TP Group
Annual Report 2006

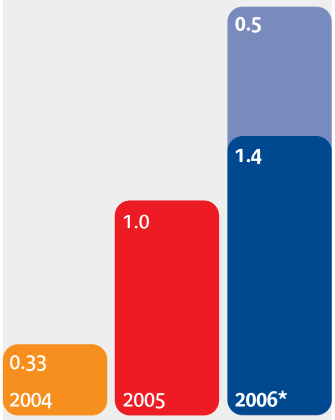
Our world, your world

TP Group at a Glance

TP Group is Poland's leading telecommunications provider. We have operations in fixed-line voice, data and mobile networks. TP Group is 47.5% owned by France Telecom. In 2006 we achieved revenues of PLN 18.6bn and a net income of PLN 2.1bn*.

Dividends per share
PLN

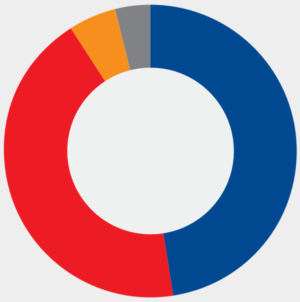
*The Company intends to recommend for the shareholders approval a cash distribution of PLN 1.9 per share, consisting of:
– PLN 1.4 per share payable in cash and
– an additional, exceptional cash distribution of PLN 0.5 per share in a form to be determined. More details are available in the CFO's statement on page 18.



TP Share price vs WIG 20
2005-2007

TP Group share capital structure
2006

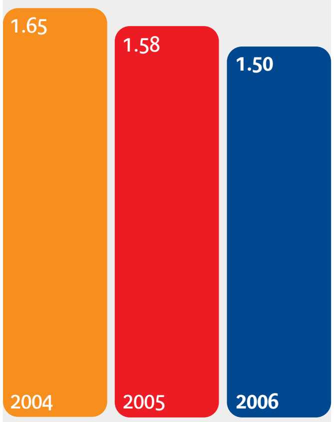
France Telecom	47.50%
Other shareholders	43.61%
GDR holders represented by Bank of New York*	5.02%
State Treasury**	3.87%



* attributable to shareholders of the parent company

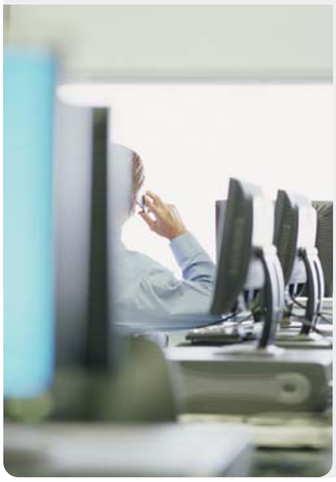
* Data as officially reported by the Bank of New York on 25 September 2006.
** The figures presented correspond to the number of shares registered by the State Treasury at the Extraordinary Meeting of Shareholders held on 9 November 2006.

Earnings per share
PLN
2005 Restated for IFRS.



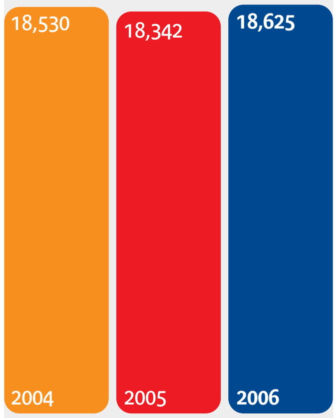
Revenue by segment
PLN mn

Fixed
11,869



Mobile
7,532

Group Revenues
PLN mn



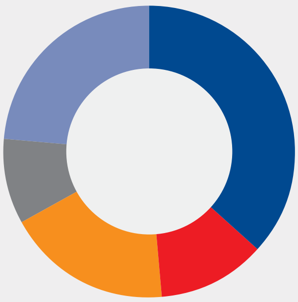
TP Group revenue composition

2005

Mobile	31.5%
Data	11.4%
Fixed-line traffic	25.3%
Interconnect & other*	8.3%
Access fees	23.5%

2006

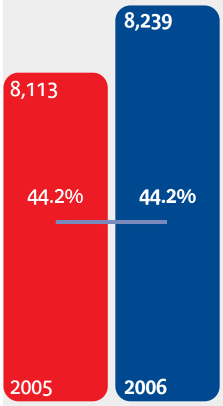
Mobile	36.8%
Data	12.0%
Fixed-line traffic	18.4%
Interconnect & other*	9.2%
Access fees	23.6%



Gross Operating Margin
PLN mn

GOM Rate

2005 Restated for IFRS.



* Including: Fixed-line interconnect, payphone, radio, telecommunications, sales of goods and other revenue.

Contents

TP Group kept to a steady course in 2006, steering through challenging market conditions to meet its operational objectives and deliver real returns for shareholders.

We defended our market share in the fixed-line business, doubled our broadband customer base and gained the number one position in the mobile market with the Orange brand. Against a challenging regulatory environment the Company has supported a competitive telecoms market while continuing to develop an extensive, high-quality network.

Strong financial results show that our strategy is on track and we have established a solid base for sustainable future performance.

TP Group Financial and Operational Highlights 2006

All figures in PLN according to IFRS

Revenue	Broadband customers
18.6bn	**1.7mn**
+1.5%	**+46.8%**

Gross Operating Margin	Mobile customers
44.2%	**12.5mn**
Maintained	**+26.2%**



President's letter to shareholders

Maciej Witucki
President of the Board and Chief Executive Officer

Dear Shareholders,
It's a great pleasure to be addressing my first letter to TP Group shareholders.

2006 highlights

My first three months at the Company have reinforced my belief that TP is a profitable, resilient and innovative organisation. Excellent results across the business in 2006 show the quality of management in place at all levels of the business and prove that our strategy to date has been on track. Through continued focus on top-line growth, innovative offers and tighter cost controls we met or exceeded all our operational objectives for the year.

We launched a number of new products on schedule and ended the year in pole position in both the mobile and Internet markets. The rebranding of our mobile services to Orange gave us the extra momentum to increase our mobile subscriber base by 26% to over 12.5 million by the end of 2006, while in broadband our 'triple play' offer and attractive promotions for 'Neostrada' helped us record an increase to the customer base of over 46% compared to the year before. We continued the Group restructuring and saw the first savings through TP and PTK Centertel synergies. Sharing common IT platforms and customer service systems across the Group does not only enable us to introduce integrated offers: it has already started to deliver substantial cost savings and enhance the user experience.

Operational successes translated into strong financial performance, with average gross operating margin (GOM) for 2006 standing slightly above our guidance at 44.2% and net free cash flow very strong, ending the year at over PLN 4.1 billion.

None of this success would have been possible without the loyalty and commitment of the TP Group workforce. In my short time at the Company so far I have been very much impressed by our people; their response to the challenges we continue to face is key to TP Group's future. I am sure that all our shareholders will join me in thanking all staff for their hard work so far. In addition, I would personally like to thank the employee representatives for engaging so constructively in the successful renegotiation of TP Group's Social Agreement.

Dividend

In determining TP Group's cash allocation policy the Management Board aims to balance three objectives: firstly, to maintain the flexibility we need to sustain profitable development of the Group by investing in both organic growth and potential strategic acquisitions in the region; secondly, to maintain the financial discipline required to support our current ratings; and thirdly, but no less importantly, to offer attractive remuneration to shareholders. Taking into account the uncertain regulatory environment and intensifying competition, the Management Board has recommended that shareholders should approve an ordinary dividend of PLN 1.4 per share which sets the bar for our dividend policy going forward. The dividend will be explained in more detail in the financial section later in this report.

Looking ahead

Our commercial and financial achievements in 2006 clearly demonstrate the adaptability of our business model in a highly competitive market and under intensifying regulatory pressure. The long process of transformation that has taken TP Group from traditional fixed voice operator to modern, customer-focused telecom access provider has given us a solid base for further development. However, the current challenging market conditions show no sign of easing. That is why the first initiatives I have taken as incoming President and CEO have been aimed at developing a more aggressive sales culture, in order to leverage TP's customer base as we expand our convergent offers. Hand in hand with this sales drive, we must redouble our efforts to improve levels of customer satisfaction.

In parallel, I am looking to further optimise the Group's cost structure by exploiting powerful integration drivers such as information systems. The rationalisation and integration of corporate and support functions across the Group will continue, as will the consolidation of sales and distribution, enabling us to take full advantage of synergies between the fixed and mobile businesses. To support these changes, a new structure of the management organisation was introduced in March 2007. In addition to the Management Board, an Executive Committee was created to oversee the day-to-day operational management. And thirdly, I want to see continuing improvements to the flexibility of our employment base while we become more selective than ever in our resource allocation. Our detailed strategy for 2007-2010 will be communicated at the end of the first half of 2007.

Regulatory challenges notwithstanding, and although the downward pressure on fixed-line revenues will continue to intensify, I am confident that the next few years will see an exciting phase in the development of the Polish telecoms market. There is untapped growth potential in the broadband market and room for growth too in mobile, where penetration still has some way to go to reach the saturation levels we see in Western Europe. TP Group's successful defence of its position in these dynamic market conditions depends on getting the customer offer right. Our services must be pragmatically priced and pegged to consumer spending power. We must continue to foster strong brand recognition and loyalty – particularly in leveraging the power of the Orange brand – which has had a hugely successful first year in Poland achieving the number one position by market share in 2006. And in the key business market, we must stay ahead of the curve by continuing to make our offer more flexible and more tailored with an emphasis on integrated offers and value-added services.

Lastly, let me reiterate TP Group's commitment to an open Polish telecoms market and fair competition. In 2007 and beyond we will continue to co-operate with those competitors who share our vision and priorities for the market, recognising the value of continued investment in a strong telecoms infrastructure.

Maciej Witucki
President of the Board and
Chief Executive Officer
31 March 2007

Market climate

During the last few years, the industry environment in which we operate has become significantly more demanding. The regulatory environment has evolved considerably and the market has become a good deal more competitive as a result. At the same time, the sector has grown in value, (based on turnover) up from €9.5 billion in 2005 to €10 billion in 2006 (source: Eurostat, IDC, Central Statistical Office).

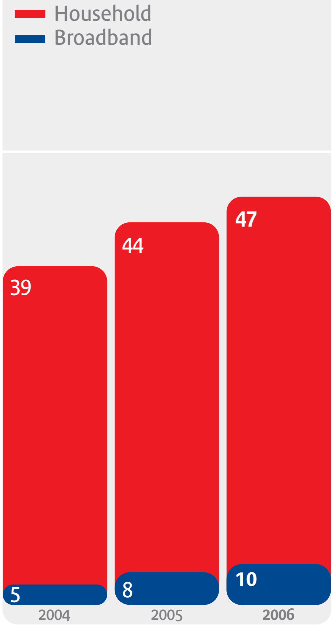
The Polish economy remains in good shape with GDP growth at 5.8% for 2006. Inflation is expected to remain well contained over the coming quarters, which should allow the Monetary Policy Council to retain its focus on growth. In addition, the National Bank of Poland forecasts double-digit investment growth and a pick up in GDP over the coming quarters. We share the view that GDP growth will remain robust in 2007 – 2008.

Unemployment in Poland is still the highest in the EU, but the trend is clearly downward. At the end of November 2006, the unemployment rate was 14.8%, compared to 17.3% twelve months earlier. Medium-term forecasts indicate further positive developments in the labour market, which should support further growth in consumers' purchasing power and boost telecom spending.

Fixed-to-mobile substitution is a major ongoing trend, particularly in Central and Eastern Europe where the fixed-line network was comparatively underdeveloped when mobile telephony was introduced. In Poland, we estimate that early in 2006 the effective minute rate charged for mobile calls dropped below the fixed-line rate in the mass market for the first time, fuelling further substitution. By September 2006, 23% of all households in Poland had a mobile phone only, as compared to some 14% in July 2005.

With 38 million inhabitants and 12 million households, with low broadband penetration, with its mobile market not yet saturated and usage per capita still far behind most EU countries, Poland offers substantial development opportunities to TP Group. Given healthy macro-economic conditions, disposable income will increase, presenting additional opportunities to grow value-added services in both the mobile and fixed-line sectors.

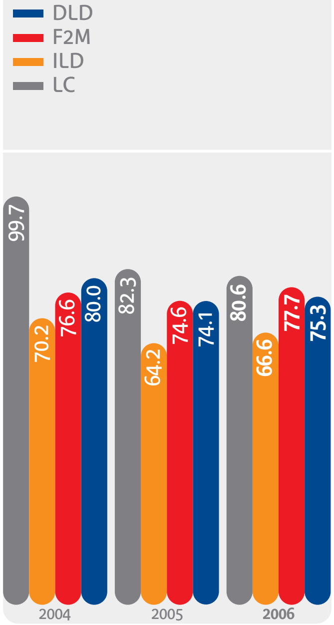
PC and broadband penetration per household
%



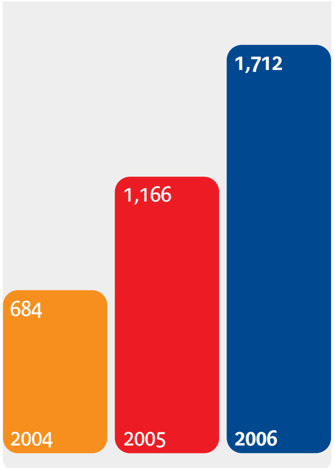
Fixed-line

Poland's fixed-line market was the scene for intense competition in 2006, with the evolution towards convergent offers; in particular, several cable TV operators launched 'triple-play' packages (TV, fixed-line voice and Internet access). Ongoing tariff reductions in the mobile market accelerated the pace of fixed-to-mobile substitution, increasing pressure on TP's fixed-line revenues. Despite several key regulatory decisions in retail and wholesale market and despite the decrease in fixed-line traffic during the year, TP has managed to maintain local call market share and even to increase it in F2M, international and long-distance markets. What is more important, TP has maintained high profitability in the fixed-line business thanks to tight cost controls: Gross Operating Margin in the fixed-line segment showed an improvement at 46.9%, up from 44.9% a year earlier.

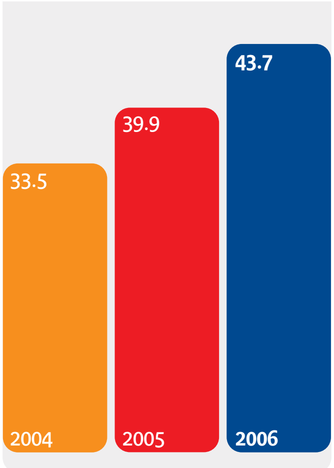
Fixed-line voice market share
% (based on traffic in TP network, mass and business segments)



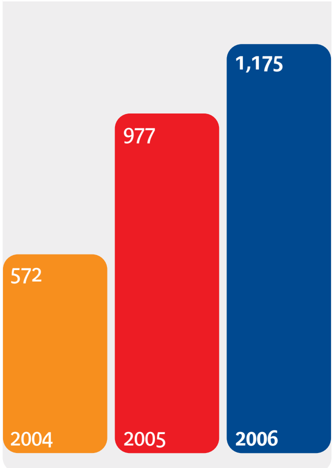
Broadband customers (ADSL + SDL)
'000



TP Group broadband market share
%



Internet access revenues
PLN mn



Voice

In the face of these challenging conditions outlined above, we maintained our share of the fixed voice market in terms of both traffic and access. Compared to December 2005, we maintained our market share in local calls and actually increased our traffic market share in all other segments. At the same time, TP continued to migrate variable voice traffic revenue to more stable access revenue by promoting new tariff plans (NTP) for Home customers. The NTP has proved effective at increasing customer loyalty and satisfaction, as well as increasing the contribution of monthly fees to total voice revenues. Customers on the NTP generate higher traffic, on average, but also contribute higher overall ARPU than subscribers on the standard tariff plan.

Data

We were able to maintain healthy growth in the data business, which is key to our long-term strategy. Our broadband customer base increased by almost 47% to 1.7 million customers, and broadband customers now make up 17% of our fixed-line customer base. At the end of the year TP commanded 43.7% of the broadband market share in Poland, and we were able to report a healthy 20.3% rise in broadband revenues in 2006.

We successfully focused on promoting faster ADSL services: in the second half of 2006, 80% of new additions were on the higher-rate options (512 and 1024 Kbps) and more than 50% of our entire broadband customer base is now on 512 Kbps or higher. Migrating customers to faster options is strategically important as a precondition for wider take-up of our new value-added services such as videostrada tp, or TV over ADSL which we launched in six major cities in 2006. We will further extend the geographical coverage and add new interactive services and other functionalities in 2007.

Uptake of our IP-VPN service amongst key business clients has also been strong. We launched IP-VPN in conjunction with France Telecom, allowing us to optimise costs and leverage France Telecom's experience in this area. The fully managed, MPLS-based IP-VPN service, using Equant technology, is one of the most technologically advanced products on the Polish market and provides corporate clients with a flexible, reliable and cost-effective network infrastructure for voice, data and video transmission.

Multimedia

At the end of 2005 we added a new multimedia modem to TP's portfolio: livebox tp. This universal multimedia gateway based on Neostrada ADSL represents a major milestone in the evolution of TP's offer to residential customers. This attractive device is offered as a Wi-Fi modem that provides wireless broadband Internet access and low cost VoIP calls, as well as, IPTV, including video-on demand services. The product is based on a near-identical service piloted in France by France Telecom, so we were able to bring livebox to market in Poland very fast and with minimal R&D investment. At the end of 2006, TP had almost 150,000 customers and we will continue to market the service to new and existing Internet customers, expanding the geographical reach of the offer gradually, in step with demand: we expect dynamic sales growth in 2007. Livebox will become a key piece of telecom equipment, the central gateway for the 'digital home' that will enhance our offer of convergent products.

TP Group maintains a high profile on the Internet thanks to our subsidiary Wirtualna Polska – the second most visited portal in Poland in 2006, reaching 66.7% of the population and featuring Poland's most popular free email account. In 2006 Wirtualna Polska launched Internet TV (wptv.wp.pl), the biggest multimedia project to date for the Polish Internet.

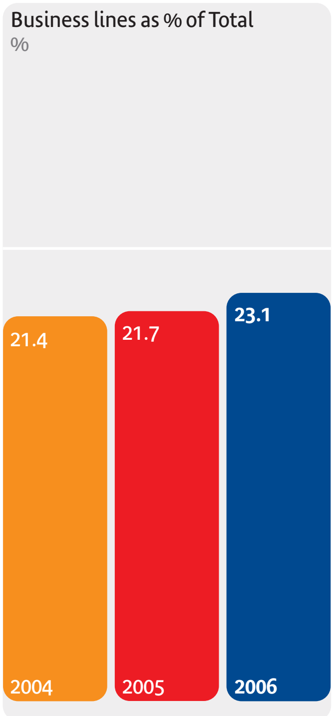
Convergence products

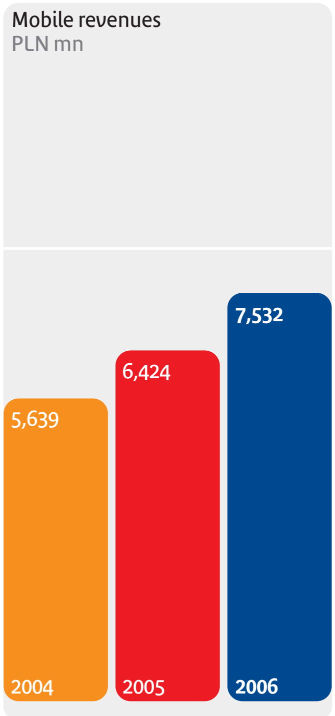
TP Group continued to develop offers that integrate fixed and mobile products. We simplified and accelerated our internal processes for developing new products, as well as making the most of our full access to France Telecom's world-class technology and R&D expertise. In February we launched fixed SMS and in March, a function that lets customers receive their fixed-line voicemail via mobile phone. And in July, we successfully introduced a single portal for fixed and mobile customers to access information on TP Group products, sales and service.

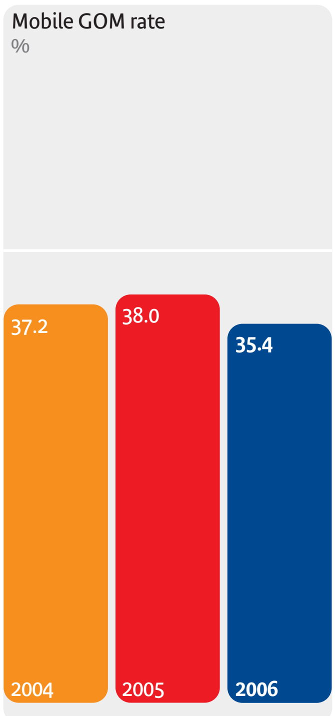
In the Enterprise segment, the stand-out product of 2006 was our convergent access service, Business Everywhere, first launched in September 2005. Customers can access their corporate intranet securely from any remote location via dial-up, broadband or wireless device (Wi-Fi, GPRS, EDGE or UMTS enabled) and receive a single, simple bill from TP Group.

Looking ahead

Our strategy for the fixed-line business in 2007 and beyond will see us leveraging the existing customer base, defending voice revenues and stimulating new revenue streams with innovative offer bundles and new DSL-based services. We will continue to push broadband development, where penetration is currently less than 10% per capita. We will be highly selective in allocating capex, favouring growth areas and reducing non-productive general and administration costs. And we will continue to exploit operational synergies between fixed and mobile.







Mobile (PTK Centertel)

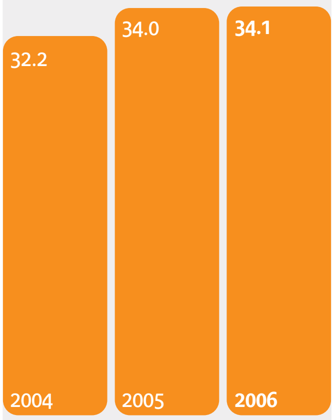
2006 was the most successful year to date for PTK Centertel with 2.6 million new customers (net additions), taking us to the number one position in the Polish mobile market in terms of both traffic volume and value (according to the National Statistics Bureau, GUS). We demonstrated that, with the right brand, the right price structure and the right content, a highly penetrated, highly competitive market still has growth potential.

The Polish mobile market grew by 26%, ending the year at 36.8 million mobile customers with SIM card penetration at 96.5%. PTK was able to grow its customer base by 26%, keeping pace with the overall market and ending the year as market leader with 34.1% market share by volume; more importantly, we significantly increased our lead in terms of value market share against our competitors, delivering the highest revenue growth on the market.

