Investment Bank	20.887	337 PLN	337 PLN	4.49%**	15 June 2012
Instituto de Credito Oficial	–	23 USD	76 PLN	1.25%	2 January 2021

* Floating rate determined by the bank every half year;
** Floating rate determined by the bank every three months;

15. Interest-bearing liabilities (continued)
(a) Bank borrowings (continued)

Bank borrowings analysed by currency are as follows:

(in PLN millions)	31 December 2005	31 December 2004
Polish zloty	337	389
Euro – hedged portion*	570	930
Euro – non-hedged portion	677	779
U.S. dollar – hedged portion*	15	17
U.S. dollar – non-hedged portion	140	156
Total	**1,739**	**2,271**

*includes the fair value adjustments to the items being hedged (Note 30)

As at 31 December 2005 and 31 December 2004, bank loans amounting to PLN 196 million and PLN 235 million, respectively, were subject to government guarantees. As at 31 December 2005 and 31 December 2004, there were no loans collateralised by specific assets of the Group.

Based on the arrangements made with banks, the Group has unused bank loan facilities amounting to PLN 2,172 million, as at 31 December 2005. The unused loan facilities are subject to floating interest rates based on WIBOR and EURIBOR and are designated to finance current operating activity and general corporate targets.

The Company was a party to certain bank borrowings which required the Company to maintain certain financial ratios. Following the changes to bank borrowing agreements in the first half of 2005, the Company has been released from all financial ratio covenants. Based on management calculations, the Group met all financial covenants included in bank borrowing agreements in the previous reporting periods.

(b) Bonds

As at 31 December 2005, bonds issued by the Group are as follows:

Issuer	Series	Nominal value	Issue price	Interest rate	Issue date	Redemption date
		(in millions)				
TPSA Finance B.V.	A	800 USD	789 USD	7.750%	10 December 1998	10 December 2008
TPSA Eurofinance B.V.	D	475 EUR	470 EUR	6.500%	13 March 2000	13 March 2007
TPSA Eurofinance B.V.	E	500 EUR	495 EUR	6.625%	1 March 2001	1 March 2006
TPSA Eurofinance France S.A.	T	300 EUR	298 EUR	4.625%	5 July 2004	5 July 2011

The redemption of all the bonds issued by the Group is guaranteed by Telekomunikacja Polska.

Bonds analysed by currency are as follows:

(in PLN millions)	31 December 2005	31 December 2004
Polish zloty	–	291
Euro – hedged portion *	3,645	3,386
Euro – non-hedged portion	1,019	1,643
U.S. dollar – hedged portion *	2,010	1,933
U.S. dollar – non-hedged portion	73	64
Total	**6,747**	**7,317**

* includes the fair value adjustments to the items being hedged (Note 30)

(c) Loan from related party

Loan from related party relates to a loan of PLN 1,000 million granted to Telekomunikacja Polska by France Telecom on 14 December 2005. The loan has been used for partial financing of the purchase of shares in PTK Centertel (see Note 2). The loan has been granted for a period of 12 months with an early repayment option. The interest on the loan is based on WIBOR for quarterly deposits plus a margin of 0.14%. Proceeds from the loan have been excluded from the 2005 consolidated cash flow statement as a non-cash transaction in accordance with IAS 7.

16. Trade and other payables

(in PLN millions)	31 December 2005	31 December 2004
Trade payables	1,717	1,553
Capital expenditure payables	1,103	1,235
Concessions payable	835	890
Employee benefit plans (see Note 17)	369	478
Social security and taxes	251	292
Accrued expenses	170	195
Social Fund (see Note 8)	135	132
Salaries and wages	127	124
Swap contracts (see Note 30)	1,218	1,176
Forward contracts (see Note 30)	82	–
Other payables	36	34
Total	**6,043**	**6,109**
Less: short-term portion	(4,015)	(3,821)
Long-term portion	2,028	2,288

Trade and other payables include PLN 1,483 million and PLN 2,445 million of amounts denominated in foreign currencies as at 31 December 2005 and 31 December 2004, respectively. The primary foreign currency payable as at 31 December 2005 and 31 December 2004 relates to the acquisition of the UMTS concession and amounted to EUR 216 million and EUR 218 million, respectively.

Payment terms for trade and other capital expenditure payables are variable depending on contract terms, usually from 30 to 60 days.

17. Employee benefit plans

Certain employees and retirees of the Group are entitled to long-term employee benefits in accordance with the Group's remuneration policy (see Note 6(q)). These benefits are not funded. The changes in the defined benefit obligations related to employee benefits for 2005 and 2004 are detailed in the table below:

(in PLN millions)	Jubilee awards	Other post-employment benefits	Total	Jubilee awards	Other post-employment benefits	Total
			2005			2004
1 January	**318**	**160**	**478**	**320**	**143**	**463**
Service Cost	22	8	30	59	30	89
Interest Cost	11	7	18	21	10	31
Benefits paid	(31)	(10)	(41)	(40)	(10)	(50)
Actuarial losses	25	23	48	–	–	–
Release	(137)	(4)	(141)	(42)	(13)	(55)
31 December	**208**	**184**	**392**	**318**	**160**	**478**
Unrecognised actuarial losses	–	(23)	(23)	–	–	–
Benefit liability	**208**	**161**	**369**	**318**	**160**	**478**

A valuation of obligations as at 31 December 2004 was performed using a discount rate of 6% and a wage increase rate of 3%. As at 31 December 2005, the value of the related obligations was adjusted to reflect the status of the restructuring programme and the modifications to the Collective Bargaining Agreement. The discount rate was accordingly decreased to 5% in line with market conditions in Poland.

Service costs, actuarial losses and effects of the release are included in employee related expenses. The amount of the release in 2005 relates mainly to changes in the Collective Bargaining Agreement as negotiated by the Company in the third quarter 2005.

18. Provisions

(in PLN millions)	Provisions for litigation and other claims See Note 28	Restructuring provision	Dismantling provision	Provision for tax risk See Note 28 (c)	Total
1 January 2004	485	249	8	62	804
Additions	81	159	72	3	315
Discount	–	7	–	–	7
Utilisation	(4)	(250)	(4)	(6)	(264)
Release	(91)	(12)	(4)	(58)	(165)
31 December 2004	**471**	**153**	**72**	**1**	**697**
Short-term portion	471	153	7	1	632
Long-term portion	–	–	65	–	65
1 January 2005	471	153	72	1	697
Additions	402	1	90	6	499
Discount	–	–	6	–	6
Utilisation	(9)	(130)	(28)	(2)	(169)
Release	(147)	–	(1)	(1)	(149)
31 December 2005	**717**	**24**	**139**	**4**	**884**
Short-term portion	717	24	12	4	757
Long-term portion	–	–	127	–	127

Restructuring provision

The restructuring provision consists of the amount of termination benefits for employees scheduled to terminate employment in the Group under the employment-restructuring program. In 2004, the Management of the Company approved the continuation of the restructuring program increasing the present value of the restructuring provision to PLN 153 million as at 31 December 2004.

