TP Group annual report 2010

Contents

TP Group is the largest telecommunications group in Poland, operating in all segments of the Polish telephony and communications industry. The Group owns the largest technical infrastructure in Poland, with operations in fixed-line voice, data and mobile networks, radio communication and satellite transmission.

At the end of 2010, our share of the Polish telecoms market (by volume) was 71.6% of fixed voice, 35.2% of fixed broadband, and 30.4% of mobile through the Orange brand. TP Group is 49.79% owned by France Telecom.

Our vision
TP Group's goal is to achieve a strong leadership position in all our core markets.

Our success will be founded on a broad portfolio of highly innovative products, a commercially powerful, proactive sales force and outstanding customer care, supported by a robust infrastructure and highly motivated employees.

Co-ordinating our efforts around a lean, agile operating model will ensure that we deliver healthy and sustainable returns to our shareholders.

group at a glance
continued

market cap*

21.8 bn

% change from 2009 +3.0%

labour expenses

2.2 bn

% change from 2009 -5.7%

dividend yield*

9.2%

total revenue

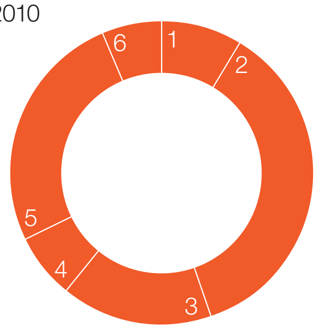
15.7 bn

% change from 2009 -5.1%

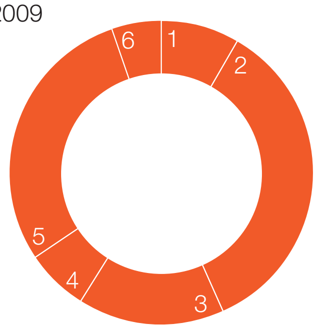
*as of the end of 2010
(market cap = share price x number of outstanding shares)

revenue transformation continues
% change on comparable basis

2010



2009



1	Mobile wholesale	-4.4%
2	Mobile retail	-1.1%
3	Fixed data	-2.9%
4	Fixed wholesale	+2.6%
5	Fixed voice retail	-16.1%
6	Sales of goods and other	+11.8%

financial highlights

mobile customer base

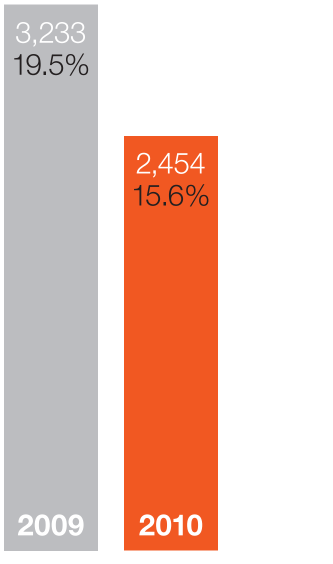
14.3mn

% change from 2009
+4.5%

total revenue
PLN mn

restated EBITDA*
PLN mn and % of revenue

net free cash flow
PLN mn and % of revenue



financial highlights

- Total revenue of PLN 15.7 bn
- Restated EBITDA* of PLN 5,772 mn, 36.7% of revenue
- Net free cash flow of PLN 2,454 mn, 15.6% of revenue
- Market cap** of 21.84 PLN bn, up 3.0% from 2009
- Dividend yield** of 9.2%
- Labour expenses down 5.7% from 2009
- PLN 481 mn cost savings delivered in 2010

operational highlights

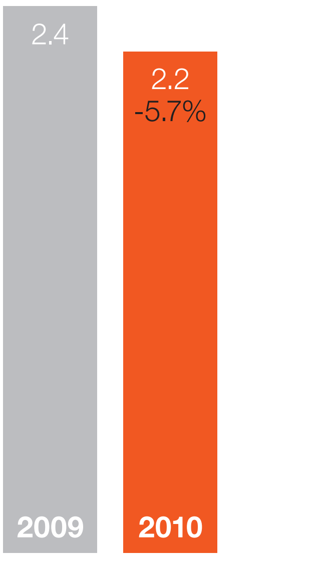
- Mobile market no.1 in Poland
- Signed framework agreement with TVN for broadband and TV bundle
- Network sharing agreement with PTC
- Launched “misja klient” programme that focusses TP around customer excellence
- Our mobile customer base has increased from 2009 by 4.5%
- Our TV customer base has increased from 2009 by 46.2% to 544 thousand

*The figures shown exclude the PLN 1.1bn increase of the provision for the DPTG dispute, recorded in 3Q2010. For a full explanation of the revised provision, see the notes to the accounts. See note 31 of the accounts

**as of the end of 2010

financial highlights
continued

labour expenses
bn



market cap*
PLN bn

*as of the end of each year

total shareholder return

+12.4%

in 2010

cost savings in 2010

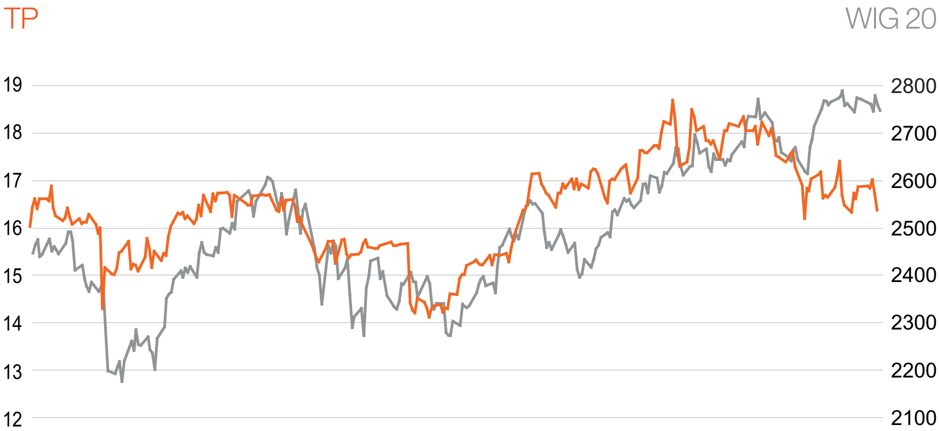
481mn

dividened per share

1.5 PLN

CEO's letter
Maciej Witucki
President of the Board
and Chief Executive Officer

TP share price vs WIG20



TPSA total shareholder return in 2010 +12.4%

CEO's letter continued

Dear shareholders,

2010 has been a year of steady and consistent progress for TP Group. We began the year by sharing with you our medium term action plan, based on three pillars: re-focus on core business, re-engage with customers, and re-balance the operating model. I am pleased to say that the company has risen to these challenges. We have made meaningful progress in every field of activity, and in each successive quarter.

This progress translates into concrete results. We were able to meet or exceed our 2010 guidance, delivering more than PLN 2.4 billion net free cash flow, at the same time as laying the foundations for a turnaround in 2011. Meeting our cash flow objectives once again allows us to offer attractive returns to our shareholders with a cash dividend per share of PLN 1.5 – a level of return in the top tier of European telco stocks.

Regulatory breakthroughs

By far the biggest change to TP Group's competitive landscape in 2010 was brought about by the Polish Regulator's decision to remove the link between TP's wholesale and retail prices. Now, the regulator's intervention is limited to ensuring that TP's retail prices are not predatory towards alternative operators. As the country's major supplier of wholesale data services, TP Group was seriously hampered by the previous system, which calculated the wholesale price on a "retail minus" basis and made it very hard for TP's retail broadband services to compete on price. The change to the regulations has allowed us to re-engage with the market on a level playing field.

The new, more stable and predictable regulatory environment has not just made us more competitive. It has also helped to create the right conditions for us to re-focus on core business, and to make the necessary investments in our network to support a new generation of high-speed data services. These developments benefit the whole of the Polish telecoms market economy and more importantly the Polish consumer.

Regaining momentum in key markets

Our commercial performance across the Group has been solid. In mobile, four consecutive quarters of growth in the Orange customer base were accompanied by a return to revenue growth in Q4. A new customer segmentation philosophy – based on usage patterns rather than spend – stimulated usage, boosted customer adds and helped us to regain the number 1 position in the market. And in broadband, we have worked hard on revamping our offer, with the result that we were able to reverse the downward trend, seeing the first signs of a turnaround in Q4 when we added 17,000 new customers.

Improving revenue trends

After a very tough couple of years, 2010 was characterised by steady improvement in our top line. We started the year with a decline of 10.2% in Q1, and by Q4 we had reduced it to -1.2% for the quarter. Full year revenue erosion was limited to 5.1%, compared to 8.8% in 2009. This vindicates our decision to focus on our core business and concentrate on establishing a sustainable leadership position in our key markets.

Robust cost saving plans implemented

We are now fully embarked on the cost saving initiatives that form a key part of our strategy to rebalance our operating model and make TP Group into a leaner and more agile business. Already, these initiatives have delivered almost half a billion zloty of savings, bringing our cost base* down by almost 4% versus 2009. These measures have helped us to defend our EBITDA margin at a level of 36.7%**.

For a full explanation of the revised provision, see note 31 of the accounts.

Looking ahead

2010 was the year that TP got back into the driving seat. Our disciplined execution of the medium term action plan enabled us to regain commercial momentum and stabilise profitability while delivering on all our promises to shareholders. But we are not relaxing our effort one bit. We believe that this turnaround in the company's performance will really take off in 2011.

*Total cost base up to EBITDA, excluding revision of the provisions for claims and litigations, amounting to PLN 1,182 million in 2010 vs PLN 56 million in 2009

**The figures shown exclude the PLN 1.1bn revision of the provision for the DPTG dispute, recorded in 3Q2010.

In 2010 we took our first steps on a number of projects which will be key to TP Group's future: a landmark deal was initiated with TVN, to offer the best bundled home entertainment packages in Poland; we explored a potential network-sharing project with ERA that could reap benefits for years to come; and Orange and TP became sponsors for the Euro 2012 championship.

For our mobile customers, 2011 will be the year of the smartphone: affordable Android-based handsets will support a step-change in the use of mobile data services. And continued investment in our network will allow us to speed things up for everyone: mobile customers will benefit from faster data transmission thanks to the HSPA2+ roll-out, while the launch of VDSL 'fibre to the curb' will bring fixed line broadband speeds up to 40Mb/s and more.

In addition, I have just launched an exciting company-wide program that will focus the entire organisation around customer excellence. Called "misja klient" – "mission customer" – it will significantly improve the way TP Group does business, taking us to best-in-class customer service. The renewed focus on our customers should be visible not only in the products and services we offer, but also in the way we sell and deliver those products and the customer service that follows. Within the next 12 months, customer relations will become the differentiating factor for TP Group in the Polish market.

These projects will secure our future growth, but they will require investment. It is therefore essential that we continue to show discipline as we follow our medium-term action plan. In 2011 and beyond, TP Group will stay focused on cutting costs, increasing efficiency and maintaining healthy cash generation.

I am proud of the way the people who make up TP Group have risen to the challenges we set ourselves in 2010. On behalf of the whole management team, I thank them for their dedication to our company. Looking back on our progress this past year, I have total confidence that we can continue to achieve all that we have set out to do in 2011 and beyond.

Maciej Witucki
President and CEO

summary of performance against strategic goals

re-focus on core

Our vision
— Capitalise on new regulatory environment
— Concentrate on products and customers
— Invest in the future of broadband

Our commitment
1.2 million new /upgraded broadband lines by end 2012, including 317,000 in 2010

Progress
— Change of 'retail minus' BSA pricing model to 'cost plus'
— Price reductions made TP competitive again
— Broadband investment programme ahead of schedule
— Renewed focus on customers and products visible in commercial performance

Key performance indicators
— Over 400,000 new/upgraded lines in 2010

re-engage with markets

Our vision
— Increase customer loyalty
— Build critical mass in TV
— Halve time to market for new products
— Move to next generation customer care

Our commitment
Regain leadership in mobile and broadband

Progress
— Signed framework agreement with TVN
— Launched "misja klient" programme
— Return to growth in mobile and broadband

Key performance indicators
— Mobile market no. 1
— Added 17,000 broadband customers in Q4
— Over 600, 000 mobile net adds
— Over 500, 000 TV clients

re-balance operating model

Our vision
— Reduce opex
— Rebalance cost structure (from non-commercial to commercial costs)
— Allocate capex to support new operating model

Our commitment
Robust cost transformation plan to offset impact of regulation and preserve margins

Progress
Cost transformation programme including
— Office space optimisation
— Consolidation of customer care operations
— Process simplification
— Intra-sector co-operation to reduce costs

Key performance indicators
— Almost PLN 500 million savings in 2010
— Cost base -3.9%*
— IT vendors consolidated from 50 to 5
— Cooperation project started with PTC

*Total cost base up to EBITDA, excluding revision of the provisions for claims and litigations, amounting to PLN 1,182 million in 2010 vs PLN 56 million in 2009

our vision

TP Group's goal is to achieve a strong leadership position in all our core markets.

Our success will be founded on a broad portfolio of highly innovative products, a commercially powerful, proactive sales force and outstanding customer care, supported by a robust infrastructure and highly motivated employees. Co-ordinating our efforts around a lean, agile operating model will ensure that we deliver healthy and sustainable returns to our shareholders.

a bright financial future

pursuing a clear strategy

spotlight on customer service

bringing smarter technology to light

our vision
financial performance improvement

For more information on how we are improving financial performance please visit http://telekom-polska-annual-report-2010.production.investis.com/our-vision/a-bright-financial-future.aspx

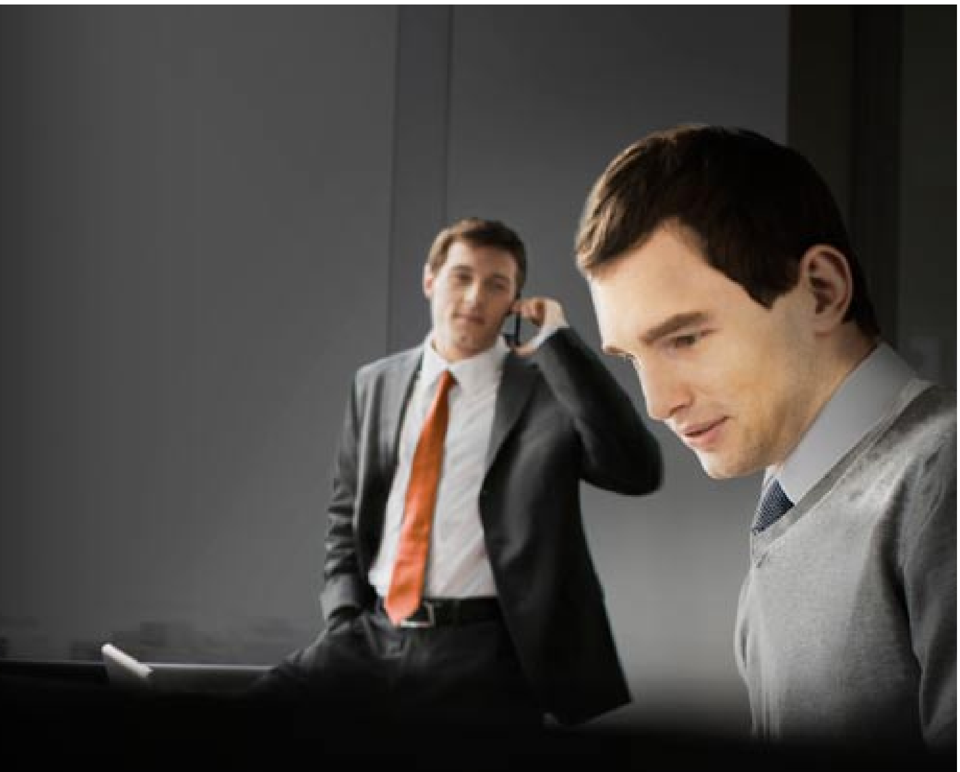
After a full year of implementing our medium term action plan, TP Group's results have reaffirmed our strategic objectives and the financial future is looking bright. Successful marketing complemented by a far-reaching cost optimisation program enabled us to deliver strong net free cash flow, preserve a robust balance sheet and offer shareholders an attractive level of remuneration. 2011 will see us concentrating mainly on restoring broadband growth and developing excellence in customer relations. At the same time, we will stand firm in our commitment to cash generation and ensuring sustainable profits. Our cost optimisation program continues, and net free cash flow generation remains our ultimate target.

a bright financial future

our vision

good strategic developments from within the medium term action plan

For more information on our strategic developments please visit http://telekom-polska-annual-report-2010.production.investis.com/our-vision/pursuing-a-clear-strategy.aspx



Our medium term action plan is based on three pillars: re-focus on core business, re-engage with customers, and re-balance the operating model. In 2010 our disciplined pursuit of these goals enabled us to regain commercial momentum and stabilise profitability while delivering on all our promises to shareholders. We made meaningful progress in every field of activity, and in each successive quarter. But we are not relaxing our effort one bit. We believe that this turnaround in TP Group's performance will really take off in 2011, as the company stays focused on cutting costs, increasing efficiency and maintaining healthy cash generation.

pursuing a clear strategy

benefits gained from the agreement with the regulator

For more information on our agreement with the regulator please visit http://telekom-polska-annual-report-2010.production.investis.com/our-vision/spotlight-on-customer-service.aspx

Our key customer service achievement in 2010 was to make significant improvements in efficiency without compromising service excellence. In 2011, our commitment to customer service is stronger than ever. While we continue to make our systems and processes more streamlined, we have also launched an exciting company-wide program – “misja klient” – that will focus the entire organisation around customer excellence. The renewed focus on our customers will be visible not only in the products and services we offer, but also in the way we sell and deliver those products and the customer service that follows. Within the next 18 months, customer relations will become the differentiating factor for TP Group in the Polish market.

spotlight on customer service

becoming market leaders in trends beyond the medium term action plan

For more information on how we are becoming market leaders please visit: http://telekom-polska-annual-report-2010.production.investis.com/our-vision/bringing-smarter-technology-to-light.aspx

Our network is undergoing a transformation, as we gear up to give our customers a revolutionary increase in fixed and mobile broadband speeds in 2011. For our mobile customers, faster data transmission coupled with affordable Android-based handsets will make 2011 the year of the smartphone, while in the home our TV customers will benefit from the best combination of content and functionality on the market, thanks to a link-up with TVN. As we continue to optimise our operating costs, we are also exploring smarter technological solutions that could spell significant efficiency savings. One of these is mobile network sharing – a solution that would cut costs while offering our customers wider coverage and a broader frequency range.

bringing smarter technology to light

2010 operating review
market climate

Polish macroeconomy

In 2010, Poland's economy showed encouraging signs of being back on track with a 3.8% rise in real GDP. Although unemployment continues to be relatively high at around 12%, this number has fallen from its peak earlier in the year and analysts are positive about the outlook for 2011, the most recent European Commission forecast on March 1st 2011 predicted 4.1% GDP growth.

The impact of the global financial crisis on the telecom sector has been moderate, as customers tend to look for economies rather than cutting down their usage.

Mobile market

Smartphones have been the big story in the global mobile phone market in 2010. The global smartphone market grew by almost 68%, and analysts estimate further growth of 43.7% in 2011 (Source: IDC). Poland is well behind the growth curve: with a relatively low penetration of smartphones, the potential for this market in 2011 and beyond is enormous. TP has laid the groundwork for this development with mid-price android platform handsets and pre- and post-paid tariffs specially tailored for smartphones. The smartphone revolution in Poland is already getting underway: 22% of post-paid customer adds in the fourth quarter of 2010 included a smartphone, up from just 4% a year earlier.

Broadband and TV market

The value of Poland's broadband market continued to grow in 2010, but more slowly than the previous year – an increase of 6.3% compared to 10.8% in 2009. Due to historical reasons, penetration in Poland reached 17% of the population by the year's end, up from 15.9% a year earlier. Poland's broadband market place is quite fragmented. New technologies, including radio access, have contributed to an increase in the number of small, local Internet providers; taken together, they represent a significant force in the broadband market.

On the other hand, market consolidation intensified in 2010 as smaller Internet providers were acquired by larger players, such as Netia, Multimedia Polska, Aster and Hyperion. In Q1 2011, UPC is due to complete the acquisition of Aster, and Vectra and Multimedia Polska are also putting together a deal.

Cable TV operators continued to put pressure on the broadband market, growing their share to 24% by value thanks to bundled offers and high speeds. In general, Poland's Internet is getting faster: TP Group is raising the game with the introduction of 40+ Mb/s VDSL technology in the first half of 2011. In comparison to other EU countries, Poland has plenty of scope for improvement.

As of July 2010, an EU Commission study noted that around 60% of Poland's broadband lines offered speeds below 2 Mb/s, compared to 9.4% of lines in Spain and just over 1% in the UK. The same study found 7.2% of lines in Poland operating at speeds of 10 Mb/s and above, compared to 28% of lines in Spain and almost 25% in the UK.

For now, Poland's satellite-based DTH TV players (TVN, Canal+, Polsat) do not compete for broadband customers. However, if regulations changed they could theoretically put together a bundled offer including mobile broadband.

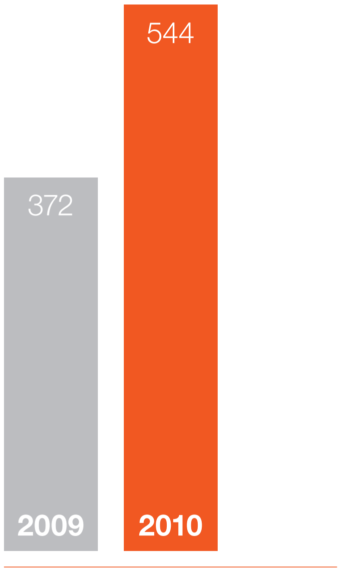
Major trends on telco market

After two years of contraction, the Polish telecom market returned to growth in the fourth quarter of 2010. This recovery was largely driven by a turnaround in the mobile market, which recorded 1.5% growth in Q3 and 5.1% growth in Q4. In the fixed line market recovery was more gradual: a 5.3% decline in the first half of the year was moderated to -4.9% in the second. The future growth of the fixed line market is dependent on broadband services, a sector that has lost ground to cable TV operators in recent years, particularly in major cities. The roll-out of higher-speed, lower-cost ADSL broadband will provide much stronger competition for cable TV operators over the next few years.

2010 operating review
market climate
continued

mobile customer base
mn

TV customers
'000



broadband customers
'000

2010 operating review
regulatory environment

In what was a relatively quiet year in terms of regulatory announcements, we concentrated on implementing the historic Memorandum of Understanding (MoU) that TP Group and UKE signed in October 2009. In accordance with the terms of the MoU, we have invested in broadband access lines, bringing over 450,000 new or upgraded lines into service so far. We have taken steps to ensure non-discriminatory practices towards alternative operators, implemented Chinese walls within our organisation and cooperated with quarterly independent audits. We have also dropped a number of pending legal cases against alternative operators. The risk of functional separation has been significantly reduced.

The transition from 'retail minus' to 'cost plus' pricing model for our wholesale data services went smoothly, giving a boost to TP Group's broadband business, but also heralding a new era of choice and competitive pricing for Polish consumers. There were no cuts to Mobile Termination Rates in 2010, but we are having a productive dialogue with UKE about next year's planned reductions.

spent on the broadband investment program in 2010

663mn

broadband lines built/ modernised in 2010

416,000

share of smartphones in post-paid sales*

*total smartphones in acquisition and retention in the period

2010 operating review
products and services

We began the year with a renewed sense of priority, centred around one of the three pillars of our medium term action plan: to re-engage with our key markets. We ended the year with both mobile and broadband customer numbers back to growth, and with the number one market position in mobile: achievements that illustrate how TP Group's relationships with customers are evolving and improving. Our "misja klient" initiative will define our approach in 2011 and beyond, as customer excellence becomes more and more of a key differentiator for TP Group.

Vincent Lobry
Vice President of the Board and Chief Marketing Officer

Mobile: more sophisticated customer offers

With Orange now positioned as the leading player in a maturing mobile market, our focus is increasingly on customer retention and development rather than new customer acquisition.

The most important development in the mobile business in 2010 was the introduction of a range of new offers based on customer usage, not just on customer spend. In the post-paid market we introduced Orange 'animal tariffs', packages tailored to suit each customer's most frequent activity – panther for browsing, dolphin for talk and pelican for text. In the pre-paid market, too, we gave customers more flexibility to adjust their bundle to their usage with 'orange na karte'. We were delighted by the success of this new approach, which was instrumental in regaining the number one position in terms of market share. The numbers confirm that the new offers are also stimulating usage, including data: customers are using more minutes and committing to higher-value bundles.

Broadband: the foundations for recovery

In broadband, we turned a number of factors to our advantage in order to lay the groundwork for a major turnaround in 2011. Firstly, the new 'cost plus' wholesale pricing model put us back in competition on equal terms with alternative operators. We responded promptly, with new price plans designed to help migrate customers to higher speeds, and new investments in our VDSL network to facilitate those speeds. The first signs of recovery were already visible in the fourth quarter, when we added 17,000 subscribers, and we anticipate a gradual gain in market share in Poland's major urban centres through 2011.

TV: a key differentiator

In 2010 TP saw a surge in demand for our TV offers. The customer base for our bundled broadband and TV packages grew dynamically, reaching 544,000 by the year's end. Demand for premium pay TV packages also increased, reaching 125,000 subscribers and making TP a viable player in the TV arena. The most exciting development in 2010 was the signing of a framework agreement with TVN, securing for TP Group's customers the best combination of content and functionality on the market today and paving the way for TP Group to make a big impact on the TV market in 2011.

UEFA Euro 2012: raising our profile

Orange Global won the major sponsor role for the UEFA Euro 2012 Championship: a major coup for TP Group. It will give us invaluable exposure for our brands on a high profile national and international stage. TP Group will also be the official telecoms partner to the tournament's organisers.

2010 operating review customers and distribution

The key challenge for this area of the business in 2010 was to make significant improvements in efficiency without compromising customer service excellence. We completed a major integration project successfully, saving time and costs while actually improving our relationships with customers. As we move into 2011, our focus on efficiency has not diminished; as we continue to make our systems and processes more streamlined, the "misja klient" initiative will keep our efforts centred on making things simpler and easier for our customers at the same time.

Mariusz Gaca
Chief Commercial Officer,
Chief Executive Officer of PTK Centertel
(TP 's Mobile arm)

e-invoices monthly

1.2 mn

up from 0.4 million in 2009

cost optimisation

0.5 bn

savings in 2010

Orange Customer Service

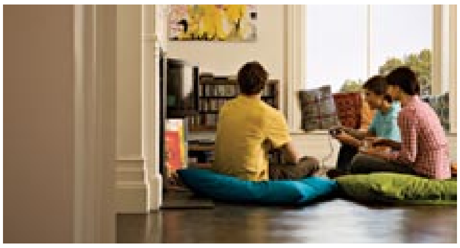
In Q3 we completed a major integration project in customer care, rationalising all our customer support teams into one subsidiary called Orange Customer Service. As well as making efficiency savings, this new model allows us to provide better customer service. For example, we now handle calls more effectively, routing them via national competence centres rather than regional call centres so that customers can speak to the right expert first time.