The pre-paid segment remained a growth engine for the entire market, with low-end offers – lower tariffs and minimal handset subsidies being most popular. In this highly competitive segment PTK led the market on innovation, competing less on price and more on the transparency and simplicity of its tariff structures. PTK prepaid users rose by 31% year-on-year to 7.7 million.

PTK market share evolution
%

PTK Centertel



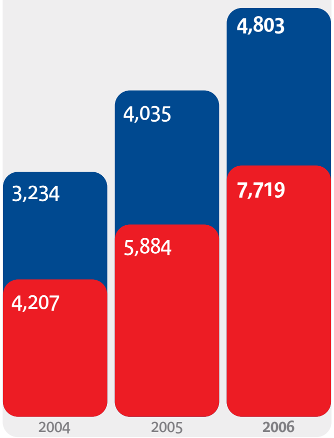
Mobile market share*
2006

* Data according to the Central Statistical Office

PTK Centertel	34.1%
ERA & Heyah	33.2%
Plus	32.7%

PTK subscribers
'000

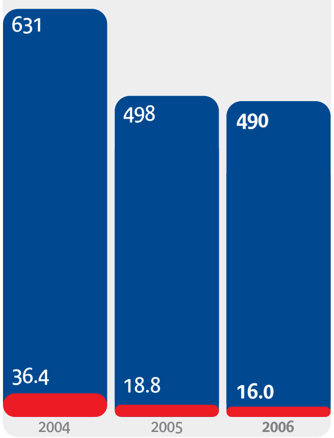
Post-paid
Pre-paid



SAC*
PLN

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

Post-paid
Pre-paid

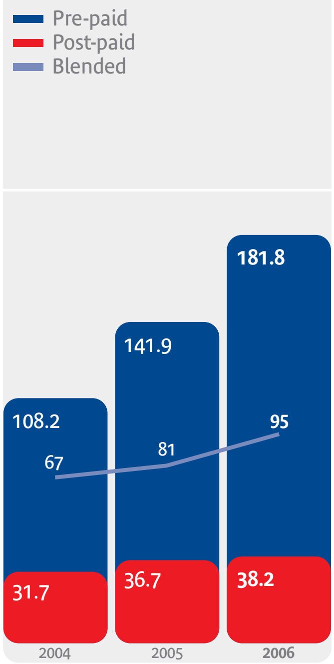


The introduction of the Orange brand, which is well-respected and perceived as bringing international standards to the Polish market, helped facilitate improvements to our customer mix. Furthermore, the Orange brand has allowed us to enhance our focus on both younger, brand- and trend-conscious customers as well as business customers to whom the brand's reputation for quality and service reliability is no less attractive. We reached 4.8 million post-paid customers by the end of 2006, a year-on-year increase of 19%. These encouraging results in terms of new additions were coupled with a reduction in acquisition costs: we brought down the blended SAC level by an impressive 15% year-on-year to PLN 135.

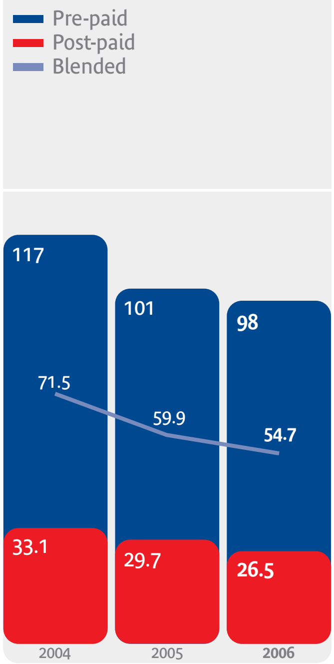
Pricing

During the year all three major mobile network operators came to bilateral agreements on mobile termination rates (MTR). These changes were implemented in October 2006 and meant an average 22% reduction in MTRs in the Polish market (see page 11 for additional details). Consequently PTK's ARPU fell in the fourth quarter of 2006, down to PLN 52 from PLN 57 in the previous quarter. Overall, the market saw a significant decrease of effective prices over the course of the year. Yet this price elasticity was positive for PTK and resulted in a 26% increase in our customer base, with total traffic rising by 51% and average traffic per user by 23%.

Average usage per user (AUPU)
Minutes



Average revenue per user (ARPU)
PLN



Product and content offers

Two major trends can be observed in the Polish mobile market. At one end, new clients are drawn to cheap handset offers and basic services. At the other end of the market, 3G and value-added multimedia services are the attraction for more affluent customers.

We had a big breakthrough in the first half of the year with the launch of Zetaphone, an offer that combined a 36 month contract with a handset for 1 zloty. This offer was the main volume driver for 2006.

The launch in April of our full UMTS service gave PTK the most extensive 3G offer on the market – and the richest content too, with 22 live TV channels, 2,300 videos and 230,000 music titles. Taking full advantage of the international development and marketing know-how available to us through Orange, we put together attractive packages for both personal and business customers that are tailor-made for the Polish consumer.

In the business market, mobile Internet access really took off in 2006 and TP Group's convergent Business Everywhere offer was very popular. PTK was able to leverage recent investment in our network to offer its customers high-speed mobile data transfer and the best network coverage on the market. Our EDGE network has close to 100% coverage, and in December we added HSDPA (High Speed Downlink Package Access), an advanced 3G technology which greatly enhances the speed and functionality of wireless Internet access over UMTS.

Our users can now benefit from a significant increase in the data transmission rate, from 384 Kbps to 1.8 Mbps, with potential for speeds of up to 14.4 Mbps in the future.

Competition

Competition in the Polish mobile market intensified this year with the appearance of a number of potential Mobile Virtual Network Operators (MVNOs). It is too early to tell which of the aspiring virtual operators will be successful. However, PTK will continue to seek profitable relationships with partners who use our networks for their own MVNO operations; similar to the agreement signed with Avon Cosmetics Polska in December 2006, ensuring that we benefit from the upside of this emerging trend in the mobile market.

Looking ahead

2007 will bring further change to the competitive landscape with a fourth mobile operator, P4, likely to launch its full service in the first half of the year. We will continue to capitalise on the Orange brand's extremely strong start with innovative new products and services to suit every pocket. In the first half of the year we will launch an Orange hybrid phone product that switches from mobile to fixed-line within reach of an in-home Wi-Fi base station.

PTK sees mobile data services as a major driver of future growth: with the network platform, product range and premium content in place we are poised to consolidate and grow our market-leading position with a major sales and marketing push in the coming year.

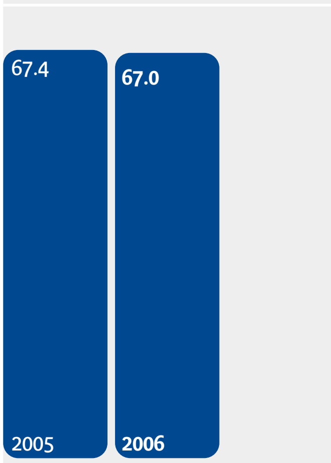
Sales & Service Poland

We successfully implemented the next stage of our strategy to leverage the potential of the Group to optimise costs, grow top line and improve the customer experience. TP and PTK Centertel began to see real savings from the newly integrated sales and customer service network and from the sharing of IT resources. General customer satisfaction for TP Group was at 67.0%.

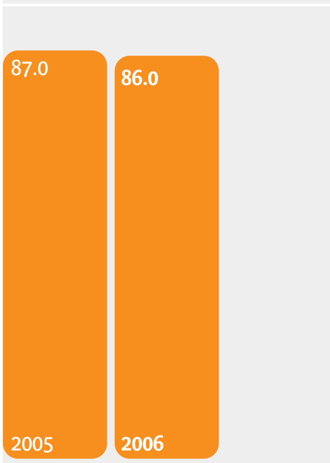
Customers benefited from a number of improvements to the efficiency of our telephone CRM system, Blue Line. In addition, an Interactive Voice Response system, launched in June, shortened operator time spent on each call; some services can now be activated or deactivated entirely automatically; and additional 'self-service' functionality is currently being added and will be available first to business customers.

In May we launched an additional channel for customer relations, Portal TP. This web-based service allows current and potential customers to order selected services, check account balances and order status, register complaints and notify failures. Fixed-line, broadband and mobile all share the same portal, allowing efficiency savings for the Group and a seamless customer experience.

TP Group customer satisfaction index
% of customers surveyed



Orange customer satisfaction
% of customers surveyed



Our platform is now utilised across the whole of TP Group. We continue to assess its performance and to simplify IT processes where possible. We have made considerable progress on the quality of billing and collection, with significant improvements in the areas of bad debts and receivables. Process improvements throughout the Sales and Service division have been facilitated by our Simplicity+ programme, an initiative that draws together research and customer feedback to identify areas where the customer experience is unnecessarily complex or frustrating, this helps us to identify simpler solutions. One of the programme tools, Greenline, is specifically for new product launches; during the introduction of livebox it allowed us to identify potential problems extremely rapidly and move to fix them just as fast.

Looking ahead, we will focus on strengthening our sales force and improving every stage of the customer experience with simpler processes and quicker response times. In terms of time-to-market with new products, TP is now the fastest in the France Telecom Group, and this pace of innovation demands a responsive front-line sales and implementation force along with a robust network structure.

Networks, carriers & IT

The major technical challenges for the Company in 2006 were the introduction of VoIP, IPTV and Video on Demand. All of them were completed as planned with no major technical problems. To enable video service we developed a dedicated GigaEthernet network that covers six major Polish cities, making the service potentially available to 1.7 million households.

2006 saw more than half a million broadband additions and 200,000 new physical access lines. Investment in our network has added 1000 km of fibre and improved data capacity.

TP Group's Data Center in Łódź (the biggest in this part of Europe) started to host not only TP fixed-line but also some of the critical IT systems for mobile. In addition, a series of minor TP data centers were transferred there to improve efficiency. Last but not least, the IT helpdesk for TP's fixed-line business was centralised, allowing higher efficiency and enhancing staff performance.

In order to have more efficient network field support teams, we have introduced new processes in accordance with a 'lean management' methodology, allowing continuous productivity improvement.

As a result, IT and Network costs have been reduced by almost 11% year on year despite the fact that many new services were added.

In 2006 we improved service levels for visitors to the tp.pl, neostrada.pl and orange.pl websites, by implementing an integrated web portal. This portal supports product cross-selling and customer service across the whole TP Group, demonstrating our convergence capability.

In order to improve our efficiency across the Group, we started integrating our infrastructure and making the fixed-line backbone more and more available for mobile purposes, always working within the regulations set by competition authorities.

In the spring, we migrated fixed voicemail onto the same platform as mobile voicemail. That allowed us to offer seamless mailbox accessibility from TP fixed and Orange phones as well as delivering maintenance savings for TP.

Human resources

At the end of 2006 TP Group's total workforce stood at 33,421 (full-time equivalents), down 0.5% on a year earlier. The cost of wages, social insurance contributions and other employee benefits for the year was down by 1.5% compared to 2005. During the year, we have focused on optimising the workforce through internal movement from 'business as usual' administration and support functions to revenue-generating growth areas.

The Employee Mobility Programme we introduced in the first half of the year is a key strategic priority for TP Group's human resources function. Our initial aim was to add 1600 staff to the customer service and sales force by incentivising the transfer of staff from network and technical support functions. Internal mobility in TP Group in a normal year is around 300 people. By mid 2006, more than 920 employees had already changed jobs under the new Programme and at year end the number reached 2041. This achievement helped us to increase the proportion of customer-facing staff from 45% at the end of 2005 to more than 50% a year later. We expect to see a further 500 internal moves under the Employee Transfer Programme in 2007.

In December 2006, we negotiated a new Social Agreement with the majority of the unions to cover the years 2007 to 2009. The Social Agreement regulates TP Group's policies in areas such as annual pay rises, the level of outsourcing, external versus internal recruitment and financial compensation for leavers. It allows the Group to effect a further 5,700 voluntary redundancies over the next three year period, for which we have established a workforce restructuring provision of PLN 277 million.

Our HR strategy is concerned with investing in human capital more than just cutting costs. We are taking gradual steps towards instilling more of a pay for performance culture at TP Group, and to this end we announced a new management incentive scheme in April 2006 which will be implemented during 2007. The scheme is open to 330 key managers and takes the form of a stock option plan, with options granted to each plan member according to their performance and achievements.

Together with the Management By Objectives programme, which sets a proportion of the annual bonus of 700 managers according to achievements against KPIs, we believe the new incentive scheme will contribute to the successful implementation of TP Group's development strategy by getting the best possible performance from our managers. By linking the remuneration of key managers directly to Group profitability and performance, we hope to ensure their active commitment and contribution to future success.

Regulatory issues

In December 2005 a new regulatory body, UKE (Office for Electronic Communications), was convened to replace URTiP (Office of the Telecommunications and Postal Regulator) in the regulation of the telecoms industry in Poland. During 2006 the new regulator issued a number of decisions concerning the opening up of TP Group's networks to the wholesale market. The implementation of these rulings had a partial impact on TP Group's business in 2006 and will have a full impact in 2007.

TP Group has appealed all UKE decisions which the Company considers unjustified, while nevertheless making every effort to implement the changes imposed by UKE's rulings in the meantime. The Company's position is that it supports a competitive telecoms market in Poland, but not the sort of competitive environment that discourages infrastructure investment. It is vital to the whole industry that TP continues to be capable of financing the maintenance and development of an extensive, high-quality network.

A major stumbling block in negotiations between TP Group and UKE has been the lack of a mutually approved cost-base model. This lack has led to repeated questioning of TP's proposals by the regulator, and to rulings that impose price levels below TP's calculated cost of service provision. In 2007 a new audit of the cost-based model will be carried out which we hope will improve the negotiation process considerably.

Regulatory changes in 2006

UKE decisions on new services

In May, the regulator obliged TP to provide wholesale bitstream access (BSA), allowing other operators to offer broadband services using TP's ADSL network. Some provisions of this decision were subsequently amended in October.

In July, the regulator amended the interconnect agreement between TP and Tele2, applying new terms and conditions on the provision of Wholesale Line Rental (WLR) by TP. On 18 October 2006 Tele2 and TP reached an agreement on the implementation of this decision. The wholesale discount on access fees is 46.99%, the highest in Europe. In November, the regulator applied the same WLR terms to the interconnect agreement between TP and GTS Energis and in December, to the agreement between TP and Dialog.

UKE decisions on existing services

In May, the regulator amended TP's reference interconnect offer (RIO), which determines the terms and conditions of line rental agreements with other operators. This ruling reduces the fees for leased line services in the wholesale market. Further rulings on RIO followed in July and August, with the result that the regulator retained the option of imposing flat rates for interconnect traffic but stopped short of imposing rates below the level of TP's costing model.

In June, the regulator instructed TP to develop new terms and conditions for local loop access. TP's proposal was further amended by the regulator in October, drastically reducing fees for full or shared access to the local loop.

In September, under regulatory pressure, all three major mobile network operators came to bilateral agreements on mobile termination rates (MTR). The agreements came into force in October across the whole Polish mobile market, with an average reduction in MTRs of 22%.

On 22 February 2007, subsequent to the publication of TP Group's Full Year Results, the regulator imposed a fine of PLN 338.97 million on TP S.A. for not submitting the neostrada tp price list and the service provision rules, in force as at 15 February 2007, to determine prices of services on the basis of the cost of their provision to meet the price setting requirements for the UKE. The Company is preparing to appeal the fine, which in our opinion is groundless.

Customer service

Our World

Our customers are the number one priority for TP Group. Poland's consumers are evolving fast, with new attitudes shaped by a more international outlook, and new spending power fuelled by EU membership and an economic boom. They have more and more choice, with the emergence of new entrants to the telecoms sector and new alternatives to traditional fixed telephony.

TP Group's success in this dynamic marketplace depends on keeping our finger on the pulse, being receptive to our customers' feedback and anticipating their demands.

We're investing in customer service to build and maintain brand loyalty: more than 50% of TP employees are now in customer-facing roles. And through our Simplicity+ programme we are continually refining and simplifying our systems to improve the customer experience, from start to finish.

Customer satisfaction

Your World

The future of the Polish telecoms market will be shaped by a new breed of consumer: more discerning and more demanding. Customers no longer look to TP only as a seller of voice services. We are increasingly acting as an access provider, putting our customers in touch with multimedia content, mobile data, IP-based services and packages tailored to suit their needs. Like Business Everywhere, which harnesses the combined power of our fixed and mobile networks to give our customers seamless secure access to Company data in the office, at home or on the move.

But let's step back to the present, for a moment. Poland still has high unemployment and low per capita disposable income. Basic telephone services are the core foundation of our business. Here, we win customers with reliable service and transparent, competitive pricing. Over the last year, we saw TP's former fixed-line customers coming back at a rate of two to every one that chose to try one of our competitors.

Future value

Our World

The next generation of telecoms products will be key to fuelling growth and creating value for TP Group going forward. In 2006 we brought a series of innovative new offers to the market – committing some PLN 3 billion of capital expenditure in the process – on time and on budget. We implemented technology that works faster and smarter, sharing systems across the Group where possible for even greater efficiency.

Leveraging our strong relationship with the FT Group helps us to provide reliable, cutting-edge solutions that set the pace in the Polish market. In fact, TP can now boast the fastest time-to-market for new products in FT Group, and several key network R&D functions are now outsourced by France Telecom to TP.

Future products

Your World

We're investing in new products that reach out to our existing customer base. TP has a solid foundation for ADSL growth given that 97% of TP's fixed-line subscribers are located within ADSL coverage (as at the end of 2006). At the other end of the pipeline, TP has brought together a wealth of content, including full digital TV and over 500 films available on demand.

Our content aggregation strategy, coupled with our accelerated roll-out of high speed broadband access, makes our livebox tp modem a future star. The livebox modem turns a regular fixed-line point into a multi-media gateway in the customer's living room offering VoIP, TV, Video on Demand and Internet access in one customisable package.

Reliable growth

Our World

Maintaining solid performance at TP Group is a question of balance. Our goal is sustainable growth, which means investing sensibly in growth areas of the business and having the flexibility to make strategic regional acquisitions if and when the opportunities arise. At the same time, we need to show the required financial discipline to maintain our current attractive ratings of BBB+/Baa1 with stable outlook.

To add to the complexity of the task, this balance must be maintained in a business environment characterised by intensifying competition and unpredictable regulatory pressures.

Reliable investment

Your World

A strategy for sustainable growth must also enable us to provide reliable returns to our shareholders. After several years of tight cost control, financial systems improvements and cautious investment strategy, TP Group has turned a corner. The business is generating strong free cash flow and we now plan to return some of this cash to shareholders.

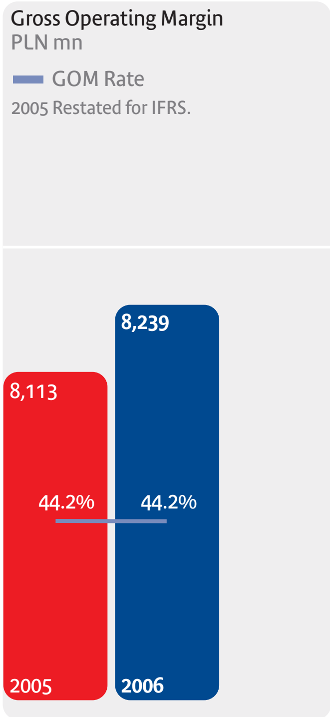
The Management Board's recommendation of an ordinary dividend of PLN 1.4 per share for 2006 sets the bar for our dividend policy going forward. In addition, the management is recommending an exceptional cash distribution for 2006 (for more details see the Chief Financial Officer's review on page 18). We will continue to monitor our policy carefully in the light of any significant future developments, but the current level is a comfortable base upon which to build.

Benoît Mérel
Chief Financial Officer

Overview

2006 was a year of solid progress for TP Group: a period of transition which nonetheless enabled us to focus on core strategic imperatives, improve our financial control and accounting processes and build a strong foundation for sustainable future growth.

The Company exceeded expectations for revenue growth, driven by particularly strong performance in the mobile and data segments. Group revenues increased by 1.5% to PLN 18.6 billion, reversing a year-on-year decline of 1% in the previous accounting period. These positive results were achieved despite a number of negative factors in the second half of the year, namely: the impact of regulatory decisions on Mobile Termination Rates (MTR) and Reference Interconnect Offer (RIO); increased competition; and aggressive pricing and promotion of broadband offers to secure market share.



In terms of profitability we met our guidance on all key indicators. Full year Gross Operating Margin (GOM) rose by 1.6% to PLN 8.2 billion, despite a 19% increase in commercial expenses, and the GOM rate stands slightly above the upper range of our annual guidance at 44.2%. This clearly illustrates the success of our cost control measures and translates into an extra PLN 126 million in the GOM compared to 2005.

Perhaps most importantly, we showed that we could translate revenue growth into strong cash flow generation, increasing Net Free Cash Flow (FCF) to PLN 4.1 billion, and maintaining Net FCF yield at 22.2% (defined as cash flow from operating activities minus capex and capex payables).

Cash distribution

The Group's strong financial performance in 2006 has enabled us to propose a cash distribution to shareholders of PLN 2.66 billion, equivalent to PLN 1.9 per share. This will consist of an ordinary dividend of PLN 1.4 per share (PLN 1.96 billion in total), payable in the first half of 2007, as well as an exceptional cash distribution of PLN 700 million (an equivalent of PLN 0.5 per share) in the second half of 2007 in a form to be determined; either cash dividend or share buyback. The recommended dividend for 2006 is subject to AGM approval.

While we are mindful of the need to maintain strict financial discipline as well as keeping the flexibility to pursue growth, the management team is satisfied that the ordinary dividend represents a sustainable base level of return going forward.

Revenue mix

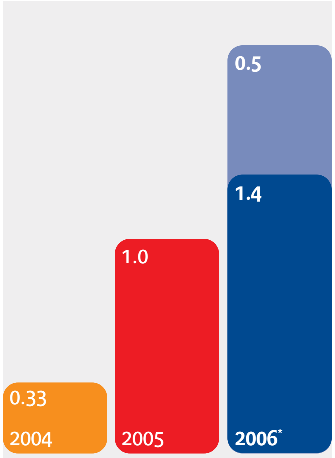
Although TP succeeded in defending fixed-line market share, 2006 saw a decline of just over 26% in fixed-line traffic revenues, reflecting the general market trend of fixed-to-mobile substitution. However, strong performance in the Mobile and Data businesses continued to offset this decline, with Mobile in particular increasing its overall share in TP Group's revenue mix by 5.3 percentage points. We also saw a slow-down in the rate of fixed-line revenue decline through the year.

Leadership in Mobile

The steady progress of our mobile arm, PTK Centertel, continued in 2006. By the end of the year, it was confirmed that the Company had achieved the market leading position in terms of both volume and value, with 12.5 million customers and revenues of PLN 7.5 billion. We achieved impressive results in terms of new subscriber additions in 2006, adding 2.6 million customers – 5% more new additions than in 2005. At the same time we managed to reduce the level of blended subscriber acquisition costs (SACs) by 15% year-on-year.