Dismantling provision

The dismantling provision relates to dismantling, removal or restoration of items of its property, plant and equipment. Based on environmental regulations in Poland items of property, plant and equipment which may contain hazardous materials should be dismantled and destroyed by the end of their useful lives by entities licensed by the State for this purpose. The costs of such dismantling may be higher than costs incurred in the past. As a result, the dismantling provision was increased by PLN 69 million in 2004 and by PLN 90 million in 2005 due to further reassessment of the Group's obligations. The related costs were capitalised in the value of property, plant and equipment.

19. Deferred income

(in PLN millions)	31 December 2005	31 December 2004
Grants	216	238
Prepaid services	483	522
Other	57	65
Total	**756**	**825**
Less: short-term portion	(410)	(423)
Long-term portion	346	402

Changes in grants were as follows:

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Beginning of period	238	257
Net amounts received	–	1
Amortisation	(22)	(20)
End of period	**216**	**238**

20. Income tax

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Current income tax	737	321
Deferred tax change*	(357)	388
Less: Deferred tax charged to equity	5	(9)
	385	**700**

* Deferred tax change for the twelve months ended 31 December 2005 and 2004 includes PLN 80 million and PLN 97 million, respectively, related to timing difference between the preparation of the IFRS consolidated financial statements and the filing of Corporate Income Tax declaration for 2004 and for 2003.

20. Income tax (continued)

The income tax on the Group's profit before tax differs from the theoretical amount that would arise using the tax rate enacted in Poland as follows:

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Profit before income tax	3,005	3,277
Statutory tax rate	19%	19%
Income tax calculated at statutory rate	571	623
Income and expenses not subject to income tax	21	106
Temporary differences*	(181)	(42)
Other	(26)	13
Income tax expense for the period	**385**	**700**

*Includes changes in unrecognised deferred tax asset

Expenses not subject to income tax consist of certain expense items, which, under Polish tax law, are specifically determined as non-tax deductible. The unrecognised deferred tax asset relates mainly to those tax losses, which are expected to expire before being realised and temporary differences, including these arising from investment in subsidiaries and associates, which based on the Group's management assessment would not be utilised for tax purposes. At 31 December, the unrecognised deferred tax asset relating to investments in subsidiaries and associates amounted to PLN 48 million and included mainly the impairment of financial investment in WP.

Deferred tax assets are recognised for tax losses carried forward to the extent that realisation of the related tax benefit through future taxable profits is probable. The Polish tax system has restrictive provisions for grouping of tax losses for multiple legal entities under common control, such as those of the Group. Thus, each of the Group's subsidiaries may only utilise its own tax losses to offset taxable income in subsequent years. Deferred tax assets are not recognised for losses the realisation of which is not probable. Tax losses are permitted to be utilised over 5 consecutive years with a 50% utilisation restriction for each annual tax loss.

Tax losses incurred by subsidiaries prior to 31 December 2005 expire as follows:

	(in PLN millions)
year of expiration:	
2006	325
2007	161
2008	144
2009	78
2010	29
Total	**737**

During the twelve months ended 31 December 2005 PTK Centertel utilised PLN 841 million of its tax losses reported in 2000-2001.

The net deferred tax liabilities/(assets) consist of the following:

(in PLN millions)	31 December 2005	31 December 2004
Deferred tax liabilities:		
Excess of book over tax value		
of property, plant and equipment and intangibles	712	758
Accrued income	286	467
Unrealised foreign exchange gains	–	169
Prepaid interest	192	269
Revaluation of financial assets	–	3
Embedded derivatives	1	2
	1,191	1,668
Offsetting deferred tax liabilities and deferred tax assets	(1,099)	(1,173)
Deferred tax liabilities after offsetting	92	495
Deferred tax assets:		
Unrealised foreign exchange losses	(114)	(292)
Accrued expenses	(460)	(374)
Unused tax losses of subsidiaries carried forward	(47)	(163)
Employee benefit plans	(63)	(85)
Excess of tax over book value of property, plant and equipment and intangibles	(187)	(245)
Bad debt provision	(18)	(57)
Deferred revenue	(93)	(88)
Restructuring provision	(4)	(29)
Impairment of financial investments	(147)	(2)
Other	(8)	(6)
	(1,141)	(1,341)
Offsetting deferred tax assets and deferred tax liabilities	1,099	1,173
Deferred tax assets after offsetting	(42)	(168)
Net deferred tax liability	**50**	**327**

Deferred tax liabilities on prepaid interest relates to interest paid by the Company in December 2003 and in July 2004 in the total amount of PLN 1,470 million to its subsidiaries TPSA Finance B.V. and TPSA Eurofinance B.V. in respect of interest due on bonds issued by the Company in 1998, 2000 and 2001. The interest on these bonds was initially scheduled to be paid from 2005 through 2008. In accordance with tax regulations in Poland, interest is deductible for corporate tax purposes when it is paid.

The decrease in the net deferred tax liability in 2005 included the recognition of deferred tax assets on costs previously disallowed for tax purposes and impairment of financial investments.

As at 31 December 2005 and 31 December 2004, deductible temporary differences, for which no deferred tax asset was recognised amounted to PLN 1,279 million and PLN 937 million, of which PLN 490 million and PLN 488 million respectively related to tax losses the realisation of which was not probable and PLN 789 million and PLN 449 million respectively related to other temporary differences, which based on the Group's management assessment would not be utilised for tax purposes.

21. Shareholders' equity

As at 31 December 2005, the share capital of the Company amounted to PLN 4,200 million and was divided into 1,400 million fully paid ordinary bearer shares of PLN 3 each. No changes were made in the number of shares in the twelve months ended 31 December 2005.