Modernising sales and distribution

By bringing our systems and processes right up to date, we are creating a simpler relationship with our customers. A bigger role for modern self-care channels – including automated phone services and online help centres – allowed us to optimise the number of physical points of sale while improving customer choice. We also increased the use of e-invoices, and found innovative ways to replace some of the formal written orders with voice recordings. These are just two examples of initiatives that offer a triple win: they are ecologically sound, they reduce our operating costs and they improve the customer experience.

Focus on loyalty and retention

Great customer care is a major part of our drive to retain customers and make them more loyal to our brands. The numbers show us that our efforts are paying off: we have stabilised customer churn in mobile, and begun an important fight-back in broadband. Part of our success in that sector is due to widening sales channels. For the first time in 2010, TP Group's broadband products went on sale direct to the consumer via the Orange shop network. In every area of our customer care and distribution operations, we are making it easier for people to stick with TP Group.



2010 operating review
technology

Our network is undergoing a transformation. Not only are we investing in building a robust and powerful broadband infrastructure for Poland, we are also gearing up to give our customers a revolutionary increase in fixed and mobile broadband speeds in 2011. Our task in 2010 was to lay the groundwork for this modern network that will shape Poland's economic and social future. Having made the necessary careful preparations, we are now ready to take our customers full speed ahead in 2011.

Piotr Muszyński
Vice President of the Board and Chief Operating Officer

VDSL in speeds of

40Mb/s+

to be offered in 2011

Mobile network

Our customers increasingly expect their mobile devices to handle large amounts of data, and they want the best speeds available. In 2010 we began to upgrade our network to HSPA2+ (3G+), completing coverage for 50% of the country by the end of the year. This technology allows transfer speeds of up to 42Mb/s.

Upgrading and maintaining the network requires investment. As we continue to optimise our operating costs, we are increasingly looking for creative ways to find significant efficiency savings – for example, through intra-sector cooperation. In 2010 we signed a letter of intent with ERA concerning possible network sharing in future – a solution that should cut costs and benefit our customers with wider coverage and a broader frequency range.

Broadband network

In addition to our major network build-out of 400,000 new or upgraded lines (according to the terms of our MoU with the Regulator), we spent 2010 preparing the whole of our broadband network for the introduction of VDSL technology in 2011. Around 6000 optical network units are now in place, and we have completed the necessary tests that pave the way to offer our customers unprecedented speeds of 40Mb/s and more.

IT efficiencies

As promised in our medium term action plan at the start of the year, we consolidated our IT vendors from over 80 down to just 5. By selecting just a small number of key partners, and by adopting a 'function points' methodology for estimating workload, we have made IT not only cheaper but more flexible too, decreasing our time to market for new products. We have also begun to implement cloud computing solutions, which cut energy use and cost, increase server efficiency and reduce demands on IT support staff.

In 2010, we worked hard to enact the principles outlined in our medium term action plan, and to unite our workforce around that plan. New incentive structures for managers, based on the action plan, aligned the individual's goals and the Group's, while we pursued a constructive dialogue with our social partners to ensure their support. Looking forwards, we need to focus all employees around the "misja klient" initiative; our people are our greatest asset in the pursuit of customer excellence.

Jacek Kowalski
Board Member in charge of Human Resources

labour cost reduction

5.7%

employees transferred to Orange Customer Service

5,000

full time equivalent

Our values
TP Group prides itself on being a good employer. We do not discriminate on the grounds of gender, ethnicity or disability and we take steps to safeguard our employees' rights – principles that are enshrined in our Code of Ethics, and monitored closely from day to day.

Talent management
Inevitably, TP Group's headcount has been on a downward curve for some years, as industry technology and more efficient ways of working have reduced the need for manual and clerical tasks. But as the size of the workforce has reduced, the talent requirement has increased. It is vitally important to us that we attract and maintain the very best people to take our vision for the company forwards. In 2010 we completely overhauled our incentive scheme for managers, tying their bonuses to the Group's strategic goals. By aligning the interests of employees and shareholders in this way, we give ourselves the best platform for success.

Cost optimisation
Headcount decreased once again in 2010, as process simplification allowed us to operate more efficiently. Around 2000 full time employees left TP Group during the year. Group labour costs were down 5.7% on a year earlier. Relations with our social partners continued to be both robust and constructive.

2010 operating review
corporate social responsibility

Our organisation has been part of the fabric of Polish society for more than 60 years. Telecommunications services have played a huge part in the successful development of our society and its economy, from post-war hardship through to EU membership. We are proud of our history and continue to take very seriously our responsibilities to the communities we serve and to the natural environment we share.

UN Global Compact

Since 2006, TP Group has been a signatory to the UN Global Compact, a set of ten core principles in the areas of human rights, labour, the environment and anti-corruption. Each year, we publish an account of the progress we have made in supporting and enacting these values.
To read the 2010 report go to www.orange.com "responsibility" column

Orange Foundation

Today, the majority of TP Group's philanthropic activities take place under the banner of the Orange Foundation. The Foundation is focused on helping children and young people, and its mission can be summed up in the motto, "Caring for the next generation". As well as its own programs, the Orange Foundation gives direct grant support to other NGOs working with similar aims in the areas of education, health care and culture. The Foundation also promotes volunteering, particularly among the employees of TP Group – more than 5% of whom gave their time to charitable projects in 2010.

Key initiatives of the Orange Foundation include:

Education with TP Internet: supports Internet access provision, Internet safety education and e-learning in over 13,000 schools throughout Poland (45% of total school system, serving over 4 million students).

Orange Academy: issues grants for innovative educational projects centred around new technology, including the installation of ICT facilities in 3,500 libraries.

Phone to Mum: supports sick children and their families by maintaining over 1000 colourful free phones in children's wards and giving out free phonecards – over a million so far.

School Without Violence: anti-bullying campaign, under the honorary patronage of the Polish President. Already taken up by 15% of Poland's schools.

Sounds of Dreams: provides hearing aids and rehabilitation services that have helped over 1000 hearing-impaired children since 2006.

You can learn more about these and other projects by visiting the Orange Foundation website here www.fundacja.orange.pl

Bridging the digital divide

As the largest telecom group, not only in Poland but also in Central and Eastern Europe, we have an important social role to play in building an information society accessible to all. Our network investments will combat digital exclusion by ensuring that state-of-the-art telecommunication infrastructure reaches even the remotest parts of Poland.

Providing broader access to digital communication tools means not only investing in infrastructure but also breaking social barriers connected with new technologies. One barrier is caused by our worries about the youngest users of modern media. TP Group's response to that is the "Education with Internet TP" program in which we offer Internet at preferential terms to schools and we support children, parent and teacher education on web safety.

We also fight exclusion due to social circumstances. Last year, we created a computer program called B-link, based on open source software technologies, which makes it possible for the disabled to use computers by eye blink. Eleven thousand people have downloaded the software so far.

Environmental awareness

We are far from indifferent to the global challenges around energy resources and environmental protection. Here, TP Group has a positive contribution to make. The latest ICT solutions we offer allow us to help limit our customers' negative impact to some extent without impeding economic development. For example, tele- and video-conferencing mean fewer business meetings that require physical presence. This, in turn, means fewer people travelling by car, train or airplane.

Even though our business is not directly responsible for hazardous emissions, we never stop thinking green. We have introduced e-document flow in our offices and provide our customers with electronic invoices. We have also taken major steps to reduce consumption of electricity in recent years by introducing power conservation policies in offices and educating staff about what they can do to save energy. A major overhaul of our IT systems in favour of "Green IT" has led to more efficient power consumption in both offices and technical infrastructure.

Code of Ethics

TP Group's corporate values are formalised in a Code of Ethics, adherence to which is scrutinised by the Ethics Committee. The Code covers the whole spectrum of corporate good behaviour, including non-discriminatory employment practices, sound relationships with suppliers, whistleblowing and respect and tolerance between members of staff.

To read more about our CSR performance in the Global Compact Report go to http://www.tp-ir.pl/csr/ethic.aspx

2010 financial review

TP Group's performance has been solid throughout the year. The success of our marketing was complemented by a robust cost optimisation program, enabling us to deliver on all our 2010 objectives. We have delivered strong net free cash flow generation, preserved a safe balance sheet, and can once again offer our shareholders an attractive level of remuneration.

Whilst we are disappointed with the award in the DPTG arbitration, we have already begun its legal challenge and we can reaffirm that this dispute will neither affect our dividend policy nor the implementation of our medium term action plan.

Jacques de Galzain
Chief Finance Officer

Revenue trends stabilising

Revenue for the full year was PLN 15.7 billion, down 5.1% on 2009. Throughout 2010, we reported gradual quarter-after-quarter improvements in revenue trends. At the end of the first quarter, revenue was down 10.2% on the same period a year earlier, and by quarter four it was just 1.2% lower, year on year. The numbers were boosted in the fourth quarter by the absence of impact from MTR cuts on the year-on-year comparison, and by strong performance in the mobile business with over 6% revenue growth backed by 200,000 net adds and stable ARPU. Revenue from the fixed segment also recovered somewhat in 2010, though at a much slower pace. A more dynamic upturn in this segment will only be possible once broadband revenue returns to healthy levels – a recovery which will be hastened by 2010's regulatory developments.

Defending margins, maintaining profitability

Our restated EBITDA margin for the full year was 36.7%*, just 1.2 percentage points down on the previous year. This performance reflects the solid results of our cost transformation program, which has delivered almost PLN 500 million of savings and brought our cost base down by about 4%* since 2009.

Full year EBITDA fell by roughly PLN 500 million to PLN 5.77 billion*. But declining depreciation and favourable foreign exchange rates helped us to maintain profitability: at roughly PLN 1.2 billion*, our restated net income was only PLN 80 million lower than the previous year. This shows that TP Group's business is resilient to revenue erosion.

Capex objectives achieved

Total capital expenditure for the year was PLN 2.7 billion, or 17.3% of revenue. When we announced our medium-term action plan a year ago, we explained that our new regulatory obligations made it inevitable that capital expenditure over the next three years would rise. We also promised that, in planning our capex allocation, we would prioritise those projects that support the new, leaner operating model that we are all working towards.

We have been true to our word, investing roughly 40% of our capex in broadband – the key area for our future growth. Another 30% went towards the IT systems that we need to manage the network and support our sales, customer care and service delivery processes. And the remaining 30% of capex went into our network infrastructure, to be shared between mobile capacity upgrades, the first phase of HSPA2+ implementation and core network investments.

Cash generation exceeds expectations

TP Group's cash generation remained robust, with net free cash flow of over PLN 2.4 billion for the year – comfortably exceeding our initial expectations of PLN 2 billion. Looking at the year-on-year comparison, net free cash flow was down, as a result of lower EBITDA and the increase in capital expenditure required for our medium term action plan, as detailed above.

Nevertheless we maintained high enough levels of cash generation to allow us to further decrease our net debt. At the end of 2010 it amounted to roughly PLN 3.8 billion, a reduction of half a billion compared to a year earlier. As a result, we have preserved the strength of our balance sheet, with our net gearing ratio at 21% and net debt to EBITDA at 0.7. A strong balance sheet and high liquidity contribute to the maintenance of our solid credit ratings (A3/BBB+) and provide the security and flexibility we need to finance our operations and maintain our dividends to shareholders.

Proposed shareholder remuneration

In considering the proposed level of shareholder remuneration for 2010, TP Group has followed its existing policy, taking the following parameters into account in order to offer its shareholders an attractive remuneration:

- the level of competition in TP Group's markets
- the resource flexibility required to make the capital expenditures necessary to sustain profitable growth
- the financial discipline needed to support the current rating at A3 / BBB+.

Based on the 2010 results and taking into account the current economic climate, the Management Board have submitted to shareholders' approval a shareholder remuneration of around PLN 2 billion, equivalent to PLN 1.50 per share.

Looking ahead

After a full year of implementing the medium term action plan, TP Group's results have reaffirmed our strategic objectives and the dividend policy we presented at the start of the year. In 2011, the continued progress of our action plan will see us concentrating mainly on restoring growth and developing excellence in customer relations. At the same time, we will stand firm in our commitment to cash generation and ensuring sustainable profits. Our cost optimisation program continues, and net free cash flow generation remains our ultimate target.

*The figures shown exclude the PLN 1.1bn revision of the provision for the DPTG dispute, recorded in 3Q2010. For a full explanation of the revised provision, see the notes to the accounts. See note 31 of the accounts.

corporate governance

As a company listed on both the Warsaw and London Stock Exchanges, we are committed to maintaining standards of corporate governance which are in accordance with international best practice. We are sensitive to the expectations of the international investment community and our domestic investor base in Poland.

Both the supervisory and Management Boards of TP Group see governance as a continuing set of processes linked to our annual business cycle. We are committed to transparency in our corporate governance.

Supervisory Board members and committees go to page 26.

Report on Supervisory Board activities go to page 27.

Reports on activities of the Supervisory Board's committees go to page 35.

Assessment of TP Group's situation in 2010 prepared by the Supervisory Board go to page 32.

Management Team members go to pages 24 and 29.

The following information is also available on our website:

Ownership structure and ownership history
http://www.tp-ir.pl/corporate-governance/ownership-structure.aspx?sc_lang=en

Articles of Association
http://www.tp-ir.pl/corporate-governance/corporate-documents.aspx?sc_lang=en

Annual shareholders' meeting procedures
http://www.tp-ir.pl/corporate-governance/corporate-documents.aspx?sc_lang=en

Operating rules for the Management Board and the supervisory board
http://www.tp-ir.pl/corporate-governance/corporate-documents.aspx?sc_lang=en

Corporate governance disclosure to the Warsaw Stock Exchange
http://www.tp-ir.pl/corporate-governance/corporate-documents.aspx?sc_lang=en

Dividend payment
http://www.tp-ir.pl/shares/shareholder-remuneration.aspx?sc_lang=en

management team

Maciej Witucki

President of the Board
and Chief Executive Officer

Vincent Lobry

Vice President of the Board
and Chief Marketing Officer

Piotr Muszyński

Vice President of the Board
and Chief Operating Officer

Jacques de Galzain

Chief Financial Officer
and Management Board Member

Jacek Kowalski

Board Member in charge
of Human Resources

Mariusz Gaca

Chief Commercial Officer,
Chief Executive Officer of PTK Centertel
(TP 's Mobile arm)

corporate governance
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 review and approval of 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 Company's Articles of Association; increase and reduction of the share 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.

the ownership structure of TP share capital
(as of 23 February 2011)

	% of votes
France Telecom S.A.	49.79
Capital Group International, Inc.*	5.06
Other shareholders, including GDR holders	45.15
Total	100.00

On 5 August 2010, the Treasury Ministry informed that it sold its entire stake in TPSA (4.15%) on Warsaw Stock Exchange.

*Number of shares according to the notification by Capital Group International, Inc. on 15 October 2010.

corporate governance
the supervisory board

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 among others 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 coordinated 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 committees to which these tasks are delegated are described in further paragraphs.

Composition of TP Supervisory Board (as of 31 March 2011)

1 Prof. Andrzej K. Koźmiński - Chairman, Independent Board Member
2 Olaf Swantee - Deputy Chairman and Chairman of Strategy Committee
3 Olivier Faure - Secretary
4 Timothy Boatman - Independent Board Member and Chairman of Audit Committee
5 Thierry Bonhomme - Board Member
6 Jacques Champeaux - Board Member
7 Ronald Freeman - Independent Board Member and Chairman of Remuneration Committee,
8 Dr Mirosław Gronicki - Independent Board Member
9 Marie-Christine Lamber - Board Member
10 Pierre Louette - Board Member
11 Prof. Jerzy Rajski - Independent Board Member
12 Gérard Ries - Board Member
13 Dr Wiesław Rozłucki - Independent Board Member.

Changes to the Supervisory Board following the period under review in this report:

In connection with resignation of Mr. Raoul Roverato from his position on the Supervisory Board of TP with effect from 26 January 2011, Mr. Gérard Ries was appointed as Supervisory Board member on January 27, 2011.

In connection with resignation of Mr. Oliver Barberot from his position on the Supervisory Board of TP, Mr. Pierre Louette was appointed as Supervisory Board member on March 24, 2011.

Composition of Committees of the Supervisory Board (as of 31 March 2011)

Audit Committee

Timothy Boatman Chairman
Olivier Faure
Ronald Freeman
Marie-Christine Lambert.

The Audit Committee is chaired by Mr. Timothy Boatman, an independent member of the Supervisory Board. He has relevant experience and qualifications in finance, accounting and audit.

Remuneration Committee

Ronald Freeman Chairman
Olivier Faure
Wiesław Rozłucki
Olaf Swantee.

Strategy Committee

Olaf Swantee Chairman
Jacques Champeaux
Mirosław Gronicki
Jerzy Rajski
Gérard Ries.

corporate governance report on supervisory board activities

TP S.A. Supervisory Board composition

Supervisory Board composition as on January 1, 2010:

1 Prof. Andrzej K. Koźmiński - Chairman
2 Olivier Barberot - Deputy Chairman and Chairman of the Strategy Committee
3 Olivier Faure - Secretary
4 Antonio Anguita - Board Member
5 Vivek Badrinath - Board Member
6 Timothy Boatman - Board Member and Chairman of the Audit Committee
7 Jacques Champeaux - Board Member
8 Ronald Freeman - Board Member and Chairman of the Remuneration Committee
9 Dr. Mirosław Gronicki - Board Member
10 Marie-Christine Lambert - Board Member
12 Prof. Jerzy Rajski - Board Member
11 Raoul Roverato - Board Member
13 Dr Wiesław Rozłucki - Board Member

In 2010, composition of the Supervisory Board changed as follows:
Mr Vivek Badrinath resigned from his position as member of the Supervisory Board with immediate effect as of 22 April 2010. The mandates of Messrs. Antonio Anguita, Jacques Champeaux, Ronald Freeman and Mirosław Gronicki expired on 23 April 2010.On the same day, Messrs. Jacques Champeaux, Ronald Freeman, Mirosław Gronicki, Thierry Bonhomme, Olaf Swantee were appointed by the Annual General Meeting as Members of the Supervisory Board.

Supervisory Board composition as on 31 December 2010:

1 Prof. Andrzej K. Koźmiński - Chairman
2 Olivier Barberot - Deputy Chairman and Chairman of the Strategy Committee
3 Olivier Faure - Secretary
4 Timothy Boatman - Board Member and Chairman of the Audit Committee
5 Thierry Bonhomme - Board Member
6 Jacques Champeaux - Board Member
7 Ronald Freeman - Board Member and Chairman of the Remuneration Committee
8 Dr. Mirosław Gronicki - Board Member
9 Marie-Christine Lambert - Board Member
10 Prof. Jerzy Rajski - Board Member
11 Raoul Roverato - Board Member
12 Dr. Wiesław Rozłucki - Board Member
13 Olaf Swantee - Board Member

In connection with resignation of Mr. Raoul Roverato from his position on the Supervisory Board of TP with effect from 26 January 2011, Gérard Ries was appointed as Supervisory Board member on January 27, 2011.

At present, TP has six independent members in the Supervisory Board, namely Messrs. Prof. Andrzej K. Koźmiński, Timothy Boatman, Ronald Freeman, Dr. Mirosław Gronicki, Prof. Jerzy Rajski, and Dr. Wiesław Rozłucki.

Three permanent committees operate within the Supervisory Board composed, as at 31 December 2010, of:

Audit Committee
Timothy Boatman - Chairman,
Ronald Freeman,
Olivier Faure and Marie-Christine Lambert - members;

Remuneration Committee:
Ronald Freeman - Chairman,
Olivier Barberot, Wiesław Rozłucki and Olaf Swantee - members;

Strategy Committee
Olivier Barberot - Chairman, Jacques Champeaux, Olivier Faure, Mirosław Gronicki and Jerzy Rajski - members.

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.

The Supervisory Board fulfilled in 2010 duties resulting from the provisions of the Commercial Companies Code:

1 Evaluated the Management Board's report on TP SA operations and the financial statements for the financial year 2009 and the Management Board's recommendation for distribution of the Company's profit,
2 Evaluated the Management Board's report on TP SA Capital Group's operations and the consolidated financial statements for the financial year 2009,
3 Filed with the General Shareholders' Meeting reports presenting results of the above-mentioned evaluation.

The Supervisory Board took due care in order to assure that the Management Board's reports and the financial statements were in compliance with the law.

The Supervisory Board also executed its rights and obligations arising from the Company's Articles of Association and Best Practices, of which the following should be mentioned:

1 recommendations of motions addressed to the General Meeting, including motion for amendment of the Articles of Association,
2 selection of an independent auditor to audit the Company's financial statements,
3 preparing an opinion on TP and TP Group budget,
4 supervision of the realisation of TP Group's operating and financial objectives,
5 expressing an opinion on financial commitments exceeding the amount of 100 M,
6 concise assessment of TP Group situation.

report on supervisory board activities

Throughout 2010 the Supervisory Board and its permanent committees focused on the following issues:

a Group's financial results and performance compared to the budget,
b Group's strategy in an increasingly competitive market and continuing volatility of the financial markets,
c Execution of the Arrangement with the President of the UKE (Office of Electronic Communication),
d Refinancing of debt approaching maturity,
e TPSA versus DPTG litigation,
f Cost optimisation programme,
g Customer satisfaction.

The Supervisory Board met 4 times in 2010. The Board adopted 24 resolutions, of which 2 in writing (by correspondence).

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

Reports of the Audit, Remuneration and Strategy committees on theirs activities in 2010 are attached as Attachments 1, 2 and 3 respectively.

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.

Evaluation of the work of the Supervisory Board

Having in mind the above operations, the Supervisory Board is of the opinion that in 2010, showing due diligence, it exercised the supervision over all areas of the activities of Telekomunikacja Polska. Involvement of individual Supervisory Board members in supervision over a number of significant projects carried out by the Company enabled early consideration of risk and recommendations being made to 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. Particular members of the Management Board manage the areas of the Company's operations dedicated to each of them.

Composition of Management Board

Maciej Witucki
President of the Board, 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 6th November 2006.

Vincent Lobry
Vice President of the Board, Chief Marketing Officer
Vincent Lobry joined France Telecom in 1979 as a systems and network management engineer. After postings in Indonesia, the US, Spain and Italy, he moved into marketing, and was appointed B2C Marketing Director at FT France in 2006. He is a Knight of the Order of Merit and a graduate of École Polytechnique et École Nationale Supérieure des Télécommunication (Telecom ParisTech). Vincent Lobry joined TP Group's Management Board in September 2009.

Piotr Muszyński
Vice President of the Board, Chief Operating Officer
Piotr Muszyński graduated from the Faculty of Law and Administration at the University of Wroc¢aw, completed Postgraduate Study in Management at the Polish International Business School and the Advanced Management Programme organised by IESE Business School, University of Navarra. He started his career in 1990 in Eastern Europe Investment Ltd (EEI) as a Partner and Project Manager. From 1993 he was employed in REMA 1000 Poland Ltd as Managing Director and Member of the Management Board and from 1999 as President of the Management Board. In parallel in 1996-1998 he was a Member of the Management Board of Intersport Poland. He joined TP S.A. in 2001 as the Director of Customer Care Branch, then served as the Director of Sales and Services Division from 2005 onwards. Piotr Muszy¢ski joined TP Group's Management Board in September 2008.

Changes to the management board following the period under review in this report:

Roland Dubois resigned from the position of Chief Financial Officer in January 2011, and was replaced by:

Jacques de Galzain
Chief Financial Officer and Management Board Member
Jacques de Galzain graduated from Bordeaux University in 1981 and qualified as a Certified Accountant in 1989. After 9 years spent in audit firms, from 1991 to 2000 he worked for USINOR, where he held several accounting positions. In 2000 he moved to ALSTOM, initially as Deputy Chief Accounting Officer. Between 2001 and 2006 he undertook board-level financial roles at ALSTOM and AREVA. He joined France Telecom – Orange in March 2006 as Group Chief Accounting Officer, head of the financial information system. In December 2009 he joined Telekomunikacja Polska S.A. as Group Director in charge of Accounting and PTK Centertel Management Board Member in charge of Finance, and he was appointed Chief Financial Officer in January 2011.

At the same time, the Management Board announced the appointment of a new member:

Jacek Kowalski
Board Member in charge of Human Resources
Mr Kowalski graduated from the history faculty of Warsaw University before moving on to postgraduate studies in local government and non-governmental organizations management, which he completed in 1996. He worked for Infor Training and served as Director of the National In-Service Teacher Training Centre before joining TP Group in 2001, as Human Resources Manager for sales and marketing in PTK Centertel. From 2005 he was the Director of Employee Competence and Management Development for TP Group, and he joined the management board as member in charge of Human Resources in January 2011. Jacek Kowalski is a member of the Program Board of the Polish Human Resources Management Association.

corporate governance
internal control including risk management

A new TP Group Code of Ethics was adopted within the Company in 2008 which encompasses TP's relationship with customers, shareholders, employees, suppliers, competition and also with respect to the environment in which the TP Group operates. A warning system related to ethics and reporting of potential and actual fraud has been enhanced by the Group which is coordinated by the TP Group Ethics Committee. Training on ethics is provided to employees, which is confirmed by a personal certification. Formal channels for whistle blowing have been established, including reporting to the Chairman of the TP Audit Committee of the Supervisory Board, the Chairman of the TP Group Ethics Committee and the TP Group Internal Audit Director.

The system of internal control and risk management has been designed and implemented by the Management Board 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.

The key elements of such system include the following procedures:

1. An internal audit function, which reports directly to the President of the Management Board. The internal audit programme is annually reviewed by the Audit Committee which also analyses the Group'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 TP Group Internal Audit Director require, since 2005, an opinion of the Audit and Remuneration Committees.

2. The Group conducts ongoing assessments of the quality of risk management system and controls. As part of this process, a Risk Map which enables identification and classification of the Group's financial and non-financial risks is maintained.

3. Procedures were implemented in order to identify, report and monitor significant risks (i.e. legal, regulatory, environmental, financial reporting and operational) effectively on an ongoing basis. It provides a framework for the TP Group Internal Audit Department's ongoing risk-controlling activities.

In 2010, the Management Board again completed a comprehensive assessment of the Group's internal controls over financial reporting. Main deficiencies were identified and corrected 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 2010.

corporate governance disclosure

TP Group is diligent in its approach to reporting financial results and its ongoing communication with the Polish and international investment community, as well as fulfilling its disclosure obligations. The TP Group Disclosure Committee is chaired by the Chief Financial Officer. 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 2010, the Committee had 5 meetings to discuss the following:
Evaluation of the statutory financial reports (quarterly, half-year, full year);
Evaluation of quarterly investors' presentations.

In 2010 TP published 152 regulatory announcements (as well as quarterly, half-year statements of results and full year results) that were sent to the Warsaw and London Stock Exchanges. Moreover, in the field of investor relations activities, TP Group held over 250 meetings with investors and analysts.

Concise assessment of the Group's standing in 2010 prepared by TP S.A. Supervisory Board

This document is the Supervisory Board assessment of TP Group performance in 2010 in accordance with recommendation no. III.1.1 of the Code of Best Practices for WSE Listed Companies, introduced by the Warsaw Stock Exchange. The assessment is based on the 2010 Financial Results of the Group (the Company and its subsidiaries), as well as, on information obtained by the Supervisory Board during conducting of its statutory tasks.

Throughout 2010, the Supervisory Board focused on the following issues:

a Group's financial results and performance compared to the budget,
b Group's strategy in an increasingly competitive market and continuing volatility of the financial markets,
c Execution of the Arrangement with the President of the UKE (Office of Electronic Communication),
d Refinancing of debt approaching maturity,
e TPSA versus DPTG litigation,
f Cost optimisation programme,
g Customer satisfaction.