Dividends per share
PLN

*The Company intends to recommend for the shareholders approval a cash distribution of PLN 1.9 per share, consisting of:
– PLN 1.4 per share payable in cash and
– an additional, exceptional cash distribution of PLN 0.5 per share in a form to be determined.



The regulatory reduction to Mobile Termination Rates in Q4 drove monthly ARPU down from PLN 57 in Q3 to PLN 52 in Q4, but because our inter-operator costs were reduced by a similar amount there was no impact on PTK Centertel's pre-commercial GOM, which ended the year at 60.0%. The combined pressure of regulation and competition meant a decrease in effective prices of 35.5%, but overall we benefited from this price elasticity with a 23.9% increase in total traffic and a 28.8% increase in customer base.

Cost control

In the 2005 annual report we laid out our strategic roadmap including a clear statement of our intention to rebalance our cost structure towards revenue generating areas. We have pursued this policy diligently in 2006: operating expenses were kept below 2005 levels in all areas except commercial costs, inter-operator costs and content services – three areas closely related to revenue generation.

Capital expenditure

Group Capex for 2006 was almost identical to 2005 at PLN 3 billion, representing 16.1% of revenue and at the low end of our guidance for the year. In terms of capital expenditure we focused on the delivery of innovative products and convergent offers – again, in line with the roadmap set out last year. In 2006 80% of capex went to growth business lines – mainly ADSL, Livebox and Mobile. This compares to 71% of capex invested in growth areas in 2005.

Cash flow

TP Group's revenue growth in 2006 translated into strong cash flow generation. Net cash flow from operating activities amounted to more than PLN 7.2 billion – almost 40% of TP Group revenues. Net free cash flow (defined as cash flow from operating activities minus capex and capex payables) matched our 2005 achievements at over PLN 4 billion, 22% of Group revenues. The management team continues to view cash flow optimisation as a key area of focus going forward.

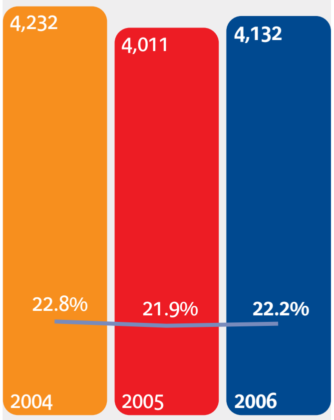
Debt structure

Net debt repayments for 2006 amounted to PLN 3.2 billion, which included a PLN 1 billion loan from France Telecom related to the PTK Centertel acquisition in 2005 and a EUR 500 million bond. Our refinancing operations achieved a reduction in average costs of financing to 7.5%, down from 8.4% in 2005. At the end of 2006 our net gearing ratio stood at 24.2%. Our healthy financing ratios are reflected in our ratings of BBB+/Baa1 with stable outlook.

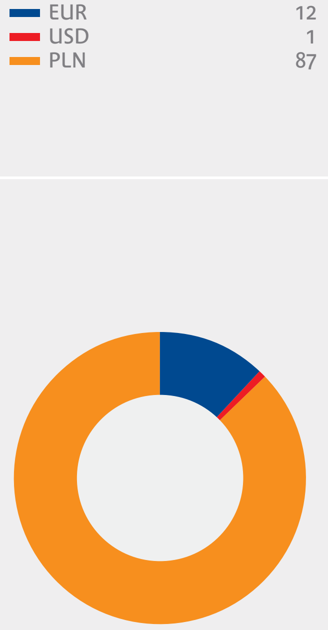
Internal and external financial reporting

We achieved several milestones in terms of accounting and reporting in 2006. The whole organisation now operates a single accounting tool, making internal reporting much more responsive and financial control far simpler, with managers throughout the business answerable for results on a quarterly basis. The integrated tool facilitates more accurate forecasting and allows us to manage capex effectively on a monthly basis. External reporting has also undergone something of a revolution, with the introduction from Q1 2006 of a single IFRS reporting format, with a condensed version for international markets. It is now bedded in and running smoothly. The relative speed of our external reporting – with 2006 full year results delivered a full two months earlier than in previous years – is just one external indicator of our successful adoption of these robust new financial processes, including budgeting.

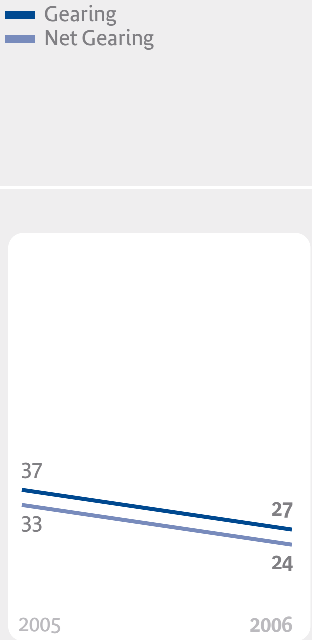
FCF before financing and FCF margin*
PLN mn
* Cash flow from operating activities – purchase of tangible and intangible assets plus interest paid net



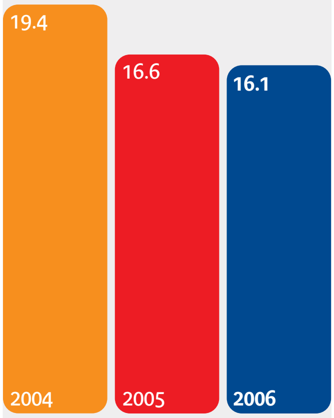
Debt structure after hedging
%



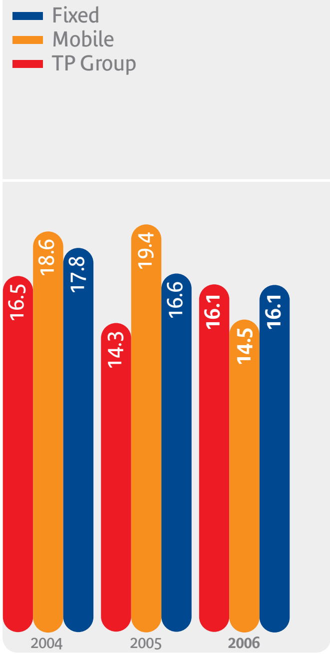
Gearing and net gearing ratios
%



TP Group Capex to Sales
%



TP Group Capex to sales ratio
%



In 2006, TP S.A. and PTK Centertel completed a comprehensive assessment of their processes of internal control over financial reporting. A number of deficiencies both in design and in the effectiveness of internal control have been identified, and either remedied immediately or marked for action. As a result of the assessment, the Management concluded that there were no weaknesses that could materially impact the internal control over the financial reporting at 31 December 2006 (for further information see page 28).

Outlook

TP Group faces a challenging year in 2007, characterised by increased competition in all segments, continuing erosion of fixed voice revenues and unpredictable changes to the regulatory outlook. We cannot change the weather, but we can ensure that we are good at anticipating and that our reactions are fast and agile.

We will continue to defend our market position by ensuring that TP has tailored products to offer to people in every income bracket, from basic, pragmatically priced fixed voice packages to the fastest IP-based services and value-added content. Over the coming years we will continue with our strategy of focussing investment on growth areas. TP has been very disciplined and effective in its cost management over the last few years, and this will not change. However, as we increase our sales efforts to stimulate promising sources of revenue, commercial costs will increase in some areas. A key role for the finance function during this phase is to assess the return on these investments, and to ensure that costs are kept within strict parameters of profitability and payback.

At the same time, we will continue to manage the cost-effectiveness of all our operations. Our new social plan allows us to invest selectively in the right people and strengthen the sales and customer support functions still further while optimising our deployment of resources across those parts of the business which are not growing. We will step up the optimisation of our real estate portfolio, disposing of surplus property and consolidating fixed-line and mobile employees into fewer and larger locations. The integration and simplification of certain IT functions across fixed-line and mobile will continue to deliver savings. And we will look to leverage the scale of the whole TP Group to make the best deals with suppliers, being as tough as we can be without compromising the supply chain.

Crucially, we now have the right tools, systems and people in place to allow us to monitor the performance of the business closely, month by month; to prioritise business needs and react quickly to both internal and external trigger factors. Our improved financial controls and healthy financial position provide a strong foundation for realisation of business opportunities.

Benoît Mérel
Chief Financial Officer
31 March 2007

Management Board

Maciej Witucki
President of the Board and Chief Executive Officer

Maciej Witucki graduated from the Electrical Department of the Poznan Technical University in 1991. Between 1992 and 1997 he undertook post graduate research in industrial system management at Ecole Centrale, Paris. In September 1997 he began working for Cetelem Bank: first in France, where he took part in the development of the business plan for Cetelem's Polish subsidiary; then in Poland, as a Member of the Management Board of Cetelem Polska Expansion S.A. In October 2001 he joined the Credit Agricole Group and in 2002 he became a Member of the Management Board of Polish retail bank LUKAS S.A., rising to the position of President and CEO in March 2005. He joined TP Group as President of the Board and Chief Executive Officer on 6 November 2006.

Benoît Mérel
Chief Financial Officer

Benoît Mérel is a graduate of the Institut Commercial Superieur in Paris, a qualified Certified Public Accountant and has 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 TP Group Controller.

Pierre Hamon
Board Member (Marketing and Customer service)

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.

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.

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.

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.

TP S.A. Supervisory Board Composition

The composition at 1 January 2006:

Dr. Jan Kulczyk	Chairman
Jean-Paul Cottet	Deputy Chairman
Andrew Seton	Deputy Chairman
Michel Monzani	Secretary
Claude Benmussa	Board Member
Timothy Boatman	Board Member
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

In 2006, composition of the Supervisory Board changed as follows:

On 28 April 2006:
– Dr. Jan Kulczyk, André Cathelineau and Jean-Pierre Temime resigned from the membership in TP S.A. Supervisory Board;
– the following persons' term of office expired: Jean-Paul Cottet and Andrew Seton;
– Messrs. Julien Billot, Jean-Paul Cottet, Prof. Andrzej K. Koźmiński, Georges Penalver and Andrew Seton were appointed by the Ordinary General Meeting members of the Supervisory Board.

We note with regret the death of Krzysztof J. Ners on 2 September 2006.

On 21 September 2006, Messrs. Jean-Paul Cottet, Claude Benmussa and Yves Le Moüel resigned from the membership in TP S.A. Supervisory Board.

On 21 September 2006, Messrs. Vivek Badrinath and Olivier Barberot, Ms. Stéphane Pallez and Prof. Jerzy Rajski were appointed by the Extraordinary General Meeting members of the Supervisory Board.

On 7 October 2006, Mr. Jerzy Drozd resigned from the membership in TP S.A. Supervisory Board.

On 9 November 2006, Dr. Wiesław Rozłucki was appointed by the Extraordinary General Meeting member of the Supervisory Board.

The composition at 31 December 2006:

Prof. Andrzej K. Koźmiński	Chairman
Olivier Barberot	Deputy Chairman
Michel Monzani	Secretary
Vivek Badrinath	Board Member
Julien Billot	Board Member
Timothy Boatman	Board Member
Jacques Champeaux	Board Member
Tadeusz Han	Board Member
Stéphane Pallez	Board Member
Georges Penalver	Board Member
Prof. Jerzy Rajski	Board Member
Dr. Wiesław Rozłucki	Board Member
Andrew Seton	Board Member

Currently, the TP Supervisory Board's composition includes six independent members: Prof. Andrzej K. Koźmiński, Timothy Boatman, Tadeusz Han, Prof. Jerzy Rajski, Dr Wiesław Rozłucki and Andrew Seton.

Three permanent committees operate within the Supervisory Board composed, as at 31 December 2006, of:
– Audit Committee: Timothy Boatman – Chairman, Michel Monzani, Stéphane Pallez and Andrew Seton - members;
– Remuneration Committee: Andrew Seton - Chairman, Jacques Champeaux and Michel Monzani - members;
– Strategy Committee – Olivier Barberot - Chairman, Tadeusz Han, Michel Monzani and Jerzy Rajski - members.

Operation

The Supervisory Board, acting according to the provisions of the Commercial Companies Code and the Company's Articles of Association, exercised permanent supervision over the Company's operations in all fields of its activities.

TP S.A. Supervisory Board fulfilled in 2006 duties resulting from the provisions of the Commercial Companies Code:
– Evaluated the Management Board's report on TP S.A. operations and the financial statements for the financial year 2005 and the Management Board's recommendation for distribution of the Company's profit,
– Evaluated the Management Board's report on TP S.A. Capital Group's operations and the consolidated financial statements for the financial year 2005,
– Filed with the General Shareholders' Meeting reports presenting results of the above-mentioned evaluation.

The Supervisory Board also executed its rights and obligations arising from TP S.A. Articles of Association and Best Practices, of which the following should be mentioned:
– Appointment of members of the Management Board,
– Recommendation of motions addressed to the General Shareholders' Meeting, including motion for amendment of the Articles of Association,
– Selection of an independent auditor to audit the Company's financial statements,
– Preparing an opinion on draft TP S.A. and TP Group budgets for 2007,
– Supervision of the realisation of TP Group's operating and financial objectives for 2006,
– Expressing an opinion referring to contracting loans exceeding the amount of 100 M €,
– Assessment of TP Group situation in 2005.

Throughout 2006 the Supervisory Board and its permanent committees focused on the following issues:

– Group's financial results and performance against the budget and the budget for 2007;
– Group's strategy in an increasingly competitive market;
– Group's position vis a vis the regulatory environment in Poland;
– Changes in the Group's Management Board;
– Company's shareholders' remuneration;
– Group's approach to internal control, including risk management;
– Incentive Program for TP Group Top Managers.

The Supervisory Board met eight times in 2006. The Board adopted 43 resolutions, of which five in writing (by correspondence).

The Supervisory Board used in its operations the opinions of the Audit Committee, the Remuneration Committee and the Strategy Committee.

The Supervisory Board formulated a number of recommendations, remarks and motions for the Management Board, referring to different aspects of the company's operations.

The Supervisory Board was abreast with examination of the execution of resolutions and recommendations, analysing information of the Management Board presented on subsequent meetings.

Corporate Social Responsibility

TP's Strategic Rule is to Get Closer

This means getting closer to both customers and other stakeholders (local communities, employees, suppliers, investors, environment). We are committed to doing business in the spirit of social responsibility and to respecting all our stakeholders, because 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.

In February 2006, TP became officially the first and only Polish telecom company to participate in the UN Global Compact, the Secretary General's initiative for business, which promotes sustainable development and works to advance ten universal principles in the areas of human rights, labour, the environment and anti-corruption.

TP and Local Communities

TP is focused on cooperation with local communities and local authorities in order to popularise Internet-based technology and facilitate the process of information society building ('BB Partnership' programme).

Apart from business cooperation, we are supporting the local community development through dedicated social programmes. In January 2006, TP and PTK Centertel established the TP Group Foundation – an indication of our long-term commitment to social initiatives.

As part of our nation wide initiatives to develop an Internet society, TP Group creates Internet connection programmes in Polish schools. Established in 2004, 'Education with TP Internet' provides schools of all levels with discounted Internet access. TP also organises teacher training courses to support the project and to encourage use of the Internet – an indispensable part of modern education. The programme is carried out in cooperation with the Ministry of Education. Almost four million pupils at 12,000 Polish schools currently use broadband Internet services thanks to the programme. And Poland has been singled out by a European Commission report as one of only eight UE countries in which more than 80% of PCs at schools are connected to the Internet.

TP has established a national grants programme for local communities aiming to create an information society. Local Action Groups were awarded grants and 40% of the local districts in Poland are covered by the programme. The initiative is carried out in cooperation with the United Nations Development Programme (UNDP) and is the biggest such UNDP programme in Europe.

TP is always on the lookout for innovative ways to use the Internet. The Virtual Museum Programme, launched in 2006, is helping museums to create virtual exhibitions and enabling a virtual tour round the museums using modern telecommunications technologies, so that the museums' collections may be visited by anyone. The first institution whose collection will be available via Internet will be the Warsaw Uprising Museum.

Another highlight among TP's social outreach initiatives is the 'Call Mum' project which gives hospitalised children access to telephones. So far, over 1,000 colourful, child-friendly phones have been installed, in almost every child's ward in Poland. Every month children are provided with 16,000 free phone cards.

The idea behind 'Phone to Mum' has been extended to the 'Internet Smile' programme. We create Internet mini-laboratories helping to continue children's education while in hospital.

TP and the natural environment

Conscious of the environment, TP aims at limiting its impact on the natural environment. As a consequence, in 1998 the Company has implemented procedures and systems that help us to achieve our objectives. Environmental audits carried out by the Company in 2002 and 2003 have 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 consumer organisations
TP builds its external relations with consumer organisations by conducting an ongoing dialogue through meetings and workshops.

TP and suppliers
TP plays an active role in the FT Group supplier evaluation programme, QREDIC. The programme includes a supplier evaluation process, which monitors suppliers' activities with regard to business ethics and environmental protection. The process 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 on pages 26-29 for details.

TP and employees

Health and safety
TP has adopted the highest standards of health and safety. In addition to health and safety internal regulations, the Company has an ongoing health and safety training programme.

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 45% of all employees at TP are women, of whom 31% are in management positions.

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 TP 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.

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 pay-as-you go retirement system and the employee premiums are paid by the employer. The employer's contribution 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 2,841 participants in TP ERP. The value of the TP ERP unit increased by 15.4% in 2006.

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). Additionally TP Group Foundation holds a special fund for employees who suffer from accident or illness. It is created from voluntary payments of TP's employees.

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 review and approval of the Management Board's recommendations on dividend payments; the Supervisory Board Assessment of the Group's situation; 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 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 2006, the Supervisory Board comprises thirteen members.

At present, TP has six independent members in the Supervisory Board, namely Messrs. Prof. Andrzej K. Koźmiński, Timothy Boatman, Tadeusz Han, Prof. Jerzy Rajski, Dr. Wiesław Rozłucki and Andrew Seton. The other members are: Olivier Barberot, Michel Monzani, Vivek Badrinath Julien Billot, Jacques Champeaux Stéphane Pallez, and Georges Penalver.

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 2006 appears on pages 30 and 31.

The Audit Committee

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 34 and 35 of this annual report.

The Remuneration Committee

The Remuneration Committee's task is to advise the Supervisory Board and Management Board on the general remuneration and nomination 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 Committee is chaired by Mr. Andrew Seton – an independent member of the Supervisory Board. The Committee report appears on page 32 and 33 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.

Until 21 September 2006 the Committee was chaired by Mr. Jean-Paul Cottet and now its Chairman is Mr. Olivier Barberot.

In 2006, the Strategy Committee met three times.

3 The Management Board

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 the 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 misstatement or loss (see also page 21).

In 2006, TP SA and PTK Centertel completed a comprehensive assessment of their processes of internal control over financial reporting. Main deficiencies both in design and in effectiveness of the internal control have been either identified, remediated or appropriate action points have been launched. As a result of the assessment, the Management concluded that there were no weaknesses that would materially impact the internal control over the financial reporting at 31 December 2006.

Further key elements of this system include the following procedures:

- An internal audit function, which reports directly to the Management Board. The internal audit programme is annually reviewed by the Audit Committee which also analyses the Company's Internal Audit reports.

In order to promote an appropriate independent outlook for the Internal Audit Department, Management Board decisions regarding the appointment and remuneration of the Head of the Internal Audit Department now require an opinion of the Audit and Remuneration Committees. 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 conducts ongoing assessments of the quality of risk management and control. As part of this process, a Risk Map which identifies and classifies the Group's financial and non-financial risks is maintained. 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.
- The Company has developed procedures for identifying, approving and accepting transactions with related parties.

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 2006

Further work was done to improve the system of risk identification and assessment according to the methodology of IAS 37. 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 of provisions is prepared quarterly by business owners.

Internal Audit Departments in TP and PTK Centertel have been merged, in order to have an integrated, TP Group Internal Audit function.

At the end of the year the Management Board decided to create a new function of the Corporate Risk Officer responsible for developing processes related to risk management (i.e. Risk Map, identification and reporting of significant risks according to IAS 37). The function will be independent from internal audit yet mutual co-operation of these functions is essential.

In 2006, 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.

Following the implementation of insurance policies in 2004 to limit the Group's exposure to civil liability claims and property damage, 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 2006, TP Internal Audit Department conducted cyclical audits of the Group's transactions with related parties that were reviewed by independent directors of the Audit Committee.

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 fulfiling 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 2006 the TP Group Disclosure Committee had four regular and three ad-hoc meetings to discuss the following:
– evaluation and approval of the statutory financial reports (quarterly, half-year, full year);
– evaluation and acceptance of quarterly investors' presentations.

In 2006 TP published 191 regulatory announcements (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 over 100 meetings with investors and analysts.

Code of Ethics

A new TP Code of Ethics was implemented in 2006, together with appointment of the Ethics Committee and the network of local ethics coordinators.

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 no tolerance for corruption;
– apolitical stance;
– environmental care.

An alert handling system related to ethics has been implemented by the Company. Further work is being conducted on the processes and policies for the prevention and reporting of potential or actual fraud, including a 'whistleblowers' charter'.

Assessment of the Group's situation in 2006 prepared by TP S.A. Supervisory Board

This document is the Supervisory Board evaluation of TP S.A. performance in 2006 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 2006 Financial Results, as well as, on information obtained by the Supervisory Board during its statutory tasks.

Throughout 2006 the Supervisory Board focused on the following issues:

– Group's financial results and performance against the budget and the budget for 2007;
– Group's strategy in an increasingly competitive market;
– Group's position vis a vis the regulatory environment in Poland;
– Changes in the Group's Management Board;
– Company's shareholders' remuneration;
– Group's approach to internal control, including risk management;
– Incentive Programme for TP Group Top Managers.

The Supervisory Board, through the work of its committees and all its members including independent members (who are now six in total), 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 review and challenge the control, risk management and budgeting functions performed by management.

TP Group operational review

During the year, TP Group launched a full range of innovative and convergent products and services (i.e Triple Play, Livebox, Videostrada TP, Rent a game, new neostrada tp offers and promotions, VoIP, WP TV on Internet, Business everywhere) and also the first integrated telecommunications portal in the Polish market (One portal for fixed and mobile customers) as well as innovation in sales model with the first MVNO contract signed by PTK Centertel.

Furthermore, several major initiatives were proposed and/or implemented by management, in particular:

– Incentive Programme for TP Group Top Managers;
– Social Agreement 2007-2009 which determines principles in regards to the major employee-related issues for the next three years.