The ownership structure of the share capital as registered as at 31 December 2005 was as follows:

	% of votes	Nominal value (in PLN millions)
France Telecom S.A. ("France Telecom")	47.50	1,995
Bank of New York	9.98	419
State Treasury	3.87	163
Other shareholders	38.65	1,623
Total	**100.00**	**4,200**

Until 5 December 2005, Cogecom S.A., a subsidiary of France Telecom, was the parent company of Telekomunikacja Polska and had the right to dismiss and appoint the majority of the members of the Management Board of Telekomunikacja Polska. At that date, Cogecom S.A. and France Telecom were merged and all assets and liabilities of Cogecom S.A., including rights over Telekomunikacja Polska, were transferred to France Telecom S.A.

According to the Company's best knowledge, the Polish government declared that it will grant a priority purchase right to France Telecom S.A. in case of sale of its remaining share in the Company's capital in a public offer. Apart from the above, the Company has no information regarding other valid agreements that may result in changes in the proportions of shares held by the shareholders.

In accordance with the Corporate Code, amounts to be distributed among shareholders shall not exceed the profit for the last financial year increased by undistributed profits from previous years and by such amounts transferred from the supplementary capital and reserve capitals created out of profit which may be apportioned to the payment of dividend. These amounts shall be reduced by uncovered losses, own shares, and sums which under the law or under the company articles should be apportioned out of the last financial year's profit to the supplementary capital or reserve capitals. As at 31 December 2005, the Company's statutory shareholders' equity included revaluation reserve amounting to PLN 1,452 million which is not distributable.

Profit available for the distribution is the annual profit of Telekomunikacja Polska according to Polish Accounting Standards and approved by the General Shareholders' Meeting. In 2004, Telekomunikacja Polska paid a dividend of PLN 168 million (PLN 0.12 per share) in respect of 2003 profit. The net profit for 2004 amounted to PLN 1,671 million. A dividend of PLN 462 million (PLN 0.33 per share) in respect of 2004 profit was approved by the General Shareholders' Meeting on 26 April 2005.

22. Revenue

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Fixed line telephony services:	**9,794**	**11,095**
Subscriptions	4,249	4,064
Connections and similar charges	85	82
Voice traffic revenues	4,443	5,903
Interconnect revenues:	820	759
– LTOs and other licensed domestic operators	398	303
– Mobile telephony operators	92	106
– International incoming traffic	330	350
Payphone revenues	94	159
Other	103	128
Mobile telephony services	**5,773**	**4,950**
Subscriptions	1,423	1,761
Connections and similar charges	32	44
Voice traffic revenues	1,862	1,477
Interconnect revenues	1,500	1,073
Messaging services	829	525
Other	127	70
Data Services	**2,099**	**1,816**
Leased lines	383	377
Data transmission	509	462
Dial – up	230	405
Broadband revenues	977	572
Radio communications	272	262
Sales of goods and other	404	407
Total	**18,342**	**18,530**

Revenues are generated mainly in the territory of Poland. Approximately 2.4% and 3.2% of the total revenues for the twelve months ended 31 December 2005 and 2004, respectively, were received from entities which are not domiciled in Poland, mostly from interconnect services.

23. Other operating expenses, net

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Gain / (loss) on disposal of non financial fixed assets	(3)	21
(Impairment charge) / Reversal of impairment charge, net, on:		
– property, plant and equipment and intangible assets	(28)	(161)
– receivables	(252)	(468)
– other	(7)	1
Release of /(Increase in) provision for tax risk, net	(5)	22
Release of /(Increase in) restructuring provision, net	(1)	(147)
Release of /(Increase in) provision for litigation and other claims, net	(388)	(6)
Donations received	20	20
Fines and penalties receivable	117	145
Foreign exchange gains/(loses), net	56	163
Other operating revenue	232	262
Property taxes, non-recoverable VAT and other charges	(532)	(518)
Donations	(8)	(6)
Other operating expenses	(312)	(261)
Total	**(1,111)**	**(933)**

24. Financial income and charges, net

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Interest income	168	111
Income from derivative transactions	204	288
Release of provisions	1	41
Other financial income	49	170
Interest revenues and other financial revenue	**422**	**610**
Interest expense	(990)	(1,285)
Costs from derivative transactions	(299)	(260)
Increase in provisions	–	(41)
Commissions and other financial charges	(33)	(97)
Total interest expense and other financial charges	(1,322)	(1,683)
Interest expense and other financial charges, net	**(900)**	**(1,073)**
Foreign exchange gains / (losses), net	**124**	**562**

In the twelve months ended 31 December 2005 and 2004, interest expense included a non-cash discounting expense related to the valuation of long-term payables and provisions amounting to PLN 67 million and PLN 60 million, respectively.

25. Commitments

(a) Operating lease commitments

Lease commitments mainly relate to the lease of buildings, land, computer equipment and vehicles. Lease costs recognised in the consolidated profit and loss account for the twelve months ended 31 December 2005 and 2004 amounted to PLN 103 million and PLN 99 million, respectively. The majority of the above mentioned agreements is denominated in foreign currencies; some of the above agreements are indexed with price indices applicable for a given currency. Future minimum lease payments under non-cancellable operating leases, as at 31 December 2005, were as follows:

	(in PLN millions)
12 months ended 31 December:	
2006	157
2007	131
2008	104
2009	72
2010	41
Thereafter	136
Total minimum lease payments	**641**

(b) Capital commitments

Capital commitments contracted for at the balance sheet date but not recognised in the financial statements were as follows:

(in PLN millions)	31 December 2005	31 December 2004
Property, plant and equipment	527	526
Intangibles	99	188
Total	626	714
Amounts contracted to be payable within 12 months from the balance sheet date	617	663

Capital commitments represented mainly purchases of telecommunications network equipment, billing systems, a customer relationship management system and other software.

(c) Agreement with Danish-Polish Telecommunication Group ("DPTG")

Refer to Note 28 (e).

26. Related party transactions

As at 31 December 2005, France Telecom owned 47.5% of shares of the Company (see Note 21).

(a) Sales and purchases of goods and services

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Sales of goods and services to:		
– France Telecom Group	77	72
Purchases of goods and services from:		
– France Telecom Group	195	159

(in PLN millions)	31 December 2005	31 December 2004
Receivables from:		
– France Telecom Group	23	29
Payables to:		
– France Telecom Group	85	111

26. Related party transactions (continued)

The Group provides services to and receives services from France Telecom and other entities controlled by France Telecom on commercial terms. In the twelve months ended 31 December 2005 and 2004 France Telecom did not provide free of charge services to the Company in significant amounts.