The Supervisory Board, through the work of its committees and all its members (including six independent), was actively engaged in the process of evaluation of the most important initiatives, having in mind the interest 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 function performed by the Management.

TP Group operational review

Throughout 2010, the Group focused most of its efforts on execution of the medium term action plan, developed in 2009. In particular, this included meaningful changes to the mobile commercial offers, namely the launch of the 'Animal tariffs' in April 2010. The modified marketing approach has proved to be a success, enabling the Group to grow its mobile customer base by 618,000 (or 4.5%) in 2010, which was a significant improvement as compared to 2009 and allowed Orange to outpace the remaining two big rivals and regain its market share leadership. Mobile broadband was also very popular in 2010, growing by 41%. In order to facilitate this trend further, TP made the necessary investments to prepare full roll-out (already begun in 2011) of the HSPA DC network, with speeds up to 42Mb/s. Further mobile network development could significantly benefit from a network sharing initiative started with Polska Telefonia Cyfrowa (PTC); in December 2010, TP Group and PTC have signed a letter of intent providing for future reciprocal use of each others' radio access networks and associated frequencies. In turn, upon implementation, this could increase TP Group's mobile coverage potential, whilst limiting investments needed to cope with increasing traffic.

In 2010, the Group also paid close attention to execution of the Arrangement with the President of UKE (signed in October 2009). Amongst other items, TP has gone to great efforts to ensure equal treatment of alternative operators and equivalence of access. The Group has also respected its investment commitments, as specified in the Arrangement, by investing into 416,000 broadband lines. On the other hand, TP benefitted from the Arrangement, as the 'retail minus' pricing model was replaced by the 'cost plus' methodology. As a consequence, following a successful 'margin squeeze test' conducted by UKE, TP S.A's retail broadband prices were detached from bitstream access fees. This allowed TP S.A. to re-price its retail broadband offering, bringing its prices back to competitive levels, while increased broadband investments made it possible for TP S.A. to promote speed options exceeding 6Mb/s. This brought positive results, as the adverse trend in Group's retail broadband base was reversed in quarter 4 and simultaneously TP was able to increase the share of higher speed options in its sales numbers.

TP Group's TV offering continued to be popular amongst consumers, which was reflected in a 46% growth of the number of its subscribers, which in 2010 reached 544,000. In October 2010, TP Group signed an important agreement relating to its TV activity – a framework agreement with Poland's leading media group – TVN Group, amongst others providing for reciprocal sales of both sides services, co-operation in the field of content acquisition. It is expected to result, in 2011, in a best broadband-and-TV bundle in Poland, giving both partners a competitive advantage over the key rivals.

corporate governance supervisory board assessment

TP Group financial overview

Operating in more stabile regulatory conditions and yet, in a very competitive markets, the Group's key strategic goals in 2010 were to:

- regain momentum on the mobile market and restore growth in the number of clients and revenue
- revamp the broadband offering, preparing grounds for a return to growth in this area in 2011,
- strengthen promotion of integrated services to increase ARPU and improve customer retention and customer satisfaction;
- further integrate fixed and mobile units and gain efficiency from integrated business processes;
- further rationalize Group's operations and processes in order to optimize operating expenses
- meet the investment targets in broadband, as committed in the Arrangement with UKE
- continue to optimize Capex spending based on sound investment criteria and without hampering growth;
- generate Net Free Cash Flow of at least PLN 2 billion
- continue Group's balance sheet optimization to improve return on assets base, including optimisation of the real estate portfolio;
- improve quality of service and shorten time to market for new products by continuing IT systems transformation and integration with CRM systems;
- deliver an attractive return to shareholders keeping in mind conditions set up in the shareholder remuneration policy;
- promote predictable regulations according to the European Regulatory Framework and consistent with comparable benchmarks;
- further enhance internal control and risk management measures.

In 2010, due to consistency in the deployment of the medium term action plan and to a stable regulatory environment, TP Group reported meaningful progress in each quarter of the year, both in the commercial field and the cost optimisation program. In turn, this allowed the Management to meet its outlook for revenue decline, EBITDA margin and Capex as percentage of revenue. TP Group has also delivered on the Management's Cash Flow guidance, by reporting Net Free Cash Flow for 2010 of PLN 2.45bn, despite capex ramp-up linked to the Arrangement with the UKE.

Facing a partial award issued by the Arbitration Tribunal in Vienna, in the case TPSA vs. DPTG (in September 2010), amounting to PLN 1,568mn for Phase I of the dispute, as well as the possible risk with regards to Phase 2, TP Group's Management raised its provision for this litigation up to approximately PLN 2.2bn, whilst pursuing legal actions in Austria and Poland aimed at challenging the award and its enforceability. The Supervisory Board supports the Management in its actions taken both with regards to the provision and the dispute, as more fully described in the notes to the financial statements.

TP Group has followed on the Supervisory Board recommendations and continued its progress in terms of the financing activity. Throughout 2010, the Company has reduced its net debt by roughly PLN 565 million, maintaining its net gearing at ~21%. It continued to pay focus to its gross debt structure, keeping a high share of bonds (at ~66%). Coupled with a strong liquidity position and an effective hedging policy, this enabled TP to maintain its credit rating of A3/ BBB+ with a stable outlook.

TP Management Board has proposed an ordinary dividend of PLN 2,003 million, an equivalent of PLN 1.5 per share, payable in cash in the first half of 2011. That proposal obtained a positive opinion of the Supervisory Board and is subject to approval by the General Assembly of TP shareholders.

Conclusions and 2011 recommendations

Despite intensive competition across all segments as well as regulatory pressure, TP Group has delivered satisfactory results in 2010. The Supervisory Board believes TP's Management Board has made the appropriate efforts to reach the 2010 objectives. Moreover, the Group, with its integrated offers and the new commercial and investment program for broadband, is in a strong position to continue creating and exploiting the new opportunities on the Polish market.

The Supervisory Board's opinion is that in 2011 the Group should focus its activities to continue to implement the medium term action plan and also to:

- Monitor business performance closely so as to be able to react quickly to unfavourable trading conditions caused by the continued volatility of the financial markets;
- Strive for leadership in value on fixed voice, mobile and broadband markets;
- Increase customer satisfaction and loyalty, also by implementing the newly launched customer excellence program;
- Monitor TP Group EBITDA margin, with particular reference to the mobile segment
- Monitor capital expenditure, with a specific focus on the spend and efficiency of the broadband investment program, which is executed in connection with the Arrangement with the Regulator
- Mitigate foreign exchange effect on commercial expenses, financial costs and capital expenditure;
- Further optimize operating cost base;
- Maintain financial stability;
- Generate Net Free Cash Flow of at least PLN 2.4billion;
- Successfully implement the Arrangement with the Regulator
- Sustain its actions in the dispute with DPTG
- Deliver an attractive return to shareholders keeping in mind conditions set up in the shareholder remuneration policy;
- Further enhance internal control and risk management measures.

supervisory board assessment

Assessment of the Group's internal control including 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.

The key elements of this system of internal control, including risk management were presented in the Management Board's Report on the Activity of Telekomunikacja Polska Group for 2010, published on February 23rd 2011.

In 2010, the Group again completed a comprehensive assessment of its processes of internal control over financial reporting within the framework of Sarbanes-Oxley Program of France Telecom Group. Main deficiencies both in design and in effectiveness of the internal control have been either identified and corrected, 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 2010. Continued efforts by Management in this regard are also needed in 2011.

The external auditors report to the Management Board and also to the Audit Committee on control deficiencies which they identified during their financial statements audit. Their recommendations are being implemented.

Activity of TP Group Audit Committee in 2010

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

The task of the Committee is to advise the Supervisory Board on the proper implementation of budgetary and financial reporting and internal control (including risk management) principles in the TP Group and to liaise with the auditors of TP Group.

Composition

In 2010, the Audit Committee was composed of the following persons:

Chairman:
Mr. Timothy Boatman
("Independent Director")

Members:
Ms. Marie Christine-Lambert
Mr. Ronald Freeman
("Independent Director")
Mr. Olivier Faure

The Secretary of the Committee was Jerzy Klonecki.

Functions of the Committee

The key functions of the Audit Committee include:

1. Monitoring the integrity of the financial information provided by the Company in particular by reviewing:
   a The relevance and consistency of the accounting methods used by the Company and the TP Capital Group, including the criteria for the consolidation of the financial results;
   b Any changes to accounting standards, policies and practices;
   c Major areas of financial reporting subject to judgment;
   d Significant adjustments arising from the audit;
   e Statements on going concern;
   f Compliance with the accounting regulations;
2. Review at least annually the Group's system of internal control and risk management systems with a view to ensuring that the main risks (including those related to compliance with existing legislation and regulations) are properly identified, managed and disclosed;
3. Annual review of the internal audit program, including the review of independence of the internal audit function, and coordination between the internal and external auditors;
4. Analysis of reports of the Company's internal audit department and major findings of any other internal investigations and responses of the Management Board to them;
5. Make recommendations in relation to the selection and remuneration of the Director of the Internal Audit department and on such department's budget;
6. Review and providing an opinion to the TP Management Board on transactions with related parties;
7. Monitoring the independence and objectivity 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, with particular attention being paid to remuneration for additional services;
8. Discussion with the Company's external auditors before the start of each annual audit on the nature and scope of the audit and monitoring the auditors' work;
9. Review the issues giving rise to the resignation of the external auditor;
10. Discussion (in or without the presence of the Company Management Board) of any problems or reservations, resulting from the financial statements audit;
11. Review the effectiveness of the external audit process, and the responsiveness of the Management Board to recommendations made by the external auditor;
12. Consideration of any other matter noted by the Audit Committee or the Supervisory Board;
13. Regularly informing the Supervisory Board about all important issues within the Committee scope of activity;
14. Providing the Supervisory Board with its annual report on the Audit Committee's activity and results.

Report on the activity of the TP Group Audit Committee in 2010

The TP Group Audit Committee held 17 meetings in 2010, out of which 11 were regular meetings and 6 dedicated ad-hoc meetings, and in particular performed the following:

1. Reviewed the Company's and Group's published financial statements, notably the relevance and consistency of the accounting methods used by the Company and the TP Capital Group;
2. Reviewed the Group's system of internal control (including risk management) as reported by the Management Board and, in particular, the way risks were identified, managed and disclosed by the Management. The Audit Committee received reports from Management on action plans in response to comments on internal controls from the internal and external auditors;
3. Reviewed the annual plan of the Internal Audit Department, its budget and progress reports, as well as monitored the responsiveness of management to internal audit findings and recommendations. The Audit Committee was provided with a report regarding the renewal in 2009 of the certification of Internal Audit activities by Institut Français de l'Audit et du Contrôle Internes (IFACI). The Audit Committee reviewed also the independence of the Internal Audit Department.
4. Made recommendation to the Supervisory Board on the external auditor, its remuneration and terms of engagement. In accordance with the Code of the Best Practices for companies listed on the Warsaw Stock Exchange, the Audit Committee recommended to the Supervisory Board the appointment of Deloitte Audit Sp. z o.o. to the audit of TP S.A. and Telekomunikacja Polska Group for the financial year 2010 and to review half-yearly financial statements for the period of six months ended June 30, 2010.
5. Kept under review the scope and the results of the external audit, independence and objectivity of the auditors and reported its conclusions to the Supervisory Board; monitored the Company's responsiveness to the recommendations from the external auditor made in its management letter;
6. Reviewed the development and operation of the Group's Ethics Committee activity, anti-fraud and whistle-blowing programs managed by the Management Board; monitored results of investigations initiated by whistle-blowing;
7. Reviewed the Group's 2010 budget and addressed recommendations on it to the Supervisory Board;
8. Reviewed the 2010 dividend distribution policy proposed by the Management;
9. Issued opinions on other matters referred to the Committee by the Supervisory Board and/or the Management Board including M&A transactions, the medium and long term financing of the Company and its subsidiaries.

In the year under review, the Audit Committee, especially its two independent members, reviewed and gave opinion to the Management Board of TP on transactions with related parties and received reports on them from the Company's Internal Audit department.

The Audit Committee took note of the Recommendations on the work of the Audit Committee issued in November 2010 by the Office of The Financial Supervision Authority in Poland and in the course of 2011 will be considering appropriate changes, if necessary.

Timothy Boatman
Chairman of the Audit Committee of the Supervisory Board

24 March 2011

Report on the activity of the Remuneration Committee of the Supervisory Board of Telekomunikacja Polska S.A. in 2010

The Remuneration Committee was established by virtue of the Resolution of the TP Supervisory Board no. 385/04 dated 16 June 2004 regarding TP S.A. Supervisory Board's Remuneration Committee establishment as consultative body acting under the Supervisory Board.

The task of the Committee is to advise the Supervisory and Management Board on general remuneration policy of TP Group and to make recommendations on appointment, performance objectives, remuneration procedures and amounts to the Supervisory and Management Board.

Composition

In 2010, the Remuneration Committee was composed of the following persons:

until April 22, 2010

Chairman:
Ronald Freeman ("Independent Director")

Members:
Olivier Barberot
Jacques Champeaux
Wiesław Rozłucki ("Independent Director")

from April 23, 2010

Chairman:
Ronald Freeman ("Independent Director")

Members:
Olivier Barberot
Wiesław Rozłucki ("Independent Director")
Olaf Swantee

The Secretary of the Committee was Jacek Kowalski, TP Group Executive Director in charge of Human Resources (from January 27, 2011 TP Management Board Member in charge of Human Resources).

Activity in 2010

The Remuneration Committee held four meetings in 2010 and in particular developed recommendations for Supervisory Board consideration focused on the following remuneration-related issues:

1. Benefits under the employment contract for the Management Board Members.
2. Discussion of CEO proposal on new solution of Management Board Members motivational system - to be decided on March 24, 2011.
3. Assessment of performance relative to objectives and decision on the bonus percentage for Management Board Members for H2 2009 and H1 2010.
4. Validation of objectives for Management Board Members for 2010 and H1 2011.

Ronald Freeman
Chairman of TP S.A. Supervisory Board's Remuneration Committee

24 March 2011

Report from the activities of the Strategy Committee of the Supervisory Board of Telekomunikacja Polska S.A.

Activies of the Strategy Committee

Major goals for the Strategy Committee is to give necessary support and advice for the Management Board in the area of TP Group strategic plans and initiatives of strategic importance.

Strategy Committee members in 2010

Chairman of the Strategy Committee:
Olivier Barberot

Other members of the Strategy Committee:
Jacques Champeaux
Olivier Faure
Mirosław Gronicki
Jerzy Rajski

Vincent Lobry was Secretary of the Strategy Committee in 2010.

Activities in 2010:

In 2010 the activities of the Strategy Committee of TP Group Supervisory Board concentrated on the Action Plan of TP Group for 2010-11.

Strategy Committee also widely discussed the key drivers for shareholders remuneration, strategy for TP Group subsidiaries, TP contribution to five year strategic plan of France Telecom, strategic implications of Orange Customer Services as well as long-term content agreement with TVN.

In all these areas the members of TP Group Management Board actively participated.

There were three Strategy Committee meetings in 2010 during which other Supervisory Board Members also participated: Chairman of the Supervisory Board, prof. Andrzej K. Koźmiński, Chairman of the Audit Committee, Timothy Boatman and Chairman of the Remuneration Committee, Ronald Freeman.

Olivier Barberot
Chairman of the Strategy Committee

24 March 2011

Consolidated income statement

(in PLN millions, except for share data)	Note	12 months ended 31 December 2010 (audited)	12 months ended 31 December 2009 (see Note 3.4, audited)
Revenue	5	**15,715**	**16,560**
External purchases	6	(7,174)	(7,438)
Labour expenses	6	(2,218)	(2,352)
Other operating expense	6	(769)	(671)
Other operating income	6	193	169
Restructuring costs	7	(34)	(23)
Gains on disposal of assets	8	59	35
Dispute with DPTG	31.d	(1,061)	–
Depreciation and amortization	14, 15	(3,792)	(4,150)
Impairment of non-current assets	9	(11)	(33)
Operating income		**908**	**2,097**
Interest income	10	85	37
Interest expense and other financial charges	10	(484)	(400)
Foreign exchange gains/(losses)	10	23	(30)
Discounting expense	10	(83)	(106)
Finance costs, net		**(459)**	**(499)**
Income tax	11	(341)	(315)
Consolidated net income		**108**	**1,283**
Net income attributable to owners of TP S.A.		107	1,281
Net income attributable to non-controlling interests		1	2
Earnings per share (in PLN) (basic and diluted)	3.4	**0.08**	**0.96**
Weighted average number of shares (in millions) (basic and diluted)	3.4	1,336	1,336

Consolidated statement of comprehensive income

(in PLN millions)	Note	12 months ended 31 December 2010 (audited)	12 months ended 31 December 2009 (see Note 3.4, audited)
Consolidated net income		**108**	**1,283**
Gains/(losses) on cash flow hedges	12	(18)	50
Actuarial losses on post-employment benefits	12	(16)	(14)
Income tax relating to components of other comprehensive income	12	7	(7)
Translation adjustment		–	2
Other comprehensive income/(loss), net of tax		**(27)**	**31**
Total comprehensive income		**81**	**1,314**
Total comprehensive income attributable to owners of TP S.A.		80	1,312
Total comprehensive income attributable to non-controlling interests		1	2

Consolidated balance sheet

(in PLN millions)	Note	At 31 December 2010 (audited)	At 31 December 2009 (see Note 3.4, audited)
Assets			
Goodwill	13	4,016	4,016
Other intangible assets	14	2,861	2,767
Property, plant and equipment	15	16,500	17,743
Investments in associates		3	3
Financial assets available for sale	16	4	4
Loans and receivables excluding trade receivables	16	22	11
Financial assets at fair value through profit or loss	16	52	62
Hedging derivatives	21	50	55
Deferred tax assets	11	603	515
Total non-current assets		**24,111**	**25,176**
Inventories		272	229
Trade receivables	17	1,637	1,475
Loans and receivables excluding trade receivables	16	10	13
Financial assets at fair value through profit or loss	16	28	9
Hedging derivatives	21	1	2
Income tax assets		7	24
Other assets	17	266	119
Prepaid expenses	17	94	100
Cash and cash equivalents	18	2,447	2,218
Total current assets		**4,762**	**4,189**
Total assets		**28,873**	**29,365**
Equity and liabilities			
Share capital	29	4,007	4,007
Share premium		832	832
Other reserves	12, 26	27	50
Translation adjustment		(6)	(6)
Retained earnings		9,760	11,656
Equity attributable to owners of TP S.A.		**14,620**	**16,539**
Non-controlling interests		14	14
Total equity		**14,634**	**16,553**

Consolidated balance sheet continued

(in PLN millions)	Note	At 31 December 2010 (audited)	At 31 December 2009 (see Note 3.4, audited)
Financial liabilities at amortised cost excluding trade payables	19, 20	4,456	6,033
Financial liabilities at fair value through profit or loss	21	90	61
Hedging derivatives	21	191	148
Trade payables	28	751	790
Employee benefits	25	342	283
Provisions	27	189	215
Deferred tax liabilities	11	9	7
Deferred income	28	66	53
Total non-current liabilities		**6,094**	**7,590**
Financial liabilities at amortised cost excluding trade payables	19, 20	1,547	375
Financial liabilities at fair value through profit or loss	21	55	89
Hedging derivatives	21	54	2
Trade payables	28	3,156	2,477
Employee benefits	25	266	302
Provisions	27	2,242	1,208
Income tax payable		72	2
Other liabilities	28	220	184
Deferred income	28	533	583
Total current liabilities		**8,145**	**5,222**
Total equity and liabilities		**28,873**	**29,365**

Consolidated statement of changes in equity

(in PLN millions)	Number of shares in issue (not in millions)	Share capital	Share premium	Treasury shares	Other reserves: Hedging instruments	Other reserves: Actuarial losses on post-employment benefits	Other reserves: Deferred taxes	Other reserves: Share-based payments	Translation adjustments	Retained earnings	Total	Non-controlling interest	Total equity
Balance at 1 January 2009 (audited)	**1,335,649,021**	**4,106**	**832**	**(704)**	**(30)**	**–**	**6**	**32**	**(8)**	**12,983**	**17,217**	**13**	**17,230**
Effect of change in accounting policy for post-employment benefits (see Note 3.4)		–	–	–	–	(36)	6	–	–	–	(30)	–	(30)
Balance at 1 January 2009 after change in accounting policy (audited)	**1,335,649,021**	**4,106**	**832**	**(704)**	**(30)**	**(36)**	**12**	**32**	**(8)**	**12,983**	**17,187**	**13**	**17,200**
Total comprehensive income for the 12 months ended 31 December 2009		–	–	–	50	(14)	(7)	–	2	1,281	1,312	2	1,314
Share-based payments		–	–	–	–	–	–	43	–	–	43	–	43
Cancellation of treasury shares	–	(99)	–	704	–	–	–	–	–	(605)	–	–	–
Dividends		–	–	–	–	–	–	–	–	(2,003)	(2,003)	(1)	(2,004)
Balance at 31 December 2009 (audited)	**1,335,649,021**	**4,007**	**832**	**–**	**20**	**(50)**	**5**	**75**	**(6)**	**11,656**	**16,539**	**14**	**16,553**
Total comprehensive income for the 12 months ended 31 December 2010		–	–	–	(18)	(16)	7	–	–	107	80	1	81
Share-based payments		–	–	–	–	–	–	4	–	–	4	–	4
Dividends		–	–	–	–	–	–	–	–	(2,003)	(2,003)	(1)	(2,004)
Balance at 31 December 2010 (audited)	**1,335,649,021**	**4,007**	**832**	**–**	**2**	**(66)**	**12**	**79**	**(6)**	**9,760**	**14,620**	**14**	**14,634**

Consolidated statement of cash flows

(in PLN millions)	Note	12 months ended 31 December 2010 (audited)	12 months ended 31 December 2009 (see Note 3.4, audited)
Operating activities			
Consolidated net income		108	1,283
Adjustments to reconcile net income to funds generated from operations			
Depreciation and amortization	14, 15	3,792	4,150
Impairment of non-current assets	9	11	33
Gains on disposal of assets	8	(59)	(35)
Change in provisions		1,088	(157)
Income tax	11	341	315
Finance costs, net excluding realised exchange rate effect on cash and cash equivalents		489	511
Operational foreign exchange and derivatives (gains)/losses, net		8	(6)
Share-based payments	6, 26	4	43
Change in working capital (trade)			
Decrease/(increase) in inventories		(43)	70
Decrease/(increase) in trade receivables		(214)	361
Increase/(decrease) in trade payables		1	(474)
Change in working capital (non-trade)			
Decrease/(increase) in prepaid expenses and other receivables		(116)	(8)
Increase/(decrease) in accrued expenses, other payables and deferred income		(12)	16
Interest received		85	37
Interest and interest rate effect on derivatives paid, net		(566)	(421)
Exchange rate effect on derivatives, net		(50)	125
Income tax paid		(337)	(302)
Net cash provided by operating activities		**4,530**	**5,541**
Investing activities			
Purchases of property, plant and equipment and intangible assets	14, 15	(2,713)	(2,185)
Increase/(decrease) in amounts due to fixed assets suppliers		637	(123)
Proceeds from sale of property, plant and equipment and intangible assets		85	33
Proceeds from sale of subsidiaries, net of cash	4	–	16
Cash paid for acquisition of subsidiaries, net of cash	4	–	(25)
Decrease/(increase) in marketable securities and other financial assets	16	(4)	10
Exchange rate effect on derivatives, net		(20)	(7)
Net cash used in investing activities		**(2,015)**	**(2,281)**

Consolidated statement of cash flows continued

(in PLN millions)	Note	12 months ended 31 December 2010 (audited)	12 months ended 31 December 2009 (see Note 3.4, audited)
Financing activities			
Issuance of bonds	19, 20	–	3,101
Repayment of long-term debt	19, 20	(230)	(1,936)
Decrease in bank overdrafts and other short-term borrowings	19, 20	(2)	(1,800)
Purchase of treasury shares including transaction cost	29	–	(4)
Dividends paid	29	(2,004)	(2,004)
Exchange rate effect on derivatives, net		(50)	(37)
Net cash used in financing activities		**(2,286)**	**(2,680)**
Net change in cash and cash equivalents		229	580
Effect of changes in exchange rates on cash and cash equivalents		–	(2)
Cash and cash equivalents at the beginning of the period		2,218	1,640
Cash and cash equivalents at the end of the period		**2,447**	**2,218**

Notes to the consolidated financial statements

Segment information

The Telekomunikacja Polska Group has two reportable operating segments:

- Fixed line segment which includes entities offering predominantly telecom services based on fixed line technology and other companies offering services predominantly for those entities, and
- Mobile segment which includes entities offering predominantly telecom services based on mobile technology and other companies offering services predominantly for those entities.

Margin earned by Orange Customer Service Sp. z o.o. on intragroup transactions is eliminated from fixed and mobile segment data.

Segment performance is evaluated based on revenue, EBITDA, EBIT and capital expenditures. EBITDA corresponds to operating income before depreciation and amortization expense and reversal of impairment/impairment of goodwill and other non-current assets. EBIT corresponds to operating income.

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

Mobile telecommunications services are provided by Polska Telefonia Komórkowa – Centertel Sp. z o.o., a provider of DCS 1800, GSM 900 and UMTS mobile telecommunications and services based on the CDMA technology.

The Group's operational activities are conducted in one geographical area, the territory of the Republic of Poland.

The accounting policies are uniform for all segments. Transactions between segments are eliminated on consolidation.

Both segments have dispersed customer base – no single customer generates more than 10% of segment revenue.

Financing and income tax are managed on a group basis and are not allocated to operating segments.