Fixed-line

The Supervisory Board noted with satisfaction that TP has succeeded in defending its market share in a declining fixed-line voice market and has partly compensated the fall in revenue by increased data service revenue. The Management of the Group devoted substantial time and resources to developing the Polish broadband market – by the end of 2006, TP broadband customer base rose by +46.4% compared to 2005. This can be attributed to TP triple play offer and to attractive promotions for neostrada tp. Continued efforts by Management in this regard are needed in 2007.

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 2006, competing principally on the quality of its products and services and the transparency and simplicity of its tariff structures. Mobile segment completed a highly successful 2006: PTK Centertel consolidated its market leadership in both volume and value while recording 79% recognition rate for its brand Orange. Total number of customers added in 2006 exceeded the guidance given by the Management.

The Supervisory Board believes there is now evidence that the Orange re-branding carried out in September 2005 successfully helped PTK Centertel to strengthen its market position.

By continuing to operate at the forefront of new technology, Orange is able to provide its clients a wide range of the most up-to-date offers on the market. UMTS coverage has increased to 17% by the end of 2006, while High Speed Downlink Packet Access was launched commercially in December, providing a basis for an even wider range of services and content.

TP Group financial overview

Facing increasing competitive pressure and responding to targets approved by the Supervisory Board, the Group's key strategic goals in 2006 were:

– to optimise operating expenses through further rationalisation of TP Group's businesses;
– to improve efficiency of the investment processes so as to optimise capex investments and its prioritisation based on payback period and revenue generating capabilities;
– to promote growth areas (mobile, broadband);
– to introduce innovative and convergent services in mobile and fixed-line;
– to continue customer-centric operating principles;
– to continue to concentrate on improving the TP Group image with its customers;

– to ensure efficiency of IT as a key lever for business flexibility;
– to deliver a return to shareholders which is a reasonable reflection of the Group's financial position and market expectations;
– to promote predictable regulation according to the European Regulatory Framework and consistent with comparable benchmarks;
– to enhance internal control and risk management measures.

All guidance financial items as committed in 2006 by the Management have been met if not exceeded. Average GOM rate for the full year stands at 44.2%, while Net Free Cash Flow generation has been very strong, ending at over 4.1 billion PLN. The key Management's commitments in regards to initiatives fuelling growth and maintaining cost control and rebalancing resources have been delivered, including accelerating broadband access penetration, accelerating the number of mobile customers, introducing new convergent products and reallocating funds to growth areas. In 2006, the Group has implemented a number of new products in fixed, mobile markets and also convergent products.

In 2006, the Management Board has followed the Supervisory Board recommendation and developed the details of the dividend policy which takes into account the following:

– the uncertainty of the regulatory environment;
– the intensification of competition in TP's markets;
– the resource flexibility needed to sustain profitable growth in the form of capital expenditure as well as value-enhancing acquisitions;
– cash to be generated from disposal of assets;
– the financial discipline needed to support the current rating at BBB+/Baa1.

The dividend proposed for 2006 by the Management Board is consistent with that dividend policy and was discussed at various points during 2006 with the members of the Supervisory Board.

Conclusions and 2007 recommendations

Despite increased competition across all segments as well as intensifying regulatory pressure, TP Group has delivered satisfactory results in 2006. The Supervisory Board believes TP's Management Board has made the appropriate efforts to attain the 2006 strategic objectives. Moreover, TP, with its integrated offers, is able to create and exploit the new opportunities available on the communication services market in Poland.

TP has achieved, if not exceeded, all 2006 objectives through continued focus on top-line growth, new innovative offers and tighter cost controls. Innovative products and services have been successfully launched, which will help to compensate the inevitable fall in future fixed voice revenues.

In the Supervisory Board's opinion, in 2007 the Company should continue its efforts to further implement the key strategic goals as set for 2006 and also:

– optimise the management structure and decision making processes;
– optimise the real estate portfolio;
– perform an in-depth strategic exercise to analyse further development of the Group;
– review potential acquisitions and implement appropriate actions within appropriate investment criteria.

Report of the Remuneration Committee of the Supervisory Board of Telekomunikacja Polska S.A. in 2006

Andrew Seton
Supervisory Board Member and Chairman of the Remuneration Committee

During 2006, the Remuneration Committee consisted of three members of the Supervisory Board, chaired by an independent member, Mr. Andrew Seton. M. Andre Cathelineau ceased to be a member following his retirement from the Supervisory Board in April and was replaced by M. Jacques Champeaux. M. Michel Monzani remained a member of the Committee throughout the year.

The Committee met 18 times during 2006 to carry out its functions of reviewing nominations, as well as determining employment and remuneration terms for members of the Management Board ('MB'). The Committee in particular formulated recommendations to the Supervisory Board on bonus awards while agreeing targets for the Management Board for each performance period.

During 2006, besides carrying out the performance assessment of the Company's top management for each half year, the Committee worked with the Executive Vice-President to endorse a more objective MBO system and a bonus mechanism carrying greater risks and rewards for the MB beneficiaries. The Committee believes that management responded well to the incentives provided by the revised scheme and that the first half-year's performance merited an unusually high level of reward. However, given the changes at the top of the management hierarchy at TP S.A. in the second half of the year, not to mention the arrival of a new President of the Management Board, the Committee has accepted that some of the aspects of the current MBO and award system will need to change again early in 2007.

The Committee inevitably expended much of its time on the various high-profile management changes which took place during the course of the year. The most important of these was the search instituted for a new President of the Management Board. The Committee members formed part of a wider selection 'jury' consisting of Supervisory Board members and chaired by Mr. Seton. After systematic screening of a long-list of candidates with the aid of external professional advice, the jury interviewed several short-listed contenders and the new incumbent, Mr. Maciej Witucki, was duly recommended to the Supervisory Board for election in the autumn. The Committee also played a role in ensuring that the severance packages of the departing President of the Management Board and the Executive Vice-President were consistent with their contracts and appropriately recognised their respective important contributions to the Company.

The Committee continued to engage with management on detailed steps leading to the implementation of the Company's Stock Option Plan, which was approved by Shareholders at the April Annual General Meeting. In view of the management changes alluded to above, it was recognised that allocations under the scheme would have to be carried out in 2007.

Andrew Seton
Supervisory Board Member
and Chairman of the
Remuneration Committee
31 March 2007

Andrew Seton joined the Supervisory Board of TP in 2003 and later became 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 and has recently started work as an independent director of Dnister Bank in Western Ukraine. Mr. Seton had experience of the telecommunications sector while at Morgan Grenfell and EBRD, and also has a working knowledge of Polish.

Report of the Audit Committee of the Supervisory Board of Telekomunikacja Polska S.A. in 2006

Timothy Boatman
Chairman of the Audit Committee of the Supervisory Board

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 consultative body acting under the Supervisory Board.

The task of the Committee is to advise the Supervisory Board on the proper implementation of budget, financial reporting and internal control principles in the TP Group and to liaise with the auditors of TP Group.

Composition:

In 2006, the Audit Committee was composed of the following persons:

Chairman:
Mr. Timothy Boatman (Independent Director)

Members:
Mr. Andrew Seton (Independent Director, Chairman of the Remuneration Committee)
Mr. Michel Monzani
Mr. Claude Benmussa – resigned on September 21st 2006
Ms. Stephane Pallez – appointed on September 21st 2006

The Secretary of the Committee was:
Mr. Cezary Klimont – resigned on March 31st 2006
Mr. Herve Langer – acting Secretary from April 1st and appointed on July 25th 2006

Functions of the Committee:

The key functions of the Audit Committee include:

1 Monitoring of 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 of the internal and external auditors' work;
3 Review of interim and annual financial statements of the Company (TP S.A.'s separate accounts as well as TP Group's consolidated accounts), focusing in particular on:
   a any changes to accounting standards, policies and practices;
   b major judgmental areas;
   c significant adjustments arising from the audit;
   d compliance with accounting regulations;
4 Discussion (with or without the presence of the Company's Management Board) with external auditors on any problems or reservations resulting from the audit of financial statements;
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 Information to the Supervisory Board about all important issues within its scope of activity.

Activity in 2006:

The TP Group Audit Committee held 12 meetings in 2006, out of which nine were regular meetings and three dedicated ad-hoc meetings, and in particular performed the following:

- reviewed the Company's and Group's financial statements, notably the way risks were assessed by the Management; reviewed the Group's 2007 budget and addressed recommendations on it to the Supervisory Board;
- reviewed reports from the Executive Managers of the Group, from the Head of Internal Audit and from the external Auditors. It kept under review the scope and the results of the audits, 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. The Audit Committee received reports from Management on action plans in response to comments on internal controls from the internal and external auditors.
- reviewed preparation of the Group's anti-fraud and whistle-blowing programmes;
- reviewed implementation of internal control systems within the framework of the Sarbanes-Oxley Programme led at France Telecom group level;
- reviewed the 2006 cash distribution policy proposed by the Management and addressed recommendations to the Supervisory Board on it.

In the year under review, the Audit Committee, especially its two independent members, reviewed and approved related party transactions and received reports on them from the Company's Internal Audit.

Timothy Boatman
Chairman of the Audit Committee of the Supervisory Board
31 March 2007

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. Until 31st December 2006 he was 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.

Consolidated Income statement
for the year ended 31 December 2006

(Amounts in PLN millions, except for share data)	Note	year ended 31 December 2006 (audited)	year ended 31 December 2005 (restated)
Net revenues	6	18,625	18,342
External purchases	7	(7,438)	(6,971)
Other operating income	7	293	268
Other operating expense	7	(889)	(1,145)
Labour expenses	7	(2,352)	(2,381)
Gross operating margin		**8,239**	**8,113**
Employee profit-sharing	7	(24)	(30)
Depreciation and amortisation	15-16	(4,489)	(4,260)
Impairment of goodwill	8	–	(43)
Impairment of non-current assets	8	(80)	15
Gains on disposal of assets	9	6	43
Restructuring costs	10	(285)	(11)
Operating income		**3,367**	**3,827**
Interest expense and other financial charges	11	(654)	(852)
Foreign exchange losses	11	(6)	(24)
Discounting expense	11	(73)	(70)
Finance costs, net		**(733)**	**(946)**
Income tax	12	(538)	(361)
Consolidated net income after tax		**2,096**	**2,520**
Minority interest		(2)	(304)
Net income attributable to equity holders of TP S.A.		**2,094**	**2,216**
Earnings per share (in PLN) (basic and diluted)		**1.50**	**1.58**
Number of shares (in millions)		1,400	1,400

The notes to the consolidated financial statements are an integral part of this Consolidated Income statement

Consolidated Balance sheet
as at 31 December 2006

(Amounts in PLN millions)	Note	At 31 December 2006 (audited)	At 31 December 2005 (restated)
Assets			
Goodwill, net	14	3,994	3,994
Other intangible assets, net	15	3,286	3,466
Property, plant and equipment, net	16	21,686	23,512
Interests in associates		3	3
Assets available for sale	17	4	4
Other non-current financial assets and derivatives	17	1	22
Other non-current assets		5	7
Deferred tax assets	12	54	99
Total non-current assets		**29,033**	**31,107**
Inventories, net		196	245
Trade receivables, net	18	1,877	1,918
Other current assets	18	104	96
Current tax assets		6	61
Prepaid expenses	18	58	105
Other current financial assets and derivatives	17	33	122
Cash and cash equivalents	20	879	1,676
Total current assets		**3,153**	**4,223**
Assets held for sale	16	425	–
Total assets		**32,611**	**35,330**
Equity and liabilities			
Share capital	30	4,200	4,200
Share premium		832	832
Other reserves	23	(77)	(92)
Retained earnings		13,143	12,449
Translation adjustment		(8)	(8)
Equity attributable to equity holders of TP S.A.		**18,090**	**17,381**
Minority interest		13	13
Total equity		**18,103**	**17,394**
Bonds	21	3,432	5,554
Bank borrowings, loans and other financial debt	22	1,145	1,426
Derivatives	23	985	818
Non-current employee benefits	26	288	323
Other non-current provisions	28	271	127
Other non-current liabilities	29	764	781
Deferred tax liabilities	12	8	9
Deferred income	29	79	151
Total non-current liabilities		**6,972**	**9,189**
Bonds	21	1,817	1,929
Bank borrowings, loans and other financial debt	22	260	313
Loan from related party	19	–	1,000
Derivatives	23	386	482
Accrued interest payable	19	135	247
Current provisions	28	890	747
Trade payables		2,683	2,976
Current employee benefits	26	333	341
Other current liabilities	29	228	197
Current tax payable		358	126
Deferred income	29	446	389
Total current liabilities		**7,536**	**8,747**
Total equity and liabilities		**32,611**	**35,330**

The notes to the consolidated financial statements are an integral part of this Consolidated Balance sheet

Consolidated Statement of changes in equity
for the year ended 31 December 2006

(Amounts in PLN millions)	Number of shares in issue (in millions)	Share capital	Share premium	Other reserves: Financial assets available for sale	Other reserves: Hedging instruments	Other reserves: Deferred taxes	Translation adjustments	Retained earnings	Total	Minority interest	Total equity
Balance at January 1, 2005 (audited)	1,400	4,200	832	9	(95)	16	(8)	11,191	16,145	736	16,881
Changes in accounting policy		–	–	–	–	–	–	(496)	(496)	–	(496)
Balance at January 1, 2005 (restated)	1,400	4,200	832	9	(95)	16	(8)	10,695	15,649	736	16,385
Losses on cash flow hedges taken to equity		–	–	–	(18)	–	–	–	(18)	–	(18)
Gain or loss on financial assets available for sale		–	–	(9)	–	–	–	–	(9)	–	(9)
Tax on items taken directly to equity		–	–	–	–	5	–	–	5	–	5
Total income and expense recognised in equity		–	–	(9)	(18)	5	–	–	(22)	–	(22)
Net income for the year ended December 31, 2005		–	–	–	–	–	–	2,216	2,216	304	2,520
Total recognised income and expense for the period		–	–	(9)	(18)	5	–	2,216	2,194	304	2,498
Dividends		–	–	–	–	–	–	(462)	(462)	(1)	(463)
Sale of a subsidiary		–	–	–	–	–	–	–	–	(16)	(16)
Purchase of shares in PTK-Centertel		–	–	–	–	–	–	–	–	(1,010)	(1,010)
Balance at December 31, 2005 (restated)	1,400	4,200	832	–	(113)	21	(8)	12,449	17,381	13	17,394
Balance at January 1, 2006 (audited)	1,400	4,200	832	–	(113)	21	(8)	13,045	17,977	13	17,990
Changes in accounting policy		–	–	–	–	–	–	(596)	(596)	–	(596)
Balance at January 1, 2006 (restated)	1,400	4,200	832	–	(113)	21	(8)	12,449	17,381	13	17,394
Gains on cash flow hedges taken to equity		–	–	–	18	–	–	–	18	–	18
Tax on items taken directly to equity		–	–	–	–	(3)	–	–	(3)	–	(3)
Total income and expense recognised in equity		–	–	–	18	(3)	–	–	15	–	15
Net income for the year ended December 31, 2006		–	–	–	–	–	–	2,094	2,094	2	2,096
Total recognised income and expense for the period		–	–	–	18	(3)	–	2,094	2,109	2	2,111
Dividends		–	–	–	–	–	–	(1,400)	(1,400)	(2)	(1,402)
Balance at December 31, 2006 (audited)	1,400	4,200	832	–	(95)	18	(8)	13,143	18,090	13	18,103

The notes to the consolidated financial statements are an integral part of this Consolidated Statement of changes in equity

Consolidated Statement of cash flows
for the year ended 31 December 2006

(Amounts in PLN millions)	year ended 31 December 2006 (audited)	year ended 31 December 2005 (restated)
Operating activities		
Net income attributable to equity holders of TP S.A.	2,094	2,216
Adjustments to reconcile net income to funds generated from operations		
Depreciation and amortisation	4,489	4,260
Gains on disposal of assets	(6)	(43)
Impairment of non-current assets	80	(15)
Impairment of goodwill	–	43
Change in other provisions	67	363
Income tax	538	361
Interest income and expense	516	450
Minority interest	2	304
Foreign exchange (gains)/ losses, net	(266)	(154)
Derivatives	626	655
Change in working capital (trade)		
Decrease/(increase) in inventories (net)	47	(68)
Decrease in trade accounts receivable	210	177
Increase/(decrease) in trade accounts payable	(211)	166
Change in working capital (non-trade)		
Increase in other receivables	(7)	(105)
Decrease in accrued expenses, other payables and deferred income	(8)	(83)
Dividends and interest income received	46	159
Interest paid and interest rate effects on derivatives, net	(777)	(963)
Income tax paid	(215)	(503)
Net cash provided by operating activities	**7,225**	**7,220**
Investing activities		
Purchases/sales of property, plant and equipment and intangible assets		
Purchases of property, plant and equipment and intangible assets	(3,000)	(3,046)
Decrease in amounts due to fixed asset suppliers	(93)	(163)
Proceeds from sale of property, plant and equipment and intangible assets	13	110
Purchase of PTK-Centertel shares (including repayment of related party loan)	(1,000)	(3,919)
Purchase of Wirtualna Polska shares	–	(217)
Proceeds from sale of Intelsat shares	–	25
Proceeds from sale of other investment securities and businesses, net of cash transferred	1	4
Effect on derivatives accounted for as a trade, net	(182)	(42)
Net cash used in investing activities	**(4,261)**	**(7,248)**
Financing Activities		
Redemptions and repayment		
Redemption of bonds	(1,930)	(300)
Repayment of long-term debt	(318)	(476)
Decrease in bank overdrafts and other short-term borrowings	–	(11)
Dividends paid	(1,402)	(463)
Exchange rate effects on derivatives accounted for as a hedge, net	(102)	(56)
Net cash used in financing activities	**(3,752)**	**(1,306)**
Net change in cash and cash equivalents	(788)	(1,334)
Effect of changes in exchange rates on cash and cash equivalents	(9)	2
Cash and cash equivalents at the beginning of the period	1,676	3,008
Cash and cash equivalents at the end of the period	**879**	**1,676**

The notes to the consolidated financial statements are an integral part of this Consolidated Statement of cash flows

1 Corporate information

1.1 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. The Telekomunikacja Polska Group ('the Group') comprises Telekomunikacja Polska and its subsidiaries.

The Group is the principal supplier of telecommunications services in Poland. 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. PTK-Centertel provides also third generation UMTS services. In addition, the Group provides leased lines, radio-communications and other telecommunications value added services, sells telecommunications equipment, produces electronic phone cards and provides data transmission, telephone directories, multimedia services and various Internet services.

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

Based on decisions issued by Telecommunications and Postal Service Regulatory Office ('URTiP', precursor of 'UKE' – Office of Electronic Communications) under the previous Telecommunications Act enacted in 2000, Telekomunikacja Polska has significant market power (SMP) on the domestic market for public fixed network telecommunications services (which has been related to the additional obligation to general service rendering from the moment of designating the Company as a general service operator), 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.

URTiP successor, UKE designated the Company as having significant market power on the telephone links beginning market in public fixed network telecommunications and also on the telephone links ending market in the Company's public fixed network telecommunications till the end of 2006. PTK-Centertel was designated as having significant market power on call termination market in its own network. That being so, the previous legally binding regulatory obligations have been replaced by the new ones imposed in accordance with the Act from 2004.

According to a UKE decision, since May 2006 TP S.A. has been an operator designated for general service rendering.

1.2 Entities of the Group

The Group comprises Telekomunikacja Polska and the following subsidiaries and associates:

Entity	Location	Scope of activities	Share capital owned by the Group 31 December 2006	31 December 2005
PTK-Centertel Sp. z o.o.	Warsaw, Poland	Construction and operation of mobile telecommunications networks and services.	100.00%	100.00%
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.)	Gdynia, Poland	E-commerce and electronic services, including GSM prepaid services, bill charging and processing of electronic financial transactions.	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%
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 Internet Sp. z o.o. ('TP Internet')	Warsaw, Poland	Call-centre services.	100.00%	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 [4][5]	Warsaw, Poland	Publishing and advertising services.	n/a	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. [2]	Opalenica, Poland	Local fixed-line telecommunications operator.	25.00%	25.00%
– Radomska Wytwórnia – Telekomunikacyjna S.A. in a state of insolvency [2]	Radom, Poland	Manufacturing of telephones.	17.50%	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%
Fundacja Grupy TP	Warsaw, Poland	Charity foundation.	100.00%	100.00%
Virgo Sp. z o.o. [1]	Warsaw, Poland	Advisory services, financial operations and property investments management.	100.00%	100.00%
– Wirtualna Polska S.A. ('WP') [3]	Gdańsk, Poland	Internet portal and database services, software and advertising services.	100.00%	100.00%
– Sklep Wirtualnej Polski S.A. in liquidation [4]	Gdańsk, Poland	No operational activities.	100.00%	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%

[1] As at 31 December 2005 100% of share capital in Wirtualna Polska S.A. and Sklep Wirtualnej Polski S.A. in liquidation was held by TP Internet Sp. z o.o.
[2] Associates accounted for under the equity method (except for Radomska Wytwórnia Telekomunikacyjna S.A. as at 31 December 2006 – for details see Note 5)
[3] Fully consolidated from 9 September 2005
[4] Excluded from consolidation due to immateriality of amounts involved
[5] As at 31 December 2006 the Group did not own shares in Tel – Arp Sp. z o.o. because on 22 November 2006 the company was crossed off the National Court Register.

1 Corporate information continued

1.2 Entities of the Group continued

In the years ended 31 December 2006 and 2005 the voting power held by the Group was equal to the Group's interest in the share capital of all of its subsidiaries and associates.

The main changes in the Group structure and consolidation scope in the year ended 31 December 2006 and 2005 are set out in Note 5.

1.3 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:

Maciej Witucki – President & CEO,
Benoît Mérel – Board Member (CFO),
Pierre Hamon – Board Member (Marketing, Sales and Customer Services),
Konrad Kobylecki – Board Member (Networks, Carriers & IT),
Jacek Kałłaur – Board Member (Human Resources),
Jean-Marc Vignolles – Board Member (CEO of PTK-Centertel).

Changes in the Management Board in the year ended 31 December 2006:

– on 28 April 2006, Mr. Benoît Mérel was appointed as Member of the Management Board of TP S.A.;
– on 26 July 2006, Mr. Bruno Duthoit resigned from the Management Board of TP S.A. with effect on 16 August 2006;
– on 28 August 2006, Mr. Maciej Witucki was appointed as President of the Management Board of TP S.A. with effect on 6 November 2006;
– on 23 October 2006, Mr. Marek Józefiak resigned from the position of President of the Management Board of TP S.A. with effect on 5 November 2006;
– on 9 November 2006, Mr. Alain Carlotti resigned from the position of Executive Vice-President of the Management Board of TP S.A. with effect on 10 November 2006.