In April 2005, PTK Centertel and Orange Brand Services Limited ("Orange") concluded a license agreement, on the basis of which PTK Centertel acquired rights to operate under the Orange brand. The brand was introduced by PTK Centertel in September 2005. The brand license agreement provided that Orange would receive a royalty fee of 1.6% of operating revenues for the full use of the Orange brand as well as access to the Orange roaming and interconnection arrangements, technology, advanced mobile handsets and consultancy services. Furthermore, Orange was to financially support the introduction of the brand in Poland by covering the communication costs.

In 2005, Telekomunikacja Polska has purchased shares in PTK Centertel from a subsidiary of France Telecom (see Note 2). In addition, there was a loan of PLN 1,000 million payable to France Telecom by Telekomunikacja Polska at 31 December 2005 (see Note 15(c)).

(b) Key management compensation

Key management relates to the Members of the Company's Management Board and to the Members of the Company's Supervisory Board. Total short-term benefits, including remuneration and bonuses (cash and benefits in kind), paid or payable to the Company's key management in the twelve months ended 31 December 2005 and 2004 amounted to approximately PLN 15 million and PLN 13 million, respectively.

In the twelve months ended 31 December 2005, approximately PLN 2 million were charged to the profit and loss account relating to post-employment or termination benefits of the Company's key management. In the twelve months ended 31 December 2004, approximately PLN 1 million was charged to the profit and loss account relating to post-employment or termination benefits of the Company's key management. The Group did not provide any share-based payment plans in the twelve months ended 31 December 2005 and 2004.

27. Segment reporting

The Group operates in two major reportable segments, fixed line telecommunications and mobile telecommunications. The two segments are strategic business units, each of which offers a different service.

Telekomunikacja Polska operates in the fixed line telecommunications sector where it provides local, long distance domestic and international public telephony services. In addition, Telekomunikacja Polska provides leased lines, radio-communication and other telecommunications value added services.

Mobile telecommunications services are provided by PTK Centertel, a provider of DCS 1800 and GSM 900 mobile telecommunications in Poland.

Other operations relate to the businesses of other companies of the Group. Other operations do not fulfil the conditions for reportable segments under International Accounting Standard No. 14 "Segment Reporting".

The Group operates in one geographical segment, the territory of the Republic of Poland.

The accounting policies are uniform for all segments. Transactions between segments take place on an arm's length basis. These transactions are eliminated on consolidation.

Basic financial data on the business segments is presented below:

	Fixed line telecommunications	Mobile telecommunications	Other	Eliminations	Consolidated
31 December 2005					
Segment assets	33,313	7,974	453	(6,161)	35,579
Investments accounted for using the equity method	–	–	3	–	3
Deferred tax assets	–	53	3	(14)	42
Total assets	33,313	8,027	459	(6,175)	35,624
Segment liabilities	15,467	4,896	340	(3,161)	17,542
Deferred tax liabilities	105	–	1	(14)	92
Total liabilities	15,572	4,896	341	(3,175)	17,634
31 December 2004					
Segment assets	32,679	7,530	420	(5,939)	34,690
Investments accounted for using the equity method	–	–	3	–	3
Deferred tax assets	–	175	7	(14)	168
Total assets	32,679	7,705	430	(5,953)	34,861
Segment liabilities	15,428	5,616	259	(3,818)	17,485
Deferred tax liabilities	498	–	–	(3)	495
Total liabilities	15,926	5,616	259	(3,821)	17,980
12 months ended 31 December 2005					
Sales:	12,496	6,424	243	(821)	18,342
inter-segment	216	497	108	(821)	–
external	12,280	5,927	135	–	18,342
Depreciation and amortisation	3,268	923	24	(4)	4,211
Operating result	2,350	1,506	(62)	(13)	3,781
Net profit / (loss)	1,450	1,042	(38)	(138)	2,316
Impairment charge on property, plant and equipment	(12)	–	3	–	(9)
Impairment charge on intangible assets	4	–	33	–	37
Capital expenditure	1,815	1,244	8	(21)	3,046
Net cash flow from:					
operating activities	6,025	2,204	(12)	5	8,222
investing activities	(4,957)	(1,194)	(187)	(910)	(7,248)
financing activities	(2,425)	(999)	216	901	(2,307)
12 months ended 31 December 2004					
Sales:	13,439	5,639	332	(880)	18,530
inter-segment	169	561	150	(880)	–
external	13,270	5,078	182	–	18,530
Depreciation and amortisation	3,566	830	38	(3)	4,431
Operating result	2,592	1,260	(72)	8	3,788
Net profit / (loss)	1,811	809	(89)	(225)	2,306
Impairment charge on property, plant and equipment	128	–	27	–	155
Impairment charge on intangible assets	(7)	–	13	–	6
Capital expenditures	2,224	1,050	16	–	3,290
Net cash flow from:					
operating activities	6,490	2,004	26	(8)	8,512
investing activities	(923)	(1,077)	(136)	(561)	(2,697)
financing activities	(4,102)	(1,061)	47	562	(4,554)

28. Contingencies

(a) Issues related to incorporation of Telekomunikacja Polska

Telekomunikacja Polska was established as a result of the transformation of the state-owned organisation PPTiT into two entities – the Polish Post Office and Telekomunikacja Polska. During the transformation process and transfer of ownership rights to the new entities, certain items of property and other assets that are currently under Telekomunikacja Polska's control were omitted from the documentation recording the transfer and the documentation relating to the transformation process is incomplete in this respect. This means that Telekomunikacja Polska's rights to certain properties may be questioned.

In addition, as the regulations concerning the transformation of PPTiT are unclear, the division of certain responsibilities of PPTiT may be considered to be ineffective, which may result in joint and several liability in respect of Telekomunikacja Polska's predecessor's obligations existing at the date of transformation.

The share premium in the equity of Telekomunikacja Polska includes an amount of PLN 713 million which in accordance with the Notary Deed dated 4 December 1991, relates to the contribution of the telecommunication business of PPTiT to the Company. As the regulations relating to the transformation of PPTiT are somewhat unclear, the division of certain rights and obligations may be considered to be ineffective. As a result, the share premium balance may be subject to changes.

(b) Environmental risk

The Group believes that its activities in respect of telecommunications services do not pose a serious threat to the environment. The Group's business does not engage in any production process which creates a significant threat to rare or non-renewable resources, natural resources (water, air, etc.) or to biodiversity.

The Group activities generate "non-household" waste for which recycling is closely controlled, such as: waste electronic equipment, electronics at end-of-life, batteries and storage cells, cables and treated poles.