Basic financial data on the business segments is presented below:

(in PLN millions)	Fixed line telecommunication	Mobile telecommunications	Eliminations and unallocated items	Consolidated
	12 months ended 31 December 2010			
Revenue	9,028	7,711	(1,024)	15,715
External	8,283	7,432	–	15,715
Inter-segment	745	279	(1,024)	–
External purchases	(3,418)	(4,981)	1,225	(7,174)
Labour expenses	(1,927)	(291)	–	(2,218)
Other operating expense	(491)	(280)	2	(769)
Other operating income	295	101	(203)	193
Restructuring costs	(34)	–	–	(34)
Gains on disposal of assets	59	–	–	59
Dispute with DPTG	(1,061)	–	–	(1,061)
EBITDA	**2,451**	**2,260**	**–**	**4,711**
Depreciation and amortization	(2,476)	(1,316)	–	(3,792)
Impairment of non-current assets	(11)	–	–	(11)
EBIT	**36**	**944**	**–**	**908**
Capital expenditures	2,007	709	–	2,716
– financed through own resources	2,004	709	–	2,713
– financed through finance leases	3	–	–	3
	At 31 December 2010			
Segment assets	15,766	10,202	(322)	25,646
Investments in associates	3	–	–	3
Unallocated assets	–	–	3,224	3,224
Total assets				28,873
Segment liabilities	5,348	2,739	(322)	7,765
Unallocated liabilities	–	–	6,474	6,474
Total liabilities				14,239
Equity	–	–	14,634	14,634
Total equity and liabilities				28,873

Notes to the consolidated financial statements continued

Segment information (continued)

(in PLN millions)	Fixed line telecommunications	Mobile telecommunications	Eliminations and unallocated items	Consolidated
	12 months ended 31 December 2009 (see Note 3.4)			
Revenue	9,863	7,745	(1,048)	16,560
External	9,121	7,439	–	16,560
Inter-segment	742	306	(1,048)	–
External purchases	(3,586)	(5,028)	1,176	(7,438)
Labour expenses	(2,018)	(334)	–	(2,352)
Other operating expense	(432)	(240)	1	(671)
Other operating income	224	74	(129)	169
Restructuring costs	(23)	–	–	(23)
Gains on disposal of assets	35	–	–	35
EBITDA	**4,063**	**2,217**	**–**	**6,280**
Depreciation and amortization	(2,727)	(1,423)	–	(4,150)
Impairment of non-current assets	(32)	(1)	–	(33)
EBIT	**1,304**	**793**	**–**	**2,097**
Capital expenditures	1,419	788	–	2,207
– financed through own resources	1,397	788	–	2,185
– financed through finance leases	22	–	–	22
	At 31 December 2009 (see Note 3.4)			
Segment assets	16,029	10,650	(230)	26,449
Investments in associates	3	–	–	3
Unallocated assets	–	–	2,913	2,913
Total assets				29,365
Segment liabilities	3,584	2,741	(230)	6,095
Unallocated liabilities	–	–	6,717	6,717
Total liabilities				12,812
Equity	–	–	16,553	16,553
Total equity and liabilities				29,365

Notes to the consolidated financial statements continued

1. Corporate information

1.1. The Telekomunikacja Polska Group

Telekomunikacja Polska S.A. ("Telekomunikacja Polska" or "the Company" or "TP S.A."), 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 telecommunications 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, TV and Voice over Internet Protocol ("VoIP"). Telekomunikacja Polska provides telecommunications services on the basis of entry number 1 in the register of telecommunications companies maintained by the President of Office of Electronic Communication ("UKE"). Through its subsidiary, Polska Telefonia Komórkowa-Centertel Sp. z o.o. ("PTK-Centertel"), the Group is one of Poland's major DCS 1800 and GSM 900 mobile telecommunications providers. PTK-Centertel also provides third generation UMTS services and services based on the CDMA technology. In addition, the Group provides leased lines, radio-communications and other telecommunications value added services, sells telecommunications equipment, electronic phone cards and provides data transmission, multimedia services and various Internet services.

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

The Group's operations are subject to regulatory controls of UKE, the government telecommunications market regulator. Under the Telecommunication Act, UKE can impose certain obligations on telecommunications companies that have a significant market power ("SMP"): Telekomunikacja Polska S.A., PTK-Centertel Sp. z o.o., TP EmiTel Sp. z o.o. ("TP EmiTel") are deemed to be SMPs on certain markets.

Notes to the consolidated financial statements continued

1. Corporate information (continued)

1.2. Entities of the Group

The Group comprises Telekomunikacja Polska and the following subsidiaries:

Entity	Location	Scope of activities	Share capital owned by the Group 31 December 2010	Share capital owned by the Group 31 December 2009
PTK-Centertel Sp. z o.o.	Warsaw, Poland|	Mobile telephony services, construction and operation of mobile telecommunications networks.	100.00%	100.00%
TP EmiTel Sp. z o.o.	Kraków, Poland	TV and radio signals broadcasting, construction, lease and maintenance of technical infrastructure.	100.00%	100.00%
Wirtualna Polska S.A.	Gdańsk, Poland	Internet portal and related services including internet advertising.	100.00%	100.00%
OPCO Sp. z o.o.	Warsaw, Poland	Facilities management and maintenance.	100.00%	100.00%
Otwarty Rynek Elektroniczny S.A.	Warsaw, Poland	Provision of complex procurement solutions, including advisory, implementation and operation of e-commerce platform and IT systems, hosting.	100.00%	100.00%
TP Edukacja i Wypoczynek Sp. z o.o.	Warsaw, Poland	Hotel services, training and conference facilities.	100.00%	100.00%
TP Invest Sp. z o.o.	Warsaw, Poland	Services for Group entities, holding management.	100.00%	100.00%
– Telefon 2000 Sp. z o.o.	Warsaw, Poland	No operational activity.	100.00%	100.00%
– TP TelTech Sp. z o.o.	Łódź, Poland	Monitoring of alarm signals, servicing telecommunications networks, design and development of telecommunications systems.	100.00%	100.00%
– Telefony Podlaskie S.A.	Sokołów Podlaski, Poland	Local provider of fixed-line, internet and cable TV services.	55.11%	55.11%
– Contact Center Sp. z o.o.	Warsaw, Poland	Call-center services and telemarketing.	100.00%	100.00%
– Orange Customer Service Sp. z o.o.(1)	Warsaw, Poland	Post-sale services for TP S.A. and PTK-Centertel customers.	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.	99.99%	99.96%
Pracownicze Towarzystwo Emerytalne Telekomunikacji Polskiej S.A.	Warsaw, Poland	Management of employee pension fund.	100.00%	100.00%
Fundacja Orange	Warsaw, Poland	Charity foundation.	100.00%	100.00%
PayTel S.A.	Warsaw, Poland	E-commerce and electronic services, including GSM prepaid services, bill charging and processing of electronic financial transactions.	100.00%	100.00%
Ramsat S.A.	Modlnica, Poland	Distributor of PTK Centertel and TP S.A. products on mass and business market.	100.00%	100.00%
– Prado Sp. z o.o.(2)	Kraków, Poland	As at 31 December 2010 the entity no longer exists.	–	100.00%

(1) in September 2010 the previous name of Virgo Sp. z o.o. was changed to Orange Customer Service Sp. z o.o.
(2) in January 2010 the entity merged with Ramsat S.A.

In the 12 months ended 31 December 2010 and 2009, the voting power held by the Group was equal to the Group's interest in the share capital of all of its subsidiaries. Significant acquisitions or divestitures are described in Note 4.

The Group owns shareholdings in the following associates:

As at 31 December 2010 and 2009, TP Invest Sp. z o.o. held a 25% interest in Telefony Opalenickie S.A., a local fixed line telecommunications operator.

As at 31 December 2010, Wirtualna Polska S.A. held a 25% interest (20% as at 31 December 2009) in Polskie Badania Internetu Sp. z o.o. which conducts studies on Internet use in Poland.

As at 31 December 2010 and 2009, PTK Centertel held a 25% interest in 4MNO Sp. z o.o. (previously Mobile TV Sp. z o.o.).

The investments in those associates are accounted for using the equity method.

Notes to the consolidated financial statements continued

1. Corporate information (continued)

1.3. The Management Board and the Supervisory Board of the Company

The Management Board of the Company at the date of the authorisation of these Consolidated Financial Statements was as follows:

Maciej Witucki – President of the Management Board, Chief Executive Officer,
Vincent Lobry – Vice President in charge of Marketing and Strategy,
Piotr Muszyński – Vice President in charge of Operations,
Jacques de Galzain – Board Member, Chief Financial Officer,
Jacek Kowalski – Board Member in charge of Human Resources.

The Supervisory Board of the Company at the date of the authorisation of these Consolidated Financial Statements was as follows:

Prof. Andrzej K. Koźmiński – Chairman of the Supervisory Board, Independent Member of the Supervisory Board,
Olivier Barberot – Deputy Chairman of the Supervisory Board,
Olivier Faure – Secretary of the Supervisory Board,
Timothy Boatman – Independent Member of the Supervisory Board,
Thierry Bonhomme – Member of the Supervisory Board,
Jacques Champeaux – Member of the Supervisory Board,
Ronald Freeman – Independent Member of the Supervisory Board,
Dr. Mirosław Gronicki – Independent Member of the Supervisory Board,
Marie-Christine Lambert – Member of the Supervisory Board,
Prof. Jerzy Rajski – Independent Member of the Supervisory Board,
Gerard Ries – Member of the Supervisory Board,
Dr. Wiesław Rozłucki – Independent Member of the Supervisory Board,
Olaf Swantee – Member of the Supervisory Board.

The following changes occurred in the Management Board of the Company in the year ended 31 December 2010 and in the year 2011 until the date of the authorisation of these Consolidated Financial Statements:

On 14 January 2011, Mr Roland Dubois resigned from the position of Management Board Member of TP S.A. in charge of Finance – Chief Financial Officer. As of 17 January 2011, his duties were passed on to Mr Jacques de Galzain.

On 27 January 2011, the Supervisory Board of the Company appointed Mr Jacques de Galzain and Mr Jacek Kowalski as Members of the Management Board of TP S.A. The Supervisory Board also appointed Mr Piotr Muszyński for the subsequent term of office.

The following changes occurred in the Supervisory Board of the Company in the year ended 31 December 2010 and in the year 2011 until the date of the authorisation of these Consolidated Financial Statements:

Mr Jacek Kałłaur resigned from the Management Board of TP S.A. and his mandate expired on 4 November 2009.

The following changes occurred in the Supervisory Board of the Company in the year ended 31 December 2009:

Mr Vivek Badrinath resigned from the Supervisory Board of TP S.A. with effect on 22 April 2010.

On 23 April 2010, the Annual General Meeting of Shareholders appointed Mr Thierry Bonhomme and Mr Olaf Swantee to the Supervisory Board of TP S.A. and renewed mandates of the following persons, whose term of office expired as of the day of this General Meeting: Mr Jacques Champeaux, Mr Ronald Freeman and Mr Mirosław Gronicki. On the same day, the term of office in the Supervisory Board of TP S.A. expired for Mr Antonio Anguita.

Mr Raoul Roverato resigned from the Supervisory Board of TP S.A. with the effect from 26 January 2011. On 27 January 2011, the Supervisory Board co-opted Mr Gerard Ries as a Member of the Supervisory Board of TP S.A.

2.Statement of compliance and basis for preparation

These Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") adopted for use by the European Union. IFRSs 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 2009 have been compiled using the same basis of preparation.

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 debt that is hedged against exposure to changes in fair value.

The financial data of all entities constituting the Group included in these Consolidated Financial Statements were prepared using uniform group accounting policies.

These Consolidated Financial Statements are prepared in millions of Polish zloty ("PLN") and were authorized for issuance by the Management Board on 22 February 2011.

The principles applied to prepare financial data relating to the year ended 31 December 2010 are described in Note 3 and are based on:

– all standards and interpretations endorsed by the European Union and applicable to the reporting period beginning 1 January 2010;
– IFRSs and related interpretations adopted for use by the European Union whose application will be compulsory for periods beginning after 1 January 2010 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.

Notes to the consolidated financial statements continued

2.Statement of compliance and basis for preparation (continued)

Use of estimates

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 2010 may be subsequently changed. The main estimates made are described in the following notes:

	Note	Type of information disclosed
3.5.7, 3.5.11, 9	Impairment of cash generating units and individual tangible and intangible assets	Key assumptions used to determine recoverable amounts: impairment indicators, models, discount rates, growth rates.
3.5.12, 16.2	Impairment of loans and receivables	Methodology used to determine recoverable amounts.
3.5.14, 11	Income tax	Assumptions used for recognition of deferred tax assets.
3.5.16, 25	Employee benefits	Discount rates, salary increases, expected average remaining working lives.
3.5.12, 21, 24	Fair value of derivatives and other financial instruments	Model and assumptions underlying the measurement of fair values.
3.5.15, 27, 31	Provisions	Provisions for termination benefits and restructurings: discount rates and other assumptions. The assumptions underlying the measurement of provisions for claims and litigation.
3.5.8, 3.5.9	Useful lives of tangible and intangible assets	The useful lives and the amortization method.
3.5.17, 26	Share-based payments	Model and key assumptions used to determine fair value of equity instruments granted: exercise price, historical volatility, risk-free interest rate, expected dividend yield, etc.
27	Dismantling costs	The assumptions underlying the measurement of provision for the estimated costs for dismantling and removing the asset and restoring the site on which it is located.
3.5.3, 5	Revenue	Allocation of revenue between each separable component of a packaged offer based on its relative fair value. Straight-line recognition of revenue relating to service access fees. Reporting revenue on a net versus gross basis (analysis of Group's involvement acting as principal versus agent).
3.5.13	Allowance for slow moving and obsolete inventories	Methodology used to determine net realisable value of inventories.

Use of judgements

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 main judgments made as at 31 December 2010 relate to provisions for claims and litigation and contingent liabilities. Details are described in Note 31.

Notes to the consolidated financial statements continued

3. Significant accounting policies

This note describes the accounting principles applied to prepare the consolidated financial statements for the year ended 31 December 2010.

3.1. Application of new standards, amendments and interpretations

Adoption of standards, amendments to standards and interpretations which are compulsory as at January 1, 2010
The following standards or amendments to standards and interpretations (already endorsed or in the process of being endorsed by the European Union) have become effective and are compulsory as at January 1, 2010:

– Revised IFRS 3 "Business Combinations",
– Revised IAS 27 "Consolidated and Separate Financial Statements",
– Amendments to IAS 39 "Financial Instruments: Eligible Hedged Items",
– IFRIC 17 "Distribution of Non-cash Assets to Owners",
– Improvements to International Financial Reporting Standards – a collection of amendments to IFRSs, the amendments are effective, in most cases, for annual periods beginning on or after 1 January 2010,
– Amendments to IFRS 2 "Share-based Payment" - Group cash-settled share-based payment transactions.

Except for revised IFRS 3 and revised IAS 27, the adoption of the standards and interpretations presented above did not result in any significant changes to the Group's accounting policies and to the presentation of the financial statements.

The main effect of revised IFRS 3 "Business Combinations" has been:

– to add an option to permit recognition of 100% of the goodwill on acquisition of an entity, not just the acquiring entity's portion of the goodwill, the choice of this option is allowed on a transaction-by transaction basis,
– to change the recognition and subsequent accounting requirements for contingent consideration,
– to require acquisition-related costs to be accounted for separately from the business combination, generally leading to those costs being expensed when incurred and,
– for business combinations achieved in stages, to require remeasurement of previously held interests in the acquired entity at fair value. Any gain or loss arising from the remeasurement to be recognised in the income statement.

Revised IAS 27 has resulted in a change in accounting policy regarding increase or decrease in the Group's ownership interest in its subsidiaries. In prior years, in the absence of specific requirements in International Financial Reporting Standards ("IFRS"), an increase in interest in existing subsidiaries was treated in the same manner as the acquisition of subsidiaries, with goodwill being recognized where appropriate. There was no decrease in the interest in subsidiaries that did not involve loss of control in TP Group in prior years. Starting from 2010 an increase or a decrease in interest in existing subsidiaries that does not involve loss of control are dealt, under revised IAS 27, within equity, with no effect on goodwill or income statement.

Revised standards have to be applied prospectively to business combinations for which the transaction date is on or after 1 January 2010. No business combinations occurred during the 12 months ended 31 December 2010.

Standards and interpretations issued but not yet adopted
Management has not opted for early application of the following standards and interpretations (already endorsed or in the process of being endorsed by the European Union):

– Amendments to IAS 32 "Financial Instruments: Presentation" applicable for financial years beginning on or after 1 February 2010,
– Amendments to IAS 24 "Related Party Disclosures" applicable for financial years beginning on or after 1 January 2011,
– IFRS 9 "Financial Instruments" applicable for financial years beginning on or after 1 January 2013. This standard has not been endorsed by the European Union,
– IFRIC 19 "Extinguishing Financial Liabilities with Equity Instruments" applicable for financial years beginning on or after 1 July 2010,
– Amendments to IFRIC 14 "Prepayments of a Minimum Funding Requirement" applicable for financial years beginning on or after 1 January 2011,
– Improvements to International Financial Reporting Standards – a collection of amendments to IFRSs, the amendments are effective, in most cases, for annual periods beginning on or after 1 January 2011. These amendments have not been endorsed by the European Union,
– Amendments to IFRS 7 "Financial Instruments: Disclosures" applicable for financial years beginning on or after 1 July 2011. These amendments have not been endorsed by the European Union.

Management is currently analyzing the practical consequences of these new standards and interpretations and the impact of their application on the financial statements.

Notes to the consolidated financial statements continued

3. Significant accounting policies (continued)

3.2.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 is not specifically (or is only partially) dealt with by any IFRS standards or interpretations endorsed by the European Union.
The Group has adopted accounting policies which it believes best reflect the substance of the transactions concerned.

Multiple-elements arrangements
When accounting for multiple-elements arrangements (bundled offers) the Group has adopted the provisions of Generally Accepted Accounting Principles in the United States, Accounting Standards Codification 605-25 „Revenue Recognition – Multiple Element Agreements" (see Note 3.5.3 Separable components of packaged and bundled offers).

3.3.Options available under IFRSs and used by the Group

Certain IFRSs offer alternative methods of measuring and recognizing assets and liabilities. In this respect, the Group has chosen:

	Standards	Option used
IAS 2	Inventories	Recognition of inventories at their original cost determined by the weighted average unit cost method.
IAS 16	Property, plant and equipment	Property, plant and equipment are measured at amortized historical cost less any accumulated impairment loss.
IAS 19	Employee benefits	Actuarial gains and losses on post-employment benefits are recognized immediately in their total amount in the other comprehensive income, with no recycling to the income statement.
IAS 20	Government grants and disclosure of government assistance	Non-repayable government grants related to assets decrease the carrying amount of the assets. Government grants related to income are deducted from the related expenses.
IAS 38	Intangible assets	Intangible assets are measured at amortized historical cost less any accumulated impairment loss.

3.4. Presentation of the financial statements

Presentation of the balance sheet
In accordance with IAS 1 "Presentation of financial statements", assets and liabilities are presented in the balance sheet as current and non-current.

In accordance with IFRS 5, non-current assets and all directly attributable liabilities that are considered as being held for sale are reported on a separate line in the consolidated balance sheet.

Presentation of the income statement
As allowed by IAS 1 "Presentation of financial statements", expenses are presented by nature in the consolidated income statement.

Earnings per share
The net income per share for each period is calculated by dividing the net income for the period attributable to the equity holders of the Company by the weighted average number of shares outstanding during that period. The weighted average number of shares outstanding is after taking account of treasury shares and the dilutive effect of the pre-emption rights attached to the bonds issued under TP S.A. incentive programme (see Note 26).

Change in accounting policy for post-employment benefits
In accordance with IAS 19 "Employee Benefits", the actuarial gains and losses are recognized:

– in profit or loss either for their total amount or up to a portion using the corridor method which was the method applied by the Group until December 31, 2009,
– or in the other comprehensive income for their total amount.

The exposure draft published by the International Accounting Standards Board in April 2010 relating to the amendment to IAS 19 confirms the removal of the corridor method and proposes the immediate recognition of actuarial gains and losses in the other comprehensive income, with no recycling to the income statement.

Following this publication, the Group has decided to account for defined benefit plans actuarial gains and losses in the other comprehensive income from January 1, 2010.
This change in accounting policy results in the financial statements providing more relevant and comparative information as this policy is generally applied in telecommunications industry.

3. Significant accounting policies (continued)

3.4. Presentation of the financial statements (continued)

Change in accounting policy for post-employment benefits affected the Group's financial statements as follows:

(in PLN millions)	Data previously reported	Impact of changes in the accountant policies	Data currently reported
	12 months ended 31 December 2009		
Consolidated income statement			
Labour expenses	(2,353)	1	(2,352)
Operating income	2,096	1	2,097
Consolidated net income	1,282	1	1,283
Earnings per share (in PLN) (basic and diluted)	0.96	–	0.96
Consolidated statement of comprehensive income			
Consolidated net income	1,282	1	1,283
Actuarial losses on post-employment benefits	–	(14)	(14)
Income tax relating to components of other comprehensive income	(10)	3	(7)
Total comprehensive income	1,324	(10)	1,314
Consolidated statement of cash flows			
Consolidated net income	1,282	1	1,283
Change in other provisions	(156)	(1)	(157)
Net cash provided by operating activities	5,541	–	5,541
	At 31 December 2009		
Consolidated balance sheet			
Assets			
Deferred tax assets	506	6	515
Total non-current assets	25,167	6	25,176
Total assets	29,356	6	29,365
Equity			
Other reserves	91	(41)	50
Retained earnings	11,655	1	11,656
Total equity	16,593	(40)	16,553
Non-current liabilities			
Employee benefits	234	49	283
Total non-current liabilities	7,541	49	7,590

(in PLN millions)	Before the change in the accounting policies	Impact of changes in the accountant policies	Data currently reported
	At 1 January 2009		
Consolidated balance sheet			
Assets			
Deferred tax assets	400	6	406
Total non-current assets	26,980	6	26,986
Total assets	31,234	6	31,240
Equity			
Other reserves	8	(30)	(22)
Retained earnings	12,983	–	12,983
Total equity	17,230	(30)	17,220
Non-current liabilities			
Employee benefits	282	36	318
Total non-current liabilities	6,589	36	6,625

The consolidated balance sheet and other comparative information as at 1 January 2009, which is the beginning of the earliest comparative period, was not presented due to immaterial effect of changes in the accounting policies.

Notes to the consolidated financial statements continued

3. Significant accounting policies (continued)

3.4. Presentation of the financial statements (continued)

Changes in presentation of the financial statements

Dispute with DPTG
Following the partial award in the arbitration proceedings between TP S.A. and DPTG (see Note 31.d), the Group decided to disclose separately the impact of the dispute on the Group's financial performance because it does not relate to current operations.

Adoption of revised IFRS 3
Following the changes in IFRS 3 "Business Combinations" (effective from 1 January 2010), the accounting term "Minority interest" was changed to "Non-controlling interests" in these Consolidated Financial Statements.

Changes in presentation of items of the consolidated statement of cash flows
In 2010 the Group changed the presentation of certain items of net cash provided by operating activities in the consolidated statement of cash flows. The changes comprise the presentation of the following two adjustments to reconcile net income to funds generated from operations: finance costs, net excluding realised exchange rate effect on cash and cash equivalents and operational foreign exchange and derivatives (gains)/losses, net. In previous accounting periods, the aforementioned items were grouped as follows: interest income and expense, foreign exchange (gains)/losses, net and derivatives (gains)/losses, net (for the 12 months ended 31 December 2009 amounting to PLN 370 million, PLN (246) million and PLN 381 million, respectively). These changes have no effect on net cash provided by operating activities.

Management believes that the current presentation better reflects the nature of transactions concluded.

3.5. Significant accounting policies

3.5.1. Consolidation rules

Subsidiaries that are controlled 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 obtained by the Company and cease to be consolidated from the date on which the Company loses control over the subsidiary.

Intercompany transactions and balances are eliminated on consolidation.

3.5.2.Effect of changes in foreign exchange rates

Translation of financial statements of foreign subsidiaries
The financial statements of foreign subsidiaries whose functional currency is not the Polish 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 income statement 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 entities constituting the Group into their functional currency at the spot exchange rate prevailing as at the transaction date. 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 and expense for commercial transactions,
– in financial income or finance costs for financial transactions.

Derivative instruments are measured and recognized in accordance with the general principles described in Note 3.5.12.

Currency hedges that qualify for hedge accounting are recognized in the balance sheet at fair value at each period-end. Gains and losses arising from remeasurement to fair value are recognized:

– in other operating income and expense for fair value hedges of commercial transactions;
– in financial income or finance costs for hedges of financial assets and liabilities;
– in other comprehensive income for the effective portion of the net gain or loss on cash flow hedges.

Gains and losses arising from remeasurement to fair value of currency derivative instruments that economically hedge commercial or financial transactions and do not qualify for hedge accounting are recognized as other operating income/cost or financial income/expense depending on the nature of the underlying transaction. Gains and losses arising from remeasurement to fair value of other currency derivative instruments are recognized as financial income or finance cost.

Notes to the consolidated financial statements continued

3. Significant accounting policies (continued)

3.5.3. Revenue

Revenue from the Group's activities is recognized and presented in accordance with IAS 18 "Revenue". Revenue comprises the fair value of the consideration received or receivable for the sale of services and goods in the ordinary course of the Group's activities. Revenue is recorded net of value-added tax and discounts.

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 and the balance of the amount received or receivable is contingent upon the future delivery of the service.

Offers that cannot be analyzed 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. Revenue from bundled offers is recognized in full over the life of the contract. The main example is connection fee: this does not represent a separately identifiable transaction from the subscription and communications, and connection fees are therefore recognized over the average expected life of the contractual relationship.

Equipment sales

Revenue from equipment sales is recognized when the significant risks and rewards of ownership are transferred to the buyer (see also paragraph "Separable components of packaged and bundled offers").

For mobile and broadband services, when equipment is sold through a distributor considered as an agent, handsets or modems/laptops and telecommunications services are a single bundled offering with multiple deliverables, and the handset or modem/laptop revenue from the sale is recognised when a subscriber is connected to the network.

Equipment leases

Equipment lease revenue is recognized 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.

Revenues from the sale or supply of content

Equipment lease revenue is recognized 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:

- the Group has the primary responsibility for providing services desired by the customer;
- the Group has inventory risk (the Group purchases content in advance);
- the Group has discretion in establishing prices directly or indirectly, such as by providing additional services;
- the Group has credit risk.

Revenues from the sale or supply of content via the Group's various communications systems (mobile, TV, fixed line, etc.) are recognized:

- gross when the Group is deemed to be the primary obligor in the transaction with respect to the end-customer (i.e. when the customer has no specific recourse against the content provider), when the Group bears the inventory risk, when the Group has a reasonable latitude in setting prices charged to the end-customer, when the Group has credit risk and
- net of amounts due to the content provider when the latter is responsible for supplying the content to the end-customer, for setting the price to subscribers, when the content provider bears the inventory risk, when it has credit risk.

Service revenue

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

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

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

Revenue from Internet advertising and from the sale of advertising space in online telephone directories is recognized over the period during which the advertisement appears. Revenue from the sale of advertising space in printed telephone directories is recognized when the directory is distributed.

Promotional offers

For certain commercial offers where customers do not pay for 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 cancellable 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 or purchase of goods.

Points awarded to customers are treated as a separable component to be delivered out of the transaction that triggered the acquisition of the points. Part of the invoiced revenue is allocated to these points based on their fair value taking into account an estimated utilization rate, and deferred. If the Group supplies the awards itself, revenue allocated to the points is recognised in the income statement when points are redeemed and the Group fulfils its obligations to supply awards. The amount of revenue recognised is based on the number of award credits that have been redeemed in exchange for awards, relative to the total number expected to be redeemed. When a third party supplies the awards and the Group is collecting the consideration on behalf of a third party, revenue is measured as a net amount retained on the Group's own account and is recognised when the third party becomes obliged to supply the awards and is entitled to receive consideration for doing so.

Loyalty programs that exist in the Group are without a contract renewal obligation.

Discounts for poor quality of services or for breaks in service rendering

The Group's commercial contracts may contain service level commitments (delivery time, service reinstatement time). If the Group fails to comply with these commitments, it is obliged to grant a discount to the end-customer. Such discounts reduce revenue. Discounts are recorded when it becomes probable that they will be due based on the non-achievement of contractual terms.

Notes to the consolidated financial statements continued

3. Significant accounting policies (continued)

3.5.3. Revenue (continued)

Barter transactions
When goods or services are exchanged for goods or services which are of a similar nature and value, the exchange is not regarded as a transaction which generates revenue. When goods are sold or services are rendered in exchange for dissimilar goods or services, the revenue is measured at the fair value of the goods or services received, adjusted by the amount of any cash or cash equivalents transferred. When the fair value of the goods or services received cannot be measured reliably, the revenue is measured at the fair value of the goods or services given up, adjusted by the amount of any cash or cash equivalents transferred. The revenue from barter transactions involving advertising is measured in accordance with Interpretation 31 of the Standing Interpretations Committee "Revenue – Barter Transactions Involving Advertising Services".