2 Statement of compliance and basis for preparation

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

Comparative amounts for the year ended 31 December 2005 have been compiled using the same basis of preparation.

The principles applied to prepare financial data relating to the year ended 31 December 2006 are described in Note 3 and are based on:
– all standards and interpretations endorsed by the European Union and applicable with effect from 1 January 2006;
– IASs/IFRSs and related interpretations adopted for use by the European Union whose application will be compulsory after 1 January 2006 but for which the Group has opted for earlier application;
– accounting positions adopted by the Group in accordance with paragraphs 10 to 12 of IAS 8.

In preparing the Group's accounts, the Company's management is required to make estimates, insofar as many elements included in the financial statements cannot be measured with precision. Management reviews these estimates if the circumstances on which they were based evolve, or in the light of new information or experience. Consequently, estimates made as at 31 December 2006 may be subsequently changed.

Lastly, where a specific transaction is not dealt with in any standard or interpretation, management uses its judgment in developing and applying an accounting policy that results in information that is relevant and reliable, in that the financial statements:
– represent faithfully the Group's financial position, financial performance and cash flows,
– reflect the economic substance of transactions,
– are neutral,
– are prudent, and
– are complete in all material respects.

The consolidated financial statements have been prepared under the historical cost convention, except for the fair value applied to derivative financial instruments, financial assets available for sale, assets held for sale and gains or losses on debt that is hedged against exposure to changes in fair value.

These consolidated financial statements are prepared in millions of Polish zloty ('PLN') and were authorised for issuance by the Management Board on 15 February 2007.

3 Significant accounting policies and changes in estimates

3.1 Significant accounting policies

This note describes the accounting principles applied to prepare consolidated financial statements for the years ended 31 December 2006 and 2005.

3.1.1 Application of new standards, amendments and interpretations

In 2006, the Group adopted the following amendments to existing accounting standards and new interpretations:
– Amendments to IAS 39 'Financial Instruments: Recognition and Measurement. The fair value option',
– Amendments to IAS 39 'Financial Instruments: Recognition and Measurement. Cash Flow Hedge Accounting of Forecast Intragroup Transactions',
– Amendments to IAS 39 'Financial Instruments: Recognition and Measurement. Financial Guarantee Contracts',
– IFRIC 4 'Determining Whether an Arrangement Contains a Lease',
– IFRIC 6 'Liabilities arising from Participating in a Specific Market-Waste Electrical and Electronic Equipment'.

The adoption of these amendments to the accounting standards and new interpretations did not result in any significant changes to the Group accounting policies.

The Group has not opted for early application of the following standards, amendments and interpretations (already adopted or in the process of being adopted by the European Union):
– IFRIC 8 'Scope of IFRS 2', applicable for financial years beginning after 1 May 2006,
– IFRIC 9 'Reassessment of Embedded Derivatives', applicable for financial years beginning after 1 June 2006,
– IFRS 7 'Financial Instruments – Disclosures', applicable for financial years beginning after 1 January 2007,
– Amendments to IAS 1 'Presentation of Financial Statements – Capital Disclosures', applicable for financial years beginning after 1 January 2007,
– IFRIC 10 'Interim Financial Reporting and Impairment', applicable for financial years beginning after 1 November 2006,
– IFRIC 11 'IFRS 2 – Group and Treasury Share Transactions', applicable for financial years beginning after 1 March 2007,
– IFRIC 12 'Service Concession Arrangements' applicable for financial years beginning after 1 January 2008,
– IFRS 8 'Operating Segments' applicable for financial years beginning after 1 January 2009.

The Group is currently analysing the practical consequences of these new standards and interpretations and the impact of their application on its financial statements.

The following are not relevant to the Group: standard IFRS 6 'Exploration for and Evaluation of Mineral Resources' and interpretations IFRIC 5 'Rights to Interests arising from the Decommissioning, Restoration and Environmental Rehabilitation Funds' and IFRIC 7 'Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies', as well as Amendments to IAS 19 'Employee Benefits' issued on 16 December 2004 and Amendment to IAS 21 'The Effects of Changes in Foreign Exchange Rates – Net Investment in a Foreign Operation'.

3.1.2 Accounting positions adopted by the Group in accordance with paragraphs 10 to 12 of IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors

The accounting position described below are not specifically dealt with by any standards or interpretations endorsed by the European Commission.

Acquisitions of minority interests in a subsidiary already controlled by the Group
These transactions are not addressed in any IAS or IFRS. Therefore goodwill is recognised as the difference between the cost of acquisition of minority interests and minority interests in the book value of the underlying net assets, without making any fair value adjustments to the assets and liabilities acquired.

3.1.3 Options available under IASs/IFRSs and used by the Group

Certain IASs/IFRSs offer alternative methods of measuring and recognising assets and liabilities. In this respect, the Group has chosen:
– to continue to recognise inventories at their original cost, determined by the weighted average unit cost method, in accordance with IAS 2 'Inventories',
– to measure property, plant and equipment using historical cost instead of remeasuring fair value at each closing, in accordance with IAS 16 'Property, Plant and Equipment' and IAS 38 'Intangible Assets',
– not to capitalise interest expense incurred during the construction and acquisition period of property, plant and equipment, as provided for under IAS 23 'Borrowing Costs',
– to recognise actuarial gains and losses on post-employment benefit obligations according to the corridor method. This method consists of recognising a specified portion of the net cumulative actuarial gains and losses that exceed 10% of the present value of the defined benefit obligation over the average expected remaining working lives of the employees participating in the plan, in accordance with IAS 19 'Employee Benefits'.

3 Significant accounting policies and changes in estimates continued

3.1.4 Presentation of the financial statements

Comparative amounts for the year ended 31 December 2005 have been restated taking into account the new format of presentation. In addition, certain reclassifications were made to provide more adequate and reliable information. These changes did not impact revenue, net profit and shareholders' equity.

Under current presentation, gross operating margin corresponds to operating income (that is, net profit before financial income, finance costs, income taxes) before:
– employee profit-sharing,
– depreciation and amortisation expense,
– impairment of goodwill and other non-current assets,
– gains and losses on disposal of assets,
– restructuring costs.

Major changes in the presentation of other items are described below:

Consolidated income statement for the year ended 31 December 2005
– operating profit presented in these consolidated financial statements is increased by PLN 46 million in comparison to that previously reported due to reclassification of the results on disposal of certain investments previously classified as financial activity.

Consolidated balance sheet as at 31 December 2005
– reclassification of goodwill from intangible assets to a separate line amounting to PLN 3,994 million,
– reclassification of construction in progress related to intangible assets from property, plant and equipment to other intangible assets line including certain changes in classification in amount of PLN 329 million,
– amounts of employee benefits are presented in separate lines of consolidated balance sheet,
– other reclassifications than those mentioned above are presented in Note 3.1.5.

Consolidated cash flow for the year ended 31 December 2005
– cash flows related to interest paid amounted to PLN 1,438 million and interest received on derivatives accounted for as a hedge amounted to PLN 485 million are presented in operating activities while previously they were presented in financing activities as interest paid and interest received on derivative transactions,
– items previously reported as changes in working capital are divided between trade and non-trade parts and there is a separate line for changes in other provisions,
– change in the presentation of Social Fund assets and liabilities as described in Note 3.1.5.

3.1.5 Other reclassifications

Social Fund
In accordance with Polish Law, the Group's entities, registered in Poland, administer a Social Fund on behalf of their respective employees. The contributions paid to the Social Fund are deposited in separate bank accounts held by the Company and its subsidiaries. The fund is used to pay for various benefits used by the employees of the Group and to provide employees with housing loans. In 2005, all assets and funds which belonged to the Fund were presented gross (cash, loans, etc.) in the Group balance sheet. In 2006, these assets and funds are disclosed below and will not be added to the assets and liabilities of the Group. The comparatives as disclosed in these consolidated financial statements have been restated, however, this restatement does not impact the shareholders' funds and net profit.

As at 31 December 2006 and 2005, cash balances for the Social Fund amounted to PLN 32 million and PLN 26 million, respectively. Receivables relating to Social Fund loans to employees as at 31 December 2006 and 2005 amounted to PLN 118 million and PLN 109 million, respectively. Liabilities related to the Social Fund as at 31 December 2006 and 2005 amounted to PLN 150 million and PLN 135 million, respectively.

Accounting for government grants and disclosure of government assistance
International Accounting Standard 20 'Accounting for government grants and disclosure of government assistance' presents two allowed alternatives of treatment of investment grants and fixed assets granted for free. Under the first option, the grants related to assets are presented in the balance sheet as deferred income. This treatment was followed by the Group before 2006.

At the beginning of 2006, the Group changed the presentation of grants and adopted the second alternative, which allows deduction of the grants in arriving at the carrying amount of the asset. The grant is recognised as income over the life of the depreciable asset by way of a reduced depreciation charge.

As a result, the deferred income and related fixed assets as at 31 December 2006 and 2005 decreased by PLN 196 and 216 million, respectively.

3.1.6 Changes in accounting policies

Hedge accounting
In accordance with IAS 39 for fair value hedges, the gain or loss on the hedged item attributable to the hedged risk shall adjust the carrying amount of the hedged item and be recognised in profit or loss. Par. 92 of the IAS 39 provides that the recognition of any adjustment described above in profit or loss (amortisation) may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value.

Based on these alternatives the Group elected to amortise the fair value adjustment starting from the earliest possible date rather than recognition at the end of the hedge relationship what was applied in prior periods.

The new methodology eliminated certain inconsistencies in the application of the model previously used and aligned the Group's accounting to IFRS interpretations that are generally used.

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 profit for the year ended 31 December 2005	Net assets as at 31 December 2005	Total assets as at 31 December 2005
Data previously reported	**2,316**	**17,990**	**35,273**
IAS 39 – hedge accounting (after tax)	(100)	(596)	57
Data adjusted	**2,216**	**17,394**	**35,330**

As a result of changes in the accounting policies described above value of debt increased by PLN 736 million as at 31 December 2005 and earnings per share for the year ended 31 December 2005 decreased by PLN 0.07.

Changes in off-balance sheet commitments presentation
As at 31 December 2006 the Group changed its presentation of the amount of contractual commitments for the acquisition of property, plant and equipment and intangible assets.

Under previously applied policy, the TP Group disclosed capital investment commitments contracted under individual agreements being part of framework purchase arrangements only if penalties for non realisation were included in the contract. Currently, investment commitments are extended to include framework purchase arrangements that will result in an outflow of resources to another party without regard to penalty clauses.

The change in presentation was applied retrospectively. As a result capital commitments as at 31 December 2005 amounted to PLN 526 million.

3.1.7 Earnings 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.

3.1.8 Consolidation rules

Subsidiaries that are controlled exclusively by Telekomunikacja Polska, directly or indirectly, are fully consolidated. Control is deemed to exist when the Group owns more than 50% of the voting rights of an entity (unless it can be clearly demonstrated that such ownership does not constitute control), or when one of the following four criteria is met:
– power over more than one half of the voting rights of the other entity by virtue of an agreement ,
– power to govern the financial and operating policies of the other entity under a statute or agreement,
– power to appoint or remove the majority of the members of the management board or equivalent governing body of the other entity,
– power to cast the majority of votes at meetings of the management board or equivalent governing body of the other 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.

Companies over which Telekomunikacja Polska exercises significant influence (generally corresponding to an ownership of 20% to 50%) are accounted for using the equity method.

Intercompany transactions and balances are eliminated in consolidation. The consolidated financial statements are prepared using uniform accounting policies for similar transactions and other events in similar circumstances.

3 Significant accounting policies and changes in estimates continued

3.1.9 Effect of changes in foreign exchange rates

Translation of financial statements of foreign subsidiaries
The financial statements of foreign subsidiaries whose functional currency in not the zloty are translated into the Group presentation currency as follows:
– assets and liabilities are translated at the National Bank of Poland ('NBP') period-end exchange rate,
– items in the statement of income are translated at the NBP average rate for the reporting period,
– the translation adjustment resulting from the use of these different rates is included as a separate component of shareholders' equity.

Transactions in foreign currencies
The principles covering the measurement and recognition of transactions in foreign currencies are set out in IAS 21 'The Effects of Changes in Foreign Exchange Rates'. Transactions in foreign currencies are converted by the Group into its functional currency at the exchange rate at the transaction date used by the bank where the transaction is conducted. Monetary assets and liabilities which are denominated in foreign currencies are remeasured at each balance sheet date at the period-end exchange rate quoted by NBP and the resulting translation differences are recorded in the income statement:
– in other operating income for commercial transactions;
– in financial income or finance costs for financial transactions.

Derivative instruments are measured and recognised in accordance with the general principles described in Note 3.1.19. Currency derivatives are recognised in the balance sheet at fair value at each period-end. Gains and losses arising from remeasurement at fair value are recognised:
– in other operating income for fair value hedges of commercial transactions;
– in financial income or finance costs for hedges of financial assets and liabilities and derivative instruments that do not qualify for hedge accounting.

3.1.10 Net revenue

Revenues from the Group activities are recognised and presented as follows, in accordance with IAS 18 'Revenue'.

Equipment sales
Revenues from equipment sales are recognised when the significant risks and rewards of ownership are transferred to the buyer (see also paragraph 'Separable components of packaged and bundled offers').

Equipment rentals
In accordance with IFRIC 4 'Determining Whether an Arrangement Contains a Lease', equipment for which a right of use is granted is analysed in accordance with IAS 17 'Leases'.

Equipment lease revenues are recognised on a straight-line basis over the life of the lease agreement, except in the case of finance leases which are accounted for as sales on credit.

Service revenues
Telephone service and Internet access subscription fees are recognised in revenue on a straight-line basis over the service period.

Charges for incoming and outgoing telephone calls are recognised in revenue when the service is rendered.

Revenues from the sale of phone cards in fixed and mobile telephony systems are recognised when they are used or expire.

Revenue-sharing arrangements (premium rate numbers, audiotel, special numbers for Internet dial-up) are recognised gross, or net of content or service provider fees when the provider is responsible for the service rendered and for setting the price to be paid by subscribers. Revenues from the supply of content are also recognised gross, or net of the amount due to the content provider, when the latter is responsible for the service content and for setting the price to subscribers.

Revenues from Internet advertising and from the sale of advertising space in online telephone directories are recognised over the period during which the advertisement appears. Revenues from the sale of advertising space in printed telephone directories are recognised when the directory is published.

Separable components of packaged and bundled offers
Sales of packaged mobile and Internet offers are considered as comprising identifiable and separate components to which general revenue recognition criteria can be applied separately. Numerous service offers on the Group's main markets are made up of two components, a product (e.g. mobile handset / internet modem) and a service. Once the separate components have been identified, the amount received or receivable from the customer is allocated based on each component's fair value. The sum allocated to delivered items is limited to the amount that is not dependent on the delivery of other items. For example, the sum allocated to delivered equipment generally corresponds to the price paid by the end-customer for that equipment. The balance of the amount received or receivable is contingent upon the future delivery of the service.

Offers that cannot be analysed between separately identifiable components, because the commercial effect cannot be understood without reference to the series of transactions as a whole, are treated as bundled offers. Revenues from bundled offers are recognised in full over the life of the contract. The main example is connection to the service: this does not represent a separately identifiable transaction from the subscription and communications, and connection fees are therefore recognised over the average expected life of the contractual relationship.

Promotional offers
Revenues are stated net of discounts. For certain commercial offers where customers are offered a free service over a certain period in exchange for signing up for a fixed period (time-based incentives), the total revenue generated under the contract is spread over the fixed, non cancelable period.

Loyalty programs
Loyalty programs consist of granting future benefits to customers (such as call credit and product discounts) in exchange for present and past use of the service (volume-based incentives). A loyalty program that exist within the Group is without a contract renewal obligation. The Group defers part of the invoiced revenue over the vesting period of the related customer rights based on the fair value of these obligations.

3.1.11 Subscriber acquisition costs, advertising and related costs

Subscriber acquisition and retention costs, other than loyalty program costs (see Note 3.1.10), are recognised as an expense for the period in which they are incurred.

Advertising, promotion, sponsoring, communication and brand marketing costs are also expensed as incurred.

3.1.12 Borrowing costs

The Group does not capitalise interest expense for the period of construction and acquisition of property, plant and equipment and intangible assets.

3.1.13 Share issuance costs

External costs directly related to share issues are deducted from the related share premium, net of any tax saving. Other costs are expensed as incurred.

3.1.14 Goodwill

Goodwill is the excess of the purchase cost of shares in consolidated companies, including transaction expenses, over the Group's corresponding share in the fair value of the underlying net assets at the date of acquisition. Goodwill represents a payment made in anticipation of future economic benefits from assets that are not capable of being individually identified and separately recognised.

Impairment tests and Cash Generating Units
In accordance with IFRS 3 'Business Combinations', goodwill is not amortised but is tested for impairment at least once a year or more frequently when there is an indication that it may be impaired. IAS 36 'Impairment of Assets' requires these tests to be performed at the level of each Cash Generating Unit (CGU) to which the goodwill has been allocated (a Cash Generating Unit is defined as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets).

Recoverable amount
To determine whether goodwill has been impaired, the carrying value of the assets and liabilities of the CGU (or group of CGUs), including allocated goodwill, is compared to its recoverable amount. The recoverable amount of a CGU is the higher of its fair value less costs to sell and its value in use.

Fair value less costs to sell is the best estimate of the amount realisable from the sale of a CGU in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. This estimate is determined on the basis of available market information taking into account specific circumstances.

Value in use is the present value of the future cash flows expected to be derived from the CGU or group of CGUs, including goodwill. Cash flow projections are based on economic and regulatory assumptions, license renewal assumptions and forecast trading conditions drawn up by the Group management, as follows:
– cash flow projections are based on the five-year business plan,
– cash flow projections beyond the five-year timeframe are extrapolated by applying a declining or flat growth rate over the next two years, followed by a growth rate to perpetuity reflecting the expected long-term growth in the market,
– the cash flows obtained are discounted using appropriate rates for the type of business concerned.

Goodwill impairment losses are recorded in the income statement as a deduction from operating income.

3 Significant accounting policies and changes in estimates continued

3.1.15 Intangible assets

Intangible assets, consisting mainly of licenses, software and development costs, are stated at acquisition or production cost.

When intangible assets are acquired in a business combination, their cost is generally determined in connection with the purchase price allocation based on their respective market values. When their market value is not readily determinable, cost is determined using generally accepted valuation methods based on revenues, costs or other appropriate criteria.

Internally developed trademarks and subscriber bases are not recognised in intangible assets.

Licenses
Licenses to operate mobile telephone networks are amortised on a straight-line basis over the license period from the date when the network is technically ready and the service can be marketed. For the details of concessions values see Note 15.

Research and development costs
Under IAS 38 'Intangible Assets', development costs should be recognised as an intangible asset if and only if the following can be demonstrated:
– the technical feasibility of completing the intangible asset so that it will be available for use,
– the intention to complete the intangible asset and use or sell it and the availability of adequate technical, financial and other resources for this purpose,
– the ability to use or sell the intangible asset,
– how the intangible asset will generate probable future economic benefits for the Group,
– the Group's ability to measure reliably the expenditure attributable to the intangible asset during its development.

Research costs, and development costs not fulfilling the above criteria, are expensed as incurred. Development costs recognised as an intangible asset are amortised on a straight-line basis over their estimated useful life, generally not exceeding four years.

Software
Software is amortised on a straight-line basis over the expected life, not exceeding five years.

3.1.16 Property, plant and equipment

Cost
The cost of tangible assets corresponds to their purchase or production cost, including costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

It also includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, representing the obligation incurred by the Group.

The cost of networks includes design and construction costs, as well as capacity improvement costs. The total cost of an asset is allocated among its different components and each component accounted for separately, when the components have different useful lives or when the pattern in which their future economic benefits are expected to be consumed by the entity varies. Depreciation is then revised accordingly.

Government grants
The Group may receive non-repayable government grants in the form of direct or indirect funding of capital projects, mainly provided by local and regional authorities. These grants are deducted from the cost of the related assets and recognised in the income statement, based on the pattern in which the related asset's expected future economic benefits are consumed.

Finance leases
Assets acquired under leases that transfer the risks and rewards of ownership to the Group are recorded as assets and an obligation in the same amount is recorded in liabilities. The risks and rewards of ownership are considered as having been transferred to the Group when:
– the lease transfers ownership of the asset to the lessee by the end of the lease term,
– the Group has the option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised,
– the lease term is for the major part of the estimated economic life of the leased asset,
– at the inception of the lease, the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset,
– the leased assets are of such a specialised nature that only the lessee can use them without major modifications.

Assets leased by the Group as lessor under leases that transfer the risks and rewards of ownership to the lessee are treated as having been sold.

Maintenance and repair costs are expensed as incurred, except where they serve to increase the asset's productivity or prolong its useful life.

Depreciation
Items of property, plant and equipment are depreciated to write off their cost less any residual value on a basis that reflects the pattern in which their future economic benefits are expected to be consumed. Therefore, the straight-line basis is usually applied over the following estimated useful lives:

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

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

These useful lives are reviewed annually and are adjusted if current estimated useful lives are different from previous estimates. These changes in accounting estimates are recognised prospectively (see Note 3.2).

3.1.17 Non-current assets held for sale

Non-current assets held for sale are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather then continuing use. Those assets are available for immediate sale in their present conditions subject only to terms that are usual and customary for sales of such assets and the sale is highly probable.

Non-current assets held for sale are measured at the lower of carrying amount and estimated fair value less costs to sell and are presented in a separate line in balance sheet if IFRS 5 requirements are met.

3.1.18 Impairment of non-current assets other than goodwill

In the case of an other-than-temporary decline in the recoverable amount of an item of property, plant and equipment or an intangible asset to below its net book value, due to events or circumstances occurring during the period (such as obsolescence, physical damage, significant changes in the manner in which the asset is used, worse than expected economic performance, a drop in revenues or other external indicators) an impairment loss is recognised.

For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separable indefinable cash flows ('cash-generating unit'). Each group of assets is tested for impairment by comparing its recoverable amount to its net book value. When an asset or group of assets is found to be impaired, the recognised impairment loss is equal to the difference between its net book value and recoverable amount.

The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

The recoverable amount of an asset is generally determined by reference to its value in use, corresponding to the future economic benefits expected to be derived from the use of the asset and its subsequent disposal. It is assessed by the discounted cash flows method, based on management's best estimate of the set of economic conditions that will exist over the remaining useful life of the asset and the asset's expected conditions of use.

3.1.19 Financial assets and liabilities

Financial assets include available-for-sale assets, held-to-maturity assets, assets at fair value through profit and loss, derivative instruments, loans and receivables and cash and cash equivalents.