Since 1998 the Company has implemented action plans aimed at the limitation of its impact on the environment and at maintaining compliance with Polish regulations on environment protection. In 2002 and 2003, the Company commissioned environmental audits which confirmed its compliance with Polish regulations and highlighted achievements in the field of limiting the impact on environment. To achieve improvements in the area of environmental protection the Group has established an on-going system for monitoring and reporting environmental impact. Dedicated regional teams were established to carry out on-going supervision regarding regulatory compliance, emission levels, as well as, to provide employees training in the area of environmental protection.

The Group has recorded the dismantling provision for obligations related to dismantlement, removal or restoration of items of its property, plant and equipment as required by the environmental regulations (see Note 18).

(c) Tax contingent liability

Tax settlements, together with other areas of legal compliance (e.g. customs or foreign exchange law) are subject to review and investigation by a number of authorities, which are entitled to impose severe fines, penalties and interest charges. The lack of reference to well established regulations in Poland results in a lack of clarity and integrity in the regulations. Frequent contradictions in legal interpretations both within government bodies and between companies and government bodies create uncertainties and conflicts. These facts create tax risks in Poland that are substantially more significant than those typically found in countries with more developed tax systems.

Tax authorities may examine the accounting records up to five years after the end of the year in which the final tax payments were to be made. Consequently, the Group may be subject to additional tax liabilities, which may arise as a result of additional tax audits. Telekomunikacja Polska and certain of its subsidiaries were subject to audits by the tax office in respect of taxes paid. Certain of these audits have not yet been finalised. The Group believes that adequate provisions have been recorded for known and quantifiable risks in this regard (see Note 18).

(d) Investigations by URTiP and UOKiK

According to the Telecommunications Act, the President of URTiP may impose on a telecommunications operator a penalty of up to a maximum amount of 3% of the operator's prior year's revenue, if the operator does not fulfil certain requirements of the Telecommunications Act. According to the amended Act on Consumer Protection and the Prevention of Monopolistic Practices, which came into force on 1 May 2004, in case of non-compliance with its regulations, the President of UOKiK is empowered to impose on an entity penalties of up to a maximum amount of EUR 50 million for refusal to provide requested information or up to a maximum amount of 10% of an entity's prior year's revenue for the breach of the law.

There are a number of proceedings against the Group initiated by URTiP and UOKiK. As at 31 December 2005 the Group recognised provisions for known and quantifiable risks related to these proceedings, which represent the Group's best estimate of the amounts, which are more likely than not to be paid. The actual amounts of penalties, if any, are dependant on a number of future events the outcome of which is uncertain, and, as a consequence, the amount of the provision may change at a future date. The information regarding the amount of the provision required to be disclosed by International Accounting Standard No. 37 "Provisions, Contingent Liabilities and Contingent Assets" has not been separately disclosed, as in the opinion of the Company's Management such disclosure could prejudice the outcome of the pending cases.

(e) Dispute with DPTG

On the basis of an agreement signed in 1991 between the Company's State-owned predecessor and the Danish Great Northern Telegraph Company, a predecessor of DPTG, a fibre optical link called North-South Link ("NSL") connecting the northern and southern Polish borders was commissioned and constructed. Ownership rights to this investment were transferred to the Company on commissioning and DPTG was granted 14.8% of the net profit from the cable during a period of 15 years starting in 1994. The Company is responsible for the maintenance of the cable and is required to maximise the data flow through the cable.

In March 2001, DPTG requested termination or renegotiation of the contract as the traffic accounted for by the Company had been decreasing since 1999. As the Company did not accept the suggested terms of termination or renegotiation of the agreement, DPTG claimed arbitration under terms of the agreement and demanded that the Company pay an estimated amount of EUR 280 million. During the arbitration proceedings, DPTG's claim was reduced to EUR 218 million plus interests for the period ended June 30, 2002. In addition, DPTG filed a petition to the Arbitration Court to determine the amount of payments due for the period thereafter, ending in January 2009.

In the course of the proceedings, the Arbitration Court appointed an independent telecommunication expert to model the relevant NSL traffic volume and to calculate related revenues. In November 2005, the expert presented a preliminary opinion, which included a model to be used to determine the relevant NSL traffic volume and to calculate related revenues. The model, if used by the Arbitration Court in the proceeding, may result in a liability higher than that expected so far by the Company. However, the assumptions used by the expert to develop the model are challenged by the Company. On February 9, 2006, the Company asked for a supplementary pre-report from the expert and for the opportunity to present its comments on such report once issued. On the same date, based on the expert's model and its own adjustments, DPTG submitted a new claim of EUR 670 million plus interests, for the period ended June 30, 2005.

Based on the new facts and circumstances, the Company reassessed its exposure in respect of the above issue and updated as of December 31, 2005 the amount of the provision recognised in previous periods. The outcome of the arbitration proceedings depends on a number of future events the outcome of which is uncertain and, as a consequence, the amount of the provision may change at a future date.

The information regarding the amount of the provision required to be disclosed by International Accounting Standard No. 37 "Provisions, Contingent Liabilities and Contingent Assets" is not presented on the grounds that it could prejudice the outcome of the litigation.

(f) Options

Contingent liabilities related to options are described in Note 30.

(g) Other contingent liabilities

Apart from the above mentioned, the Group is a party to a number of legal proceedings and commercial contracts related to its operational activities. The Group believes that adequate provisions have been recorded for known and quantifiable risks in this respect.

29. Financial risk management

The Group's activities expose it to certain financial risks. The principal group of financial instruments consists of bonds, bank loans and cash and cash equivalents which serve the purpose of securing adequate financing for the Group's operations. The other group of financial instruments consists of financial derivatives, whose primary function is to offset the financial risks brought about by the principal group. The remaining financial instruments, as trade payables and trade receivables, arise directly from the Group's operations.

Financial risk management is co-ordinated by the TP Group Finance Branch (PFGK) according to the policies approved by the Chief Financial Officer. PFGK identifies, evaluates and hedges financial risks in close co-operation with the Group's entities. The principles for overall financial risk management which concern such areas as foreign exchange risk or liquidity risk are provided in the written policies. The Group policy is to hedge at least 90% of its financial foreign exchange risk exposure.

The primary hedging instruments used by the TP Group are 1) cross currency swaps, currency options and forwards for reducing the foreign exchange risks and 2) interest rate swaps and FRA contracts for hedging the exposure to interest rates fluctuations. The Group classifies some of its derivatives (i.a. interest rate swaps) as non-hedging for accounting purposes due to the fact that not all of the formal requirements in respect to the documentation for hedge accounting could be met (see Note 30).