3.5.4.Subscriber acquisition costs, advertising and related costs

Subscriber acquisition and retention costs, other than loyalty program costs (see Note 3.5.3), are recognized as an expense for the period in which they are incurred. Advertising, promotion, sponsoring, communication and brand marketing costs are also expensed as incurred.

3.5.5. Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset are capitalized as part of the cost of that asset. Qualifying assets are assets that necessarily take a substantial period of time to get ready for their intended use or sale.

3.5.6. Share issuance costs and treasury shares

External costs directly related to share issuance are deducted from the related share premium. Other costs are expensed as incurred.

If TP S.A. or its subsidiaries purchase equity instruments of the Company, the consideration paid, including directly attributable incremental costs, is deducted from equity attributable to the Company equity holders and presented in the balance sheet separately under "Treasury shares" until the shares are cancelled or reissued. The Group does not recognise in the income statement any gain or loss on the purchase, sale, issue or cancellation of its own equity instruments.

Treasury shares are recognised using settlement date accounting.

3.5.7. Goodwill

Goodwill is the excess of (a) over (b) below:

(a) the aggregate of:
- (i) the consideration transferred measured generally at acquisition-date fair value;
- (ii) the amount of any non-controlling interest in the acquiree measured either at its fair value or at its proportionate interest in the net identifiable assets;
- (iii) in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree.

(b) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured at fair value, apart from limited exceptions provided in IFRS 3.

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 amortized 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). The allocation is made to those CGUs or groups of CGUs that are expected to benefit from the synergies of business combination.

Recoverable amount
To determine whether an impairment loss should be recognised, 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 realizable 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 business plan and its extrapolation to perpetuity by applying a declining or flat growth rate reflecting the expected long-term trend in the market,
- the cash flows obtained are discounted using appropriate rates for the type of business concerned.

If the recoverable amount of CGUs to which the goodwill is allocated is less than its carrying amount, an impairment loss is recognised in the amount of the difference. The impairment loss is firstly allocated to reduce the carrying amount of goodwill and then to the other assets of CGUs on a pro rata basis.

Goodwill impairment losses are recorded in the income statement as a deduction from operating income and are not reversed.

Notes to the consolidated financial statements continued

3. Significant accounting policies (continued)

3.5.8. Intangible assets (excluding goodwill)

Intangible assets, consisting mainly of licenses, software and development costs, are initially stated at acquisition or production cost comprising its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, any directly attributable costs of preparing the assets for their intended use or sale, and, if applicable, attributable borrowing costs.

When intangible assets are acquired in a business combination, they are initially stated at their fair values. They are 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 revenue, costs or other appropriate criteria. The intangible assets are recognized at the acquisition date separately from goodwill if the asset's fair value can be measured reliably, is identifiable, (i.e. is separable) or arises from contractual or the legal rights irrespective of whether the assets had been recognised by the acquiree before the business combination.

Internally developed trademarks and subscriber bases are not recognized as intangible assets.

Telecommunication licenses
Expenditures to acquire telecommunication licenses are amortized 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 14.

Research and development costs
Under IAS 38 "Intangible Assets", development costs are recognized 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.

Development costs not fulfilling the above criteria and research costs are expensed as incurred. The Group's research and development projects mainly concern:

– upgrading the network architecture or functionality;
– developing service platforms aimed at offering new services to the Group's customers.

Development costs recognized as an intangible asset are amortized on a straight-line basis over their estimated useful life, generally not exceeding four years.

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

Useful lives of intangible assets are reviewed annually and are adjusted if current estimated useful lives are different from previous estimates. These changes in accounting estimates are recognized prospectively.

3.5.9. Property, plant and equipment

The cost of tangible assets corresponds to their purchase or production cost or price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, as well as 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, and, if applicable, attributable borrowing costs.

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 is 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 established for each component accordingly.

Maintenance and repair costs (day to day costs of servicing) are expensed as incurred.

Government grants
The Group may receive non-repayable government grants in the form of direct or indirect funding of capital projects. These grants are deducted from the cost of the related assets and recognized in the income statement, as a reduction of depreciation, based on the pattern in which the related asset's expected future economic benefits are consumed.

Finance leases
Assets acquired under leases that transfer substantially all risks and rewards of ownership to the Group are recorded as assets and an obligation in the same amount is recorded in liabilities. Normally, the risks and rewards of ownership are considered as having been transferred to the Group when at least one condition is met:

– 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 specialized nature that only the lessee can use them without major modifications.

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

3. Significant accounting policies (continued)

3.5.9. Property, plant and equipment (continued)

Derecognition
An item of property, plant and equipment is derecognized on its disposal or when no future economic benefits are expected from its use or disposal. The gain or loss arising from the derecognition of an item of property, plant and equipment is recognized in operating income and equals the difference between the net disposal proceeds, if any, and the carrying amount of the item.

Depreciation
Items of property, plant and equipment are depreciated to write off their cost, less any estimated 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
Networks and terminals	2 to 33 years
IT equipment	3 to 5 years
Other	2 to 10 years

Land is not depreciated. Perpetual usufruct rights are amortised over the period for which the right was granted, not exceeding 99 years.

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 recognized prospectively.

3.5.10. 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 than continuing use. Those assets are available for immediate sale in their present condition 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 the balance sheet if IFRS 5 requirements are met.

Those assets are no longer depreciated. If fair value less costs to sell is less than its carrying amount, an impairment loss is recognised in the amount of the difference. In subsequent periods, if fair value less costs to sell increases the impairment loss is reversed up to the amount of losses previously recognised.

3.5.11. Impairment of non-current assets other than goodwill

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 recognized whenever the carrying amount of an asset exceeds its recoverable amount. Where possible, the recoverable amount is estimated for individual assets. The recoverable amount of such assets is determined at their fair value less cost to sell or their value in use. If it is not possible to estimate the recoverable amount of the individual asset, the Group identified the cash-generating unit ("CGU") to which the asset belongs.

In the case of 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 revenue or other external indicators), an impairment loss is recognized.

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 flow 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.

The impairment loss recognised equals the difference between net book value and recoverable amount.

Impairment tests are carried out on individual assets, except where they do not generate independent cash flows. In such cases the recoverable amount is then determined at the level of the cash-generating unit (CGU) to which the asset belongs, except where:

– the fair value less costs to sell of the individual asset is higher than its book value; or
– the value in use of the asset can be estimated as being close to its fair value less costs to sell, where fair value can be reliably determined.

Given the nature of its assets and operations, most of the Group's individual assets do not generate cash flow independently from other assets.

3.5.12. Financial assets and liabilities

Financial assets include assets available-for-sale, assets at fair value through profit or loss, hedging derivative instruments and loans and receivables.

Financial liabilities include borrowings, other financing and bank overdrafts, liabilities at fair value through profit or loss, hedging derivative instruments, trade accounts payable and fixed assets payable, including the UMTS license liability.

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

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

Management determines the classification of financial assets and liabilities at initial recognition.

Notes to the consolidated financial statements continued

3. Significant accounting policies (continued)

3.5.12. Financial assets and liabilities (continued)

Recognition and measurement of financial assets
When financial assets are recognized initially, they are measured at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

Assets available-for-sale
Available-for-sale assets consist mainly of shares in companies and marketable securities that are those non-derivative financial assets that are designated as available for sale or are not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss. They are measured at fair value and gains and losses arising from remeasurement at fair value are recognized in other comprehensive income. 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. Investments in unquoted equity instruments whose fair value cannot be reliably measured are measured at cost, less any impairment losses.

When there is objective evidence that available-for-sale assets are impaired, the cumulative loss included in other comprehensive income is taken to the income statement. A significant or prolonged decline in the fair value of equity instruments below costs is considered as an indicator that the securities are impaired. Impairment losses on equity instruments are not reversed through the income statement.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and include trade receivables, cash and cash equivalents, cash deposits paid to banks as a collateral for derivatives and other loans and receivables. They are recognized initially at fair value plus directly attributable transaction costs and are subsequently measured at amortized cost using 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.

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 subject to insignificant changes in value.

Loans and receivables are carried in the balance sheet under:, "Loans and receivables excluding trade receivables", "Trade receivables" and "Cash and cash equivalents".

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 recognized in the income statement.

Trade receivables that are homogenous and share similar credit risk characteristics are tested for impairment collectively. When estimating the expected credit risk the Group uses historical data as a measure for a decrease in the estimated future cash flows from the group of assets since the initial recognition.

In calculating the recoverable amount of receivables that are individually material and not homogenous, significant financial difficulties of the debtor or probability that the debtor will enter bankruptcy or financial reorganisation are taken into account.

The carrying amount of loans and receivables is reduced through an allowance account. Uncollectable receivables are written off against that account.

Assets at fair value through profit or loss
Financial assets at fair value through profit or loss are the following financial assets held for trading:

– financial assets acquired by the Group principally for the purpose of selling them in the near term;
– financial assets that form a 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;
– derivative assets not qualifying for hedge accounting as set out in IAS 39.

Recognition and measurement of financial liabilities
Financial liabilities at amortised cost
Borrowings and other financial liabilities are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method. Financial liabilities measured at amortised cost are carried in the balance sheet under "Financial liabilities at amortised cost excluding trade payables" and "Trade payables".

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 recognized at fair value that usually corresponds to the fair value of the sums paid or received in exchange for the liability. The costs are subsequently amortized 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 costs paid or received between parties to the contract.

Certain borrowings are designated as being hedged by fair value hedges. Gain or loss on hedged borrowing attributable to a hedged risk adjusts the carrying amount of a borrowing and is recognized in the income statement.

3. Significant accounting policies (continued)

3.5.12. Financial assets and liabilities (continued)

Financial liabilities at fair value through profit or loss
Financial liabilities at fair value through profit or loss include derivatives that do not qualify for hedge accounting as set out in IAS 39 and are measured at fair value.

Upon initial recognition the Group did not designate financial liabilities as financial liability at fair value through profit or loss.

Recognition and measurement of derivative instruments
Derivative instruments are recognized in the balance sheet and measured at fair value. Derivatives used by the Group are not traded in an active market and their fair value is determined by using standard valuation techniques. 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 for gains and losses on hedging instruments (as explained below), gains and losses arising from changes in fair value of derivatives classified as financial assets and liabilities at fair value through profit or loss are immediately recognized in the income statement. The interest rate component of derivatives held for trading is presented under interest expense within finance cost. The foreign exchange component of derivatives held for trading that economically hedge commercial or financial transactions is presented under foreign exchange gains or losses within other operating income/expense or finance cost, respectively, depending on the nature of the underlying transaction. The foreign exchange component of other derivatives held for trading is presented under foreign exchange gains or losses within finance cost, net.

The Group treats the whole derivative as its unit of account and presents derivatives either as current or non-current based on the date of last cash flows either within or beyond 12 months from the balance sheet date.

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 recognized 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 recognized 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 a 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 recognized in profit or loss and is offset by the effective portion of the loss or gain from remeasuring the hedging instrument at fair value. The adjustment to the hedged item is amortized starting from the date when a hedged item ceases to be adjusted by a change in the fair value of the hedged portion of liability attributable to the risk hedged,
– for cash flow hedges, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognized directly in other comprehensive income and the ineffective portion of the gain or loss on the hedging instrument is recognized in profit or loss. Amounts recognized directly in other comprehensive income are subsequently recognized in profit or loss in the same period or periods during which the hedged item affects profit or loss. If a hedge of a forecast transaction results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously deferred in other comprehensive income are transferred from other comprehensive income and included in the initial measurement of the cost of the asset or liability.

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 derecognized when:

– 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 derecognized 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 recognized in profit or loss.

Fair value measurements
The Group classifies fair value measurements using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

– Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities,
– Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices),
– Level 3: inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

3. Significant accounting policies (continued)

3.5.13. Inventories

Inventories are stated at the lower of cost and net realizable 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 revenue 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. Net realizable value is the estimated selling price in the ordinary course of business, less selling expenses.

3.5.14. Income tax

The tax expense comprises current and deferred tax.

Current tax
The current income tax charge is determined in accordance with the relevant tax law regulations in respect of the taxable profit. Income tax payable represents the amounts payable at the balance sheet date. If the amount paid on account of current income tax is greater than the amount finally determined, the excess is recognised in the balance sheet as an income tax asset.

Deferred taxes
In accordance with IAS 12 "Income Taxes", deferred taxes are recognized for all temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and their tax bases, as well as for unused tax losses, using the liability method. Deferred tax assets are recognized only when their recovery is considered probable, that is when future taxable profit will be available against which the temporary differences can be utilised. At each balance sheet date unrecognised deferred tax assets are re-assessed. A previously unrecognised deferred tax asset is recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax is not accounted for if it arises from the initial recognition of an asset and liability in a transaction that is not a business combination and at the time of the transaction, affects neither accounting nor taxable profit or loss. IAS 12 requires, in particular, the recognition of deferred tax liabilities on all intangible assets recognized in business combinations (trademarks, subscriber bases, etc.).

A deferred tax asset is recognised for all deductible temporary differences arising from investments in subsidiaries and associates, to the extent that, and only to the extent that, it is probable that:

– the temporary difference will reverse in the foreseeable future; and
– taxable profit will be available against which the temporary difference can be utilized.

A deferred tax liability is recognized 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. Deferred income tax is calculated using the enacted or substantially enacted tax rates at the balance sheet date.

3.5.15. Provisions

In accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets", a provision is recognized 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 (i) possible obligations that are not recognized 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 (ii) to present obligations arising from past events that are not recognized 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 Consolidated Financial Statements.

Restructuring
A provision for restructuring costs is recognized only when the general recognition criteria for provisions are met and when the Group:

– has a detailed formal plan for the restructuring, and
– has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

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 is 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 corresponding entry to the asset to which it relates.

3. Significant accounting policies (continued)

3.5.16. Pensions and other employee 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 to some of 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).

Actuarial gains and losses on jubilee awards plans are recognized as income or expense when they occur. Actuarial gains and losses on post-employment benefits are recognized immediately in their total amount in the other comprehensive income, with no recycling to the income statement. 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 recognizes 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.

3.5.17. Share-based payments

TP S.A. operates an equity-settled, share-based compensation plan under which employees render services to the Company and its subsidiaries as consideration for equity instruments of TP S.A. The fair value of the employee services received in exchange for the grant of the equity instruments is recognised as an expense, with a corresponding increase in equity, over the period in which the service conditions are fulfilled (vesting period).

France Telecom S.A. operates its own equity-settled, share-based compensation plan under which employees of the Group render services to the Company and its subsidiaries as consideration for equity instruments of France Telecom S.A. In accordance with IFRS 2 "Share-based Payment", the fair value of the employee services received in exchange for the grant of the equity instruments of France Telecom S.A. is recognised in these Consolidated Financial Statements as an expense with a corresponding increase in equity, over the period in which the service conditions are fulfilled (vesting period).

The fair value of the employee services received is measured by reference to the fair value of the equity instruments at the grant date.

Vesting conditions, other than market conditions, were taken into account by adjusting the number of equity instruments included in the measurement of the transaction so that, ultimately, the expense recognised for services received is based on the number of equity instruments that are expected to vest.

4. Main acquisitions and divestitures of companies
There were no significant acquisitions and divestitures in the 12 months ended 31 December 2010.

Significant acquisitions and divestitures in the 12 months ended 31 December 2009 are described below.

On 24 March 2009, the Group and LUX MED Sp. z o.o. concluded a share sale agreement under which the Group disposed of its 100% shareholding in TP Med Sp. z o.o., for a sales price totalling PLN 19 million.

On 8 April 2009, the Group set up a company PayTel S.A., with a share capital amounting to PLN 12 million. The company was registered on 25 June 2009. The company's activities include electronic payment services.

In May 2009, the Group purchased 100% of the shares in Ramsat S.A. ("Ramsat") – an authorized dealer of PTK Centertel. The purchase price amounted to PLN 25 million. As a result of accounting as a business combination the Group recognized goodwill in the amount of PLN 22 million, as well as PLN 8 million of the acquirees' non current assets, PLN 45 million of the acquirees' current assets and PLN 50 million of the acquirees' liabilities which represent carrying amounts of each of those classes determined immediately before the combination.

Notes to the consolidated financial statements continued

5. Revenue

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Fixed line telephony services	**5,157**	**5,908**
Subscriptions and voice traffic revenue	4,033	4,800
Wholesale revenue (including interconnect)	1,109	1,081
Payphone revenue	14	26
Other	1	1
Mobile telephony services	**7,065**	**7,188**
Voice traffic revenue	4,193	4,271
Interconnect revenue	1,361	1,423
Messaging services and content	1,436	1,437
Other	75	57
Data Services	**2,517**	**2,591**
Leased lines	291	313
Data transmission	677	686
Dial – up	5	14
Broadband and TV revenue	1,544	1,578
Radio communications	**215**	**213**
Sales of goods and other	**761**	**660**
Total revenue	**15,715**	**16,560**

Revenue is generated mainly in the territory of Poland. Approximately 3.0% and 2.8% of the total revenue for the 12 months ended 31 December 2010 and 2009, respectively, was received from entities which are not domiciled in Poland, mostly from interconnect services.

6. Operating income and expense

6.1. External purchases

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Commercial expenses	(2,509)	(2,543)
– cost of handsets and other equipment sold	(1,301)	(1,353)
– commissions, advertising, sponsoring costs and other	(1,208)	(1,190)
Interconnect expenses	(2,139)	(2,179)
Costs relating to network and IT expenses	(905)	(974)
Other external purchases	(1,621)	(1,742)
Total external purchases	(7,174)	(7,438)

Other external purchases include customer support and management services, postage costs, costs of content, rental costs, real estate operating and maintenance costs, subcontracting fees, advisory and legal services, costs of other services, supplies and equipment for internal use.

6. Operating income and expense (continued)

6.2. Labour expenses

(in PLN millions, except for number of employees)	12 months ended 31 December 2010	12 months ended 31 December 2009
Average number of employees (full time equivalent)	25,687	28,096
Wages and salaries	(1,872)	(1,926)
Social security and other charges	(392)	(411)
Capitalized personnel costs	162	139
Other employee benefits	(112)	(111)
Wages and employee benefit expenses	**(2,214)**	**(2,309)**
Share based-payments	**(4)**	**(43)**
Total labour expenses	**(2,218)**	**(2,352)**

6.3. Other operating income and expense

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Impairment losses on trade and other receivables, net	(114)	(109)
Taxes other than income taxes	(318)	(325)
– property tax and perpetual usufruct charges	(184)	(196)
– frequency fee, fees for subscribers' numbers and telecommunications charges	(100)	(93)
– other taxes	(34)	(36)
Operating foreign exchange losses, net	(8)	–
Other expense and changes in provisions, net	(329)	(237)
Total other operating expense	**(769)**	**(671)**
Total other operating income	**193**	**169**

Other expense and changes in provisions include brand fees, changes in provisions for claims and litigation, risks and other charges (see Note 27), except for provision for the dispute with DPTG (see Note 31.d).

Other operating income includes operating foreign exchange gains, net, as well as late payment interest on trade receivables, recoveries of customer bad debts written off and other individually immaterial items.

During the 12 months ended 31 December 2010 and 2009, foreign exchange gains/(losses) on cash flow hedges that were transferred from other comprehensive income to other operating income/expense and adjusted foreign exchange differences on hedged UMTS liability amounted to PLN (6) million and PLN (3) million, respectively (see Note 12).

During the 12 months ended 31 December 2010 and 2009, foreign exchange gains/(losses) presented in other operating expense/income related to derivatives classified as held for trading under IAS 39 and economically hedging commercial transactions amounted to PLN (46) million and PLN (21) million, respectively.

6.4. Research and development

In the 12 months ended 31 December 2010 and 2009, research and development costs expensed in the income statement amounted to PLN 60 million and PLN 62 million, respectively.

7. Restructuring costs

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Employee termination	(34)	(25)
Other	–	2
Total restructuring costs	**(34)**	**(23)**

Movements in restructuring provisions are described in Note 27.

Notes to the consolidated financial statements continued

8. Gains on disposal of assets

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Disposal of subsidiaries [1]	–	13
Disposals of property, plant and equipment and intangible assets [2]	59	22
Total gains on disposal of assets	**59**	**35**

[1] In the 12 months ended 31 December 2009 includes gain on disposal of TP Med Sp. z o.o. (see Note 4).
[2] In the 12 months ended 31 December 2010 and 2009 includes gains on disposals of property amounting to PLN 56 million and PLN 19 million, respectively.

9. Impairment

9.1.Information concerning the Cash Generating Units

Most of the Group's individual assets do not generate cash flow independently from other assets due to the nature of the Group's activities. The entire fixed network, the entire radio diffusion network, the entire mobile network and internet portal are treated as separate Cash Generating Units.

The Group considers certain indicators, including market liberalization and other regulatory and economic changes in the Polish telecommunications market, in assessing whether there is any indication that an asset may be impaired. As at 31 December 2010 and 2009 the Group performed impairment tests of all Cash Generating Units. No impairment loss was recognized in 2010 and 2009 as a result of these tests.

The following key assumptions were used to determine the value in use of the groups of CGUs:

– market value, penetration rate and market share decisions of the regulator in terms of 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 of changes in net revenue on direct costs 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.

Main CGUs	Fixed network	Mobile network	Radio diffusion network	Internet portal
	At 31 December 2010			
Basis of recoverable amount	Value in use	Value in use	Value in use	Value in use
Source used	Business plan	Business plan	Business plan	Business plan
	5 years cash flow projections	5 years cash flow projections	5 years cash flow projections	5 years cash flow projections
Growth rate to perpetuity	0%	0%	2.5%	1%
Pre-tax discount rate	11.0	11.5	11.7	14.0

Main CGUs	Fixed network	Mobile network	Radio diffusion network	Internet portal
	At 31 December 2009			
Basis of recoverable amount	Value in use	Value in use	Value in use	Value in use
Source used	Business plan	Business plan	Business plan	Business plan
	5 years cash flow projections	5 years cash flow projections	5 years cash flow projections	5 years cash flow projections
Growth rate to perpetuity	0%	0%	1%	1%
Pre-tax discount rate	12.1	12.8	13.9	15.9

Sensitivity of recoverable amounts

Management believes that no reasonably possible change to any of the above key assumptions would cause the carrying value of fixed network, mobile network, radio diffusion network and internet portal to materially exceed their recoverable amounts.

Notes to the consolidated financial statements continued

9. Impairment (continued)

9.2. Goodwill

In the 12 months ended 31 December 2010 and 2009, there was no goodwill written off. Details regarding impairment tests of goodwill are presented in Note 9.1.

9.3.Other property, plant and equipment and intangible assets

In the 12 months ended 31 December 2010, the impairment loss on property, plant and equipment charged to the income statement amounted to PLN 10 million, primarily including a net impairment loss as a result of a review of certain Group's properties.

In the 12 months ended 31 December 2009, the impairment loss on property, plant and equipment charged to the income statement amounted to PLN 22 million, primarily including a net impairment reversal as a result of a review of certain Group's properties and an impairment loss on liquidated network assets.

In the 12 months ended 31 December 2010 and 2009, the impairment loss on other intangible assets charged to the income statement amounted to PLN 1 million and 11 million respectively and was recognized as a result of a review of expected future cash flows.

10. Financial income and expense

	12 months ended 31 December 2010							
	Finance costs, net					Operating income		
(in PLN millions)	Interest Income	Interest expense and other financial charges	Foreign exchange gains/ (losses)	Discounting expense	**Financial income/ (costs), net**	Interest income/ expense	Foreign exchange gains/ (losses)	Impairment losses
Loans and receivables	85	–	29	–	**114**	36 [3]	(6)	107 [4]
– including cash and cash equivalents	83	–	29	–	**112**	–	–	–
Liabilities at amortized cost	–	(331) [1]	163	(36)	**(204)**	–	14	–
Derivatives	–	(153)	(169)	(10)	**(332)**	–	(52)	–
– hedging derivatives	–	(64)	(97)	–	**(161)**	–	(6)	–
– derivatives held for trading	–	(89)	(72)	(10)	**(171)**	–	(46)	–
Non-financial items	–	–	–	(37) [2]	**(37)**	–	36	(18) [5]
Total	**85**	**(484)**	**23**	**(83)**	**(459)**	**36**	**(8)**	**(125)**

[1] Includes mainly interest expense on bonds and bank borrowings and change in fair value of liabilities hedged by fair value hedges.
[2] Includes discounting expense related to employee benefits, restructuring provisions and provisions for dismantling.
[3] Includes late payment interests on trade receivables.
[4] Includes impairment losses on trade receivables.
[5] Includes impairment losses on other receivables and non-current assets.

	12 months ended 31 December 2009							
	Finance costs, net					Operating income		
(in PLN millions)	Interest Income	Interest expense and other financial charges	Foreign exchange gains/ (losses)	Discounting expense	**Financial income/ (costs), net**	Interest income/ expense	Foreign exchange gains/ (losses)	Impairment losses
Loans and receivables	37	–	10	–	**47**	28 [3]	6	(106) [4]
– including cash and cash equivalents	36	–	10	–	**46**	–	–	–
Liabilities at amortized cost	–	(325) [1]	218	(47)	**(154)**	(1)	10	–
Derivatives	–	(75)	(258)	(24)	**(357)**	–	(24)	–
– hedging derivatives	–	(26)	(7)	–	**(33)**	–	(3)	–
– derivatives held for trading	–	(49)	(251)	(24)	**(324)**	–	(21)	–
Non-financial items	–	–	–	(35) [2]	**(35)**	–	14	(36) [5]
Total	**37**	**(400)**	**30**	**(106)**	**(499)**	**27**	**6**	**(142)**

[1] Includes mainly interest expense on bonds and bank borrowings and change in fair value of liabilities hedged by fair value hedges.
[2] Includes discounting expense related to employee benefits, restructuring provisions and provisions for dismantling.
[3] Includes late payment interests on trade receivables.
[4] Includes impairment losses on trade receivables.
[5] Includes impairment losses on other receivables and non-current assets.

During the 12 months ended 31 December 2010 and 2009 there was no significant ineffectiveness on cash flow hedges and fair value hedges.

Notes to the consolidated financial statements continued

11. Income tax

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Current income tax	420	429
Deferred tax change[1]	(86)	(107)
Less: Deferred tax charged to other comprehensive income	(7)	7
Total income tax	**341**	**315**

[1] Excludes deferred tax change as a result of acquisitions and divestitures of subsidiaries (see Note 4).

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

(in PLN millions)	12 months ended 31 December 2009	12 months ended 31 December 2008
Consolidated net income before tax	449	1,598
Consolidated net income before tax, dispute with DPTG excluded	1,510	1,598
Statutory tax rate	19%	19%
Theoretical tax	287	304
Reassessment of deferred tax asset on dispute with DPTG	31	–
Change in unrecognised deferred tax asset and other	(10)	(14)
Expense not deductible for tax purposes, net	33	25
Effective tax	**341**	**315**

Due to uncertainty related to tax relief on deductible temporary differences on DPTG provision resulting from the statute of limitation, the deferred tax asset has been reassessed and decreased by PLN 31 million as at 31 December 2010.