Financial liabilities include borrowings, other financing and bank overdrafts, derivative instruments and accounts payable.

Financial assets and liabilities are measured and recognised in accordance with IAS 39 'Financial Instruments: Recognition and Measurement'.

A regular way purchase or sale of financial assets is recognised using settlement date accounting.

Measurement and recognition of financial assets
When financial assets are recognised initially, they are measured at fair value plus, in the case of investments not at fair value through profit and loss, directly attributable transaction costs.

Held-to-maturity assets
Held-to-maturity assets are non-derivative financial assets with fixed or determinable payments and fixed maturity, other than loans and receivables, that the Group has the positive intention and ability to hold to maturity. They are recognised initially at fair value and are subsequently measured at amortised cost by the effective interest method.

At each balance sheet date, the Group assesses whether there is any objective evidence that held-to-maturity assets are impaired. If any such evidence exists, the asset's recoverable amount is calculated. If the recoverable amount is less than the asset's book value, an impairment loss is recognised in the income statement.

3 Significant accounting policies and changes in estimates continued

3.1.19 Financial assets and liabilities continued

Available-for-sale assets
Available-for-sale assets consist mainly of shares in non-consolidated companies and marketable securities that do not fulfill the criteria for classification in any of the other categories of financial assets. They are measured at fair value and gains and losses arising from remeasurement at fair value are recognised in equity. Fair value corresponds to market price for listed securities and estimated fair value for unlisted securities, determined according to the most appropriate financial criteria in each case.

When there is objective evidence that available-for-sale assets are impaired, the cumulative impairment loss included in equity is taken to the income statement.

Loans and receivables
Loans and receivables include loans to and receivables from non-consolidated companies, other loans and receivables and trade receivables. They are recognised initially at fair value and are subsequently measured at amortised cost by the effective interest method. Short-term receivables with no stated interest rate are measured at the original invoice amount if the effect of discounting is immaterial. Cash flows on loans and receivables at variable rates of interest are remeasured periodically, to take into account changes in market interest rates.

At each balance sheet date, the Group assesses whether there is any objective evidence that loans or receivables are impaired. If any such evidence exists, the asset's recoverable amount is calculated. If the recoverable amount is less than the asset's book value, an impairment loss is recognised in the income statement.

Assets at fair value through profit or loss
Assets at fair value through profit or loss are assets held for trading that the Group acquired principally for the purpose of selling them in the near term in order to realise a profit, that form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. This category also includes assets not fulfilling the above criteria that the Group has opted to measure using the fair value option.

Assets at fair value through profit or loss, consisting mainly of derivatives and mutual fund units, are carried in the balance sheet under 'Other current financial assets and derivatives'.

Cash and cash equivalents
Cash and cash equivalents are held primarily to meet the Group's short-term cash needs rather than for investment or other purposes. They consist of cash in bank and on hand and highly-liquid instruments that are readily convertible into known amounts of cash and are not exposed to any material risk of impairment.

Measurement and recognition of financial liabilities

Financial liabilities
With the exception of financial liabilities held for trading and derivative instruments which are measured at fair value through profit or loss, borrowings and other financial liabilities are initially recognised at fair value and subsequently measured at amortised cost by the effective interest method.

Transaction costs that are directly attributable to the acquisition or issue of the financial liability are deducted from the liability's carrying value. This is because financial liabilities are initially recognised at cost, corresponding to the fair value of the sums paid or received in exchange for the liability. The costs are subsequently amortised over the life of the debt, by the effective interest method.

The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial instrument or, when appropriate, through the period to the next interest adjustment date, to the net carrying amount of the financial liability. The calculation includes all fees and points paid or received between parties to the contract.

Certain borrowings are designated as being hedged by fair value hedges. A fair value hedge is a hedge of the exposure to changes in fair value of a recognised liability or an identified portion of the liability, that is attributable to a particular risk and could affect profit or loss. Gain or loss on hedged borrowing attributable to a hedged risk adjusts the carrying amount of a borrowing and is recognised in a profit and loss account.

Certain borrowings are designated as being hedged by cash flow hedges. A cash flow hedge is a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with a recognised liability or a highly probable forecast transaction (such as a purchase or sale) and could affect profit or loss.

Financial liabilities held for trading
Financial liabilities held for trading are measured at fair value.

Measurement and recognition of derivative instruments
Derivative instruments are recognised in the balance sheet and measured at fair value. 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 as explained below, gains and losses arising from remeasurement at fair value of derivative instruments are systematically recognised in the income statement.

Hedging instruments
Derivative instruments may be designated as fair value hedges or cash flow hedges:
– a fair value hedge is a hedge of the exposure to changes in fair value of a recognised asset or liability or an identified portion of the asset or liability, that is attributable to a particular risk – notably interest rate and currency risks – and could affect profit or loss,
– a cash flow hedge is a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (such as a future purchase or sale) and could affect profit or loss.
A hedging relationship qualifies for hedge accounting when:
– at the inception of the hedge, there is formal designation and documentation of the hedging relationship,
– at the inception of the hedge and in subsequent periods, the hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated (i.e. the actual results of the hedge are within the range of 80-125 per cent).

The effects of applying hedge accounting are as follows:
– for fair value hedges of existing assets and liabilities, the change in fair value of the hedged portion of the asset or liability attributable to the hedged risk adjusts the carrying amount of the asset or liability in the balance sheet. The gain or loss from the changes in fair value of the hedged item is recognised in profit or loss and is offset by the effective portion of the loss or gain from remeasuring the hedging instrument at fair value,
– for cash flow hedges, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity – because the change in the fair value of the hedged portion of the underlying item is not recognised in the balance sheet
– and the ineffective portion of the gain or loss on the hedging instrument is recognised in profit or loss. Amounts recognised directly in equity are subsequently recognised in profit or loss in the same period or periods during which the hedged item affects profit or loss.

Derecognition of financial assets and liabilities

Financial assets
A financial asset (or where applicable a part of financial assets or part of a group of similar financial assets) is derecognised where:
– the rights to receive cash flows from the asset have expired,
– the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement, or
– the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the assets, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Financial liabilities
A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

3.1.20 Inventories

Inventories are stated at the lower of cost and net realisable value, except for mobile handsets or other terminals sold in promotional offers. Inventories 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. Cost corresponds to purchase or production cost determined by the weighted average cost method.

3 Significant accounting policies and changes in estimates continued

3.1.21 Deferred taxes

In accordance with IAS 12 'Income Taxes', deferred taxes are recognised for all temporary differences between the book values of assets and liabilities and their tax basis, as well as for unused tax losses, using the liability method. Deferred tax assets are recognised only when their recovery is considered probable.

IAS 12 requires, in particular, the recognition of deferred tax liabilities on all intangible assets recognised in business combinations (trademarks, subscriber bases, etc.).

A deferred tax liability is recognised for all taxable temporary differences associated with investments in subsidiaries and associates except to the extent that both of the following conditions are satisfied:
– the Group is able to control the timing of the reversal of the temporary difference (e.g. the payment of dividends); and
– it is probable that the temporary difference will not reverse in the foreseeable future.

In accordance with IAS 12, deferred tax assets and liabilities are not discounted.

3.1.22 Provisions

In accordance with IAS 37 'Provisions, Contingent Liabilities and Contingent Assets', a provision is recognised when the Group has a present obligation towards a third party and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation.

The obligation may be legal, regulatory or contractual or it may represent a constructive obligation deriving from the Group's actions where, by an established pattern of past practice, published policies or a sufficiently specific current statement, the Group has indicated to other parties that it will accept certain responsibilities, and as a result, has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

The estimate of the amount of the provision corresponds to the expenditure likely to be incurred by the Group to settle its obligation. If a reliable estimate cannot be made of the amount of the obligation, no provision is recorded and the obligation is deemed to be a 'contingent liability'.

Contingent liabilities – corresponding to probable obligations that are not recognised because their existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the Group's control, or to present obligations arising from past events that are not recognised because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation or because the amount of the obligation cannot be measured with sufficient reliability – are disclosed in the notes to the financial statements.

Restructuring
Provisions for restructuring costs are recognised only when the restructuring has been announced and the Group has drawn up or has started to implement a detailed formal plan, prior to the balance sheet date.

Provisions for dismantling and restoring sites
The Group is required to dismantle equipment and restore sites. In accordance with paragraphs 36 and 37 of IAS 37 'Provisions, Contingent Liabilities and Contingent Assets', the provision was based on the best estimate of the amount required to settle the obligation. It is discounted by applying a discount rate that reflects the passage of time and the risk specific to the liability. The amount of the provision is revised periodically and adjusted where appropriate, with a contra-entry to the asset to which it relates.

3.1.23 Pensions and similar benefits

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. 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. This method sees each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation which is then discounted. The calculation is based on demographic assumptions concerning retirement age, rates of future salary increases, staff turnover rates, and financial assumptions concerning future interest rates (to determine the discount rate) and inflation.

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.

Termination benefits
The Group recognises termination benefits as a liability and an expense when it is demonstrably committed to either terminate the employment of an employee or group of employees before the normal retirement date, or provide termination benefits as a result of an offer made in order to encourage voluntary redundancy. An entity is demonstrably committed to a termination when it has a detailed formal plan for the termination and is without realistic possibility of withdrawal.

Benefits falling due more than 12 months after the balance sheet date are discounted.

3.2 Changes in estimates

Useful life
Property, plant and equipment are depreciated to write off their cost less any residual value on a basis that reflects the pattern in which their future economic benefits are expected to be consumed.

As described in Note 3.1.16, useful lives of assets are reviewed annually and are adjusted if current estimated useful lives are different from previous estimates. These changes in accounting estimates are recognised prospectively, in accordance with IAS 8, and the depreciation charge for the current year and future accounting periods is adjusted accordingly. The main impacts of this analysis carried out within Group companies in 2005 are described below.

During the first half-year of 2005, the Group completed a project of verification of accounting for its property, plant and equipment and intangibles. The main goals of the project were to reassess the useful lives of property, plant and equipment and intangibles and to ensure that all significant parts of an item of property, plant and equipment and intangibles 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 and intangibles as a result of the project.

The effect of the above change 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.

4 Segment information

The primary segment reporting format is determined to be business segments as the Group's risks and rates of return are affected predominantly by differences in services delivered. The Group operates in two major reportable segments, fixed-line telecommunications and mobile telecommunications. The two segments are strategic business units.

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.

The fixed-line telecommunications segment also includes other operations which were previously presented as 'Other' in the IFRS Consolidated Financial Statements of the Group for the year ended 31 December 2005 as the activities became linked with the fixed-line telecommunications segment.

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

The Group operates in majority 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 commercial terms. These transactions are eliminated on consolidation.

4 Segment information continued

Basic financial data on the business segments is presented below:

(in PLN millions)	Fixed-line telecommunications	Mobile telecommunications	Eliminations	Consolidated
year ended 31 December 2006				
Net revenue	11,869	7,532	(776)	18,625
External	11,636	6,989	–	18,625
Inter-segment	233	543	(776)	–
Gross operating margin	5,570	2,669	–	8,239
Employee profit-sharing	(24)	–	–	(24)
Share-based compensation	–	–	–	–
Depreciation and amortisation	(3,427)	(1,062)	–	(4,489)
Impairment of goodwill	–	–	–	–
Impairment of fixed assets / (Reversals of impairment losses of fixed assets)	(77)	–	–	(77)
Impairment of intangibles / (Reversals of impairment losses of intangibles)	(3)	–	–	(3)
Gains (losses) on disposal of assets	14	(8)	–	6
Allocated by segment	14	(8)	–	6
Not allocable				–
Restructuring costs	(285)	–	–	(285)
Significant non-cash expenses – other than those mentioned above	–	–	–	–
Share of profits (losses) of associates	–	–	–	–
Operating income	1,767	1,600	–	3,367
Allocated by segment	1,767	1,600	–	3,367
Not allocable				–
Interest expense and other financial charges				(654)
Foreign exchange gains (losses)				(6)
Discounting				(73)
Income tax				(538)
Net income before minority interests				2,096
Capital expenditures	1,906	1,094	–	3,000
				At 31 December 2006
Segment assets	20,278	11,432	(79)	31,631
Investment in associate	3	–	–	3
Unallocated assets				977
Total assets				32,611
Segment liabilities	3,780	2,275	(79)	5,976
Unallocated liabilities				8,532
Total liabilities				14,508
Equity				18,103
Total equity and liabilities				32,611

(in PLN millions)	Fixed-line telecommunications	Mobile telecommunications	Eliminations	Consolidated
year ended 31 December 2005				
Net revenue	12,629	6,424	(711)	18,342
External	12,415	5,927	–	18,342
Inter-segment	214	497	(711)	–
Gross operating margin	5,670	2,443	–	8,113
Employee profit-sharing	(30)	–	–	(30)
Share-based compensation	–	–	–	–
Depreciation and amortisation	(3,337)	(923)	–	(4,260)
Impairment of goodwill	(43)	–	–	(43)
Impairment of fixed assets / (Reversals of impairment losses of fixed assets)	11	–	–	11
Impairment of intangibles / (Reversals of impairment losses of intangibles)	4	–	–	4
Gains (losses) on disposal of assets	57	(14)	–	43
Allocated by segment	57	(14)	–	43
Not allocable				–
Restructuring costs	(11)	–	–	(11)
Significant non-cash expenses – other than those mentioned above	–	–	–	–
Share of profits (losses) of associates	–	–	–	–
Operating income	2,321	1,506	–	3,827
Allocated by segment	2,321	1,506	–	3,827
Not allocable				–
Interest expense and other financial charges				(852)
Foreign exchange gains (losses)				(24)
Discounting				(70)
Income tax				(361)
Net income before minority interests				2,520
Capital expenditures	1,802	1,244	–	3,046
				At December 31 2005
Segment assets	21,898	11,596	(151)	33,343
Investment in associate	3	–	–	3
Unallocated assets				1,984
Total assets				35,330
Segment liabilities	3,737	2,446	(151)	6,032
Unallocated liabilities				11,904
Total liabilities				17,936
Equity				17,394
Total equity and liabilities				35,330

5 Main acquisitions and divestitures of companies

Main transactions carried out in the year ended 31 December 2005 are described below:

Under the settlement with WP minority shareholders of 21 July 2005, the Group acquired the remaining 19.54% of WP shares for 221 million. 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.

On 16 November 2005, TP S.A. acquired 34.0% of the share capital of PTK-Centertel Sp. z o.o. from a subsidiary of France Telecom S.A. (See also Note 33.2)

There were no significant acquisitions and divestitures in the year ended 31 December 2006.

6 Revenues, net

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Fixed-line telephony services	**8,716**	**9,794**
Subscriptions	4,390	4,318
Voice traffic revenues	3,364	4,554
Interconnect revenues	885	820
Payphone revenues	72	94
Other	5	8
Mobile telephony services	**6,848**	**5,773**
Voice traffic revenues	3,780	3,334
Interconnect revenues	1,902	1,500
Messaging services	1,163	934
Other	3	5
Data Services	**2,227**	**2,099**
Leased lines	380	383
Data transmission	540	509
Dial – up	132	230
Broadband revenues	1,175	977
Radio-communications	**244**	**241**
Sales of goods and other	**590**	**435**
Total revenues, net	**18,625**	**18,342**

Revenues are generated mainly in the territory of Poland. Approximately 2.5% and 2.4% of the total revenues for the years ended 31 December 2006 and 2005, respectively, were received from entities which are not domiciled in Poland, mostly from interconnect services.

7 Operating income and expense

7.1 External purchases

External purchases consist of the following:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Commercial expenses [1]	(2,284)	(1,922)
Purchases and payments to operators	(2,835)	(2,605)
Costs relating to network and IT expenses	(835)	(937)
Other external purchases [2]	(1,484)	(1,507)
Total external purchases	**(7,438)**	**(6,971)**

[1] Includes cost of handsets and other equipment sold, commissions, advertising and sponsoring.
[2] Includes retail fees and overheads, real estate costs, subcontracting fees, rentals and purchases of equipment.

In the years ended 31 December 2006 and 2005, research and development costs recognised in the profit and loss account amounted to PLN 53 million and PLN 55 million, respectively.

7.2 Other operating income and expense

Other operating income and expense consist of the following:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Late payment interest on trade receivables	39	41
Other income [(1)]	254	227
Total other operating income	**293**	**268**
Impairment losses on trade receivables, net	(132)	(188)
Impairment losses on other receivables, net	–	(4)
Taxes other than income taxes	(519)	(512)
Operating foreign exchange gains/(losses), net	(10)	40
Other expense and change in provisions	(228)	(481)
Total other operating expense	**(889)**	**(1,145)**

[(1)] Includes recoveries on customer bad debt written-off, fines and penalties received and charges on termination of post-paid contracts.

7.3 Labour expenses

Labour expenses consist of the following:

(in PLN millions, except for number of employees)	year ended 31 December 2006	year ended 31 December 2005
Average number of employees (full time equivalent)	32,909	34,365
Wages and salaries	(1,938)	(1,993)
Social security charges	(423)	(447)
Capitalised personnel costs (positive amount)	67	43
Other [(1)]	(58)	16
Wages and employee benefit expenses	**(2,352)**	**(2,381)**
Employee profit sharing	**(24)**	**(30)**
Total labour expenses	**(2,376)**	**(2,411)**

[(1)] Includes payroll taxes for the years ended 31 December 2006 and 2005 amounting to PLN 20 million and PLN 18 million, respectively, and other employee benefits (including change in provisions) for the year ended 31 December 2006 amounting to PLN 39 million and for the year ended 31 December 2005 in the positive amount of PLN 34 million.

8 Impairment

8.1 Goodwill

During the year ended 31 December 2006, there was no goodwill impairment recognised. Details regarding impairment tests of goodwill are presented in Note 8.3.

8.2 Other property, plant and equipment and intangible assets

In the year ended 31 December 2006, the impairment loss on property, plant and equipment charged to the profit and loss account amounted to PLN 77 million, primarily including an impairment loss as a result of a semi-annual and annual review of TP Group's properties. In the year ended 31 December 2005 the reversal of impairment loss on property, plant and equipment charged to the profit and loss account amounted to PLN 11 million.

In the year ended 31 December 2006, the impairment loss on intangible assets charged to the profit and loss account amounted to PLN 3 million. In the year ended 31 December 2005, the reversal of impairment loss on intangible assets charged to the profit and loss account amounted to PLN 4 million.

8 Impairment continued

8.3 Information concerning the definition of Cash Generating Units

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. 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. For the purpose of the impairment test, the entire fixed network, the entire mobile network, the entire radio diffusion network and internet portal were treated as separate cash-generating units.

The Group has identified certain indicators, including market liberalisation and other regulatory and economic changes in the Polish telecommunications market that could act as triggering factors for the potential impairment of assets.

As a consequence, as at 31 December 2006 the Group performed impairment tests regarding CGUs of the fixed network. No impairment losses were recognised as a result of this test.

CGUs include goodwill with net book value as at 31 December 2006 and 2005 in the amount of: PLN 85 million for the internet portal and PLN 3,909 million for the mobile network.

In 2006 and 2005 the Group performed annual impairment tests of the goodwill of the internet portal (external valuation) and mobile network. No impairment losses were recognised as a result of these tests in 2006. The impairment recognised for goodwill on internet portal amounted to PLN 162 million in 2005.

Due to the lack of impairment indicators no impairment tests were made regarding the radio diffusion network as at 31 December 2006 and 2005.

Key assumptions used to determine the value in use of the principal groups of CGUs:
– market level, penetration rate and market share; decisions of regulators in terms of the pricing, accessibility of services; the level of commercial expenses required to replace products and keep up with existing competitors or new market entrants; the impact on costs of changes in net revenues; and
– the level of investment spending, which may be affected by the roll-out of necessary new technologies.

The amounts assigned to each of these parameters reflect past experience adjusted for expected changes over the timeframe of the business plan, but may also be affected by unforeseeable changes in the political, economic or legal framework.

CGU Group	Fixed network	Mobile network
Key assumptions on which management has based its cash flow projections	value in use, budget and strategic business plan	value in use, budget and strategic business plan
Description of management's approach to determining the values assigned to each key assumption	DCF	DCF
Model parameters:		
– Applicable period for projected future cash flows	5 years	5 years
– Growth rate used to extrapolate cash flows beyond projection period	0%	3%
– Discount rate applied [(1)]	11.6%	11.6%

[(1)] Discount rate is based on a pre-tax discount rate defined by IAS 36.

9 Gains and losses on disposal of assets

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Disposals of property, plant and equipment and intangible assets	6	(3)
Sale of Intelsat, Parkiet Media and other shares	–	16
Impairment on shares and loans granted	–	30
Total gains and losses on disposal of assets	6	43

10 Restructuring costs

Restructuring costs, net of restructuring provision reversals, consist of the following:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Employee termination costs	(266)	(1)
Other	(19)	(10)
Total restructuring costs	**(285)**	**(11)**

Movements in restructuring provisions are described in Note 28.

11 Financial income and expense

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Interest income	46	169
Interest expense	(749)	(947)
Changes in fair value of debt and derivatives	49	(74)
Interest expense and other financial charges	**(654)**	**(852)**
Foreign exchange losses [1]	**(6)**	**(24)**
Discounting expense	**(73)**	**(70)**
Finance costs, net	**(733)**	**(946)**

[1] Including currency derivatives.

12 Income tax

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Current income tax	500	737
Deferred tax change [1]	41	(381)
Less: Deferred tax charged to equity	3	(5)
	538	**361**

[1] Deferred tax change in the years ended 31 December 2006 and 2005 includes PLN 77 million and PLN 80 million, respectively, related to timing difference between the preparation of the IFRS consolidated financial statements and the filing of Corporate Income Tax declarations for 2006 and for 2005.

The reconciliation between effective income tax expense and the theoretical tax calculated based on the Polish statutory tax rate is as follows:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Consolidated net income before tax	2,634	2,881
Statutory tax rate	19%	19%
Theoretical tax	500	547
Change in valuation allowance and other	(22)	(181)
Income and expense not subject/deductible for tax purposes	60	(5)
Effective tax	**538**	**361**

Expenses not deductible for tax purposes consist of certain cost items, which, under Polish tax law, are specifically determined as non-deductible. Unrecognised deferred tax asset relates mainly to those tax losses, which are expected to expire rather than being realised, and temporary differences, which based on the Group's management assessment could not be utilised for tax purposes.

12 Income tax continued

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 incurred in the year 2000 and subsequent years are permitted to be utilised over 5 consecutive years with a 50% utilisation restriction for each annual tax loss in a particular year.