Foreign exchange risk
The Group's exposure to market risk for changes in foreign exchange rates relates primarily to the long-term interest bearing liabilities, including bonds and bank loans as well as to the UMTS concession payable. At the end of the fourth quarter 2005, 94.4% of foreign exchange risk attributable to bank loans and bonds was economically hedged via cross currency swaps, forwards contracts and foreign exchange currency cash holdings. Additionally, the Group has economically hedged 100.0% of payments related to UMTS concession.

Interest rate risk
The Group's exposure to market risk for changes in interest rates relates primarily to long-term interest bearing liabilities, including bonds and bank loans. At the end of 2005, 69.4% of TP Group debt after economical hedge is based on fixed rate.

Liquidity risk
The Management of the Company believes that the liquidity of the Group remains secure in the foreseeable future. As at 31 December 2005, the current liabilities of the Group exceeded its current assets by PLN 4,332 million. In the twelve months ended 31 December 2005, the net cash inflows from the Group's operating activities amounted to PLN 8,222 million. Additionally, based on arrangements made with banks, the Group has the unutilised bank loans facilities amounting to PLN 2,172 million as at 31 December 2005.

Credit risk
There are no significant concentrations of credit risk within the Group.

Price risk
Pursuant to the Polish telecommunication law (see Note 1), prices for the telecommunication services should be based on transparent and objective criteria. Detailed conditions are set for all significant types of the services. Consequently, specific requirements relating to regulatory accounting and cost calculations are defined for SMP operators. Certain charges have to be approved by URTiP before they are applicable and price increases have to be announced minimum one settlement period in advance. In addition, cost calculations of an SMP operator are subject to URTiP audit and approval. If prices of certain services are assessed to be inconsistent with the law, URTiP may adjust charges, taking into account their level on similar markets ('benchmarks').

The Group believes that it fulfils all requirements in relation to regulatory accounting and cost calculations as stipulated in the telecommunication law.

30. Financial instruments

The fair value of cash and cash equivalents, receivables, short-term financial assets and current loans, borrowings and other payables approximates the carrying amounts reported in the balance sheet due to the relatively short-term maturity of these financial instruments. The fair value of non-current financial assets as well as loans, borrowings and other payables with variable interest rates approximates their carrying amounts. The carrying amount of the telecommunication concession payable approximates its fair value. As at 31 December 2005 and 31 December 2004 the fair value of non-current loans, borrowings and other payables with fixed interest rates, including telecommunication concessions payable, amounted to PLN 9,089 million and PLN 9,878 million, respectively (carrying amount: PLN 8,004 million and PLN 8,683 million, respectively).

The derivative financial instruments used by the Group are presented below:

31 December 2005		**Principal (millions)**		**Interest**			**Fair value (PLN millions)**	
Type of instrument[1]	Hedged item	Receive	Pay	Receive	Pay	Maturity	Financial Asset	Financial Liability
Fair value hedge								
CCIRS[2]	Bank borrowings	4 USD	17 PLN	1.25%	6M WIBOR-3.11%	2008	–	(3)
CCIRS	Bonds	775 USD	3,051 PLN	7.75% to 7.8644%	6M WIBOR+1.75% to 6M WIBOR+5.60%	2008	–	(625)
CCIRS[3]	Bank borrowings	42 EUR	175 PLN	3M EURIBOR	3M WIBOR-1.02% to 3M WIBOR-0.6%	2008	–	(20)
CCIRS	Bonds	675 EUR	2,823 PLN	6.5% to 6.6875%	6M WIBOR+1.59% to 6M WIBOR+4.08%	2006 - 2007	21	(159)
CCS	Bonds	10 EUR	42 PLN	–	6M WIBOR-3.92%	2011	–	(2)
Cash flow hedge								
CCIRS[4]	Bank borrowings	62 EUR	293 PLN	3.81% or 3M EURIBOR	4.52% to 7.81%	2006 - 2008	–	(72)
CCIRS[5]	Bonds	237 EUR	873 PLN	4.625% to 6.6875%	5.03% to 14.78%	2006 - 2008	80	(54)
CCS[6]	Bank borrowings	44 EUR	192 PLN	–	2.91% to 3.09%	2012	–	(33)
CCS	Bonds	130 EUR	549 PLN	–	1.57% to 2.95%	2011	12	(83)
IRS	Bank borrowings	337 PLN	337 PLN	3M WIBOR - 0.17%	6.89% to 6.99%	2012	–	(24)
Trade								
CCIRS	Other	110 EUR	422 PLN	3M EURIBOR	3M WIBOR-1.35% to 3M WIBOR+1.56%	2006 - 2012	18	(26)
CCIRS	Bonds	25 USD	75 PLN	7.75%	6M WIBOR +2.98%	2008	0	–
CCS	Other	2 EUR	9 PLN	0.8%	PLN 1 mln quarterly	2008	–	(3)
IRS	Other	4,786 PLN	4,786 PLN	3M WIBOR to 6M WIBOR	5.24% to 6.95%	2007-2008	–	(114)
NDF	Other	390 EUR	1,580 PLN	–	–	2005-2006	2	(68)
FWD	Other	62 EUR	254 PLN	–	–	2006	–	(14)
Total of fair value								
Swap contracts							**131**	**(1,218)**
NDF							**2**	**(68)**
FWD							**–**	**(14)**
Total							**133**	**(1,300)**

[1] CCIRS – cross currency interest rate swap, CCS – cross currency swap, IRS – Interest rate swap, FWD – currency forward, NDF – non-deliverable forward
[2] Interest is calculated based on notional amounts of USD 23 million and PLN 86 million as modified by the payment schedule
[3] Interest is calculated based on notional amounts of EUR 119 million and PLN 505 million as modified by the payment schedule
[4] Interest is calculated based on notional amounts of EUR 121 million and PLN 568 million as modified by the payment schedule
[5] Including EUR 42 million which constitutes hedging of coupon payments only on bond series T
[6] Interest is calculated based on notional amounts of EUR 44 million and PLN 192 million as modified by the payment schedule