Expenses not deductible for tax purposes consist of certain cost items, which, under Polish tax law, are specifically determined as non-deductible.

Deferred tax assets are recognized for tax losses carried forward to the extent that realization 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 utilize its own tax losses to offset taxable income in subsequent years. Tax losses are permitted to be utilized over 5 consecutive years with a 50% utilization 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)
2011	39
2012	4
2013	37
2014	47
2015	14
Total	**141**

During the 12 months ended 31 December 2010 and 2009, the Group entities utilized PLN 138 million and PLN 40 million, respectively, of their tax losses previously incurred.

Notes to the consolidated financial statements continued

11. Income tax (continued)

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

(in PLN millions)	Consolidated balance sheet At 31 December 2010	At 31 December 2009 (see Note 3.4)	Consolidated income statement 12 months ended 31 December 2010	12 months ended 31 December 2009
Property, plant and equipment and intangible assets	91	146	55	86
Impairment of financial assets	(69)	(53)	16	(5)
Finance costs, net	11	(21)	(62)	2
Accrued income/expense	(375)	(366)	36	43
Employee benefit plans	(60)	(53)	3	1
Deferred revenue	(161)	(119)	42	7
Tax losses and other differences	(31)	(42)	(11)	(20)
Net deferred tax (assets)/liabilities	**(594)**	**(508)**	**–**	**–**
Deferred tax income/(expense)	**–**	**–**	**79**	**114**

Unrecognized deferred tax asset relates mainly to those tax losses, which are expected to expire rather than to be realized, and temporary differences, which based on the Group's management assessment could not be utilized for tax purposes. As at 31 December 2010 and 2009, deductible temporary differences, for which no deferred tax asset was recognised, amounted to PLN 128 million and PLN 195 million gross, of which PLN 18 million and PLN 168 million, respectively, related to tax losses and PLN 110 million and PLN 27 million, respectively, related to other temporary differences.

12. Components of other comprehensive income

12.1. Cash flow hedges

The change in fair value of cash flow hedges charged to other comprehensive income is presented below:

(in PLN millions)	12 months ended 31 December 2010 Before tax	Tax	After tax	12 months ended 31 December 2009 Before tax	Tax	After tax
Beginning of period	**20**	**(4)**	**16**	**(30)**	**6**	**(24)**
The effective part of gains/(losses) on hedging instrument	(134)	26	(108)	(17)	3	(14)
The amount transferred to the income statement	120	(23)	97	35	(7)	28
The amount transferred to the initial carrying amount of the hedged item	(4)	1	(3)	32	(6)	26
End of period	**2**	**–**	**2**	**20**	**(4)**	**16**

During the 12 months ended 31 December 2010 and 2009, interest income/(expense) on cash flow hedges that were transferred from other comprehensive income and adjusted interest expense on hedged debt amounted to PLN (46) and PLN (22) million, respectively (see Note 10).

During the 12 months ended 31 December 2010 and 2009, foreign exchange gains/(losses) on cash flow hedges that were transferred from other comprehensive income and adjusted foreign exchange differences on hedged debt amounted to PLN (69) and PLN (7) million, respectively (see Note 10).

During the 12 months ended 31 December 2010 and 2009, foreign exchange gains/(losses) on cash flow hedges that were transferred from other comprehensive income and adjusted foreign exchange differences on hedged UMTS licence payables presented under other operating income/expense, amounted to PLN (6) million and PLN (3) million, respectively (see Note 6.3).

During the 12 months ended 31 December 2010 and 2009, foreign exchange gains/(losses) on cash flow hedges that were transferred from other comprehensive income to external purchases and adjusted rental costs amounted to PLN 1 million and PLN (3) million, respectively (see Note 6.1).

During the 12 months ended 31 December and 2010 and 2009, foreign exchange gains/(losses) on cash flow hedges of highly probable forecast transactions that were transferred from other comprehensive income and adjusted the initial carrying amount of property, plant and equipment and inventories amounted to PLN 4 million and PLN (32) million, respectively.

During the 12 months ended 31 December 2010 and 2009, there was no material forecast transaction for which hedge accounting was discontinued as it was no longer expected to occur.

The amounts presented in other comprehensive income as at 31 December 2010 are expected to mature and affect the income statement in the years 2011-2014.

Notes to the consolidated financial statements continued

12. Components of other comprehensive income (continued)

12.2. Actuarial losses on post employment benefits

The change in actuarial losses on post-employment benefits charged to other comprehensive income is presented below:

	12 months ended 31 December 2010			12 months ended 31 December 2009		
(in PLN millions)	Before tax	Tax	After tax	Before tax	Tax	After tax
Beginning of period	**(50)**	**9**	**(41)**	**(36)**	**6**	**(30)**
Actuarial losses on retirement bonuses	(12)	2	(10)	(9)	2	(7)
Actuarial losses on other post-employment benefits	(4)	1	(3)	(5)	1	(4)
End of period	**(66)**	**12**	**(54)**	**(50)**	**9**	**(41)**

13. Goodwill

Goodwill arising from consolidated subsidiaries is as follows:

		At 31 December 2010			At 31 December 2009		
(in PLN millions)	CGU	Cost	Accumulated impairment	Net	Cost	Accumulated impairment	Net
Wirtualna Polska	Internet portal	247	(162)	85	247	(162)	85
PTK Centertel	Mobile network	3,909	–	3,909	3,909	–	3,909
Ramsat	Mobile network	22	–	22	22	–	22
Total goodwill		**4,178**	**(162)**	**4,016**	**4,178**	**(162)**	**4,016**

14. Other intangible assets

	At 31 December 2010			
(in PLN millions)	Cost	Accumulated amortization	Impairment	Net
Telecommunications licenses	2,345	(1,067)	–	1,278
Software	4,757	(3,256)	–	1,501
Other intangibles	168	(73)	(13)	82
Total	**7,270**	**(4,396)**	**(13)**	**2,861**

	At 31 December 2009				At 1 January 2009
(in PLN millions)	Cost	Accumulated amortization	Impairment	Net	Net
Telecommunications licenses	2,345	(921)	–	1,424	1,570
Software	4,186	(2,917)	–	1,269	1,277
Other intangibles	164	(78)	(12)	74	67
Total	**6,695**	**(3,916)**	**(12)**	**2,767**	**2,914**

Movements in the net book value of other intangible assets were as follows:

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Opening balance net of accumulated amortization and impairment	**2,767**	**2,914**
Acquisitions of intangible assets	720	546
Disposals and retirements	(6)	–
Amortization	(618)	(675)
Impairment	(1)	(11)
Reclassifications and other, net	(1)	(7)
Closing balance	**2,861**	**2,767**

Notes to the consolidated financial statements continued

14. Other intangible assets (continued)

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

(in PLN millions)	Acquisition date	Concession term	Acquisition value	Net book value At 31 December 2010	Net book value At 31 December 2009
DCS 1800 Concession	1997	2012	318	41	66
GSM 900 Concession	1999	2014	402	91	116
UMTS Concession	2000	2023	2,495	1,146	1,242
Total telecommunications licenses			**3,215**	**1,278**	**1,424**

15. Property, plant and equipment

(in PLN millions)	At 31 December 2010 Cost	Accumulated depreciation	Impairment	Net
Land and buildings	3,619	(1,374)	(98)	2,147
Networks and terminals	39,963	(26,112)	(4)	13,847
IT equipment	2,119	(1,573)	–	546
Investment grants	(243)	111	–	(132)
Other	415	(316)	(7)	92
Total	**45,873**	**(29,264)**	**(109)**	**16,500**

(in PLN millions)	At 31 December 2009 Cost	Accumulated depreciation	Impairment	Net	At 1 January 2009 Net
Land and buildings	3,627	(1,241)	(93)	2,293	2,416
Networks and terminals	38,725	(23,684)	(12)	15,029	16,401
IT equipment	1,990	(1,504)	–	486	811
Investment grants	(246)	98	–	(148)	(163)
Other	426	(337)	(6)	83	124
Total	**44,522**	**(26,668)**	**(111)**	**17,743**	**19,589**

Investment grants are non-repayable and relate to certain property, plant and equipment received by TP S.A. from Public Telephone Committees (Społeczne Komitety Telefonizacji).

Movements in the net book value of property, plant and equipment were as follows:

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Opening balance net of accumulated depreciation and impairment	**17,743**	**19,589**
Acquisitions of property, plant and equipment	1,996	1,661
Disposals and retirements	(43)	(19)
Depreciation	(3,174)	(3,475)
Impairment	(10)	(22)
Reclassifications and other, net	(12)	9
Closing balance	**16,500**	**17,743**

The carrying value of equipment held under finance leases as at 31 December 2010 and 2009 amounted to PLN 19 million and PLN 22 million, respectively. During the 12 months ended 31 December 2010 and 2009, acquisitions of equipment financed through finance leases amounted to PLN 3 million and PLN 22 million, respectively. Leased assets cannot be sold, donated, transferred by title or pledged and are a collateral for the related finance lease liability.

16. Financial assets

16.1. Assets available for sale

The Group's assets available for sale are presented below:

	At 31 December 2010			At 31 December 2009		
(in PLN millions)	Cost/Fair value	Impairment	Net	Cost/Fair value	Impairment	Net
Main unlisted companies						
Exatel	14	(11)	3	14	(11)	3
Other	2	(1)	1	2	(1)	1
Total assets available for sale	**16**	**(12)**	**4**	**16**	**(12)**	**4**

Financial assets available for sale are measured at historical cost less impairment and mainly comprise shares for which there is no active market and fair value cannot be reliably measured except for the shares in ICO Global Communications (Holdings) Limited which are traded on NASDAQ.

16.2. Loans and receivables excluding trade receivables

The Group's loans and receivables excluding trade receivables are presented below:

	At 31 December 2010			At 31 December 2009		
(in PLN millions)	Cost	Impairment	Net	Cost	Impairment	Net
Finance lease receivables	17	–	17	19	–	19
Long-term deposits	12	–	12	–	–	–
Other	3	–	3	5	–	5
Total loans and receivables excluding trade receivables	**32**	**–**	**32**	**24**	**–**	**24**
Current	10	–	10	13	–	13
Non-current	22	–	22	11	–	11

The Group's maximum exposure to credit risk is represented by the carrying amounts of loans and receivables.

16.3. Financial assets at fair value through profit or loss

The Group's assets at fair value through profit or loss are presented below:

	Fair value	
(in PLN millions)	At 31 December 2010	At 31 December 2009
Derivatives – held for trading [1]	71	62
Marketable securities – held for trading [1]	9	9
Total financial assets at fair value through profit or loss	**80**	**71**
Current	28	9
Non-current	52	62

[1] Included in net financial debt calculation (see Note 19).

The Group's maximum exposure to credit risk is represented by the carrying amounts of derivatives. The Group enters into derivatives contracts with leading financial institutions. Limits are applied to monitor the level of exposure on the financial counterparties. In case the counterparty's financial soundness is deteriorating, the Group applies the appropriate measures mitigating the default risk.

16. Financial assets (continued)

16.4. Financial assets measured at fair value

The following tables provide an analysis of the Group's financial assets that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable (see Note 3.5.12).

	At 31 December 2010			
	Fair value measurement			
(in PLN millions)	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss	9	71	–	80
Derivatives – held for trading	–	71	–	71
Marketable securities – held for trading	9	–	–	9
Hedging derivatives	–	51	–	51
Total	**9**	**122**	**–**	**131**

	At 31 December 2009			
	Fair value measurement			
(in PLN millions)	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss	9	62	–	71
Derivatives – held for trading	–	62	–	62
Marketable securities – held for trading	9	–	–	9
Hedging derivatives	–	57	–	57
Total	**9**	**119**	**–**	**128**

During the 12 months ended 31 December 2010 and 2009, there was no transfer between Level 1 and Level 2 fair value measurements, and no transfer into and out of Level 3 fair value measurement.

17.Trade receivables, other assets and prepaid expenses

(in PLN millions)	At 31 December 2010	At 31 December 2009
Trade receivables (net of impairment) [(1), (3)]	**1,637**	**1,475**
VAT receivables	105	39
Other taxes receivables	34	3
Employee-related receivables	2	2
Other [(2)]	125	75
Other assets [(1)]	**266**	**119**
Inactivated mobile phones and terminals in the external dealership network	55	61
Other prepaid expenses	39	39
Prepaid expenses	**94**	**100**

[(1)] Additions to impairment of trade and other receivables (net of reversals) are presented in Note 6.3.
[(2)] Mainly includes receivables related to: advances and prepayments to suppliers, sales of fixed assets, reinvoicing cost of advertising and promotion, compensations and penalties.
[(3)] Classified as loans and receivables under IAS 39.

The Group considers there is no concentration of credit risk with respect to trade receivables due to its large and diverse customer base consisting of individual and business customers.

The Group's maximum exposure to credit risk at the reporting date is best represented by the carrying amounts of those instruments recognised in the balance sheet. The Group holds the following collaterals: bank guarantees, trade credit insurances, sureties, blocking of funds in a bank account.

Movement in the impairment of trade, employee-related and other receivables in the 12 months ended 31 December 2010 and 2009 is presented below:

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Beginning of period	**298**	**323**
Net change in impairment	48	(25)
End of period	**346**	**298**

In the 12 months ended 31 December 2010 and 2009, impaired receivables written off amounted to PLN 187 million and PLN 250 million, respectively.

17.Trade receivables, other assets and prepaid expenses (continued)

As at 31 December 2010 and 2009, the analysis of trade receivables that are past due but not impaired is as follows:

At 31 December 2010:

(in PLN millions)	Carrying amount	Neither impaired nor past due	Past due in the following periods Less than 180 days	Between 180 and 360 days	More than 360 days
Trade receivables – collectively analysed for impairment	1,612	1,085	464	51	12
Trade receivables – individually analysed for impairment	25				
Total trade receivables, net	**1,637**				

At 31 December 2009:

(in PLN millions)	Carrying amount	Neither impaired nor past due	Past due in the following periods Less than 180 days	Between 180 and 360 days	More than 360 days
Trade receivables – collectively analysed for impairment	1,463	858	526	51	28
Trade receivables – individually analysed for impairment	12				
Total trade receivables, net	**1,475**				

18. Cash and cash equivalents

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

(in PLN millions)	At 31 December 2010	At 31 December 2009
Cash on hand	1	–
Current bank accounts and overnight deposits	296	324
Deposits up to 3 months	1,839	1,022
Securities with a maturity up to 3 months	311	872
Total cash and cash equivalents [(1)]	**2,447**	**2,218**

[(1)] Classified as loans and receivables under IAS 39.

The Group's cash surplus is invested into short-term highly-liquid financial instruments e.g. bank deposits and T-bills. The term of the investments depends on the immediate cash requirements of the Group. Short term deposits are made for varying periods of between one day and three months. The instruments earn interest which depends on the current money market rates and the term of investment.

As at 31 December 2010 and 2009, cash and cash equivalents included an equivalent of PLN 18 million and PLN 52 million, respectively, denominated in foreign currencies.

The Group's maximum exposure to credit risk at the reporting date is best represented by carrying amounts of cash and cash equivalents. The Group deposits its cash and cash equivalents with leading financial institutions with investment grade. Limits are applied to monitor the level of exposure on the financial counterparties. In case the counterparty's financial soundness is deteriorating, the Group applies the appropriate measures mitigating the default risk.

19. Net financial debt

19.1.Analysis of net financial debt by composition and maturity

Net financial debt corresponds to the total gross financial debt (converted at the period-end exchange rate), after net derivative instruments (liabilities less assets) classified as at fair value through profit or loss, cash flow hedges and fair value hedges, less cash and cash equivalents, marketable securities and including the impact of the effective portion of cash flow hedges.

The maturity analysis of the Group's financial liabilities is based on contractual undiscounted payments. As at 31 December 2010 and 2009 amounts in foreign currency were translated at the NBP period-end exchange rates. The variable interest payments arising from the financial instruments were calculated using the latest interest rates fixed before 31 December 2010 and 2009, respectively. Financial liabilities that can be repaid at any time at the Group's discretion are classified as current or non-current, depending on the expected repayment date; non-current balance is assigned to the period of the final contractual maturity date.

The table below provides a breakdown of net financial debt by category and maturity analysis of financial liabilities based on contractual undiscounted cash flows:

Notes to the consolidated financial statements continued

19. Net financial debt (continued)

At 31 December 2010:

(in PLN millions)	Note	Carrying amount	Undiscounted contractual cash flows [(1)] Within 1 year	Non-current 1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years	Total non-current	Total
Trade payables (excl. UMTS) (A)	**28**	**3,099**	**3,099**	**–**	**–**	**–**	**–**	**–**	**–**	**3,099**
UMTS license payables (B)	**28**	**808**	**59**	**59**	**59**	**111**	**111**	**788**	**1,128**	**1,187**
Bonds	20	4,118	1,410	167	167	2,939	–	–	3,273	4,683
Bank borrowings	20	1,867	287	691	951	39	38	25	1,744	2,031
Finance lease liabilities		18	7	7	3	3	–	–	13	20
Financial liabilities at amortized cost [(2)]		**6,003**	**1,704**	**865**	**1,121**	**2,981**	**38**	**25**	**5,030**	**6,734**
Derivatives – net [(3)]	21	268	166	64	62	293	–	–	419	585
Gross financial debt after derivatives (C)		**6,271**	**1,870**	**929**	**1,183**	**3,274**	**38**	**25**	**5,449**	**7,319**
Total financial liabilities (A) + (B) + (C)		**10,178**	**5,028**	**988**	**1,242**	**3,385**	**149**	**813**	**6,577**	**11,605**
Marketable securities	16	9								
Cash and cash equivalents	18	2,447								
Sub-total (D)		**2,456**								
Effective portion of cash flow hedges (E)		2								
Net financial debt (C)-(D)+(E)		**3,817**								

[(1)] Includes both nominal and interest payments.
[(2)] Excluding trade payables and UMTS license payables.
[(3)] Both assets and liabilities are included.

At 31 December 2009:

(in PLN millions)	Note	Carrying amount	Undiscounted contractual cash flows [(1)] Within 1 year	Non-current 1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years	Total non-current	Total
Trade payables (excl. UMTS) (A)	**28**	**2,418**	**2,418**	**–**	**–**	**–**	**–**	**–**	**–**	**2,418**
UMTS license payables (B)	**28**	**849**	**62**	**62**	**62**	**62**	**115**	**931**	**1,232**	**1,294**
Bonds	20	4,259	228	1,461	172	172	3,048	–	4,853	5,081
Bank borrowings	20	2,128	302	297	700	953	40	64	2,054	2,356
Finance lease liabilities		21	6	6	6	3	2	–	17	23
Financial liabilities at amortized cost [(2)]		**6,408**	**536**	**1,764**	**878**	**1,128**	**3,090**	**64**	**6,924**	**7,460**
Derivatives – net [(3)]	21	181	190	90	55	54	173	–	372	562
Gross financial debt after derivatives (C)		**6,589**	**726**	**1,854**	**933**	**1,182**	**3,263**	**64**	**7,296**	**8,022**
Total financial liabilities (A) + (B) + (C)		**9,856**	**3,206**	**1,916**	**995**	**1,244**	**3,378**	**995**	**8,528**	**11,734**
Marketable securities	16	9								
Cash and cash equivalents	18	2,218								
Sub-total (D)		**2,227**								
Effective portion of cash flow hedges (E)		20								
Net financial debt (C)-(D)+(E)		**4,382**								

[(1)] Includes both nominal and interest payments.
[(2)] Excluding trade payables and UMTS license payables.
[(3)] Both assets and liabilities are included.

As at 31 December 2010 and 2009, most of the Group's trade payables mature within 3 months.

Notes to the consolidated financial statements continued

19. Net financial debt (continued)

19.2. Analysis of net financial debt by currency

	At 31 December 2010				
(equivalent value in PLN millions at the period-end exchange rate)	PLN	EUR	USD	GBP	Total
Net financial debt by currency	(677)[1]	4,453	42	(1)	3,817
Impact of derivatives notional amount	6,867	(6,769)	(98)	–	–
Net financial debt by currency after impact of derivatives notional amount	**6,190**	**(2,316)**	**(56)**	**(1)**	**3,817**

[1] Including market value of derivatives.

	At 31 December 2009				
(equivalent value in PLN millions at the period-end exchange rate)	PLN	EUR	USD	GBP	Total
Net financial debt by currency	(415)[1]	4,760	38	(1)	4,382
Impact of derivatives notional amount	6,934	(6,823)	(111)	–	–
Net financial debt by currency after impact of derivatives notional amount	**6,519**	**(2,063)**	**(73)**	**(1)**	**4,382**

[1] Including market value of derivatives.

20.Financial liabilities at amortised cost excluding trade payables

20.1. Bonds

The table below provides an analysis of 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 2010	31 December 2009
TPSA Eurofinance France S.A.	T	300 EUR	4.625%	5 July 2004	5 July 2011	1,214	1,258
TPSA Eurofinance France S.A	A1	500 EUR	6.000%	22 May 2009	22 May 2014	2,042	2,115
TPSA Eurofinance France S.A	A2	200 EUR	6.000%	17 July 2009	22 May 2014	862	886
Total bonds issued by the Group						**4,118**	**4,259**
Current						1,315	132
Non-current						2,803	4,127

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

The weighted average effective interest rate on the Group's bonds, before swaps, amounted to 5.41% as at 31 December 2010 and 2009.

20.Financial liabilities at amortised cost excluding trade payables (continued)

20.2. Bank borrowings

The table below provides an analysis of bank borrowings by creditor:

Creditor	Interest rate as at 31 December 2010	Repayment date	Amount outstanding at [1] 31 December 2010 Currency (millions)	31 December 2010 PLN (millions)	31 December 2009 Currency (millions)	31 December 2009 PLN (millions)
Floating rate						
European Investment Bank	1.71% [2]	15 December 2015	42 EUR	165	50 EUR	206
European Investment Bank	1.16% [2]	15 June 2012	50 EUR	197	83 EUR	343
European Investment Bank	4.04% [2]	15 June 2012	78 PLN	78	130 PLN	130
European Investment Bank	3.90%-4.29% [2,3]	17 September 2012 - 15 September 2013	1,398 PLN	1,398	1,399 PLN	1,399
Bayern LandesBank (syndicated)	–	20 February 2011	–	–	(1) PLN [4]	(1)
Bank Handlowy (syndicated)	–	18 April 2010	–	–	(1) PLN [4]	(1)
Bank Handlowy (syndicated)	–	22 October 2015	(11) PLN [4]	(11)	–	–
Bank Handlowy (syndicated)	–	18 April 2013	(8) PLN [4]	(8)	–	–
Other credit lines	–	–	1 PLN	1	3 PLN	3
Fixed rate						
Instituto de Credito Oficial	1.25%	2 January 2021	16 USD	47	17 USD	49
Total bank borrowings borrowed by the Group				**1,867**		**2,128**
Current				227		238
Non-current				1,640		1,890

[1] Includes accrued interest and bank borrowings issue costs.
[2] Floating rate determined by the bank every three months.
[3] Floating rate determined by the bank individually for every drawing.
[4] Paid arrangement fees.

The weighted average effective interest rate on the Group's bank borrowings, before swaps, amounted to 3.54% as at 31 December 2010 and 3.49% as at 31 December 2009.

21. Derivatives

As at 31 December 2010 and 2009, the majority of the Group's derivatives portfolio constitutes financial instruments for which there is no active market (over-the-counter derivatives) i.e. the interest rate and currency swaps. To price these instruments the Group applies standard valuation techniques, where the prevailing market zero-coupon curves constitute the base for calculation of discounting factors. A fair value of swap transaction represents a discounted future cash flows converted into PLN at the period-end exchange rate.

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

Type of instrument[1]	Hedged risk	Hedged nominal amount (in millions of currency)	Maturity	Fair value[4] (in PLN millions)	
				Financial Asset	Financial Liability
		At 31 December 2010			
Derivative instruments – fair value hedge					
CCIRS	Currency and interest rate risk	180 EUR	2011-2014	–	(31)
CCS	Currency risk	10 EUR	2011	–	(1)
IRS	Interest rate risk	180 EUR	2014	35	–
Total of fair value hedges				35	(32)
Derivative instruments – cash flow hedge					
CCIRS	Currency and interest rate risk	303 EUR	2014	–	(109)
CCS	Currency risk	184 PLN	2011-2014	5	(47)
NDF	Currency risk	4 USD	2011	1	–
IRS	Interest rate risk	53 EUR	2014	10	–
IRS	Interest rate risk	1,419 PLN	2012-2014	–	(57)
Total of cash flow hedges				16	(213)
Derivative instruments – held for trading					
CCIRS	Currency and interest rate risk	314 EUR	2011-2014	25	(82)
NDF	Currency risk	668 EUR	2011	2	(28)
NDF	Currency risk	29 USD	2011	0	(6)
FX option	Currency risk	50 EUR	2011	3	(5)
IRS	Interest rate risk	217 EUR	2014	41	–
IRS	Interest rate risk	1,089 PLN	2011-2014	–	(24)
Total of derivatives held for trading				71	(145)
Total of derivative instruments				**122**	**(390)**
Current				20	(109)
Non–current				102	(281)

[1] CCIRS – cross currency interest rate swap, CCS – cross currency swap, IRS – interest rate swap, NDF – non-deliverable forward, FWD – forward.
[2] Value 0 or (0) represents an asset or a liability below PLN 500 thousand, respectively.

21. Derivatives (continued)

Type of instrument [1]	Hedged risk	Hedged nominal amount (in millions of currency)	Maturity	Fair value [4] (in PLN millions) Financial Asset	Financial Liability
		At 31 December 2009			
Derivative instruments – fair value hedge					
CCIRS	Currency and interest rate risk	180 EUR	2011-2014	6	(4)
CCS	Currency risk	10 EUR	2011	1	–
IRS	Interest rate risk	180 EUR	2014	20	–
Total of fair value hedges				27	(4)
Derivative instruments – cash flow hedge					
CCIRS	Currency and interest rate risk	303 EUR	2014	–	(78)
CCS	Currency risk	205 EUR	2011-2014	22	(32)
NDF	Currency risk	66 EUR	2010	1	(2)
NDF	Currency risk	10 USD	2010	1	–
IRS	Interest rate risk	53 EUR	2014	6	–
IRS	Interest rate risk	1,471 PLN	2012-2014	–	(34)
Total of cash flow hedges				30	(146)
Derivative instruments – held for trading	Currency and interest rate risk	314 EUR	2011-2014	25	(82)
CCIRS	Currency and interest rate risk	285 EUR	2011-2014	38	(41)
NDF	Currency risk	612 EUR	2010	0	(80)
NDF	Currency risk	29 USD	2010	–	(6)
IRS	Interest rate risk	217 EUR	2014	24	–
IRS	Interest rate risk	1,259 PLN	2010-2014	–	(23)
Total of derivatives held for trading				62	(150)
Total of derivative instruments				**119**	**(300)**
Current				2	(91)
Non–current				117	(209)

[1] CCIRS – cross currency interest rate swap, CCS – cross currency swap, IRS – interest rate swap, NDF – non-deliverable forward, FWD – forward.
[2] Value 0 or (0) represents an asset or a liability below PLN 500 thousand, respectively.