The amounts and expiry dates of unused tax losses are as follows:

year of expiration:	(in PLN millions)
2006	71
2007	160
2008	139
2009	66
2010	29
2011	145
Total	**610**

During the year ended 31 December 2006 the Group entities utilised PLN 273 million of its tax losses previously incurred.

Value added tax, corporate income tax, personal income tax or social security regulations are subject to frequent changes which often leads to the lack of reference to well established regulations or legal precedents. There is also a lack of clarity in current regulations which results in contradictions in legal interpretations both within government bodies and between companies and government bodies. Tax settlements and other (e.g. customs or foreign exchange law) may be subject to review and investigation by a number of authorities, which are entitled to impose severe fines, and additional liabilities resulting from such tax audits must be paid together with interest charges. 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. As a result liabilities presented in the consolidated financial statements may change later after the final decisions of tax authorities.

Deferred income tax

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

	Consolidated balance sheet	
(in PLN millions)	At 31 December 2006	At 31 December 2005
Accrued expenses	(450)	(457)
Property, plant and equipment and intangible assets	432	460
Tax loss carried forwards	(2)	(47)
Other differences	(26)	(46)
Net deferred tax (assets)/liability	**(46)**	**(90)**

As at 31 December 2006 and 31 December 2005, deductible temporary differences, for which no deferred tax asset was recognised amounted to PLN 832 million and PLN 1,279 million, of which PLN 600 million and PLN 490 million respectively related to tax losses the realisation of which was not probable and PLN 232 million and PLN 789 million respectively related to other temporary differences, which based on the Group's management assessment would not be utilised for tax purposes.

13 Discontinued operations

In the year ended 31 December 2006 the Group did not discontinue any significant business operations.

14 Goodwill

The principal goodwill items arising from fully consolidated subsidiaries are as follows:

	At 31 December 2006			At 31 December 2005
(in PLN millions)	Cost	Accumulated impairment	Net	Net
Wirtualna Polska	247	(162)	85	85
PTK-Centertel	3,909	–	3,909	3,909
Total goodwill	**4,156**	**(162)**	**3,994**	**3,994**

There were no movements in the net book value of goodwill in the year ended 31 December 2006.

15 Other intangible assets

	At 31 December 2006				At 31 December 2005
(in PLN millions)	Cost	Accumulated amortisation	Impairment	Net	Net
Telecommunications licenses	2,345	(484)	–	1,861	2,006
Software	3,856	(2,473)	(10)	1,373	1,095
Other intangibles	87	(35)	–	52	365
Total	**6,288**	**(2,992)**	**(10)**	**3,286**	**3,466**

Movements in the net book values were as follows:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Opening balance net of accumulated amortisation and impairment	**3,466**	**3,469**
Acquisitions of intangible assets	452	365
Impact of changes in the scope of consolidation	–	4
Amortisation	(698)	(525)
Impairment	(3)	4
Reclassifications and other	69	149
Closing balance	**3,286**	**3,466**

Details of the Group's principal intangible assets (telecommunications licenses) are as follows:

(in PLN millions)	Acquisition date	Acquisition value	Net book value at 31 December 2006	Concession term
DCS 1800 Concession	1997	318	139	2012
GSM 900 Concession	1999	402	193	2014
UMTS Concession	2000	2,495	1,529	2023
Total telecommunications licenses		**3,215**	**1,861**	

15 Other intangible assets continued

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 telecommunications concessions were met as at 31 December 2006.

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.

As at 31 December 2006 and 2005, there were no intangibles pledged as security for loans or bank guarantees.

16 Property, plant and equipment

	At 31 December 2006				At 31 December 2005
(in PLN millions)	Cost	Accumulated amortisation	Impairment	Net	Net
Land and buildings	3,472	(641)	(124)	2,707	3,078
Networks and terminals	33,442	(14,894)	(30)	18,518	20,039
IT equipment	1,661	(1,080)	–	581	509
Investment grants	(196)	–	–	(196)	(216)
Other	942	(848)	(18)	76	102
Total	**39,321**	**(17,463)**	**(172)**	**21,686**	**23,512**

Investment grants relate to certain property, plant and equipment received by Telekomunikacja Polska from Public Telephone Committees (Społeczne Komitety Telefonizacji).

Changes in the net book value of property, plant and equipment are as follows:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Opening balance net of accumulated depreciation and impairment	**23,512**	**24,684**
Acquisitions of property, plant and equipment	2,548	2,681
Impact of changes in the scope of consolidation	–	7
Disposals and retirements	(9)	(65)
Depreciation	(3,791)	(3,735)
Impairment	(77)	11
Reclassifications and other [(1)]	(497)	(71)
Closing balance	**21,686**	**23,512**

[(1)] Include reclassifications described below.

As a result of the Real Estate Optimisation Programme, the Group classified certain properties with a value amounting to PLN 425 million as assets held for sale as at 31 December 2006.

The carrying value of plant and equipment held under finance leases as at 31 December 2006 and 2005 amounted to PLN 1 million and PLN 1 million, respectively. There were no additions during the years ended 31 December 2006 and 2005 of plant and equipment held under finance leases. Leased assets are pledged as security for the related finance lease and hire purchase liabilities.

As at 31 December 2006 and 2005, there were no property, plant and equipment pledged as security for loans or bank guarantees.

17 Financial assets

(in PLN millions)	At 31 December 2006 Cost/Fair value	Impairment	Net	At 31 December 2005 Net
Main unlisted companies				
Exatel	14	(11)	3	3
Other	5	(4)	1	1
Assets available for sale [1]	**19**	**(15)**	**4**	**4**
Derivatives [3]	–	–	–	22
Other	1	–	1	–
LT other financial assets and derivatives [2]	**1**	**–**	**1**	**22**
Derivatives [3]	28	–	28	117
Marketable securities held for trading [3]	3	–	3	2
Other	2	–	2	3
ST other financial assets and derivatives	**33**	**–**	**33**	**122**
Total financial assets	**53**	**(15)**	**38**	**148**

[1] Financial assets available for sale are measured at historical cost less impairment and mainly comprise of shares for which there is no active market and fair value cannot be reliably measured.
[2] Carried at fair value.
[3] Items included in the calculation of net debt (see Note 19).

The Group does not hold any financial assets to maturity.

18 Trade receivables, other receivables, prepaid expenses and other current assets

(in PLN millions)	At 31 December 2006	At 31 December 2005
Trade receivables (net of provisions) [1]	**1,877**	**1,918**
VAT receivable	14	59
Other taxes receivable	1	–
Employee-related receivables	3	–
Other [2]	86	37
Other current assets [1]	**104**	**96**
Inactivated mobile phones and terminals maintained in the external dealership network	40	74
Other prepaid expenses	18	31
Prepaid expenses	**58**	**105**

[1] Additions to impairment of trade and other receivables (net of reversals) are presented in Note 7.2.
[2] Includes receivables from debt collector and penalties from suppliers.

19 Net debt

19.1 Analysis of net debt by composition and maturity

Net debt corresponds to the total gross debt (converted at the period-end exchange rate), less derivative instruments carried in assets for trading, cash flow hedges and fair value hedges, less cash and cash equivalents and marketable securities and including the impact of the effective portion of cash flow hedges.

The table below provides a breakdown of net debt by category and period due.

At 31 December 2006:

(in PLN millions)	Note	Within 1 year	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years	Total at 31 December 2006
Bonds	21	1,817	2,289	–	–	1,143	–	5,249
Bank loans	22	260	238	216	216	216	259	1,405
Impact of derivatives (liabilities)	23	386	883	29	24	47	2	1,371
Accrued interest		135	–	–	–	–	–	135
Gross financial debt (A)		**2,598**	**3,410**	**245**	**240**	**1,406**	**261**	**8,160**
Impact of derivatives (assets)	17 and 23	28	–	–	–	–	–	28
Marketable securities	17	3	–	–	–	–	–	3
Cash and cash equivalents	20	879	–	–	–	–	–	879
Sub-total (B)		**910**	**–**	**–**	**–**	**–**	**–**	**910**
Effective portion of cash flow hedges (C)		(2)	(28)	–	–	(29)	(36)	(95)
Net financial debt (A)-(B)+(C)		**1,686**	**3,382**	**245**	**240**	**1,377**	**225**	**7,155**

At 31 December 2005:

(in PLN millions)	Note	Within 1 year	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years	Total at 31 December 2005
Bonds	21	1,929	1,834	2,569	–	–	1,151	7,483
Bank loans	22	313	265	242	218	218	483	1,739
Loan from related party		1,000	–	–	–	–	–	1,000
Finance lease liabilities		–	1	–	–	–	–	1
Impact of derivatives (liabilities)	23	482	194	569	22	18	15	1,300
Accrued interest		247	–	–	–	–	–	247
Gross financial debt (A)		**3,971**	**2,294**	**3,380**	**240**	**236**	**1,649**	**11,770**
Impact of derivatives (assets)	17 and 23	117	22	–	–	–	–	139
Marketable securities	17	2	–	–	–	–	–	2
Cash and cash equivalents	20	1,676	–	–	–	–	–	1,676
Sub-total (B)		**1,795**	**22**	**–**	**–**	**–**	**–**	**1,817**
Effective portion of cash flow hedges (C)		(8)	(8)	(47)	–	–	(50)	(113)
Net financial debt (A)-(B)+(C)		**2,168**	**2,264**	**3,333**	**240**	**236**	**1,599**	**9,840**

19.2 Covenants

The covenants on TP Group's borrowings and credit lines are presented in Note 24.

19.3 Analysis of net debt by currency

				At 31 December 2006
(equivalent value in PLN millions at the period-end exchange rate)	PLN	EUR	USD	Total
Net debt by currency [1]	872	4,027	2,256	7,155
Impact of derivatives notional amount	5,743	(3,524)	(2,219)	–
Net debt by currency after impact of derivatives notional amount	**6,615**	**503**	**37**	**7,155**

[1] Including market value of derivatives in local currency

				At 31 December 2005
(equivalent value in PLN millions at the period-end exchange rate)	PLN	EUR	USD	Total
Net debt by currency [1]	1,224	5,956	2,660	9,840
Impact of derivatives notional amount	9,261	(6,637)	(2,624)	–
Net debt by currency after impact of derivatives notional amount	**10,485**	**(681)**	**36**	**9,840**

[1] Including market value of derivatives in local currency

20 Cash and cash equivalents

The Group's cash and cash equivalents are as follows:

(in PLN millions)	At 31 December 2006	At 31 December 2005
Cash on hand	1	6
Current bank accounts and overnight deposits	580	557
Deposits up to 3 months	294	924
Securities with a maturity of less than 3 months	–	186
Other	4	3
Total cash and cash equivalents	**879**	**1,676**

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short term deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates.

As at 31 December 2006 and 2005, cash and cash equivalents include an equivalent of PLN 217 million and PLN 515 million respectively, denominated in foreign currencies.

Restricted cash as at 31 December 2006 and 2005 amounted to PLN 203 million and PLN 15 million, respectively. As at 31 December 2006 the amount of restricted cash related mainly to the special purpose deposits.

21 Bonds

The table below provides an analysis of bonds by issuer:

Bonds issued by the Group

(in PLN millions)						Amount outstanding at[1]	
Issuer	Series	Nominal value (in millions of currency)	Nominal interest rate	Issue date	Redemption date	31 December 2006	31 December 2005
TPSA Finance B.V.	A	800 USD	7.750%	10 December 1998	10 December 2008	2,289	2,569
TPSA Eurofinance B.V.	D	475 EUR	6.500%	13 March 2000	13 March 2007	1,817	1,834
TPSA Eurofinance B.V.	E	500 EUR	6.625%	1 March 2001	1 March 2006	–	1,929
TPSA Eurofinance France S.A.	T	300 EUR	4.625%	5 July 2004	5 July 2011	1,143	1,151
Total bonds issued by the Group						**5,249**	**7,483**

[1] Includes the fair value adjustment to the bonds hedged by fair value hedge.

The effective interest rate on TP Group bonds, before swaps, amounted to 6.75% as at 31 December 2006 and 6.80% as at 31 December 2005.

22 Bank borrowings

Bank borrowings borrowed by the Group

(in PLN millions)				Amount outstanding at			
				31 December 2006		31 December 2005	
Creditor	Agreement	Interest rate	Repayment date	Currency (millions)	PLN (millions)	Currency (millions)	PLN (millions)
Floating rate							
International Bank for Reconstruction and Development	33190 POL	5.38% [1]	15 March 2008	12 USD	34 PLN	19 USD	63 PLN
European Investment Bank	1.9251	3.65% [2]	15 December 2015	75 EUR	287 PLN	83 EUR	322 PLN
European Investment Bank	20.887	3.65% [2]	15 June 2012	183 EUR	702 PLN	217 EUR	836 PLN
European Investment Bank	20.887	4.10% [2]	15 June 2012	286 PLN	286 PLN	337 PLN	337 PLN
Fixed rate							
European Investment Bank	1.5286	6.454%	10 June 2008	3 USD	8 PLN	5 USD	16 PLN
European Investment Bank	1.5286	7.112%	10 June 2008	7 EUR	25 PLN	11 EUR	42 PLN
European Investment Bank	0.2218	3.81%	18 August 2006	–	–	12 EUR	47 PLN
Instituto de Credito Oficial	–	1.25%	02 January 2021	22 USD	63 PLN	23 USD	76 PLN
Total bank borrowings borrowed by the Group					**1,405 PLN**		**1,739 PLN**

[1] Floating rate determined by the bank every half year.
[2] Floating rate determined by the bank every three months.

The effective interest rate on TP Group bank borrowings, before swaps, amounted to 3.76% as at 31 December 2006 and 3.06% as at 31 December 2005.

23 Derivatives

The derivative financial instruments (excluding embedded derivatives) used by the Group are presented below:

At 31 December 2006								
		Principal (millions)		Interest			Fair value[7] (in PLN millions)	
Type of instrument [1]	Hedged Item	Receive	Pay	Receive	Pay	Maturity	Financial Asset	Financial Liability
Fair value hedge								
CCIRS	Bonds	775 USD	3,051 PLN	7.75% to 7.86%	6M WIBOR + 1.75% to 6M WIBOR + 5.60%	2008	–	(896)
CCIRS	Bonds	440 EUR	1,847 PLN	6.50% to 6.56%	6M WIBOR + 1.59% to 6M WIBOR + 4.08%	2007	–	(116)
CCS	Bonds	10 EUR	42 PLN	–	6M WIBOR - 3.92%	2011	–	(3)
Cash flow hedge								
CCIRS [2]	Bank borrowings	33 EUR	157 PLN	3M EURIBOR	4.52% to 5.30%	2008	–	(38)
CCIRS [3]	Bonds	63 EUR	255 PLN	4.63% to 6.56%	5.03% to 14.27%	2007 – 2008	11	(36)
CCS [4]	Bank borrowings	44 EUR	192 PLN	–	2.91% to 3.09%	2012	–	(37)
CCS	Bonds	130 EUR	549 PLN	–	1.57% to 2.95%	2011	–	(87)
IRS	Bank Borrowings	285 PLN	285 PLN	3M WIBOR - 0.17%	6.89% to 6.99%	2012	–	(18)
CCS	UMTS	72 EUR	286 PLN	–	1.23 % to 1.41%	2014	–	(15)
Trade								
CCIRS	–	25 USD	75 PLN	7.75%	6M WIBOR + 2.98%	2008	–	(7)
CCIRS [5]	–	114 EUR	445 PLN	3M EURIBOR	3M WIBOR -1.02% to 3M WIBOR + 1.56%	2008 – 2012	15	(28)
CCIRS [6]	–	3 USD	11 PLN	1.25%	3M WIBOR -3.11%	2008	–	(3)
CCS	–	1 EUR	5 PLN	0.80%	PLN 1 mln quarterly	2008	–	(3)
IRS	–	4,678 PLN	4,678 PLN	3M WIBOR	5.24% to 6.95%	2007 – 2008	–	(73)
NDF	–	108 EUR	424 PLN	–	–	2007	0	(10)
FX swap	–	–	–	–	–	2007	–	(0)
Total of fair value								
Swap contracts							**26**	**(1,360)**
NDF							**0**	**(10)**
FX Swap							**–**	**(0)**
Total							**26**	**(1,370)**

[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 on notional amounts of EUR 92 million and PLN 433 million, which are subject to adjustment in accordance with repayment schedule,
[3] Including EUR 28 mln which constitutes hedging of only coupon payments on bond series T,
[4] Interest is calculated on notional amounts of EUR 44 million and PLN 192 million, which are subject to adjustment in accordance with repayment schedule,
[5] Interest is calculated on notional amounts of EUR 229 million and PLN 938 million, which are subject to adjustment in accordance with repayment schedule,
[6] Interest is calculated on notional amounts of USD 22 million and PLN 81 million, which are subject to adjustment in accordance with repayment schedule,
[7] Value 0 or (0) represents an asset or a liability below PLN 500 thousand, respectively.

23 Derivatives continued

At 31 December 2005

Type of instrument [1]	Hedged Item	Principal (millions) Receive	Principal (millions) Pay	Interest Receive	Interest Pay	Maturity	Fair value[7] (in PLN millions) Financial Asset	Fair value[7] (in PLN millions) Financial Liability
Fair value hedge								
CCIRS	Bonds	775 USD	3,051 PLN	7.75% to 7.8644%	6M WIBOR +1.75% to 6M WIBOR +5.60%	2008	–	(625)
CCIRS	Bonds	675 EUR	2,823 PLN	6.50% to 6.69875%	6M WIBOR +1.59% to 6M WIBOR +4.08%	2006 – 2007	27	(164)
CCS	Bonds	10 EUR	42 PLN	–	6M WIBOR -3.92%	2011	–	(2)
Cash flow hedge								
CCIRS [2]	Bank borrowings	62 EUR	293 PLN	3.81% or 3M EURIBOR	4.52% to 7.81%	2006 – 2008	–	(72)
CCIRS [3]	Bonds	237 EUR	873 PLN	4.63% to 6.6875%	5.03% to 14.78%	2006 – 2008	85	(61)
CCS [4]	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	–	(70)
IRS	Bank borrowings	337 PLN	337 PLN	3M WIBOR -0.17%	6.89% to 6.99%	2012	–	(24)
Trade								
CCIRS	–	25 USD	75 PLN	7.75%	6M WIBOR +2.98%	2008	0	–
CCIRS [5]	–	151 EUR	597 PLN	3M EURIBOR	3M WIBOR -1.35% to 3M WIBOR +1.56%	2006 – 2012	18	(46)
CCIRS [6]	–	4 USD	17 PLN	1.25%	6M WIBOR -3.11%	2008	–	(3)
CCS	–	2 EUR	9 PLN	0.80%	PLN 1 mln quarterly	2008	–	(3)
IRS	–	4,786 PLN	4,786 PLN	3M WIBOR to 6M WIBOR	5.24% to 6.95%	2007 – 2008	–	(114)
NDF	–	390 EUR	1,580 PLN	–	–	2006	2	(68)
FWD	–	62 EUR	254 PLN	–	–	2006	–	(14)
Total of fair value								
Swap contracts							**130**	**(1,217)**
NDF							**2**	**(68)**
FWD							**–**	**(14)**
Total							**132**	**(1,299)**

[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 on notional amounts of EUR 121 million and PLN 568 million, which are subject to adjustment in accordance with repayment schedule
[3] Including EUR 42 mln which constitutes hedging of only coupon payments on bond series T
[4] Interest is calculated on notional amounts of EUR 44 million and PLN 192 million, which are subject to adjustment in accordance with repayment schedule
[5] Interest is calculated on notional amounts of EUR 301 million and PLN 1,241 million, which are subject to adjustment in accordance with repayment schedule
[6] Interest is calculated on notional amounts of USD 23 million and PLN 86 million, which are subject to adjustment in accordance with repayment schedule
[7] Value 0 or (0) represents an asset or a liability below PLN 500 thousand, respectively.

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

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Beginning of period	**(92)**	**(79)**
The effective part of the gain/loss on hedging instrument	18	(107)
The amounts transferred to the profit and loss account	–	89
Deferred tax effect	(3)	5
End of period	**(77)**	**(92)**

24 Financial Risk management

The Group's activities expose it to certain financial risks. The principal group of financial instruments comprises 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 coordinated 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 cooperation with the Group's entities. The written policies with respect to financial risks provide written principles for overall financial risk management and covering specific areas, such as foreign exchange and interest rate risk.

The primary hedging instruments used by the TP Group are 1) cross currency swaps, currency options and forwards for reducing foreign exchange risks and 2) interest rate swaps and FRA (Forward Rate Agreement) contracts for hedging the exposure of interest rate fluctuations. The Group classifies some of its derivatives (interest rate swaps) as non-hedging for accounting purposes due to the fact that not all of the formal requirements specified in IAS 39 in respect to the documentation of hedge accounting could be met (see Note 23).

Foreign exchange risk

The Group's exposure to market risk for changes in foreign exchange rates relates primarily to long-term interest bearing liabilities, including bonds and bank loans as well as to the UMTS concession payable. At the end of the year 2006, 86.5% (at the end of the year 2005: 94.4%) of foreign exchange risk attributable to bank loans and bonds was economically hedged via cross currency swaps, forward contracts and foreign exchange currency cash holdings. Additionally, the Group has hedged about 20% (2005: 100%) of cash flows resulting from PTK-Centertel liability related to the 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. In the year ended 31 December 2006 the proportion of gross debt based on fixed rate did not change significantly. At the end of the year 2006, 82.6% (at the end of the year 2005: 69.4%) of TP Group debt after economical hedge is based on fixed rate.

Analysis of the Group's sensitivity to changes in interest rates

Sensitivity of financial expenses

Assuming a constant amount of debt based on a floating rate and a consistent management policy, a 1% rise in interest rates would result in an increase of approximately PLN 6 million in financial expenses.

Sensitivity of net debt

A 1% rise in interest rates would lead to an estimated reduction in the market value of debt after swaps of approximately PLN 98 million, which represents 1% of the Group's net debt.

Liquidity risk

The Management of the Company believes that the liquidity of the Group remains secure in the foreseeable future. As at 31 December 2006, the current liabilities of the Group exceeded its current assets and assets held for sale by PLN 4,082 million (as at 31 December 2005: PLN 4,524 million). In the year ended 31 December 2006, the net cash inflows from the Group's operating activities amounted to PLN 7,225 million (in 2005: PLN 7,220 million). Additionally, based on arrangements made with banks, the Group has unutilised bank loan facilities amounting to PLN 4,656 million as at 31 December 2006 (as at 31 December 2005: PLN 2,172 million), based on arrangements with France Telecom, the Group has a loan facility amounting to PLN 1,000 million as at 31 December 2006.