30. Financial instruments (continued)

31 December 2004		Principal (millions)		Interest			Fair value (PLN millions)	
Type of instrument[1]	Hedged item	Receive	Pay	Receive	Pay	Maturity	Financial Asset	Financial Liability
Fair value hedge								
CCIRS[2]	Bank borrowings	6 USD	22 PLN	1.25%	6M WIBOR-3.11%	2008	–	(9)
CCIRS	Bonds	775 USD	3,051 PLN	7.75% to 7.8644%	6M WIBOR+1.75% to 6M WIBOR+5.60%	2008	–	(798)
CCIRS[3]	Bank borrowings	56 EUR	233 PLN	3M EURIBOR	3M WIBOR-1.02% to 3M WIBOR - 0.6%	2008	1	(28)
CCIRS	Bonds	585 EUR	2,465 PLN	6.5625% to 6.6875%	6M WIBOR+1.59% to 6M WIBOR+3.88%	2006 - 2007	93	(82)
CCS	Bonds	10 EUR	42 PLN	–	6M WIBOR – 3.92%	2011	0	(1)
IRS	Bonds	200 PLN	200 PLN	7.25%	6M WIBOR+1.71%	2005	–	(2)
Cash flow hedge								
CCIRS[4]	Bank borrowings	129 EUR	601 PLN	3.81% or 3M EURIBOR	4.52% to 8.60%	2005 - 2008	–	(94)
CCIRS	Bonds	251 EUR	934 PLN	4.625% to 6.6875%	5.03% to 14.78%	2006 - 2008	106	(39)
CCS	Bank borrowings	44 EUR	192 PLN	–	2.91% to 3.09%	2012	–	(19)
CCS	Bonds	80 EUR	350 PLN	–	2.74% to 2.95%	2011	–	(37)
CCS	Other	3 EUR	11 PLN	0.8%	PLN 1 mln quarterly	2008	–	(3)
IRS	Bank borrowings	389 PLN	389 PLN	3M WIBOR - 0.17%	6.89% to 6.99%	2012	–	(15)
Trade								
CCIRS	–	133 EUR	516 PLN	3M EURIBOR	3M WIBOR – 1.345% to 3M WIBOR+1.56%	2006 - 2012	39	(26)
CCIRS	–	25 USD	75 PLN	7.75%	6M WIBOR +2.98%	2008	–	(7)
IRS	–	4,044 PLN	4,044 PLN	3M WIBOR to 6M WIBOR	6.28% to 6.95% or 6M WIBOR - 0.19% to 6M WIBOR+0.05%	2006 -2008	15	(16)
CCS	–	18 EUR	24 USD	–	–	2005	(0)	–
Options	–	150 EUR	–	–	–	2005	1	–
Total of fair value								
Swap contracts							**254**	**(1,176)**
Options							**1**	**–**
Total							**255**	**(1,176)**

(1) CCIRS – cross currency interest rate swap, CCS – cross currency swap, IRS – Interest rate swap, FWD – currency forward, NDF – non-deliverable forward
(2) Interest is calculated based on notional amounts of USD 25 million and PLN 92 million as modified by the payment schedule
(3) Interest is calculated based on notional amounts of EUR 133 million and PLN 564 million as modified by the payment schedule
(4) Interest is calculated based on notional amounts of EUR 187 million and PLN 877 million as modified by the payment schedule

The change in fair value of cash flow hedges charged to equity is presented below:

(in PLN millions)	12 months ended 31 December 2005	12 months ended 31 December 2004
Beginning of period	**(78)**	**(116)**
The effective part of the gain/loss on hedging instrument	(107)	(307)
The amounts transferred to the profit and loss account	89	354
Deferred tax effect	4	(9)
End of period	**(92)**	**(78)**

In 2005, the Group was a party to the following put and call option arrangements:

(a) Put and call options issued to/acquired from the shareholders of WP

On 26 October 2001, TP Internet issued a put option to the minority shareholders of WP ("WP minority shareholders"). Under the terms of this option, TP Internet was obliged to acquire all shares of WP held by the WP minority shareholders. This put option could be exercised from 1 June 2005 to 1 June 2006 under certain conditions. TP Internet also acquired a call option issued by the WP shareholders to acquire the WP shares held by the WP minority shareholders.

On 9 April 2004, the District Court in Gdańsk declared Wirtualna Polska bankrupt due to its insolvency. Under the settlement with WP minority shareholders of 21 July 2005, the Group acquired the remaining 19.54% of WP shares for PLN 221 million. As a result, all options related to WP shares expired. On 8 September 2005, the District Court in Gdańsk terminated the proceedings in bankruptcy with respect to WP. As a result of the above, the Group has regained control over WP (see also Note 2).

31. Subsequent events

(a) Loan agreement

On 20 February 2006, TP S.A. concluded a revolving loan agreement ("the Agreement") for the total amount of PLN 2,500 million with a syndicate of nineteen banks. The purpose of the Agreement is to finance TP S.A.'s current liquidity management, including bond redemption totalling EUR 500 million par. The loan interest is based on the WIBOR rate for the relevant interest periods plus a bank's margin. The ultimate maturity date of the loan falls five years after the date of the Agreement.

(b) Bonds redemption

On 1 March 2006, TPSA Eurofinance B.V., a TP S.A.'s subsidiary, redeemed at maturity five-year debt securities totalling EUR 500 million that had been issued on 1 March 2001.

Independent Auditor's report

"To the shareholders of Telekomunikacja Polska S.A.

1 We have audited the attached consolidated financial statements[1] of Telekomunikacja Polska Capital Group ('the Group'), for which the holding company is Telekomunikacja Polska S.A. ('the Company') located in Warsaw at 18 Twarda St., for the year ended 31 December 2005, containing:
   - the consolidated balance sheet as at 31 December 2005 with total assets amounting to 35,624 million zlotys,
   - the consolidated profit and loss account for the period from 1 January 2005 to 31 December 2005 with a net profit amounting to 2,620 million zlotys,
   - the consolidated cash flow statement for the period from 1 January 2005 to 31 December 2005 with a net cash outflow amounting to 1,331 million zlotys,
   - the consolidated statement of changes in shareholders' equity for the period from 1 January 2005 to 31 December 2005 with a net increase in shareholders' equity amounting to 890 million zlotys and
   - the additional notes and explanations ('the attached consolidated financial statements').

2 The truth and fairness of the attached consolidated financial statements and the proper maintenance of the consolidation documentation are the responsibility of the Company's Management Board. Our responsibility was to audit the attached consolidated financial statements and to express an opinion whether, based on our audit, these financial statements are, in all material respects, true and fair.

3 We conducted our audit of the attached consolidated financial statements in accordance with the following regulations being in force in Poland:
   - with International Standards on Auditing,
   - with the following regulations being in force in Poland:
     - chapter 7 of the Accounting Act, dated 29 September 1994 ('the Accounting Act'),
     - the auditing standards issued by the National Chamber of Auditors,

   in order to obtain reasonable assurance whether these financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the attached consolidated financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by Management Board, as well as evaluating the overall presentation of the attached consolidated financial statements. We believe our audit has provided a reasonable basis to express our opinion on the attached consolidated financial statements treated as a whole.