The Group's maximum exposure to credit risk is represented by the carrying amounts of derivatives. The Group enters into derivatives contracts with leading financial institutions. Limits are applied to monitor the level of exposure on the financial counterparties. In case the counterparty's financial soundness is deteriorating, the Group applies the appropriate measures mitigating the default risk.

The following tables provide an analysis of the Group's financial liabilities that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable (see Note 3.5.12).

	At 31 December 2010			
	Fair value measurement			
(in PLN millions)	Level 1	Level 2	Level 3	Total
Financial liabilities at fair value through profit or loss	–	145	–	145
Derivatives – held for trading	–	145	–	145
Hedging derivatives	–	245	–	245
Total	**–**	**390**	**–**	**390**

	At 31 December 2009			
	Fair value measurement			
(in PLN millions)	Level 1	Level 2	Level 3	Total
Financial liabilities at fair value through profit or loss	–	150	–	150
Derivatives – held for trading	–	150	–	150
Hedging derivatives	–	150	–	150
Total	**–**	**300**	**–**	**300**

21. Derivatives (continued)

During 12 months ended 31 December 2009 and 2008, there was no transfer between Level 1 and Level 2 fair value measurements, and no transfer into and out of Level 3 fair value measurement.

22.Objectives and policies of financial risk management

22.1. Principles of financial risk management

The Group is exposed to some risks arising mainly from financial instruments that are issued and held as part of its operating and financing activities. That exposure can be principally classified as market risk (encompassing currency risk and interest rate risk), liquidity risk and credit risk. The Group manages the financial risks with the objective to limit its exposure to adverse changes in foreign exchange rates and interest rates, to stabilize cash flows and to ensure an adequate level of financial liquidity and flexibility.

The principles of the Group Financial Risk Management Policy have been approved by the Management Board. Operationally, financial risk management is conducted by TP Group Corporate Finance according to developed strategies confirmed by the Treasury Committee under the direct control of the Chief Financial Officer.

Group Financial Risk Management Policy defines principles and responsibilities within the context of an overall financial risk management and covers the following areas:

– risk measures used to identify and evaluate the exposure to financial risks,
– selection of appropriate instruments to hedge against identified risks,
– valuation methodology used to determine the fair value of derivatives,
– methods for testing hedging effectiveness for accounting purposes,
– transaction limits for and credit ratings of the leading financial institutions with which the Group concludes hedging transactions.

22.2. Hedge accounting

The Group has entered into numerous derivative transactions to hedge exposure to currency risk and interest rate risk. The derivatives used by the Group include: cross currency interest rate swaps, cross currency swaps, interest rate swaps, currency options, currency forwards and non-deliverable forwards.

Certain derivative instruments are classified as fair value hedges or cash flow hedges and the Group applies hedge accounting principles as stated in IAS 39 (see Note 3.5.12). The fair value hedges are used for hedging changes in the fair value of financial instruments that are attributable to particular risk and could affect the income statement. Cash flow hedges are used to hedge the variability of future cash flows that is attributable to particular risk and could affect the income statement.

Derivatives are used for hedging activities and it is the Group's policy that the derivative financial instruments are not used for trading (speculative) purposes. However, certain derivatives held by the Group are classified as held for trading as they do not fulfil all requirements of hedge accounting as set out in IAS 39 and hedge accounting principles are not applied to those instruments. The Group considers those derivative instruments as economic hedges because they, in substance, protect the Group against currency risk and interest rate risk.

Detailed information on derivative financial instruments, including hedging relationship, that are used by the Group is presented in Note 21.

22.3. Currency risk

The Group is exposed to foreign exchange risk arising from financial liabilities denominated in foreign currencies, namely bonds and bank borrowings denominated in EUR and USD (see Note 20) and trade receivables, trade payables and provisions of which a significant balance relates to the UMTS license payable denominated in EUR (see Note 19 and Note 28) and the dispute with DPTG.

The Group's hedging policy, minimizing the impact of fluctuations in exchange rates, is set on a regular basis. The acceptable exposure to a selected currency is a result of the risk analysis in relation to an open position in that currency, given the financial markets' expectations of foreign exchange rates movements during a specific time horizon.

Within the scope of the given hedging policy, the Group hedges its exposure entering mainly into cross currency swaps, cross currency interest rate swaps and forward currency contracts, under which the Group agrees to exchange a notional amount denominated in a foreign currency into PLN. As a result, the gains/losses generated by derivative instruments compensate the foreign exchange losses/gains on the hedged items. Therefore, the variability of the foreign exchange rates has a limited impact on the consolidated income statement, as well as consolidated other comprehensive income.

As at 31 December 2010, 99.8% (as at 31 December 2009, 99.9%) of the outstanding balance of bonds and bank borrowings denominated in foreign currencies were hedged against currency risk by use of derivative instruments. As at 31 December 2010 and 2009, 57% of the outstanding nominal amount of the UMTS license payable was hedged against currency risk. As at 31 December 2010, 75% (as at 31 December 2009, 100%) of the nominal amount of DPTG provision was hedged against currency risk.

The Group is also actively hedging the exposure to foreign exchange risk generated by operating and capital expenditures.

The Group uses the sensitivity analysis described below to measure currency risk.

The Group's major exposures to foreign exchange risk (net of hedging activities) and potential foreign exchange gains/losses on these exposures resulting from a hypothetical 10% appreciation/depreciation of the PLN against other currencies are presented in the following table.

Notes to the consolidated financial statements continued

22.Objectives and policies of financial risk management (continued)

22.3. Currency risk (continued)

(in millions of currency)	Effective exposure after hedging impacting consolidated income statement				Sensitivity to a change of the PLN against other currencies			
Hedged item	31 December 2010		31 December 2009		31 December 2010		31 December 2009	
					+10%	-10%	+10%	-10%
	Currency	PLN	Currency	PLN	PLN		PLN	
Bonds and bank borrowings (EUR)	–	–	–	–	–	–	–	–
Bonds and bank borrowings (USD)	3	9	2	6	1	(1)	1	(1)
UMTS license payable (EUR)	129	511	135	555	51	(51)	56	(56)
DPTG provision (EUR) (1)	136	539	–	–	54	(54)	–	–
Total		**1,059**		**561**	**106**	**(106)**	**57**	**(57)**

(1) Potential settlement would be made in DKK.

The sensitivity analysis presented above is based on the following principles:

– unhedged portion of the notional amount of liabilities (including the UMTS license) is exposed to foreign exchange risk (effective exposure),
– derivatives satisfying hedge accounting requirements and those classified as economic hedges are treated as risk-mitigation transactions,
– cash and cash equivalents are excluded from the analysis.

The changes in fair value of derivatives classified as cash flow hedges of forecast transactions affect consolidated other comprehensive income. The potential foreign exchange gains/losses on these hedges resulting from a hypothetical 10% appreciation/depreciation of the PLN against other currencies are as follows:

(in millions of PLN)	Sensitivity of fair value of cash flow hedges to a change of the PLN against other currencies			
Hedged item	At 31 December 2010		At 31 December 2009	
	+10%	-10%	+10%	-10%
	PLN		PLN	
Commercial transactions (EUR)	–	–	(27)	27
Commercial transactions (USD)	(1)	1	(3)	3
Total amount impacting other comprehensive income	**(1)**	**1**	**(30)**	**30**

22.4. Interest rate risk

The interest rate risk is a risk that the fair value or future cash flows of the financial instrument will change due to interest rates changes. The Group has interest bearing financial liabilities consisting mainly of bonds and bank borrowings (see Note 20).

The Group's interest rate hedging policy limiting exposure to unfavourable movements of interest rates is set on a regular basis. The preferable split between fixed and floating rate debt is the result of the analysis indicating the impact of the potential interest rates evolution on the financial costs.

According to the given hedging strategy, the Group uses interest rate swaps and cross currency interest rate swaps to hedge its interest rate risk. As a result of the hedge, the structure of the liabilities changes to the desired one, as liabilities based on the floating/fixed interest rates are effectively converted into fixed/floating obligations.

As at 31 December 2010 and 2009, the Group's proportion between fixed/floating rate debt (including hedging activities) was 47/53% and 46/54%, respectively.

The Group uses the sensitivity analysis described below to measure interest rate risk.

The table below provides the Group's exposures to interest rate risk (net of hedging activities) assuming a hypothetical decrease/increase in the interest rates by 1 percent.

(in PLN millions)	Potential increase /(decrease) in value resulting from 1% change of interest rates			
	At 31 December 2010		At 31 December 2009	
	+1%	-1%	+1%	-1%
Finance costs, net	53	(53)	63	(64)
Other comprehensive income	3	(4)	2	(2)
Fair value of gross financial debt after derivatives	(62)	62	(88)	88

The sensitivity analysis presented above is based on the following principles:

– finance costs, net include the following items exposed to interest rate risk: a) interest cost on financial debt based on floating rate, after derivatives classified as hedges for accounting purpose and b) the change in the fair value of derivatives that do not qualify for hedge accounting,
– the effective portion of the change in the fair value of derivatives classified as cash flow hedges is recognized directly in other comprehensive income,
– as at 31 December 2010, the fair value of gross financial debt after derivatives (excluding finance lease and arrangement fees) was PLN 6,382 million (as at 31 December 2009, PLN 6,705 million).

22.Objectives and policies of financial risk management (continued)

22.5. Liquidity risk

The liquidity risk is a risk of encountering difficulties in meeting obligations associated with financial liabilities. The Group's liquidity risk management involves forecasting future cash flows, analysing the level of liquid assets in relation to cash flows, monitoring balance sheet liquidity and maintaining a diverse range of funding sources and back-up facilities.

In order to increase efficiency, the liquidity management process is optimised through a centralised treasury function of the Group, as liquid asset surpluses generated by entities constituting the Group are invested and managed by the central treasury. The Group's cash surplus is invested into short-term highly-liquid financial instruments e.g. bank deposits and T-bills.

The Group also manages liquidity risk by maintaining committed, unused credit facilities, which create a liquidity reserve to secure solvency and financial flexibility. As at 31 December 2010, the Group had the following unused credit facilities amounting to PLN 3,605 million (as at 31 December 2009, PLN 5,801 million):

– PLN 2,021 million of the credit lines,
– EUR 400 million of back-up credit facility.

Liquidity risk is measured by applying following ratios calculated and monitored by the Group regularly:

– liquidity ratios,
– maturity analysis of undiscounted contractual cash flows resulting from the Group's financial liabilities,
– average debt duration.

The liquidity ratio, which represents the relation between available financing sources (i.e. cash, cash collateral and credit facilities) and debt repayments during next 12 and 18 months is presented in the following table.

(in PLN millions)	Liquidity ratios	
	At 31 December 2010	At 31 December 2009
Liquidity ratio – next 12 months (%)	429%	3,517%
Unused credit facilities	3,605	5,801
Cash and cash equivalents	2,447	2,218
Debt repayments [(1)]	1,410	228
Liquidity ratio (incl. cash collaterals and derivatives) – next 12 months (%)	384%	1,918%
Derivatives [(2)]	166	190
Cash collateral paid	–	–
Liquidity ratio – next 18 months (%)	398%	2,345%
Unused credit facilities	3,605	5,801
Cash and cash equivalents	2,447	2,218
Debt repayments [(1)]	1,521	342
Liquidity ratio (incl. cash collaterals and derivatives) – next 18 months (%)	355%	1,399%
Derivatives [(2)]	185	231
Cash collateral paid	–	–

(1) Undiscounted principal payments on debt.
(2) Undiscounted net cash flows on derivatives; negative/positive amount represents positive/negative net result on cash flows.

The maturity analysis for the remaining contractual undiscounted cash flows resulting from the Group's financial liabilities as at 31 December 2010 and 2009 is presented in Note 19. The average duration for the existing debt portfolio as at 31 December 2010 is 2.4 years (as at 31 December 2009, 3.3 years).

22.6. Credit risk

The Group's credit risk management objective is defined as supporting business growth while minimizing financial risks by ensuring that customers and partners are always in a position to pay amounts due to the Group.

The main function of the Credit Committee under the control of the Chief Financial Officer is to coordinate and consolidate credit risk management activities across the Group, which involve:

– clients' risk assessment,
– monitoring clients' business and financial standing,
– managing accounts receivable and bad debts.

The policies and rules regarding consolidated credit risk management for the Group were approved by the Credit Committee.

The credit risk management functions were consolidated in 2010 with a dedicated organizational structure developed within TP Group Corporate Finance.

There is no significant concentration of credit risk within the Group.

Further information on credit risk is discussed in Notes 16, 17, 18 and 21.

22. Objectives and policies of financial risk management (continued)

22.7. Price risk

Pursuant to the Polish telecommunication law, prices for telecommunication services should be based on transparent and objective criteria.

In case of operators which are SMPs, UKE determines requirements for regulatory accounting and calculation of costs of telecommunication services. Fees for services provided on the relevant markets in which TP S.A., PTK–Centertel or TP EmiTel is a SMP must be approved by UKE before they become binding.

Cost calculations of wholesale services, which are provided based on regulatory obligations, are subject to examination and approval by UKE. If fees proposed by the operator, which is a SMP, are assessed as not in conformity with relevant regulations, UKE may change these fees.

The President of UKE declared in Memorandum of Understanding (see Note 30.1 c) that wholesale rates for regulated services, and for Bitstream Access (under certain conditions), will be maintained at unchanged levels until the end of 2012.

Retail prices for services provided on the relevant retail markets where TP S.A. is a SMP and under universal service obligation are subject to UKE acceptance. TP S.A. may launch promotions and price changes which have not been objected to by the President of UKE. Moreover, the retail price increases should be announced with at least one settlement period in advance.

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

22.8. Management of covenants

As at 31 December 2010, TP S.A. was a party to loan and guarantee agreements containing financial covenant, upon which the Group should meet the following financial ratio: Net Debt/EBITDA to be no higher than 3.5:1 confirmed on a semi-annual basis. As at 31 December 2010, the covenant was met.

As at 31 December 2009, the Group had no credit facilities or borrowings subject to specific covenants with regard to financial ratios.

23. Management of capital

The Group manages its capital through a balanced financial policy, which aims at providing both relevant funding capabilities for business development and at securing a relevant financial structure and liquidity.

The Group's capital management policy takes into consideration three key elements:

– business performance together with applicable investments and development plans,
– cash distribution policy and debt repayment schedule,
– the Group's rating and financial market environment.

In order to combine these factors the Group periodically establishes a framework for the financial structure. The current Group's objectives in that area are the following:

– Net Gearing ratio – maximum at the range of 35% – 40%,
– Net financial debt to EBITDA ratio – remaining below 1.5

The table below provides the capital ratios as at 31 December 2010 and 2009 and presents the sources of capital involved in their calculation. The Group regards capital as the total of equity and net financial debt.

(in PLN millions)	At 31 December 2010	At 31 December 2009
Interest bearing bonds and bank borrowings and finance lease	6,003	6,408
Cash and cash equivalents	2,447	2,218
Marketable securities	9	9
Net financial debt before hedging	3,547	4,181
Derivatives [(1)]	270	201
Net financial debt	3,817	4,382
Equity	14,634	16,553
Equity and Net financial debt before hedging	18,181	20,734
Equity and Net financial debt	18,451	20,935
EBITDA [(2)]	5,772	6,280
Net Gearing before hedging ratio [(3)]	19.5%	20.2%
Net Gearing ratio [(4)]	20.7%	20.9%
Net financial debt before hedging/EBITDA ratio	0.6	0.7
Net financial debt/EBITDA ratio	0.7	0.7

[(1)] Marked-To-Market valuation of derivative portfolio (excluding effective portion of cash flow hedges).
[(2)] Dispute with DPTG is excluded from EBITDA, because it does not relate to the Group's current operations.
[(3)] Net Gearing before hedging = Net financial debt before hedging/(Net financial debt before hedging + Equity).
[(4)] Net Gearing = Net financial debt/(Net financial debt + Equity).

The above policy imposes financial discipline, providing appropriate flexibility needed to sustain profitable development and the Group's cash distribution policy as set on an annual basis with a focus on delivering an attractive remuneration to the Group's shareholders. There are no external capital requirements imposed on the Group.

Notes to the consolidated financial statements continued

24. Fair value of financial instruments

As at 31 December 2010 and 2009, the carrying amount of cash and cash equivalents, current trade receivables and trade payables, current loans and receivables and current financial liabilities at amortised cost approximates their fair value due to relatively short term maturity of those instruments or cash nature.

As at 31 December 2010 and 2009, the carrying amount of financial liabilities at amortised cost which bear variable interest rates approximates their fair value.

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

(in PLN millions)	At 31 December 2010		At 31 December 2009	
	Carrying amount[1]	Estimated fair value	Carrying amount[1]	Estimated fair value
Bonds with fixed interest rate	4,118	4,232	4,259	4,403
Bank borrowings with fixed interest rate	47	42	49	42
UMTS license payables	808	870	849	899
Total	**4,973**	**5,144**	**5,157**	**5,344**

[1] Carrying amount includes accrued interest.

The fair value of financial instruments is calculated by discounting expected future cash flows at the prevailing zero coupon rate. In order to obtain all the necessary zero coupon rates, a theoretical zero coupon curve is constructed for each currency. Such a curve is derived from the SWAP rate curve adjusted by adding the prevailing credit spread for the debt issued by a telecom company with the same rating as the Group has. All the fair value amounts are translated to PLN at the National Bank of Poland period-end exchange rate.

25. Employee benefits

(in PLN millions)	At 31 December 2010	At 31 December 2009 (see Note 3.4)
Jubilee awards	162	151
Retirement bonuses and other post-employment benefits	198	176
Salaries, other employee-related payables and payroll taxes due	248	258
Total carrying value of employee benefit obligations	**608**	**585**
Current	266	302
Non-current	342	283

Certain employees and retirees of the Group are entitled to long-term employee benefits in accordance with the Group's remuneration policy (see Note 3.5.16). These benefits are not funded. The changes in the present value of liabilities related to employee benefits for the 12 months ended 31 December 2010 and 2009 are detailed in the table below:

	12 months ended 31 December 2010				12 months ended 31December 2009 (see Note 3.4)			
(in PLN millions)	Jubilee awards	Retirement bonuses	Other post-employment benefits	Total	Jubilee awards	Retirement bonuses	Other post-employment benefits	Total
Present/carrying value of obligation at the beginning of the period	**151**	**103**	**73**	**327**	**152**	**87**	**78**	**333**
Current service cost[1]	9	6	1	16	9	7	1	17
Interest cost[2]	8	6	4	18	7	5	4	16
Benefits paid	(26)	(3)	(8)	(37)	(36)	(5)	(8)	(49)
Actuarial losses for the period	20[1]	12[3]	4[3]	36	19[1]	9[3]	5[3]	33
Curtailment[1]	–	–	–	–	–	–	(23)[4]	(23)
Present/carrying value of obligation at the end of the period	**162**	**124**	**74**	**360**	**151**	**103**	**73**	**327**

[1] Recognised under labour expense in the consolidated income statement.
[2] Recognised under discounting expense in the consolidated income statement.
[3] Recognised under actuarial losses on post-employment benefits in the consolidated statement of comprehensive income.
[4] Curtailment of medical care provided to some of the Group's retired employees following the disposal of the Group's shareholding in TP Med Sp. z o.o (see Note 4).

25. Employee benefits (continued)

The valuation of obligations as at 31 December 2010 and 2009 was performed using the following assumptions:

	At 31 December 2010	At 31 December 2009
Discount rate	6%	6.1%
Wage increase rate	3%	3%
Expected average remaining working lives (in years)	9.3 – 21.5	12.6 – 22.9

Present value of defined benefit obligation for the current period and previous four annual periods is presented below:

(in PLN millions)	Jubilee awards	Retirement bonuses	Other post-employment benefits	Total
As at				
31 December 2010	162	124	74	360
31 December 2009	151	103	73	327
31 December 2008	152	87	94	333
31 December 2007	167	91	78	336
31 December 2006	177	85	80	342

26. Share-based payments

26.1. Group incentive programme

On 28 April 2006, the General Meeting of Shareholders of TP S.A. approved an incentive programme ("the Program") for the key managers and executives ("the Beneficiaries") of Telekomunikacja Polska and its selected subsidiaries in order to further motivate management in their efforts aimed at the Group development and the Company's value maximisation. On 12 December 2006, the Management Board of TP S.A adopted the Incentive Programme Rules for the members of the Management Board and the key managers of the Group. In order to fulfil the assumptions of the Program 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.

As a result of the Program, on 9 October 2007 TP S.A. issued 6,202,408 registered bonds with a nominal value, equal to issue price, of PLN 0.01 each with a pre-emption rights attached to the Bonds to subscribe for Company shares with priority over the existing shareholders. A total of 6,047,710 Bonds were subscribed and allocated to the Beneficiaries. The remaining Bonds which had not been subscribed, in the amount of 154,698 were acquired by an agent acting as a custodian. These Bonds may be allocated in the future to existing or new Beneficiaries in accordance with the terms and conditions of the Program.

Pre-emption rights attached to the Bonds to subscribe for the Company's shares may be exercised within seven years after the end of the restricted period. The restricted period ends on the third anniversary of the issue of the Bonds, inclusive. The redemption of the Bonds will take place on the 10th anniversary of the issue date or, in the case of the Bonds kept by the Agent acting as the custodian, after the expiration of the restricted period. One Bond gives a right to subscribe for one ordinary share with a nominal value of PLN 3. The shares acquired upon exercising pre-emption right attached to the Bond are ordinary bearer shares and are not subject to any restriction in trading. The right to subscribe for the shares shall be vested exclusively in the bondholders. The issue price of the shares is PLN 21.57 per share.

The following table illustrates the number and weighted average exercised price of equity instruments granted by TP S.A.:

	12 months ended 31 December 2010		12 months ended 31 December 2009	
	number	weighted average exercised price (PLN)	number	weighted average exercised price (PLN)
Outstanding at the beginning of the period	**4,357,425**	**21.57**	**4,746,102**	**21.57**
Granted during the year	–	–	–	–
Cancelled during the year	(422,199)	–	(388,677)	–
Exercised during the year	–	–	–	–
Expired during the year	–	–	–	–
Outstanding at the end of the year	**3,935,226**	**21.57**	**4,357,425**	**21.57**
– of which exercisable	3,935,226	–	55,072	–

Notes to the consolidated financial statements continued

26. Share-based payments (continued)

26.1. Group incentive programme (continued)

The following table illustrates the key assumptions used in calculation of the fair value of equity instruments granted by TP S.A.:

Key assumptions	TP S.A. plan
Dividend yield	6%
Expected volatility	30%
Risk-free interest rate	5.59%
Exercised price	21.57
Vesting period	3 years
The weighted average expected life	7 years
Model used	binomial

During the 12 months ended 31 December 2010 and 2009 the fair value of services received recognised in labour expenses and equity amounted to PLN 3 million and PLN 4 million, respectively.

26.2. France Telecom S.A. free share award plan

In 2007 France Telecom S.A. established a free share, equity-settled, award plan ("NExT plan"). Under the plan 988,400 shares were offered to employees and executives of the Group. The grant date was established on 18 March 2008 that is the date when the main terms and conditions of the plan were announced personally to TP Group employees. The shares granted can not be sold for a period of two years after the vesting date. The fair value of shares at grant date was PLN 63.57 (an equivalent of EUR 17.95 translated at NBP period-end exchange rate at 18 March 2008).

The plan was contingent upon meeting the following criteria in France Telecom Group:

- performance conditions: achievement of the cash flow set out in the NExT plan in 2007 and 2008 (EUR 6.8 billion and EUR 6.8 billion, respectively), and cost of the plan to be covered by additional cash flow generated over the same period. The cash flow performance condition has been met in 2007 and 2008.
- beneficiaries must be contractually employed by the France Telecom Group at the end of the vesting period.

The following table illustrates the key assumptions used in calculation of the fair value of equity instruments granted by France Telecom S.A. to the Group employees:

Key assumptions	France Telecom S.A. free share plan
Price of the underlying at the grant date	PLN 76.15 (1)
Subscription price – zero in case of free share award plan	PLN 0.00
Dividend yield	6%
Performance conditions	100%
Risk-free interest rate	3.48%
Lending-borrowing rate	5.24% (2)
Vesting period	2 years
Model used	binomial

(1) An equivalent of EUR 21.50 translated at NBP period-end exchange rate at 18 March, 2008
(2) Corresponds to the lending-borrowing rate on France Telecom S.A. shares used to calculate the non-transferability costs.

During the 12 months ended 31 December 2010 and 2009, the fair value of services received, recognised in accordance with IFRS 2 "Share-based Payment" in labour expenses and equity, amounted to PLN 1 million and PLN 39 million, respectively.

27. Provisions

For the 12 months ended 31 December 2010 the movements of provisions were as follows:

(in PLN millions)	At 1 January 2010	Increases	Reversals (utilizations)	Reversals (releases)	Foreign exchange effect	Discounting effect	At 31 December 2010
Provisions for claims and litigation (see Note 31), risks and other charges	1,098	1,196	(53)	(12)	(35)	–	2,194
Restructuring provisions	126	34	(123)	–	–	5	42
Provisions for dismantling	199	–	(2)	(13)	–	11	195
Total provisions for risks and charges	**1,423**	**1,230**	**(178)**	**(25)**	**(35)**	**16**	**2,431**
Current	1,208						2,242
Non-current	215						189

For the 12 months ended 31 December 2009 the movements of provisions were as follows:

(in PLN millions)	At 1 January 2009	Increases	Reversals (utilizations)	Reversals (releases)	Foreign exchange effect	Discounting effect	At 31 December 2009
Provisions for claims and litigation (see Note 31), risks and other charges	1,093	73	(42)	(13)	(13)	–	1,098
Restructuring provisions	229	25	(134)	(2)	–	8	126
Provisions for dismantling	194	16	(5)	(17)	–	11	199
Total provisions for risks and charges	**1,516**	**114**	**(181)**	**(32)**	**(13)**	**19**	**1,423**
Current	1,220						1,208
Non-current	296						215

The discount rate used to calculate the present value of restructuring and dismantling provisions amounted to 4.95% - 6.00% as at 31 December 2010 and 6.1% as at 31 December 2009.

Restructuring provisions
The restructuring provisions consist of the estimated amount of termination benefits for employees scheduled to terminate employment in TP S.A. under the 2009-2011 Social Agreement and in Orange Customer Service Sp. z o.o. ("OCS") under an arrangement with Trade Unions for the period from October 2010 to December 2011.

In the fourth quarter of 2008, TP S.A. concluded a new Social Agreement for years 2009-2011 with all TP S.A. trade unions. Up to 4,900 employees may take advantage of the voluntary departure package between 2009 and 2011. In the fourth quarter of 2010, OCS concluded an arrangement with Trade Unions. Up to 329 employees may take advantage of the voluntary departure package in the period from October 2010 to December 2011. The amount of termination benefit varies depending on individual salary, employment duration and year of resignation. The basis for calculation of the employment restructuring provision is the estimated number, remuneration and service period of employees who will accept the voluntary termination until the end of 2011. As at 31 December 2010, 4,417 employees in TP S.A. and 77 employees in OCS took advantage of the voluntary departure packages described above.

Dismantling provision
The dismantling provision relates to dismantling or removal of items of property, plant and equipment and restoring the site on which it is located. Based on environmental regulations in Poland, items of property, plant and equipment which may contain hazardous materials should be dismantled and utilized by the end of their useful lives by entities licensed by the State for this purpose.