Credit risk

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

24 Financial Risk management continued

Price risk

Pursuant to the Polish telecommunication law, prices for telecommunication services should be based on transparent and objective criteria. Detailed conditions are set for all significant types of services. Consequently, specific requirements relating to regulatory accounting and cost calculations are defined for SMP operators. Certain charges have to be approved by UKE before they are applicable and price increases have to be announced a minimum, one settlement period in advance. In addition, cost calculations of an SMP operator are subject to UKE audit and approval. If prices of certain services are assessed to be inconsistent with the law, UKE 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.

Management of covenants

As at 31 December 2006 and 31 December 2005 the Group did not have any credit facilities or borrowings subject to specific covenants with regard to financial ratios.

25 Fair value of 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.

A comparison by category of carrying amounts and fair values of those Group's financial instruments, for which estimated fair value differs from the book value, is presented below.

The fair value of long-term loans has been calculated by discounting the expected future cash flows at prevailing interest rates.

	At 31 December 2006		At 31 December 2005	
(in PLN millions)	Book value[1]	Estimated fair value	Book value[1]	Estimated fair value
Bonds with fixed interest rate	5,380	5,553	7,724	8,082
Bank loans with fixed interest rate	97	84	181	173
Total	**5,477**	**5,637**	**7,905**	**8,255**

[1] Book value includes accrued interests.

26 Employee benefits

Key Figures

(in PLN millions)	At 31 December 2006	At 31 December 2005
Jubilees	177	208
Retirement bonuses and other post-employment benefits	147	161
Salaries, other employee-related payables and payroll taxes due	297	295
Total employee benefit obligations	**621**	**664**
Current	333	341
Non-current	288	323

Certain employees and retirees of the Group are entitled to long-term employee benefits in accordance with the Group's remuneration policy (see Note 3.1.23). These benefits are not funded. The changes in the present value of liabilities related to employee benefits for the years ended 31 December 2006 and 2005 are detailed in the table below:

	year ended 31 December 2006				year ended 31 December 2005			
(in PLN millions)	Jubilee awards	Retirement bonuses	Other post-employment benefits	Total	Jubilee awards	Retirement bonuses	Other post-employment benefits	Total
At 1 January	**208**	**82**	**79**	**369**	**318**	**84**	**76**	**478**
Current service cost	12	7	1	20	22	6	1	29
Interest Cost	9	3	3	15	15	5	5	25
Benefits paid	(27)	(2)	(5)	(34)	(37)	(4)	(3)	(44)
Actuarial gains/losses [1]	–	–	–	–	30	–	–	30
Plan amendments	–	–	–	–	(134)	(5)	–	(139)
Curtailment	(25)	(16)	(5)	(46)	(6)	(4)	–	(10)
At 31 December	**177**	**74**	**73**	**324**	**208**	**82**	**79**	**369**

[1] if any

A valuation of obligations as at 31 December 2006 and 2005 was performed using a discount rate of 5.25% and 5%, respectively and a wage increase rate of 3% and 3%, respectively.

The corresponding defined benefit obligation (DBO) as at 31 December 2006 and 2005 is as follows:

	At 31 December 2006			At 31 December 2005		
(in PLN millions)	Retirement bonuses	Other post-employment benefits	Total	Retirement bonuses	Other post-employment benefits	Total
Provision	74	73	147	82	79	161
Unrecognised actuarial losses	11	7	18	16	7	23
Defined benefit obligation (DBO)	**85**	**80**	**165**	**98**	**86**	**184**

27 Share-based compensation

On 28 April 2006, the General Meeting of Shareholders of TP approved an Incentive Programme based on a 'Stock Option Plan'. On 12 December 2006, the Management Board of TP adopted the Incentive Programme Rules for the Members of the Management Board and the Key Managers of the Group. The main purpose of the Programme is to link remunerations of key managers with their contribution into TP Group's development through enabling them to benefit from the planned growth of the Company's value; getting them more involved in the active management of the TP Group in order to increase its profitability. The aforementioned objectives coincide with the interest of the Company's shareholders.

In order to fulfil the assumptions of the Programme on 28 April 2006 the General Shareholders' Meeting decided that TP S.A. will issue not more than 7,113,000 A series bearer bonds ('the Bonds') with priority right over existing shareholders to subscribe for B series shares issued by the Company. The nominal value and issue price of one Bond amounts to PLN 0.01. The bonds will be offered to certain employees and executives of the Group ('the Beneficiaries'). The number of Bonds granted to beneficiaries will depend upon the assessment of performance and commitment of each of the Beneficiaries as well as upon certain indices accepted in the Programme. The redemption of the Bonds will take place on 10th anniversary of the issue date (date on which the Bonds were granted). One Bond will give right to subscribe for one B series share of PLN 3. The issue price of B series shares will equal the average quotation price of the Company's shares during twenty sessions on the Warsaw Stock Exchange immediately preceding the Bonds issue date. As a result of exercising the subscription right for B series shares attached to the Bonds and B series shares being subscribed for by the holders of the Bonds, the share capital of TP S.A. will be increased by the amount not higher than PLN 21,339 thousand.

The Programme is awaiting implementation at TP.

28 Provisions

For the year ended 31 December 2006 the movements within particular classes of provisions were as follows:

(in PLN millions)	At 1 January 2006	Increases	Reversals (utilisations)	Reversals (releases)	Discounting effect	At 31 December 2006
Restructuring provisions (total)	24	314	(17)	(29)	–	292
Provisions for claims and litigations (see Note 32), risks and other charges	711	65	(16)	(33)	–	727
Provisions for dismantling	135	7	(3)	(8)	7	138
Provision for potential tax risks	4	4	(3)	(1)	–	4
Total provisions for risks and charges	**874**	**390**	**(39)**	**(71)**	**7**	**1,161**
Current	747	232	(39)	(50)	–	890
Non-current	127	158	–	(21)	7	271

For the year ended 31 December 2005 the movements within particular classes of provisions were as follows:

(in PLN millions)	At 1 January 2006	Increases	Reversals (utilisations)	Reversals (releases)	Discounting effect	At 31 December 2005
Restructuring provision	153	1	(130)	–	–	24
Provisions for claims and litigations (see Note 32), risks and other charges	476	389	(7)	(147)	–	711
Provisions for dismantling	67	87	(25)	–	6	135
Provision for potential tax risks	1	6	(2)	(1)	–	4
Total provisions for risks and charges	**697**	**483**	**(164)**	**(148)**	**6**	**874**
Current	632	401	(140)	(148)	2	747
Non-current	65	82	(24)	–	4	127

Restructuring provision

The restructuring provision consists of the discounted estimated amount of termination benefits for employees scheduled to terminate employment in the Group under the 2007-2009 Social Agreement and of the costs related to the operational restructuring in satellite capacity rental activities of the Group.

Dismantling provision

The dismantling provision relates to dismantling or removal 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 utilised by the end of their useful lives by entities licensed by the State for this purpose. The costs of such utilisations may be higher than costs incurred in the past. As a result, the dismantling provision was increased by PLN 7 million and PLN 87 million in the years ended 31 December 2006 and 2005, respectively due to further reassessment of the Group's obligations. The related costs were capitalised in the value of property, plant and equipment.

29 Other liabilities and deferred income

29.1 Other liabilities

(in PLN millions)	At 31 December 2006	At 31 December 2005
Payables due in more than 1 year relating to UMTS licenses	762	779
Other non-current liabilities	2	2
Other non-current liabilities	**764**	**781**
VAT payable	182	145
Other taxes payable	29	31
Other	17	21
Other current liabilities	**228**	**197**

29.2 Deferred income

(in PLN millions)	At 31 December 2006	At 31 December 2005
Sales of products and services billed in advance, including telephone subscriptions, phone cards, unused minutes and minutes deferred under loyalty programs	494	498
Revenue from inactivated mobile phones and terminals in the external dealership network	6	12
Other	25	30
Total deferred income	**525**	**540**
Current	446	389
Non-current	79	151

30 Equity

30.1 Share capital

As at 31 December, 2006, 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 during the year ended 31 December 2006.

The ownership structure of the share capital as at 31 December 2006 was as follows:

(in PLN millions)	% of votes	Nominal value
France Telecom S.A.	47.50	1,995
GDR holders represented by the Bank of New York [(1)]	5.02	211
State Treasury [(2)]	3.87	162
Other shareholders	43.61	1,832
Total	**100.00**	**4,200**

(1) Data as at 25 September 2006.
(2) Figures presented are based on the number of shares registered by the State Treasury at the Extraordinary Meeting of Shareholders of TP S.A. which was held on 21 September 2006.

France Telecom S.A. is the parent company of Telekomunikacja Polska and appoints the majority of the members of the Supervisory Board of Telekomunikacja Polska.

According to the Company's best knowledge, the Polish government has committed itself to grant a priority purchase right to France Telecom S.A. in case of a 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.

30 Equity continued

30.2 Dividends

In the year ended 31 December 2006 TP S.A. distributed PLN 1,400 million of dividend, including PLN 1,221 million of the 2005 profit and PLN 179 million of undistributed profits from previous years. The dividend of PLN 1 per share was approved by the General Shareholders' Meeting on 28 April 2006. Dividend, net of withholding tax, was paid in June 2006.

31 Contractual obligations and off balance sheet commitments

31.1 Off balance sheet contractual obligations and other commitments

At 31 December 2006, Management considers that, to the best of its knowledge, there are no existing commitments, other than those described below, likely to have a material impact on the current or future financial position of TP Group.

31.1.1 Investment, purchase and leasing commitments

a Commitments related to operating leases – group as lessee

Operating 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 years ended December 31, 2006 and 2005 amounted to PLN 281 million and PLN 331 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 2006, were as follows:

(in PLN millions)	At 31 December 2006
within one year	302
after one year but not more than five years	465
more than five years	74
Total minimum future lease payments	**841**

b Investment commitments

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

	At 31 December 2006	At 31 December 2005
Property, plant and equipment	458	456
Intangibles	11	70
Total	**469**	**526**
Amounts contracted to be payable within 12 months from the balance sheet date	469	517

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

31.1.2 Other off-balance sheet commitments

31.1.2.1 Guarantees

Bank guarantees in PTK Centertel as at 31 December 2006 amounted to PLN 7 million and related mainly to the leasing transactions.

31.2 Assets covered by commitments

The value of the assets held under finance leases amounted to PLN 2 million and PLN 2 million as at 31 December 2006 and 2005, respectively.

32 Litigation and claims

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 audit 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 and removal of items of its property, plant and equipment as required by the environmental regulations (see Note 28).

32 Litigation and claims continued

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 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 28).

d Investigations by UKE and UOKiK

According to the Telecommunications Act, the President of UKE 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 is a number of proceedings against the Group initiated by UKE and UOKiK. As at 31 December 2006 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 (Poczta Polska Telegraf i Telefon) and the Danish Great Northern Telegraph Company, a predecessor of Danish Polish Telecommunication Group I/S ('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 (Arbitration Court in Vienna) 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 30 June 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 draft expert 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 were challenged by the Company by filing its comments on the draft expert opinion. On 9 February 2006, based on the expert's model and its own adjustments, DPTG increased its claim from EUR 218 million (for the period up to 2002) to EUR 670 million for the period up to January 2006 plus interests.

Taking into account the developments the Company conducted a reassessment of its risk analysis in this litigation and revised as at 31 December 2005 the amount of the provision it had previously determined.

In April 2006, the coming to light of a situation of conflict of interest led the tribunal chairman to resign. A new Chairman was designated by the other members of the arbitral panel in September 2006. This tribunal has set a new calendar that foresees a final hearing in July 2007.

On November 9, 2006 and December 18, 2006 the Company filed its comments to the adjusted claim of DPTG containing own calculations of the relevant NSL traffic volume and questioning new DPTG claims' legitimacy.

The other developments that have occurred in 2006 have had no impact on the risk assessment.

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 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.

33 Related party transactions

33.1 Management Board and Supervisory Board compensation

Management Board compensation was as follows:

(in PLN thousand)	year ended 31 December 2006	year ended 31 December 2005
Short-term benefits excluding employer social security payments [1]	16,588	11,900
Post-employment benefits [2]	676	1,010
Termination benefits	540	1,101
Share-based compensation [3]	–	–
Total	**17,804**	**14,011**

[1] Gross salaries, compensation, bonuses and non-monetary benefits, profit-sharing, incentive bonuses
[2] Service cost
[3] Expense recorded in the income statement in respect of stock option plans and employee share offers

Remuneration and bonuses, compensation and termination indemnities, including compensation under a competition prohibition clause (cash, benefits in kind or any other benefits) paid or payable by Telekomunikacja Polska S.A. to TP S.A.'s Management Board and Supervisory Board members in 2006 and 2005 are presented on page 78.

33 Related party transactions continued

33.1 Management Board and Supervisory Board compensation continued

Management Board

(in PLN thousand)	year ended 31 December 2006	year ended 31 December 2005
Maciej Witucki	440	n/a
Benoît Mérel	1,252	n/a
Pierre Hamon	2,433	2,327
Konrad Kobylecki	1,703	1,560
Jacek Kałłaur	1,587	469
Jean-Marc Vignolles	–	–
Marek Józefiak [1]	4,431	3,714
Alain Carlotti [1]	3,265	n/a
Bruno Duthoit [1]	1,770	1,614
Roger de Bazelaire [1]	923	1,492
Bertrand Le Guern [1]	n/a	237
Wojciech Roman [1]	n/a	2,598
Total	**17,804**	**14,011**

[1] Persons that were not members of Management Board of the Company as at 31 December 2006 but were members of the Management Board of the Company in previous periods.

In addition, in 2006 the Group recorded a reserve for the estimated costs of termination benefits for Mr. Marek Józefiak and Mr. Alain Carlotti amounting to PLN 5,340 thousand and PLN 879 thousand, respectively.

Supervisory Board

(in PLN thousand)	year ended 31 December 2006	year ended 31 December 2005
Prof. Andrzej Koźmiński	92	n/a
Andrew Seton	171	119
Tadeusz Han	127	61
Timothy Boatman	165	72
Prof. Jerzy Rajski	24	n/a
Dr. Wiesław Rozłucki	5	n/a
Olivier Barberot (2)	–	–
Michel Monzani (2)	–	–
Jacques Champeaux (2)	–	–
Julien Billot (2)	–	–
Georges Penalver (2)	–	–
Vivek Badrinath (2)	–	
Stephane Pallez (2)	–	–
Jerzy Drozd (1)	68	76
Dr. Jan Kulczyk (1)	47	107
Krzysztof Ners (1)	85	61
Bożena Dyjak (1)	n/a	32
Stefan Kawalec (1)	n/a	32
Elżbieta Pacuła (1)	n/a	32
Dr. Jan Waga (1)	n/a	12
Claude Benmussa (1)(2)	–	–
Yves Le Moüel (1)(2)	–	–
Jean-Paul Cottet (1)(2)	–	–
André Cathelineau (1)(2)	–	–
Jean-Pierre Temime (1)(2)	–	–
Total	**784**	**604**

(1) Persons that were not members of the Supervisory Board of the Company as at 31 December 2006 but were members of the Supervisory Board of TP S.A. in previous periods.
(2) Persons appointed to the Supervisory Board of the Company employed by France Telecom do not receive remuneration for the function performed.

Remuneration and bonuses (cash, benefits in kind or any other benefits) paid or payable by TP S.A.'s subsidiaries and associates to TP S.A.'s Management Board members in 2006 were as follows: Maciej Witucki PLN 2 thousand, Jean-Marc Vignolles PLN 1,929 thousand, Marek Józefiak PLN 78 thousand, Konrad Kobylecki PLN 41 thousand, Alan Carlotti PLN 39 thousand, Pierre Hamon PLN 17 thousand.

Remuneration and bonuses (cash, benefits in kind or any other benefits) paid or payable by TP S.A.'s subsidiaries and associates to TP S.A.'s Management Board members in 2005 were as follows: Jean-Marc Vignolles PLN 1,124 thousand, Marek Józefiak PLN 87 thousand, Konrad Kobylecki PLN 23 thousand, Wojciech Roman PLN 69 thousand, Jacek Kałłaur PLN 7 thousand, Pierre Hamon PLN 41 thousand.

In 2006 and 2005 the members of TP S.A.'s Management Board did not receive any compensation or termination indemnities, including compensation under a competition prohibition clause (cash, benefits in kind or any other benefits) from TP S.A.'s subsidiaries and associates.

In 2006 and 2005 the members of TP S.A.'s Supervisory Board did not receive any remuneration, bonuses, compensation or termination indemnities, including compensation under a competition prohibition clause (cash, benefits in kind or any other benefits) from TP S.A.'s subsidiaries and associates.

In 2006 and 2005 TP S.A. did not grant any loans to members of the Supervisory Board.

As at 31 December 2006 and 2005 members of the Supervisory Board had no liabilities arising from loans granted by the Company.
In 2006 and 2005 TP S.A. did not enter into any transactions with companies in which the members of its authorities had significant shareholdings.

In 2006 and 2005 the Company did not enter into any significant transactions with members of the Management Board and Supervisory Board and their spouses, relatives up to second degree individuals who are guardians or wards of the above persons or other persons with whom they have personal connections or with the entities in which these persons are members of the Management or Supervisory Board, and did not grant them any loans, advances, guarantees or other agreements resulting in significant benefits for TP S.A, its subsidiaries and associates.

33 Related party transactions continued

33.2 Related party transactions

As at 31 December 2006, France Telecom S.A. ('France Telecom'), owned 47.5% of shares of the Company (see Note 30).

Related parties transactions were made on normal commercial terms.

Sales and purchases of goods and services:

(in PLN millions)	year ended 31 December 2006	year ended 31 December 2005
Sales of goods and services to:	**120**	**77**
– France Telecom (parent)	59	53
– France Telecom (group)	61	24
Purchases of goods and services from:	**332**	**195**
– France Telecom (parent)	135	97
– France Telecom (group)	197	98
Financial expense	**42**	**–**
– France Telecom (parent)	42	–
–France Telecom (group)	–	–

(in PLN millions)	At 31 December 2006	At 31 December 2005
Receivables from:	**37**	**23**
– France Telecom (parent)	28	19
– France Telecom (group)	9	4
Payables to:	**134**	**85**
– France Telecom (parent)	87	37
– France Telecom (group)	47	48

In April 2005, PTK-Centertel and Orange Brand Services Limited ('Orange') concluded a licence agreement, on the basis on which PTK-Centertel acquired rights to operate under Orange brand. The brand was introduced by PTK-Centertel in September 2005. The brand licence 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, the Company acquired 34.0% of the share capital of PTK-Centertel Sp. z o.o. from a subsidiary of France Telecom SA. 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 SA (see Note 19). 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 as a result of this transaction. As a result of the above, Telekomunikacja Polska holds 100.0% of share capital in PTK-Centertel.

34 Foreign exchange rates

The balance sheet data as at 31 December 2006 and 2005 presented in the table 'Selected financial data' was translated into Euro at the average exchange rate of the National Bank of Poland on the balance sheet dates. The profit and loss data, together with the cash flow data for the year ended 31 December 2006 and 2005, were translated into Euro at an exchange rate which is the arithmetical average of the average NBP rates published by the NBP on the last day of each month of years ended 31 December 2006 and 2005.

The exchange rates used in translation of balance sheet, profit and loss and cash flow data are presented below:

	31 December 2006	31 December 2005
Balance Sheet	3.8312 PLN	3.8598 PLN
Profit and Loss, Cash Flow data	3.8991 PLN	4.0233 PLN

35 Subsequent events

There were no significant events after the balance sheet date.

Independent Auditor's report

'To the Shareholders of Telekomunikacja Polska S.A.

1 We have audited the attached consolidated financial statements[1] of the 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 2006, containing:
- the consolidated balance sheet as at 31 December 2006 with total assets amounting to 32,611 million zlotys,
- the consolidated profit and loss account for the period from 1 January 2006 to 31 December 2006 with a net profit amounting to 2,096 million zlotys,
- the consolidated statement of changes in shareholders' equity for the period from 1 January 2006 to 31 December 2006 with a net increase in shareholders' equity amounting to 113 million zlotys,
- the consolidated cash flow statement for the period from 1 January 2006 to 31 December 2006 with a net cash outflow amounting to 797 million zlotys and
- the additional notes and explanations

('the attached consolidated financial statements').

2 The Company's management is responsible for the preparation and fair presentation of these financial statements in accordance with International Accounting Standards and International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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

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 the 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 2006 to 31 December 2006, as well as its financial position as at 31 December 2006;
- have been prepared, in all material aspects, in accordance with International Accounting Standards and International Financial Reporting Standards as adopted by the European Union;
- are in accordance with the provisions of laws affecting the content of the attached consolidated financial statements.

5 Without qualifying our opinion, we draw attention to the following issue:
As more fully explained in notes 32 (d) and 32 (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 'Management Board's Report[2] on the Group's activity for the period from 1 January 2006 to 31 December 2006 and the rules of preparation of the annual consolidated financial 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 on current and periodic information.'

on behalf of Ernst & Young Audit Sp. z o.o. Rondo ONZ 1, 00-124 Warszawa Reg. No. 130

Wojciech Pułkownik Certified Auditor No. 10477/7677	Jacek Hryniuk Member of Management Board Certified Auditor No. 9262/6958

Warsaw, 15 February 2007

[1] As presented on pages 36-81.
[2] As included in the Annual Report filed on the Warsaw Stock Exchange

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Glossary

Access Fee
revenues from monthly fee from New Tariff Plans (incl. Free minutes).

ADSL
see xDSL.

ARPL
Average Revenue per Line.

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

AUPU
Average Usage per User.

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.

DSLAM
Digital Subscriber Line Access Multiplexer.

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.

GOM
Gross Operating Margin.

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 TV
TV over Internet Protocol.

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.

LLU
Local Loop Unbundling.

MTR
Mobile Termination Rates.

MVNO
Mobile Virtual Network Operator.

Net FCF
Net Free Cash Flow = Net Cash provided by Operating Activities – (CAPEX + CAPEX payables).

NTP
New Tariff Plans.

Opex
Operating Expenditure (Total operating costs).

PLN
Polish złoty.

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

RIO
Reference Interconnection Offer.

SAC
Subscriber Aquisition Costs.

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

SMP
Significant Market Power.

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

UKE
Office of Electronic Communications (formerly URTiP-Polish Telecommunications & Post Regulator).

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

USO
Universal Service Offer.

VoIP
Voice over 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.

WLR
Wholesale Line Rental.

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.

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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

Quarterly reports
Q1'07 May 11, 2007
Q2'07 August 14, 2007
Q3'07 November 29, 2007
Q4'07 February 29, 2008

Half year report
H1'07 August 31, 2007

Full year results 2007
March 28, 2008

Consolidated full year results 2007
March 28, 2008

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

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