4 In our opinion, the attached consolidated financial statements, in all material respects:
   - present truly and fairly all information material for the assessment of the results of the Group's operations for the period from 1 January 2005 to 31 December 2005, as well as its financial position as at 31 December 2005;
   - have been prepared, in all material aspects correctly, i.e. in accordance with International Financial Reporting Standards as adopted by the EU;
   - are, in respect of the form and content, in accordance with the legal regulations governing the preparation of financial statements.

5 Without qualifying our opinion, we draw attention to the following:
   - As more fully explained in notes 28 (d) and 28 (e) to the consolidated financial statements the Company is a party to a number of legal and administrative proceedings. To the extent the obligations in respect of these proceedings could be reliably measured the Company has made provisions in this respect, which represent the Company's best estimate of the amounts that according to the Company's Management Board are more likely than not to be paid. The amount of the liabilities depends on a number of future events, the outcome of which is uncertain and as a consequence the amount of the provisions may change at a future date.

6 We have read the 'Directors' Report[2] for the period from 1 January 2005 to 31 December 2005 and the rules of preparation of annual statements' ('the Directors' Report') and concluded that the information derived from the attached consolidated financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with the relevant regulations of the Decree of the Minister of Finance of 19 October 2005, on current and periodic information published by issuers of securities (Journal of Law No. 209, item 1744)."

On behalf of
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Certified Auditor
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Member of Management Board
Certified Auditor
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Warsaw, March 27, 2006

1 as presented on pages 33 - 70
2 as included in the filed financial statements for Warsaw Stock Exchange

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Glossary

ADSL
see xDSL

ARPU
Monthly Average Revenue Per User

Audiotex
A voice processing application allowing callers to select from a menu of options using the telephone keypad (e.g. automated ticket booking services).

Broadband
High-speed voice, data and video networked services that are digital, interactive and packet-based.

Capex
Book value of capital expenditures

CRM
Customer Relationship Management.
A central database system or set of systems enabling a company to manage, analyse and utilise customer data.

DCS
Digital Cellular System.
A global system for mobile communications – it is used in Europe and Asia-Pacific.

DLD
Domestic Long Distance

EBITDA
Operating profit plus amortisation and depreciation

EDGE
Enhanced Data-rates for Global Evolution. A system for increasing data transmission rates within existing GSM bandwidth. EDGE is part of the evolution towards UMTS; an advance on "2.5G" GPRS, it is sometimes referred to as "2.75G".

F2M
Fixed to Mobile

Free cash flow before financing
Cash flow from operating activities minus purchase of tangible and intangible assets minus interest paid net.

Free cash flow margin before financing
Free cash flow before financing and revenues

GPRS
General Packet Radio System. System to improve the efficiency of current mobile networks by transmitting data in "packets" of bytes which are then reassembled at the user's end. GPRS enables "always on" connections which effectively allow the mobile terminal to become part of the Internet.

GSM
Global System for Mobile Communication. The most widely-used set of mobile telecom standards in Europe. Falls into the category of "second generation" mobile services.

ILD
International Long Distance

IP-VPN
Internet Protocol Virtual Private Network.
IP represents the network layer underlying all Internet communication. Network operators offer VPNs as a means of enabling customers to interconnect sites and users in a virtual network without needing to invest in direct physical links between sites or having to build a network of their own.

ISDN
Integrated Services Digital Network. An international communications standard which enables voice, video and data transfer at rates of 64Kb per second over normal or digital telephone lines.

KPI
Key Performance Indicator

MVNOs
Mobile Virtual Network Operators

NTP
New Tariff Plans

Opex
Operating Expenditure (Total operating costs)

PAS
Polish Accounting Standards

PLN
Polish złoty

POTS/PSTN line
Plain Old Telephone Service. Standard analogue telephone service using copper wires.

SAC
Subscriber Aquisition Costs

SDI
A system which allows "always on" internet access via standard telephone lines.

SMS
Short Messaging Service. Allows users to send short text messages to other mobile phones.

UMTS
Universal Mobile Telecommunications System – GSM-based 3G (Third Generation) technology

URTiP
Polish Telecommunications & Post Regulator (in 2006 renamed into UKE- Office of Electronic Communications)

VoIP
Voice over Internet Protocol. Technology used to transmit voice conversations over a data network using the Internet Protocol.

VPN
Virtual Private Network.
A private network of computers or mobile phones – usually in a business or other large organisation – which is at least partially connected by public telephone lines.

Wi-Fi
Short for 'wireless fidelity' used for certain types of local area network.

WLAN
Wireless Local Area Network. A wireless LAN is one in which a mobile user can connect to a local area network through a wireless (radio) connection.

xDSL
Collective description for a range of Digital Subscriber Line technologies. These systems use modulation schemes to pack data onto existing copper telephone lines (POTS). This speeds up data transfer between a telephone switching station and a home or office.

Certain of the statements contained in this report that are not historical facts, are statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those in such statements due to, among other factors, (i) changes in the competitive and regulatory framework in which our companies operate, (ii) changes in exchange rates, including particularly the exchange rate of the PLN to the US dollar and Euro, (iii) changes in economic or technological trends, (iv) customers and market concentration, and (v) general competitive and market factors on a global, regional and/or national basis. We have no obligation to update these statements.

None of the Company or any of its affiliates, advisors or representatives shall have any liability whatsoever (in negligence or otherwise) for any loss howsoever arising from any use of this document or its contents or otherwise arising in connection with the document.

Any decision to transact TP's securities should be made solely on the basis of information officially reported in accordance with the appropriate securities regulations.

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The TP Management Board is committed to creating and sustaining a meaningful dialogue with the investment community. TP has therefore undertaken to offer its shareholders the following services:

- access to company management at regular investor roadshows;
- a timely flow of news and information through our website and via email alerts;
- the opportunity to give feedback through regular third-party perception audits;
- convenient access to the IR team in Warsaw via phone and email.

Your comments and suggestions help us to improve the communication process, so don't hesitate to get in touch. You can also keep up to date with the latest news and results by visiting our IR web pages at www.tp-ir.pl

Enlarged consolidated quarterly reports
Q1'06 May 12, 2006
Q2'06 August 11, 2006
Q3'06 November 14, 2006
Q4'06 March 1, 2007

Consolidated enlarged half year report
H1'06 August 31, 2006

Full year results 2006
March 30, 2007

Consolidated full year results 2006
March 30, 2007

These dates represent the latest publication date in each case and results may be published earlier.

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