The amount of dismantling provision is based on the estimated: number of items that should be utilized/sites to be restored, period of utilization/time to restoration (20-100 years), current utilization/restoration cost (obtained through a tender process conducted on normal commercial terms) and inflation.

28.Trade payables, other liabilities and deferred income

28.1. Trade payables

(in PLN millions)	At 31 December 2010	At 31 December 2009
Trade payables	1,611	1,606
Fixed assets payables	1,488	812
UMTS licence payables	808	849
Total trade payables (1)	**3,907**	**3,267**
Current	3,156	2,477
Non-current (2)	751	790

(1) Classified as financial liabilities measured at amortised cost under IAS 39.
(2) It includes only UMTS licence liability.

Notes to the consolidated financial statements continued

28.Trade payables, other liabilities and deferred income (continued)

28.2. Other liabilities

(in PLN millions)	At 31 December 2010	At 31 December 2009
VAT payable	142	143
Other taxes payables	56	20
Other	22	21
Total other liabilities	**220**	**184**
Current	220	184
Non-current	–	–

28.3. Deferred income

(in PLN millions)	At 31 December 2010	At 31 December 2009
Sales of products and services billed in advance	588	603
Revenue from inactivated mobile phones and terminals in the external dealership network	11	24
Other	–	9
Total deferred income	**599**	**636**
Current	533	583
Non-current	66	53

29. Equity

29.1. Share capital

As at 31 December 2010 and 2009, the share capital of the Company amounted to PLN 4,007 million and was divided into 1,336 million fully paid ordinary bearer shares of PLN 3 each.

The ownership structure of the share capital as at 31 December 2010 was as follows:

(in PLN millions)	% of votes	Nominal value
France Telecom S.A.	49.79	1,995
Capital Group International, Inc. (1)	5.06	203
Other shareholders	45.15	1,809
Total	**100.00**	**4,007**

(1) Number of shares according to the notification by Capital Group International, Inc. on 15 October 2010.

As at 31 December 2010 and 2009, France Telecom S.A. owned 49.79% of shares of the Company and held 49.79% of votes at the General Shareholders' Meeting.

On 5 August 2010, the State Treasury announced that it sold 4.15% shares of TP S.A. through the Warsaw Stock Exchange in the period from 14 January to 5 August 2010.

The Group has no information regarding valid agreements or other events that may result in changes in the proportions of shares held by the shareholders.

29.2. Dividends

On 23 April 2010, the General Shareholders' Meeting of TP S.A. adopted a resolution on the payment of an ordinary dividend of PLN 1.50 per share, i.e. PLN 2,003 million. The dividend was paid on 1 July 2010.

30. Unrecognised contractual obligations

30.1. Unrecognised contractual obligations

At 31 December 2010, Management considers that, to the best of its knowledge, there are no existing unrecognised contractual obligations, other than those described below, likely to have a material impact on the current or future financial position of the Group.

a) Commitments related to operating leases
When considering the Group as a lessee, operating lease commitments mainly relate to the lease of buildings, land and vehicles. Lease costs recognised in the consolidated income statement for the years ended 31 December 2010 and 2009 amounted to PLN 404 million and PLN 412 million, respectively. Approximately half of the 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 2010 and 2009 (upon revised criteria for considering future lease payments as non-cancellable), were as follows:

(in PLN millions)	At 31 December 2010	At 31 December 2009
within one year	211	251
after one year but not more than five years	233	279
more than five years	55	65
Total minimum future lease payments	**499**	**595**

When considering the Group as a lessor, future minimum lease payments under non-cancellable operating leases as at 31 December 2010 and 2009 amounted to PLN 100 million and PLN 76 million, respectively.

b) Investment commitments
Capital commitments contracted for at the balance sheet date but not recognized in the financial statements were as follows:

(in PLN millions)	At 31 December 2010	At 31 December 2009
Property, plant and equipment	761	224
Intangibles	73	59
Total	**834**	**283**
Amounts contracted to be payable within 12 months after the balance sheet date	695	263

Capital commitments represent mainly purchases of telecommunications network equipment, IT systems and other software.

c) Memorandum of Understanding with UKE
On 22 October 2009, TP S.A. and UKE signed a Memorandum of Understanding concerning implementation of transparency and non-discrimination in inter-operator relations. In 2010, TP S.A. carried out activities in accordance with a schedule established together with UKE and was systematically implementing technical and organisational solutions, in order to secure non-discriminatory relations with other operators including equal access to information. It is anticipated that as TP S.A. fulfils the arrangements, the President of UKE will withdraw the consideration of functional separation of TP S.A. which had been considered by UKE as a regulatory tool to implement effective competition on regulated telecommunication wholesale markets in Poland.

Over the years 2010-2012, TP S.A. is to invest in the development of 1.2 million broadband access lines (0.479 million new lines and 0.721 million upgraded existing lines), of which 1 million lines will provide bandwidths of at least 6 Mbps. As at 31 December 2010, TP S.A. has delivered 0.45 million broadband access lines.

30.2. Assets covered by commitments

The gross book value of the assets held under finance leases amounted to PLN 26 million and PLN 23 million as at 31 December 2010 and 2009, respectively. Leased assets cannot be sold, donated, transferred by title or pledged and are a collateral for the related finance lease liability.

31. Litigation and claims (including contingent liabilities)

a.Issues related to the incorporation of Telekomunikacja Polska
Telekomunikacja Polska was established as a result of the transformation of the state-owned organisation Poczta Polska Telegraf i Telefon (“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 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.

Notes to the consolidated financial statements continued

31. Litigation and claims (continued)

b. 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. Value added tax, corporate income tax, personal income tax and other taxes or social security regulations are subject to frequent changes which often leads to the lack of well established regulations or legal precedents. 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.

c.Proceedings by UKE, UOKiK and the European Commission
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 Act on Competition and Consumer Protection, in case of non-compliance with its regulations, the President of the Office of Competition and Consumer Protection ("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 a breach of the law.

Proceedings by UKE related to broadband access
On 25 September 2006, UKE imposed a fine of PLN 100 million on TP S.A. for the infringement of the obligation to determine the price of the services on the basis of the cost of their provision and on clear, objective and non-discriminatory criteria, as a result of not implementing the offer to sell Neostrada (Internet services) separately from the fixed line subscription (allocating costs of local loop entirely to fixed line subscription). TP S.A. did not pay the fine and appealed to the Court of Competition and Consumer Protection ("SOKiK"). On 22 May 2007, the Court invalidated the fine on procedural grounds. UKE appealed this verdict and on 10 April 2008, the Appeal Court revoked the judgment of SOKiK and remanded the case back to consideration by SOKiK. On 2 June 2009, SOKiK suspended the proceeding until the end of the European Commission proceeding against Poland in the European Court of Justice on attempts of UKE to regulate retail prices of broadband services without a prior analysis of a relevant market, the result of which could, in SOKiK opinion, impact the proceeding suspended by SOKiK.

On 22 February 2007, after TP S.A. had separated providing Neostrada from fixed line services, UKE imposed a fine of PLN 339 million on TP S.A. for non-performance of the regulatory obligation to submit its Neostrada price list for UKE's approval, and for failing to demonstrate that TP S.A. had met the requirements of the Polish Telecommunication Law that the price of services (in particular the additional charge for the maintenance of the local loop paid by the Neostrada customers who do not subscribe for TP S.A.'s traditional fixed-line analogue services on the same local loop) be based on their cost and determined on clear, objective and non-discriminatory criteria. TP S.A. did not pay the fine, and, on 7 March 2007, appealed against the decision. SOKiK suspended also this proceeding.

On 6 May 2010 the European Court of Justice passed a judgment in the European Commission proceeding against Poland. The Court ruled that by regulating retail tariffs for broadband access services without carrying out a prior market analysis, Poland has failed to fulfil its obligations under the Universal Service Directive in conjunction with the Framework Directive. On 12 November 2010, SOKiK resumed the appeal proceeding concerning the fine of PLN 100 million. TP S.A. believes that UKE has no right to challenge the Neostrada price since it is not defined as a regulated service and that the criteria used for setting Neostrada price were transparent and objective.

Proceedings by UOKiK related to IP traffic
On 20 December 2007, UOKiK issued a decision concluding that TP S.A. had engaged in practices restricting competition when it downgraded IP traffic coming from domestic operators' networks to TP S.A.'s network via foreign operators' networks and imposed a fine of PLN 75 million on the Company. At the same time, UOKiK ordered TP S.A. to immediately cease this practice. TP S.A. disagrees with the decision of UOKiK and did not pay the fine. On 2 January 2008, TP S.A. appealed to SOKiK against the decision. The matter is currently being investigated by SOKiK.

Proceedings by UOKiK related to mobile television
On 21 September 2010, UOKiK initiated competition proceedings against PTK- Centertel, Polkomtel S.A., Polska Telefonia Cyfrowa Sp. z o.o. and P4 Sp. z o.o. claiming that they concluded an agreement regarding their relations with Info TV FM Sp. z o.o.

Info TV FM Sp. z o.o. is a telecommunications operator working in the field of radio diffusion and providing its services to radio and television broadcasters. 4MNO Sp. z o.o. (formerly Mobile TV Sp. z o.o.) is a company in which the four above companies involved in the proceedings are shareholders. UOKiK gave its prior approval to set up Mobile TV Sp. z o.o. Both companies applied to UKE for a license to broadcast in the frequency band designed for the provision of audiovisual media services in DVB-H technology.

In March 2009, Info TV FM Sp. z o.o. was granted permission to use these frequencies. However, none of the four companies decided to introduce mobile television services to its customers.

UOKiK claims that there was an agreement concluded between the four companies involved in the proceedings and it could restrict competition on the domestic wholesale market for mobile television based on DVB-H technology, and, as a result, limit the possibility for consumers to use mobile television.

The Management Board of PTK-Centertel did not agree on common actions with the other companies aimed at restricting the introduction of DVB-H service based on the offer of Info TV FM Sp. z o.o. It decided not to introduce mobile television services due to the market situation and for commercial reasons.

PTK-Centertel provided explanations to UOKiK on 5 October 2010. At this stage, the Group is not in a position to predict the evolution of these proceedings, and the risk related thereto is therefore classified as a contingent liability as defined by IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

31. Litigation and claims (continued)

c.Proceedings by UKE, UOKiK and the European Commission (continued)

Proceedings before the European Commission related to broadband access

In September 2008, the European Commission conducted an inspection at the premises of TP S.A. and PTK-Centertel. The aim of the inspection was to gather evidence of a possible breach by TP S.A. of competition rules on the broadband Internet market. On 17 April 2009, the European Commission notified TP S.A. of initiation of proceedings on the supposed refusal to provide services and non-price discrimination on the Polish wholesale market of broadband access to the Internet. On 1 March 2010, TP S.A. received a Statement of Objections from the European Commission regarding an alleged abuse of dominant position, by refusing to supply access to its wholesale broadband services. The Company responded to the Statement of Objections on 2 June 2010 and an audience before the European Commission took place on 10 September 2010. In the course of the proceedings, state of play meetings with the European Commission also took place, with the latest meeting on 9 December 2010. TP S.A. received from the European Commission the letter of facts dated 28 January 2011 presenting evidence collected after the issue of the Statement of Objections as well as findings of the European Commission. Although the letter does not state additional objections against TP S.A., the Commission still asserts that TP S.A. has infringed the competition rules. The deadline for responding to the letter of facts is 7 March 2011.

Under European law, the European Commission may impose a fine on an entity of up to 10% of its total turnover of the preceding business year if it proves infringement of rules on competition. Moreover, the Commission may impose any behavioural or structural remedies which are proportionate to the infringement committed and necessary to bring the infringement effectively to an end. Such a decision can be appealed to the General Court (formerly the Court of First Instance). The Commission may also impose a fine of up to 1% of the total turnover of the preceding business year for providing incorrect or misleading information.

As at 31 December 2010, the Group recognised provisions for known and quantifiable risks related to proceedings against the Group initiated by UKE, UOKiK and the European Commission, 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 dependent 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. Information regarding the amount of the provisions has not been separately disclosed, as in the opinion of the Company's Management such disclosure could prejudice the outcome of the pending cases.

d. Dispute with DPTG

Information on the matter has been consistently referred to in the consolidated financial statements of the Group since 2001 together with the development of the case over the years.

In 2001, a dispute arose over the interpretation of a contract for the sale and installation by the Danish company DPTG of a fiber optical transmission system (known as "North-South Link", or "NSL") for the State-owned PPTiT, the predecessor of TP SA. The contract, signed in 1991 and for which work was completed in 1994, provided for payment of part of the contract price by allocating to DPTG 14.8% of certain profit from the NSL for fifteen years from the system's installation, that is, from February 1994 to January 2009. In 1999, the parties came into disagreement regarding the calculation of this revenue. In 2001, DPTG initiated ad hoc arbitration proceedings before the Arbitration Tribunal (under UNCITRAL rules) sitting in Vienna.

The Arbitration Tribunal appointed a first expert in 2004 to evaluate the revenue "from the NSL" to be used as a basis for calculating the share attributable to DPTG. Between November 2005 and December 2007, this expert delivered three reports proposing widely differing estimates. In January 2008, a second expert named by the Tribunal to assess the appropriateness and the consistency of the first expert's models, concurred, in all material respects, with the conclusions of the latest report of the first expert. In February 2008, the President of the Austrian Federal Economic Chamber sustained the challenge filed by TP S.A. against the chairman of the Arbitration Tribunal for lack of impartiality and a new chairman was named.

In June 2008, the Arbitration Tribunal decided to split the case into two periods and to render firstly an award settling DPTG's rights for the period from February 1994 to June 2004. On 3 September 2010, the Tribunal issued its partial award for the period from February 1994 to June 2004 (Phase I). It settles DPTG's claims at DKK 2,946 million (approximately EUR 396 million) including interest. The partial award was issued after nine years of arbitration proceedings. During this time, TP S.A. consistently contested both the basis of the DPTG case and, in particular, its interpretation of the contract as a joint-venture and its related broad interpretation of the financing sub-clause at the heart of the dispute, as well as the amount claimed. According to TP S.A., the contract is a sale contract. The contract valued DPTG's supplies remaining to be paid at EUR 17 million. By 2006, DPTG had already received from TP S.A. over EUR 84 million in performance of the contract.

The partial award states that the contract is a sale contract but nevertheless awards DPTG an amount as if the contract was a joint-venture. TP S.A., its legal counsel and independent experts all believe that the amount awarded is many times higher than DPTG's rights. Given the amounts awarded for Phase I, and potentially for Phase II, and the lack of consistency of the award, it is TP S.A's position that this award is contrary to Public Policy.

Since 2001, TP S.A. has made what it considered to be an appropriate provision for this matter, as supported by outside counsel and other professional advisors. TP S.A.'s Management Board has conducted the necessary reassessment of the provision in consideration both of this partial award and of the potential award to DPTG for the period from July 2004 to January 2009 (Phase II). The provision has been increased from approximately DKK 2,050 million (an equivalent of EUR 275 million or PLN 1,100 million) to approximately DKK 4,040 million (an equivalent of EUR 542 million or PLN 2,161 million). The revised amount is made up of the sum of the Arbitration Tribunal's award for Phase I (including interest) and of the result of the linear projection of the DKK 2,001 million awarded in the partial decision of the Tribunal for the 125 months of Phase I onto the 55 months of Phase II, amounting to DKK 880 million (EUR 118 million) in principal and approximately DKK 216 million (EUR 29 million) in interest. The Management will assess the level of the provision on a regular basis taking into account further developments of the matter.

The Company's Management has been obliged to adjust the level of provision for this matter by virtue of the fact that an arbitral award has been rendered. Nevertheless, it strongly disputes both the contractual basis of the claim and the amounts awarded. Therefore, the amount of the provision should in no way be viewed as an indication by TP S.A. of the proper outcome of the dispute. On the contrary, and as mentioned above, it is the strongly held opinion of TP S.A.'s Management and its counsel that the award is in clear violation of the basic rules of Public Policy. TP S.A.'s Management, acting in the best interests of the Company and its shareholders, will use all reasonable legal actions to resist the award issued by the Arbitration Tribunal.

As a consequence, TP S.A. did not pay the partial award. On 13 October 2010, TP S.A. challenged the three arbitrators, claiming for their dismissal from the potential further proceedings on Phase II. On 2 December 2010, TP S.A. filed a claim before the commercial court in Vienna claiming for the setting aside of the partial award. In the setting aside procedure, the court ordered a hearing on 30 March 2011.

On 22 December 2010, TP S.A. was notified by the Court in Warsaw that DPTG had filed a motion to ascertain enforceability and obtain an enforceability clause with regards to the partial award. The court hearing with regards to this matter is scheduled for 9 March 2011. TP S.A. is currently preparing a robust defence to this motion.

On 14 January 2011, DPTG filed its claim for Phase II, which amounts to DKK 2,386 million (approximately EUR 320 million) including interest. The Tribunal has directed TP S.A. to submit its answer to this claim by 27 May 2011.

31. Litigation and claims (continued)

e. Other contingent liabilities and provisions

Apart from the above mentioned, operational activities of the Group are subject to regulations of legal-administrative nature and 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.

32. Related party transactions

32.1.Management Board and Supervisory Board compensation

Management Board compensation was as follows:

(in PLN thousands)	12 months ended 31 December 2010	12 months ended 31 December 2009
Short-term benefits excluding employer social security payments (1)	9,318	13,647
Post-employment and other benefits	–	1,860
Termination costs	2,225	2,550
Total	**11,543**	**18,057**

(1) Gross salaries, compensation, bonuses and non-monetary benefits.

Remuneration and bonuses, compensation and termination indemnities, including compensation under a competition prohibition clause (cash, benefits in kind or any other benefits) paid in accordance with contractual commitments, by TP S.A. to TP S.A.'s Management Board and Supervisory Board members during the 12 months ended 31 December 2010 and 2009 are presented below.

Persons that were Members of the Management Board of the Company as at 31 December 2010

(in PLN thousands)	12 months ended 31 December 2010	12 months ended 31 December 2009
Maciej Witucki	3,019	2,687
Vincent Lobry	2,131	350 (1)
Piotr Muszyński	1,811	1,496
Roland Dubois	2,357	2,047
Total	**9,318**	**6,580**

(1) From the date of appointment

Persons that were Members of the Management Board of the Company in 2010 or previous periods

(in PLN thousands)	12 months ended 31 December 2010	12 months ended 31 December 2009
Mariusz Gaca	–	617 (2)
Jacek Kałłaur	–	4,157 (1)
Ireneusz Piecuch	–	3,308 (1)
Richard Shearer (3)	2,225	3,395 (1)
Total	**2,225**	**11,477**

(1) Until the termination date
(2) For the period of appointment
(3) In addition to the amounts presented above, as at 31 December 2009 termination benefits payable in 2010 amounted to PLN 2.2 million.

In addition to the amounts presented above, during the 12 months ended 31 December 2010, the estimated cost of share-based payments under TP S.A.'s incentive programme allocated to the Company's Management Board amounted to PLN 0.6 million. During the 12 months ended 31 December 2009, the estimated cost of share based payments under TP S.A.'s and France Telecom S.A.'s incentive programmes allocated to the Company's Management Board amounted to PLN 0.7 million. In the 12 months ended 31 December 2010, no cost was recognized in respect of France Telecom S.A.'s incentive programme as the vesting period of the programme ended in 2009. In the 12 months ended 31 December 2010 and 2009, the amount of accrued costs for bonuses for the Company's Management Board amounted to PLN 1.5 million and PLN 1.5 million, respectively.

In the years ended 31 December 2010 and 2009 the members of TP S.A.'s Management Board did not receive any remuneration and bonuses (cash, benefits in kind or any other benefits) from TP S.A.'s subsidiaries and associates.

In the years ended 31 December 2010 and 2009, 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.

32. Related party transactions (continued)

32.1.Management Board and Supervisory Board compensation (continued)

Supervisory Board compensation was as follows:

(in PLN thousands)	12 months ended 31 December 2010	12 months ended 31 December 2009
Prof. Andrzej Koźmiński	333	318
Olivier Barberot [(2)]	–	–
Olivier Faure [(2)]	–	–
Timothy Boatman	250	239
Thierry Bonhomme [(2)]	–	–
Jacques Champeaux	167	159
Ronald Freeman	250	239
Dr. Mirosław Gronicki	167	159
Marie-Christine Lambert [(2)]	–	–
Prof. Jerzy Rajski	167	159
Raoul Roverato [(2)]	–	–
Dr. Wiesław Rozłucki	167	159
Olaf Swantee [(2)]	–	–
Antonio Anguita [(1)(2)]	–	–
Vivek Badrinath [(1)(2)]	–	–
Stephane Pallez [(1)(2)]	–	–
Georges Penalver [(1)(2)]	–	–
Total	**1,501**	**1,432**

(1) Persons that were not members of the Supervisory Board of the Company as at 31 December 2010 but were members of the Supervisory Board of TP S.A. in 2010 or previous periods.
(2) Persons appointed to the Supervisory Board of the Company employed by France Telecom S.A. do not receive remuneration for the function performed.

In the years ended 31 December 2010 and 2009, 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 the years ended 31 December 2010 and 2009, TP S.A. did not grant any loans to members of the Management Board and the Supervisory Board.

As at 31 December 2010 and 2009, members of the Management Board and the Supervisory Board had no liabilities arising from loans granted by the Company.

In the years ended 31 December 2010 and 2009, TP S.A. did not enter into any transactions with companies in which the members of its authorities had significant shareholdings.

In the years ended 31 December 2010 and 2009, the Company did not enter into any significant transactions with members of the Management Board and the 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.

Notes to the consolidated financial statements continued

32. Related party transactions (continued)

32.2. Related party transactions

As at 31 December 2010, France Telecom S.A. owned 49.79% of shares of the Company. France Telecom S.A. has the power to appoint the majority of TP S.A.'s Supervisory Board members. The Supervisory Board appoints and dismisses members of the Management Board.

The Group's income earned from related parties comprise mainly interconnect, data transmission and research and development services. The purchases from the France Telecom Group mainly comprise costs of interconnect and leased lines, network services, IT services, consulting services and brand fees.

(in PLN millions)	12 months ended 31 December 2010	12 months ended 31 December 2009
Sales of goods and services to:	**197**	**195**
– France Telecom S.A. (parent)	139	129
– France Telecom (group)	58	66
Purchases of goods (including inventories, tangible and intangible assets) and services from:	**323**	**331**
– France Telecom S.A. (parent)	121	123
– France Telecom (group)	202	208
including Orange Brand Services Limited (brand licence agreement)	120	117
Dividends paid:	**997**	**997**
– France Telecom S.A. (parent)	997	997
– France Telecom (group)	–	–

In April 2005, PTK-Centertel and Orange Brand Services Limited (UK) (hereinafter referred to as "Orange") concluded a licence agreement, on the basis of which PTK-Centertel acquired rights to operate under the Orange brand. The brand licence agreement provides that Orange receives a fee of 1.6% of operating revenue for full use of the Orange brand as well as access to the Orange roaming and interconnection arrangements, technology, advanced mobile handsets and consultancy services. The agreement has been concluded for 10 years with the possibility of renewal.

On 24 July 2008, TP S.A., France Telecom S.A. and Orange concluded a licence agreement, on which basis TP S.A. will acquire rights to use the Orange brand (trade marks) in relation to the provisioning of TV, ISP and B2B goods and services. The license fee for the use of the Orange trade mark by TP S.A. will amount to 1.6% of the Company's operating revenue earned under the Orange brand. The agreement has been concluded for 10 years with the possibility of renewal.

(in PLN millions)	At 31 December 2010	At 31 December 2009
Receivables from:	**96**	**87**
– France Telecom S.A. (parent)	66	59
– France Telecom (group)	30	28
Payables to:	**189**	**230**
– France Telecom S.A. (parent)	102	124
– France Telecom (group)	87	106

33. Subsequent events

There was no significant event after the balance sheet date.

Auditor's Opinion

To the Shareholders and Supervisory Board of Telekomunikacja Polska S.A.

We have audited the attached consolidated financial statements [1] of the Telekomunikacja Polska Group ("the Group") with Telekomunikacja Polska S.A., with its registered office in Warsaw at Twarda 18 St., as the Parent ("TP S.A.", "the Company"), which comprise consolidated balance sheet prepared as of 31 December 2010, consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated statement of cash flows for the financial year from 1 January 2010 to 31 December 2010 and notes comprising a summary of significant accounting policies and other explanatory information.

Preparation of consolidated financial statements and a report on the activities of the Group in line with the law is the responsibility of the Management Board of the Parent.

The Management Board of the Parent and members of its Supervisory Board are obliged to ensure that the consolidated financial statements and the report on the activities of the Group meet the requirements of the Accounting Act of 29 September 1994 (Journal of Laws of 2009, No. 152, item 1223, as amended), hereinafter referred to as the "Accounting Act".

Our responsibility was to audit and express an opinion on compliance of the consolidated financial statements with the accounting principles (policy) adopted by the Group, express an opinion whether the financial statements present fairly and clearly, in all material respects, the financial and economic position as well as the financial result of the Group.

Our audit of the financial statements has been planned and performed in accordance with:

– section 7 of the Accounting Act,
– national auditing standards, issued by the National Council of Statutory Auditors in Poland and
– International Standards on Auditing.

We have planned and performed our audit of the consolidated financial statements in such a way as to obtain reasonable assurance to express an opinion on the financial statements. Our audit included, in particular, verification of the correctness of the accounting principles (policy) applied by the Parent and the subsidiaries, verification – largely on a test basis – of the basis for the amounts and disclosures in the consolidated financial statements, as well as overall evaluation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the audited consolidated financial statements in all material respects:

– present fairly and clearly the information material to evaluate the economic and financial position of the Group as of 31 December 2010 as well as its profit or loss in the financial year ended 31 December 2010,
– have been prepared in accordance with the International Accounting Standards, International Financial Reporting Standards and related interpretations published as European Commission regulations, and in all matters not regulated in the standards – in accordance with the provisions of the Accounting Act and secondary legislation to the Act,
– comply with the provisions of law applicable to the Group which affect the contents of the consolidated financial statements.

Without qualifying our audit opinion, we draw attention to the following matter:

As more fully explained in explanatory note 31 to the attached consolidated financial statements, the Group is involved in a number of legal, arbitration and administrative proceedings. Any costs that may result from these proceedings are provided for when they become probable and when the amount may be reliably quantified. The amount of any provision is based on an assessment of the risk level in each case and represents the Group's best estimate of the amounts that are more likely than not to be payable. Occurrence of events during the proceedings, the outcome of which is uncertain, may lead to re-assessment of the risk and as a consequence the amount of the provisions may change.

The Report on the activities of the Group [2] for the 2010 financial year is complete within the meaning of Article 49.2 of the Accounting Act and the Decree of the Minister of Finance of 19 February 2009 on current and periodic information to be disclosed by issuers of securities and consistent with underlying information disclosed in the audited consolidated financial statements.

Krzysztof Sowada
Key Certified Auditor
conducting the audit
No. 10944

represented by

entity authorized to audit
financial statements entered under
number 73 on the list kept by the
National Council of Statutory Auditors

Warsaw, 22 February 2011

The above audit opinion together with audit report is a translation from the original Polish version. In case of any discrepancies between the Polish and English version, the Polish version shall prevail.

[1] as presented on pages 38-92.
[2] as included in the filed financial statements for Warsaw Stock Exchange.